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business review

FEDERAL RESERVE
BANK OF
PHILADELPHIA

CREEPING INFLATION: THE PICKPOCKET OF PROSPERITY

*Inflation is a vice of so frightful mien,
As to be hated needs but to be seen;
Yet seen too oft, familiar with her pace,
We first endure, then explain, then embrace.*
— With profound apologies to Alexander Pope

THE NEW MATURE ECONOMY

The new mature economy thesis is different from its predecessor. It isn't shrouded in gloom. It has a Hollywood ending—happy.

THIRD DISTRICT BANKING

Expansion in loans during first half year accompanied by decline in investments. Substantial increase in total earnings over a year ago largely offset by higher current expenses.

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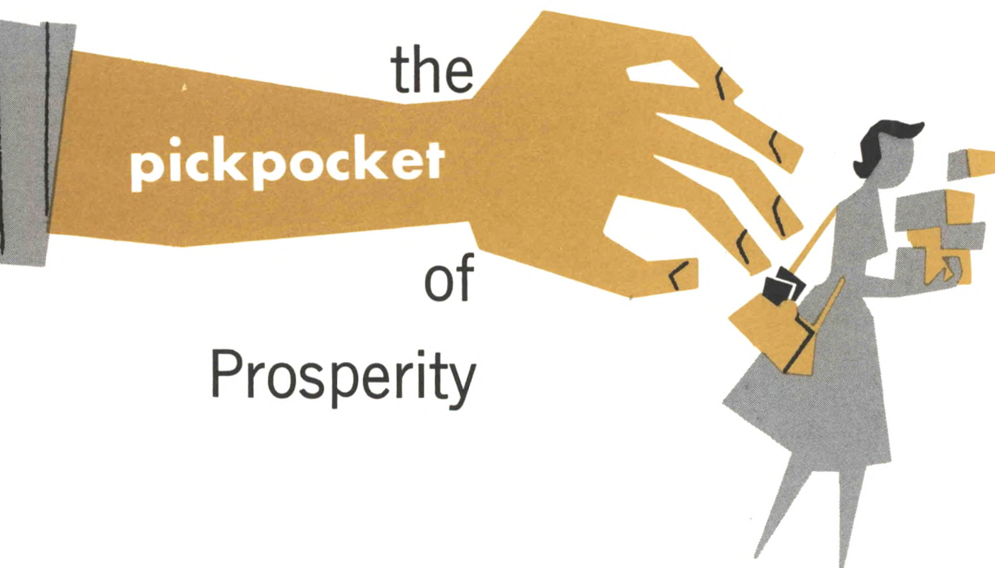
Creeping Inflation: the pickpocket of Prosperity



Cost of Living Rose to New Record in June for 10th Month in a Row—WALL STREET JOURNAL, *July 25, 1957*

A simple act of inflation is to blow air into a toy balloon. Kids love it. A more sophisticated form of inflation is to blow too much money into the economy. Some adults love it because it creates a feeling of prosperity.

Not prosperity, but a feeling of prosperity. For what does it profit a man if he gets twice as much money, when it costs three times as much to live?

Money bewitches people. They fret for it, and they sweat for it. They devise most ingenious ways to get it, and most ingenuous ways to get rid of it. Money is the only commodity that is good for nothing but to be gotten rid of. It will not feed you, clothe you, shelter you, or amuse you unless you spend it or invest it. It imparts value only in parting. People will do almost anything for money, and money will do almost anything for people. Money is a captivating, circulating, masquerading puzzle.

Ask an economist about money and you may be sorry. He will tell you that money is a medium of exchange, a standard of value, a store of value, and a standard of deferred payments. See what we mean!

How money works as a medium of exchange, we first discovered at a tender age when we found with great delight that pennies buy lollipops. As we became bigger operators, we developed bigger wants that required bigger money. Bigger wants are taken care of nicely with 2½″ by 6″ paper portraits of various notables—Washington for a dollar, Lincoln for five dollars, Hamilton for ten, and so on. These are freely passed from hand to hand with almost total disregard as to whose portrait is worth what. That's what "medium of exchange" means.

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The claim that money is a standard of value is one of those things. If money were the standard of value that it is supposed to be, the same amount of money would always buy the same amount of goods. But it doesn't. We know from recent experience that the dollar is slipping because it takes more of them to get the essentials of life. The one-dollar silver certificate is identified as one dollar no less than 15 times on the face and 10 times on the back—and so it is. But in the market place, it's not the dollar it used to be. The dollar is a standard of value but not a stable standard like a yard or a gallon or a ton.

The claim that money is a store of value also requires some apology. When you check a suitcase full of personal belongings at a baggage counter, you get a ticket or a claim check and go about your business confident that you can reclaim the bag upon surrender of the ticket. If, upon doing so, you find that half of your clothing and other personal effects have been removed, you would set up a big howl, saying, "I've been robbed." In like manner, if you tucked $100 under the mattress several years ago for safekeeping, you find you have been robbed because those dollars buy less in today's markets.

As a standard of deferred payment, money also leaves considerable to be desired. The investor that today buys a 10-year bond for $1,000 is entitled to $1,000 in 1967, but who knows what the purchasing power of the dollar will be in 1967? If the dollar will be worth more than it is at present, the investor makes a speculative gain; if it will be worth less, he will suffer a speculative loss. The dollar can be as fickle in the future as it has been in the past.

