For immediate release March 25, 1946

Statement by Chairman Eccles:

In testifying before the Banking and Currency Committee of the House in opposition to continuance of price controls, President Wason of the National Association of Manufacturers contended that the enormous accumulation of liquid funds available to the general public does not constitute an inflationary danger at this time.

As an aid to correct evaluation of the inflationary pressures inherent in this volume of liquid funds, I am making public the attached comments on the reasoning and arithmetic whereby Mr. Wason arrives at his astonishing conclusion.

The National Association of Manufacturers on Liquid Assets

President Wason of the National Association of Manufacturers in his testimony in opposition to the extension of the Price Control Act on March 18 commented on an earlier statement by Mr. Bowles with regard to the inflation potential inherent in the accumulation of wartime savings. In discussing consumer demand, Mr. Bowles stated that wartime savings of the people now amount to 145 billion dollars. He appraised the significance of these savings as follows:

> "Should people, whether consumers or businessmen, once lose confidence that the price line will be held and rush to meet future needs ahead of anticipated price increase, these vast wartime savings could throw the Nation into a wild inflationary scramble exceeding any it has ever experienced."

Mr. Wason apparently interprets Mr. Bowles figure of 145 billion as referring to the Federal Reserve estimate of liquid assets (that is currency, deposits and U.S. securities) held by individuals and trust funds at the close of 1945. Although Mr. Bowles' reference was to different data, Mr. Wason's interpretation will be followed for purposes of these comments.1/ How, then, does Mr. Wason manage to reduce his initial figure of 145 billion to a mere 17 billion, and how does he conclude that these assets do not constitute an inflationary danger if only production is allowed to expand without price ceilings?

Mr. Wason's Figures

(1) At the outset it must be noted that Mr. Wason's total of 145 billion is no overall figure for liquid assets held by the public. It is limited to personal holdings only and excludes holdings by corporations and unincorporated businesses. If 52 billion dollars of corporate holdings (excluding banks and insurance companies) and 28 billion dollars of holdings by unincorporated businesses are added, the overall figure for December 1945 becomes 225 billion.2/ Business demand at this time is as much a part of the inflation problem as are purchases by consumers. The danger of excessive inventory accumulation is an important factor. Thus, liquid assets held by businesses, as well as by individuals, are part of the broader picture.

(2) Even the 225 billion holdings for these groups is not all inclusive. It excludes Treasury deposits which will be added to private cash holdings and checking accounts when the Treasury balance is disbursed. Also, it excludes holdings of liquid assets by non-profit associations, State and local governments and certain other groups. A more inclusive figure (still excluding holdings by Government trust funds, commercial banks, savings banks, and insurance companies) for December 1945 approaches 275 billion dollars.

1/ Figures used by Mr. Bowles were derived from Dept. of Commerce estimates of individual savings during the war period. By coincidence the total happened to be the same as FRB figures for total personal holdings of liquid assets as of Dec.31,1945. Accordingly, Mr. Wason's interpretation is readily explained.

2/ For a breakdown of these figures, see Federal Reserve Bulletin for February 1946, p. 123.

(3) In reducing the 145 billion dollars of personal holdings to 17 billion dollars, Mr. Wason first excludes all items other than currency and demand deposits held by individuals -- that is, he excludes holdings of all types by trust funds (16 billion), as well as all time deposits (45 billion) and U.S. security holdings (41 billion) of individuals. Thus, he reduces the total from 145 to 43 billion. While there is justification for arguing that liquid assets held in the form of currency or demand deposits are more likely to be spent than those held in the form of time deposits or as investments in U.S. Government securities, this difference is one of degree only. Certainly, it is not justifiable to exclude altogether the 86 billion dollars of time deposits and U.S. security holdings by individuals. Should investors be given reason to fear that the purchasing value of their investments might dwindle away due to price increases, securities would be offered for sale on a large scale. In protecting the Government security market the banking system would have to stand ready to absorb these securities and in the process they would be transformed into cash and demand deposits, which would then be available for expenditure.

(4) Taking the 43 billion dollars of currency and demand deposits held by individuals, Mr. Wason argues that the amount held in 1939, or 11 billion dollars, should be deducted and only the increase of 32 billion be considered. Some adjustment of this kind is not unreasonable. Individuals and businesses may be expected to draw more readily upon recent additions to their liquid assets than to reduce their holdings below a level to which they have been accustomed for some time. Yet, it does not follow that, therefore, the entire amount of prewar holdings cannot be drawn on under any circumstances. That depends on people's expectations as to price developments.

(5) Next, Mr. Wason points out that personal incomes have about doubled since 1939 and concludes that people may hence be expected to carry approximately twice the amount of their prewar holdings of liquid assets. Deducting another 15 billion on these grounds, he arrives at a total of about 17 billion. Again, Mr. Wason much overshoots the mark.

