The Annual Economic Review
January 1953

A Report to the President
By the
COUNCIL OF ECONOMIC ADVISERS
LETTER OF TRANSMITTAL

COUNCIL OF ECONOMIC ADVISERS,
Washington, D. C., January 12, 1953.

The President:

Sir: The Council of Economic Advisers herewith submits a report, the Annual Economic Review: January 1953, in accordance with section 4 (c) (2) of the Employment Act of 1946.

The members of the Council, in this our final Review, desire to acknowledge the fine assistance and cooperation received during its preparation from economists on the Council's staff, including Karl M. Arndt, Benjamin Caplan, John C. Davis, Rosalie K. Epstein, Joseph L. Fisher, Catherine A. Heitzman, Frances M. James, John P. Lewis, David W. Lusher, Walter S. Salant, Charles Schultz, Mary W. Smelker, Penelope Hartland Thunberg, Haskell P. Wald. We desire also to cite the conscientious hard work performed by our administrative and clerical staff, including Mayme Burnett, Catherine T. Connors, Margaret F. Foley, Robert A. Garlock, Margaret E. Gooding, Cathryn S. Inman, Nina A. Kleger, Joseph W. McKenney, Mary M. Millspaugh, Isabelle M. Peterson, Dorothy L. Reid, Odelia C. Scales, Gertrude Shepard, Royal E. Shepard, Mabel Skrock. And without listing their names, we shall never forget the contribution made by earlier Council members and staff during the vital formative years of the Council and its work. Finally, our work would not have been possible without the constant cooperation of other governmental agencies and personnel upon whom we must draw heavily for data and critical evaluation; or without the eager and continuous interest of those representatives of business, labor, farm, and consumer groups with whom we have consulted at frequent intervals during more than 6 years.

Respectfully,

Leon H. Keyserling
Chairman.
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Chapter 1. Developments During 1952

THE ECONOMY IN GENERAL

At the beginning of 1952, it appeared likely to most observers that the security program, showing accelerated strength throughout the year and making heavier inroads into the stocks of scarce materials, would absorb all the expected gain in national output and curtail the production of consumers' durable goods and private construction.

By the second quarter of the year, however, these expectations had begun to waver, and by the fourth quarter they had been overturned. The economy was prosperous as it entered the year, and it was even more prosperous as it moved into 1953; but during the year the expansive factors of production and employment shifted from public demand toward private demand and were adequate to sustain both types of demand without strain. Meanwhile, a remarkable degree of price stability was achieved. Neither Government spending for security nor private demand expanded enough to force a rise in the general level of prices in the face of powerful general measures such as high taxation to restrain inflation, while wage and price controls served to curb increases in those selected areas where inflationary pressures were greatest.

In the first 6 months of the year, increasing Federal outlays for defense, together with a small rise in spending by consumers and a slight gain in other Government expenditures, more than offset a fall in net foreign investment and the drop in domestic private investment which resulted from a sharp decline in the rate of inventory accumulation. The combined effect of these changes (seasonally adjusted rates) was a moderate growth in total production. These developments were mainly a repetition of the second half of 1951, except that there seemed to be a few more soft spots in the economy, and the possibility of deflation began to receive some of the attention long given to inflation. (See appendix table B-1.)

In the second half, output expanded considerably faster than during the first half, despite the fact that national security expenditures were only slightly higher. There was a general rise in private demand, particularly in the last few months. Beginning in the third quarter, there was a marked upturn in the rate of net additions to business inventories, and in the fourth quarter, consumer expenditures made the best gain of the year. Net foreign investment continued to fall, and there was little change during the period as a whole in the rate of gross private domestic investment other than in inventories.
It is noteworthy that the accelerated rise in total demand during the last months of 1952 did not result in a new rise in prices. The increases in demand were heaviest in consumer goods areas where there had been some underutilization of productive capacity. Moreover, the rapid growth in productive capacity during the previous 2 years had improved the general ability of the economy to meet increases in spending.

**CHART 5**

**CHANGES IN TOTAL PRODUCTION**

Total output of goods and services, measured in either current or constant prices, expanded about one-third as much in 1952 as in the preceding year.

<table>
<thead>
<tr>
<th>PERCENTAGE CHANGE IN GROSS NATIONAL PRODUCT</th>
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<tr>
<td>0</td>
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**CURRENT PRICES**

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**1952 PRICES**

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**SOURCES:** DEPARTMENT OF COMMERCE AND COUNCIL OF ECONOMIC ADVISERS.

**Production**

The output of goods and services during 1952 totaled 345 billion dollars, compared with 329 billion during 1951, a rise of 16 billion or about 5 percent. When allowance is made for price changes, this represents an expansion of about 2½ percent in physical output, much less than in 1951. (See chart 5 and appendix table B-2.) In 1951, production had responded to strong pressure from private expenditures only during the early months of the year, and to strong pressure from Government demand throughout. In contrast, additional demands were less in 1952, although private demand showed increasing vigor toward the end of the year while public demand was rising very little.

The monthly index of industrial production, which is more sensitive than gross national product to changes in the business weather, averaged
Industrial production declined after the first quarter of 1952, and reached a low during July largely as a result of the steel strike. But it rebounded rapidly during the fall and ended the year about 5 percent above the 1951 high reached in April.

INDEX, 1935-39 = 100*

219 percent during 1952 (1935-39 = 100), or about the same as during the previous year, but varied considerably from month to month. (See chart 6 and appendix table B-17.) During the first quarter, the index averaged moderately higher than in the fourth quarter of 1951, but by July it had been pulled down 13 percent, as a work stoppage in the petroleum industry was followed by an 8-week shutdown in steel and iron ore production which in time curtailed the output of durable manufactures, notably automobiles. Industrial production rebounded rapidly in the third quarter to reach a new postwar high in September, as the output of steel soared to new record rates. During the fourth quarter, the index was pushed up further by generally increased production, which reflected in large part the rise in consumer and inventory buying.

Employment and unemployment

Total civilian employment was estimated at 61.5 million in December 1952, or 500,000 more than in December 1951. Comparing the 2 years as a whole, the civilian labor force averaged about 63.0 million in 1952, or approximately the same as in 1951. (See chart 7 and appendix table

37
The civilian labor force averaged about the same in 1952 as in the preceding year, due to the build-up in the armed forces. Nonagricultural employment was at its highest recorded level, while employment in agriculture continued its long-run decline.

### CHART 7

**CIVILIAN LABOR FORCE**

The civilian labor force averaged about the same in 1952 as in the preceding year, due to the build-up in the armed forces. Nonagricultural employment was at its highest recorded level, while employment in agriculture continued its long-run decline.

**MILLIONS OF PERSONS**

- **CIVILIAN LABOR FORCE**
  - 1950
  - 1951
  - 1952

- **NONAGRICULTURAL EMPLOYMENT**
  - 1950
  - 1951
  - 1952

- **AGRICULTURAL EMPLOYMENT**
  - 1950
  - 1951
  - 1952

- **UNEMPLOYMENT**
  - 1950
  - 1951
  - 1952

*14 YEARS OF AGE AND OVER.

**SOURCE:** DEPARTMENT OF COMMERCE.
Civilian employment rose only slightly from a monthly average of 61.0 million in 1951 to about 61.3 million in 1952. At the same time, unemployment fell from 1.9 million in 1951 to 1.7 million, or 2.7 percent of the total civilian labor force, in 1952, the lowest annual average since World War II.

Over the year, there were small increases in the number of government civilian workers (Federal, State, and local) and those engaged in finance and service activities. Agricultural employment between 1951 and 1952 continued its long-term decline, and there was a fairly sizable drop in mining. Employment in manufacturing industries was somewhat irregular. A rather steady drop during the first 7 months of the year was followed by a sharp rise during the last 5 months, concentrated largely in industries producing durable goods. The monthly average for manufacturing was 16 million in 1952, about the same as in 1951. (See appendix table B-13.)

Despite the reduction in unemployment generally, the labor supply situation in most of the Nation's major production and employment centers was not markedly different at the end of 1952 than it was a year before, although some tightening appeared to have developed. During the past year, the labor force was on the whole adequate to meet defense and civilian needs, although there were shortages in some areas and surpluses in others. In November, the Department of Labor reported 4 labor shortage areas and 18 areas with substantial labor surplus.

Work stoppages. Man-days of idleness directly due to work stoppages during 1952 were more than double the 1951 total. More time was lost because of strikes than in any other year since 1946. The brief strike in the steel industry in April and May, and the prolonged one in June and July, directly involved about 560,000 workers, and accounted for more than two-fifths of the total time lost. Among other important work stoppages were those in petroleum refining and natural gas, railroads, carpet and rug manufacturing, coal mining, West Coast lumber, the manufacturing of farm machinery, the telephone and telegraph industries, and construction.

Economic stability

Although the economy encountered many changing currents during 1952, it demonstrated a remarkable degree of over-all stability. It was marked by selective inflationary pressures, mainly in the markets most directly affected by the defense program, and with considerable easiness in the markets for consumer goods. The high degree of general stability was aided by general and direct restraints which limited inflationary pressures in some markets, while the interaction of supply and demand held down prices or reduced them in others.

Prices. Consumers' prices varied little from month to month, and in November were only 1.3 percent higher than a year before. (See chart 8 and appendix table B-24.) In contrast, during 1951 there had been a rise of nearly 6 percent. Much of the rise in 1952 is accounted for by the upward creep of rents, the cost of utilities and services, and
Consumers' prices rose 1.3 percent during the year. Food prices reached a peak in August, and then dropped during the rest of the year. Apparel prices were steady during the last few months, after falling earlier. Rents increased throughout the year.

The monthly index of wholesale prices was about 3½ percent lower in December than a year earlier. (See chart 9 and appendix table B–23.) In the first half of the year, the average decline was a continuation of the downward wholesale price trend during the last 3 quarters of 1951, and reflected reductions in most major commodity categories. In the second half of the year, however, it reflected only the sharp drops in farm prices and, as a result, in prices of processed foods. Industrial wholesale prices showed some disposition to stabilize.

It was increasingly apparent that the readjustment of the price structure during the 15 months after March 1951 had eliminated the worst interprice
distortions caused by the violent waves of post-Korean inflation, and had re-established roughly the relationships among raw material, industrial, and retail prices that prevailed in early 1950. The most dramatic aspect of this readjustment had been the prolonged rapid decline of the prices of imported raw materials from their early post-Korean peaks.

Wages. Wages continued to increase slowly in 1952. Average hourly earnings for the Nation's factory workers reached a new peak of $1.715 in November, 5½ percent above the year before. Excluding overtime, average hourly earnings of manufacturing workers increased about 4 percent during the same period. During 1951 and 1952, workers in manufacturing industries producing durable goods enjoyed the greater gains, although the differential was considerably larger in 1952. Wages of all other major groups of workers also increased during the past year. (See chart 11 and appendix table B-15.)

Only a small part of the wage increases during the past year was dissipated by higher living costs. But when account is taken of taxes as well as prices, the wage gains of workers were moderate. Thus, the take-home pay, that is, net spendable average weekly earnings of factory workers with 3 dependents, adjusted for price changes, increased only about $2.50 during
The divergence in the movements of the wholesale and consumers' price indexes since the Korean outbreak has resulted mainly from price changes in items which are not common to both indexes.

1/ The consumer price index.

2/ This wholesale group includes raw and semifinished materials and producers' equipment; the retail, rents and services.

Source: Board of Governors of the Federal Reserve System, based on data from Department of Labor.
1952, compared with an increase in gross average weekly earnings of approximately $5. (See appendix table B-16.)

Price and wage control. Early in 1952, the Office of Price Stabilization adopted a policy of suspending price controls in those areas where market conditions permitted. Among the commodities affected by this suspension of ceilings were fats and oils, hides and skins, leather, shoes, cotton, wool, synthetic fibers, textile fabrics, most clothing items, soft floor coverings, and radios and television sets. In addition, Congress in renewing the Defense Production Act in mid-1952 exempted fruits and vegetables from price control. At the present time, ceilings apply to about 70 percent of the wholesale price index, compared with over 90 percent early last year, and about 50 percent of the consumers’ price index, compared with about 65 percent when price control was established. About one-quarter of the portion of the consumers’ price index under control, however, involves commodities for which, under the law, ceilings automatically rise if farm parity prices rise.

Exceptional price ceiling increases were made in 1952: in the case of steel after the strike; in the case of copper after the foreign price of copper rose from 27 1/2 to 36 1/2 cents a pound when the agreement with the Chilean Government was not renewed; and in the case of aluminum to increase supplies. Otherwise, requests for price increases to offset cost increases were approved or rejected in accordance with OPS’ regular relief standards. The increases granted were mainly in defense-related areas where, in the absence of controls, it seems clear that prices would have gone even higher.

Since the establishment of the Wage Stabilization Board, approximately 121,000 applications have been submitted by employers wishing to alter, in one respect or another, the compensation of their employees. Until the Wage Stabilization Board became inoperative on December 6, as a result of the resignation of the industry members, this tripartite Board had examined and acted on 109,000 of these cases, of which 83.3 percent were approved, while 16.7 percent were modified or denied.

The result of wage stabilization—which is not, and cannot be, an absolute and enduring wage freeze—is shown by some comparisons of wage movements. During 1950, adjusted for shifts in employment, average hourly earnings of production and related workers in manufacturing, as calculated by the Wage Stabilization Board, rose at an average rate of 0.7 percent a month. During the second half of 1950, following the Korean outbreak but prior to the start of the wage stabilization program, the rate of increase was even higher—0.9 percent a month. From the date of the establishment of the program in January 1951 until November 1952, average hourly earnings advanced at the rate of only 0.4 percent a month.

One outcome of the steel case, which was settled after a prolonged strike, was that in renewing the Defense Production Act the Congress replaced the original Wage Stabilization Board with a statutory board having more limited authority. Under the revised Act, the disputes function
CHART 11

CHANGES IN HOURLY EARNINGS IN MANUFACTURING INDUSTRIES

DURABLE GOODS INDUSTRIES

PERCENTAGE CHANGE, 1951 TO 1952

0 +1 +2 +3 +4 +5 +6 +7 +8 +9 +10

- PRIMARY METALS
- ORDNANCE
- TRANSPORTATION EQUIPMENT
- INSTRUMENTS
- TOTAL DURABLE GOODS
- FABRICATED METALS
- MISCELLANEOUS
- MACHINERY (EXCEPT ELECTRICAL)
- STONE, CLAY, AND GLASS
- ELECTRICAL MACHINERY
- FURNITURE
- LUMBER

NONDURABLE GOODS INDUSTRIES

PERCENTAGE CHANGE, 1951 TO 1952

0 +1 +2 +3 +4 +5 +6 +7 +8 +9 +10

- RUBBER
- PETROLEUM AND COAL PRODUCTS
- PAPER
- CHEMICALS
- PRINTING AND PUBLISHING
- FOOD
- LEATHER
- TOTAL NONDURABLE GOODS
- TOBACCO
- TEXTILE-MILL PRODUCTS
- APPAREL

\[\text{\% CHANGE FROM NOVEMBER 1951 TO NOVEMBER 1952.}\]

SOURCE: DEPARTMENT OF LABOR.
was separated from the wage stabilization authority. More recently, the Wage Stabilization Board, in acting on a request by the coal industry for an increase of $1.90 a day, which had been agreed to by the union and the operators, approved only $1.50 a day. After a thorough review of the case, the President directed the Economic Stabilization Agency to approve the original agreement. This decision was made because it was felt that no steps should be taken at that time which might lead to an industry-wide work stoppage, or that might make it impossible to turn over a going stabilization program to the incoming administration. Following this, the Chairman of the Wage Stabilization Board and the industry members resigned. Because of difficulties in securing new industry members, the Economic Stabilization Administrator designated the four public members to serve as a Wage Stabilization Committee. Thus, efforts to reduce the backlog of 12,000 cases can continue.

**Bank credit and money supply.** It had been thought early in 1952 that the banking system might have to supply a considerable amount of new money to the Government to finance a substantial cash deficit. There was also reason to believe that the volume of private borrowing from commercial banks would level off, partly because of restraints on civilian production. However, private borrowing once again, as in the preceding year, was the principal agent of expansion of bank credit and the money supply.

Commercial bank loans increased more than 6.5 billion dollars or about 12 percent during 1952, compared with 5.5 billion or 11 percent during 1951. Consumer loans accounted for a much higher percent of the rise in 1952. Commercial bank holdings of U. S. Government securities, which had de-

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<td>Factor</td>
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<tr>
<td>Loans of commercial and mutual savings banks</td>
</tr>
<tr>
<td>Securities of U. S. Government held by banking system</td>
</tr>
<tr>
<td>Securities of corporations and State and local governments held by commercial and mutual savings banks</td>
</tr>
<tr>
<td>Treasury deposits</td>
</tr>
<tr>
<td>Monetary gold stock</td>
</tr>
<tr>
<td>Other factors, net</td>
</tr>
<tr>
<td>Net change in privately held deposits and currency</td>
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</tbody>
</table>

1 Includes State and local government deposits.
2 Estimates based on incomplete data; second half by Council of Economic Advisers.
3 Includes commercial banks, mutual savings banks, Federal Reserve banks, and the Postal Savings System.
4 A decrease in Treasury deposits is denoted by a positive figure, and an increase by a negative figure. In the case of other specific factors, the reverse is true.
5 Less than 50 million dollars.
6 See appendix table B-29 for aggregate money supply and its components.

NOTE.—Detail will not necessarily add to totals because of rounding. Signs preceding figures in columns indicate effect on the money supply.

Source: Board of Governors of the Federal Reserve System (except as noted).
creased 0.5 billion dollars or less than 1 percent in 1951, rose by 2 billion or 3 percent in 1952, and in both years investments in corporate securities and State and local government issues expanded about 1 billion dollars or 7 percent. (See appendix table B-28.)

In both 1951 and 1952, an expansion of Federal Reserve bank credit was one of the factors which supplied commercial banks with reserves. During 1952, borrowing by member banks provided the greater amount of reserves from this source, while in the previous year the net increase in Federal Reserve bank holdings of U. S. Government securities was more important. The average of Federal Reserve discounts in 1952 was more than one and one-half times greater than in 1951, but Federal Reserve holdings of Government obligations averaged about the same. (See chart 12.)

The privately held money supply (including the bank deposits of State and local governments) expanded almost 9 billion dollars or about 5 percent in 1952, nearly as much as in the previous year. The principal factor in the rise last year was the growth in bank loans, with the increase in investments next in importance. The agents which tended to expand the

**CHART 12**

**BANK LOANS AND INVESTMENTS**

Total bank loans rose at about the same rate in 1952 as in 1951. Investments expanded more rapidly than a year earlier, primarily because of increased holdings of U. S. Government securities.

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money held in the non-Government sector of the economy were only partly offset by the higher level of Treasury deposits, and by other factors. Also, in 1952, a large part of the growth in the private money supply was in time deposits, about 4.2 billion dollars compared with slightly more than 2 billion in 1951. Demand deposits and currency, the active portion of the money supply, increased in substantially smaller volume in 1952 than in 1951.

Credit policy. During 1952, the credit controls which had been imposed under authority of the Defense Production Act were terminated or suspended. These actions, whether on the initiative of the administrative agencies concerned or in compliance with new legislation, reflected the moderate character of consumer demand relative to supply, the increasing availability of many scarce materials for civilian production, and the growing belief that the return of serious inflationary pressures had at least been postponed.

In May, the voluntary program of credit restraint was placed on a stand-by basis, and the regulations applying to consumer instalment credit were suspended. In June, the terms of residential mortgage loans were eased. Then, at midyear, in renewing the Defense Production Act the Congress withdrew or extensively limited the power to use these controls. The new legislation provided that, in the future, voluntary campaigns to restrain credit could no longer be organized under the authority of the Act. It also withdrew authority to place controls on instalment credit or other forms of consumer borrowing, and restricted the power to impose significant restrictions on residential mortgage credit to periods when the seasonally adjusted annual rate of housing starts, based on the activity of the preceding 3 months, exceeds 1.2 million units.

In accordance with the last provision, mortgage credit restrictions, with minor exceptions, were removed in September, since the adjusted index of new starts during June-August fell below the stipulated rate. The restrictions on loans for commercial construction were lifted at the same time.

During 1952, the Federal Reserve System, through purchases of Government securities in the open market, partly offset the drain on bank reserves resulting from a growth of currency in circulation. Additional bank reserves required to support expansion of bank deposits resulting from increases in bank credit were obtained by banks through borrowing from the Federal Reserve Banks. No change was made in the Federal Reserve Banks’ discount rates during the year.

Materials policies. In addition to the effects of price, wage, and credit policies during the year, an important contribution to stability was made by materials allocations and controls. These measures, primarily directed to the facilitation of essential production, have helped to expand our total economic strength, the most fundamental approach in the longer run to overcoming inflation. These measures have also assisted in the stabilization of scarce commodity prices by limiting the effective demand for such
 commodities. Under the current mobilization program, early 1952 was the peak period of materials controls restraint. The improving materials supply situation was reflected in increased allocations for the second half of 1952 and the first half of 1953.

Moreover, important as all of these specific anti-inflationary programs were in 1952, probably the greatest supports to stability were those provided by the Nation’s continued rapid expansion of productive capacity and by the maintenance of the high tax rates enacted in 1950 and 1951.

TRENDS WITHIN MAJOR SECTORS

Consumers

Income. Personal income was about 14 billion dollars or 5½ percent higher in 1952 than in 1951. Most of the 1952 rise occurred in the last months of the year as labor income, which had been creeping up gradually, began to climb sharply because of higher wages, increasing employment, and longer working hours. (See chart 13 and appendix tables B-6 and B-7.)

Net income of farm proprietors was slightly lower than in 1951, with prices falling and costs still rising. The level of net farm income in 1952 was substantially higher than in 1949–50, but well below 1948. Income from other businesses and the professions rose in 1952, but less rapidly than in the year before. Dividends, rents, interest, and transfer payments also increased.

Total personal earnings expanded about 6 percent during the year, but personal taxes went up at a faster rate, so that spendable income gained about 10 billion dollars or 4 percent. In constant prices, this rise in disposable personal income represents an increase in per capita purchasing power from $1,486 to $1,496 (1952 prices), a level exceeded only in 1944. (See appendix table B-10.)

Spending and saving. In 1952, for the second consecutive year, the average rate of personal saving was exceptionally high, measured by either prewar or earlier postwar experience. Consumer expenditures were about 8 billion dollars greater in 1952 than in 1951, an amount sufficiently less than the expansion in disposable income to lift the percent of income saved from 7.6 percent to approximately 8 percent. (See appendix tables B-4 and B-9.)

During the first half of the year, consumer buying (at seasonally adjusted annual rates) increased faster than relatively stable disposable income. The rate of saving dropped from about 9 percent in the second half of 1951, a postwar record, to less than 7.5 percent in the first half of 1952. (See chart 14.) During the third quarter, however, the rate of consumption expenditures remained steady, despite a considerable rise in earnings; and the saving ratio climbed most of the way back to the peak level reached in 1951. The third-quarter calm in the consumer markets was partly the result of the steel strike, which by sharply reducing the output of automobiles contributed to a reduction in sales.
In 1952, personal income increased about half as much as in 1951, with most of the rise occurring in the second half of the year. All major components except farm proprietors' income participated in the increase.

Compared with the third quarter, the fourth quarter was one of vigorous activity. Disposable income, seasonally adjusted, registered the largest quarter-to-quarter rise since the last 3 months of 1950, and spending the greatest gain since the first 3 months of 1951. The saving ratio, however, remained virtually unchanged from the previous quarter.

The markets for durable goods felt the greatest impact of the fourth-quarter growth in consumer spending, as might be expected from the jump in automobile production following the end of the steel shutdown. But the increased buying was by no means limited to automobiles or to the relatively small number of other commodities which had been scarce. Nor can it be directly accounted for simply by the suspension of instalment credit
Personal income and consumption expenditures expanded significantly in the fourth quarter of 1952, after 3 quarters of moderate growth. Saving for the year as a whole continued at a high level.

**Sources:** Department of Commerce and Council of Economic Advisers.
controls early in May, which appeared to have given a fillip primarily to automobile sales. The rise in buying during the last months of 1952 embraced nondurable goods as well as durables, textiles as well as cars. It was felt throughout the Nation and in the markets for all major classes of commodities.

**Housing.** Expenditures for new residential construction in 1952, which had seemed to many analysts likely to fall from the 1951 level under the combined pressure of materials shortages, credit restrictions, tightness in the market for Government-insured or guaranteed mortgage loans, and a decline in the rate of new marriages, slightly exceeded the 1951 total of 11 billion dollars. New nonfarm housing starts, which had been just below 1.1 million units in 1951, were just above that level in 1952. (See appendix tables B-18 and B-19.)

**Personal debt.** Although consumer and residential mortgage debt continued to increase, the former much more rapidly than in 1951, saving in the form of liquid and other financial assets also remained at a very high rate. The high rate of liquid saving, and the steadiness of the price level, probably resulted in some net improvement in the financial position of consumers in 1952 despite the rapid rise in debt.

Consumer credit outstanding expanded more than 3 billion dollars or about 15 percent, compared with about 0.5 billion or 2.7 percent in 1951, and 3.3 billion or 19.6 percent in 1950. Practically all of the 1952 expansion was in instalment credit, which began to climb largely in connection with purchases of automobiles after the suspension of the consumer credit regulations in May. (See chart 15 and appendix table B-27.)

It is estimated that in 1952 residential mortgage debt on 1- to 4-family nonfarm houses expanded 7 billion dollars or 14 percent, to reach a total of 59 billion. The dollar increase was about the same as in 1951, but about 10 percent lower than the increase in 1950.

**Business**

As is apparent from the general production and employment data already cited, 1952 was a good year for business. The first half of the year was much like the last part of 1951. But the story of the second half of 1952 was quite different. It began quietly enough, but it ended with a display of activity which raised sales and incomes for the year as a whole above the levels in the last half of 1951 without causing significant upward pressures on prices. This rise was associated mainly with a pick-up in inventory buying and with a substantial increase in retail sales, particularly of durables. (See appendix tables B-21 and B-22.)

**Inventories and sales.** Beginning in the third quarter of 1951, the rate of business inventory accumulation declined, as businessmen attempted to bring over-plentiful stocks into line with sales volume. By mid-1952, sellers of such diverse commodities as textiles, apparel, autos, and home appliances appeared to have completed the process of paring down the excess inven-
Consumer credit outstanding declined seasonally in the first quarter of 1952, and then climbed in each succeeding month. Most of the expansion was in instalment credit, reflecting in part the rapid rise in loans on automobiles which followed the suspension of consumer credit restrictions early in May.

During the third quarter, a change became evident as nonfarm inventories were accumulated at an annual rate of 3 billion dollars. Since there was some decline in inventories of steel during this quarter, the rate of accumulation of nonsteel items exceeded 3 billion dollars. Most nondurable goods industries and the nonsteel-using segments of durable goods industries shared in this rise. However, business sales to ultimate consumers did not rise in line with inventories; production and shipment of producers’ durables and automobiles fell, largely as a result of the steel strike. But as the final quarter of the year got under way, metal-using firms had already completed in most cases a remarkable recovery. Production and sales of automobiles, appliances, apparel, and almost all types of commodities expanded considerably. At the same time, inventories con-
continued the more rapid climb begun earlier, while government purchases of goods and services rose moderately.

Earnings. Business earnings reflected the change in the pattern of general economic activity. Corporate profits before taxes in the first half of 1952 were slightly above the levels to which they had fallen in the latter part of 1951. Rising costs in relation to prices, and lagging sales volume, joined with continued increases in depreciation allowances to prevent a more substantial improvement. During the third quarter of the year, profits before taxes remained approximately unchanged. Considering, however, the sharp drop in third-quarter profits of auto manufacturers and many steel producers and fabricators, the maintenance of over-all profit levels meant that many firms not affected by the steel strike improved their profit positions noticeably. (See appendix tables B-34 through B-38.)