Living as we do in a money economy there is nothing for free. Everything costs money. Everything has its price, and the price is always so much money. Now money, as has already been insinuated, does not always behave as it should and the telltale evidence of the misbehavior of money is the behavior of prices.

THE BEHAVIOR OF PRICES

Prices seldom stand still for any length of time. When the housewife goes to market she may observe that coffee and potatoes cost a cent or two less than the week before, and that pork and butter cost two or three cents more. A price-conscious housewife is also quick to observe similar changes in department-store merchandise. At the same time that prices of linens and yardgoods may be falling, the prices of men's shirts and children's shoes may be rising. That's the way life is.

Price changes are the inevitable result of changing conditions of demand and supply in markets where freedom of competition prevails. Increasing demand or diminishing supply tends to bring about higher prices, and decreasing demand or increasing supply tends to bring about lower prices. Moreover, changing prices are not only passive results of changes in supply and demand but also active causes thereof. Rising prices stimulate production and discourage demand, and falling prices encourage demand and discourage production.

Prices are the automatic regulators that tend to keep production and consumption in line with each other. In the performance of this function, however, it is quite common for the prices of some goods and services to be rising while the prices of others are falling, and that is the point we wish to stress here.

THE MISBEHAVIOR OF MONEY

When prices of everything are going up, it is not because everything is worth more, but because the dollar is worth less. The value of a good is its power to command another good in exchange for

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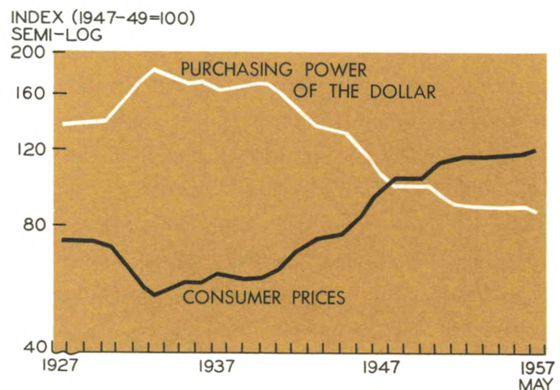
itself. If a pencil costs 10 cents and a pen costs a dollar, it means that a pen is worth ten pencils, or a pencil is worth one-tenth of a pen. Should prices of everything double, then pens would sell for $2 and pencils for 20 cents each. Ten pencils would still exchange for one pen, and inasmuch as prices of all things have doubled, their exchange ratios or value remain the same. But something has happened to the value of the dollar. It has been cut in half. That's inflation.

Again, should prices of everything be halved it would not be because everything is worth less but because the dollar is worth more. That's deflation. During a period of inflation, prices rise and the dollar loses purchasing power. During a period of deflation, prices fall and the dollar gains purchasing power.

How money misbehaves is shown by the chart with only two lines. The line labeled "Consumer Prices" is the official consumer price index compiled by the Bureau of Labor Statistics, and it measures the changes in prices of goods and services purchased by families of city wage earners and salaried clerical workers. The index is based upon prices of about 300 items in 46 cities. In short, the line shows how the cost of living rises and falls with respect to a base period (1947-1949 = 100) to which the line is anchored.

The other line labeled "Purchasing Power of the Dollar" is the same story translated so that it shows what happens to the value of the dollar when consumer prices rise and fall. You can see that the two lines are reciprocal, as indeed they must be because when the cost of living rises, the purchasing power of the dollar falls and it takes more dollars to maintain your standard of living. When consumer prices fall, the purchasing power of the dollar rises and it takes fewer dollars to buy the goods and services to which you are accustomed.

WHAT CHANGING PRICES DO TO THE BUYING POWER OF THE DOLLAR



Now look what has happened during the past three decades. In the years of the Great Depression from 1930-1933, consumer prices took quite a slide. You can see what World War II did to the cost of living. Note the rise in consumer prices from 1940 to 1943. After the end of the war, consumer prices took another big jump. They seemed to have reached a plateau in the stretch between 1952 and 1955, after which they again started moving upward. The index rose from 60 in 1940 to 120 at present, which means that we now pay one dollar for what cost only 50 cents in 1940. World War II caused most of the inflation.

War requires weapons and wampum

Producing weapons for war is inflationary. Output of civilian goods is reduced to a minimum as productive facilities are pressed into the making of weapons. The gainfully employed, however, receive wages for their work regardless of whether they make bazookas or butter. But civilians don't spend their money for munitions, so the extra bazooka money which is not taken away from them in taxes churns up prices in the butter market despite desperate efforts to prevent it. War always fills the purse faster than the pantry.

