

## THE FEDERAL GOVERNMENT SPENDING PROCESS

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This study is concerned with the impact on the economy of the different stages of the Federal Government spending process. Because of the length of time involved in carrying out many government procurement programs, it is important to know whether the economic impact occurs at the point where expenditures are made or also, or instead, at some other place in the process.

The concern with the process of government spending arises in connection with the fluctuations in the level of governmental outlays. For many purposes of public policy and fiscal administration it is essential to have accurate instruments to record present movements and to understand their relationships to future trends. An inappropriate indicator of government spending may show an upturn when, in reality, the basic force of government spending is operating in the reverse fashion. An insensitive indicator may show little movement when in fact a great fluctuation is taking place. A lagging indicator may only show movement with considerable delay.

### A DESCRIPTION OF THE GOVERNMENT SPENDING PROCESS

An important first step in evaluating the economic impact of government spending is to understand the operation of the Federal Government spending process. The following section is devoted to explaining the major phases of the process.

#### *Basic authorizing legislation*

The first step in the process is the enactment of basic legislation authorizing a given agency, program, or activity. Some such statute must be on the books before an appropriation can be enacted to provide funds for the agency or program involved.<sup>2</sup> Basic authorizing legislation of this nature ordinarily does not contain financial authorization enabling an agency to obligate government funds or to make expenditures.

There are a number of exceptions. Some authorizing statutes, such as the Federal-Aid Highway Act, do simultaneously grant Federal agencies obligational authority. The annual appropriation request in that case is merely to liquidate the obligations previously incurred. Many government corporations are authorized by basic legislation to spend the receipts from their operations without securing annual appropriations from the Congress.

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<sup>2</sup>This is the result of congressional procedure rather than statutory requirement. Cf., U. S. House of Representatives, Constitution, Jefferson's Manual, and Rules of the House of Representatives, Washington, Government Printing Office, 1949, rule 21, clause 2.

It is important to consider the increment of legislation which is proposed each fiscal year—the extension of expiring legislation, the enactment of new legislation, and modification or repeal of existing statutes—for this is the birth stage of new governmental spending programs.

#### *Enactment of new funds*

In January of each year, the President transmits to the Congress the budget for the coming fiscal year, the 12-month period beginning the following July 1. Within the next 6 months, and sometimes over a longer period, the Congress reviews and modifies the President's recommendations and enacts the appropriation bills for the coming year. The total of financial authorizations made available to the Federal agencies is composed of a number of types of enactments.

The most prevalent type is the ordinary appropriation, which empowers Federal agencies (1) to place orders, enter into contracts, or otherwise commit or "obligate" the Government to make expenditures in the future, and (2) to make the expenditures required by such obligations.

Another type of financial grant is the contract authorization. This empowers the agencies only to incur obligations. In these cases, the agencies have to make a later request for an appropriation to pay for or "liquidate" the obligation.

Authorizations to spend from "debt" receipts are usually used to finance government enterprises, where proceeds from operations may repay the initial advances from the Treasury. The availability of obligational and expenditure authority is the same as that of ordinary appropriations. However, such authorizations need not go through the appropriations committees and are not usually included in congressional tallies of appropriations enacted.

Most financial authorizations are enacted for a 1- or 2-year period and expire if not obligated during that time. Because of lags in Federal procurement, requests are sometimes made to extend such authorizations beyond the original period of enactment. The effect of reauthorizations is generally the same as if new authorizations were voted in their place.

The total of appropriations (other than those to "liquidate") and other financial authorizations made available to the agencies for a given year is called new obligational authority. The common characteristic of all such authorizations is that they empower the agencies to obligate the Government to make expenditures in the future.

The granting of obligational authority is a major control point over Federal spending. Given the grant of new authority, the usual functioning of Government will result in a subsequent flow of expenditures.