The rapid rise in business activity during the closing months of the year showed up in substantially higher profits. (See appendix table B-34.) The rise in profits was not due, however, to any general rise in price levels, although in some areas higher profits reflected price increases permitted by the Office of Price Stabilization under its relief standards. And in other areas they reflected lower prices of raw materials. Profits after taxes in 1952 averaged about the same as in the second half of 1951, but well below the level of 1951 as a whole.

Investment. During 1952, gross private domestic investment was about 7 billion dollars lower than in 1951. (See chart 16 and appendix table B-5.) All of this decline was due to a drop in the rate of inventory accumulation from over 10 billion dollars in 1951 to 2 billion in 1952. Investment in fixed capital actually rose during the year by about 1 billion dollars. New construction, both residential and other, remained relatively constant in 1952, while producers' durable equipment rose by 1 billion. Investment expenditures for nonfarm producers' plant and equipment rose during the first half of the year to an annual rate of 31 billion dollars, 3 percent more than it had been in the final half of 1951. In the third quarter of 1952, however, delays in shipments of producers' durables and slower rates of progress on construction projects, under the impact of the steel strike, caused investment outlays by business to decline moderately. The quick recovery of steel operations and equipment deliveries made possible an increase in expenditures for nonfarm plant and equipment in the fourth quarter to a new record level.

The largest increases in investment during 1952 were made by manufacturing industries, which added 1.3 billion dollars to their expenditures. (See appendix table B-20.) This new investment was fairly evenly distributed between manufacturers of durable and nondurable goods. In nonmanufacturing, only public utilities showed increased plant and equipment expenditures for the year as a whole, with mining, transportation, and commercial firms showing a decline. Beginning in the fourth quarter of 1951, and until the third quarter of 1952, expenditures for plant and
equipment by the commercial, communication, and construction group of industries declined, responding to restrictions on the use of steel, aluminum, and copper. The final quarter of 1952 found these firms once again increasing their expenditures.

Table 2. Changes in business expenditures for new plant and equipment, 1951 to 1952

<table>
<thead>
<tr>
<th>Industry</th>
<th>Percentage change, 1951 to 1952</th>
</tr>
</thead>
<tbody>
<tr>
<td>All industries: total</td>
<td>+2.0</td>
</tr>
<tr>
<td>Selected manufacturing industries:</td>
<td></td>
</tr>
<tr>
<td>Primary iron and steel</td>
<td>+28.9</td>
</tr>
<tr>
<td>Primary nonferrous metals</td>
<td>+81.2</td>
</tr>
<tr>
<td>Electrical machinery and equipment</td>
<td>+8.4</td>
</tr>
<tr>
<td>Machinery except electrical</td>
<td>+13.0</td>
</tr>
<tr>
<td>Motor vehicles and equipment</td>
<td>+10.1</td>
</tr>
<tr>
<td>Transportation equipment excluding motor vehicles</td>
<td>+17.6</td>
</tr>
<tr>
<td>Chemicals and allied products</td>
<td>+47.5</td>
</tr>
<tr>
<td>Petroleum and coal products</td>
<td>+23.8</td>
</tr>
<tr>
<td>Public utilities</td>
<td>+2.7</td>
</tr>
</tbody>
</table>

Sources: Department of Commerce and Securities and Exchange Commission.

One of the important factors influencing the heavy investment program in 1952 was the Government’s policy of allowing accelerated tax amortization for defense or defense-supporting types of investment. Since Korea, investment programs amounting to 25 billion dollars have been aided in this manner, about 60 percent of this total being subject to accelerated amortization for tax purposes. It is estimated that during 1952 approximately 10 billion dollars in facilities were put in place under this program. Table 2 lists industries showing the most significant increases in plant and equipment expenditures.

As 1952 drew to a close, most industries increased investment expenditures, and civilian industries increased their relative share in the total. A few of the defense-supporting industries cut back moderately, reflecting the substantial expansion accomplished since 1950. The combination of increased allotments, immediate or prospective, of metals for less essential uses and the beginning of a decline in accelerated amortization-type investments was partly responsible for this changing pattern.

Business financing. Business borrowing from commercial banks expanded about 1.8 billion dollars or 7 percent during 1952, compared with 4 billion or 18 percent during the previous year. A breakdown by half-years reveals that business loans increased 1.7 billion dollars during the first half of 1951, but declined 0.6 billion during the first half of 1952. During the second half of each year, which includes the period of seasonal expansion, business borrowing rose—but somewhat more rapidly in 1952 than in 1951. (See appendix table B-28.)

The contraseasonal rise of commercial and industrial loans in the first 6 months of 1951 was in large measure due to the build-up of inventories. The somewhat greater expansion in the second half of 1952 than in
The increase in business investment during the second half of 1952 was due largely to a rise in the rate of inventory accumulation. Expenditures for producers' durable equipment were at record levels for the year as a whole.

The previous year reflected the higher rate of inventory building and the increased tempo of consumer buying. Loans to wholesalers and retailers were greater than in the comparable period of 1951, and borrowing by manufacturers of textiles declined slightly compared to the very sharp drop the year before. Sales finance companies, which had reduced their bank debt in 1951, increased it substantially in the second half of 1952. On the other hand, there was a sharp falling off in the rate of increase in loans to manufacturers of metals and metal products and the public utility and transportation industries—activities generally considered to be defense-related.

Corporations increased bank loans in 1952 at a much less rapid rate than in the previous year, but they floated a record volume of new securi-
ties. Outstanding bank loans and mortgages of corporations increased 1.5 billion dollars in 1952 compared with 5 billion in 1951, while net new security issues, which totaled 7 billion dollars in 1952, exceeded the previous high reached the year before by 9 percent. The relatively greater importance of long-term external financing last year reflected the fact that corporate outlays for plant and equipment were also running at a new high, while net investment in inventories was negligible in contrast with inventory expansion of more than 10 billion dollars in 1951. The total volume of corporate funds available from retained earnings and depreciation allowances was about the same in both years. (See appendix tables B–11 and B–39 and chart 17.)

CHART 17

SOURCES AND USES OF CORPORATE FUNDS

Internal sources of corporate funds totaled about the same in 1952 as in 1951, while funds from external sources were considerably less. The large decline in corporate inventory accumulation was the greatest change in uses of funds.

$\text{BILLIONS OF DOLLARS}$

<table>
<thead>
<tr>
<th>SOURCES</th>
<th>1951</th>
<th>1952</th>
</tr>
</thead>
<tbody>
<tr>
<td>RETAINED EARNINGS</td>
<td></td>
<td></td>
</tr>
<tr>
<td>DEPRECIATION RESERVES</td>
<td></td>
<td></td>
</tr>
<tr>
<td>OTHER SOURCES (EXTERNAL)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>USES</th>
<th>1951</th>
<th>1952</th>
</tr>
</thead>
<tbody>
<tr>
<td>PLANT AND EQUIPMENT OUTLAYS</td>
<td></td>
<td></td>
</tr>
<tr>
<td>CHANGE IN INVENTORIES</td>
<td></td>
<td></td>
</tr>
<tr>
<td>OTHER USES</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

\*PROFITS ESTIMATES FOR THIRD AND FOURTH QUARTERS 1952 BY COUNCIL OF ECONOMIC ADVISERS.

NOTE: EXCLUDES FINANCIAL CORPORATIONS.

SOURCE: DEPARTMENT OF COMMERCE ESTIMATES BASED ON SECURITIES AND EXCHANGE COMMISSION AND OTHER FINANCIAL DATA (EXCEPT AS NOTED).
Developments in selected industries. The improvement in the level of business activity, although fairly general, was especially noteworthy in some industries. Table 3 compares the sales of a few of these industries with total business sales.

Table 3. Retail sales, total and selected groups

<table>
<thead>
<tr>
<th>Period</th>
<th>Total retail sales</th>
<th>Motor vehicle and other automotive dealers</th>
<th>Household appliance and radio stores</th>
<th>Apparel stores</th>
</tr>
</thead>
<tbody>
<tr>
<td>1952: January</td>
<td>13,154</td>
<td>1,968</td>
<td>310</td>
<td>871</td>
</tr>
<tr>
<td>February</td>
<td>13,406</td>
<td>2,147</td>
<td>310</td>
<td>830</td>
</tr>
<tr>
<td>March</td>
<td>13,020</td>
<td>1,928</td>
<td>291</td>
<td>823</td>
</tr>
<tr>
<td>April</td>
<td>13,345</td>
<td>2,148</td>
<td>274</td>
<td>844</td>
</tr>
<tr>
<td>May</td>
<td>13,338</td>
<td>2,505</td>
<td>294</td>
<td>848</td>
</tr>
<tr>
<td>June</td>
<td>14,000</td>
<td>2,407</td>
<td>318</td>
<td>910</td>
</tr>
<tr>
<td>July</td>
<td>13,648</td>
<td>2,302</td>
<td>308</td>
<td>876</td>
</tr>
<tr>
<td>August</td>
<td>13,543</td>
<td>1,758</td>
<td>297</td>
<td>889</td>
</tr>
<tr>
<td>September</td>
<td>13,538</td>
<td>2,129</td>
<td>310</td>
<td>865</td>
</tr>
<tr>
<td>October</td>
<td>14,157</td>
<td>2,404</td>
<td>304</td>
<td>925</td>
</tr>
<tr>
<td>November</td>
<td>13,991</td>
<td>2,444</td>
<td>315</td>
<td>870</td>
</tr>
</tbody>
</table>

1 Estimates based on incomplete data.
Source: Department of Commerce.

The first half of 1952 found the textile industry still in the doldrums. Just before midyear, a gradual improvement set in and it continued throughout the rest of 1952. Retail inventories of apparel, and in turn producers’ inventories of textiles, had been reduced throughout the latter part of 1951 and early 1952, and some retailers and textile product manufacturers found themselves understocked as sales began to rise.

Prices, production, and employment in the industry responded to the increase in sales. On the other hand, a sizable cotton crop, sharply reduced exports of cotton, large capacity for producing rayon, and the absence of large-scale military buying of wool kept raw material prices from rising. The end of 1952 found the textile industry in a much improved position.

The automotive industry also showed fluctuation of considerable magnitude during the year. Reduced from the peaks of late 1950 and early 1951 by materials restrictions, credit controls, and moderate consumer demand, automotive production and sales in the early part of 1952 were at good but not record levels. Producers took advantage of available price increases to advance average prices about 5 percent. While buyers accepted these increases during the spring, there were some fears of market softening until the steel strike cut sharply into production. Production fell from 394,000 cars in May of 1952 to 160,000 in July, and as a result inventories and sales of cars at the distributor level fell off.

The comeback was equally rapid. By September, production reached 441,000 cars, retail sales were increasing rapidly, automakers were pressing for greater allotments of metals, and looking forward to further improvement in sales throughout 1953. During the second half of 1952, they did not apply for further ceiling price increases which were available under
price control standards, and in some instances they reduced slightly the prices of 1953 models.

_Agricultural_ output for 1952 is estimated at a record level, 44 percent above the 1935-39 average and 3½ percent larger than in 1951. (See appendix table B-17.) Production records were realized despite drought in large areas and a shrinking farm labor force. Indicated food production was up 4 percent from 1951, a large part of this gain being due to the big wheat crop, some of which went into reserve stocks. Cattle marketings rose substantially in the latter part of the year.

With the large volume of marketings, prices received by farmers in 1952 averaged almost 5 percent lower than in 1951, with rather marked declines in the latter part of the year. For 1952 as a whole, lower average prices for livestock products were only partly offset by slightly higher average prices for crops. Prices paid by farmers averaged about 2 percent above the level of 1951 and, with the reduction in prices received for their products, the parity ratio dropped from 107 percent in 1951 to 101 percent for 1952 as a whole. In December, the ratio was 96. (See appendix table B-25.)

_Government_

The flow of goods and services to the government sector of the economy was almost one-fourth higher in 1952 than in 1951. This flow accounted for 22 percent of the gross national product in 1952, compared with 19 percent in 1951 and 14 percent in the period immediately preceding the Korean outbreak. More than four-fifths of the increase in governmental purchases in 1952 was attributable to the major national security programs. The next largest increase was in purchases of goods and services by State and local governments. (See appendix table B-1.)

Governmental cash revenues also increased in 1952, in absolute amounts and in relation to the gross national product. However, for the Federal Government as well as the State and local governments, the rise in receipts fell somewhat short of the advance in expenditures. The cash deficit for all governmental units combined was 3.1 billion dollars, divided about equally between the Federal Government and State-local governments. (See chart 18 and appendix table B-33.)

_Federal fiscal operations._ The results of Federal fiscal operations, as shown in the conventional budget, are summarized in table 4. Expenditures totaled 71.4 billion dollars in the calendar year 1952, and receipts 65.5 billion. The budget deficit of 5.8 billion dollars compares with a deficit of 3.4 billion in 1951. The sources of financing the deficit are indicated in table 4.

The public debt expanded from 259.4 billion dollars at the end of 1951 to 267.4 billion at the close of last year. Almost half of the increase of 8.0 billion dollars in public debt issues was taken up by the Government investment accounts which held 45.9 billion dollars of Federal securities at the year-end. (See appendix table B-30.)
In 1952, cash payments rose more than cash receipts, resulting in small cash deficits for both the Federal and the State and local governments.

**Sources:** Treasury Department, Department of Commerce, and Council of Economic Advisers.
The impact of Federal fiscal operations on the current flow of private income and purchasing power is shown more clearly when the conventional budget accounts are adjusted to a consolidated cash basis. Two broad types of adjustments are involved: first, the elimination of noncash transactions, such as interest accruals on outstanding U. S. savings bonds, interest on securities held by the trust accounts, and transfers to the trust accounts; and second, the merging of the budget accounts with the trust and miscellaneous accounts. The result of these adjustments is a consolidated statement of all cash receipts from and payments to the public, apart from sales and redemptions of Government securities. (See appendix tables A-6 and A-7 for a statistical reconciliation of the conventional budget and consolidated cash figures.)

As shown in table 5, both receipts and expenditures are higher on a cash than on a budget basis. The difference, however, is considerably larger in the case of receipts, chiefly because the substantial tax collections for the social security funds are much in excess of expenditures therefrom. The cash deficit of the Federal Government was 1.6 billion dollars in 1952, or 4.2 billion less than the deficit in the conventional budget. There were cash surpluses in both 1950 and 1951, although the conventional budget showed deficits during these years.

*Expenditures for national security.* The major national security programs (including military services, international security and foreign rela-
### Table 5. Federal receipts and expenditures: Conventional budget and consolidated cash statement

<table>
<thead>
<tr>
<th>Accounting basis</th>
<th>Calendar year 1950</th>
<th>Calendar year 1951</th>
<th>Calendar year 1952</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Total 1</td>
</tr>
<tr>
<td>Conventional budget:</td>
<td></td>
<td></td>
<td>First half</td>
</tr>
<tr>
<td>Receipts</td>
<td>37.8</td>
<td>53.5</td>
<td>65.5</td>
</tr>
<tr>
<td>Expenditures</td>
<td>38.3</td>
<td>56.8</td>
<td>71.4</td>
</tr>
<tr>
<td>Surplus or deficit (—)</td>
<td>—.4</td>
<td>—3.4</td>
<td>—5.8</td>
</tr>
<tr>
<td>Consolidated cash statement:</td>
<td></td>
<td></td>
<td>Second half 1</td>
</tr>
<tr>
<td>Receipts</td>
<td>42.4</td>
<td>59.3</td>
<td>71.4</td>
</tr>
<tr>
<td>Expenditures</td>
<td>42.0</td>
<td>58.0</td>
<td>72.0</td>
</tr>
<tr>
<td>Cash surplus or deficit (—)</td>
<td>.4</td>
<td>1.2</td>
<td>—1.6</td>
</tr>
</tbody>
</table>

1 Estimates based on incomplete data.

Note.—Detail will not necessarily add to totals because of rounding. Source: Treasury Department.

### Table 6. Federal budget expenditures by major classes

<table>
<thead>
<tr>
<th>Expenditure class</th>
<th>Calendar year 1950</th>
<th>Calendar year 1951</th>
<th>Calendar year 1952</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Total 1</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>First half</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Second half 1</td>
</tr>
<tr>
<td>Total expenditures</td>
<td>38.3</td>
<td>56.8</td>
<td>71.4</td>
</tr>
<tr>
<td>Major national security programs</td>
<td>18.5</td>
<td>37.1</td>
<td>51.0</td>
</tr>
<tr>
<td>Department of Defense, military functions 1</td>
<td>13.3</td>
<td>31.0</td>
<td>45.1</td>
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<tr>
<td>International security and foreign relations 1</td>
<td>4.0</td>
<td>3.5</td>
<td>5.0</td>
</tr>
<tr>
<td>Stockpiling of materials</td>
<td>.6</td>
<td>1.3</td>
<td>1.8</td>
</tr>
<tr>
<td>Other national security 4</td>
<td>.5</td>
<td>.5</td>
<td>.5</td>
</tr>
<tr>
<td>Veterans' Administration</td>
<td>5.8</td>
<td>5.2</td>
<td>4.6</td>
</tr>
<tr>
<td>Interest on public debt</td>
<td>5.6</td>
<td>6.0</td>
<td>6.1</td>
</tr>
<tr>
<td>All other</td>
<td>8.4</td>
<td>8.6</td>
<td>9.8</td>
</tr>
</tbody>
</table>

1 Estimates based on incomplete data.

Note.—Detail will not necessarily add to totals because of rounding. Source: Daily Treasury Statement, Treasury Department.
Other budget expenditures. Veterans benefits were somewhat lower in 1952 than a year earlier. On the other hand, interest on the public debt was slightly higher. The increase in expenditures of the Commodity Credit Corporation accounted for about half the rise in the “all other” classification shown in the table.

![FEDERAL BUDGET EXPENDITURES](chart19.png)

Budget receipts. The advance in budget receipts in calendar year 1952 was due to the over-all expansion of business activity and the tax legislation enacted in 1950 and 1951. (See table 7.) Each of the major sources of tax revenue was affected by the legislation. The increased withholding rates for the individual income tax under the Revenue Act of 1951 became effective in November 1951, as did the excise tax changes made by that Act. In the case of corporate taxes, the full increase imposed by the 1951 Act will not be reflected in receipts until March 1953, when most corporations will make their first tax payments on their profits for 1952. Corporate tax payments during 1952 were based for the most part on profits and tax rates in 1951.

Because of the 1951 rate increases for the individual income tax, and the rise in incomes, the percentage of personal income withdrawn by direct Federal taxes on individuals rose to 11.4 percent in 1952, according to the
TABLE 7. Federal budget receipts by source

<table>
<thead>
<tr>
<th>Source</th>
<th>Calendar year 1950</th>
<th>Calendar year 1951</th>
<th>Calendar year 1952</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net receipts</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Direct taxes on individuals</td>
<td>17.5</td>
<td>28.4</td>
<td>30.5</td>
</tr>
<tr>
<td>Direct taxes on corporations</td>
<td>9.5</td>
<td>16.3</td>
<td>21.9</td>
</tr>
<tr>
<td>Excise taxes</td>
<td>8.1</td>
<td>8.6</td>
<td>9.6</td>
</tr>
<tr>
<td>Customs</td>
<td>.5</td>
<td>.6</td>
<td>.6</td>
</tr>
<tr>
<td>Other</td>
<td>2.2</td>
<td>2.7</td>
<td>2.9</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>53.5</strong></td>
<td><strong>57.5</strong></td>
<td><strong>65.5</strong></td>
</tr>
<tr>
<td><strong>First half</strong></td>
<td><strong>38.3</strong></td>
<td><strong>43.5</strong></td>
<td><strong>53.5</strong></td>
</tr>
<tr>
<td><strong>Second half</strong></td>
<td><strong>27.2</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

1 Estimates based on incomplete data.
2 Gross receipts less appropriations to the Federal Old-Age and Survivors Insurance Trust Fund and re-funds of receipts.
3 Individual income taxes and estate and gift taxes.

NOTE.—Detail will not necessarily add to totals because of rounding.
Sources: Treasury Department and Bureau of the Budget.

national income accounts. The percentage was 10.0 percent the year before; in the first half of 1950, it was 8.4 percent. Although the proportion of total personal income left after payments of direct taxes declined during this period, the dollar amount moved steadily upward.

Corporate taxes became relatively more important as a source of Federal revenue in 1952. They accounted for 33.4 percent of budget receipts last year, compared with 25 percent in 1950. This shift is the combined result of the tax legislation, including the imposition of the excess profits tax in 1950, and the response of corporate profits to changes in general business activity. Federal corporate tax liabilities, as distinguished from corporate tax payments, were 56 percent of profits before tax in 1952; in 1949, when the pre-Korea rates applied, they were 38 percent.

TABLE 8. Government cash receipts from and payments to the public

<table>
<thead>
<tr>
<th>Receipts or payments</th>
<th>Calendar year 1950</th>
<th>Calendar year 1951</th>
<th>Calendar year 1952</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total government:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash receipts</td>
<td>60.8</td>
<td>78.9</td>
<td>92.3</td>
</tr>
<tr>
<td>Cash payments</td>
<td>61.4</td>
<td>78.7</td>
<td>93.4</td>
</tr>
<tr>
<td>Total cash surplus or deficit (—)</td>
<td>-.6</td>
<td>.2</td>
<td>-3.1</td>
</tr>
<tr>
<td>Federal Government:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash receipts</td>
<td>42.4</td>
<td>59.3</td>
<td>71.4</td>
</tr>
<tr>
<td>Cash payments</td>
<td>42.0</td>
<td>58.0</td>
<td>73.0</td>
</tr>
<tr>
<td>Federal cash surplus or deficit (—)</td>
<td>.4</td>
<td>1.2</td>
<td>-1.6</td>
</tr>
<tr>
<td>State and local governments:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash receipts</td>
<td>18.4</td>
<td>19.7</td>
<td>20.9</td>
</tr>
<tr>
<td>Cash payments</td>
<td>19.4</td>
<td>20.7</td>
<td>22.4</td>
</tr>
<tr>
<td>State and local cash surplus or deficit (—)</td>
<td>-1.0</td>
<td>-1.0</td>
<td>-1.5</td>
</tr>
</tbody>
</table>

1 Estimates based on incomplete data.
2 Federal grants-in-aid have been deducted from State and local government receipts and payments since they are included in Federal payments.

NOTE.—Detail will not necessarily add to totals because of rounding.
Sources: Treasury Department, Department of Commerce, and Council of Economic Advisers. (See appendix tables A-5 and B-33.)

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State and local finances. Cash payments by State and local governments have exceeded cash receipts by a small margin in each year since 1948. (See chart 18.) The excess of payments is estimated at 1.5 billion dollars in 1952, compared to 1.0 billion in 1951. These data are given in table 8.

Revenues have more than kept pace with the rise in operating expenses in recent years, but increasing amounts have been required for capital outlays by State and local governments. Expenditures for new construction, primarily highways and public schools, were 6.6 billion dollars in 1952.

Outstanding debt of these governments amounted to 29.6 billion dollars on June 30, 1952, having increased by 2.6 billion during the previous 12 months. Because of the relatively low interest rates of the past decade, the annual interest on this debt was no higher in 1952 than in 1942, even though the amount of State and local government debt outstanding rose by about 50 percent in this period.

Public debt operations. In addition to a net increase during 1952 of 3.3 billion dollars in special issues for U. S. Government investment accounts, the volume of new borrowing by the Treasury from the public was considerably larger than in other postwar years. (See appendix table B-31.) Some of the new financing was used to repay holders of issues that were redeemed and of that portion of matured issues which was not exchanged for other Government obligations; some was used to augment the General Fund balance, which rose by 1.8 billion dollars during the year, and some of it went to meet the cash deficit of the second half of 1952. The combined effect of sales to the investment accounts and to outsider buyers was to increase the total public debt to 267 billion dollars at the end of 1952. This represented an increase of 8 billion dollars for the calendar year, compared with an increase of 2.7 billion in 1951.

New marketable securities offered to the public were short- or medium-term maturities. Several increases in the weekly offerings of 3-month Treasury bills lifted the outstanding volume from an average of 15.6 billion dollars in January 1952 to 17.2 billion in December. In June, the Treasury accepted bids in the amount of 4.2 billion dollars for a heavily oversubscribed issue of 2¾ percent 6-year bonds, and in October and November it sold two series of tax anticipation bills, totaling 4.5 billion, one to mature in March 1953 and the other the following June.

Securities of the last-named kind are useful in meeting the problem arising from the unequal seasonal flow of Treasury receipts, which generally run much higher in the first half of the calendar year than in the second half. This imbalance has been accentuated by the plan under which an increasingly large percent of corporate taxes on the earnings of the preceding year must be paid in March and June.

As for nonmarketable securities, which with few exceptions may be purchased only by investors other than banks, the Treasury offered in May,
partly for cash subscription, long-term nonmarketable bonds of the series first issued in the spring of 1951. In May and June, furthermore, extensive changes were made in the types and terms of U. S. savings bonds with the intention of making them more attractive to the individual investors, for whom they are especially designed.

There was, after some easing early in 1952, an upward trend in yields on short-term Government securities. This became quite pronounced in the closing months, the average yield on new issues of 3-month Treasury bills being 1.92 percent in the fourth quarter of 1952 compared with 1.65 percent a year earlier. (See appendix table B–32.)

International developments

United States exports. United States total merchandise exports dropped sharply during the middle of 1952, and in the second half were below the rate of both preceding half years. (See appendix table B–43.) Exports of United States goods, excluding Department of Defense shipments financed by the Mutual Security Program, declined even more sharply than total exports. (See chart 20.) From a monthly average of about 1.2 billion dollars both in the second half of 1951 and in the first half of 1952, domestic exports, exclusive of military aid items, declined to a monthly average of about 1 billion dollars. This drop of nearly 17 percent was almost entirely one of quantity, with export prices remaining practically unchanged. (See appendix table B–44.) Only exports of manufactured goods maintained their 1951 level in the second half of 1952; exports of crude foodstuffs and raw materials declined sharply. Geographically, the decline was widespread, but commodity exports to Western Europe, the sterling area, Argentina, and Brazil suffered the largest decreases. (See appendix tables B–41 and B–43.)

The drop in the volume of United States exports in the second half of 1952 is traceable to a variety of factors. Among the most important was the decline in United States commodity imports between March and September 1951, to a level more than 25 percent below the peak reached briefly in the first quarter. From the fourth quarter of 1951 to the third quarter of 1952, imports fluctuated on a level moderately above the 1951 low. The resultant decline in the dollar earnings of foreign countries, occurring as it did while their expenditures in the United States remained at record heights, contributed to an eventual drop in United States exports. The export surplus of the United States in the second half of 1951, only partially counterbalanced by foreign aid, caused some foreign countries to lose gold to this country and to draw more heavily on their dollar holdings.

In its Midyear 1952 Review, the Council described the developments abroad which had accounted for the size of our export surplus and the imposition by other countries during the period since mid-1950 of increased import restrictions and anti-inflationary policies. Briefly, the payments balances of many industrialized countries, especially in Western Europe, had de-
teriorated because of rapid accumulation of inventories of imported goods after June 1950, and a lag in the rise of their export prices relative to import prices. At later dates, many raw material producing countries also suffered balance of payments problems when the declining rate of inventory accumulation in the United States caused their exports to fall, while their imports, swollen because of high internal incomes and demand, remained high. In late 1951 and early in 1952, the United Kingdom, many other members of the sterling area, France, and certain South American countries imposed sharp important restrictions and adopted anti-inflationary policies to correct balance of payments deficits and to stop losses of reserves.

The decline in the gold and dollar reserves of the sterling area, which had started in mid-1951, was halted after the first quarter of 1952. By the fourth quarter of 1952, the area as a whole was earning gold and dollars from the European Payments Union which approximately balanced its deficit with the dollar area. The improvement in the international position of the sterling area in the second half of the past year resulted from the previously imposed import restrictions, the decision in many instances to draw on existing stocks of imported commodities, and restraint on internal demand by credit and fiscal policies.

