

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date August 12, 1937.

To Chairman Eccles

Subject: Memorandum on Fiscal Receipts

On Lauchlin Currie
LC

and Expenditures

Attached is a memo by Gayer and Krost on the prospective decline in the stimulation to business afforded by the fiscal operations of the government, and a breakdown of expenditures according as they stimulate construction or consumption. The memo appears in this week's Current Comments, but I thought you might like to have the original copy. No mention was made of the President's statement on this subject, but you will observe that construction expenditures are expected to remain up while expenditures stimulating consumption will experience a substantial decline, the very opposite of what the President said. The calculations were most laborious and I am sure they have not been done by anybody else.

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GOVERNMENT RECEIPTS AND EXPENDITURES
IN THE
FISCAL YEARS 1937 and 1938 IN RELATION TO BUSINESS ACTIVITY

BY

Arthur Gayer and Martin Krost

With the growth in receipts and decline in expenditures anticipated in the fiscal year 1938, the net stimulation to business activity attributable to the fiscal operations of the Federal Government, which has been an important factor in increasing buying power and the demand for goods since 1933, may be expected to decline. The main purpose of this memorandum is to afford some indication of the magnitude of the decline. In addition, the gross expenditures of the Government have been broken down into expenditures for construction and expenditures that stimulate consumption in the first instance.

In brief, it appears that the decline in the Federal Government's contribution to total community expenditures from the fiscal year 1937 to the fiscal year 1938 will be somewhere in the range from \$2.5 billion to \$3.8 billion. This decline measures the extent to which Government stimulation of business will be less in the fiscal year 1938 than in the preceding year. The decrease is attributable in part to increased tax collections and in part to decreased expenditures. A large part of the decline in expenditures is attributable to the bonus payments which were

made in the fiscal year 1937. Turning to the other aspect of the study--the distribution of the gross Government expenditures between those stimulating construction and those stimulating consumption in the first instance--it was found that construction expenditures will decline by \$39 million, or 2 percent, as contrasted with the decline of \$2.0 billion, or 31 percent (including the bonus), in expenditures stimulating consumption in the first instance. Excluding the bonus, expenditures stimulating consumption will decline by \$500 million, or 10 percent. Although from a budgetary point of view the payment of the bonus is a non-recurring item which distorts the comparison of expenditures between fiscal years, it is taken into account here because the bonus payment had a stimulating effect on consumer expenditures which is absent this year.

I

The contribution of the Federal Government to total community expenditures cannot be measured by the gross expenditures of the Government. For one thing, the gross expenditures include such things as debt retirements, appropriations to the Old-Age Reserve Account, purchases of investments by the Unemployment Trust Fund, and gold purchases, none of which directly increase incomes or stimulate business activity. The first step, therefore, in building up these estimates was to deduct such items from gross expenditures in both years. To the resulting figure of expenditures in the fiscal year 1937, there was added the proceeds of the bonds and odd-amount checks which were issued in payment of adjusted service certificates and cashed in June 1936. This was done because the interest of this memorandum is

focused on business activity and it seems probable that the actual spending of bonus money took place in the fiscal year beginning July 1, 1936.

In addition to these adjustments to the expenditure figures it is necessary, in seeking to arrive at an estimate of the net contribution of the Government to community spending, to take cognizance of the nature and amount of Government receipts. The payment of some taxes obviously decreases the amount the taxpayer would have otherwise spent on goods and services. The spending of such tax receipts by the Government, therefore, results in no net increase in total community spending. In the case of other tax receipts, however, the case is not so clear. If the Government had not collected taxes and spent them, the money might have remained unspent for either consumer or producers' goods in the period in question. The collection and spending of such taxes by the Government, therefore, may result in a net increase in total community spending.

If it is assumed that only the payment of taxes by the lower income groups resulted in an equivalent contraction of expenditures in other directions, we may deduct such tax receipts from the adjusted Government expenditures to arrive at a maximum estimate of the net contribution to community spending attributable to the fiscal operations of the Government. If, therefore, indirect taxes on consumption, manufacturers' excise taxes, social security taxes paid by employees, and income taxes paid by the group of taxpayers with net incomes of \$15,000 or less are deducted from adjusted expenditures, we arrive at maximum estimates of \$6.7 billion in the fiscal year 1937, and \$4.2 billion in the fiscal year 1938, or a decline of \$2.5 billion.

In order to arrive at a minimum estimate of the net contribution to community spending, it may be assumed that the payment of all taxes, the

net collections of Government credit agencies, and all other Government receipts except borrowing, reduce expenditures in other directions. This method of estimation gives an excess of expenditures of \$3.1 billion for the fiscal year 1937, and an excess of receipts of \$700 million for the fiscal year 1938, a decline of \$3.8 billion.

