

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

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Office Correspondence

Date October 16, 1937To Chairman EcclesF. Lauchlin Currie*ABC*Subject: The decline in the Federal
contribution to the growth in community
expenditures

In view of the revival of interest in this subject I have had our monthly series brought up to date and am contributing the attached story to Current Comments next week.

THE DECLINE IN THE FEDERAL CONTRIBUTION TO THE GROWTH IN COMMUNITY

EXPENDITURES

How the contribution is measured

1. The monthly expenditures of the Government and its agencies are checked item by item in order that expenditures that appear likely to result in current purchases may be separated from those that do not result in current buying. Appropriations to the Old Age Reserve Fund, for example, do not increase current buying. One-half of the proceeds of bonus bonds cashed were assumed to result in current purchases.

2. From the gross activity-stimulating expenditures are then deducted all tax receipts except estate taxes and gift taxes. Estate taxes are assumed not to result in a deduction from current expenditures. Doubtless the payment of a portion of income taxes likewise does not result in a contraction of current buying, but little basis exists for estimates of this amount on a monthly basis. It should be kept in mind, however, that by deducting all income taxes this particular series may tend to understate the Government's contribution and to overstate the decline from 1936. Income tax payments are smoothed over a three-month period.

Significance of the contribution

The excess of activity-increasing expenditures over activity-decreasing receipts is one source of the increase in national money income. It should therefore be related to the factors affecting changes in the national income rather than to the national income totals themselves. The importance of this single factor in the recovery movement

may be judged by comparing it with the yearly increases in the national income:

	<u>1934</u>	<u>1935</u>	<u>1936</u>
	(In billions of dollars)		
Increase in national income over previous year	7.8	5.4	8.8
Net federal contribution	3.2	3.1	3.8

This comparison makes no allowance for the fact that a substantial portion of income tax payments, at least in the earlier years, would not have been currently spent if they had been retained by the taxpayers, nor for the secondary spending arising from the original contribution.

Significance of the decline in the contribution in 1937

The drastic decline in the monthly contribution this year from the levels prevailing in the second half of 1936 should not in itself be expected to bring about a business recession, since to date there has continued to be a net contribution, though small. The growth in the A. A. A. Index of Monthly National Income from 93 in January to 97.5 in May appears to be in part attributable to higher wages and increasing building activity. These forces expended themselves by May. From May to September there was little change in the index. The Federal Reserve Board index of production leveled off after March. Moreover, there are disturbing indications that a portion of industrial production has been going into increased inventories. Monthly department store sales showed no increase this year up to August as contrasted with

a substantial increase in the same period last year. Broadly speaking, it appears that private income-increasing expenditures did not expand this year at a rate sufficient to offset the decline in the federal contribution, so that the rate of recovery slackened.

Prospects for the next six months

The series under discussion has some bearing on the prospects for business activity in the near future. Instead of there being a net federal contribution to buying power in the first half of 1938, there may be a decrement, attributable mainly to increased tax receipts. One factor that has operated to increase national income will either be considerably diminished or become negative, depending upon the influence of increased income tax receipts. At the time of the recession in 1934 the federal contribution on a minimum basis continued to run above \$250 million monthly.

Net Federal Government Contribution to Community Expenditure

(Unit: \$1,000,000)