#### *Apportionment of funds*

After the Congress has voted funds, the control over expenditures shifts back to the executive branch. Each quarter, the Bureau of the Budget apportions to the agencies the funds appropriated to them. The apportionment power arises from the desire to prevent the agencies from spending their appropriations early in the year and returning for deficiency appropriations.

The apportionment power has been used to keep the amount of government spending for a particular item below the limit granted by the Congress. The general Appropriation Act of 1951 affirmed this authority "whenever savings are made possible by or through changes in requirements, greater efficiency of operations, or other developments subsequent to the date on which such appropriation was made available."<sup>3</sup>

Following the making of apportionments, which is a centrally administered control, allotments are made by agency heads to administrative units within the agencies.

#### *Incurring obligations*

Within the limits of the apportionment of funds made available to them, the Federal agencies place orders and take other actions which obligate their apportioned funds. To the extent that the goods and services needed by the Government are ordered from and produced in the private sector, this is the first stage of the process in which government procurement activity directly involves private industry. It is also the last clearly discretionary step in the process which will ultimately involve governmental disbursement of funds.

Obligations may be incurred for a wide variety of objects, in addition to the purchase of goods and services from the private sector. Purchases of goods and services from the public sector itself, transfer and interest payments, subsidies, grants to State and local governments, and purely financial transactions are also included.

#### *Producing government-ordered goods*

Pursuant to the contracts and orders placed, the suppliers of government goods and services produce or otherwise obtain the items previously obligated for. To the extent that production is carried on in the private sector, this stage of the Federal spending process is not usually reflected in the Federal financial accounts. The fact that disbursements to factors by government contractors do not appear in the Government accounts at this time but in the private accounts will be of considerable significance in the subsequent analysis.

In the case of production carried on by a government agency, the actual disbursements to factors in the course of production are reflected as expenditures in the Federal accounts. In the case of expenditures which are not for currently produced goods and services, such as transfer payments, interest payments, and the acquisition of land, the lag between obligations and expenditures is usually non-existent or at a minimum.

#### *Making payments*

In accordance with customary business practice, the Federal Government generally pays for the items it orders after they have been delivered, inspected, and approved. A number of agencies are authorized to make advance and progress payments. These are usually confined to large orders in the fulfillment of which the supplier requires considerable additions to his normal working capital.

Advance payments are made prior to the performance under a contract and are expected to be liquidated from payments due the contractor from performance. This device is rarely used at the present

<sup>3</sup> 64 Stat. 595.

time, although advance payments were an important source of business credit at the beginning of World War II. Progress payments are usually made for a percentage of the work performed or cost incurred under a government contract and are still generally employed, especially in military procurement.

### *The lags in the process*

As a result of the number of steps involved in the Federal spending process and due to the length of time often required by suppliers to produce the goods ordered by the Government, there is, in aggregate, a substantial lag between the time expenditures are authorized and the time they are made.

The lags in the early stages of the process are primarily administrative. It takes time for the agencies to prepare and obtain approval of their apportionment requests, for specifications to be drawn up for individual orders, and for contracts to be awarded.

A later and more important lag is technological, the lag between the letting of contracts and the beginning of quantity production. This is the contractor's period of "make ready" which may range from a few weeks to more than a year. In the case of a new type of heavy equipment, hundreds of additional engineers may be hired and trained by the contractor, thousands of detailed drawings made, production lines laid out, material requirements computed, schedules prepared, and subcontracts negotiated.

There are certain legal limits to the lags in the Federal spending process. Most forms of new obligational authority are available for obligation for either 1 or 2 years and are available for expenditures for no more than 2 years beyond that. Within these limits, the lag between the Government's embarking on a program and its execution is largely determined by private decision making. Military procurement of "hard goods," however, is generally financed from no-year appropriations, which are available until spent.

### *Reducing government spending*

The actions which can be taken to curtail government expenditures would operate in somewhat the same fashion as the actions involved in making expenditures. A reduction in government spending can be initiated at various stages in the spending process. The effects of the actions taken at each stage can be cumulative in their effects on expenditures during any given period.