From a high of 730 million dollars in the fourth quarter of 1951, United States exports (exclusive of "special category items") to the sterling area declined to 313 million in the third quarter of 1952. This drop of nearly 60 percent may, of course, have involved some seasonal factors. United States exports to the United Kingdom alone declined from 299 million dollars to 117 million. The improvement in the United Kingdom’s balance of payments occurred despite a decline in total United Kingdom exports, reflecting import restrictions imposed by the rest of the sterling area and other countries. Exports by the United Kingdom to the United States, however, were as high in the second and third quarters of 1952 as they had been in the first half of 1951.

United States exports to other Western European countries together similarly declined from a seasonal high of nearly 900 million dollars in the fourth quarter of 1951 to about 500 million in the third quarter of 1952, a drop of about 45 percent. Exports to continental Western Europe, like exports to the United Kingdom and the entire sterling area, fell off sharply in the second half of 1952, because of increased import restrictions imposed by certain countries; because of increased availability of certain commodities, especially agricultural goods and coal, from domestic and nondollar sources; because of the existence of sizable stocks of imported goods in many countries; and because of a lower level of demand for consumers’ goods, especially textiles. This last development was the foreign counterpart to the softness in certain consumer goods industries in this country.

United States commodity exports to countries in the Western Hemisphere in the aggregate remained at about their 1951 level during the
After mid-1952, the U.S. merchandise export surplus fell sharply. The increasing volume of shipments of grant-aid military equipment failed to offset the drop in the volume of other exports. Merchandise imports averaged somewhat lower than during the first half of the year.

In 1952, for the first time since 1945, industrial production in Western Europe failed to rise above the previous year, as chart 21 indicates. The failure of industrial output to rise was not all loss; the breathing spell in this rapid advance was accompanied by significant gains. It appears that the reaction to the post-Korean buying spree has about completed its course, thus permitting a continuation of post-World War II economic growth on a more stable foundation. The year 1952 represents a period of consolidation and internal industrial adjustments, in contrast to the rapid expansion which characterized the earlier phases of the post-Korean boom. The inflation suffered by many Western European countries after
June 1950 injected considerable distortion into their economies—especially in their external position—which required much subsequent correction.

The serious inflation that developed in France, for example, tended to divert production from exports to domestic markets. In other Western European countries, the previous rapid expansion in the output of consumers' goods had made more difficult a shift of resources to defense output. Thus, the decline in demand for soft goods, which developed in mid-1951 while the output of the machinery, coal, steel, electric power, and defense industries was rising, has aided in facilitating these adjustments.

Wholesale prices were generally lower at the end of 1952 than at the beginning of the year. Cost-of-living indexes either remained the same or moved somewhat higher. (See appendix table B–26.) Unemployment, while higher during the first half of 1952 than during previous years, was of significant size only in Italy, Germany, and Belgium. In Germany, unemployment at the end of 1952 was the lowest in the postwar period and was ceasing to be a serious economic problem.

United States imports. United States commodity imports in the second half of 1952 were slightly higher in value than those in the second half of
1951 after the sharp decline had occurred. (See appendix table B-45.) The relative constancy in the value of imports, however, conceals the substantial recovery in volume that has meanwhile occurred. The index of import unit values (1936-38=100) has declined from 299 in the fourth quarter of 1951 to 280 in the same quarter of 1952, while the quantity index has risen from 136 to 154 (1936-38=100). (See appendix table B-46.) The lower level of commodity prices throughout the world is responsible for some of the increases in volume of imports, for when prices were at their peak in early 1951 price ceilings in this country served to keep United States prices below those elsewhere, and thereby to discourage imports of some commodities into the United States. The higher level of imports in 1952, however, can also be accounted for in part by the previous working off of inventories of imported goods which had been accumulated earlier.

The relative constancy of aggregate foreign dollar earnings from commodity sales in the United States between the second half of 1951 and of 1952 was not shared by all areas. United States imports from Latin America were substantially higher in value than in the previous period. The value of imports from a few countries, including Japan, Italy, and the Netherlands increased somewhat, but lower imports from some other areas offset these rises.

Other means of financing exports. The level of foreign economic and defense-support aid was slightly lower in 1952 than in the previous year, since a substantial rise in military aid did not counterbalance the decline in economic aid. (See appendix table B-42.) United States Government purchases of goods and services abroad, largely in Western Europe and Japan, continued to play an increasingly important role in financing United States exports. Direct investment of United States capital abroad reached the record amount of 560 million dollars in the first half of 1952, almost equal to the entire outflow of the previous year. Total net outflow of private capital was smaller in 1952 than in 1951, however, chiefly because of sales of Canadian securities by United States residents in the last half of the year. Again in 1952 the largest part of private investment abroad occurred in Canada and Latin America, but the capital outflow to countries in Africa, the Near East, and Far East increased somewhat.

In the first quarter of 1952, the size of the export surplus of goods and services forced foreign countries to sell gold and draw on dollar balances in order to cover their dollar payments; in the latter part of the year this situation was reversed. With a considerable reduction in the export surplus, other dollar receipts proved sufficiently large to enable foreign countries as a whole to accumulate gold and dollars. (See appendix table B-40.)
Chapter II. Near-Term Prospects and Policies

The Outlook

A year ago, the official estimates of the prospective pace of defense expenditures were higher than the developments which actually followed. This led the Council and other business observers to expect somewhat stronger inflationary pressures and civilian shortages in 1952 than in fact developed. By midyear 1952, the Council’s reexamination of short-run prospects led to a modification of its earlier view in the light of the revised mobilization program. At that point, the Council foresaw a 12-month period not likely to differ markedly from the period of high-level stability which had preceded it for a year and a quarter. It seemed that production and incomes were apt to keep rising and unemployment to stay low, without substantially augmenting inflationary pressures. But the Council stated that there might be a shift, in the event of incalculable changes in inventory investment and consumer buying—for which funds were ample—which might for a time accentuate the risk of inflation. Moreover, it appeared that, at some point beyond the short-run outlook as then defined, new demands might be necessary to protect the economy from deflationary dangers.

In broad outline, this general approach is still applicable for the months now ahead. The principal change thus far has already been underscored in the discussion of 1952. It is the relative shift in emphasis from rising public to rising private demand, reflected in the volume of consumer and inventory buying in the final quarters of 1952, accompanied by the absence of a significant rise in defense spending during recent months. Before evaluating to what extent this shift may continue, and the significance thereof, it is desirable to examine the components in some detail.

Government expenditures and the fiscal outlook

In 1953, as in the 2 preceding years, the course of national security expenditures constitutes the best starting point for an analysis of prospective developments. Under the present national security program, expenditures are expected to rise gradually during most of this calendar year, and thereafter to level off on a plateau which will carry well into next year. While most of the growth in this sector of demand has already occurred, the annual rate of expenditures in the fourth quarter of 1953 may be 4 or 5 billion dollars higher than in the fourth quarter of 1952.
Government outlays at State and local levels probably will continue to increase slowly, as defense-related restraints diminish and the pressure to meet long-term developmental needs grows stronger. Some recent surveys of State and local government spending plans indicate increases in 1953 of from 1 to 2 billion dollars over the 1952 level of 23.3 billion.

The fiscal outlook is for a moderately larger Federal deficit in 1953 than in the calendar year just closed. The Budget of the President estimates a Federal deficit of about 2 billion dollars on a consolidated cash basis in the fiscal year which ends June 30, 1953; it indicates a cash deficit of 6.6 billion dollars in the succeeding fiscal year. If the post-Korea tax increases are not allowed to run off as provided by present law, the cash deficit in fiscal 1954 would be about 2 billion lower. The State-local deficit has ranged between 1 and 2 billion dollars a year in the recent period, and will probably continue at that level in calendar 1953.

Private domestic investment

There are strong indications that, taken as a whole, private expenditures for new fixed capital assets will hold up to the very high 1952 level during all or most of 1953. In the case of plant and equipment outlays, while most of the private projects "programmed" under the Government's industrial expansion effort had been approved and more than half put in place by the first of this year, the expansion in many "nonprogrammed" areas probably will prevent any significant weakening in the total this year. This follows from the recent survey of business investment intentions for 1953 made by the Commerce Department and the Securities and Exchange Commission, just reported in detail in the Commerce Department's study of "Markets After the Defense Expansion," and summarized in table 9.

<table>
<thead>
<tr>
<th>Industry</th>
<th>1951</th>
<th>1952 ¹</th>
<th>1953 ¹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total expenditures</td>
<td>26,332</td>
<td>26,860</td>
<td>26,271</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>11,130</td>
<td>12,432</td>
<td>11,907</td>
</tr>
<tr>
<td>Durable goods</td>
<td>6,166</td>
<td>5,589</td>
<td>5,338</td>
</tr>
<tr>
<td>Nondurable goods</td>
<td>5,962</td>
<td>6,883</td>
<td>6,582</td>
</tr>
<tr>
<td>Mining</td>
<td>911</td>
<td>859</td>
<td>871</td>
</tr>
<tr>
<td>Transportation</td>
<td>2,966</td>
<td>2,792</td>
<td>2,504</td>
</tr>
<tr>
<td>Public utilities</td>
<td>3,855</td>
<td>3,961</td>
<td>4,017</td>
</tr>
<tr>
<td>Commercial and other ¹</td>
<td>7,479</td>
<td>6,804</td>
<td>6,972</td>
</tr>
</tbody>
</table>

¹ Estimates for the fourth quarter of 1952 and for 1953 are based on anticipated capital expenditures as reported by business in October and November 1952.
² Includes trade, service, finance, communication, and construction.

The same survey indicates that commercial and recreational construction, much of which up to now has been held back by materials controls,
should rise in 1953. In housing, the removal of credit restrictions last fall, together with rising incomes, seems likely to keep 1953 starts fairly close to the 1952 figure of 1.1 million.

Inventory accumulation, as already has been emphasized, will play an unpredictable role in the months ahead. An acceleration of the rates of inventory-building estimated to have occurred in the last 2 quarters could lead to some pressures on prices. Excessive stocks could, in turn, lead to a reversal of the inventory movement later in the year.

**Net foreign investment**

If United States imports and private investment abroad in 1953 follow the trends of 1952, and if Government expenditures for foreign aid conform to the pattern now in prospect, foreign countries will be able to continue rebuilding their depleted dollar reserves, and perhaps even to relax somewhat their import restrictions. However, assuming no change in United States international economic policies, it seems unlikely that the dollar positions of foreign nations will permit United States exports to rise greatly from present levels before the end of 1953. Agricultural exports during 1952-53 will be down substantially from the record levels of the crop year 1951-52. A general increase in foreign output of farm products is largely responsible for the reduced foreign demand for United States farm products.

**Personal income and consumption**

Personal income will probably rise in 1953 at a more moderate rate than in the last half of 1952. Wage rates can be expected to increase under present and prospective high levels of employment. Business earnings should exceed the levels of 1952. The income of farm operators, which decreased moderately in 1952, threatens to decline further in the absence of countervailing policies, as a result of rising costs and somewhat lower farm prices.

Spendable income will not increase as much as personal income, under present tax rates, because personal taxes and other types of taxes will absorb part of the income increases. Nevertheless, moderate gains in consumption expenditures are likely, since there is no reason to forecast an early increase in the rate of personal saving.

Expenditures on services should continue to mount. In addition to the effect of income changes, prices are still rising in this area, and the rapid rate of new home construction requires expansion of all types of utilities.

The demand for automobiles may exceed total sales in 1952, and lead to a further increase in instalment debt. If prewar patterns are followed, many persons who bought a new car in the peak years of 1949 and 1950 will again be in the new-car market in 1953.

**Supplies**

In general, the condition of supply, which proved ample along with restraining measures to prevent inflationary trends during 1952, should certainly continue in 1953. In fact, the productive power as well as the actual
product of the economy now are considerably higher than a year ago, and these sources of basic strength can and should be augmented in the year ahead. If high-level employment is maintained, we are now clearly in position to lift the total output of the economy by far more than the increase in the defense take, and by sufficient amount to meet moderately rising demands in other sectors of the economy. In fact, these moderately rising demands are likely to occur only if high employment is maintained and production thus increased.

Turning to more specialized supply problems, although some effects of the steel strike are still being felt, the outlook for steel supplies for civilian users is generally optimistic. Because of the increase in capacity, and the leveling off of military requirements, manufacturers of civilian-type products will receive during the second quarter of 1953 allotments higher than any yet granted under the Controlled Materials Plan. However, steel plate, heavy structural shapes, tubular products, and certain other items are expected to remain relatively scarce for a somewhat longer period.

Despite the rapid increase in aluminum capacity since Korea, domestic supplies increased less than expected this autumn as a result of power

CHART 22

EXPANSION IN MAJOR INDUSTRIES

While scheduled capacity expansion in some industries is nearly finished, the programs in other industries are far from complete.

STEEL

EXPANSION GOAL
DEC. 31, 1955

PRESENT CAPACITY

ALUMINUM

DEC. 31, 1954

ELECTRIC POWER

DEC. 31, 1955

SOURCE: OFFICE OF DEFENSE MOBILIZATION.
shortages in the Northwest. Larger imports from Canada have helped ease this situation. The general outlook is for increasingly available supplies for nonmilitary uses, although it should be noted that aluminum capacity in the United States is by no means over-plentiful in terms of either requirements for full mobilization or expanding peacetime civilian usage. (See chart 22.)

Copper appears to be the scarcest of the three basic metals. Fabricators of copper products, however, have recently been rebuilding their inventories. While potential supplies should not fall significantly short of demand for current use during 1953, they are somewhat deficient in terms of stockpiling objectives. Consequently, contemplated second quarter 1953 allotments are only slightly higher than fourth quarter 1952. Taking the longer view, it is expected that military requirements will soon begin to decline modestly, the extent depending heavily not only upon ammunition use in Korea, but also upon how rapidly progress is made in substituting steel for copper in shell cases. The price of imported copper is still above the ceiling price established for domestic supplies, and the outlook for a narrowing of this differential depends upon the rapidity with which supplies improve and upon the foreign suppliers.

The generally optimistic picture for the major metal supplies cannot, of course, be transferred to the much scarcer alloying metals. The heavy military requirements both for current usage and for stockpiling of these scarce alloy metals promises to keep them in tight supply, certainly through the near future. The technology of modern armaments puts a severe drain on these high temperature alloys, and even though the Government's program of increasing the supplies of these metals has borne fruit in most cases, the enlarged production must be channeled into the defense program.

Prices

The general price structure seems now to have readjusted to a reasonably stable condition. Within the structure itself, there are only selective pressures for further realignments of raw material, manufacturers', and distributors' prices. There seem to be no demand developments in early prospect which would force the general level of prices either up or down—unless it were a more sudden shift in inventory accumulation or durables buying by consumers than there now is good reason to expect.

There will be some upward pressures. For one thing, many businesses will face further cost increases. Moreover, in those areas where ceilings are now holding prices below what would be their present "equilibrium" levels if markets were uncontrolled, there would be a tendency for prices to rise if controls were too quickly abandoned. On the other hand, increasing supplies should reduce this risk as the year progresses. And it is quite possible that the tendency toward more competitive pricing now observable in many retail quarters will spread. As more and more new productive capacity comes into operation, supplies are becoming increasingly abundant relative to demand.
The composite near-term outlook

On balance, the economic outlook for the near-term future does not justify at this time any sharp change in the mood of the business community or the consuming public, nor does it justify any sharp change in public policy. The period should witness in the main a mild continuance of the shift toward relatively more emphasis on civilian demand, and relatively less emphasis upon the increase in military demand. Since civilian demand is directed toward sectors of the economy where our productive facilities can meet this demand with less strain than the highly selective demand of military expansion, it should be easier in 1953 than during the past 2 years to hold inflationary pressures in check. This outlook for stability makes it desirable to continue or even speed up the process of sloughing off direct controls.

The question remains whether the increase in civilian demand during 1953 will be sufficient to close the gap between further increases in our general productive power and the less sizable increases in military demand, or whether in the alternative we shall be faced with substantial deflationary trends and corresponding unemployment. For the major portion of the year 1953, the weight of evidence is clear that such a deflationary movement is not in prospect. And there is certainly no reason yet to alter drastically private or public economic policies on a premature assumption that these unfavorable developments will take place toward the end of the year.

The only factors which the Council can now discern which might prevent the late portion of 1953 from being bright would be (1) a prevalent determination early in the year, contrary to the weight of the evidence, that the business outlook for the latter part of the year is gloomy, or (2) sharp departure from private and public policies which as of now have brought us to a position of price stability combined with maximum production and employment. Such unfavorable shifts would be unwarranted, and the Council advises against them. While there are always new problems to be solved, the Council feels that the year 1953 commences with the economy in better shape than at the beginning of any year since our work was started 6 years ago. We are not confronted with the highly ambiguous situation of early 1947, when it was not clear whether the then current inflation would continue or explode in the much-advertized postwar deflation. We are not confronted by the hectic inflationary trends of early 1948, or the disturbing downward movements of early 1949. The throb of economic activity and of confidence are stronger than in early 1950. And our ability to sustain the heavy burden of our new world responsibilities without economic impairment is now clear, although many doubted it in early 1951 and some still doubted it in early 1952.

In taking this fairly firm stand with respect to the near-term future, the Council does not challenge the proposition that a later period will confront us with more difficult tests of our ability to maintain stability and growth.
In subsequent portions of this Review, we shall discuss this longer-range issue, and point out that it is none too early to begin improving our defenses against the forces of deflation. Nor is it too early to note that the sea even now is not entirely placid. The recent trends in the agricultural sector of the economy, and in international economic arrangements, challenge us even now to forestall events fraught with real dangers to be averted later on even though not in the short run.

**Near-Term Policy Issues**

The Council's discussion of near-term policy will focus on three issues: defense mobilization policy, tax policy, and international trade policy. The expiration of basic statutes affecting each of these national policies will compel congressional decision, in the current session, to permit the respective statutes to expire, to renew them, or to replace them with new or modified plans.

**Defense mobilization policy**

Since the Korean outbreak, the Nation's prime production objective has been to build up its defenses and expand its mobilization base. To accomplish this in an orderly fashion and at the same time to maintain stability, it was necessary to increase taxes greatly, to erect a comprehensive structure of controls covering materials, prices, wages, and credit, and to develop additional incentives for the expansion of supply both at home and abroad. It is a tribute to the coordination of public and private efforts that during the past 2 years the Nation has built up its productive and military strength with relatively little strain on the economy, while maintaining a high degree of economic stability. The great resiliency of our productive system has permitted maintenance of a very high and increasing over-all level of consumption. These developments have led during the past year to a progressive relaxation of the controls in those areas where expansion of supply and the absence of excessive demand have permitted.

It would be imprudent to make changes now in economic policies which would be so drastic as to interfere with the continued orderly build-up of our defenses or to upset the balance in the economy. This note of caution is underscored by four basic considerations: (1) the mobilization program under present plans has yet to achieve its peak, and we do not yet know the scope or direction of any change which may be made; (2) the level of private demand is now very high and may increase; (3) the controls program, though in process of contraction, continues to make a positive and major contribution to the orderly flow of materials and to economic stability in important areas; and (4) the international situation continues highly uncertain.

The Defense Production Act expires June 30, 1953, except price, wage, and rent controls, which expire April 30. The improving materials supply will justify further relaxation in controls during the first half of 1953. But it is quite clear that the improvement in the supply of materials will not
be sufficient in all cases to permit the complete termination of controls before the existing powers expire. It will be absolutely essential to have continuing authority for priorities and allocations controls to assure the supply of necessary types of steel, copper, aluminum, and certain other materials for defense production. Under these circumstances, it would be wise to extend the present legislative authority for the direct controls. This would enable a continuation or acceleration of the present policy of tapering off controls as shortages and inflationary pressures in individual markets ease. To end these controls prematurely would adversely affect the defense program most of all, since the shortages and price-pressures are greatest in certain of the metal and metal products industries. At this time, with the Budget as high as it is, it would be poor economy to add to the cost of the defense program through inflationary price and wage increases.

Unless some new international crisis should occur, or the national security program should be expanded substantially above the levels now planned, it probably will be desirable to eliminate practically all of the present direct controls well within fiscal 1954. It now appears, however, that in the interest of national security two types of controls should probably be continued even beyond that date. The first of these is allocation of the most critical materials—particularly, certain of the scarce alloying metals—in order to expedite accumulation of the stockpile. The second is priority powers to assure that basic materials and certain critical types of equipment are channeled to military and atomic energy needs ahead of all other needs.

This raises, as part of the current policy problem, the question of what our longer-run preparedness policy should be. Our traditions of freedom make us naturally impatient with direct controls. We prefer in more normal times to let the market forces determine the flow of goods and services and the levels of most prices and wages. But these are not normal times. The Nation recognizes that, so long as the cold war lasts, it must maintain an adequate state of military preparedness. It must also maintain an adequate state of economic preparedness. This suggests careful consideration of stand-by legislative authority to be invoked under specific conditions, and maintaining the nucleus of a staff which can keep plans for controls continuously up to date and be prepared to meet quickly the contingency of any new Koreas. The experience after the Korean outbreak indicates that it may take as much as 6 months to enact legislation, recruit staff, and put controls into effect. We should be forearmed to prevent recurrence of such costly delay under comparable conditions.

Tax policy

One of the most notable features accompanying the build-up of the present defense program has been the effectiveness of fiscal policy. Federal budgetary expenditures are estimated at over 185 billion dollars for the fiscal years 1951 through 1953. The security program accounts for about 125 billion of this total. Yet the cumulative deficit in the conventional budget
is expected to be less than 6½ billion, and on a cash basis there will be a surplus of more than 5½ billion. This is a remarkable result, considering that in fiscal 1953 spending will be almost double that of fiscal 1950, increasing by about 35 billion. To achieve this result, it has been necessary to increase Federal taxes to the point where, in combination with State-local levies, they take a larger percentage of our national income than at any other time in our history.

From the start of the mobilization program, the fiscal objective has been to strive for a pay-as-we-go policy as a bulwark against inflation and to permit a fair distribution of the defense burden. In the July 1952 Economic Review it was said: “Taxation should be the last inflation control measure to be relaxed, since it is a basic measure and the most effective one for long-continued use.” This statement is now all the more pertinent, since important tax decisions must be made in the coming months. The President’s Budget indicates a deficit of 10 billion dollars in fiscal 1954, on a conventional budget basis, and about 6½ billion dollars on a cash basis, assuming tax reductions in accordance with scheduled termination dates. If the excess profits tax, which is due to expire June 30, 1953, and the 1951 increases in the individual income tax, which will terminate December 31, 1953, were to be extended beyond these dates, revenues would be increased by over 2 billion dollars in fiscal year 1954, and by about 6 billion dollars in subsequent fiscal years, above what they would be with the tax reductions.

To decide now to let the excess profits tax expire without compensating increases in the regular corporate income tax would be to furnish a stimulant to the economy which it does not now need and might need later on. The scheduled termination date for the individual income tax increases might also prove to be premature. Because these increases are not due to expire until December 31, 1953, however, more time is available to study the matter in the light of the developing budgetary situation and economic prospects generally.

Unquestionably, present rates create heavy burdens for large sections of the population. It is also true that the present high rates are not always conducive to maximum efficiency in industry and may in certain circumstances undermine incentives. In urging that it would be premature to effect a general rate reduction in 1953, the Council is not insensitive to these considerations. It is convinced, however, that high taxes are on balance an important stabilizing influence under current economic conditions, and that insufficient taxation would represent a greater risk to our economic well-being in 1953 than the continuance of the present high rates.

Looking beyond the near-term outlook, the time may come, as discussed in chapters III and IV of this Review, when it will be necessary to provide some new support to the economy. Under such circumstances, it would be appropriate to reduce the tax burden to stimulate private demand. But it would be inappropriate to make these tax reductions prematurely,
when they are not needed to stimulate demand and could even have inflationary effects, and when we are facing the prospect of sizable budget deficits despite full employment.

**International trade policy**

Another basic decision to be taken in 1953 is with respect to international trade policy. The Reciprocal Trade Agreements Act expires on June 12, 1953. This Act has been a powerful, constructive force in expanding the flow of trade in the free world, and it has symbolized our awareness that trade must be a two-way street. We are engaged in forging a strong community of free nations with great defensive strength. Basic to the other free nations' military strength is their economic strength. The more they are enabled to pay their own way, the better for us as well as for them.

The Reciprocal Trade Agreements program has also been an important factor in giving the countries of the free world some assurance that, as their trade with the Soviet Bloc declines, trade elsewhere will increase. Alternative sources of supply are largely in the dollar area, and the ability to earn dollars depends in large part on United States trade policy. However, in its most recent form, the Act contains certain new provisions, contrary to its basic objectives, which have threatened an increase in duties whenever consumption of foreign products became anything more than insignificant in the United States. Provisions of this sort are directly in conflict with and tend to defeat the broad purposes of the Act. So far as the United States is concerned, it is sound economics to adopt legislation on tariffs and customs procedures which furthers our objective of a greater volume of international trade without crippling qualifications.
Chapter III. Longer-Run Needs and Prospects

INTRODUCTION

IN Chapter IV of its Midyear 1952 Economic Review, the Council began to explore the longer-run outlook for the economy—the outlook extending further ahead than the year or so which we have generally encompassed in the near-term outlook. In the 6 months since midyear 1952, this longer-run problem has been receiving increasing attention. It has already been made the subject of several helpful private and public studies, among them the recently released report on "Markets After the Defense Expansion" issued by the Department of Commerce. In the current Review, the Council extends its midyear 1952 analysis of the longer-run outlook, first by attempting to identify the problem with somewhat greater precision, and then by pressing further the discussion of general private and public policies.

There is a prevalent tendency to fix a point in time ahead at which it is presumed that the basic economic climate will change, and that new problems—usually designated as deflationary—will confront us throughout the economy. There are many who follow the line of reasoning that this change will occur when defense spending stops rising and either levels off or begins to decline. This line of reasoning, in terms of only one sector of the economy, however important that sector, is clearly inadequate. A complete analysis must encompass all parts of the economy, private and public, and it must view the economy as a whole, for the whole is more than the sum of its parts. It must identify those factors which have been mainly responsible in driving the economy upward since Korea, and which may lose some of their up-pushing momentum. It must also identify other areas which may come forward to take their place in an economy where stability and prosperity require not merely the maintenance but the expansion of total demand. And it must study the interrelationships among these factors, and how they interact upon each other and upon the total.

The Council accepts and follows this last-mentioned broad type of analysis, but our interest in the longer-run problem and our point of concentration go beyond it. The Council recognizes that for purposes of economic analysis there is a proper distinction between immediate and long-range problems and policies, and that it is always important to devote attention to both. At the same time, we recognize that the dichotomy is not absolute; that what is done now affects what happens later on; that the present merges with the future; and that it is neither practical nor necessary for the purposes of effective action to forecast exactly at what point in time the economic climate will undergo the profound change which
some anticipate, or even whether the profound change will occur at all in the foreseeable future.

We are particularly wedded to this approach because the core of our philosophy under the Employment Act is not to wait for a depression or even a serious recession before taking action, but instead to work constantly toward the maintenance of maximum production and employment. We concern ourselves with the longer run not because we assert that a depression is inevitable or even in the offing, but rather because we believe that the long perspective as well as the short perspective is continually vital to the maintenance of a healthy economy. While the near-term outlook is largely determined by forces which are already in being and therefore leaves much room for forecasting but relatively little room for new policy, the approach to the longer-term problem should place less emphasis upon forecasting and relatively more emphasis upon a realization that the United States is richly enough endowed with resources and brains to make the longer-range future what we want it to be. This confidence, this commitment, is clearly written into the Employment Act.

It is thus clear that the reasons why the Council extends the discussion now being undertaken through the year 1955 is not because we now are ready to predict any profound change in general economic conditions in any particular month or year between now and 1956. It is rather because we believe that a period of 3 years ahead is long enough to carry us beyond narrow preoccupation with the immediate, and short enough so that an analysis of demand prospects can still be kept fairly concrete. To be sure, many of our economic problems, for example shortages of certain raw materials, require an even longer-time perspective for effective treatment.