When considering the increased volume of liquid assets, some allowance can properly be made for the simultaneous expansion in the level of output and income. Some increase in the level of liquid asset holdings is to be expected. However, the sharp increase in liquid assets relative to the level of national income that has occurred (see table) far exceeds a reasonable allowance for this factor under present conditions, when a large part of the gross national product is not yet available to civilian purchasers and production is not yet adjusted to demand. Thus, liquid assets held by businesses and individuals were 60 per cent of gross national product in 1941; for the end of 1945 the same percentage is estimated at 124 per cent. Taking demand and currency alone, the increase is from 30 to 48 per cent. Taking U.S. security holdings, the increase is from 12 to 50 per cent. These are large increases and should not be dismissed as merely the result of higher levels of income and production.

LIQUID ASSET HOLDINGS AND GROSS NATIONAL PRODUCT
(in billion dollars)

Calendar Year	GNP	Liquid Assets Held by Individuals and businesses[1/]				As Percentage of GNP			
		Total	Demand Deposits and Currency	Time Deposits	U.S. Govt. Securities	Total	Demand Deposits and Currency	Time Deposits	U.S. Govt. Securities
1921	70.7	52.9	17.5	16.6	18.8	74.8	24.8	23.5	26.6
1929	99.4	60.7	22.1	28.6	10.0	61.1	22.2	28.8	10.1
1932	55.4	51.0	17.1	24.8	9.1	92.1	30.9	44.8	16.4
1940	97.1	67.6	28.9	26.7	12.0	69.6	29.8	27.5	12.4
1941	120.5	74.2	33.9	27.1	13.2	61.6	28.1	22.5	11.0
1942	151.5	90.3	41.1	26.5	22.7	59.6	27.1	17.5	15.0
1943	187.8	130.9	57.6	29.6	43.7	69.7	30.7	15.8	23.3
1944	198.7	169.7	67.8	35.0	66.9	85.4	34.1	17.6	33.7
1945[2/]	182.0	225.3	87.4	48.2	89.7	123.8	48.0	26.5	49.3

1/ Holdings as of June 30. Commercial banks, savings banks and insurance companies are excluded.

2/ GNP is tentatively estimated annual rate for end of year and liquid asset figures are for December 31.

For further details see Federal Reserve Bulletin for February 1946, p. 122.

Mr. Wason's Interpretation

Even if Mr. Wason's residual of 17 billion were accepted, there would be no reason for complacency. It is still twice the corresponding 1939 figure and sufficient, if expended rapidly, to touch off inflation. An analysis of the liquid asset figures in itself does not mean much unless it is related to the abnormal economic situation with which we are confronted at this time when, as a result of the war, demand is far in excess of supply. It is obvious that in urban and farm real estate, in security markets and in other areas not subject to price controls, prices have sharply advanced.

Because of the abnormality of the present situation, a sharp distinction must be drawn between the economic significance of these liquid assets in the current setting and their likely effect later on when the economy has returned to a more normal situation. At such a time the liquid assets may well be helpful in maintaining adequate demand and high employment. In the present situation, if expended prematurely, they would have disastrous inflationary consequences.

It is true, of course, that inflation is caused not by the existence of liquid assets but by their use to bid up prices. It is difficult to say to what extent they have been thus used to date, but it is a fact that there has been a sharp reduction in the rate of saving. Personal savings as a percentage of disposable income which had reached 30 per cent in the second quarter of 1945 are now less than 20 per cent and may decline still further in the course of the year. This tendency should not be accelerated by raising expectations that those who do not buy now will have to pay higher prices later on. Such a development would be invited by a weakening of OPA controls.

Mr. Wason is correct in pointing out that the use of liquid assets for purchases does not of itself reduce the total volume of such assets. If individuals or businesses draw on their liquid assets to finance purchases, the result is merely a shift of funds from the buyer to the seller. The volume of liquid assets can be reduced only to the extent that Government debt is paid off out of tax receipts or securities are sold by commercial banks to nonbank investors. Mr. Wason is therefore right in emphasizing the need for a balanced budget and contending that liquid assets cannot be absorbed by increased production.

It does not follow, however, that because large liquid assets will continue to exist, it will also be necessary to retain OPA price controls indefinitely. Inflationary pressures at this time result from the fact that there are large backlog as well as current demands while the supply of goods in many lines is inadequate and cannot become adequate in a few months because production and distribution in sufficient volume take time. Once goods become available in ample supply to satisfy current demand and the most urgent backlog demand has been met, the excessive pressures from buyers will be reduced and at the same time competition among sellers will be increased. When this happens, price controls can be removed safely even though liquid asset holdings remain large.