For example, the Congress may decide to eliminate or reduce the scope of a program by changing its basic authorization or by eliminating or reducing the amount of funds authorized for it. These actions can be implemented, either through eliminations or reductions in the amount of new obligational authority being considered or in the rescission of existing obligational authority.

The President may decide that a given agency should not spend all of the funds it has been authorized and reduce its quarterly apportionments. The agencies can reduce the amount they spend by slowing down the rate at which they obligate funds, by obtaining a slowdown in the production of items they have ordered, or by canceling contracts they have already entered into.

There are obstacles to the reductions in expenditures which can be made through rescinding contracts, such as payment of damages and the loss of investment already made on a project.

## TIMING OF THE ECONOMIC IMPACT: A SIMPLE CASE

An indication of the possible effect on the economy of each of the major stages of the Government spending process will be given in this section. A number of simplifying assumptions are made, so that the effects on the economy arising directly from an increase in government spending can be examined.

An increase in government spending is assumed which consists entirely of expenditures for goods currently produced in the private sector of the economy. It is assumed that these expenditures are financed by borrowing idle funds.

It is also assumed that there are sufficient mobility and idle resources in the economy to produce the goods ordered by the Government without new, fixed, business investment or price or wage increases and without displacing any private demand. Also postulated is the availability of adequate financing for the Government contractors. It is further assumed that this increase in spending will generate no indirect psychological effects on consumer or business expectations nor any changes in other Government programs.

*Appropriation of funds*

It is assumed that the President transmits to the Congress a supplemental appropriation request which it enacts. Under the assumed conditions, there would be no immediate effect on the economy. Neither would any change be registered in the measures of Government spending.

*Placement of contracts*

The Government agency to which the appropriation is made places contracts with business firms in the private sector of the economy. The following are some of the events that would occur following the receipt of a Government order by a typical manufacturer.

The contractor finds that he cannot fill the order out of existing inventory or even from existing production lines. He determines that this additional volume of production can be obtained through more intensive utilization of existing capacity, but that it will require substantial increases in inventories and in his labor force. This, in turn, will necessitate increased working capital, which will have to be obtained outside of the firm.

On the basis of the company's past performance and the Government's order, the contractor obtains a working-capital loan from his bank. He begins to place orders for materials, to hire additional workers, and to subcontract parts of the order to other firms. These suppliers or subcontractors will be going through a similar process at this time, in some cases involving another tier of suppliers or subcontractors.

The first effect on the volume of economic activity will now be taking place. As deliveries begin to be made on raw materials and wages are earned by the newly hired workers who are tooling up, the contractor will be drawing upon his loan authorization and making small amounts of payments to the various factors of production. An increase will be registered in the outstanding loans of commercial banks and in the money supply. Also, some increase will occur in gross private domestic investment, the component of gross national

product which contains the inventory accumulation resulting from the small amounts of goods in process.

The economic activity represented by contract placement is not reflected in any of the measures of Government spending. These contracts are included, but not identified separately, in the monthly reports by the Department of Commerce on new orders received by business firms.

That the placement of Government orders ("obligations incurred" by the Federal agencies) is the phase of the Government spending process which energizes private production on Government account has been noted by a number of observers:

The initial stimulus to production is provided by Government contracts for procurement.<sup>4</sup>

\* \* \* it is the placing of a contract, or its anticipation which leads industry to plan its acquisition of materials and labor and to schedule its production. \* \* \*<sup>5</sup>

It is in the stimulus to productive activity rather than in the minor amounts of "make ready" production that the contract placement stage exercises an important effect on the level of economic activity.

#### *Production of goods*

As quantity production gets underway on the Government order, payments are made by the Government contractor for wages to the employees engaged in the work, materials delivered, and the interest due on the working-capital loan. He also will be accruing profits on the order. The costs incurred by the contractor during the entire production period—the value added—should total the amount of the order.