A long-range economic problem requires either early, preventive action to avert a danger in the more distant future, or early, positive action to commence solution of a problem which in its very nature takes a long time to solve. This is particularly true because, in our type of free economy, the attitudes of people throughout the Nation are no less a controlling fact than laws upon the statute books. Our economic situation in 1955, and during the intervening years until then, will depend largely upon the prevalent sentiment now as to whether the maintenance of maximum employment and production is attainable in our kind of economy, and whether it is worth the continuous efforts which must be directed toward its attainment. The Council believes in the worth and practicality of this goal. We believe also that its attainment depends not so much upon the accuracy or precision of long-range forecasting, either as to timing or substance, as it does upon the popular commitment to the goal and the day-by-day evolution of improved analyses and policies, both short-run and long-run.

In the following discussion, we follow closely the methodology set forth in the Employment Act which we believe to be sound: First, to identify the employment, production, and purchasing power needs of the economy for the period under consideration; second, to estimate prospective trends for
the period in the event that policies remain constant; and third, to study and recommend any changes in private and public economic policies which may seem helpful to bring prospective trends into line with our national needs and capabilities.

**EMPLOYMENT AND PRODUCTION NEEDS, 1953–1955**

To define maximum production and employment in terms of the objectives of the Employment Act, it is necessary to take account of the whole complex of our economic society—the size of the labor force, the average length of the workweek, and the productivity potential of all of our physical and human resources. The estimate involves also some imponderables or values not subject to quantitative measurement, such as what level of "frictional" unemployment is consistent with maximum employment, or what balance is to be struck between more leisure and more goods as productivity increases.

*The labor force*

The size of the labor force is determined primarily by the expected growth in the population of working age. It is assumed for our purposes here that in a high employment period in the near future, the over-all "participation rate," i.e., the proportion of the noninstitutional population 14 years of age and over in the labor force, will remain practically unchanged from the past 2 years' level of about 58.8 percent, even though participation rates for particular groups of workers within this total will change. The total of 58.8 percent is a little higher than in earlier peacetime high employment years. As shown in table 10, an expansion of the total labor force from 66½ million last year to 68½ million in 1955 is estimated. The labor force trends shown in the table are based on data from the Census Bureau's Current Population Survey since 1940 and data from the censuses of 1920

### Table 10.—Population and labor force

<table>
<thead>
<tr>
<th>Item</th>
<th>1950</th>
<th>1951</th>
<th>1952</th>
<th>Projections*</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1953</td>
<td>1954</td>
<td>1955</td>
<td></td>
</tr>
<tr>
<td>Total population, including armed forces overseas</td>
<td>151.7</td>
<td>154.4</td>
<td>157.0</td>
<td>159.2</td>
</tr>
<tr>
<td>Noninstitutional population, 14 years of age and over</td>
<td>110.8</td>
<td>111.9</td>
<td>113.1</td>
<td>114.3</td>
</tr>
<tr>
<td>Labor force, including armed forces</td>
<td>64.6</td>
<td>65.8</td>
<td>66.5</td>
<td>67.2</td>
</tr>
<tr>
<td>Labor force participation rate *</td>
<td>58.3</td>
<td>58.8</td>
<td>58.8</td>
<td>58.8</td>
</tr>
</tbody>
</table>

*Projections of population by Department of Commerce, Bureau of the Census; all others by Council of Economic Advisers. See Current Population Reports, Series P-25, No. 58, and P-50, No. 42, for basic data.

*14 years of age and over.

*Labor force as percent of noninstitutional population 14 years of age and over.

**Note.**—Total population figures are for July 1 of each year and are consistent with the 1950 Census. Noninstitutional population, 14 years of age and over, and labor force data represent current estimates and projections consistent with the 1940 Census levels. Therefore the series are not exactly comparable but the differences are relatively small.

**Sources.** Department of Commerce and Council of Economic Advisers.
to 1940, adjusted for comparability with current estimates. The population estimates represent the medium series of projections.

Under the present defense program, the armed forces during the next few years are projected to remain at the current level of 3.6 million which was reached in 1952. And it is assumed for the purposes of this study that unemployment, which during the past 2 years has been below the 2-million mark, could rise to as much as 2½ million by 1955 without presenting a general unemployment problem. Such an unemployment figure in a considerably larger labor force would not depart so markedly from the Nation's legislated objective of "maximum employment" as to call for new counteracting public measures, although it is desirable, in the Council's judgment, to strive consistently to keep unemployment lower than this figure.

These two estimates, then—armed forces and unemployment—point to the need for about 62½ million civilian jobs in 1955, contrasted with 61.0 million for 1952 as a whole. This contemplates a considerable increase in private nonagricultural employment, and a continuation through 1955 of the long-run decline in the number of persons engaged in farm work. A moderate further increase in government employment at the State and local level can be anticipated.

Table 11.—Labor force, employment, and unemployment

<table>
<thead>
<tr>
<th>Item</th>
<th>1950</th>
<th>1951</th>
<th>1952</th>
<th>Projections¹</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1953</td>
</tr>
<tr>
<td>Labor force: total</td>
<td>64.6</td>
<td>65.8</td>
<td>66.8</td>
<td>67.2</td>
</tr>
<tr>
<td>Armed forces</td>
<td>1.5</td>
<td>2.9</td>
<td>3.8</td>
<td>3.6</td>
</tr>
<tr>
<td>Civilian labor force</td>
<td>63.1</td>
<td>62.9</td>
<td>63.0</td>
<td>63.6</td>
</tr>
<tr>
<td>Employment</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agricultural</td>
<td>69.0</td>
<td>61.0</td>
<td>61.3</td>
<td>61.9</td>
</tr>
<tr>
<td>Nonagricultural</td>
<td>7.5</td>
<td>7.1</td>
<td>6.8</td>
<td>6.7</td>
</tr>
<tr>
<td>Civilian government</td>
<td>52.4</td>
<td>56.0</td>
<td>55.8</td>
<td>55.2</td>
</tr>
<tr>
<td>Private</td>
<td>3.1</td>
<td>1.9</td>
<td>1.7</td>
<td>1.7</td>
</tr>
<tr>
<td>Unemployment</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unemployment as percent of civilian labor force¹</td>
<td>5.0</td>
<td>3.0</td>
<td>2.7</td>
<td>2.7</td>
</tr>
</tbody>
</table>

¹ Projections by Council of Economic Advisers; total labor force based on projections in Current Population Reports, Series P-50, No. 42.
² Percent based on unrounded figures for 1950-52.

NOTE.—Detail will not necessarily add to totals because of rounding.

Sources: Department of Commerce and Council of Economic Advisers.

Hours of work

The average number of hours worked each week is assumed to decline slightly in the private nonagricultural segment of the economy—from 39.7 in 1952 to an estimated 39.5 in 1955, reflecting chiefly increases in paid vacations and some further reductions in the amount of overtime. In manufacturing, it is assumed that the basic 40-hour week will be continued.
In agriculture, technological development should continue to make shorter hours possible, but a declining labor force will make for longer hours. On balance, it seems reasonable to assume that the farm workweek will show little if any change during the next 3 years. (See appendix table B-14.)

**Productivity**

Productivity, in its generalized meaning, is the ratio of output to input. Here, as is the common practice, the term is restricted to the relationship between total output and labor input, so that a rise in productivity is an increase in total output per man-hour. In these projections, productivity in the private nonagricultural sector of the economy is assumed to increase about 2.5 percent this year, and by slightly larger percentages in the next 2 years. This would involve increases which are a shade above the average gains over the long-run past, in recognition of the extraordinary expansion and improvement of capital equipment throughout the postwar period, but which are still somewhat below the average productivity increase of the last 5 years.

**Total needed production**

When, as shown in table 12, these estimated productivity increases are applied to the input of labor as previously projected for the private nonagricultural sector of the economy, there results an estimate of private nonagricultural production needed in 1955. And when this is added to an estimate of farm and government output, the result is this: A gross national product of about 375 to 380 billion dollars, calculated in 1952 prices, consistent with high-level production and employment in 1955. If the Nation should build up steadily to this 1955 level of output, it would mean increments of about 10 to 12 billion dollars annually.

### Table 12.—Gross national product: 1952 and projections of needed levels, 1953–55

<table>
<thead>
<tr>
<th>Item</th>
<th>1952</th>
<th>Projections 1</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>1953</td>
</tr>
<tr>
<td>Private nonagricultural employment, hours, and productivity:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employment, millions</td>
<td>48.0</td>
<td>48.6</td>
</tr>
<tr>
<td>Hours worked per week</td>
<td>39.7</td>
<td>39.7</td>
</tr>
<tr>
<td>Total man-hours worked per year, millions</td>
<td>99,091</td>
<td>100,330</td>
</tr>
<tr>
<td>Output per man-hour:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Index, 1952=100</td>
<td>100.0</td>
<td>102.5</td>
</tr>
<tr>
<td>Dollars, 1952 prices</td>
<td>2.9286</td>
<td>3.0018</td>
</tr>
<tr>
<td>Gross national product: billions of dollars, 1952 prices:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private nonagricultural</td>
<td>290.2</td>
<td>301</td>
</tr>
<tr>
<td>Farm</td>
<td>26.2</td>
<td>25</td>
</tr>
<tr>
<td>Government</td>
<td>35.8</td>
<td>31</td>
</tr>
<tr>
<td>Total gross national product</td>
<td>352.1</td>
<td>357</td>
</tr>
</tbody>
</table>

1 Projections by Council of Economic Advisers.
2 Compensation of general government employees.
3 Preliminary estimates for fourth quarter, 1952, indicate that gross national product has already reached an annual rate of about 335 billion dollars in average 1952 prices. If the projected growth were to be based on only the fourth quarter of 1952, the projected gross national product in 1953 would be somewhat higher than shown. It seems more appropriate, however, to base the projection on the full year 1952, in light of the fact that, as is emphasized in the text, the projection is a minimum objective, not a forecast.

NOTE.—Detail will not necessarily add to totals because of rounding.

Source: Department of Commerce and Council of Economic Advisers.
It should be noted that, throughout the calculation, a rule of moderation has been followed. We have allowed for an increase of about a million above recent levels of unemployment, although it would be obviously desirable to hold unemployment to a much lower figure, and we should try to do so. And the annual productivity gain posited is more modest than some experts expect, and certainly more modest than that for which it might well be argued the Nation should strive. In short, the needed levels of employment and production pictured are by no means those of a drum-tight economy, and they probably would not provide as much additional production as would be needed if substantially greater national security efforts should become necessary. From the viewpoint of a full-employment policy, they constitute a minimum standard against which to measure our prospects for the next 3 years.

Amplifying comment by Mr. Keyserling

The national objective set forth above for our productive growth between now and 1955 prompts me to make this amplifying comment, in view of my known commitment to the philosophy of an expanding economy. I have no reason to believe that my colleagues are not in general accord with the amplification that I now set forth, and I do not regard it as inconsistent with any portion of this Review. I set it forth singly because it is a little aside from the main stream of this Review, and yet germane enough to afford an opportunity in the context of this discussion at this time to respond to many of the questions presented to me over the years concerning my reiterated interest in the philosophy of an expanding economy. This amplification, which may be of interest, to some who read this Review, should not be interpreted to cast any doubt upon my complete agreement with the Review in its entirety, both as to analysis and conclusions.

From the time of the Korean outbreak, I have had several opportunities to emphasize that America's productive power and potential constitute the greatest nonsecret weapon of the free world. While I have favored the various control and restraint programs (both indirect and direct) designed to divide up what we have in accord with national priorities in time of danger, I have constantly pointed out that if there were excessive relative emphasis upon these methods, it could distract us from full attention to the build-up of our greatest nonsecret weapon. Further, I have felt that any such misplacement of emphasis would tend to increase friction among the functional sectors of our economy when unity is of the essence.

The events of the past 2½ years have in the main strengthened my earlier views. The actual productive record of the economy, generating an expansion of civilian supplies along with the vast increase in defense output, has far exceeded estimates which were generally regarded as fanciful when first offered for discussion and appraisal in mid-1950. Yet the issue is still very much alive. There are some who would give consideration to the reduction of our primary defense efforts and our international commit-
ments, not on a finding that lower targets seem consistent with our world safety (which would of course justify such action), but rather because they still grossly undervalue the productive power of the American economy. Any such undervaluation of our productive potential can lead—and in a few instances has led—to unwarranted fears about the availability of certain types of civilian supplies, thus creating some inflationary pressures based upon false expectancy, and creating some unnecessary dislocations. Today, with crying needs for our exportable products among millions of free people throughout the world whose very freedom is imperiled by want, with numerous families in the United States in need of a better standard of living and a vast majority of the people of the United States well able to benefit by a still higher standard of living, with the chances possibly 50-50 that the world situation may call for an intensification rather than a slackening of our international efforts, and with the Soviet Union and its satellites pursuing an increasingly relentless course, it would indeed be ironical if any substantial segment of our own people doubted whether we will be able fully to use our current productive capacity, instead of realizing that we have the brains immeasurably to increase our economic and political security in the most profound sense by drawing the weapon of our ever-increasing productive ability fully from its sheath.

I have believed since the Korean outbreak, and I now believe even more firmly, that nothing would contribute so much not only to our national security and progress, but also to the fullest generation of our moral and spiritual energies, as an intensified drive to make the whole Nation conscious of and uniformly engaged in the full utilization of this great nonsecret weapon. Despite generally "full employment," there is some underutilization of some parts of the labor force; some underutilization of some of our current productive resources in agriculture and even in industry; some underutilization of existing technology and retardment in the application of established science to the practical arts; and some underutilization of brains and good will. With an effort commensurate to our problems in a troubled world, it would seem that by 1955 we might lift our national output even above the target used for the purposes of this Review, without inflationary strain and without resort to the forced pressures and controls which would be imperative in a full war economy but which would be undesirable in a long middle course between war and peace.

It is manifestly not feasible for me to spell out in this brief amplifying comment the detailed means by which the Nation might move even more effectively than it has thus far along this already established course. I must be content here to clarify a permeating philosophy rather than cite a precise program. Nor do I intend to imply that those in charge of the mobilization program, as well as many leaders throughout the Nation, have not joined largely in this philosophy. Had they not, the marvelous accomplishments since mid-1950 would have been impossible. But their great
and effective labors have been made more difficult at times by some who desired to cut down our world security efforts on the ground that our economy could not produce enough to meet them without disaster, and who then in turn have desired to take it easier on the over-all production front on the ground that our world security efforts could safely be less than had originally been thought necessary. Such reasoning draws a vicious circle. Considerations of our domestic economic well-being must, of course, be meshed with considerations of world security. But stating this is the beginning of the problem, not its solution.

To avoid possible misunderstanding, it is not asserted that the 375–380 billion dollar target set forth in this Review is a “forecast” of what our actual output will be in 1955. If we were to have a serious recession or depression, the 1955 output may be far less. The figures are merely objectives—merely a quantification as to what we mean by maximum production looking forward to 1955. I readily admit that practical objectives must be kept within the range of the attainable, taking fully into account other national purposes, and also taking fully into account the current state of the economy from which we start. But the concept of maximum employment and production under the Employment Act would be impoverished if it hewed to the line of what is likely to happen without effort, or even what is attainable with slight effort. If the term “forecast” is used in this connection, the concept involves a forecast not of what we will automatically accomplish but rather of what we can do and ought to do. And what we ought to do, within the limits of what we can do, should be set within the context of the current world situation.

These views are not predicated upon a desire to foist more controls or “central planning” upon the economy. On the contrary, since the Korean outbreak, I have insisted constantly that the full release of our productive energies throughout the Nation—sparked as it only can be by vision and imagination—is the true alternative to (1) the economic straitjacket which would result from trying to make inadequate production cover our full needs or (2) the equal danger which would result from failing to meet our full needs in terms of the world situation.

Nor am I unmindful of the sound requirement that maximum employment and production should not be defined at such high levels as to generate inflation. The subject of the causes of inflation is too comprehensive for discussion in this amplifying note. Those who would oversimplify this matter should observe the price stability which has been maintained recently when unemployment has reached an all-time low point short of total war, and should observe also the inflationary spurts which have occurred in other recent periods when our resources were by no means being fully employed. I will not here discuss the momentous question of whether a slight increase in inflationary pressures would outweigh, under current world conditions, the gains to be derived from a much larger national product. Such analysis is unnecessary to my current purpose, because I
believe that our resources are sufficiently plentiful to reach a 1955 national product as high as or possibly even higher than that set forth in this Review without inflation, and with the progressive casting off of the direct controls. In all probability, most of those who might take issue with my belief in the desirability of a relatively rapid expansion of output would do so, not because they fear inflation, but rather because they fear that a deflation will result from lack of the brains or will to use fully the greatest potential blessing to which any nation in the history of the world has ever fallen heir— the great nonsecret weapon of the United States.

The idea, often expressed by the Council, and in fact by other persons through the ages, that a free and great people should be able to use all of what they have the ability to produce seems to me so commonplace and impregnable that I am concerned about the disposition of some, not including any of my associates, to underestimate our productive power at maximum employment because they are concerned that America’s great nonsecret weapon may become a Frankenstein if used fully. Instead, I believe that economists and others should be devoting all of their talents toward finding ways to capitalize fully upon this magnificent asset. In the long run, I believe that the pace at which we move toward further progress in this vital matter may well determine the future of freedom. This issue—whether we shall shrink from or measure up to the challenge of potential abundance—is perhaps the supreme issue of the Twentieth Century. I have not issued this challenge: It is written into the Employment Act of 1946, and underscored by the towering menace of communist aggression. (End of amplifying comment by Mr. Keyserling.)

**Demand Prospects for the Longer Run**

Whether the Nation maintains maximum production and employment over the long pull depends directly upon sufficient demand in the aggregate to induce enough production, and provide enough jobs, to keep unemployment below the margin of tolerance indicated earlier in this Review.

The economy’s rate of actual performance in the future is far more uncertain, of course, than the needs just portrayed. We have and want a free and flexible economy, in which no one hand is on the throttle, and in which production is guided by the separate decisions of millions of consumers and businessmen as well as government. In a free economy, the amount of total future demand and its components can be estimated and shaped only within very broad ranges.

*Prime assumptions*

Any analysis of economic trends 2 or 3 years ahead (in the absence of policies designed to modify these trends) must be grounded in certain working assumptions which it is important to make explicit. For the purposes of this study, as a matter of methodology for estimating demands in particular sectors, it is assumed:
First, that the level of general business activity will be high during the period in question. This assumption merely extends into the future a situation which now exists in fact. This approach is defensible as a starting point for analysis, because we are dealing with an economy now moving under the momentum of prosperity and not one trying to gain speed after a stall. The problem is to identify possible elements of weakness which may arise in a vigorous economy, rather than to search for weakness in a deteriorating economy where all prospects are discouraging.

This initial assumption is not meant to prejudge the conclusion as to over-all prospects which will be drawn at the end of the sector-by-sector discussion; that conclusion might force a revision of the initial assumption. But for purposes of making a first working estimate of investment and consumption prospects, some initial hypothesis as to the general tone of the economy is necessary, and the present one is the most tenable;

Second, that there will be no significant change in the degree of international tension. While it could be unlikely that the situation of the last year and a half will actually continue without variation, an assumption that it will is the most prudent one available for purposes of the general economic analysis here undertaken;

Third, since the purpose of this analysis is to suggest later on in this Review what changes in private and public policies may become appropriate, to postulate new policy actions initially would be to assume at the start the results of the inquiry. Therefore, we start by assuming current policies. It is initially assumed, for example, that Federal tax rates will be at levels set by present laws, which call for the termination of the corporate excess profits tax in mid-1953, reductions in personal income taxes at the end of 1953, and cuts in excise taxes and the basic levy on corporate earnings in April 1954; that there will be no increase in Government expenditure for anti-cyclical purposes; and that present credit policies will remain unaltered. (It should be noted that, despite the assumption that no additions to the Federal deficit will be made for specifically anti-cyclical purposes, the assumption that the tax reductions now provided by law will be carried out on schedule while present expenditure programs are maintained implies substantial deficits in both 1954 and 1955.)

Fourth, that there will be no mass changes in consumer expenditures or business investment of such caliber as might be touched off by unpredictable or fortuitous events; that is, that endogenous forces will predominate.

Government expenditures

National security. On the basis of present plans, as incorporated in the Budget of the President for the fiscal year 1954, security expenditures are scheduled to rise moderately above the rate reached in the second quarter of 1952. Over half of the increase is scheduled to occur in components of national security expenditures other than the military services, notably in the Mutual Security Program and in atomic energy. It is antic-
Budget expenditures for national security are scheduled to rise moderately through 1953, and then level off. It is anticipated that a gradual decline will begin late in 1954.

It should be emphasized that these forward estimates are based on presently planned programs. Even without major changes in the program, any further "stretching-out" of individual production schedules beyond that already anticipated, or failure to meet established schedules, would tend to result in a somewhat lower peak level in expenditures, probably reached at a somewhat later date. Any increase or decrease in unit costs from original estimates—and such estimates are usually made conservatively high when funds are initially obligated—would affect final expenditures.

If these estimates prove to be roughly valid, they indicate that, measured in terms of new demand in the market, the major economic impact of the national security program has already occurred. Although total expenditures will continue to be large, the month-to-month, or quarter-to-quarter, increases will be small, in contrast with the large increases from mid-1950 to the second quarter of 1952. Moreover, business buying of raw material...
and component inventories, and recruitment of labor, often precede by many months the Government expenditure for the finished product. Even though expenditure data include advance payments on military contracts, and thus already reflect, in part, these production lead-times, it would seem that the maximum impact of the security program on materials and labor may have been reached some months ago.

Nevertheless, present plans indicate that, in the next 2 years at least, the national security program will continue to be a large and powerful influence in the United States economy. It will provide an assured and reasonably stable volume of demand for the products of industry. But other sources of new demand will be needed to provide the growth in total demand needed to maintain high employment, in an economy characterized by a growing and increasingly productive labor force.

Other government expenditures. One of the great reserves of potential demand is to be found among government expenditures other than for national security, specifically, for the development and conservation of natural resources, and for public transportation, education, health and recreation facilities. In general, these forms of governmental investment are not endangered by the threat of "overcapacity," or by the fear that there will not be "markets" for their products or services.

During the next few years under the assumption of no change from present policies, it is not likely that Federal expenditures for these programs will rise significantly. State and local purchases should increase more substantially, perhaps reaching the level of 28 billion dollars in 1955, compared with 23 billion in 1952. Greater expansion on the State and local level must await the solution of difficult financing problems.

Private domestic investment

Plant and equipment, including commercial construction. During the period between World War II and the Korean outbreak, business invested large sums in plant and equipment. To this already high level of expenditures there was added, after June 1950, the vast expansion of capacity called for by the defense program, stimulated by such aids as accelerated tax amortization. Most of the Government-aided expansion will have been completed by the end of 1953. But for the Government inducements, much of it probably would have been spread out over a longer period.

Moreover, studies of the relationship between the stock of capital equipment and the volume of total output during the last four decades indicate that, as a result of the unusually high rate of investment in the postwar years, the stock of equipment is now somewhat high relative to output. This suggests that higher rates of investment, or even a continuation of the present rate, may be difficult to maintain during the next few years.

These evidences of the possibility of a downturn in business investment are significant, but they are not conclusive when considered in conjunction with the other determinants of investment plans.
The demands of businessmen and consumers alike are influenced by current earnings, and to some degree by past income, from which they may have saved funds for spending or investing. But far more than in the case of the consumer, the expenditures of the businessman reflect expectations about the future. His long-run investment programs are shaped by his judgment about long-run market prospects; all his decisions are made primarily with his eye on tomorrow. Business investment must also take account of existing plant and the stock of capital goods, and the possibility that capacity may already be more than ample. But the stock of capital goods, however large, does not preclude the possibility or the necessity of further investment in a dynamic economy. Equipment must be replaced or modernized. It may often be discarded, though still usable, in the search for means of cutting costs to maintain or improve a firm’s competitive position. New products, and the machines to make them, must be devised for consumers who soon have enough of the old and are attracted by the new. In the struggle for profits, plant and equipment are always expendable.

In making his investment plans, the businessman naturally considers his financial position. Measured by the ratio of liquid asset holdings to sales or to current debt, corporations in general are in a more favorable financial situation than before World War II. (See chart 24.) Though corporate debt has been mounting—it rose 19.4 billion dollars or 14 percent in 1951 and about 7.5 billion or 5 percent in 1952—corporate savings in the form of retained profits and depreciation reserves have been higher recently than in most postwar years. The last-named type of saving has been augmented by accelerated tax amortization.

The availability of external financing must also be taken into account, and the possibility that taxes will be raised or lowered. On the first score, the high rate of private saving, which is likely to increase at least in the business sector for the reason already noted, will probably be an abundant source of lendable funds. As for taxes, the Council has assumed for the purpose of this initial analysis that they will be reduced in accordance with the provisions of the present law. Even if the cuts do not turn out to be so large, or are not made so soon as now scheduled, the prospects are that whatever tax action is taken will tend to stimulate business investment.

Finally, although the outlook for earnings and all the other factors which are conducive to new investment may be favorable, the quality of management is the ingredient which finally determines whether or not business will capitalize opportunities. Business management in the United States has amply demonstrated its resourcefulness in turning new investment potentialities into actual plant and equipment.

How businessmen are now weighing and reacting to the several factors which influence investment decisions is indicated by a recent survey of investment intentions, conducted by the Department of Commerce and the Securities and Exchange Commission. This survey revealed that in-
CORPORATE LIQUIDITY

For the period since World War II as a whole, liquid asset holdings of corporations have risen less than current liabilities. However, in 1952, the ratio of liquid assets to current liabilities was more favorable than in 1939.

NOTE: DATA ARE FOR ALL U.S. CORPORATIONS EXCLUDING BANKS AND INSURANCE COMPANIES.

SOURCE: SECURITIES AND EXCHANGE COMMISSION.
vestment firmly planned for 1953 is only slightly below the level of 1952. A special survey of large companies found that their budgeted capital expenditures in 1954 are 15 percent below the 1952 rate, and 20 percent below that rate in 1955. These 1954 and 1955 plans are subject to change. They could move downward more rapidly in the face of unfavorable conditions; they can move more favorably if businessmen grasp the scope of the markets waiting to be probed. In addition to these budgeted plans, the companies are considering a substantial amount of other investment which may be undertaken if conditions prove auspicious.

Surveys which look so far into the future are naturally subject to many hazards. But if the economic environment continues to be good, they are not likely to be biased in the direction of exaggeration. The future has a way of turning up opportunities which cannot be seen at the present. It should also be emphasized, however, that generally speaking the businessmen interviewed in the surveys had built their investment plans on the assumption that the Nation would remain prosperous. A decline in an important sector of economic activity might well bring a reconsideration and postponement of many of these investment plans.

Investment by farmers in machinery and buildings has been at a high level in the post-World War II period, exceeding depreciation by a substantial amount. Some decline in the rate of farm investment in equipment particularly may occur over the next several years, especially if the downtrend in farm income is not checked or reversed. However, if farm prices and incomes remain high, the decline may be quite small.

Conservatively appraised, the prospects are that, under the initial working assumptions set forth at the start of this chapter, total investment in plant and equipment, in the absence of new policies subsequently to be discussed, will decline but not substantially during the next 3 years.

Housing. An estimate of the demand for housing in the next 3 years must take into account demographic factors relating to population, marriage and birth rates, physical factors relating to the stock and condition of existing housing, and monetary factors such as incomes and credit conditions. Effective demand is partly dependent on all of these.

Viewed by themselves, most of the nonmonetary considerations suggest a decline in the demand for housing in the next few years. The year 1945 ended a long period of low residential construction resulting, first, from the depression in the 1930's and, second, from the unavailability of materials and labor during the war. The number of families who were forced to double up because of lack of housing accommodations was large, and the number of vacancies was negligible. The backlog of demand was supplemented, in the immediate postwar years, by a phenomenally large number of new families resulting from high marriage rates.

The volume of residential construction since the end of the war—nearly 8 million units, farm and nonfarm—together with conversions of existing housing, has been sufficient to house the net increase in the number of
After moving up steadily to an all-time high in 1950, new nonfarm housing starts receded, but continued on a level that was still high, considering the competing demands of the defense program.

