#25

April 21, 1952

MEMORANDUM

To: The President

From: The Council of Economic Advisers

Subject: Quarterly Report on the Economic Situation

Summary

Economic developments in the first quarter of 1952 brought further evidence that, so far as the impact on the civilian economy is concerned, we could afford to step up defense production--if strategically desirable.

Statistically, the first quarter was an extension of the last 9 months of 1951: Output kept rising slowly. Employment stayed high, but the labor market got no tighter. Prices edged a bit lower; wages were relatively stable. (pp. 2-3.)

But there were these changes: (1) a sharp revision in the critical materials outlook, promising more steel, aluminum, and copper the rest of this year and still more in 1953(pp. 3-4); (2) a stretching-out of military production schedules along with some new production lags (pp. 4-5).

The story of the quarter by major economic groups: Consumers spent a little more out of slightly smaller incomes after taxes, but kept on saving at a high rate (pp. 5-6). Business invested heavily in plant and equipment but cut back on inventory expansion. Corporate profits probably were higher than the quarter before but much lower than the first quarter of 1951 (pp. 6-8). Federal receipts and expenditures point to a smaller 1952 deficit than that estimated in January (p. 8). International economic developments fell into no clear pattern, but a recovery seemed under way in U. S. imports (pp. 8-9).

Short-range economic outlook (assuming no new international outbreak): Despite growing talk about deflation in the business community (pp. 9-11), the outlook for the near future probably still is for further moderate growth and substantial stability. The steel controversy and/or a Korean truce could upset this estimate, but effects of both are susceptible to exaggeration (pp. 11-12).

The longer run is much more uncertain. There are deflationary as well as inflationary possibilities which require close study (p. 13).

As for policy, (1) the general economic picture, and our general productive strength, permit decisions regarding the size and pace of the security program to rest more heavily on strategic considerations, without restraints being imposed for purely economic reasons. (2) The steel situation has intensified the need for better coordination of wage-price policy, and increased utilization of the Economic Reports as a guide to operating economic policies. (3) It is essential to resist premature decontrol, both of materials and of prices and wages (pp. 13-15).

The First Quarter in General

The first quarter of 1952 was not dramatic; it brought no sharp turns in the major statistical series. By this very token, the period was a good one; the conditions which persisted were high and rising levels of output, and pronounced price stability. Underneath the surface, however, there were developments which complicate the picture.

The output of the economy continued to rise. Gross national product, at a seasonally adjusted annual rate of 339.0 billion dollars, was about 4.5 billion higher in the first quarter of 1952 than in the fourth quarter of 1951, which had showed a gain of 5.1 billion over the third quarter. In the first quarter of 1952, government purchases of goods and services, on an annual rate basis, increased nearly 4 billion with almost all of the increase being in national security expenditures. Personal consumption increased slightly. Private investment declined slightly because of reduced inventory accumulation. (See Economic Indicators, p. 2.)

The industrial production index, which does not measure such major kinds of production as construction, services, and farm output, recorded about the same percentage gain as the quarterly change in gross national product. (See Indicators, p. 12.)

Like production, employment was high. By March, the usual seasonal decline in the demand for workers had reduced employment to 59.7 million, or about 1¼ million below December. The decline in employment, however, was largely offset by a seasonal reduction in the civilian labor force. Unemployment, which totaled about 1.8 million persons, or 2.9 percent of the civilian labor force, was at the lowest March level since 1945. (See Indicators, p. 7.)

Continuing the pattern of the last 3 quarter of 1951, the new quarter was marked by stability as well as by production gains. The high personal saving rate, which has provided the biggest economic puzzle of 1951, held up very well. (See Indicators, p. 24.) Prices showed downward tendencies. Wholesale priced edged lower during each month of the quarter. While this was due mainly to some fairly sharp and presumably temporary breaks in particular farm prices, it is a fair assumption that many wholesale prices, especially in raw materials, are in the process of reacting from excessive speculative peaks reached earlier. (See Indicators, p. 4.) Consumers' prices, after failing to rise between December and January, in February recorded their first significant drop since Korea. The decline, however, was only 0.6 percent, and was largely the result of a temporary drop in food prices. It left the retail price level still 10.4 percent above June 1950. (See Indicators, p. 3.)