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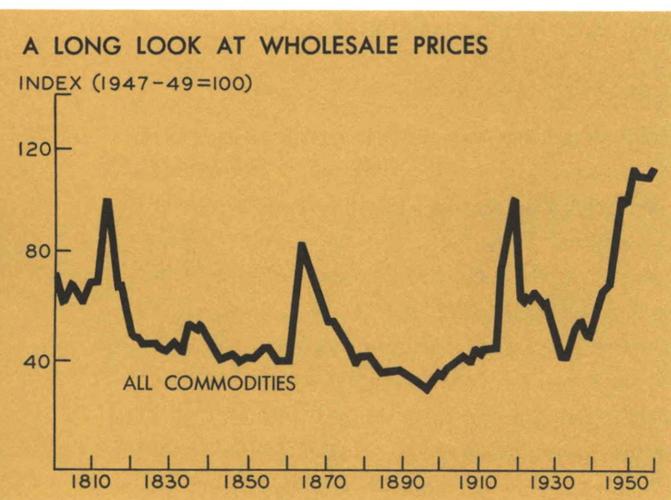
War is inflationary in still another way—the way it is paid for, or rather the way it is not paid for. The cost of the war not raised by taxes is borrowed by selling bonds. Government bonds bought by people, savings banks, insurance companies, commercial and industrial corporations come out of savings, and such bond buying is not inflationary.

Not so the buying of bonds by commercial banks. The bonds they buy feed the fires of inflation because they do not buy bonds out of their savings but out of money which they create. The money comes right off the keyboard of the bookkeeping machine in the bank. Technically, such money is called "demand deposits" against which the borrower can draw checks.

"There she blows!"

After World War II a lot of the Government bonds were turned into money, and that can be done faster than making automobiles, so there was more inflation. People cashed their bonds at the banks, lenders sold Governments to make loans, and the Federal Reserve as the ultimate buyer under the support program supplied the high-powered reserve dollars needed to support the swelling money supply.



Inflation seems to be an inevitable by-product of war. This is confirmed by the long-run record of wholesale prices, shown in the accompanying chart. All the mountain peaks are the handiwork of Mars. Germany, after World War I, had an inflation that out-flated all inflations. Printing presses turned out paper marks by the trainload, and the cost of living rose 1,200 billion times. Mortgages, bonds, and other long-term contracts became absolutely worthless, and life insurance policies were not worth the postage required to notify the company of the decease of the policy holder. What started out as just a little inflation wound up in complete collapse and chaos.

To be sure, no one is advocating that we go on a gigantic inflationary fling and wreck our economy like the Germans wrecked theirs. But why not try a little inflation, just a few cents worth a year —an "ever normal" debasement of the dollar, a planned inflationary prosperity?

THE CHARM OF CREEPING INFLATION

Creeping inflation has charm, seductive charm. It is a delusion, but such a delightful delusion. It affords an apparently easy way out of so many of the daily difficulties that confront us.

Creeping inflation sends up prices on the securities markets, farmers wishing to sell out get fancy prices for their farms, businessmen find it easier to make profits that come from inventory appreciation and higher selling prices, and workers get higher wages. The prosperity doesn't ring true, but it rings the cash registers because there is more money around. People on fixed incomes do not share in the additional money unless they own a share or two of stock, in which case they get a whiff of prosperity.

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Creeping inflation is a monetary patent medicine, an economic elixir. It is a soothing compound containing syrup sweet to the taste, and alcohol to dull the senses. Recommended doses: 2 to 3 per cent a year. It is good for all diseases of the body economic. Will prevent falling pricitis, underflourishment, profit deficiency, and inventory indigestion. Creeping inflation is a habit-forming economic tranquilizer.

Because creeping inflation wears a false face of prosperity, many people are easily fooled by it. First, it is tolerated, then it is accepted, and finally it is rationalized. In fact, the rationalizing has already begun. We are told that the country is confronted with a choice of three evils. We must accept enough unemployment to keep labor costs from rising, or impose direct Government controls over wages and prices, or embrace creeping inflation. The first is socially undesirable, the second is politically impossible in times of peace—which leaves creeping inflation as the least of the three evils. So goes the argument.

Is it true that we must choose some form of evil? To say so does not necessarily make it so. It has not been proven that the only solution to heavy unemployment is ever-rising prices. On the contrary, if inflation is allowed to run its course we may ultimately precipitate unemployment of really serious proportions.

THE PICKPOCKET OF PROSPERITY

Simply because all our business reckoning is done in dollars, it is so easy to fall for the fallacy that more dollars bring more prosperity. The essence of prosperity is not more dollars, but more goods and services. We can consume only what we produce. If we want to consume more, we must produce more—and there is no money magic that will enable us to consume more than we produce.

Currently we—all 170 million of us—are producing and consuming goods and services at the rate of $434 billion a year. Last year we were producing and consuming at the rate of $415 billion. With pride we point to the $19 billion increase. But that was in dollars, and don't forget that consumer prices rose over 3 per cent during the past year, so a large part of the increased prosperity was phoney. Well over half of the gain was nullified by the depreciation in the purchasing power of the dollar. And yet there are a lot of grown-up people who still believe in Santa Claus. Confusing money with wealth, they think that if everybody has more money everybody is better off.

Well, suppose the Government were to adopt a policy of creeping inflation, say, 3 per cent a year so frequently advocated. Consider the factory worker, head of a family, making $6,000 a year. Knowing that the cost of living will rise 3 per cent each year, he will demand an escalator clause so that his wages will go up automatically with the rising cost of living. By so doing he contributes to further inflation because contracts of this kind cause price increases to spread far and wide.

Consider the school teacher, age 40, whose only income is his salary. What a dreary prospect creeping inflation holds for him! A 3 per cent yearly increase in the cost of living is tantamount to an annual cut in salary. Creeping inflation picks his pocket year after year. When he is 65 and ready to retire, his dollars will have shrunk to 47 cents, and a $3,000 annual retirement income will have less than $1,500 purchasing power. Government workers, hospital employees, social service workers, and many other salaried people will have their pockets picked in this kind of "prosperity."