The expected decline in the number of new households formed will have a pronounced effect upon the demand for housing in the next few years. The young people reaching marriage age in the next few years will be those who were born in the mid-1930’s, when the birth rate was very low. It is probable that net household formation will decline from the level of 900,000 in the year ending April 1, 1952, to an average of around 700,000 during the next 3 years. This compares with 1,600,000 in the peak year 1947-48.

One offsetting physical factor is the fact that many of the houses which have been built since the war are small and inadequate for growing families. The high birth rate of the last several years will result in increasing pressure for larger accommodations which, in part, will require the building of new
houses regardless of the adequacy of the total housing supply in terms of numbers of houses. In addition, a net demand for housing will continue to result from the migration of families. Further, many other houses are very old, seriously substandard, or located in deteriorated or commercialized neighborhoods. These are candidates for demolition or conversion to uses other than for housing.

These nonmonetary factors, which on balance indicate a sliding off of effective demand, are at least partially offset by certain favorable monetary factors. Incomes are now much higher than they were before or immediately after the war, and if a generally high level of business activity continues, as we have assumed, it will mean a continued rise in average personal incomes. The great majority of American families are housed less adequately than they would like to be. With a continuation of high incomes, it can be expected that there will be "trading up" all along the line, which will require new housing at higher quality levels and frequently at intermediate levels. Many other families, already respectably housed, will build new houses to get exactly what they want because they can afford to do so. It is also to be anticipated that builders will continue to improve the quality of new houses and to offer better values, which should have a stimulative effect on demand. Moreover, the level of housing construction has been repressed to some extent during the last 2 years by residential real estate credit control (Regulation X and its Government-agency counterparts). The removal of these controls last September has already contributed to some pick-up (after adjustment for normal seasonal variation) in new housing starts. On balance, assuming a generally high level of business activity but the absence of any change in private and public policies, it seems that private residential construction may be somewhat below recent levels in the next 3 years, but that the monetary factors just described would hold the total close to about 1 million nonfarm dwelling units a year.

Expenditures for conversion of large houses or other buildings into apartments, for rehabilitation of existing units, and for new and reclaimed farm dwellings are expected to hold at levels of recent years. Expenditures for additions and alterations may increase somewhat under the pressure of larger families.

These estimates do not make allowances for large-scale expansion of either the public housing program or the slum clearance and urban redevelopment programs. In each of these areas, there is a large reservoir of work which awaits a more intensive application of public policy to these tasks. This will be discussed subsequently in this Review.

Inventories. About the only certainty about investment in inventories, which is ultra-sensitive to the slightest shift in the business weather, is that it is highly unstable. It is therefore wise to make no long-range estimate of its size in the future, but simply to note that inventories now
appear to be approximately in balance with total sales, and to assume that they will tend to grow with the total output of the economy, but with many a short-term fluctuation.

Net foreign investment

Exports from the United States, United States imports, foreign aid programs and the flow of long-term capital to other countries, are subject to a multitude of conditions and policy measures, foreign as well as domestic. Hence the forecasting of trends is especially perilous. Only one general observation may be hazarded: On the basis of recent developments, and assuming no change in international commercial policies, the prospects are for only a moderate expansion of exports. (International economic prospects and problems are discussed separately in chapter V.)

Consumer expenditures

Estimates of the volume of spending by consumers must take three things into account: the flow of personal income; the level of personal taxes which determines how much of the total income is spendable, i.e., disposable income; and the percent of disposable income which is spent, i.e., the saving ratio.

If business activity is high and employment continues to rise during the next 3 years, as has been assumed, total personal income will continue to rise. If Federal tax rates should remain at present levels, the gain in disposable personal income would be somewhat less than proportionate to the gain in personal income. However, if rates are reduced as called for by present law, as we have assumed, there would be a substantial immediate effect, and the full effects of the reduction, which would be felt during most of 1954 and all of 1955, would be to increase the gain in disposable personal income, directly and indirectly, by around 10 billion dollars (annual rate). How much of an increase in consumption expenditures might be expected in either case depends upon the choices of individuals between spending and saving.

The total which statisticians call "personal saving"—that is, the difference between total disposable income and total purchases classified as consumption—includes many heterogeneous elements which have little or no relation to the man-in-the-street's idea of "saving."

A part of total personal saving is increased equities in homes and in the physical assets of unincorporated businesses when the saving is automatically balanced by spending, or more properly, investment. Saving includes also rising equities in insurance reserves. Even if purchasing power can be extracted from these equities through policy loans or cancellations, most persons are reluctant to draw upon them excepting in emergencies.

An element in saving which is thought to supply consumers with ready reserves of purchasing power is additions to liquid asset holdings. While holdings of these assets have risen since the war and are still rising, it is doubtful whether they are high enough in the minds of most consumers
either to discourage further additions or to make a large portion of present liquid assets ready candidates for "dissaving." (See chart 26.) The latest Survey of Consumer Finances indicates that many consumers still are quite dissatisfied with their current degree of liquidity. Included also in liquid savings are the funds and securities of unincorporated businesses, which are either a part of current working capital or which have been accumulated for future investment in business plant, equipment, and inventories. While liquid asset holdings have grown since World War II, their purchasing

**CHART 26**

**LIQUID ASSETS AND DISPOSABLE PERSONAL INCOME**

At the end of World War II, liquid assets were unusually high in relation to disposable income. Over the period since then, however, income has grown at a faster rate than liquid assets.

<table>
<thead>
<tr>
<th>BILLIONS OF DOLLARS</th>
<th>BILLIONS OF DOLLARS</th>
</tr>
</thead>
<tbody>
<tr>
<td>300</td>
<td>280</td>
</tr>
<tr>
<td>260</td>
<td>260</td>
</tr>
<tr>
<td>240</td>
<td>220</td>
</tr>
<tr>
<td>200</td>
<td>180</td>
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<td>160</td>
<td>160</td>
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<tr>
<td>120</td>
<td>120</td>
</tr>
<tr>
<td>80</td>
<td>80</td>
</tr>
<tr>
<td>40</td>
<td>40</td>
</tr>
</tbody>
</table>

**DISPOSABLE PERSONAL INCOME**

**PERSONAL LIQUID ASSET HOLDINGS**

1939 40 41 42 43 44 45 46 47 48 49 50 51 52

1/ Includes currency, demand and time deposits, savings and loan shares, and U.S. government obligations.

Sources: Department of Commerce, Board of Governors of the Federal Reserve System, and Council of Economic Advisers.
power has been reduced by inflation, and the amount of "spare cash" contained within them, which might any day be exchanged for goods, has been commensurately reduced.

Personal liquid assets are highly concentrated in ownership. It is estimated that the highest one-tenth of income receivers hold about 39 percent of all liquid assets (excluding currency), according to the 1952 Federal Reserve Survey of Consumer Finances. In contrast, only 26 percent of total liquid assets are divided among the many families in the lower half of the income scale.

One of the most volatile elements in saving is change in consumer debt outstanding, an increase in the total being considered a form of dissaving or negative saving, and a decrease a form of saving. Consumer debt is far more widely distributed among families in the several income brackets than are liquid asset holdings; it is a liability that at least partially offsets the ownership of liquid assets, weakening the financial position of some families and their willingness to spend. In all cases, it is an imperious charge on future earnings, requiring repayments which are a kind of compulsory saving.

Since the greater part of consumer debt arises from the buying of durable goods, such as automobiles and household appliances, the course of the saving rate may depend heavily on the strength of demand for such goods. The future market for consumer durables is favorable, but it shows less possibilities for increases than in the years immediately following World War II. Consumers are better stocked with goods than they were at that time, and they are carrying a higher burden of debt. Although total consumer debt is not out of line with the prewar relationship to disposable income, and there is no evidence that the economy is as yet "top-heavy" with such debt, it seems likely that the rate of increase will slow down sometime in the not too far distant future. (See chart 27.)

In the postwar period, a rising percentage of families has become financially able to own cars, and many families have moved into the two-car class. In addition, new car demand has been bolstered by the need to replace the superannuated cars of prewar make. Under these stimuli, production in the period 1948 through 1951 averaged 5.2 million a year. In 1952, only 4.4 million cars were produced, but this was partly due to metal shortages.

As discussed in chapter II above, automobile sales in 1953 are expected to be higher than in 1952. They may approximate the 1948-51 average. In 1954 and 1955, however, there will be fewer prewar cars, and more postwar cars on the roads. The replacement rate will therefore be lower. Under these circumstances, it may present a difficult problem of salesmanship and price-income adjustments to expand sales of passenger cars above the 1953 level.

The potential demand for some other consumer durable goods is suggested by table 13, which shows the degree of "saturation" in the market
Total consumer credit, after dropping during the World War II years, rose sharply thereafter.

Although the ratio of outstanding consumer credit to disposable personal income has increased during the years since World War II, it is still slightly below the prewar peak.

\[ / \]

CONSUMER CREDIT OUTSTANDING AT END OF YEAR AS PERCENT OF DISPOSABLE PERSONAL INCOME FOR YEAR AS A WHOLE.

SOURCES: BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM AND COUNCIL OF ECONOMIC ADVISERS.
for several products. Some of these, such as dishwashers and home freezers, show very strong growth trends, and should be of increasing importance in sustaining the demand for consumer durables. Others, such as refrigerators and radios, will depend increasingly on the replacement market, rather than sales to new owners.

It should be emphasized that this evaluation of the demand for consumer goods, as well as the estimates of demand in other sectors of the economy, is an initial one, precluding important changes in private and public economic policies. In its policy discussion later on, the Council will indicate some changes in policy designed to augment some types of demand so that the total demand may equate with maximum production.

Table 13.—Household appliances in use and degree of saturation, January 1953

<table>
<thead>
<tr>
<th>Appliance</th>
<th>Number (millions)</th>
<th>Percentage of wired homes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Air conditioner (room)</td>
<td>0.5</td>
<td>1.3</td>
</tr>
<tr>
<td>Cleaners, vacuum (floor)</td>
<td>25.1</td>
<td>59.4</td>
</tr>
<tr>
<td>Dishwashers (electric)</td>
<td>1.3</td>
<td>3.0</td>
</tr>
<tr>
<td>Dryers, clothes (electric and gas)</td>
<td>1.5</td>
<td>3.6</td>
</tr>
<tr>
<td>Food waste units</td>
<td>1.4</td>
<td>3.3</td>
</tr>
<tr>
<td>Freezers (electric)</td>
<td>4.9</td>
<td>11.5</td>
</tr>
<tr>
<td>Fryers</td>
<td>37.9</td>
<td>89.6</td>
</tr>
<tr>
<td>Radios</td>
<td>43.7</td>
<td>96.2</td>
</tr>
<tr>
<td>Refrigerators (electric)</td>
<td>37.8</td>
<td>89.2</td>
</tr>
<tr>
<td>Televisions (electric)</td>
<td>19.8</td>
<td>46.7</td>
</tr>
<tr>
<td>Toasters</td>
<td>10.0</td>
<td>70.9</td>
</tr>
<tr>
<td>Washers (electric)</td>
<td>32.2</td>
<td>76.2</td>
</tr>
</tbody>
</table>

Note.—All figures, except those for radios, are based on 42,306,600 domestic and farm electric customers. Radios are based on 45,404,000 total homes. Percentages computed from unrounded data.


To review the consumption prospects: If, as we have assumed, the level of economic activity should remain high, and if there should be no change in basic private and public policies (specifically, if taxes are reduced as provided by present law), disposable income should increase considerably. The saving rate will no doubt fluctuate as it has in the past, but there is no clear evidence to project an important shift in either direction. The saving rate could be expected to decline, at least temporarily, with a decline in incomes. But with generally high and rising incomes, and no change in private and public policies, as we have assumed, a decline in the saving rate large enough to provide a substantial offset to declines (or absence of growth) in expenditures elsewhere in the economy does not appear to be likely. One reason for this is the contractual character of many of the methods of saving, including payments on home mortgages, insurance policies, and instalment loans, and the relatively high volume of consumer credit outstanding. On the other hand, the market for consumer goods appears to be sufficiently buoyant so that a substantial increase above the relatively high 8.6 percent saving rate in the last half of 1952 also appears to be unlikely. Consumption expenditures,
therefore, on these assumptions, would probably keep in step with the gain in disposable income, but a greater than proportionate rise could not be counted on as a certain source of additional demand.

**The composite longer-run outlook**

The foregoing preliminary analysis of prospects is not a forecast of what is going to happen. As indicated earlier, it is merely a first approximation, designed to provide a starting point for further analysis of the steps needed to assure optimum economic stability and growth. The foregoing sector-by-sector analysis does not indicate the source of the 10–12 billion dollar annual increase in demand and in real output required for such stability and growth between now and 1955. Moreover, when the economy is viewed as a whole, it is clear that if a substantial deficiency in demand should in fact occur in one sector, and not be offset elsewhere, the interaction of this sector upon others, and in turn the effect of the total on each, could produce a much greater shrinkage in total demand than a sector-by-sector review suggests.

This analysis might seem to strike a note of pessimism. Yet the Council believes that, while real problems are visible, the high objective of uninterrupted economic stability and growth is attainable if proper and adequate adjustments in private and public policies are made. We believe that action taken in time to bolster up limited areas, where the danger of insufficiency of demand seems most likely, or to develop alternative sources of demand, can forestall the spread of the danger. And since it is easier to deal with a limited shortcoming than with one which pervades the entire economy, and certainly easier to act when the economy as a whole has great momentum forward than to lift it out of a pronounced general decline, there is high promise that the prompt application of sensitive private and public policies can maintain the forward momentum. They can limit the deviations from maximum employment and production to the mild undulations implicit in a flexible and dynamic economy. The quantitative analysis thus far undertaken has been designed to make concrete the treatment of the following basic problem: What policy adjustments—both private and public—will enable the Nation to close the moderate gap between the sum total of the trends depicted above and the requirements for fairly steady growth toward a 375–380 billion dollar economy by 1955?

*Separate note by Mr. Clark*

Many fluctuations will develop within our free, erratic economy during the next 3 years, but I am not able to see changes in business conditions which would bring about a recessionary trend threatening enough to require new counterdeflationary action by the Government. Therefore, I do not join in the analysis and policy discussion in chapters III and IV.

Continued Government expenditures for goods and services upon the planned mobilization scale will, in my opinion, support a fully employed economy. If business slows down, the policies adopted during the past 20
years should bring about an early reversal of the downward trend, as they did in 1949, without any additional action by Government.

If trouble develops in the economy by 1955, it will be due to conditions, international or political, which are outside the ordinary processes of the domestic economy, which cannot be foreseen now, and which will not be cured by the kind of supporting policies discussed in chapter IV. (End of separate note by Mr. Clark.)
Chapter IV. Needed Policies for Sustained Prosperity

The General Nature of the Adjustment Problem

The foregoing needs and prospects analysis raises the possibility that, some time within 2 or 3 years beyond the horizon of the immediate outlook, the predominant economic risks to be counteracted may be deflationary rather than inflationary. And while the preceding analysis offers some clues regarding offsets, further interpretation is desirable before coming to policy issues.

The size of the problem

While the problem ahead has been identified, the discussion thus far has not measured its size. For there is inherent in the economy one set of forces which would tend to aggravate a deflationary problem if it first emerged in one sector. And mostly in consequence of relatively recent changes in our institutional structure, there is another set of forces which would tend to cushion the effects.

Cumulative aggravating forces. The first working assumption, upon which the foregoing analysis of component-by-component prospects has been based, is that incomes will be generally high, markets healthy, and business conditions prosperous in the 3-year period ahead. The prospects for private investment and consumption which have been identified rest heavily on this assumption. But the total prospect into which this piece-by-piece analysis adds up may challenge somewhat the underlying assumption itself. For while this first approximation of the adequacy of demand does not seem to indicate a large deficiency, it does indicate some slackness in markets, some shortfall from full employment incomes, and an increase in unemployment to an unacceptably high level. Both reason and experience tell us that this kind of situation, if left alone, could degenerate into a far more serious deflationary spiral. Although reflecting investor and consumer assumptions of high prosperity, when the components of demand fail to add up to a total which justifies such attitudes, businessmen and consumers speedily bring their assumptions into line with reality. And if this causes a contraction of investment and consumption still further below needed levels, total demand is further weakened, and a down-spiral may be on its way.

This danger could be greatly accentuated by a bunching of whatever declines are in prospect. If moderate declines in national security spending, plant and equipment expenditures, housing, and other items, should be
spaced out over a considerable period, the effect might not be serious. If such declines should be more or less simultaneous, the result would be more than additive. One area of weakness would aggravate another.

Reductions in investment tend to bring reductions in employment, incomes, and consumption. Then shrinking profits can compound into greater losses of income by inducing both investment declines and wage cuts. Certain kinds of price reductions can be healthy, but prices which go into an out-of-control tailspin frighten buyers away rather than bring them to market, and accelerate the collapse. And finally, all of these mechanisms, and others, can be speeded along their destructive paths by contractions of credit or the collapse of financial institutions.

*Sustaining institutional dampeners and shock-absorbers.* The fact that a variety of forces in the American economy can magnify the impact of what might otherwise be a moderate or even minor discrepancy in total demand does not have to be belabored. Certainly it would be foolhardy to conclude that a cumulative economic decline in the United States is no longer possible. The risk, however, is much less than it was a generation ago, and the tools to deal with it are vastly superior.

Since World War II, the United States economy has shown a remarkable capacity for unleashing the new demand forces needed to sustain a growing total demand when previous front-runners have fallen back. Much of this buoyancy—though not so much as sometime ascribed—undoubtedly has been the work of demands accumulated during the war, and of exceptional expenditures associated with the international stresses of the postwar period. Nonetheless, this record of recent resiliency does justify our facing the period ahead with more confidence than would have been possible in the twenties or thirties. Specifically, it directs attention to a number of recent institutional changes which, taken as a whole, provide arrestors to the kind of cumulative shrinking of demand just indicated.

As the Council has discussed in earlier Reviews, a number of “built-in stabilizers,” such as unemployment compensation, farm price supports, and a progressive tax system have become commonplaces of public policy. The expanded fiscal role of the Federal Government increases the amount of spendable income which the progressive tax system releases to the private economy when before-tax incomes fall. And if Federal expenditures can be counted as a relatively firm element of demand, their higher level makes their stabilizing influence far greater than it was prewar. Other significant braking mechanisms have developed in the private economy. The 1949 recession suggested a willingness on the part of consumers, in the face of moderate declines in income, to resist declines in living standards by cutting their saving rate rather sharply. Also during the 1949 setback, the increased strength of organized labor, coupled with more far-sighted business policies, made for a minimum resort to wage and payroll cutting—two of the swiftest engines of deflation in the past. In addition, the pronounced business trend during the postwar period toward longer-run capital planning and budget-
ing based on long-run market projections probably has made private investment somewhat less sensitive to short-run market fluctuations.

The resistance of our monetary and credit institutions to deflationary collapse is far greater than it was only a couple of decades ago. Our securities markets are less susceptible to influence by purely speculative factors, and the banking system is greatly strengthened against failures and rapid monetary contraction. While the monetary system often initiated or aggravated recessions in the past, in the future it can be expected to be at least neutral and perhaps positively stabilizing.

More profound than any of these specialized changes, and in part the consequence of all of them, there has taken place during this generation a broader distribution of national income among families and among functional economic groups. There is still room for debate among economists as to whether this trend has not proceeded far enough, or whether it has proceeded too far in terms of incentives to reward ability and to stimulate risk-taking. But there would be rather general agreement that the current and prospective distribution of income, under our free institutions, is more conducive to a fairly steady rate of economic growth than the conditions of income distribution which prevailed two or three decades ago. The concurrence on this point may be almost as important as the changes in the income structure which have taken place; in fact one of the happiest omens for the future is the increasing realization of the relationship between mass consumption and mass production on the part of those who make the basic decisions within the private economy.

**Cumulators versus arresting forces: the net effect.** While the institutional changes just indicated have reduced the economy’s susceptibility to deflation, it would be easy to rely on them too heavily. Although their existence probably has contributed to the climate of business and consumer confidence which has stimulated the emergence of new elements of demand during the postwar period, they are not essentially recession-preventing or recession-reversing forces. Their direct effect is only to slow or check a decline once it starts. Also, this new institutional apparatus does not yet constitute a rugged enough set of brakes to set any sure limit on a major downturn. It is only certain to retard a decline. If the basic deficiency of demand were large and nothing remedial were done, or if the traditional accelerators should begin to feed on a growing and then rampant deflationary psychology, eventually the stabilizers would prove to be feeble in proportion to the need, the brakes would wear thin, and “bottom” might turn out to be almost as far down as it used to be.

Thus, our new institutional safeguards are no substitute for positive anti-deflation policy. But beside mitigating hardships while their effectiveness lasts, they do—and this is supremely important to successful policymaking—give us time. One of the tragedies of many past business downturns has been the suddenness and sharpness with which recession has struck. The plunge often was well under way and gathering speed before
counter-measures could be devised and made effective. In this respect the economy is now better off. If the problem ahead should be that hypothesized above, our institutional apparatus should provide a reasonably adequate interval for diagnosis and decision. And the effectiveness and timeliness of private and public policy-making may largely determine whether the cumulators succeed in magnifying, or the arrestors in minimizing, any developing weakness in total demand.

The primacy of private adjustments

The problem under study has been identified simply as a possible shortage of total spending emerging within the next 2 or 3 years. An analysis of workable offsetting adjustments, however, must be more specific than this. It scarcely can be content with the principle that any additional demand will do. It is necessary to survey a variety of relatively specific policy courses, and to decide on grounds of desirability and feasibility what relative emphasis they should be assigned. In doing this, it will be helpful first to formulate certain broad priorities for guiding policy choices. Two such matters of general priority will be suggested, one having to do with the choice between public and private measures, and the other concerning our comparative needs for investment raising and consumption raising.

A dollar spent by private hands is not, by definition and regardless of circumstance, a more virtuous dollar than one spent out of the public treasury. However, the country has a general preference for private economic adjustments rather than public policies which expand the economic role of government. The Council shares this preference, on general grounds of dynamism, flexibility and free-wheeling. This preference is likely to be especially pronounced in the period after a large defense acceleration, during which it has been necessary to operate more elaborate and direct economic controls than Americans like and when, under the relentless pressure of national security needs, the Federal budget has run at unprecedentedly high levels for peacetime or even semi-peace-time conditions. If, on top of this, an incipient deflationary problem brought immediate and substantial resort to additional Federal spending programs, the difficulties of readjusting at any early date to a level of Federal activity more in line with the country's desires would be correspondingly magnified. Finally, if we adhere to the present national security program, and if present tax laws are followed, the outlook already is for deficits in the next 2 or 3 fiscal years which, although reasonably moderate in comparison with the size and strength of the economy, are nevertheless a source of legitimate concern.

The present analysis therefore recognizes, for a problem of the scope projected, a general preference for solutions which rely mainly on private rather than public policy. It also recognizes, however, the risk of relying solely on such actions and the necessity of taking stock of what supporting public policies will be available.
The needed emphasis on consumption

A current or prospective deficiency in total private demand might, depending upon circumstances, call for primary emphasis on either consumption-stimulus or investment-stimulus. The period ahead, if it should have the characteristics suggested here, will call for the former shading of emphasis. This conclusion, in which many other analysts seem to concur, does not reflect any “prejudice” against business investment. Consumption is, of course, the principal objective of economic activity. But conversely, the rapid economic growth which supports increasing consumption over the long run also requires high and rising rates of business investment. The emphasis upon consumption is simply a reflection of recent relationships between the two principal components of private demand, is meant to apply only to the 3-year period under consideration, and during that period is believed to reflect the best interests of business itself. It should be noted that, after mid-1950, the Council placed even more emphasis upon expanding certain types of business investment than did many members of the business community, and that the Council also placed more stress upon restraint of consumption than many others did.

Before proceeding to a more detailed analysis of investment-consumption relationships, two side notes should be inserted. In the first place, in discussing the balance between investment and consumption, the following paragraphs deliberately by-pass the subject of “investment” in housing. The latter, so far as the demand for the products of industrial capacity is concerned, is more properly treated in connection with the consumption side of the balance. It is separately discussed later on in this Review.

Secondly, the following discussion may seem to overlook the possibility for demand stimulation in the field of net foreign investment. But even under the most sanguine assumptions, the scope for adjustment in this sector is small in comparison with possible demand needs of the domestic economy. And more important, the United States’ international economic policy, of which our net foreign investment will be partly the resultant, should not be shaped primarily in the interests of general domestic stability and economic growth. Regarding these objectives, its direct impact in any case can be only marginal, although with respect to the Nation’s vital objectives of international political stability and free world strength its international economic policies may be all-important. Because these issues might be distorted and would be unduly submerged in the present analysis, they are treated separately in chapter V of this Review.

The investment-consumption balance and sustainable business investment rates. Both consumption and investment can grow continuously in an expanding economy, if they grow in a balanced relationship with each other. But there is a limit to how far either investment growth or consumption growth can outrun the other without pausing for the laggard to catch up. Eventually, if investment runs ahead for a time, a new balance must be struck between the newly expanded productive capacity which it creates
PERSONAL CONSUMPTION EXPENDITURES

PER CAPITA CONSUMPTION EXPENDITURES
1952 PRICES

CONSUMPTION EXPENDITURES AS PERCENT OF DISPOSABLE INCOME

CONSUMPTION EXPENDITURES AS PERCENT OF GROSS NATIONAL PRODUCT

SOURCES: DEPARTMENT OF COMMERCE AND COUNCIL OF ECONOMIC ADVISERS.
and consumption expenditures. If, in the absence of such an adjustment, a weakening in total demand is forestalled temporarily by an additional step-up in new investment, the underlying problem is only postponed and deepened.

Certainly it is true that the years since 1945 have witnessed a varying but unbroken investment boom—a boom, it should be emphasized, which, in the broadest terms, has been admirable and needed. The Nation entered this period having suffered a private investment famine, first in the thirties and then during the war. Capacity for civilian production was thoroughly inadequate to satisfy the new income levels achieved during the war, and business proceeded to expand it at a very high rate. Because of the very fact that this ratio of new investment to the total economy represented the reduction of a previous shortage as well as growth, it was unlikely that it could be maintained indefinitely.

And then on top of this postwar recovery in civilian capacity, the post-Korean mobilization program has laid on an accelerated rate of defense-related investment. Meanwhile, although consumption levels since 1945 have been high, total real per capita consumption has increased very little. In relative terms, as a percentage of disposable income, consumption was not extraordinarily high in the postwar pre-Korean period, despite the fact that it too was subject to the additional stimulus of accumulated shortages. (See chart 28.) And as a percentage of total production, consumption held fairly steady in the neighborhood of 69 percent up through 1950, and then, under the joint impact of the security program and a higher savings rate, tumbled to about 63 percent in 1951 and 1952—the latter at a time when fixed business investment as a percent of total output remained at or somewhat above its high postwar pre-Korean rates.

It would be dangerous to try to identify any single ratio between private investment and consumption that would be uniquely compatible with a balanced economic growth at some particular annual rate. However, the rough comparisons just indicated seem to justify a presumption that some relative gain in consumption sooner or later will be necessary. And various closer, but still not exact, analyses of the relationships between the economy's stock of capital equipment and such variables as gross output and the man-hours of labor employed seem on balance to confirm this impression.

*Stimulating investment via consumption.* The net conclusion that the Council draws is certainly not that, to avoid slack demand during the period ahead, encouragement of investment is to be avoided. Some additions to investment beyond the prospects outlined earlier are to be hoped for and, as indicated in the discussion of policy below, sought by positive measures. The conclusion is simply that if a large increment of private demand is needed by 1955, it is most unlikely that the bulk of it can be achieved in the form of additional private investment. And even if by some quirk of circumstance it could be, it might well be an unhealthy adjustment, simply postponing further the day of reckoning.
The same considerations lead back to a very familiar point—one which recent business surveys have often uncovered: A vigorous growth in consumption may not only be the primary requisite for a successful adjustment in the economy as a whole; it may also be the most effective means under present circumstances for stimulating additional investment itself. Particularly under the longer-run capital budgeting practices which many businesses have adopted, business investment is heavily dependent upon the prospects for the scope of markets—perhaps even more so, within limits, than upon the short-run prospects for profit margins. In a very real sense, a reasonable policy emphasis upon consumption raising may be the best single course that can be devised for supporting and strengthening investment.

