FINANCIAL MOBILIZATION

by

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I. THE PROBLEM: GREAT EXPANSION OF DEFENSE EFFORT

Contrast with last large defense effort a decade ago

A. Differences between 1941 and 1951

1. Size and duration of the effort
   a. 11.6 million men vs. 3½ million
   b. 40 per cent vs. 16 per cent of GNP

2. Status of the Economy

3. Psychology of deflation/inflation

4. Experience with direct controls
   Difficult to administer
   At best they postpone - do not solve - inflation

B. The Economics of Defense

1. The burden arises from decision to defend
   NOT from the need to raise the money

2. Government: Defense incl. foreign aid
   Expansion of capacity (investment)
   Fiscal 1950 1952
   17.6 34 51.3

   Consumption - especially of durables - must go down
   - it doesn't make any difference how much money we have! The goods will not be available!
II. FINANCIAL MOBILIZATION

A. Current income = current output

BUT current expenditures are not limited by current income

1. Can \( \uparrow \) by spending past savings

2. Can borrow and spend future income

If some segments spend \( > \) Income
other segments must SAVE (spend \( < \) Income)

B. An Economists' Program

(Quote p. 54)

"Faced with this long-run inflationary prospect, we recom-
mend that the increase in total spending be continuously curbed in three
principal ways, and that these constitute the first line of defense against
inflation:

1. Scrutinize carefully all Government expenditures and postpone or
eliminate those that are not urgent and essential. Substantial re-
ductions can be achieved only if some programs are cut.

2. Raise tax revenues even faster than defense spending grows so as
to achieve and maintain a cash surplus. Merely to balance the
budget is not enough. If the inflationary pressure is to be re-
moved, taxes must take out of private money incomes not only as
much as Government spending contributes to them but also a part
of the increase of private incomes resulting from increased private
spending of idle balances and newly borrowed money. Larger taxes
must be paid by all of us. Reliance should be placed primarily on
increases of personal income taxes on all income in excess of
present exemptions. Higher corporate profits taxes, in one form
or another, are also imperative. In addition, loopholes in our
tax laws should be closed.

3. Restrict the amount of credit available to businesses and individuals
for purposes not essential to the defense program. An expanding
supply of low-cost credit which swells private spending cannot fail
to stimulate inflation when the supply of goods available for pri-

cate use will be difficult to expand and may even decline.

Selective controls over consumer credit, real-estate credit, and loans on
securities are useful for this purpose and should be employed. But we
believe that general restriction of the total supply of credit is also
necessary. This can be accomplished only by measures that will involve
some rise of interest rates.

If general inflationary pressure is not removed by fiscal and credit
measures, we face two alternatives: (1) Continued price inflation, or
(2) a harness of direct controls over the entire economy which, even if
successful in holding down prices and wages for a while, would build up
a huge inflationary potential in the form of idle cash balances, Govern-
ment bonds, and other additions to liquidity. Such accumulated savings
would undermine the effectiveness of direct controls and produce open
inflation when the direct controls are lifted. Everyone remembers vividly
the sharp inflation of 1946-48 when the wartime accumulation of liquid
assets went to work on prices after the removal of direct price and wage controls. "Either of these alternatives is extremely dangerous."

Variety of economists signing: Not necessarily correct but evidence of error should be clear and overwhelming. I haven’t seen such evidence yet.

C. These are difficult times

This is Lincoln’s birthday

Lincoln - Second Inaugural Address - 1865

"With malice toward none, with charity for all, with firmness in the right as God gives us to see the right, let us strive on to finish the work we are in ..."

Ol’ Mose

"Mose, you better be careful; you may be handing an innocent man!"

I spent 3 days in Washington last week. I can confirm your impression that it is a place where sound travels faster than light.

Reported in press

Everyone wants to get into act.