The outlays of government contractors are not reflected in government purchases of goods and services, nor in any other government expenditure series at the time they are made. They will show up in gross national product, in the change in inventory segment.

Simultaneously, the costs incurred will also show up as compensation of employees, corporate profits, interest and rental income, and, depending on the legal status of the contractor and subcontractors, earnings of unincorporated enterprises. Increases in consumer expenditures and fixed business investment may also occur as a result of the income payments.

#### *Payment for goods*

After the completion of production, the goods would be delivered to the Government and paid for. This is the period during which the Government purchase shows up as a budget expenditure and a cash payment to the public.

Following the payment by the Government, the contractor would repay the working-capital loan. These actions would tend to reduce the amount of private credit, reduce the Government's cash balances, and increase the cash position of the contractor.

The delivery of the goods shows up in the national income accounts as a decline in business inventories and, hence, in gross private domestic investment. It also is recorded as a government purchase of goods

<sup>4</sup> Melvin Anshen and Frances D. Wormuth, *Private Enterprise and Public Policy*, New York, Macmillan, 1954, p. 530.

<sup>5</sup> John Perry Miller, *Pricing of Military Procurements*, New Haven, Yale University Press, 1949, pp. 24-25.

and services. These two movements tend to cancel out, with the result that there is no net effect on the level of economic activity at the time the Government expenditure is made; the contribution to purchasing power has been made earlier during the contract placement and production stages.

#### TIMING OF THE ECONOMIC IMPACT—SOME COMPLICATIONS

Some of the possible effects on the economy of the operation of the various stages of the Government spending process will be examined here under more complicated circumstances than in the previous section.

##### *Anticipatory effects*

In the simplified situation in the previous section, it was assumed that the new government spending program would be neutral in its effects on consumer and business expectations. However, the Government's embarkment on a new program can have an "announcement" effect on consumer and business expectations. Such was the case in the early stages of the Korean mobilization program, when memories of World War II price rises and shortages set off a wave of private ordering in advance of any government purchasing.

On the other hand, the reaction to the new program may be negative. Businessmen may fear or oppose it as undue government interference and competition.<sup>6</sup>

The announcement effect of government spending is too diffuse and elusive to be measurable. We simply do not know what the actions of businessmen and consumers would have been in the absence of the anticipatory effect of government activity. We can only obtain some indication of the magnitude of the catalyst through a measure such as new obligational authority. However, the public reaction in a given situation will depend on recent experience, available purchasing power, and other variables.

##### *Availability of resources*

If the necessary labor, materials, or equipment are not available, the mere placing of a Government contract will not be sufficient to initiate productive activity. This was the situation during much of the World War II period when, once relatively full employment had been attained, additional orders merely resulted in increased backlogs. Through its economic control system, the Government was able to shift productive facilities from peacetime to wartime use. However, such action would have little effect on total economic activity.

Under other situations, such as at the outset of the Korean mobilization, the shortage was of particular resources. Here, much fixed investment preceded production on Government orders for end items. Both groups of expenditures show up initially in gross private domestic investment. However, the capital expenditures, when made by private firms, would be included as additions to plant and equipment and nonresidential construction and would remain in the stock

<sup>6</sup> Cf. an indication of reaction in the 1930's " \* \* \* who could tell where the experimenters would turn next?" Douglas A. Hayes, *Business Confidence and Business Activity: A Case Study of the Recession of 1937*, Ann Arbor, University of Michigan Press, 1951, p. 120.

of business assets. The production on Government orders, on the other hand, would, on completion, be recorded as Government purchases and become part of the stock of Government assets.

Where the contractor can fill the Government order out of existing inventory production would not take place until the firm decides to replace the depleted inventory. The Government payments in this case would precede the impact on GNP.

#### *Financing the Government expenditure*

In the simple situation, it was assumed that the Government expenditures would be financed by borrowing idle funds. It would be more usual for the Government to finance a large increase in expenditures through raising the level of taxation or borrowing investment funds. Either of the actions would tend to reduce private demands for output and, hence, to offset the expansive effect of the Government expenditure.

