C
O
P
Y

April 6, 1949

MEMORANDUM

TO: The President

FROM: The Council of Economic Advisers (Mr. Clark absent)

SUBJECT: First Quarter (1949) Review

The first quarter of 1949 contained a mixture of trends which makes it hard to characterize the quarter by a simple label or to discern the immediate outlook with clarity. The ambiguity and lack of conclusive evidence in the situation may be indicated by a brief examination of employment, production and business activity, and prices.

Employment. Employment in January and February 1949 declined more than in January and February 1948, but employment in March 1949 increased more than in March 1948. Further, in each of the first three months of this year, employment was higher than in each of the first three months of last year.

Bearing these figures in mind, and noting particularly the March 1949 increase of almost half a million in employment, it is fair to say that the employment situation is still strong. On the other hand, the growing labor force has not been sufficiently absorbed to prevent an increase in unemployment, which stood at 3,167,000 in March 1949, contrasted with 2,440,000 in March 1948, although unemployment declined slightly from February to March 1949. Another month or two should reveal more clearly whether the upswing in employment during March and the decline in unemployment will be continued or whether the trend of January and February was of more than seasonal significance.

Production and Business Activity. Industrial production in the first quarter of 1949 averaged 2.6 percent below the levels of a year ago. Taken alone, this decline is not of compelling significance, because some shifts in the pattern of activity were to be expected as we moved farther from postwar reconversion toward more normal peacetime patterns. For individual industries, data available for the first two months of this year show iron and steel output up to 13 percent and automobile industry output up 5 percent, contrasted with the first two months of 1948, while decreases of more than 10 percent were registered in lumber and products, textiles and products, and rubber products. Retail sales in the first quarter of 1949 were slightly below levels of last year in dollar terms, and during March the lower level of retail sales compared with a year ago was particularly evident in certain regions. Some part of the difference between last spring and this may be due to the fact that Easter comes about three weeks later this year, but all factors considered, it seems that there has been a moderate weakening in consumer demand.

During the first two months of 1949, new orders received by manufacturers ran about 8 percent below the corresponding months of last year. In February 1949, orders were about at the same level as in January and there is no general evidence of a suddenly generated decline. The absence of any serious break in the producers' durable field is indicated by a March survey of machinery producers in which only 3 percent of the respondents thought that there had been a recent increase in cancellations.

Two months earlier, 14 had answered the same question in the affirmative.

Prices. Between the end of December and the end of March, overall wholesale prices declined 2.5 percent, with the largest decline in wholesale prices of farm products and of foods. Prices of agricultural products moved down sharply until early February, even below government support levels in some cases. A sharp rebound recovered half of the loss since January 1. Industrial prices declined .7 percent during the first quarter of 1949, although metals and metal products reached a peak in February, since which time they have declined. Consumer prices between December and February (the March figures are not yet available) declined 1.4 percent. The general decline in prices thus far has been moderate and there is no sign that panic has gripped the markets.

The foregoing resume indicates that the present economic situation is equivocal, and three possible lines of development need to be considered.

First, there is the possibility of another spurt of inflation. This seems least likely unless the Congress votes large appropriations not offset by new taxes. Consumers have recently shown a disposition to save more and to spend less, and if this mood changes there could be a market increase in market demand because personal incomes remain very high. Businessmen, while talking in terms of uncertainty and hesitation, have thus far continued to make investments at a high rate. Government expenditures will increase, and without increased taxes the surplus will be reduced to negligible proportions or become a deficit. Wage increases, if moving beyond increases in productivity, might be inflationary. The crop outlook is always undertain although it now looks promising. These factors do not permit us to rule out the possibility, although there is decreasing likelihood, of another spurt of inflation.

Second, there is the possibility that the substantial downturn in business activity predicted or feared for several years may develop within 1949. Much depends upon attitudes which have not yet crystallized fully. The uncertainty of businessmen could lead to substantial contraction tion of investment and production. The more extensive price readjustments that will be necessary as more and more markets become buyers' markets may be harder to execute skillfully and may cause more repercussions in employment and production than those which have thus far taken place. The future character of consumer responses is still hard to appraise. Because of the more ambiguous economic situation, we feel that the magnitude of tax increases proposed at the beginning of the year should be reconsidered.

Third is the hoped for further process of price adjustment in a manner to facilitate the clearing of markets with only moderate temporary departure from maximum levels of employment and production. Thus far, this process of healthy adjustme nt has taken place in a more orderly and constructive fashion than many people anticipated and we may find ourselves hanging up an unparalleled record of transition from a postwar boom to a period of stable prosperity without intervening hard times. The Government by word and deed should extend every feasible encouragement to this process of adjustment.

In view of these three possibilities, the Council will need to examine the evolving economic situation for another month or two before making further proposals with respect to the economic program recommended in January. Meanwhile, we are concentrating our attention upon more comprehensive development of the stabilization devices studies which we have had under way since early 1947 in order that we may be fully prepared with adequate recommendations if seriously unfavorable developments in levels of employment and production should occur or be clearly indicated.