Creeping inflation makes suckers out of savers. It would systematically pick the pockets of the 100 million holders of life insurance policies, the 15 million savings and loan shareholders, the 14 million employees with pension rights under private

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plans, the 66 million people covered by social security, and the 67 million with savings deposits in commercial and savings banks. It is a delusion to think that creeping inflation—a mere 2 or 3 per cent a year—does no harm. A 2 per cent annual rise, compounded, would double the price level about every 35 years. A 3 per cent annual rise would double prices about every 23 years.

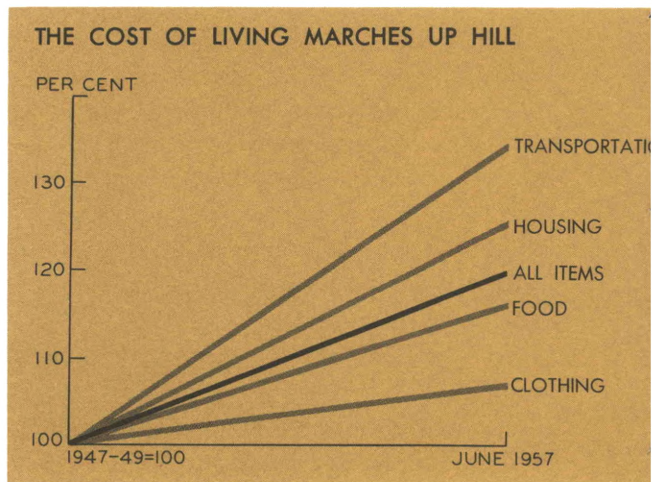
Moreover, there is a world of difference between a fortuitous creeping inflation, such as we are now having, and a planned creeping inflation. Suppose the Government were to accept as a national policy the inevitability of a 2 or 3 per cent annual inflation. As citizens would come to know that the Government is not only accepting but seeking a slow and steady depreciation of the dollar, they would realize that there is no point in holding insurance policies or putting money into savings accounts, savings bonds, and other forms of dollar assets. Instead of saving, they would put their money into real estate, commodities, equity securities, and other forms of investment that ride with the rising tide of inflation. It would make us a nation of speculators rather than savers.

It is naive to believe that a deliberate policy of 2 or 3 per cent inflation could be maintained indefinitely. Inflation, by its very nature, feeds on itself, and it would not be long before creeping inflation would accelerate to running inflation and ultimately galloping inflation. Moreover, if we are simple-minded enough to believe that a little inflation brings a little prosperity, then why not double the inflation and double the prosperity? Having gone that far, let's redouble the inflation and redouble prosperity. If more money is the royal road to prosperity, it is easy to make ourselves fabulously wealthy.

Inflation, wherever and whenever it is tolerated, is a pickpocket of prosperity, and the bigger the inflation the bigger the pocket picking.

THE COURSE OF CREEPING INFLATION

Pocket-picking is going on right now, all around us. The cost of living has already gone up 20 per cent above the 1947-49 base period, as shown by the "All Items" line in the chart. As might be expected, some items rose more briskly than others. The clothing dollar was the best behaved and the food dollar also did not get too far out of line. The bad actors were housing, which includes rent, and transportation costs. These costs rose 25 and 35 per cent, respectively.



For four years we seemed to have achieved price stability. From 1952 to early 1956 the cost of living held very steady. Rents rose during this period but the declining cost of food helped to keep the over-all average on a fairly even keel.

Early in 1956, however, the cost of living resumed its upsurge and all of the components, including food, joined in the advance. In June 1957 the cost of living was about 5 per cent above the March 1956 level when the uphill march began. That is a very high rate of depreciation for the American dollar.

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CAUSES OF CREEPING INFLATION

Currently, the critics can't agree as to the causes of our creeping inflation. One group says it is basically demand pulling prices higher, and the other group says it is rising costs pushing prices higher. Let us examine the debate between the "demand pullers" and the "cost pushers." The demand pullers stress the fact that we have in our economy three great groups of spenders—namely, consumers, business, and government—whose combined actions exert a powerful pull on prices.

The country's 170 million consumers, as a group, have a lot of pull. They stepped up their expenditures from $231 billion in 1953 to a current annual rate of $278 billion. Most people love to spend and will do so at the drop of a down payment.

Governments are easy spenders. They spend $87 billion a year for things no one can possibly object to—common defense and general welfare. But defense and welfare are costly commodities with bigger price tags each year.

Businessmen are courageous spenders. The amount of money they put into new plant and equipment since the end of World War II has amazed everybody including the businessmen themselves. In the past four years, they have spent over $160 billion for this purpose, and this year they are spending at the rate of $49 billion. Businessmen, governments, and consumers are a powerful trio of demand pullers, and it is hardly becoming for any one of them to hold the others responsible for contributing toward inflation.