#### *Reducing Government spending*

In general, the economic impact of a reduction in government spending is analogous to that of an increase. The very act of embarking upon a contraction of government spending can have an "announcement" effect.

Under circumstances of a large pent-up private demand, as in the reconversion period following World War II, the curtailing of government demand may evoke waves of private buying. In other circumstances, such as the cessation of the Korean mobilization program, the heralded decline in government purchasing may mean a decline in total demand.

#### *Summary*

The impact of the various stages of the government spending process may vary with surrounding circumstances. Although all of these complications may modify the economic impact, the basic relationship generally holds: the primary impact of government procurement on the level of economic activity occurs in advance of the actual government expenditure.

### OTHER TYPES OF GOVERNMENT SPENDING PROGRAMS

The preceding two sections have been devoted to Government purchases of goods and services from the private sector. Other types of Government expenditures will now be examined.

#### *Transfer and interest payments*

Transfer and interest payments by the Government do not constitute a demand for output but are income to the recipients. Normally, these payments only affect the level of output with a lag and indirectly, as they are respent by the recipients for goods and services.

Anticipatory effects could take place, such as newly unemployed workers maintaining a certain level of spending in anticipation of the future receipt of unemployment compensation.

Also, accruals of interest can have some economic effect in advance of the actual payment. Some bondholders report interest on an accrual basis for tax purposes. Moreover, the knowledge that their

net worth position is growing stronger may also influence the spending decisions of some investors.<sup>7</sup>

### *Subsidy payments*

Subsidy payments also constitute income to the receivers and are not a demand for output. To the extent that they have favorable repercussions on the expectations of producers, these payments may evoke a positive effect in advance of the Government expenditure.

### *Grants-in-aid*

Federal grants-in-aid to State and local governments normally affect economic activity as they are utilized by the non-Federal government units. However, circumstances can arise under which the very act of the Federal Government in embarking on a new or expanded grant-in-aid program, or even its anticipation, can evoke an important stimulus to private or State and local activities in advance of any Federal payment or even pledge of funds.

The expansion in 1956 of the program of Federal grants for highway construction furnishes a recent example. In advance of congressional authorization, potential suppliers, such as cement producers and manufacturers of road-building equipment, began to plan for expansion of capacity and markets. The States stepped up advance planning of potential highway projects and many had qualifying projects ready to go as soon as the legislation was enacted.<sup>8</sup>

### *Lending programs*

Federal lending programs provide a number of variations in the timing of the economic impact of Government spending. The main effect of the loan normally would arise from the purchases made by the recipient of the loan. For example, housing loans can be used to finance new private residential construction; production loans to business firms and farmers for inventory accumulation and, ultimately, for sales to consumers, governments, or other private businesses; and loans abroad for net foreign investment.

In some circumstances, the expansive effect on the economy would precede the Government disbursement. This would be true if private firms order goods and services, hire additional employees, and begin production on the basis of the Government's commitment to make the loan at a later date.

In many instances, private production (and, hence, the initial impact on economic activity) would take place after the Government loan. This would be true of loans to farmers for implements, feed, and other items needed before production could get underway.

### *Purchases of existing assets*

Government purchases of land and other existing assets merely add to the liquidity of the recipients. Only to the extent that the proceeds are used to finance or purchase current output will there be any impact on economic activity.

Neither this category of government expenditures, nor the preceding category of loans, appear as government purchases of output or as income to the recipients.

<sup>7</sup> Carl S. Shoup, Postwar Federal Interest Charge, American Economic Review, supplement, pt. 2, June 1944, p. 54.

<sup>8</sup> Engineering News-Record, June 7, 1956, p. 26; July 5, 1956, p. 23.