The wage data for the first quarter also denoted a relatively stabilized situation. Average hourly earnings in manufacturing industries crept upward only 0.7 percent in the 3 months from November through February. In January and February average weekly earnings were a little less than in December because of lower hours. (See Indicators, pp. 9-11.) The big wage issue of the quarter--that in steel--remained unresolved at its end. (See below.)

Developments in the field of money and credit during the quarter conformed to the usual first quarter pattern. The drop of about 3.3 billion dollars in the privately-held money supply from the record December 1951 level could be interpreted as a deflationary factor. But it probably was largely a seasonal dip accompanying heavy income tax payments.

All told, the general production, employment, and purchasing power record for the quarter was a favorable one. However, it would be incomplete and very possibly misleading to leave the over-all analysis of the period on this rather bland, "more-of-the-same" note. Two developments deserve emphasis: first, the nature and the potential impact of the changed critical materials situation which became evident in the middle of the quarter; and second, a "stretch-out" in scheduled production for the national security program. These developments, it should be noted, took place under the growing cloud of the steel dispute, which is discussed briefly later in this report.

The changed materials situation

The major industrial metals--steel, aluminum, and copper--stayed near the center of the economic stage during the first quarter, but their role shifted. As recently as January, severe shortages of these materials were feared for a year or more, tighter in the second half of 1952 than in the first. Now it appears that the scarcity of metals for nondefense purposes probably reached its peak in the first quarter of 1952 and should ease sufficiently by the second half of this year to make nondefense steel and aluminum supplies for 1952 as a whole only slightly below their 1951 levels, and copper supplies only moderately lower.

The sudden turn-about in the metals outlook apparently is explained by a combination of factors. For one thing, the materials requirements of the military program had been miscalculated, partly because metals-use per unit of end-items was put too high. In addition, the Defense Department program upon which earlier materials calculations were based was higher than the program officially implied in the January Budget. Moreover, some types of nonmilitary requirements, notably general-purpose machinery and components, were grossly overstated. For another thing, it now is clear that for the first 18 months after Korea both military and nonmilitary producers hoarded metals, accumulating inventories at abnormal rates. Now, partly because the Controlled Materials Plan has assured priority producers that metals allocated to them will be available on schedule, partly because the pace of the military production is not up to previous expectations, and partly because demand for consumer durables has been weaker than expected, the building up of metals inventories has abated sharply.

The materials outlook later this year for consumer durables, housing, schools, roads, and commercial construction has improved. It is one of several factors which suggest a potential further abatement of inflationary pressures unless the security program should be accelerated.

Military production

During the first quarter, the defense establishment stretched out its production schedules for military end-items, so that they now involve lower month-to-month targets in the build-up phase of the military production program, less peaking, and a longer plateau of production. The reasons for this decision were complex, and, in part, their evaluation lies outside the scope of the Council's advisory responsibility. However, it is our business to examine one reason frequently adduced for the "stretch-out": the need to minimize the program's impact on the civilian economy. We do not find this particular explanation of the action persuasive.

As the easier materials outlook suggests, and as an examination of other economic factors confirms, there is no indication that present military production schedules will curtail supplies of civilian goods significantly below demand during the remainder of 1952. Moreover, in 1953 the available supply of materials would permit a step-up in the military program's rate of metals-use at least to the levels contemplated in the January 1952 Budget estimates, without squeezing civilian metals supplies in 1953 below the rather generous quantities which will be available the rest of this year.

Such a revision of the program, of course, would tend to halt the further moderate and selective weakening of prices now evident. But there is no reason to think that it would greatly augment upward pressure or would heighten the risk of serious inflation--unless our anti-inflationary program were generally abandoned at the same time.

The first quarter also brought evidence of further lags in military deliveries behind earlier schedules, and apparently even somewhat behind the new lower schedules now developed. Expenditures for military supplies to NATO, for example, seem to be falling far behind estimates made in the January 1952 Budget only 3 months ago. On the other hand, some of the more important bottlenecks, notably machine tools, have been overcome, and defense production rates for March present much more of an on-schedule picture than the average data for the quarter as a whole.