The table-thumping theory of wages

Creeping inflation is also aided and abetted by a vast army of cost pushers. The country's 66 million workers are potential cost pushers, and the 18 million organized workers are organized cost pushers. Fed up with having their pockets picked by the rising cost of living, workers demand more wages. Fearful of what higher wage costs will do to their profit margins, employers resist the demands of workers. Then starts the collective bargaining—the democratic process of table thumping. In due time an agreement is reached, and the betting on the sidelines is on the question of how much prices will be raised as a result of the higher wages.

It should not be necessary to raise prices if the wage increases do not rise faster than the increases in labor productivity. That all the wage increases taking place are "necessary" is both alleged and denied. In any event, it appears that price increases always follow on the heels of wage increases, and because wages are the largest cost component in so many industries it is difficult to escape the conclusion that rising wages have something to do with creeping inflation.

Moreover, some of the wage agreements have escalator clauses that gear the wage rates right into the cost of living. An escalator clause provides that for every change of so many decimal points in the B.L.S. index of consumer prices, the workers shall automatically get an increase or decrease of so many cents in their basic wage rates. Last April when the cost of living rose three-tenths of 1 per cent, about a million-and-a-half workers in the automobile, electrical, and farm-equipment industries got automatic pay boosts of several cents an hour. Sooner or later the increased costs of production break out in higher prices of these items, and up goes the cost of living. Then the workers in escalated industries are entitled to another automatic pay increase. Sure enough, in May, the official cost of living rose another three-tenths of 1 per cent and up went the wage rates. The June increase in the cost of living jacked up wage rates another notch. More and more union-

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ized workers are jumping on the escalator bandwagon, and you can see why.

Inflation automation

Wage escalation is automated inflation without vacuum tubes, transistors, or printed circuits. It is built-in inflation. Once installed it is automatic, requires no servicing or adjustment, never wears out. It has no moving parts except wages and the cost of living. Rising costs of living drive up wages, and rising wages drive up the cost of living.

The cost pushers are only seeking to escape the ravages of inflation. Workers are trying to preserve their standard of living, and businessmen are trying to preserve their profit margins. But in pushing up prices, both of them are helping to bring about the very thing they seek to avoid. Everybody's price is someone else's cost.

Is creeping inflation caused by demand pullers or cost pushers? It is not a case of one or the other; both forces are at work. Trying to assess their relative importance in the current inflationary climate is like trying to determine which blade of the scissors does most of the cutting. But we do know that demand pullers and cost pushers together are cutting down the dollar.

Whether demand pulling or cost pushing, the inevitable side-car of rising prices is money—sufficient money to support the rising prices. How eagerly and easily banks accommodate the demand for more money has already been observed, and currently businessmen are borrowing heavily. Prices, however, are not solely dependent upon how much money is at work but also upon how hard the money supply is working. Money goes round and round from butcher to baker to lipstick maker, and the same amount of money going around twice as fast has the same effect on prices as twice the amount going around at the former rate of circulation. Last year the money supply increased only 1 per cent, but it circulated 8 per cent faster. That helped inflation to creep.

THE CURE FOR CREEPING INFLATION

Dollars without goods do no good

We need not be unduly concerned about the relative merits of the push-or-pull argument. One thing we do know, and know full well, is that there can be no inflation without an over-abundance of money that leaves a gap between total spending and the available supply of goods. Dollars without goods do no good.

Sometimes it is advocated that the best way to close the gap is to produce more goods. Increased production alone, however, will not solve the problem because extra output means extra input. The additional man-hours and the extra flow of materials together with increased profit on the extra output will yield additional income—so we have not made any progress toward licking inflation. The gap remains.

A more effective way is to remove the surplus money that's doing the damage to the dollar. Making money scarcer means people will have to pay more to borrow it. Money, like everything else, has its price and the price is the interest rate.

The interest rate is determined in the credit market in the same way that the price of steers is determined in the cattle market. Droves of steers stampeding the market depress prices; a big demand in the face of light shipments boosts prices. In the credit market, borrowers—consumers, businessmen, and governments—seek funds from the lenders: insurance companies, mutual savings banks, savings and loan associations, and commercial banks.

When the borrowers want more funds than the available supply of the lenders, interest rates go up and money is said to be "tight," in the jargon of the trade. Interest rates have been rising and

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money has been tight for over a year, primarily because the demand has been greater than could be supplied out of savings.

The Federal Reserve is commended by some and condemned by others for allowing money to get tight and for raising the discount rate, which is the interest that commercial banks must pay when they borrow from the Fed. Control over the money supply is exercised by regulation of the reserves available to commercial banks so that growth in the money supply will not put excessive pressure on the demand for goods and services available.

In restricting the supply of money and credit, spending borrowed funds is discouraged because of the increased price of money—the higher rate of interest. In effect, higher-priced money is substituted for higher-priced goods. The available supply of money and credit then goes to those who are willing to pay the higher price for borrowed money. So money becomes "tight" not through an actual reduction in the supply of money and credit but because of increased demands of borrowers. Had the Federal Reserve obliged with enough credit to satisfy all the demands, it would have added greatly to inflationary pressures without adding to the supply of goods, and prices would have shown an even greater rise.

Tight money is said to pinch the small businessman and to interfere with the construction of much-needed schools, roads, and housing. So it does, but so do rising prices or direct rationing. There is no painless way to stop inflation. If it is allowed to continue unchecked, ever-higher prices and ever-rising costs will hurt more people and hurt them harder than tight money.