Federal Government Contribution to Total Community Expenditures
(Millions of dollars)

	1937 <u>Actual</u>	1938 <u>Budget Estimates</u>	<u>Change</u>
<u>Expenditures (exclusive of debt retirements)</u>			
1. Reported	8,001	7,324	-677
2. Addition <u>1/</u>	<u>1,411</u>	<u>193</u>	<u>-1,218</u>
3. Gross expenditures	9,412	7,517	-1,895
<u>Deductions</u>			
4. Old-age reserve account	265	540	+275
5. Taxes paid by lower income groups <u>1/</u>	2,444	2,756	+312
6. Total receipts except borrowing	6,088	7,712	+1,624
<u>Estimates of net contribution</u>			
7. Maximum (3 minus 4 and 5)	6,703	4,221	-2,482
8. Minimum (3 minus 4 and 6)	3,059	<u>2/735</u>	-3,794

1/ For items comprising this total see Table 1 at end of article.

2/ Excess of receipts.

II

It is of interest to examine the directions in which reductions of Government expenditures are proposed. The accompanying tables present a comparison of the breakdown of the 1938 and 1937 budgets into construction and non-construction items. In most cases the figures for 1938 are those of the revised budget released in April, although in a few instances they reflect changes made in the actual appropriation bills.

Distribution of Expenditures in 1937 and 1938 Budgets by Classes^{1/}
(Millions of dollars)

	<u>1937</u>	<u>1938</u>	<u>Change</u>	<u>Percent Change</u>	<u>Percentage Distribution 1937</u>	<u>1938</u>
Construction expenditures	1,785	1,746	-39	-2.2	19.0	23.2
Expenditures tending to stimulate consumption						
Recovery and relief	2,504	1,856	-648	-25.9	26.6	24.7
General (including bonus)	<u>3,891</u>	<u>2,560</u>	<u>-1,331</u>	<u>-34.2</u>	<u>41.3</u>	<u>34.1</u>
Total	6,395	4,416	-1,979	-31.0	67.9	58.8
Expenditures uncertain in effect or involving no cash outlay	<u>1,232</u>	<u>1,355</u>	<u>+123</u>	<u>+10.0</u>	<u>13.1</u>	<u>18.0</u>
Total gross expenditures	9,412	7,517	-1,895	-20.1	100.0	100.0

^{1/} For items comprising the totals shown see Table 2 at end of article.

Table 2, which presents the distribution of expenditures by general classes, shows that total gross expenditures (inclusive of the Old-Age Reserve Account) in the 1938 budget are some 20 percent lower than in 1937. Of the total reduction in expenditures of \$1,895,000,000, the reduction in construction expenditures represents \$39 million, a reduction of 2 percent from the 1937 figure for these items. Most of the reduction in expenditures is attributable to the absence this year of \$1,500,000,000 bonus payments which were made last year. The other significant economy proposed is the cutting of recovery and relief expenditures involving expenditures primarily for personal services and light public works, i.e., the Works Progress Administration, the Resettlement Administration, and the Civilian Conserva-

tion Corps. The reductions in these items total \$648 million, a decrease of 26 percent from the 1937 level. The sharp cuts in these expenditures are offset in part by increased expenditures for non-construction items in the national defense category (primarily for wages and salaries) and increased outlays under the Social Security Act.

Total expenditures of types which tend in the first instance to stimulate consumption show a decrease of \$1,980,000,000, or 31 percent, as contrasted with the 2 percent decrease in construction expenditures. In terms of the percentage composition of total expenditures, aggregate construction expenditures show a rise to 23 percent of the whole in 1938 as compared with 19 percent in 1937, while expenditures tending to stimulate consumption decline from 68 percent to 59 percent.

An examination of the classification of construction items by purposes given in Table 3 shows that most ^{categories} are substantially lower in 1938, but that estimated increases in PWA loans and grants to states and municipalities (from the PWA revolving fund), RFC and REA construction loans, and subsidies for merchant marine construction more than offset the reductions in other items. The aggregate cut for 1938 in the reduced items amounts to \$236 million, while the aggregate increase in the three items which are raised amounts to \$197 million, although it is somewhat uncertain whether the full amounts budgeted for the RFC and the Maritime Commission will be spent. On balance the reduction in construction items as budgeted amounts to only \$39 million in contrast to a cut in Works Progress Administration, Resettlement Administration, and Civilian Conservation Corps expenditures approximating \$650 million.

Since the figures for 1938 are derived primarily from the revised Budget issued in April, they underestimate those items which have been increased by the subsequent action of Congress, such as the contribution to the Railroad Retirement Trust Fund and the payment to the Federal Land Banks to enable reduction of interest rates on mortgages. The effect on total expenditures of these increases is likely to be offset by reductions in the outlays of the Government credit agencies, which appear to be overestimated in the Budget and by the effect of the recent action taken by the President directing Government departments and agencies to reduce expenditures by 10 percent of the amounts appropriated wherever such action is possible.