*Government production*

A substantial portion of government purchases of goods and services is made directly from the public sector itself and involves no production in the private sector. Conventionally, this gross product of the public sector is taken as the compensation of General Government employees.<sup>9</sup>

Government "obligations" are recorded as the personal services are rendered. With a lag of usually 1 to 2 weeks, the employees receive payments for their services as they are rendered. Hence, the lag between obligations and expenditures is at a minimum. From the viewpoint of economic activity, the payments to factors (government employees) are recorded as government purchases of goods and services when the services are rendered and when payments are made. There is no time lag involved for "intersector" transfers as is the case for goods and services which the Government buys from private business firms.

## NEW MEASURES OF GOVERNMENT SPENDING

A number of measures of the Federal Government spending process are currently available and used. These individual measures have arisen for a variety of reasons and are used for different purposes. Additional series may be required and can be prepared.

*Existing expenditure measures*

The three most widely known measures of government spending are (1) budget expenditures, based on the Federal administrative budget; (2) Federal Government payments to the public, prepared on a cash-consolidated basis; and (3) Federal purchases of goods and services, computed as a part of the national income and product accounts. Each of these series varies in coverage, basis of measurement, and types of payments included.

Budget expenditures include the outlays of wholly owned Federal departments and agencies, but exclude payments from government trust funds. Expenditures are recorded at the time checks are issued by governmental disbursing officers, except for interest on the public debt which is generally reported as it accrues.

Payments to the public include the outlays of Federal agencies as well as trust funds, eliminating transfers of funds within the Government. This series reports the amounts of checks paid by the Government.

Federal purchases are recorded as goods and services ordered by the Government are delivered. Unlike the other two series, only items involving the acquisition of current output are included.<sup>10</sup>

Despite the differences in the scope and type of transactions covered, all of the three series are closely related; they are all variations of a basic budget expenditure series and generally measure the flow of the Government spending process at its completion, when production is completed and delivery or payment is made.

Contrasted to this general uniformity of measurement, Federal spending is a process, a flow of activity; "expenditures" or "payments"

<sup>9</sup> 1954 National Income Supplement, Survey of Current Business, p. 53.

<sup>10</sup> For detailed description of the three series, see Budget of the United States Government for the Fiscal Year Ending June 30, 1958, Washington, GPO, 1957, pp. A2, A3, 1131-1133; 1954 National Income Supplement, Survey of Current Business, pp. 146-147.

or "purchases" represent just one point in an often lengthy series of actions. Under some circumstances, attention should be focused on the earlier phases of the process in order to gauge or understand adequately the economic impact of a Government spending program.

#### *Measures of other stages*

Except for the expenditure series, which are generally prepared monthly or quarterly, only limited information is available on the various stages of the Government spending process.

The budget document reports, on an annual basis, the amount of new obligational authority voted by the Congress. The absence of quarterly or monthly totals may not be very important due to the annuality of the appropriation cycle.

No series is currently published on the total obligations incurred by the Federal Government. However, the following section contains an attempt to construct such a series.

Neither is there available any information on the amount of private production on Government account. What is needed is a breakdown, not now available, showing how much of business inventories relates to private orders and how much to Government orders.<sup>11</sup>

#### *Derivation of a series on obligations*

Information on the obligations incurred by individual Government agencies are available as a result of the requirements of budgetary control. Such data may be utilized in preparing series for the Federal Government as a whole.

The annual budget document lists obligations for each appropriation account, but does not contain any summarization. These data can be aggregated and, with some necessary adjustments for changes in the concept of the budget total, can be used to provide an annual series on obligations incurred by Federal agencies.

A rudimentary series can be prepared showing Federal Government obligations incurred, by quarters. The series presented in table 1 is intended for illustrative purposes only. It was derived as follows:

1. The annual totals were based on the obligation figures reported in budget documents.

2. The figures for "military" obligations were taken from reports of the Department of Defense and cover the military functions of the Department and foreign military assistance.

3. The obligation figures for "interest" are the amounts reported by the Treasury Department as interest payments. This procedure was possible because there is no lag between obligations and expenditures for this item.