The investment-consumption balance and price-income relations. There is a price-income side to the consumption-investment story already outlined. Broadly speaking, the economy may be thought of as including three groups of income receivers—businesses, consumers, and government. Government, in turn, gets its income from businesses and consumers, for the most part via taxes.

A rise in prices relative to wages, other things being equal, increases before-tax business earnings relative to before-tax personal income. A shift in this direction tends to favor investment relative to consumption when the general business outlook is good; conversely, a rise in wages relative to prices tends to favor consumption—unless there is an offsetting change in taxes. If business taxes rose at the same time that before-tax business earnings increased, for example, business would not keep its relative gain of income from consumers; it would simply serve as a channel for transferring that income to government.

If there is need for an increase in consumption relatively faster than investment—as it now appears there will be during the next few years—a variety of income adjustments might support such an adjustment in expenditures. Some would involve a direct shift of spendable incomes from government to consumers, via either consumer-oriented tax reductions or increased government transfer payments to individuals. But another method—and the one which lies within the province of private price, wage, and other income adjustments—would involve a relative shift from before-tax business incomes to consumers' incomes, via either wage and salary increases or consumer price reductions.

If such a shift were made in the absence of parallel tax adjustments, it would mean, of course, some reduction of after-tax profit margins (although, as is emphasized below, not necessarily of dollar profits in the long run). If it were coupled with business tax reductions, it could simply mean a shift to consumers of income which previously had been going to government.

Table 14 shows that the increases in real disposable personal income in the postwar period have been relatively small, and suggests the need for improvement. In this connection it is interesting to note chart 29, which indicates that during the period over-all, contrary to the common impression,
Table 14.—Indexes of gross national product, personal consumption expenditures, and per capita disposable personal income, constant prices: 1

[1946=100]

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross National Product</th>
<th>Personal Consumption Expenditures</th>
<th>Per Capita Disposable Income</th>
</tr>
</thead>
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<tr>
<td>1947</td>
<td>100</td>
<td>103</td>
<td>95</td>
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<td>104</td>
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<td>115</td>
<td>103</td>
</tr>
<tr>
<td>1951</td>
<td>121</td>
<td>112</td>
<td>103</td>
</tr>
<tr>
<td>1952</td>
<td>124</td>
<td>114</td>
<td>104</td>
</tr>
</tbody>
</table>

1 Indexes based on data in 1952 prices.
2 Estimates based on incomplete data; Council of Economic Advisers.
Sources: Department of Commerce and Council of Economic Advisers. (See appendix tables B-2 and B-10.)

average hourly earnings in manufacturing, adjusted for consumers' price changes, have not risen faster than the economy's general productivity gains, but instead apparently have lagged significantly.

Chart 29

Changes in Over-all Productivity and Manufacturing Earnings

Since World War II, average hourly earnings in manufacturing have not increased as rapidly as output per man-hour for the economy as a whole.

INDEX, 1946 = 100

TO TOTAL GROSS NATIONAL PRODUCT, 1952 PRICES, PER MAN-HOUR FOR ALL EMPLOYED PERSONS.

SOURCES: DEPARTMENT OF LABOR AND COUNCIL OF ECONOMIC ADVISERS.
However, while study of data on corporate profits (see appendix tables B-34 and B-38) and other business earnings confirms the need for some relative shift of before-tax income from business to consumers, it raises doubts as to the extent to which such an adjustment can feasibly be made in the absence of tax reductions. Before the last half of 1951, after-tax corporate profits were generally above historical levels. But recently, the ratios of after-tax profits to sales have for the most part been significantly below earlier postwar levels. It is not very likely that many businesses whose after-tax margins currently are below the present average will narrow them further. On the other hand, a general effort to return these net margins to their earlier and much higher levels, at a time when a shift toward consumption is needed, would be unfortunate and self-defeating.

The implications are clear: (a) The room available for general transitional price and wage adjustments may be partially dependent upon business tax adjustments; and (b) in the absence of such tax adjustments, an opportunity for helpful price and wage adjustments will center mainly in those industries and firms where present profit margins are relatively favorable. Roughly speaking, in the manufacturing sector this opportunity seems greatest—in terms of product—among durable goods producers, and—in terms of size—among the largest corporations.

Workable Lines of Policy

Private price and wage policies

Turning now to the various lines of policy which are available, it is logical first to take up private price-wage policy, because it is perhaps best attuned to the broad preference priorities previously established. Adjustments in price-wage policy afford the greatest amplitude for private action as an alternative to public compensatory action.

It is possible that the development in business and labor circles of an effective and coherent price-wage policy can raise real consumption several billion dollars annually. Such private "policy," it should be noted, is by definition the province of decision-makers in the so-called "administered price" sectors of the economy. It would be imprudent to rely solely upon this answer to the deflationary risk—for one thing because, as the following analysis suggests, the scope of the opportunity for helpful price and wage adjustments may in turn depend partly on what happens to business taxes. Yet the contribution which private price and wage policy can make should not be overlooked.

Needed wage adjustments. In line with the above analysis, the specific wage and price considerations of a longer-run character which the Council wants to suggest may be set down as follows:

In the case of wages: First, in the event of a weakening in demand, wage cutting should be avoided. While such an adjustment may temporarily ease the situation of an individual firm, it can set off a dangerous chain reaction.
Second, during the period ahead, wage adjustments should continue to do their long-run job of helping to distribute the increased incomes resulting from improved productivity. As was said in the Economic Review of January 1950, with a growing potential for national output, the only way to translate this potential into actuality is to distribute more goods. If the price level is to be kept reasonably stable when the economy is in balance, then the increasing purchasing power necessary for expanding markets must come mainly in the form of consumer incomes rising in accord with improved productivity. And since wages constitute the bulk of personal income, the preferable general formula—once wages, prices, and profits are in a workable relationship—is for money wages to increase with productivity trends in the whole economy.

Third, while this long-run wage policy should be continued and more firmly established, it would be impractical and undesirable generally to strive for average wage increases in excess of productivity gains. The aggressive seeking of large wage increases under conditions of market weakness or threatening weakness would prompt abnormal industrial strife. And if won, increases in excess of productivity gains would subject many businesses to extraordinary cost pressures at a time when these would be most discouraging to new business activity. Wage policy, by and large, should stick to the job of helping to maintain the price-income balance and thereby the consumption-investment balance. In the price-wage sector, it is primarily the function of prices to help correct the balance. These general principles may have exceptions in some industries or business situations.

**Needed price adjustments.** The present challenge to managers to develop self-enlightened merchandising programs which also serve the needs of general stability, is a very real one, and it is not remote. Instead this is one strand of policy which, in the coming months, can safely anticipate the problems ahead without any serious risk either to those who make the venture or to the economy generally.

If a substantial deflation of economic activity should materialize, lower prices sooner or later would be inevitable. The need is for those in a position to do so—and in a position where such action will do the most good—to choose deliberate, anticipatory, and selective price reductions and other forms of aggressive merchandising. This is a positive means of avoiding the general economic break which might be the consequence of cautious or standpat pricing. And this general recommendation can be somewhat particularized.

First, for a variety of reasons, the suggestion is directed especially at the manufacturers of consumer goods. Even under present tax rates, opportunities for margin squeezing exist in many consumer lines. This is evident from profit data, and is suggested by the recent weakening of many raw materials prices relative to manufacturers' prices. Among consumer goods, the opportunities for promotional price reductions and for expanding markets for new and improved products may be especially great in case of
consumer durables, although they do not end there. Moreover, the relatively stable character of distributors' percentage mark-ups tends to result in even greater absolute reductions at the retail level and thus bring about an added stimulus to buying.

Second, there is a need for more flexibility and willingness to experiment on the part of manufacturers. A high degree of conservatism, bred of a decade and more of sellers' markets—cautiousness in estimating demand elasticities, in estimating probable operating levels for price-making purposes, in adhering to stereotyped profit margin rules, and in experimenting with new products—may prove self-defeating. The scope of the demand for new or lower priced products can never be fully known in advance, but it can be explored.

Third, as long as the excess profits tax remains in force, for those manufacturers whose marginal tax rates are high and who at the same time can accept relatively minor reductions in after-tax margins, the tax provides a relatively costless and riskless umbrella under which they can experiment with promotional pricing and products aimed at untapped markets. Moreover, as implied earlier, if and when business taxes are reduced, it may be a mark of wise management to view the tax savings, not as a means for boosting margins back to earlier levels, but rather as an opportunity for developing markets via lower prices and product improvements.

To reemphasize, in conclusion, what was stated earlier, reductions in profit margins during the period ahead need in no sense conflict with a stable and indeed increasing level of absolute profits. In order to provide the needed growth in sales volume, a relative increase in the portion of national income going to disposable personal income seems necessary. In providing an increasing real volume of sales, margin reductions are far from being a dampener on profits. Anticipatory price adjustments tend, at the least, to prevent a fall in total profits with declining sales, and to stimulate the growth in the economy which is needed to improve dollar profit positions. Such anticipatory adjustments are far removed from the disorganized downspiral in prices which feed on themselves and contract rather than expand markets. Appropriately timed price changes should forestall rather than initiate this process.

Supporting public policies. Besides encouraging helpful private wage and price adjustments during the next 2 or 3 years, the Federal Government can help to make the economic environment more favorable for the kind of private adjustments which have been outlined.

First, if healthy wage adjustments are to help support the transition, it will be important that changes in industrial relations law do nothing to undermine the collective bargaining position or general morale of labor.

Second, Federal legislation may, to a significant degree, determine the effectiveness of retail price competition, and, as a result, the extent of the impact which promotional pricing at the manufacturing level would have on consumers. To a considerable extent in recent years, it has been the
aggressiveness of chain store, mail order, and department store merchandising which has kept a keen edge on retail competition. It is essential that the Government undertake a thoughtful review of its antimonopoly and market regulating policies to guard against any progressive blunting or weakening of competition in consumer markets.

Private investment policies

Promotional pricing and aggressive merchandising, by increasing sales and sales prospects, would themselves tend to react favorably on business investment. In addition, looking ahead toward 1955, private investment may be strengthened more directly by certain private and Government policies. The need is for positive and energetic search for new and expanding investment lines, for opportunities in the less developed regions in this country and abroad, and for the fuller exploitation of potential markets for existing products and services.

As chapter III has indicated, there are many growth possibilities which will open up in the next few years to the vigorous enterprise which has characterized the American economy more notably perhaps in the last decade than ever before. These fast growing lines, for which future growth prospects appear bright, include many newer ones such as man-made fibers other than rayon, plastics, magnesium, synthetic rubber, antibiotics, air conditioning units, television sets, combination washer-driers and other household equipment, and frozen foods. Many older lines such as aluminum, gypsum board, rayon, fertilizers, certain acids and other chemicals, and tractors are also growing rapidly. These promising prospects include, not only raw materials, capital equipment items, and both durable and non-durable consumer goods, but also a variety of services such as air freight and passenger business, motor courts, electric power, and telephone service. Other fast growing activities are quality improvements in established products such as power steering and automatic transmission mechanisms on automobiles, and electronic devices used to control industrial operations. Undoubtedly numerous other industries and products, now barely on the horizon of economic possibility, will move into the range of active business development within the next few years.

What may private business on its own initiative do to bring about the fullest realization of private investment opportunities, both for growth and stabilization purposes?

First, private business can maintain and expand the whole range of its activities which come under the heading of research and development. In 1951, some 1.2 billion dollars was spent directly by private industry for this purpose, with additional large amounts being spent on industrial and related research through Government. Many of the more progressive firms devote relatively high percentages of their sales revenues to research and accord research an important place in management.

Second, the practice already widespread among business leaders of programming investment several years ahead, often 5 to 10 years, might adva-
tageously be adopted more widely. With business generally in a strong financial position, this would serve to promote growth and stability at the same time. It permits more orderly financing, more regularized purchasing programs, and sets a condition for more stable and longer-term wage and other agreements with labor.

Third, more careful surveys might be made of the markets for present and possible new products and services. This would provide a firmer underpinning for both research and development and long-range investment planning. Again, many firms undertake this kind of analysis, but it could well be done more generally.

Fourth, existing business firms, especially those looking to the establishment of new plants or branches, as well as persons contemplating the formation of altogether new firms, would do well to examine carefully the prospects for their particular operation in some of the less developed areas of the country. Relatively rapid growth in population and incomes in the Southwest and the Far West, for example, mean better market prospects. In the old South, the momentum of the industrial development which has gained strength in recent years, plus the rapid increase in income, point to this part of the country as a desirable location for many types of business, operating at wage rates compatible with those in other areas. In the older industrial areas of the Northeast, especially New England, most strenuous private efforts are being made, and will have to continue to be made, to move from the older textile and shoe industries toward new and rapidly growing lines such as electronics, research services, electrical and machinery lines, among others.

While first reliance should be placed upon privately initiated action to strengthen investment, there are many Government measures which may be taken to encourage private investment, and which do not add much if anything to Government expenditures. First, basic research and experimentation carried out by Government can provide the technical basis for private investments. For example, technical and economic research in synthetic liquid fuels has reached the point where private investors are now actively interested in the establishment of synthetic liquid fuel plants. Second, credit guarantees of various sorts on the part of Government, such as in housing, provide a stimulus to private investment. As noted later, the terms on which such credit is guaranteed may be altered to encourage investment. Third, in certain instances, the extension of certain socially desirable Government regulations may, as a by-product, induce private investment. For example, State and city governments may require through ordinances that both municipal and industrial water pollution control measures be taken. Fourth, properly timed tax reductions, discussed subsequently in this Review, can be a potent force for maintaining investment—particularly under present circumstances, those which expand consumer markets.

The smaller business segment of the economy might be aided by a further
development of the program of the Small Defense Plants Administration, which already has done good work in helping small business to carry its share of the defense program, and by a strengthening of the various technical services offered business by the Department of Commerce.

More important than these specific governmental measures is the influence which the Government exerts upon the general business climate. That climate is the product of all these specific measures taken together, but it is something else besides. It resides in ever increasing realization that the objectives of business and of Government are mutual and compatible, that neither can succeed in the long run if the other fails, and that the instrumentalities for a working relationship between the two need to be continually improved. This problem can by no means be solved, although it may be reduced, simply by bringing businessmen, workers, or farmers into the Government; for when this is done, they become part of the Government and not a part of the private business community. The most important need, as the Council has frequently urged, is for a process of consultation between Government officials and private operators, based not upon a confusion of their respective and clearly different functions, but rather upon realization that each has much to contribute to the functioning of the other. The exploratory machinery thus far established at various levels of the Government for this purpose has been of considerable use, but improved machinery is necessary. More important than blueprints, however, is the need that those on all sides of the table take this effort more seriously and pursue it more diligently. In the final analysis, it is the only middle way between the danger of excessive economic instability and the danger of excessively centralized authority—quite aside from the fact that the former evil produces the latter.

Credit policy

Measures of general credit policy, which are generally thought of as instruments of stabilization, are highly regarded by some theorists as means of curbing inflation—assuming that the measures are applied vigorously enough; but they are held in rather low repute as antideflationary devices. The black mark put in the record because of their poor performance in the 1930's has not yet been erased. However, the first reputation is not unclouded, and the second is perhaps unjust.

General credit policy attempts to regulate the availability (and therefore necessarily the cost) of lendable funds, a steady yet appropriately flexible supply of which is essential to production in a growing economy. The first objective of credit policy is to assist production; stabilization is an associated purpose. This does not mean, however, that stabilization is not a highly important objective; it merely suggests that credit policy must be used with great discretion as an instrument of stabilization and must be heavily accompanied by other measures.

The prime role of credit in production is, of course, not to create demand, but to implement it; its job is to facilitate rather than generate. It is possible
for credit policy to achieve a victory over inflation by withholding funds from those desiring to buy, although such action may thwart the first objective of the credit mechanism. At the other extreme, in a deflationary situation, it is hardly to be expected that credit policy alone can arouse business from recession by making funds available to finance demands which do not exist.

It would seem, then, that the actions of general credit policy most effective in maintaining prosperity might be those taken, first, while the level of business activity is still high, or, second, at the very first signs of a recessionary development. The first situation requires delicate balance between restrictive actions which prevent speculative excesses, and the avoidance of extreme measures which might hamper production, as by holding interest rates at a level discouragingly high for long-range investment programs. The second situation requires the prompt liberalizing of credit while private demand is still strong enough to grasp the opportunity.

Much success in uncovering latent demand, or in making borrowing feasible and safe for larger numbers of persons, has marked the policies of reducing down payments, extending maturities, and the repayment of loans through amortization, for which the Federal Government should be credited with much of the leadership. Examples of this leadership are to be found in the housing and farm credit programs. The latter, in addition to pioneering new credit terms, have more effectively mobilized and channeled credit into agricultural uses, thereby cutting interest rates and other borrowing costs.

Furthermore, the insurance or guarantee of residential mortgage loans by the Federal Housing Administration and the Veterans Administration, and the guarantees by Government procurement agencies of loans to businesses with defense contracts under the Defense Production Act, represent another method of making credit more widely available, especially to the small borrower, and indeed benefiting borrower and lender alike.

It should be noted that, in about all of the examples cited, the improved loan services are offered to borrowers by privately owned institutions.

Very likely, considerably more could be done by these means to stabilize borrowing and private demand, and to stimulate business in the event of another recession. Some further liberalization of terms might be possible under the present programs, and consideration might be given to the feasibility of extending the insurance principle, with some lengthening of maturities, to consumers’ loans for the purchase of durable goods (beyond what is permitted under Title I of the Federal Housing Act) and to loans to small businesses.

**Tax policy**

In the discussion in chapter II of short-run policy issues, it was stated that general economic considerations favor the continuation of present tax rates. To lower taxes in 1953 would not only increase the budget deficit, but would make it more difficult to reduce taxes later on, when the economy will be
in the transition to a lower level of defense spending and could benefit most from tax reduction.

As individual taxpayers, we always welcome tax reductions at the earliest possible moment. But as members of the community, we should understand that the benefits of lower taxes sometimes prove illusory. In one set of economic circumstances, tax reduction will encourage larger total production, with more goods and services available for consumption and business investment. Under other conditions, the result may simply be more dollars competing for substantially the same supply of goods and services.

Apart from issues as to timing, there are important questions regarding the form which tax reduction should take. The executive departments and the Congress will be concerned with the problem of how tax reduction may be combined with basic improvements in the Federal tax system. For a time it looked as though the years immediately following World War II would provide the long awaited opportunity for an overhauling of the tax system, and several comprehensive studies were issued in the late war years with this objective in mind. In 1945, however, and again in 1948, tax reductions were made but there was no concerted effort to fit the tax reductions into an over-all plan for an improved tax structure. The present situation may be compared to that of the late war years, because of the indications that the next major revenue legislation will be a tax reduction measure. For important practical reasons, proposals for tax reforms meet with less resistance when they are combined with reductions for most taxpayers. If the pattern of tax reduction laid down in the present law is accepted without careful examination, the country would lose an opportunity to effect needed structural changes, some of which are long overdue.

**Economic effects of taxation.** The Council is particularly concerned that tax policy be used most effectively for the promotion of a high and stable economy. Yet we recognize that revenue programs must take into account a number of competing and sometimes conflicting objectives. Taxes are needed to supply funds to the Government, and the extent to which they exceed or fall short of expenditures determines changes in the public debt. The fairness of the distribution of the tax load is always an important factor to be considered, and also the ability of the Government to administer the revenue laws and the ease with which taxpayers can comply with them. All these considerations have a direct and important bearing upon the usefulness of tax policy as an economic instrument.

Taxes affect economic activity in two ways: (1) by changing the amount of money that taxpayers have at their disposal; and (2) by altering the complex of motivations that guide taxpayers’ decisions with respect to spending, saving, investing, and producing. In the preceding analysis of adjustments for maintaining economic prosperity, great stress was laid upon the need for measures to stimulate larger consumer spending. Is tax policy an effective instrument for this purpose?

Although almost any kind of tax reduction would contribute to larger
consumer spending, some kinds would contribute more than others. For example, a reduction in personal income taxes will ordinarily stimulate consumption more than a reduction of the same amount in corporate taxes. In the case of the personal income tax, the full amount of the reduction is placed almost immediately at the disposal of consumers. In the case of corporate taxes, the tax savings first accrue to corporations, which then decide whether to use the funds to increase dividends, reduce prices, raise wages, or add to retained earnings. As has already been indicated, it will be important over the next few years for corporations, by price reductions and other means, to channel into the support and expansion of markets the bulk of whatever tax reductions do occur. But it would be hazardous even to guess what proportion of a corporate tax reduction actually would reach the hands of consumers, or how quickly. It should not be overlooked that lower personal taxes, through higher consumer spending, indirectly channel funds into the hands of business.

A reduction in excise taxes also merits priority as a means of making additional purchasing power available to consumers. When goods are in ample supply, excise reductions will be followed in most cases by equivalent price reductions. Thus, consumers would be enabled to step up their spending, or saving, by approximately the amount of the tax reduction. Even if some part of the tax reduction first showed up in higher profits, some of the profit increase would eventually filter through to consumers.

Estate and gift taxes, on the other hand, probably have little effect on consumption. As a matter of equity, it is often proposed that these taxes be increased. This might be done at the same time that other taxes are being reduced.

The objective of stimulating consumption will be better served if tax reduction is distributed as much as possible in favor of consumer groups who are heavy spenders. This is usually interpreted to mean that the reduction should go more to low income groups than to high income groups, since the former spend a higher proportion of their earnings. Changes in the rates and exemptions for the personal income taxes may easily be designed so as to conform with this pattern, and excise reductions will usually benefit low income groups relatively more than others.

While favoring, during the period under consideration, reductions in those taxes which have the greatest repressive effects on consumer spending, the Council realizes that some taxes probably will need to be adjusted because of their adverse effects on incentives and investment funds, or for other reasons. Large corporations subject to the excess profits tax pay to the Federal Government either 82 or 70 percent of any increases in their earnings; conversely, the Government absorbs either 82 or 70 percent of reductions in earnings. Such high rates are tolerable during an emergency period of limited duration; they have no place as a permanent feature of a tax system which is designed to spur initiative and productive efficiency. Similarly, the high surtax rates paid by upper-bracket individual taxpayers
may also, in some circumstances, adversely affect investment incentives.

Other proposals meriting analysis include those for granting special tax concessions in order to encourage specific types of economic activity or to strengthen particular taxpayer groups. An example is the proposal to liberalize the treatment of depreciation deductions, on the ground that this would stimulate plant modernization and expansion, or the proposal to reduce taxes on income from foreign investments in order to encourage more investment abroad. Many tax recommendations are focused on the special tax problems of small business.

Such proposals, while deserving careful consideration, should be studied in the framework of the total tax program. Whatever their separate merits, their combined effect might be to make serious inroads on the tax base and make higher rates necessary in areas not granted favored tax treatment. Moreover, we must be careful that they do not conflict with the continuing objective of improving the tax structure in order to remove unjustified advantages to a few at the expense of everybody else.

Social security programs and other transfer payments

The incomes of many old, needy, handicapped, unemployed, and underemployed persons, who make up the bulk of the low income groups, are heavily dependent upon transfer payments by governments, i.e., expenditures which are not made for currently produced services or goods. The long-run expansion of protection in this sector of the community represents one of the Nation's broad purposes. It also represents the strengthening of groups whose needs require that they spend virtually all of their income for consumption.

The total transfer payments to the public made by the Federal Government, including social insurance, public assistance, veterans' benefits, and interest payments on the public debt, came to about 17 billion dollars in 1952, or 7 percent of total personal income. Not counting the interest payments, the remainder of some 12 billion dollars was paid to the aged, unemployed, indigents, veterans, and others who spend most of it promptly. State and local transfer payments increased this amount by 3 billion dollars. Many of these transfer payment programs fall into the "built-in stabilizer" class—payments under them would expand more or less automatically in the event of a downturn. Improvement or expansion of these programs can properly be included in the present roster of positive adjustment policies.

The label of "fixed income groups" when it is applied to transfer payment recipients is, as table 15 indicates, something of a misnomer. "Lagging income groups" would be more accurate. Since 1940, the index of average income of groups receiving public transfer payments has risen, but less than the index of average earnings of fully employed groups. While average payments to public assistance recipients and unemployment insurance payments, generally speaking, have kept abreast or ahead of increases
**Table 15.**—Indexes of per capita social security benefits and per capita earnings of selected groups, and consumers' prices

[1940 = 100]

<table>
<thead>
<tr>
<th>Item</th>
<th>1943</th>
<th>1946</th>
<th>1949</th>
<th>1951</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Consumers' prices</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Earnings per full-time employee:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Farm</td>
<td>262</td>
<td>330</td>
<td>354</td>
<td>376</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>164</td>
<td>176</td>
<td>216</td>
<td>250</td>
</tr>
<tr>
<td>Government</td>
<td>135</td>
<td>175</td>
<td>215</td>
<td>253</td>
</tr>
<tr>
<td><strong>Old-age retirement payments per beneficiary:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Old-age and survivors insurance</td>
<td>92</td>
<td>100</td>
<td>106</td>
<td>181</td>
</tr>
<tr>
<td>Railroad retirement</td>
<td>127</td>
<td>149</td>
<td>164</td>
<td>149</td>
</tr>
<tr>
<td>Federal civil service</td>
<td>100</td>
<td>100</td>
<td>113</td>
<td>122</td>
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<td>State and local government retirement</td>
<td>101</td>
<td>104</td>
<td>111</td>
<td>117</td>
</tr>
<tr>
<td><strong>Disability payments per beneficiary, veterans' program</strong></td>
<td>100</td>
<td>118</td>
<td>141</td>
<td>134</td>
</tr>
<tr>
<td><strong>Unemployment payments per beneficiary:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State unemployment insurance</td>
<td>131</td>
<td>180</td>
<td>196</td>
<td>200</td>
</tr>
<tr>
<td>Railroad unemployment insurance</td>
<td>156</td>
<td>197</td>
<td>222</td>
<td>181</td>
</tr>
<tr>
<td><strong>Public assistance payments per recipient:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Old-age assistance</td>
<td>132</td>
<td>174</td>
<td>221</td>
<td>220</td>
</tr>
<tr>
<td>Aid to dependent children per family</td>
<td>128</td>
<td>162</td>
<td>229</td>
<td>254</td>
</tr>
<tr>
<td>Aid to the blind</td>
<td>110</td>
<td>145</td>
<td>182</td>
<td>189</td>
</tr>
<tr>
<td>General assistance per case</td>
<td>114</td>
<td>163</td>
<td>208</td>
<td>194</td>
</tr>
</tbody>
</table>

1 Aggregate net incomes of farm operators plus wages of hired laborers divided by average farm employment.

**Note.**—Unemployment payments are based on average weekly figures, railroad unemployment on average daily, public assistance on December average; all other payments or earnings are based on annual averages.

**Sources:** Department of Agriculture, Department of Commerce, and Federal Security Agency.

in the cost of living, the retirement and survivor programs have not. Even more important than these trends, from the viewpoint both of family need and strengthening purchasing power, is the low absolute level of income which characterizes these groups. The average monthly payment to a single retired worker receiving old-age and survivors insurance is about $40, to a retired worker and his wife $70, to a surviving aged widow $36, and to a young widow with two children $94. The average weekly unemployment insurance payment is about $24, and average monthly payments for old-age assistance are about $45. By contrast, average weekly earnings in all manufacturing industries are about $70 per worker.

While the present social security system represents a major bulwark against social and economic hazards, and one which has been partially strengthened against the tide of inflation in recent years, there obviously is large scope for needed improvement. In the case of unemployment insurance, extension of coverage, raising of weekly benefit amounts, or increasing the number of weeks for which insurance payments could be made, are improvements in the unemployment insurance system often suggested during recent years which would increase payments, and hence consumer expenditures, in event of a recession.