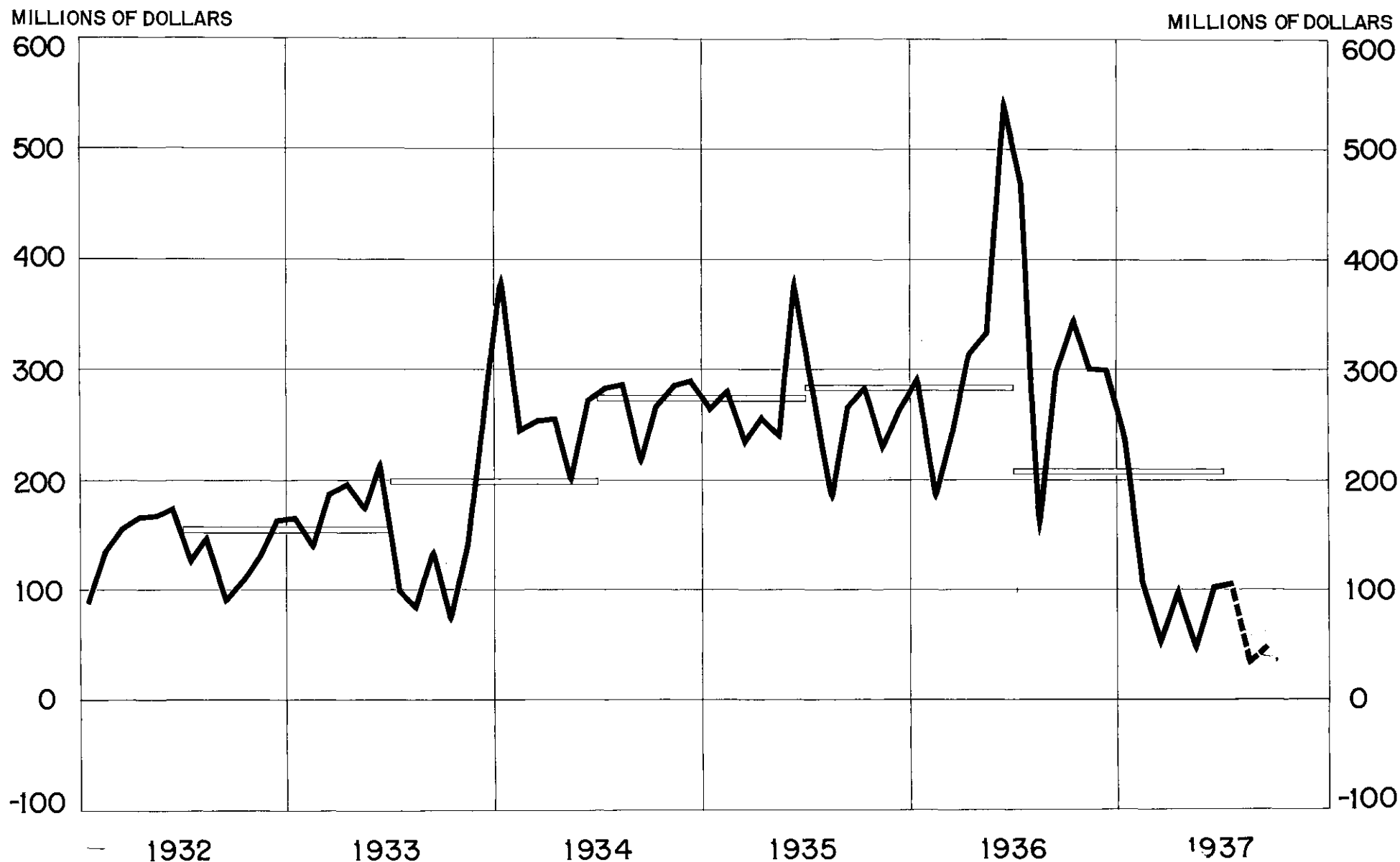
	1932	1933	1934	1935	1936	1937
January	88	164	384	264	291	237
February	133	139	244	280	184	107
March	155	187	253	232	244	50
April	165	195	255	256	314*	99
May	166	172	200	240	332	46
June	173	215	272	383	543	101
Fiscal year	1,047	1,838	2,392	3,285	3,407	2,502
July	126	97	283	272	469	103
August	148	82	286	183	152	32p
September	90	134	217	268	296	47p
October	109	73	268	284	346	
November	131	140	286	229	300	
December	162	258	290	263	299	
Calendar year	1,646	1,856	3,238	3,154	3,770	

*Half the cash bonus payments made in 1936 are distributed over the month of payment, the two months preceding, and the three months following.