TABLE 1

Federal Government Contribution to Total Community Expenditures
(Millions of dollars)

	<u>1937</u>	<u>1938</u>	<u>Change</u>
Total expenditures as reported (exclusive of debt retirements)	8,001	7,324	-677
<u>Add:</u>			
Net receipts of credit agencies.	464	193	-271
Bonus bonds and checks cashed in June, 1936.	800		-800
Excess of bonus bonds and checks cashed in 1937 over amount charged to general fund.	147		-147
Gross expenditures <u>1/</u>	9,412	7,517	-1,895
<u>Deduct from gross expenditures:</u>			
Old-age reserve account.	265	540	+275
Indirect taxes on consumption	2,181	2,243	+62
Employees' share of social security taxes.	104	304	+200
Income taxes on incomes of \$15,000 or less.	159	209	+50
Maximum estimate of net contribution	6,703	4,221	-2,482
<u>Deduct from gross expenditures:</u>			
Net receipts of credit agencies.	464	193	-271
Old-age reserve account.	265	540	+275
General fund receipts as reported.	5,294	6,906	+1,612
Unemployment trust fund receipts.	294	577	+283
FDIC assessments.	36	36	-
<u>Minimum estimate of net contribution</u>	3,059	<u>2/</u> 735	-3,794

1/ These figures understate gross expenditures since they fail to take into account the expenditures of credit agencies which are partially or wholly offset by the receipts of those agencies. In the fiscal year 1937 such expenditures amounted to \$548,000,000. No estimates of these expenditures are available for the fiscal year 1938.

2/ Excess of receipts.

TABLE 2

Distribution of Expenditures in 1937 and 1938 Budgets by Purposes
(Millions of dollars)

	<u>1937</u>	<u>1938</u>	<u>Change</u>	<u>Percent Change</u>
<u>Construction expenditures</u>				
General Public Works Program	300	440	+140	+46.7
Recovery & relief program - public works	1,104	799	-305	-27.6
Other public works	104	113	+9	+ 8.7
Not classified as public works	277	394	+117	+42.2
Total	1,785	1,746	- 39	- 2.2
<u>Recovery and relief expenditures involving light public works or personal services only</u>				
WPA (and FERA)	1,908	1,400	-508	-26.6
Resettlement Administration	210	106	-104	-49.5
Emergency Conservation Work	386	350	- 36	- 9.3
Total	2,504	1,856	-648	-26.9
<u>General expenditures tending to stimulate consumption</u>				
AAA	533	524	- 9	- 1.7
National defense - non-construction items	570	618	+ 48	+ 8.4
Social security payments (excl. of old-age reserve)	183	286	*103	*56.3
Veterans pensions and benefits	580	570	-10	- 1.7
Adjusted compensation payment <u>1/</u>	1,504	-	-1,504	-100.0
Dept. expenses excl. of construction items	479	532	+ 53	+11.1
Postal deficiency	42	30	- 12	-28.6
Total	3,891	2,560	-1,331	-34.2
<u>Expenditures uncertain in effect, and expenditures involving no cash outlay</u>				
Interest on public debt	866	860	-6	-.7
Old-age reserve account	265	540	+275	+103.8
Retirement funds	47	73	+26	+55.3
Refunds	49	53	+4	+8.2
All other <u>2/</u>	5	-171	-176	-
Total	1,232	1,355	+123	+10.0
Total gross government expenditures <u>2/</u>	9,412	7,517	-1,895	-20.1

1/ Adjusted service bonds redeemed and odd-amount checks cashed.

2/ These figures understate gross expenditures since they fail to take into account the expenditures of credit agencies which are partially or wholly offset by the receipts of those agencies. In the fiscal year 1937 such expenditures amounted to \$548,000,000. No estimates of these expenditures are available for the fiscal year 1938.

TABLE 3

Construction Expenditures in 1937 and 1938 Budgets by Purposes
(Millions of dollars)

	<u>1937</u>	<u>1938</u>	<u>Change</u>	<u>Percent Change</u>
PWA - gross expenditures	385	419	+34	+8.8
Highways, rural roads, grade crossings	371	303	-68	-18.3
Public and institutional buildings	93	79	-14	-15.1
TVA, Boulder Canyon, reclamation, dams, etc.	167	123	-44	-26.3
River & harbor works, flood control	238	186	-52	-21.8
RFC and REA construction loans	102	194	+92	+90.3
War Department - military construction	87	68	-19	-21.8
Navy Department - military construction	278	277	-1	-0.4
Merchant marine - construction	8	79	+71	+887.5
Miscellaneous	<u>55</u>	<u>18</u>	<u>-37</u>	<u>-67.3</u>
Total	1,785	1,746	-39	-2.2