There is also a less obvious automatic antirecession aspect to old-age insurance payments. In the event of a downturn, some of the 1.4 million persons entitled to such payments but not receiving them because they have well-paid employment would undoubtedly leave their jobs and apply
for benefits. Half a billion dollars of payments might be added in this event, or possibly twice this amount in a severe recession. Even without such a recession-induced expansion, it is estimated that under high employment conditions old-age and survivors insurance payments will rise from about 2.9 billion dollars in 1953 to 3.3 billion dollars in 1954. In addition, the provision of disability benefits and of hospitalization benefits for the insured old people and other beneficiaries would act to increase consumer expenditures.

Federally supported public assistance payments and "general assistance," the catch-all category now entirely financed by States and localities, provide minimum income for those needy persons and their dependents not covered by other programs, and in some cases supplement old-age insurance payments. Although the number of persons receiving public assistance is expected to decrease during the years ahead as more and more of the burden is taken over by old-age insurance, still in a general recession it would undoubtedly be necessary to increase transfer payments made through these programs.

Agricultural policies

The Council has frequently noted that, despite long-term gains which have raised agriculture out of its forlorn position in our economy, the sound objective of "parity for agriculture" has not yet been achieved. This is particularly true now because agriculture has not shared proportionately in the great and continuing economic advance during the past year or so. The "farm problem" in the critical degree that it existed for a decade or longer after World War I, is not yet with us and never again should be. But there are already signs that, regardless of whether one believes that farm price supports should be higher or lower or different, many vigorous things will need to be done on a broad front to enable the farm population to have a standard of living and a degree of opportunity closer to that of other groups than it has thus far been.

The problem is particularly acute for 1.7 million farm families who have long been living at seriously depressed levels, some of them tenants, many trying to work very poor land, and all of them especially subject to such problems as inability to get credit, unfamiliarity with newer farm methods, and lack of needed equipment. Basically for human reasons, but also because of the desirable general economic effect of raising the purchasing power of one needy group, efforts to improve productivity and incomes of the low income farm families should be strengthened.

The issue is a very complex one. It involves not only price and income policy, but also questions such as export markets for farm products, and the still broader question of the evolving pattern of relationship between the part of our human and other resources devoted to agriculture and those devoted to other pursuits. A shift in this pattern is certainly taking place as a long-range trend, and attention should be given as to how it may
be accomplished without undue hardship. More generally, the improve-
ment of living conditions in many of the farm areas depends upon develop-
mental programs supported by public funds, and also upon industrial
development, because the shift from agriculture to industry need not be
identical with the geographical shift of population. Some things different
from those now being done may be required to deal with the farm problem.
But whatever they are, they will offer abundant opportunity to contribute
both to general economic stability in the next 2 or 3 years, and to long-run
improvement in the economic position of farmers.

Housing policies

As noted previously, expenditures on new housing construction in the
absence of new private and public policies may be lower in 1955 than in
1952, chiefly because of the progressively smaller number of new households
expected to be formed between now and 1955. This drop in housing might
be moderate if economic conditions in general remain brisk. However,
it could be large. The continuing active desire to move to the suburbs, plus
the high proportion of old, less advantageously located houses, especially
in the presence of high incomes generally, indicate a large latent replace-
ment demand for housing which can be made effective during the coming
years. Further preparation and progress in this segment of the economy
are essential. Whatever additional amount of housing may result will fall
well within the Nation's needs.

First, emphasis in policies and programs to maintain a sufficient level
of housing demand should be given to private actions. Reduction in sales
prices or improvements in quality would undoubtedly broaden the market
for new housing. Cost-reduction innovations, such as the development
of more efficient building techniques, new materials, and improved financ-
ing arrangements, are important avenues to lower prices. Such innova-
tions require constant research. Moreover, it would be in the builders'
interest to pass the benefits of increased efficiency along to the consumer
in the form of price reductions. More attractive mortgage terms, especially
lower down payments and longer maturities, are another method for in-
creasing sales. In addition to the market for new homes, a large demand
exists for additions and alterations in existing houses, to take care of
numerous growing families. Demand from this source will probably in-
crease, and it should be served actively. Financing could be assisted by
increased use of open end mortgages, which provide for more economical
financing of improvements.

Second, these private actions can be supported and facilitated by Gov-
ernment assistance of various indirect types which do not involve much
increase in Government outlays. Government can assist industry in ac-
complishing cost and price reductions by supporting housing research proj-
ects directed toward reducing construction costs, improving quality, and
solving financing problems. The volume of housing construction is most
sensitive to mortgage credit terms, over which during the past two decades
the Government has had an increasing degree of influence. There is evi-
dence that the easing of terms on Government-assisted mortgage credit in
1949 was a factor in the early resumption of activity in the housing industry
during a general though brief business recession. With the recent relaxa-
tion of Regulation X, terms now available for FHA-insured and VA-guaran-
teed loans are, with minor exceptions, as liberal as permitted by law. Thus,
having already in a sense “used up” this instrument for stimulating demand,
any substantial further liberalization of Government-aided mortgage credit
would require new legislation. To make further liberalization of terms
actually effective, it would probably be necessary for the Government to
stand ready to purchase such mortgages to the extent that private funds
were not available. This could be done by extending and enlarging the
authority of the Federal National Mortgage Association to purchase and
make advance commitments to purchase privately originated mortgages.
Another method is direct lending of Government funds to home purchasers,
such as that now done on a limited scale by the Veterans Administration.
Also, extension of the loan insurance principle to new forms of financing,
and to higher quality (and cost) housing, would provide a means of
tapping private funds for housing investment at more liberal terms. It
should be noted, however, that Government credit aids cannot by them-
selves alone directly create housing demand unless individuals actively wish
to buy more houses. Credit aid is a favoring but passive condition within
which private decision and action are encouraged. If a downward tend-
cency commences to spiral steeply, such credit aid may have limited effect.
But with no such spiral development, or if action can be timed in the earliest
phases of a downward tendency, credit easing and assistance can be im-
portant in maintaining housing demand.

Third, there is a basic need for a large expansion of the locally operated
low-rent housing and slum clearance program, assisted by Federal contri-
butions. No need has more general recognition, and no need has been
more carefully analyzed by repeated congressional studies and more fully
supported by general enabling legislation.

The provision of decent housing for those who now live in urban and
rural slums is not primarily an antirecessionary measure. It is an essential
part of the fulfillment of an American standard of living which is well within
our current productive capacity. Basically, in accord with fundamental
congressional policy already established, the slum clearance and low-rent
housing program should be conducted on a long-range basis, in sufficient
volume to liquidate the preponderance of bad housing within a decade.
To bring it up to this level would so many times multiply the recent and
current rate of construction in this field, that the question of accelerating
this program merely to maintain economic stability and growth is largely
academic. And for much the same reason, any argument that this program
should be held at its current low levels until the signs of economic recession
appear is without foundation. Nonetheless, the purely economic argument for the expansion of this program is also powerful. There are few programs the expansion of which would so thoroughly unite the ultimate objective of defensible living standards for the whole American population with the intermediate objective of economic stability and growth.

The problem of an adequate supply of low-rent housing and the problem of urban redevelopment and slum clearance are inseparably connected. Both have been unduly retarded; and it is hard to say which retardation has been the primary cause and which the primary effect. Decaying residential areas at the core of our cities cannot be cleared until decent housing is provided for their residents at costs within their means. And without the clearance of these areas, low-rent housing cannot gain the general popular support required for its success, nor can a balanced program of municipal redevelopment be carried forward successfully.

The proposition that for a time we may experience a decrease in the new rate of family formation is of real but limited significance in this connection. Population growth is important, but it has not been the chief impetus to our unrivaled material progress. That impetus has come from the irrepressible urge to lift the general standard of living, which has no final frontiers. And these frontiers are not even in sight with respect to housing, one of the most precious of all commodities in its effect upon family life, where for millions of families the absolute standard and the rate of progress has lagged far behind what we have accomplished in other fields. In few fields of economic enterprise can we look for so large an addition to the expansion of useful economic activity as in the case of improving and enlarging the housing supply under the impact of a sufficiently broad and comprehensive program—a balanced program serving all income groups with a good standard of housing.

Public developmental and service programs

In a strong, growing economy the main role of public development activities is to contribute toward providing such basic services as health, education, transportation, resources conservation, and public welfare, without which neither growth nor stability can be sustained. The several levels of government share in these responsibilities. In most instances, private individuals and organizations are already doing a significant part of the job.

Development and welfare needs. Needs for developmental and welfare outlays are large when viewed against recent expenditures, or against standards of service accepted as desirable. Chart 30 shows in constant dollars the public expenditures since 1939 in a number of development programs. It also presents several alternative patterns of expenditures for 1955, based on different assumptions.

The highway system of the country is deteriorated and inadequate. Although road use has increased rapidly for several decades, constant dollar highway expenditures per vehicle-mile are now far less than in any year of
the 1920's or 1930's. Recent surveys indicate that more than one-third
of the backbone interstate highway system of 38,000 miles is in need of com-
plete reconstruction; more than two-thirds of the Federal-aid system of
about 600,000 miles needs improvement; and about one-half the mileage
in non-Federal rural roads requires work. Some 30 billion dollars would
have to be spent to bring the Federal-aid highways to adequate standards,
while large additional amounts might well be used to improve non-Federal
roads. Adding to this the amounts which will be needed over the next
decade to replace highways that will wear out, to accommodate increased
traffic, and for maintenance, a total of possibly 7–8 billion dollars of high-
way construction expenditures a year for 10 years appears to be necessary
if we are to have really adequate roads and streets a decade hence. Recent
expenditures for new highway construction have run from 2.4 billion dol-
lars to 2.7 billion a year, while the estimate for 1953 is 3.0 billion.

The problem of getting more schools, and more and better qualified
teachers, is beginning slowly to yield results, as public opinion increasingly
makes itself felt. But much greater expenditures, well beyond those now
planned, will be required to place the educational system on a firm and
adequate basis by the end of the decade. To take care of increased en-
rollments, to provide for normal replacements, and to reduce the backlog
of need, some 600,000 public elementary and secondary classrooms, costing
more than 18 billion dollars, will be needed by 1958 when the higher birth-
rates of recent years will be fully felt. Additional expenditures for nonpub-
lic schools, and for both public and private colleges and universities, would
lift the total needed construction considerably. In 1952, educational con-
struction expenditures came to about 2 billion dollars, and they are expected
to increase by nearly 10 percent in 1953. This is still well below the amount
which would have to be spent if the needs are to be met by 1960 or so. In-
creasing the number and competence of teachers is largely a matter of rais-
ing salaries. Teachers' salaries have not kept pace with the rise in incomes
of other professions, nor with the rise in earnings generally.

Similarly in the health field, needs are great for hospitals and other
facilities, and for health personnel. The President's Commission on the
Health Needs of the Nation recently estimated that about 900,000 addi-
tional hospital beds of all types are now needed to provide adequate care.
To provide these and adequately to meet needs which will accumulate in the
next 10 years would cost about 18 billion dollars, an average of about 1.8
billion dollars a year. In 1952, an estimated 866 million dollars was spent
on hospital construction. Expenditures are expected to fall during the
next 3 years unless there is substantial increase in the amount of Federal
funds for hospital construction. Public health centers are needed in many
communities. The shortage of doctors, dentists, nurses, and sanitary per-
sonnel remains critical. The President's Commission has estimated that
the Nation can now expect to have at least 22,000 fewer doctors, 17,000
couples dentists, and 50,000 fewer nurses by 1960 than it will need.
PUBLIC OUTLAYS FOR NEW CONSTRUCTION
SELECTED DEVELOPMENT PROGRAMS

BILLIONS OF DOLLARS, DECEMBER 1952 PRICES

1939
- Transportation
- Education
- Natural Resources
- Health Institutions, Water, and Sewer

1943

1948

1950

1951

1952

PROJECTIONS

1953

1955

A

B

C

/ BASED ON PERCENT OF 1939 GROSS NATIONAL PRODUCT SPENT FOR DEVELOPMENT PROGRAMS.
/ ASSUMES FAIRLY RAPID PROGRESS IN MEETING WIDELY APPROVED STANDARDS.
/ THOUGHT TO BE WITHIN THE RANGE OF FEASIBLE INCREASE.

SOURCES: DEPARTMENT OF LABOR, DEPARTMENT OF COMMERCE, AND COUNCIL OF ECONOMIC ADVISERS.
Demands placed upon natural resources and raw materials are expected to be very large during the next quarter of a century, as has been pointed out in the reports of two recent Presidential commissions which have studied long-range problems of water resources and raw materials. The need for many resources or materials in 1975 is expected greatly to exceed the level of use in 1950. (See chart 31.) During the next few years, with a highly active economy, demand for these resources and other resources and raw materials is expected to rise proportionately.

The outlook is for increasing unit costs for many raw materials, especially metals and minerals. The problem is not one of running out of supplies altogether; rather, it is one of slowly and inexorably increasing costs of development and production. This sets the main problem, which is to diminish and circumvent the cost increases by means of various technological and economic measures. These include new discoveries, cost-reducing techniques of mining and production, the aggressive search for cheaper
and more plentiful substitute materials, the fuller development of world sources, and strong programs of conservation at every stage in the production of goods using scarce raw materials.

The severity of this outlook is softened somewhat by the considerable potentials which still exist in this country, and in many other countries of the free world, for increasing supplies of various resources and raw materials. In this country, for example, there still are enormous reserves of coal. It is estimated that there are about 80 million kilowatts of undeveloped hydroelectric power. Certain developments, such as the St. Lawrence project, can produce large amounts of low-cost power, along with other benefits. To supplement the diminishing reserves of high-grade iron ore are large reserves of taconite, which, with sufficient capital investment, can be made to yield large amounts of iron ore usable in blast furnaces.

The trend of increasing productivity in agriculture seems to be continuing, so that increased output of most farm products continues to be achieved even though each year sees a diminution in the number of persons at work in agriculture. New land is available for development, although frequently at increasing cost, by means of irrigation, land drainage, and flood control. Increasing productivity rests primarily upon more farm mechanization, more and better fertilizers, and all manner of other improvements which agricultural research increasingly is making available.

**Financing and planning problems.** The most pervasive limitation to a rapid increase in public development expenditures is the lack of willingness or capacity of governments to raise or otherwise allocate funds to this purpose. Any large increase in Federal financing, at least in the next 2 years, is checked by the competing requirements of defense and by the prospect for a budget deficit. Indeed, a determined effort to cut Federal expenditures could mean less Federal spending on development, although the pressures behind these programs combined with an increasing recognition of needs indicate a level or slightly advancing amount of spending.

The financial position and outlook for State and local governments apparently will permit a substantial increase in both operating and capital outlays during the next few years. Furthermore, evidence indicates a willingness on the part of States and localities to increase their bonded indebtedness. The increasing resort to public and quasi-public authorities for such facilities as toll roads makes it possible to avoid constitutional debt ceilings. Tax yields at the local level may be expected to increase over the next few years, as property reassessments move upward in a lagging response to the inflation of recent years. State governments will gain revenue in pace with increases in income payments, vehicle travel, volume of business, and other elements depending on their revenue sources. Perhaps 2 to 3 billion dollars of additional capital outlays will be made by States and localities in 1955, while additional sums will be available for teachers' salaries, public health services, highway patrols, and the like.
In the event of an economic recession, State and local development expenditures would be expected to fall, or at least rise more slowly after some lag. Federal expenditures could more readily be increased, since the Federal Government is a more powerful instrument for antirecession financing. Not too much should be claimed, however, for expanding developmental expenditures for purposes of offsetting contraction forces in a mild or short recession. To be sure, certain types of public construction programs can be stepped up promptly. These include the simpler public buildings, smaller schools, street improvements, small-scale rural conservation works, and a few others. But the heavy engineering-type projects, such as multiple-purpose dams, divided lane highways, and the large complex building projects such as hospitals and public housing developments, present numerous obstacles to both rapid acceleration and deceleration. Their timing can be speeded up slightly, but their main anticyclical effects would be felt only in a severe and extended depression.

There should be full speed ahead with preparatory measures so that development projects to the extent feasible may be accelerated promptly as part of a total antirecession economic strategy. Advance planning in most public development programs now seems to be in fairly good shape, although development agencies at all governmental levels should review continuously the status of their preparation. Particular emphasis might well be given to those kinds of projects likely to be most helpful in time of recession, noting the speed with which they can be put into action, the amount and type of employment they provide, their location, the kinds of equipment and materials they require, the possible financing obstacles, and finally the speed with which they can be decelerated. Of course, all such projects should fall within the range of the truly needed and defensible.

Policies and programs directed toward reducing the overhang of needs in these primarily public development lines are essential, not only for anticyclical purposes, but also as a condition of continued economic growth. Scientific leadership and a skilled intelligent labor force in the years ahead depend on decisions for better schools today. Having enough raw materials in 1960 or 1975 depends on the geological mapping, the river basin planning, the minerals research, the forest and soil conservation, the multiple-purpose dams, and many other programs which have to be undertaken well before that time. More efficient highway transportation in future years is predicated on increasing programs in intervening years. Furthermore, the timing of these programs and improvements should not be delayed any longer than absolutely necessary; otherwise the human and natural resources base for future economic growth simply will not be there.

In 1955 and in following years, when the Federal budget outlook is expected to be more favorable, the major public development projects can be increased more in line with needs and long-term relationships with total national product. As always, the scrutiny should be close so that public funds are spent on the most desirable particular projects and activities.
Programs which have greatest effects in inducing private economic activities, and self-liquidating programs, should be stressed. Workable arrangements for cooperation with State and local governments and with private groups in the planning, financing, and execution of programs are to be sought.

**Two Matters of Emphasis**

The effort in the foregoing pages has been to examine, as dispassionately as possible, the probable nature and scope of the adjustments which may be needed as the economy moves away from the focus upon defense which has dominated the past 2 years. In summary, the thesis has been that (1) even under moderate assumptions and favorable evaluations of specific demand prospects, the chances nevertheless are that we may run into a problem of deflation and possible recession within the next 2 or 3 years unless it is anticipated by policy measures; (2) the initial size of the problem should not be particularly threatening or its advent precipitous; and (3) in terms of private and public policies which are available for dealing with the problem, it should be an altogether manageable one, provided countermeasures are not too timid or badly timed. With these measures, the uninterrupted maintenance of maximum employment and production from now through 1955 is a sound and attainable objective.

In the concluding paragraphs of this Review, it is appropriate to underscore two points which already are partly explicit and partly implicit in the preceding analysis. The first is, once again, the matter of timing; the second involves the role of business decision-making in the next few years.

**Anticipatory Adjustments**

It is easier to prevent or forestall a depression than to stop or reverse one. This is generally true, and it is peculiarly applicable to the problem at hand. We seem likely to approach the years ahead with both business and consumers in a frame of mind which should ease the necessary adjustments. This psychology will not be the frothy, short-lived sentiment associated with old-fashioned boom-and-bust cycles. Rather, the business and consumer expectations should be the steadier, more solid sort which have grown out of the conviction, developed over the last dozen years, that a high level of prosperity is an economic good which can and will be maintained. Such expectations lend real support to the idea of momentum in a high-level economy, and should reduce the margin of additional demand which new programs and policies may need to bring forth. Any expectations, however, are a very fragile fabric on which to rest the fortunes of an economy. No matter how habit forming continuing prosperity has been, it may take very little in the way of an adverse turn to demoralize sellers and buyers alike. In this lies the importance of adjustments which prevent any adverse turn from taking on frightening aspects; by so doing, they will minimize the total amount of adjustment necessary.

The need for adjustments which anticipate, rather than react, is especially evident in the present instance because of the degree of reliance which it is
hoped can be placed upon private price and wage policies. In this area, as has already been emphasized, the risk is particularly grave that a mechanism of constructive realignment may be transformed, by the alchemy of deflation, into an element of disruption. In no field is it more important that constructive adjustments anticipate any general weakening of markets.

It should be recognized that the preference for adjustments which prevent rather than counteract deflations is not equally applicable in all policy sectors. In the case of many governmental policies, especially in such fields as tax policy, it often places a heavier burden on our abilities to forecast general economic developments than the complexities and uncertainties of economic analysis justify. This fact has two implications. First, it emphasizes the importance, within the Government, of maintaining at all times the most current and most sharply focused body of economic intelligence available, and of keeping current a set of alternative policy programs for meeting various eventualities. Second, it heightens the importance of private policy adjustments as anticipators and minimizers of deflationary danger.

The responsibility of business

During the postwar period to date, American business has contributed more to and received more from the American economy than in any comparable interval of the past. Many businessmen in these years since World War II have lengthened the scope of their decision-making to encompass a longer reach of the future, and have broadened it to include a keener awareness of the dependency of their own enterprises upon the maintenance of stable prosperity in the economy as a whole. This is a praiseworthy development, and the Council often has noted it. But it also has been a relatively facile accomplishment up to now; the times themselves have been conducive to this kind of business decision-making.

For the period behind us has been one in which the economy has demanded and pressed for rapid business expansion, and in which high profits have been desirable to help finance and encourage such expansion. It has not thus far been very difficult to see the prospects for strong and growing markets, particularly with internationally needed Government spending usually on the increase; to make investments to satisfy such markets, particularly with Government inducements; to sell in sellers' markets; or to recognize the desirability of rising consumer incomes, when in a pinch a higher wage could usually be passed on in a higher price.

The period ahead may be of a very different character; it is likely to test the fiber of our new longer-viewed and broader-gauged business thinking much more sternly than any other situation since World War II. And, as it happens, our reliance upon business leadership will be unusually heavy. Government, in view of the heavy demands of recent years, will be little disposed toward fiscal expansion or hasty action. The success of the adjustment—at least if it is an early success—will be very largely up to business. And it will be up to business at precisely a time when many of the older
habits of business investing, price making, and collective bargaining behavior are apt to be more at variance with obviously desirable policy than in any other period since the war.

Business will need to keep its judgment of markets within the framework of a prosperous, growing economy in a period when that prospect is less predictable than it has been for some time, and to invest accordingly; to see the problem of market maintenance both at its collective bargaining tables and in its approach to tax legislation; to grasp the tools of price and product improvements as market cultivators; and to revise downward the notions of desirable profit margins which have become conventional during the postwar years.

This is a big order, but it may hold the key, not only to uninterrupted prosperity for the economy, but also to long-run profit maximization for business itself. In view of the structure and patterns of influence within the business community, the burden upon the leaders of our larger industrial corporations and of the major business organizations will be a peculiarly heavy one. The smoothness with which a transition away from defense is negotiated may depend largely on how wisely these men rise to the sobering challenge. The Council is optimistic that their response will measure up.
Chapter V. International Economic Adjustments

INTRODUCTION

THE PROBLEM of financing imports from the United States has troubled much of the world since World War I, and has become especially acute since the end of World War II. Because of the persistent inadequacy of foreign dollar earnings to provide for the level of United States exports which this country and others believe essential to the economic well-being and political security of the community of free nations, the Council deems it important to consider in some detail the complex of economic, political, and social problems which has been described loosely as “the dollar shortage.”

But first it should be pointed out that the term “the dollar shortage” does not convey accurately the full meaning of the problem. In the first place, other countries in the free world are confronted not only with an inability to earn enough dollars to import enough goods from the United States; they are also confronted with an inability to achieve a high and varied enough level of trade with one another. Although the predominant role of the United States in the free world economy makes the solution of the “dollar shortage” a crucial issue, it is important not to oversimplify the issue by assuming that there is solely a “dollar problem,” or by assuming that if the economic relationship between the United States and these other nations is effectively straightened out, all the other maladjustments will automatically disappear.

Furthermore, the term “the dollar shortage,” by its emphasis upon a unit of currency, perhaps conveys an excessive stress upon monetary problems in the technical sense which masks the underlying resource and production problems throughout the free world. The inability of various nations within the free world currently to meet their economic problem satisfactorily is basically a reflection of the fact that their current productive resources will not support three minimum purposes of any economy, i. e., a sufficiently high level of capital formation to lay the foundation for progress, a sufficiently high level of consumption to prevent deprivation or acute political stress, and a sufficiently high level of defense investment to maintain a modicum of national security. Inadequate trade, while aggravated by many technical factors, is basically a by-product of this central shortcoming. A country cannot import enough goods to supplement deficiencies in its domestic pro-
duction when it cannot produce enough at home to have a surplus for export, at competitive prices.

It follows, if one takes a long enough time perspective, that the main way in which a national entity can solve the foregoing insufficiencies on a permanent basis is to bring its productive power up to the level required to serve the three great purposes indicated above, through its own production and through the international interchange of goods on the basis of relative efficiencies.

Among the nations of the free world, there are two main types of reasons for the insufficiency of production which is at the root of their difficulties. In the economically advanced nations, Western Europe and Japan, for example, these difficulties may be classified as somewhat abnormal. They result in large part from the heavy drain of two world wars, and from the need to assume a new defense program before they could restore the damage visited upon them by World War II. In the so-called underdeveloped countries, the insufficiency of production results from reasons which are fairly well described by the very term “underdeveloped.” And because the two types of situations are fundamentally different, they call for differing solutions, both internally and in the relationships of these nations with one another and with the United States.

The reason why the United States has concerned itself with this problem is largely that, particularly in view of the communist threat acutely felt since the end of World War II, we have had an enormous interest in the strengthening of the free nations at a more rapid rate than they could achieve through their own productive output and through the volume of international trade which this productive output would support. In the earliest stages of this problem, we in the United States recognized that the only temporary solution was to enlarge the availability of goods to these countries by devoting to their immediate use part of what we produced without exacting repayment in the goods that they produced. Stated simply, this has been the main rationale of our aid programs.

However, it has always been our purpose, and likewise the purpose of these other free nations, that these aid programs should gradually be reduced and finally terminated, through increased production in these other countries which would enlarge their supply of goods for home consumption and also enlarge their capacity to pay for imports with exports. Viewed in this light, the purposes and priorities which should guide our foreign economic policy are reasonably clear. For a time, we cannot afford in our own self-interest to taper off what goes under the name of assistance so rapidly as to prevent the fuller fruition of the great productive gains in these other free countries—gains which have resulted in part from this assistance since the end of World War II, but primarily from their own hard efforts. Of course, we must constantly screen this assistance to make sure that it provides an incentive rather than an alternative to the continued exercise of these hard domestic efforts in the other free countries.
We should be realistic about the type of assistance, whether military or economic, which will contribute most toward this end. Meanwhile, we should reach out vigorously for more permanent solutions. These more permanent solutions should come, not through a reduction of our exports to these other countries, but rather through an increasing ability of these other countries to pay for the goods we send them through their own export of goods, either directly or indirectly. A part of this problem relates to the reduction of barriers against imports into the United States, although as will be pointed out, this in itself is not an adequate remedy compared with the central remedy of expanding production in these countries. And because the United States is now and will remain a creditor nation, we are also interested that insofar as feasible private investment will increasingly supplant the need for public investment of United States' capital abroad.

The expression "trade, not aid" is designed to cover this whole complex of objectives in a general phrase. But the simplicity and appeal of this expression should put us on our guard against oversimplification. It does not mean that the United States can help sufficiently in the build-up of international economic arrangements by pursuing a narrowly selfish course, or by thinking that we can get benefits without paying the cost. The build-up of world trade will involve some inconveniences to some sectors of our domestic economy, though these inconveniences will be a minor price to pay for improved world conditions, and far less costly than the aid which thus far has proved temporarily necessary.

The essence of the problem ahead is how swiftly and realistically the shift may be made from aid to trade without imperiling the progress thus far made in free world revival and reconstruction, and with prime attention to the transcendentally important objective of strengthening the free world as a whole—strengthening it not only in a purely economic or military sense, but also in the more important aspect of mutual trust based upon true adjustment to one another's problems. While we in the United States must conserve our own strength, and while we join with the other free nations in their desire for greater financial independence, we cannot safely afford to avoid the palpable fact that our own economic position is unique, and that, because we have so much, we have the most to gain by maintaining a predominantly free world and the most to lose if the balance of strength should shift over to the totalitarians.