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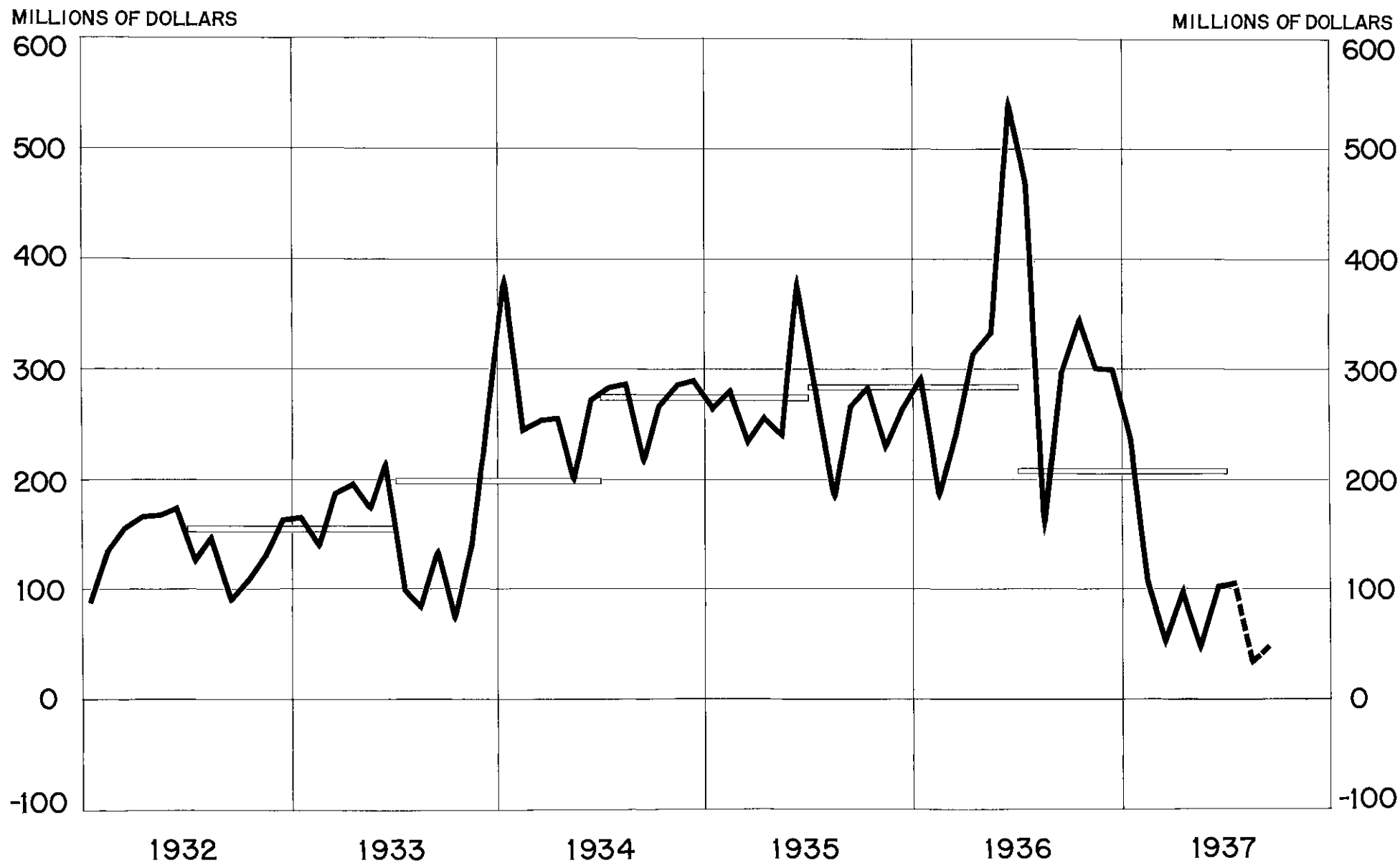
Revised October 11, 1937.

NET FEDERAL GOVERNMENT CONTRIBUTION TO COMMUNITY EXPENDITURE



PREPARED BY M. KROST

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