4. The annual obligations for all other programs were divided evenly into four quarters. Although there are definite seasonal patterns in government ordering, the period covered in Table 1 is dominated by sharp fluctuations in military programs and comparatively little distortion is introduced by this procedure.<sup>12</sup>

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<sup>11</sup> A recommendation that such data be prepared was made by the Subcommittee on Economic Statistics. Cf. U. S. Congress, Joint Committee on the Economic Report, 1955 Report of the Subcommittee on Economic Statistics, 84th Cong., 1st sess., Washington, GPO, 1955, pp. 5-6.

<sup>12</sup> For data concerning the seasonal patterns of Federal procurement, see Clem C. Linnenberg and Dana M. Barbour, Government Purchasing—An Economic Commentary, Temporary National Economic Committee, Monograph No. 19, Washington, GPO, 1940, p. 24; U. S. Treasury Department, Financial Statements Relating to the United States Government, Obligations, Expenditures, and Balances Under Appropriations and Contract Authorizations, Washington, 1942-49 (processed).

TABLE 1.—*Obligations incurred by the Federal Government*

[In billions of dollars]

Fiscal year	Military	Interest	Other	Total
1951				
1st quarter.....	8.6	1.1	6.9	16.6
2d quarter.....	8.7	1.3	7.0	17.0
3d quarter.....	16.1	1.2	7.0	24.3
4th quarter.....	16.2	2.0	7.0	25.2
Total.....	49.6	5.6	27.9	83.1
1952				
1st quarter.....	13.0	1.1	9.2	23.3
2d quarter.....	13.0	1.7	9.2	23.9
3d quarter.....	15.3	1.1	9.2	25.6
4th quarter.....	20.6	2.0	9.2	31.8
Total.....	61.9	5.9	36.8	104.6
1953				
1st quarter.....	16.8	1.1	8.2	26.1
2d quarter.....	10.4	1.9	8.2	20.5
3d quarter.....	10.8	1.1	8.1	20.0
4th quarter.....	8.5	2.4	8.1	19.0
Total.....	46.5	6.5	32.6	85.6
1954				
1st quarter.....	6.5	1.0	7.4	14.9
2d quarter.....	6.0	1.8	7.4	15.2
3d quarter.....	6.9	1.2	7.3	15.4
4th quarter.....	10.5	2.4	7.3	20.2
Total.....	29.9	6.4	29.4	65.7

Source: Budget Documents for 1953-56; U. S. Department of Defense, Monthly Report on Status of Funds by Budget Category, June 30, 1954, p. 33; Treasury Bulletin, August issues, 1951-54, p. 3.

The quarterly movements in the obligation series clearly show the rapid buildup of the Korean mobilization program. They also afford an insight into the substantial increases in economic activity which accompanied the new defense program. The expenditure series, in contrast, registered a rather slight rise in the fiscal year 1951. In fact, substantial budget and cash surpluses resulted for the period.

It should be noted that more exact obligation series can be provided by the Government on a quarterly basis, provided that the need is shown and the agencies involved in the preparation are directed to do so. This can be done because the individual agencies report their obligations each month or quarter to the Bureau of the Budget.<sup>13</sup> However, no summarization of these reports is made at the present time.

#### SOME USES OF THE ANALYSIS

The applications of this study for purposes of economic analysis and governmental administration are twofold: (1) A proper understanding of the operation of the Federal spending process is important in analyzing economic developments and government activity during periods of fluctuation in government purchasing; and (2) the measures of the early stages of the spending process are lead series which often quickly register changes in governmental demand and indicate future trends in actual governmental disbursements.

<sup>13</sup> Budget, Treasury Regulation No. 1: Washington 1952.

*Analysis of economic conditions*

An understanding of the Government spending process is of especial value in the analysis of economic conditions during periods when government purchasing provides the dominant influence in the economy. This is particularly true because the early stages of the process often show up in the private sector rather than in the public sector, and it is important to understand where the underlying demand originates.