The most serious immediate threat to the speedy achievement of the security program--and one which is related to the widespread and perhaps exaggerated talk about lags and slowdowns lately--is the tentative House of Representatives action which would limit military expenditures, exclusive of foreign aid, during fiscal 1953 to about 46 billion dollars. Since the rate of expenditures by the end of this June will be very close to, if not at, this level, such action would choke off virtually all expansion in military output in the coming fiscal year. This would have the most serious consequences for the timing of the security build-up, particularly in the case of a number of key long-lead-time items which will be coming into heavy production early in fiscal 1953.

Detail of Activities in the Major Economic Sectors

Consumers: income, spending, saving, and borrowing

According to first estimates, consumers received a little less income, after taxes, in the first quarter of 1952 than in the fourth quarter of 1951; but they spent at a somewhat higher rate. Total personal income was about 1 billion dollars higher than in the preceding quarter (at seasonally adjusted annual rates), but since personal taxes rose even more, income available for spending fell for the first time since the third quarter of 1949. (See Indicators, p. 24.)

The small rise in the rate of spending--the increase was at an annual rate of around 2 billion dollars, or 1 percent above the preceding 3 months--is evident only after an adjustment for the season. Actual expenditures declined; there was a rise only in the sense that there was more spending than might have been expected in the quiet months following the year-end holiday period. Yet, the relative rise did not stir up much business enthusiasm; many businessmen had expected, or hoped for, more business than came their way.

Spending on durable goods, for the first quarter as a whole, is estimated to have remained near the levels of the last 3 quarters of 1951, though in January and February sales of durable goods by retail stores were moderately above December, on a seasonally adjusted basis. Expenditures for nondurables and for services accounted for virtually all of the increase in total expenditures during the quarter.

The first quarter gave evidence that the demand for new houses is still strong. January 1952 witnessed an unexpected increase over December in new houses on which work was started. The rise continued in February and again in March. New starts for the first quarter amounted to 243,000. (See Indicators, p. 16.) It now appears that new units begun during 1952 will be closer to 1 million than to the 800,000-850,000 contemplated earlier.

The first quarter movements in consumer income and spending do not necessarily indicate that disposable personal income has ended its long upward course, or that a rise in consumer buying is under way. By the same token, the dip in the percent of spendable income saved, from 9 percent to something under 8 percent, is not a clear sign of a change in the trend of saving. The income and spending data for the quarter just ended have the frailty of first estimates; changes in both series were relatively small; and the bulge in personal tax payments, which cut disposable income, largely reflected the delayed impact of the higher tax rates imposed late in 1951. A similar step-up in tax payments is not likely to occur in succeeding quarters.

Individuals reduced their nonmortgage debts during the first months of 1952 about as much as they usually do at that time of the year. Total consumer instalment credit fell 300 million dollars from December through February, and there was a net reduction of nearly 600 million in charge accounts during the same period. (See Indicators, p. 28.) However, the rise in residential mortgage debt during the first quarter of 1952, which was at a rate nearly as high as during the first quarter of 1951, more than offset the fall in shorter-term consumer debt. The high personal saving ratio of the first quarter did not apparently result from an overall reduction in personal debts.

<u>Business: investment, sales, earnings, and financing</u>

In the first quarter of 1952, private business not only supplied consumers with an abundance of goods and produced a growing volume of materials for the security program, but it also added substantially to the Nation's productive strength.

Most of the new business investment was in plant and equipment, for the accumulation of inventories came almost to a halt. Nonfarm inventories, which had expanded at the phenomenal annual rate of 14 billion dollars, seasonally adjusted, during the second quarter of 1951 and had expanded 3.3 billion in the fourth quarter, crept up only 0.5 billion during the first quarter of 1952. All of the rise was probably in defense or defense-supporting industries. In contrast, new business construction (i.e., private construction exclusive of nonfarm residential) reversed a fourth-quarter decline and rose approximately 1 billion dollars, or more than 8 percent, on a seasonally adjusted annual rate basis. Outlays for durable equipment in the first quarter were at an annual rate of 30 billion dollars, an all-time high.

The continuation through the first quarter of the descent in the rate of inventory accumulation, which had been an important factor in holding inflation in check, was, as in the preceding 6 months, only partially the result of materials controls. It reflected, and magnified, the impact of the calm in the markets for consumers' goods.