Uncle Sam spends over a billion dollars a week

It is difficult, if not impossible, to curb creeping inflation without some help from Uncle Sam. He is a big operator who spends at a rate in excess of a billion dollars a week, and that has a terrific impact on our economy. Like so many of us, he finds it hard to live within his income and when he doesn't, he adds to the inflationary pressures.

Money taken from us in the form of taxes reduces our spending power, to be sure, but if the Government spends the money inflationary pressure is not *reduced* one whit. If the Government spends more money than it takes from us in taxes, inflationary pressures are increased.

Uncle Sam could really be helpful in the fight against inflation if he learned not only to live within his income but to have a good surplus when inflation threatens. If the Federal Government wants stable money and lower interest rates, it can have them by reducing its expenditures and its heavy demands on the money market.

In days gone by, unscrupulous sovereigns debased their currencies by nicking the coin of the realm, which had disastrous results. By tolerating creeping inflation—which is the pickpocket of prosperity—we could go down the same road. With mass prosperity and mass savings, economic welfare requires a dollar that is kept sound both as a medium of exchange and a store of value. Which would you rather have—a stable economy built on a stable dollar or a wobbling economy built on a woozy dollar?

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THE NEW MATURE ECONOMY

A few years ago we heard a lot of the saying "Old soldiers never die, they just fade away." It seems to some of us who read the literature on economics that old ideas don't even fade away, they're just reclothed to fit the times.

One explanation for the depression of the 1930's was called "the mature economy thesis." Many will remember it and shudder. Contemplating it doesn't make for pleasant reflection. Briefly, it said that our population totals were growing and would continue to grow only very slowly; our capital plant was completed and additions to it would not involve tremendous expenditure; our frontiers were closed—there was no room to push out.

To be sure, not everyone accepted this diagnosis, even in the 1930's. But it made a deep impression. It haunted us during the war years and shortly thereafter. (How much reconversion planning was based on the expectation of 8 to 10 million unemployed in 1946 and 1947?) Slowly, however, we moved away from the shadow of the mature economy thesis.

The recession of 1949 was barely observable. Some refused to call what happened in 1953 and early 1954 anything more than a mild readjustment. Boom in 1955 clinched it. The mature economy thesis was just one of those ridiculous notions that in times of stress gain acceptance, or so it's been said.

Now, however, a new mature economy thesis may be developing. It is different from the first. It isn't shrouded in gloom. It has a Hollywood ending—happy.

THE NEW "MATURE" ECONOMY

The new thesis has not as yet been announced as such, but its general outline is fairly well defined. It says that 1957 is the first year of an "interim" period. This interim period will be characterized by noticeably slower growth in business activity. About 1965 or so, a new era will be ushered in when the economy will burgeon forth at 1947-1956 speed once more.

The slower growth interim period comes about because: (1) War-created shortages of homes, cars, appliances, etc. have been filled. (2) The age composition of our population is such that family formation is taking place at a much slower rate than in the earlier postwar years. (3) Our capacity to produce is more adequate in terms of current and forseeable requirements.

It says, too, that our three big spending groups are showing signs of advancing age. Maturity is overtaking consumers, businessmen, and government leaders.

The mature consumer

Certainly there are many who agree that consumers are showing signs of new maturity. To some it seemed until recently that consumers' tastes were very limited. All consumers wanted were newer, bigger and better houses, cars, and television sets.

Now, however, consumers have changed their ways of living a little. They are settling down, improving their homes by gardening, adding an outdoor fire place, an extra bathroom, recreation room, or bedroom.

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Instead of buying a new car as soon as payments on the old one stop, consumers are looking to other areas of spending. Advertisements remind them that a swimming pool can be installed in the back yard for the price of a new car. Some consumers have figured out for themselves that if they drive their present car even after its ashtrays are full, they can afford an occasional trip to the shore or mountains, a dinner out for the whole family every now and again, a new suit for dad before the old one looks frayed, and, of course, another new hat for mother.

Like homes and cars, television sets are still popular but they don't seem to command quite as much consumer attention as heretofore. Consumers now talk of a piano for the recreation room, air conditioning for at least one bedroom, a clothes dryer in the basement, and an automatic dishwasher in the kitchen. Records, rock and roll and classical, are enjoying new and increased attention. Hi-fi sets and tape recorders are being bought at all levels of the income ladder. Lobster tanks and high priced appetizer counters in neighborhood supermarkets are signs of the times.

Yes, a case can be made for calling the consumer mature. But exactly what do we mean when we talk of mature consumers. Are we talking about people withdrawing from the market place and hoarding funds under the mattress? Or do we mean to say that consumers have sharpened their taste buds, and are searching for new ways (most of which cost money) of enriching their lives.

The mature businessman

The new mature businessman is said to be much different from his pre-war counterpart. He is not frightened into hasty, ill-timed actions by gyrations in the stock market. He thinks in the long run not the short run. He thinks of the broad social implications of his actions as well as the effect on profits for his firm. As such, the new mature businessman's spending is said to be much more stable —less subject to sudden violent swings one way or the other.

The original mature economy thesis was pretty much an explanation for the virtual collapse of business spending on new plant and equipment in the 1930's. The new mature economy thesis purports to prophesy that spending on plant and equipment has reached a plateau from which ascent will come only very slowly until later in the 1960's.