Under such circumstances, reports on new obligational authority granted by the Congress and obligations incurred by Federal agencies are in the nature of "lead" series or "exceptional" statistics which indicate future economic developments.

*Formulation of economic policy*

Attention to the timing of the Government spending process can be useful in the formulation of public policy. For example, if a \$5 billion decline in gross national product (at annual rates) had been experienced in period 1 and a \$10 billion decline is anticipated in period 2, it may be of little avail (aside from exceptional effects) to embark upon a large construction program for which contracts could not be let until period 3 and production gotten underway until period 4. In such case, recourse to actions which involve shorter lead time may be more appropriate. A stepup could be attempted instead in the rate of production of equipment already on order.

The timing of the economic impact of government expenditures had an important bearing on fiscal policy during the early stages of the Korean mobilization period. The inflationary pressures were unaccompanied by any immediate Federal deficit. Under a policy of a balanced budget, there was no need for added taxation. However, the administration was partially successful in coupling the need for increased revenue with recently enacted appropriations and the high levels of procurement:

Under present conditions, expenditures for defense exert an inflationary pressure on the economy substantially in advance of the actual disbursement of funds. Demands for materials, for labor, and for capital outlays occur very soon after the Government contracts are let \* \* \*<sup>14</sup>

*Governmental administration*

The measurements of the early stages of the Federal spending process lend themselves to a number of administrative uses. Forecasts of government expenditures can be prepared by using data on new obligational authority and available balances together with assumptions as to obligation and production rates.<sup>15</sup>

In a more general way, changes in the level of new authorizations and/or new commitments can be used to gage the future course of expenditures in a somewhat similar manner that series on new orders are used by business analysts to estimate future sales trends.

It is the belief of the writer that aggregating the individual agency reports on obligations incurred could also be a helpful tool in assessing

<sup>14</sup> Testimony of Treasury Secretary John Snyder before the House Ways and Means Committee, quoted in Annual Report on State of the Finances for the Fiscal Year Ended June 30, 1951, Washington, GPO, 1952, p. 406.

<sup>15</sup> For a recent example of this approach, see U. S. Department of the Navy, Statistical Approach to Forecasting Expenditures, NAVEXOS, p. 1571 (undated).

the progress being made on government programs from the point of view of governmental administration and budgetary control.

An understanding of the government spending process can also be useful in effectively controlling government spending, with the particular view of reducing. Much of the discussion has centered on expenditures per se. However, if adequate controls are to be exercised, attention must also be given to the early stages where expenditures are authorized and committed, rather than only to the payments for goods and services already ordered and produced.

#### CONCLUSIONS AND RECOMMENDATIONS

It is a fundamental finding of this study that the variations in the timing and economic impact of the various stages of the governmental spending process necessitate taking measurements of the spending stream at earlier points than merely the completion stage represented by deliveries or payments.

When the Government is about to embark upon a new program, often the most useful indicator of the scope of this new activity will be the amount appropriated for it by the Congress. A more direct indication of the current economic impact may be the aggregate of orders placed and contracts let. Where the increase in government activity consists of transfer payments to the public, a series on expenditures would be of particular value.

The use of any of these measures need not be mutually exclusive and their contribution may be additive. What is needed is not a single standard measure of Federal spending but a tool kit of series, each of which is adapted to special analytical purposes.

The specific recommendations that arise from this study are that series on new obligational authority granted by the Congress and obligations incurred by government agencies be computed regularly by the Federal Government and that they should be published in the standard compendia of economic statistics. They should be supplemented from time to time by reports on unobligated balances and on unpaid commitments outstanding.

Such series would be useful and complementary additions to the sections on government finance in such publications as the Economic Indicators, the Treasury Bulletin, the Federal Reserve Bulletin, and the Survey of Current Business.

A better understanding of the workings of the Federal spending process will assist in the use of these tools for purposes of economic analysis and policy formulation. In an even broader way, it is important to understand the operation of the Government spending mechanism as one of the important processes of the economy.