In general, retail inventories now seem to be in "normal" relationship to sales. The stock-sales ratio of department stores in February 1952 stood about where it was in February 1950. There are a few conspicuous exceptions: supplies of television sets and refrigerators are very high, and are still out of line with sales. Manufacturers' inventories--again with such conspicuous exceptions as metals and synthetic fibers--also seem to be in better balance with sales.

While retail inventories of many goods may no longer serve to cushion the impact of a sudden increase in consumption to the extent possible a year ago, increases in output can now provide a considerable cushion. Production of both durable and nondurable consumer goods can be stepped up considerably in response to a rise in demand; and the expansibility of civilian output, in many industries, will undoubtedly increase as the year moves on.

Business sales increased slightly during the first quarter. Retail sales were 4.6 percent higher in February than in December 1951, after allowance for seasonal variations, and attained the highest level since February 1951. Sales by manufacturers rose 10 percent during the same period, and in February they were larger than in any other month since May 1951. (See Indicators, p. 19.)

Business earnings, in general, kept pace with business activity during the first quarter of 1952. Corporate profits before taxes are estimated to have been at the seasonally adjusted annual rate of 42.5 billion dollars, more than 3 percent above the previous quarter, but 18 percent below the first quarter of 1951. However, corporate profits after taxes were about the same as in the fourth quarter of 1951. (See Indicators, p. 22.) Earnings of unincorporated businesses and the professions rose slightly. However, the earnings of farm proprietors dropped, returning to the level of the first two quarters of 1951. (See Indicators, p. 23.)

Business borrowing at banks in January began the unsteady seasonal decline that typically extends through the first half of the year. In February and early March, however, seasonal repayments were offset by the continued rise in borrowing by defense-related industries and by some borrowing to meet heavy first quarter tax payments, though the latter was less than expected. Toward the end of March business loans again declined. As a result of this combination of influences, commercial and industrial loans decreased about 300 million dollars during the 3-month period. In contrast, during the first quarter of 1951, business loans expanded nearly 2 billion dollars.

Federal Government: receipts, expenditures, and debt operations

The Government enjoyed a substantial budget surplus in the first quarter of 1952--4.1 billion dollars, compared with the record 5.7 billion in the first quarter of 1951. (See Indicators, p. 31.) This large seasonal surplus was in a great part the result of a lag in the growth of expenditures on the major security programs. In January, the Budget implied an annual rate of 53.4 billion dollars of expenditures on these programs for the first quarter of 1952; the actual rate was 46.6 billion.

The "cash" budget, which is a better measure of the impact of the Government's financial operations on the economy than is the administrative budget, showed cash income for the quarter 5.2 billion dollars larger than cash outgo. This cash surplus was significant, not because it occurred--first quarter income tax payments quite frequently give the cash budget a temporary deflationary aspect--but rather because it was somewhat larger than anticipated. It suggested, as have similar favorable budgetary movements in earlier quarters, that, over the longer period, less danger from inflation may be inherent in the defense build-up than had been feared earlier. Should the lag in the growth of expenditures continue through the current quarter, the cash deficit for fiscal 1952 will be much less than the 4 billion dollars estimated in January.

The budget surplus of the first quarter was used in part to build up the Government's cash balance, and in part to reduce the public debt, which fell 1.4 billion dollars.

In the first quarter, a feature of Treasury refinancing which reflected the impact of general credit controls on interest rates was the offer of 2-3/8 percent 5 to 7 year bonds in exchange for bonds called for redemption on March 15. The most recent comparable issue was the 5-year note of December 1950, which bore a coupon rate of 1-3/4 percent. Yields on new issues of Treasury bills during the first quarter of 1952 averaged 1.64 percent, compared with 1.40 percent during the first quarter of 1951. Yields on long-term Government bonds averaged 2.72 percent for the January-March quarter of this year, compared with 2.42 percent a year before.

International

In January and February 1952, as in the preceding months, the irregular movement of U. S. exports showed no clear pattern, but a recovery seemed under way in U. S. imports. U. S. imports during the second half of 1951 were low in relation to the high level of total output in this

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country, and stocks of many imported goods have been running down. Some rise in imports is therefore to be expected. (See Indicators, p. 20.)