On the surface, there is much to support the new thesis. Certainly, capacity in many industries seems more adequate than heretofore in the postwar period. For example, we have proven that we can make more houses, cars, and television sets than we are currently consuming. But the changing nature of consumer demand prophesies inadequate capacity in other lines.

Also, while the age structure of our population makes for a relatively low level of household formation, it also promises slower growth in our working population. And many businessmen are guessing that wages and salaries will continue to climb. What these forces suggest is that employers will be under constant pressure to invest in labor-saving machinery.

The new mature businessman, therefore, may find himself investing more in the next 10 years than he did in the past decade. This may sound fanciful to some, but it is a real probability.

The mature government

It seems that government spending as a portion of our total product has been expanding since most of us can remember. There has been good reason for this. In a society like ours, the demand for services from government is constantly growing —not only for traditional services but also for

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new services. During many of our lifetimes the government has taken on new services such as lending, underwriting, anti-cyclical economic policy, and the encouragement of steady economic growth. Of course, the main reason government spending is so high today has to do with wars—past and potential.

The new mature economy thesis says that government spending as a part of total spending has hit its peak. For the next few years, at least, it will be a slowly declining part of Gross National Product. This seems to presuppose some relaxation of international tensions, since other government spending seems almost certain to increase. Certainly state and local spending for schools and highways looks as if it will continue to climb. And anyone projecting a decline in the demand for Federal services is betting against the odds.

It is entirely likely that government spending will form a smaller part of total spending in the near future. This, however, seems to depend upon a marked reduction in demand from the military. As good a guess as any might be that the government sector will continue to take about the present bite from the total income pie.

CONCLUSIONS

To some extent, the whole question is a matter of semantics. Mature economy, unfortunately connotes very old age and senility. If the word "mature" were taken without these connotations, it might be fairly descriptive of the current scene. Our economic system seems more adult than in earlier years, and only a few would deny that our major consuming groups have grown up.

If the interim period were changed to "transition period" it might suit better also. What seems to be happening is that, for the moment at least, the demand for some traditional items of mass consumption may be running out of steam. In the meantime, new mass markets for air conditioning, hi-fi sets, dishwashers, outboard motors, and the like are developing.

In the past, transition periods have been punctuated by recessions and depressions. Declines in the demand for business bellwethers so shocked the investing community as to cause sharp drops in capital spending. This time the transition promises to be more successfully bridged. More mature (adult) reactions on the part of business leaders is one reason. Another is the very heavy volume of Government spending, which tends to cushion the reverberations coming as a result of increases and declines in consumer demand for different products. The fact is, our economy could very possibly enjoy at least as rapid a rate of growth in the "transition" period ahead as it has over the years since the war.

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FIRST-HALF BANKING—THIRD DISTRICT

Outstanding credit of member banks in the Third Federal Reserve District increased relatively little in the first half of 1957, duplicating performance a year earlier. Loans expanded and investments declined in both periods, but the changes were smaller this year. The higher level of loans and somewhat higher rates of return contributed to further growth in the total income of banks, but rising expenses and subsequent adjustments provided sufficient offsets to cause a decline in profits available for distribution.

Over the six months ended June 26, growth in loans approximated $150 million or nearly 4 per cent. This increase, while substantial, was about $100 million less than in the corresponding period a year earlier. The bulk of the increase was outside of Philadelphia, while in the earlier period increases in loan portfolios were more equally divided between Philadelphia institutions and banks elsewhere in the District. The latest date for which loan details are available for all member banks is June 6. Compared with the turn of the year, the figures show expansion most pronounced in commercial and industrial loans, with smaller increases in consumer paper and miscellaneous loans and virtually no change in those on real estate. The lack of change in the latter was the result of a decrease at Philadelphia banks and a further rise outside of the city. Later in June, business loans increased further, reflecting corporate borrowing over the income tax period.

Near the middle of the year, deposits of all member banks in the District were higher than they were a year earlier, reflecting a substantial gain in the last half of 1956. As in other recent years, deposits declined in the first half of the present year. The average level in the last half of June was $8,231 million, as compared to $8,040 million in the corresponding period of 1956. Part of this increase, less than one-third, was due to the merging of nonmember banks into member banks of the Federal Reserve System. The over-all increase was largely in time deposits.

Earnings of member banks in this District totaled over $174 million in the first half of 1957, according to preliminary tabulations. The increase over the corresponding period a year ago was more than $13 million, after mergers are taken into account. This increase, due mainly to growth in loan portfolios and some increase in rates of return on earning assets, was largely offset by heavier current expenses, with the result that net current earnings were up only $1½ million. To arrive at the amount available for distribution, further adjustments have to be made. The figures show an increase in net losses and transfers to valuation reserves and a moderate increase in income taxes, with the result that net profits were down $2 million to approximately $27½ million. Dividend payments increased.

MEMBER BANKS Third Fed. Res. District (Millions $)	First half 1957*	Change from a year ago**
Earnings:		
On securities	$ 38.0	+$ 1.1
On loans	109.7	+ 10.3
Other earnings	26.8	+ 2.0
Total earnings	$174.5	+$13.4
Current expenses	110.6	+ 11.9
Net current earnings	$ 63.9	+$ 1.5
Net losses and transfers to reserves	$ 14.2	+$ 3.1
Taxes on income	22.3	+ .4
Net profits	$ 27.4	—$ 2.0
Cash dividends declared	17.0	+ 1.8

* Preliminary tabulation.
** Adjusted for mergers, etc.

