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## WHAT LIES AHEAD

No one is now in a position to state with certainty just what lies ahead. It depends first on what the consumer public and business firms do, which is always difficult to forecast with any great degree of accuracy. It depends second, on what the Government does -- that is, on the size of Government spending, particularly for foreign aid and defense -- which the present unsettled state of international relations makes so uncertain. Finally, it depends on the methods used by the Government to finance the spending which is actually undertaken.

So far as the buying public and business firms are concerned, there has recently been evidence that the pressure of inflation may be subsiding, at least temporarily. But this is not the first time things have looked that way since the war; and so, to judge the current situation properly we must place it in the setting of the entire postwar period.

### Origin of Inflationary Pressures

We all know that the economic developments that we have experienced in the postwar period to date have been an outgrowth of the war itself. First, while the war lasted, it absorbed about 40 per cent of our production, and as a result the things we were accustomed to in civilian life became either scarce or not obtainable. Everyone had to do without, had to postpone buying till the war was over, had to await the return of peace and prosperity. Second, in addition, the war left us with heavy responsibilities for relief and reconstruction abroad, placing a further heavy demand on our factories, on our farms, and on our other productive resources.

And, finally, the method of getting the money to pay the cost of the war has also been an important factor in the postwar inflation. Less than half the expenditure for war goods and services was financed by the noninflationary method namely by taxation. The remainder was financed through Government borrowing which is inflationary. This heavy reliance on Government borrowing meant that when the war ended people had available for spending both their high current incomes and also a large accumulation of savings put away during the war. Besides that, they had exceptionally easy access to credit. Consequently, people had a tremendous, long-deferred demand for goods for both personal and business uses; and to back up that demand they had more dollars than they had ever had before.

You can see, then, that the result has been that the public has been trying to buy things faster than they could be produced. The demand was greater than the supply. Therefore, prices have risen steadily. And rising prices produce greater incomes, which in turn produce still greater demand, which in turn produces still higher prices. Thus the vicious spiral goes round and round and up and up. And here, in brief, are the results: Wholesale prices have increased about 110 per cent since 1939; consumer prices 73 per cent; and personal income increased almost 200 per cent.

## Domestic Impact of the International Situation

Now it is important to note that the problem of maintaining price stability has been considerably aggravated by a disturbed international situation. The end of World War II meant the termination of hostilities but not the resumption of peace, except peace of a very uneasy kind. We have not been able to ignore the possibility that an international crisis might develop at any time.

As a result, expenditures for national defense are higher than they ever were in peacetime and are going still higher. Added to these are the country's vast foreign aid programs for relief and reconstruction, which reflect not only humanitarian motives but also a desire for security. We have been sending abroad more goods than we have been receiving, and this excess is financed largely by Government aid. Though this excess of what we send out of the United States over what we receive from abroad has declined from its peak reached in the first half of 1947, it is none the less still very great.

## Past Interruptions in the Course of Inflation

However, the postwar inflation has not followed an entirely uninterrupted course. In the period from March to June last year, and again in the first two months of this year there was evidence that things were getting better. But each time it turned out to be only a temporary lull, after which the inflation resumed its progress, carrying prices to still higher levels.

## Recent Indications of Abatement of Inflationary Pressures

And now again the pressure of inflation seems to be subsiding. First, both retail and wholesale prices on the average are somewhat lower than they were at the peak last August. Second, the supply of many goods is now in better balance with demand at current prices than at any time since before the war. Third, the big harvest of this year has resulted in reduced prices of such basic crops as wheat, corn, and cotton, which are now down close to the levels supported by our Government; also important is the fact that the agricultural situation abroad has also improved. Fourth, the number of new houses and apartments started each month has been declining since May of this year, in contrast to the pattern of 1947 when the number of new units started kept on rising through the summer and early fall. Fifth, department store sales in the pre-holiday period were below those of 1947 until well into December; while for November and December as a whole sales only about equalled those of last year, despite higher personal incomes. Sixth, the figures show that for some time now people seem to have been saving larger portions of their current incomes after taxes, and this of itself may reduce the demand for goods and the upward pressure on prices. Further, and finally, the use of consumer credit seems to have moderated somewhat; in October installment credit increased much less than a year ago, and also there has been a noticeable slackening in the volume of additional bank credit extended to all types of borrowers.

## Elements of Continued Strength

But, mind you, this is not the whole story, because underlying factors

remain by which a considerable expansion is possible. In the first place, practically everybody is employed and wage increases are continuing to spread. This sustains incomes and purchasing power. Also, not only business firms but people generally have large bank deposits and hold large amounts of Government securities which they can readily turn into cash. These factors form a strong base for continued high levels of buying by the consumer public.

In the second place, large programs still remain for expansion of factories and manufacturing equipment, for railroads, utilities, and other industries; also the profits of business corporations are still at record levels. And, what's more, shortages persist for many strategic commodities, particularly metals and metal products; and these shortages are being reflected in rising prices in many specific areas, such as iron, steel, lead, zinc, farm machinery, and automobiles.

In the third place, State and local governments, which have rapidly increased their spending throughout the postwar period, must still meet urgent needs for schools, other public buildings, and roads.

And finally, perhaps the factor of greatest single importance in determining the course that our domestic economy will travel from here on is the size of the Federal Government's expenditures. Even if the President's recently recommended 15 billion dollar ceiling on the military budget is followed, Federal expenditures for the next fiscal year, from July 1949 to June 1950 are still likely to be higher than for the current year. But if it is necessary to enlarge the military budget to a figure greatly in excess of this amount, as informed and able military leaders seem to recommend, according to published reports, then further price inflation is bound to follow unless we find some positive means of preventing it. What will we have to do? The answer is clear. The supply of critically important materials will have to be tightly allocated. Taxes will have to be raised in order to avoid an inflationary Government deficit. And if we fail to raise taxes sufficiently, we shall be able to avoid substantial price increases only by extensive price and other direct controls.

It is clear, then, that the problem of maintaining stability in our domestic economy is greatly dependent on the state of the international situation. In the absence of further substantial increases in defense expenditures, there would be some grounds for believing that stability might be achieved through successive readjustments in the supply and in the price of one commodity after another. But if defense expenditures do mount rapidly, then this certainly means that we can avoid further inflation only if we have the courage to adopt vigorous countermeasures and the wisdom to adopt them before it is too late.

Therefore, what lies ahead, speaking broadly, depends largely on the international situation abroad and our collective action at home.