The outlook for U. S. exports has been altered by actions recently taken by many nations, notably in the sterling area, to regress internal demand and to restrict imports from the United States as well as from other countries. The full impact of these measures and of last year's accumulation of inventories has not yet been felt by the United States or by the many other countries which will be affected. The expected reduction in U. S. nonmilitary exports from the level of the fourth quarter of 1951 is not likely to be a substantial deflationary force in the aggregate, but there may be significant effects, direct and indirect, on exports of coal, oil, and certain manufactured consumers' goods.

The foreign trade balances of the major Western European countries, especially of Britain, improved in the last quarter of 1951. The few figures now available indicate that the improvement in the British trade balance continued in January and February, but in Germany and Italy the earlier improvement was reversed and the French trade deficit continued the steady rise which has been going on since last September. British gold and dollar reserves continued to decline rapidly in January and February, but in March the drain was greatly reduced.

Industrial production on the whole in Western Europe was about the same as in the last quarter of 1951, but in the textile industries production has declined and unemployment has risen substantially. Recession in textiles is worldwide, appearing, for example, in Britain, Belgium, Holland, Austria, and Japan as well as in the United States. There is no indication, however, that it foreshadows general recession or unemployment abroad.

Wholesale prices in Western Europe, which were rising in the last part of 1951, stopped rising or fell slightly in most countries in January and February. The cost of living continued to rise, but the rise appeared to be less rapid than in the late months of last year.

Outlook and Policy Implications

The economic outlook for the rest of 1952

A year or even 9 months ago, another onslaught of heavy inflationary pressures was foreseen as a relatively sure thing; the question was its timing. By January, while the third attack of inflation was regarded as a risk rather than a predictable development, the odds were still on the inflationary side. A principal, if intangible, economic development of the first quarter was the strengthening of opinion in business circles that, barring new international crises, our present stability is more likely to issue into a deflationary rather than an inflationary problem.

The reasons assigned for this drift of attitudes toward the economic outlook, insofar as they can be linked up with first quarter developments, seem to be the following:

(1) The very duration of the "lull" itself may have weakened the plausibility of the "lull" diagnosis. The longer it continues the greater the number who believe that inflation is not coming back at all--during the defense build-up.

(2) The expected increase in the availability of metals may stimulate some nondefense investment such as commercial construction, and may thereby cause some additional inflationary pressure; however, it has strengthened fear that we are building up excess capacity in the hard goods sector of the economy, and that investment in plant and equipment after a time will be rather generally discouraged.

(3) In the opinion of some, price downturns, though slight, may lead to further deferment of postponable purchases, because of expectations of greater price declines.

(4) The outlook for a continued lag in the growth of the security program expenditures behind the rates projected in January, and for smaller deficits both this fiscal year and next, invites the conclusion that demand arising in the government sector of the economy may not be strong enough to offset deflationary movements in the private sector.

(5) With the increasing vigor of anti-inflationary policies and import restrictions abroad and a prospect of reduced U. S. exports, foreign demand appears to be lining up on the side of deflation.

In framing an evaluation of the economic outlook, the Council has considered all of these factors. Those who would advocate quick relaxation of controls on the basis of these factors, however, should observe these notes of caution.

First, those with policy responsibilities should be careful not to over-react to moderate shifts in the situation. Particularly in the case of materials, there is a danger of swinging from one wrong extreme to the other. The improvement in nondefense supplies is partly the result of the successful operation of the allocations program; it provides no self-evident case for the abandonment of the program and the liberation of all the demand for materials which it now is bottling up.

Second, the "risk" argument for retention of a working and operable anti-inflationary apparatus is in no sense weakened by any of the foregoing considerations. The judgment of the most extreme deflationists would be completely upset by a new international crisis or by a sharp fall in the rate of personal saving. The same is true of those who expect a continuation of relative stability.

Third, even were one to take all of the above "deflationary" factors most seriously, it would not answer the question of timing. It would not be clear whether they make a case for deflation in the near future--say, during the remainder of this year--or thereafter. It is hard to see how the economy can fail to keep operating at very high levels for all or virtually all of 1952.