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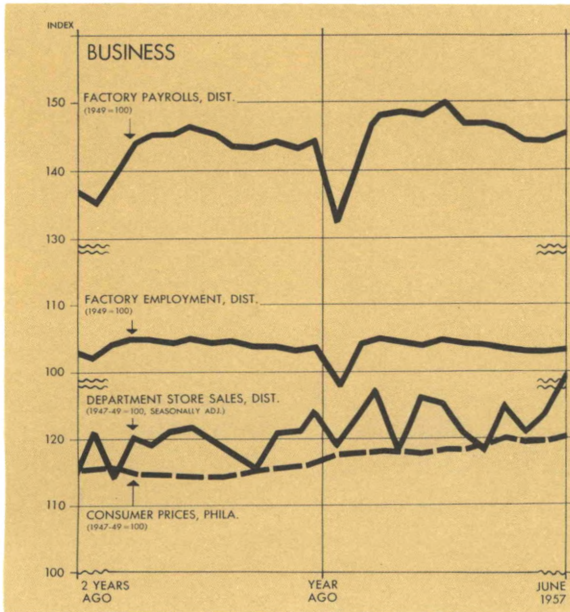

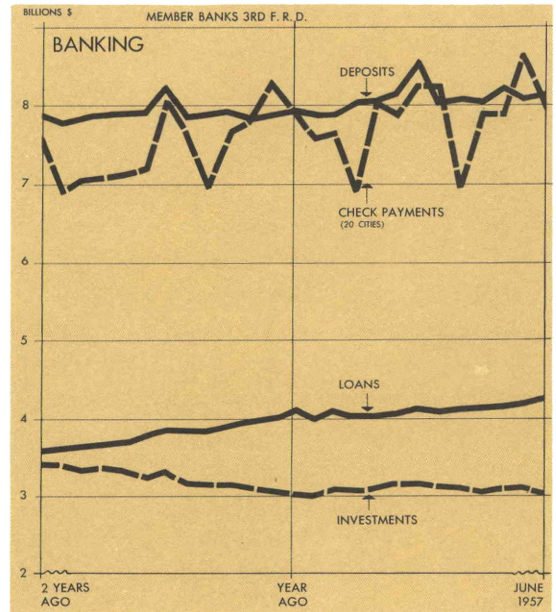

SUMMARY	Third Federal Reserve District			United States		
	Per cent change			Per cent change		
	June 1957 from		6 mos. 1957 from year ago	June 1957 from		6 mos. 1957 from year ago
	mo. ago	year ago		mo. ago	year ago	
OUTPUT						
Manufacturing production	0	−4	−4	0	+2	+2
Coal mining	+12	+7	−2	+6	+5	−1
EMPLOYMENT AND INCOME						
Factory employment (Total)	0	0	0	0	0	0
Factory wage income	+ 1	+1	+1	...	...	...
TRADE**						
Department store sales	+ 5	+4	+2	+2	+2	+1
Department store stocks	+ 2	+5	...	+2	+4	...
BANKING (All member banks)						
Deposits	+ 1	+3	+3	+1	+3	+2
Loans	+ 2	+4	+5	+2	+7	+8
Investments	− 3	0	−1	−2	−2	−3
U.S. Govt. securities	− 4	0	0	−3	−3	−4
Other	+ 1	+2	−2	0	+1	−1
Check payments	− 7†	+1†	+3†	−2	+4	+7
PRICES						
Wholesale	...	...	...	0	+3	+3
Consumer	0‡	+3‡	+3‡	+1	+3	+4

*Based on 3-month moving averages.
**Adjusted for seasonal variation.
†20 Cities
‡Philadelphia

LOCAL CHANGES	Factory*				Department Store				Check Payments	
	Employment		Payrolls		Sales		Stocks			
	Per cent change June 1957 from		Per cent change June 1957 from		Per cent change June 1957 from		Per cent change June 1957 from		Per cent change June 1957 from	
	mo. ago	year ago	mo. ago	year ago	mo. ago	year ago	mo. ago	year ago	mo. ago	year ago
Allentown	0	−2	−4	+2	...	...	...	...	− 8	− 1
Harrisburg	+1	+3	+2	+9	...	...	...	...	− 3	+ 3
Lancaster	+2	−1	+2	+4	−9	+10	− 8	+ 2	− 8	− 3
Philadelphia	0	+1	+1	+5	−1	+ 3	− 7	+ 8	− 9	0
Reading	0	−2	0	+1	−3	+17	−10	+19	−17	− 6
Scranton	+1	−1	+2	+2	−7	+ 4	− 8	− 3	− 4	− 2
Trenton	0	−1	+1	+6	+9	+ 4	− 1	+ 7	−10	+25
Wilkes-Barre	+1	+1	+2	+6	−3	− 1	− 7	+ 2	− 1	+10
Wilmington	0	+3	+2	+7	0	+ 6	− 7	+11	+15	+ 1
York	+1	−5	+2	−3	+8	− 1	− 7	− 8	− 3	− 5

*Not restricted to corporate limits of cities but covers areas of one or more counties.

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