Assuming no new international outbreak, the economic outlook for the coming months is for moderately rising output within a framework of general economic stability. This working hypothesis appears to be the best choice from among several combinations of alternatives, for two reasons.

First, it is highly probable that the aggregate demand for goods and services will increase through the year. A rise in Government demand for the security program is almost certain, though the rate of increase is not so clear. Likewise, it is reasonably sure that consumer buying will expand. The prospect is for higher disposable personal income; and even assuming that the saving ratio remains at approximately the level of the past year, a moderate increase in spending would occur. At the same time, business investment should not vary much from its first quarter level. The one type of business investment which is most likely to cause abrupt changes in total investment--inventory accumulation--should exert its influence on the side of growth rather than decline. With inventories of most civilian goods worked down to a normal relationship with sales, not much further attrition is to be looked for from this source; and rising defense output should bring some net addition to total nonfarm inventories.

Second, the pressure of rising aggregate demand on supplies, and ultimately on materials sources and manpower, is not likely to be significantly inflationary. It should result in growth of physical output and continued high level employment rather than rising prices.

The topography of the markets, at any time, may not of course be a level plain. There may be inflationary peaks and deflationary valleys; but no upheavals are on the near horizon.

Average prices, both retail and wholesale, may be expected to move within a very narrow range the remainder of this year, although fairly sharp changes in either direction in limited segments of the price structure are always possible. This is particularly true in the farm and food areas. While the chances of a major price movement are slight in both the inflationary and deflationary directions, for the time being they remain somewhat greater on the inflationary side. Growth exposes an economy already operating at high levels of output and employment to the danger of inflation. Furthermore, while there is no clear evidence that personal saving will drop, a decline is a possibility. For example, with disposable personal income at the first quarter level, a shift of only 2 percent of income from saving to spending would add 4.5 billion dollars to consumer expenditures. During the second half of this calendar year, there will be a substantial Government deficit, and while its magnitude will probably be smaller than estimated in January, it will nevertheless be a potential disturber of the economic calm.

It may be that these possibilities of expansion in demand will be reinforced by the effects of the wage-price dispute in steel. First, there is the strictly economic consequence of what, broadly speaking, seems to be the probable settlement: wage increases roughly in line with the recent WSB recommendation and, as a corollary, a moderate advance in steel prices. This consequence would be the impetus given to the wage-price spiral in the private economy, through "pattern-spreading" on the wage side, through the pressure exerted on prices in the industries to which the "pattern" spread, and through the impact of higher steel costs on the prices of steel users. But these effects are readily exaggerated. For one thing, many industries will continue to face soft demand for their products; they will not be able to pass on cost increases whether they want to or not. For another thing, many features of the "package" recommended in the steel case are already included in other major labor contracts; they cannot spread to such industries a second time. However, it may be that the unanalyzed total size of the package will act as a psychological stimulant to labor leaders in other industries.

The outlook could also be affected, of course, by an early truce in Korea. It is commonly assumed that in the event of a truce the balance between inflationary and deflationary forces would be resolved in favor of the latter. But it is not possible to foresee whether such would be the case, what the extent and the timing of consumer and business reaction would be, and what alterations might result in the size or character of the national security program. A truce would be a factor, initially psychological in nature, that might upset the working assumptions on which the present outlook is based. It too, however, is a factor which can be exaggerated. It seems that a good deal of its early psychological impact may already, because of the protracted character of the negotiations, have been heavily discounted, both by businessmen and by consumers.

The outlook for the longer run

Our analysis seems to lead with fair assurance to the short-run conclusion that--within the framework of an unchanged international situation--maintenance of a high degree of stability is the best economic guess for all or most of 1952. But this analysis does not carry us much farther. In planning its study and work in the months immediately ahead, the Council intends to give close attention to the longer-run outlook. It now appears that the key factors which largely will determine the inflationary-deflationary balance over the longer period are: (1) the firmness of military production schedules and the actual pace of the security program, (2) the vitality of nondefense investment in plant and equipment, particularly as affected by vanishing shortages of materials and possible excess capacity in some basic industries, and (3) the course of the personal spending rate, as affected by income distribution, the price structure, and the pattern of saving.

Policy implications of the short-run outlook

If we assume that the international front remains relatively quiet for the remainder of this year, and that work stoppages or other unforeseen upheavals in the private economy do not reach dangerous proportions, the current economic outlook does not seem to call for major policy revisions at this time. It is timely, however, to concentrate attention now upon these immediate policy considerations:

1. The expansion of the productive power of the economy which has already taken place, and the room for further expansion, have brought concrete support to the original thesis of the Council that a defense program within the current framework would not excessively strain our resources. The present situation does not justify the concern about a drastic deflation now expressed in some quarters. But it does enable decisions regarding the size and pace of the security program to rest more heavily on the best appraisal of the international need, with somewhat less concern about the ability of the economy to carry the burden without excessive inflationary or other strain.

The Council would not for a moment lend its support to defense outlays in order to "stabilize" the economy; there are better ways of doing that if that should become necessary. But if a moderate expediting or enlargement of the security effort is determined to be in the national interest, then no valid considerations of the effects upon our economic strength should stand in the way. Correspondingly, if to any extent the slow-down in the security program has been dictated by general current economic considerations, rather than by a new appraisal of the world situation, this matter should be reconsidered in the light of the now accumulated evidence concerning the productive power of the economy. Particularly, these considerations should be impressed upon the Congress, as it moves towards drastic downward revisions in the security program, based seemingly upon concern whether the economy has the power to support them.

There would also appear to be in some of the operating agencies a naturally understandable zeal to lift the level of civilian supplies, without first considering whether the unanticipated abundance in some lines of supply might not be used to modify the trend towards some let-down of effort on the security front, including mutual security.

2. With respect to economic stabilization, it is too late for the Council to comment helpfully again on the specific terms of the wage recommendations in the steel situation. That particular matter, and the accompanying question of the size of the price adjustments to be made, have moved into an area of extremely difficult practical negotiation. But it is not too late for the Council to remark, because it has a bearing upon future policy, that in our judgment the steel situation might not have reached the current degree of difficulty if operating officials had moved, during the ample time they had to do so, toward an integrated and consistent price and wage stabilization policy. The recurrent Economic Reports of the President, in our opinion, not only underscored the vital need for an integrated and clearly announced price and wage policy, but also set forth in general terms the contours of such a policy as a guide to the operating agencies. Most emphatically on various occasions, the Council has expressed its extreme concern about what seemed to us the inescapable consequence of handling price and wage policy in separate compartments, and especially about the absence of a sufficiently clear, formulated and adhered-to wage policy.

With the current steel situation as an example, there should be renewed determination, when that particular situation has been resolved, to recognize the vital importance of formulating and promulgating an inter-related wage and price policy supported by general economic analysis and understandable to management, labor, the Congress, and the public. In our opinion, there is no other way to save the stabilization program, and we believe that the national interest requires that it be saved.

The accomplishment of this objective requires, in our opinion, (a) a more effective coordination of operating and policy-making responsibility for various aspects of the mobilization and stabilization program, and (b) further recognition by various officials of the proper and useful role which the Reports under the Employment Act should perform in providing general and unifying guides for specific economic policies.

3. In stating that the stabilization program must be saved, the Council feels it of great importance that the Government not be stampeded prematurely into decontrol, either on the materials side or on the price-wage side, in view of the easing of inflationary pressures and the currency of deflationary talk. It would be particularly easy to err in this

respect in the case of the allocation program where, as noted above, some of the easiness in materials supplies undoubtedly is the result of the controls themselves. In addition, it is urgently important that we maintain an effective, going controls apparatus in view of the risks and uncertainties in the precarious international situation. Partly for this reason, it will be wise to press selective decontrol efforts--or, as OPS more accurately phrases it, "selective suspension" as actively as a careful and continuing survey of individual markets warrants. So far as possible, efforts of the Congress to impose rigid, mechanical decontrol formulas should be resisted. This can be done best by demonstrating that conscientiously applied administrative discretion can bring the desired results.

4. Consideration is being given within the Administration to some further easing of selective credit restraints, especially instalment credit regulations. Such action may constitute a mild and appropriate adjustment to the changed materials outlook.

Respectfully submitted,

Leon H. Keyserling

Leon H. Keyserling, Chairman

John D. Clark

John D. Clark

Roy Blough

Roy Blough