**The Size of the Problem**

The United States export surplus of goods and services provides a first approximation to the size of the inability of other nations thus far to match what they import from us with exports drawn out of their own production, i.e., their "dollar shortage." Since United States exports of military goods represent an extraordinary movement associated with the immediate build-up of defensive strength, the measure should exclude exports financed by military aid. Also, since gifts of money (private remittances) sent by
individuals resident in the United States to friends and relatives abroad are a means of financing a part of our exports, they also should be deducted, as should pension payments and other such government remittances. The measure of the inadequacy of foreign means for financing United States exports that thus emerges is equal to our export surplus of goods and services minus (1) military aid, and (2) "unilateral transfers" other than aid. Data for the years 1947 through 1952 are summarized in table 16.

**Table 16.** Measure of the insufficiency of foreign dollar earnings

<table>
<thead>
<tr>
<th>Period</th>
<th>Exports of goods and services</th>
<th>Less: imports of goods and services</th>
<th>Equals: surplus of exports of goods and services</th>
<th>Less: Private and other remittances</th>
<th>U.S. military aid</th>
<th>Equals: net surplus of goods and services requiring dollar financing</th>
</tr>
</thead>
<tbody>
<tr>
<td>1947</td>
<td>19.8</td>
<td>8.3</td>
<td>11.5</td>
<td>.7</td>
<td>.1</td>
<td>10.7</td>
</tr>
<tr>
<td>1948</td>
<td>17.0</td>
<td>10.3</td>
<td>6.7</td>
<td>.7</td>
<td>.4</td>
<td>5.6</td>
</tr>
<tr>
<td>1949</td>
<td>16.0</td>
<td>9.6</td>
<td>6.4</td>
<td>.6</td>
<td>.2</td>
<td>5.6</td>
</tr>
<tr>
<td>1950</td>
<td>14.4</td>
<td>12.1</td>
<td>2.3</td>
<td>.6</td>
<td>.6</td>
<td>1.1</td>
</tr>
<tr>
<td>1951</td>
<td>20.2</td>
<td>15.1</td>
<td>5.2</td>
<td>.5</td>
<td>1.5</td>
<td>3.2</td>
</tr>
<tr>
<td>1952</td>
<td>20.4</td>
<td>15.4</td>
<td>5.0</td>
<td>.5</td>
<td>2.4</td>
<td>2.2</td>
</tr>
<tr>
<td>Annual rates:</td>
<td></td>
<td></td>
<td>ahrenheit</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1950: First half</td>
<td>15.3</td>
<td>10.5</td>
<td>4.8</td>
<td>.6</td>
<td>.2</td>
<td>2.3</td>
</tr>
<tr>
<td>Second half</td>
<td>15.3</td>
<td>10.5</td>
<td>4.8</td>
<td>.6</td>
<td>.2</td>
<td>2.3</td>
</tr>
<tr>
<td>1951: First half</td>
<td>19.3</td>
<td>15.7</td>
<td>3.6</td>
<td>.5</td>
<td>1.4</td>
<td>1.7</td>
</tr>
<tr>
<td>Second half</td>
<td>21.1</td>
<td>14.4</td>
<td>6.7</td>
<td>.5</td>
<td>1.5</td>
<td>4.7</td>
</tr>
<tr>
<td>1952: First half</td>
<td>21.3</td>
<td>15.4</td>
<td>5.8</td>
<td>.5</td>
<td>2.0</td>
<td>3.4</td>
</tr>
<tr>
<td>Second half</td>
<td>19.5</td>
<td>15.4</td>
<td>4.2</td>
<td>.5</td>
<td>2.7</td>
<td>1.0</td>
</tr>
</tbody>
</table>

1 Includes income on investment.
2 Other remittances consist of Government unilateral transfers, other than aid, including pension payments to persons living abroad.

**Note.**—Detail will not necessarily add to totals because of rounding.

Source: Department of Commerce (except as noted).

This measure is arbitrary in certain respects. First, since foreign countries have limited their dollar imports through import restrictions and currency controls, the measure understates the inadequacy of foreign dollar earnings. Second, measuring the dollar insufficiency solely in terms of United States trade ignores the fact that other countries besides the United States also conduct their trade in dollars. Finally, the operation of economics of receiving countries is influenced by the amount of nonmilitary aid which we provide. Their demands for United States exports are therefore affected: some may be increased, others reduced. That is, our financing of the foreign dollar insufficiency tends to influence its size.

In former days, this deficiency was met by foreign countries through sales of gold to the United States or by long-term American foreign investments. The amount of gold that is now available to foreign countries is only of modest proportions. Our long-term foreign investments, which have averaged about a billion dollars a year since the end of the war, are now made mainly in other parts of the dollar area, such as Canada and the dollar area parts of Latin America, and as a result the nondollar area derives relatively little direct benefit from such investment flows.
As may be observed in table 17, the net export surplus requiring dollar financing declined steadily from 1947 through the first half of 1950. The improvement in the dollar position that occurred from 1947 through the first half of 1950 resulted from the recovery of foreign production, which made possible a decline in United States exports, and also from the improvement in the competitive position of foreign goods in world markets after the 1949 devaluations.

Table 17.—Means of financing the insufficiency of foreign dollar earnings

<table>
<thead>
<tr>
<th>Period</th>
<th>Net surplus of goods and services requiring dollar financing</th>
<th>U.S. Government economic aid</th>
<th>Liquidation of gold and dollar assets</th>
<th>U.S. Government loans and other capital outflow</th>
<th>United States private investment</th>
<th>Errors and omissions</th>
</tr>
</thead>
<tbody>
<tr>
<td>1947</td>
<td>10.7</td>
<td>1.8</td>
<td>3.9</td>
<td>7.0</td>
<td>1.0</td>
<td>-1.0</td>
</tr>
<tr>
<td>1948</td>
<td>5.6</td>
<td>3.7</td>
<td>1.2</td>
<td>.9</td>
<td>.9</td>
<td>-1.0</td>
</tr>
<tr>
<td>1949</td>
<td>5.0</td>
<td>5.0</td>
<td>-1.1</td>
<td>.6</td>
<td>.6</td>
<td>-1.0</td>
</tr>
<tr>
<td>1950</td>
<td>3.5</td>
<td>3.5</td>
<td>-2.6</td>
<td>.2</td>
<td>1.3</td>
<td>-2.0</td>
</tr>
<tr>
<td>1951</td>
<td>3.3</td>
<td>3.0</td>
<td>-.4</td>
<td>.2</td>
<td>1.1</td>
<td>-5.0</td>
</tr>
<tr>
<td>1952*</td>
<td>2.2</td>
<td>1.9</td>
<td>-.8</td>
<td>.6</td>
<td>.9</td>
<td>-5.0</td>
</tr>
</tbody>
</table>

Annual rates:

<table>
<thead>
<tr>
<th>Period</th>
<th>U.S. Government economic aid</th>
<th>Liquidation of gold and dollar assets</th>
<th>U.S. Government loans and other capital outflow</th>
<th>United States private investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950:</td>
<td>2.3</td>
<td>4.0</td>
<td>-2.2</td>
<td>.2</td>
</tr>
<tr>
<td>First half</td>
<td>1.1</td>
<td>3.0</td>
<td>-5.0</td>
<td>.1</td>
</tr>
<tr>
<td>Second half</td>
<td>1.7</td>
<td>3.0</td>
<td>-2.1</td>
<td>.3</td>
</tr>
<tr>
<td>1951:</td>
<td>4.7</td>
<td>2.8</td>
<td>1.2</td>
<td>(.1)</td>
</tr>
<tr>
<td>First half</td>
<td>3.4</td>
<td>2.0</td>
<td>(-)</td>
<td>.7</td>
</tr>
<tr>
<td>Second half</td>
<td>1.0</td>
<td>1.8</td>
<td>-.6</td>
<td>.8</td>
</tr>
</tbody>
</table>

1 Includes net sales of gold to the United States and net liquidation of foreign assets, including those held by international institutions.

2 U.S. Government loans and capital outflow include subscriptions to the capital of the International Bank for Reconstruction and Development and the International Monetary Fund. United States private investment includes purchases of obligations of the International Bank.

3 Consists of net increase in gold and dollar holdings of the International Bank and the International Monetary Fund of 2.5 billion dollars, and liquidation of gold and dollar assets by foreign countries in the amount of 4.4 billion dollars.

4 Includes subscription to the capital of the International Bank and the International Monetary Fund of 3.1 billion dollars.

5 Less than 50 million dollars.

6 Estimates based on incomplete data; second half by Council of Economic Advisers.

Note.—Detail will not necessarily add to totals because of rounding.

Source: Department of Commerce (except as noted).

The fact, however, that foreign countries were still dependent on economic aid, had only small holdings of gold and dollar assets and continued to maintain extensive controls over their imports of goods from the United States, indicates the far from satisfactory situation that existed in mid-1950. At the beginning of that year, foreign countries as a group, excluding the USSR and Canada, held gold and dollar assets amounting to 13.9 billion dollars (in addition to their drawing rights in the International Monetary Fund). This represented a decline of 4.4 billion, or 24 percent, from the abnormally low level in June 1945 of 18.3 billion dollars. Moreover, not only had foreigners lost reserves but, in addition, the reserves remaining to them had declined in dollar purchasing power with the increase in prices which had meanwhile occurred in the United States.
After the start of hostilities in June 1950, the world's hectic attempt to expand production and accumulate inventories brought inflationary price rises, especially in the case of raw materials. Higher prices and larger quantities caused the volume of United States imports to rise more rapidly than exports and thereby caused a sharp decline in the net export surplus requiring financing. Economic aid was larger than the net export surplus during 1950 and the first half of 1951, and consequently the rest of the free world was able to rebuild somewhat its gold and dollar reserves.

For several months after early 1951, there was an increase in the deficiency of dollar earnings again as the level of our export surplus doubled in response to the post-Korean boom abroad, to increased levels of defense production throughout the free world, and to a decline in United States imports. In 1952, however, a new advance in United States purchases of goods and services together with the decline in United States commodity exports, caused by import restrictions and the drawing down of inventories abroad, brought foreign dollar accounts more nearly into balance. Throughout the postwar period, the impact of insufficient dollar earnings has been felt with differing degrees of severity by different countries and regions. The deterioration in foreign dollar reserves between mid-1951 and early 1952 was suffered mostly by the sterling area and certain Latin American countries.

THE NATURE OF THE PROBLEM

Before possible solutions other than aid can be appraised, it is necessary to gain some insight into the reasons for the inadequacy of dollar earnings, which, as has been stressed above, is basically an inadequacy of productive resources and of production. War has been a powerful factor in destroying and then retarding productive growth. It also necessitated the sale of foreign assets and the incurring of foreign debt by the European countries which formerly relied on income from foreign investments to pay for a substantial part of imports. The rearmament effort caused by threat of Soviet aggression has increased the demand for imports and reduced the supply of exports. Moreover, the decline in trade with the Soviet Bloc has made it necessary for Western Europe and Japan to turn to sources of supply in the dollar area. The failure of the production of food and raw materials in the rest of the free world to keep pace with population increases and the growth of industrial output has induced an extraordinary demand for food produced in the dollar area, and has caused relative price changes which have adversely affected industrialized countries. The lag of food production behind population growth has put pressure on the already intolerably low levels of consumption of underdeveloped countries. The relatively greater degree of inflation abroad than in the United States since the war has been a symptom of these composite shortages. Meanwhile, in seeking to balance accounts, other countries have entered into bi-
lateral settlements and currency controls which have distorted trade patterns, so that purchases are often no longer made in the cheapest market.

Another basic factor is the dynamic character and size of the United States economy. Rapid technological change yields a large volume of new and improved products that are in strong world-wide demand. The size of the internal market gives producers greater assurance of covering the costs associated with new products than is usually the case in countries having smaller domestic markets. Thus foreign producers of manufactured goods have had to meet strong competition in their own markets, as well as in the markets of other countries and in the United States itself. Moreover, restrictions upon imports imposed by the United States, in limiting the access of foreign producers to the American market, have curtailed their ability to earn dollars. Structural changes, such as the shift to a net earnings position on United States shipping account under the stimulus of Government subsidies, and the substitution of synthetics for such imported materials as silk and rubber, have also worked to reduce dollar earnings.

The intensity of the problem, moreover, varies with changes in the level of economic activity in the United States. A decline of 1 or 2 percent in the volume of industrial production tends to cause a much larger decline in United States imports of goods and services and thereby in dollar earnings. It is difficult for us in this country to comprehend the importance of foreign trade to the level of income, employment, and purchasing power in economies where imports and exports amount to as much as 20 or 30 percent of total output. Variations in imports, which are to us insignificant, can represent a calamitous drop in the exports and production of other countries.

The problem which inadequate dollar earnings symbolize thus has roots in not-easily-reversible historical developments, and in technological and marketing advantages possessed by the United States, as well as in the more temporary difficulties of postwar reconstruction and financial stabilization. An evaluation of the above factors can perhaps best be made by discussing (1) the adequacy of United States demand for foreign goods and services and (2) the adequacy of foreign supply of exports at competitive prices. The following paragraphs consider each side of the problem in turn.

**UNITED STATES DEMAND FOR IMPORTS**

Chart 32 depicts the declining relationship between the volume of United States commodity imports and industrial production. The relative decline in imports appeared first in the mid-1930's, and then was intensified during the war. Since the end of the war in 1945, the increase in the quantity of United States imports has been sizable, amounting to more than 25 percent. But in relation to industrial production, the level of imports is far below that of the 1920's and 1930's.

**Factors operating to curtail United States imports**

Two factors probably account for the major part of the precipitous drop in the quantity of imports after 1929. First, the sharp decline in income,
prices, and production in this country, with the deepening of the depression, curtailed demand for all goods including imports. Purchases of raw materials abroad declined because the demand for the finished product had contracted; purchases of imported luxuries dropped because fewer people could afford them.

Second, in 1930, the passage of the Smoot-Hawley Tariff Act raised the level of import duties beyond anything previously experienced. From 1930 to 1934, when the Reciprocal Trade Agreements Act was passed, the ratio of customs receipts to the value of dutiable imports (the ad valorem burden of import duties) varied between 53 and 60 percent, in contrast to 36 percent under the Fordney-McCumber Tariff.

After 1939, the low volume of United States imports can be explained primarily by the fact that the extension of hostilities first in Europe, then in the Far East, made foreign goods less and less available to the United States. Even after the conclusion of hostilities, the war damage to productive facilities throughout the world kept availabilities low.

In addition, over the past decade or so, import quotas have been levied against the entry of certain agricultural commodities in order to make effective domestic price support programs; the “Buy American” Act has virtually eliminated Federal Government purchases of foreign goods if
domestically produced substitutes are available. These developments have all operated to curtail the volume of United States imports.

Still another influence has been technological change in this country, the introduction of substitutes, and the fact that the raw material component of consumption is relatively less as products become more highly processed.

Although tariffs have been continuously reduced through an extension of reciprocal trade agreements since 1934, they still act as substantial deterrents in the case of many commodities. In addition, other devices have been introduced which operate to restrict the volume of imports, such as the nature of the operation of food and drug inspection. Some part of the low level of United States imports in relation to industrial production in recent years is explained by the uncertainties of other countries as to the permanence of economic stability here and as to the extent and duration of access to the United States market resulting from volatile United States trade regulations. The Defense Production Act of 1950, as amended, directs the Secretary of Agriculture to determine the degree to which imports of specified goods may be permitted entry without interfering with domestic marketing or production programs, or resulting in unnecessary expenditures under price support programs. Under this authority major dairy products have been made subject to quota as have rice, peanuts, and flaxseed.

Some foreign countries state that uncertainties with respect to customs procedure and tariff classification are as great a barrier to imports as are the tariffs themselves. Some imports have been subject to unexpected costs that have meant the difference between profit and loss. Many of these difficulties arise from the complexities of tariff classification under the Tariff Act of 1930. A simplification of tariff classification would encourage foreign producers, especially of new products, to try to tap the American market. In addition, a simplification of customs administrative laws would help to decrease the delay in customs handling of imports and thereby encourage new exports to the United States.

The "escape clause" amendment to the Reciprocal Trade Agreements Act enables domestic producers to seek increased tariff or quota protection under certain broad conditions. The threat of such restrictions has undoubtedly caused foreign producers, who might otherwise have sought a market for their product in this country, to refrain from undertaking the marketing expenditures necessary to introduce their product to American consumers. Any United States policy which gives promise of being stable, and removes the threat of suddenly imposed barriers to imports, would be likely by itself to be followed by a gradually increasing volume.

It seems likely, however, that existing restrictions do not fully explain the recent low level of imports, and an elimination of these import restrictions in their various forms, even were it feasible, would not fully enable the free world to earn sufficient dollars to import in accord with its needs. A large reduction of import barriers would be followed by large increases
in imports of certain commodities, and a decline in their price to a level below that of the cost of production in this country. But with the adaptability, inventiveness, and productivity of American industry, it seems likely that in many cases the increased competition in the domestic market would be successfully countered. Especially would this be true in the field of manufactured products, which have been the chief goal of tariff protection. The size of the domestic market will continue to provide United States producers with a tremendous advantage in world trade by way of cost, diversity of product, and ability to introduce new techniques so long as foreign markets continue to be compartmentalized by trade restrictions or limited by lack of economic development. The strength of competition within the domestic market further provides the motivating force toward a high degree of adaptability and change. The very fact of a more rapid rate of change in the American economy probably explains a large part of the consistently high level of foreign demand for American goods.

Thus, it does not appear that the insufficiency of dollar earnings can be entirely, or even primarily, explained in terms of United States import barriers, or that it would disappear with a substantial reduction in import barriers. Yet a very real contribution would be made by a reduction of United States import restrictions. In addition, such a move would be an act of good faith on the part of this country, indicating that the United States is willing to do its part. And an expansion of United States imports, even by an amount small in terms of the total volume of United States production, could represent a significant increase in the exports and output of foreign countries. Moreover, an increase in United States imports would make possible a reduction in foreign aid, and could increase real living standards in this country.

Reduction of import barriers could not, of course, be achieved without cost. Some individuals may be harmed thereby, although efforts should be made to lessen such dislocations or to compensate for them by expansion of employment in other lines. But that part of the world's dollar earning problem which stems from the curtailment of United States demand for foreign products imposed by unnecessary import barriers is the responsibility of the United States, and can only be remedied by action here.

It is now desirable to turn attention to the even more fundamental aspect of the problem, the productive ability—or inability—of other free countries to satisfy their own needs, including their need to export enough to pay for their necessary imports.

**FOREIGN SUPPLY OF EXPORTABLE GOODS**

*Industrialized areas*

Since the end of World War II the world-wide dollar earnings problem has been felt most acutely by the countries of Western Europe. In every year except 1950 and 1952, Western Europe was forced to sell gold or draw on dollar balances in order to settle accounts with this country, despite economic aid. The problems of Japan are very similar in nature, and,
although they have remained submerged beneath a large inflow of dollars from expenditures associated with the Korean war, they may eventually become even more acute.

Despite adverse developments, since the initiation of the Marshall Plan the volume of European production has expanded remarkably. Although it was conceived as a 4-year program, after 2 years of operation one of the goals of the Marshall Plan—the achievement of prewar levels of output and consumption—had been gained. Since then, the necessity for defense production and curtailment of trade with the Soviet Bloc have tended to obscure the very real progress that has been made. But the contribution which Western Europe is today making to the combined defense efforts of the free world is traceable in part to the success of the Marshall Plan in restoring production capacity.

It is well known that most Western European countries are extremely dependent on imports for food and raw materials. Imports are equivalent to as much as 35 percent of the total output of certain countries. The 40 percent increase in the volume of industrial production which occurred between 1948 and the first half of 1952 was accompanied by an expansion of the volume of imports of 32 percent. Meanwhile, however, total exports expanded 70 percent in quantity, while exports to the United States expanded about 85 percent in volume.

Table 18.—Indexes of industrial production and exports of Western Europe and United States imports of manufactured goods

<table>
<thead>
<tr>
<th>Period</th>
<th>Industrial production</th>
<th>Volume of exports</th>
<th>Volume of U. S. imports of manufactured goods</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(1938=100)</td>
<td>Total</td>
<td>To United States</td>
</tr>
<tr>
<td>1948</td>
<td>100</td>
<td>83</td>
<td>92</td>
</tr>
<tr>
<td>1949</td>
<td>113</td>
<td>101</td>
<td>83</td>
</tr>
<tr>
<td>1950</td>
<td>125</td>
<td>131</td>
<td>158</td>
</tr>
<tr>
<td>1951</td>
<td>127</td>
<td>148</td>
<td>192</td>
</tr>
<tr>
<td>1950: First quarter</td>
<td>119</td>
<td>116</td>
<td>110</td>
</tr>
<tr>
<td>Second quarter</td>
<td>123</td>
<td>119</td>
<td>115</td>
</tr>
<tr>
<td>Third quarter</td>
<td>120</td>
<td>127</td>
<td>168</td>
</tr>
<tr>
<td>Fourth quarter</td>
<td>136</td>
<td>155</td>
<td>226</td>
</tr>
<tr>
<td>1951: First quarter</td>
<td>155</td>
<td>142</td>
<td>212</td>
</tr>
<tr>
<td>Second quarter</td>
<td>140</td>
<td>151</td>
<td>208</td>
</tr>
<tr>
<td>Third quarter</td>
<td>130</td>
<td>145</td>
<td>177</td>
</tr>
<tr>
<td>Fourth quarter</td>
<td>142</td>
<td>153</td>
<td>179</td>
</tr>
<tr>
<td>1952: First quarter</td>
<td>140</td>
<td>146</td>
<td>182</td>
</tr>
<tr>
<td>Second quarter</td>
<td>138</td>
<td>136</td>
<td>175</td>
</tr>
<tr>
<td>Third quarter</td>
<td>129</td>
<td>133</td>
<td>179</td>
</tr>
</tbody>
</table>

1 Not adjusted for seasonal variation.

Sources: Organization for European Economic Cooperation, Mutual Security Agency, and Department of Commerce.

In terms of advances above prewar levels, the recovery of production, and especially of exports to the United States between 1948 and 1952, is equally noteworthy. As table 18 indicates, by the beginning of 1950 the volume of exports to the United States had reached the prewar level, and by the end of 1950 was more than twice as high. By comparison, import
volume was only 12 percent greater than prewar. Production and exports were able to be increased as much as they were, while imports were held down, only because of consumer sacrifices. Since 1948, the percent of total available resources devoted to private consumption has declined somewhat, with increases in the absolute and relative amounts of resources devoted to defense production.

The achievement of individual countries in exporting to the United States has been varied. The exports of nearly all countries were swollen in 1951 because of abnormally large shipments of such short-supply commodities as steel and chemicals to the United States, which in 1952 declined as shortages in this country disappeared. In terms of advances above the 1938 level (which was abnormally low), according to the estimates contained in table 19, Germany and the Netherlands have had most success in expanding exports to the United States. Until mid-1951, the estimated index of the quantity of exports from France to this country was above that of all Western European countries combined, largely because of the extraordinarily high exports of steel and industrial alcohol to the United States. In late 1951, however, while the demand of the United States for foreign steel and industrial alcohol declined, internal inflation in France tended to divert export-type goods to the domestic market, with a resulting sharp decline in the volume of French exports to the United States. Through 1951, the exports of the United Kingdom to the dollar area were prevented from keeping pace with those of Western Europe as a whole by strong demand in other sterling area countries, in many cases supported by domestic inflation. There is some evidence to indicate that as 1952 progressed, after declining sterling area reserves had forced sharp import restrictions on all members, exports of the United Kingdom to the United States and Canada were increasing in volume and value.

Table 19.—Indexes of volume of exports of certain Western European countries to the United States

<table>
<thead>
<tr>
<th>Period</th>
<th>Total</th>
<th>United Kingdom</th>
<th>France</th>
<th>Western Germany</th>
<th>Belgium-Luxembourg</th>
<th>Netherlands</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950: First quarter</td>
<td>110</td>
<td>111</td>
<td>63</td>
<td>72</td>
<td>124</td>
<td>67</td>
</tr>
<tr>
<td>Second quarter</td>
<td>115</td>
<td>121</td>
<td>84</td>
<td>79</td>
<td>115</td>
<td>109</td>
</tr>
<tr>
<td>Third quarter</td>
<td>168</td>
<td>185</td>
<td>122</td>
<td>161</td>
<td>115</td>
<td>140</td>
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<tr>
<td>Fourth quarter</td>
<td>226</td>
<td>203</td>
<td>257</td>
<td>280</td>
<td>187</td>
<td>223</td>
</tr>
<tr>
<td>1951: First quarter</td>
<td>212</td>
<td>175</td>
<td>255</td>
<td>254</td>
<td>183</td>
<td>224</td>
</tr>
<tr>
<td>Second quarter</td>
<td>208</td>
<td>185</td>
<td>222</td>
<td>296</td>
<td>185</td>
<td>265</td>
</tr>
<tr>
<td>Third quarter</td>
<td>177</td>
<td>157</td>
<td>211</td>
<td>307</td>
<td>135</td>
<td>216</td>
</tr>
<tr>
<td>Fourth quarter</td>
<td>179</td>
<td>140</td>
<td>162</td>
<td>261</td>
<td>136</td>
<td>270</td>
</tr>
<tr>
<td>1952: First quarter</td>
<td>182</td>
<td>198</td>
<td>139</td>
<td>247</td>
<td>120</td>
<td>237</td>
</tr>
<tr>
<td>Second quarter</td>
<td>175</td>
<td>178</td>
<td>118</td>
<td>234</td>
<td>111</td>
<td>318</td>
</tr>
<tr>
<td>Third quarter</td>
<td>179</td>
<td>157</td>
<td>114</td>
<td>259</td>
<td>129</td>
<td>346</td>
</tr>
</tbody>
</table>

1 Indexes computed by deflating the value of exports to the United States by the export unit value index of the individual country.
2 Includes OEEC countries other than those listed in this table.
Source: Organization for European Economic Cooperation.
Although Western Europe as a whole succeeded in achieving a substantial volume of shipments to the United States in recent years (though these have not increased proportionally to the growth of the American economy), it might have been able to provide even a larger quantity of exports, had not inflation either in certain European markets or in other foreign markets made sales elsewhere easier and profitable.

That part of the world’s insufficiency of dollar earnings which stems from deep-rooted productive insufficiency or from internal policies which aggravate the restriction of their exports in general, and especially their exports to the dollar area, can be remedied mainly and in the long run only by these countries themselves. Thus, insofar as open or suppressed inflation has prevented an expansion of the exports of industrialized countries, they alone can take effective action. Similarly, only they in the long run can remedy the competitive disadvantage under which their producers may operate in world markets because their economies are less well equipped technologically, less adaptable to change, and limited by small markets. However, the United States can and has encouraged the development of larger markets, especially through its support for trade liberalization measures such as the General Agreement on Tariffs and Trade, the European Payments Union, through customs unions, and the European Coal and Steel Community known as the Schuman Plan. Through our programs and policies the United States has also sought to promote increasing interest in appropriate fiscal and monetary policies, increased productivity, and the elimination of harmful business practices. Individual business firms and labor organizations in this country, working in cooperation with the Mutual Security Agency, have also assisted in raising European productivity through an interchange of technological knowledge with visiting groups both here and abroad.

Food and raw material producing areas

Those countries which are predominantly producers of food and raw materials have suffered a dollar problem which is quite different in its nature and its effects from that of Western Europe. The difference is the result of two factors. First, these countries are in general less economically developed than Western Europe and Japan, and consequently their levels of production and consumption are very low. They are, moreover, extremely desirous of increasing their production, and in aiding them to apply more modern techniques, the Point Four program has played an important role. Developing countries typically would be long-term foreign borrowers with an excess of imports financed by long-term lending. Such a deficiency would be a normal one and would continue as long as they remain underdeveloped. In pursuit of economic development, these countries are engaged in long-term programs involving both large expenditures and the purchase from abroad of capital goods, whose source of supply has been chiefly the United States. One part of their demand for dollars, then,
is in connection with the maintenance of their planned rate of economic
development. In general, their programs have called for a steady rate of
dollar expenditures for the purchase of machinery and equipment, but the
flow of dollar investments to these countries has been small.

Second, the prices of primary products, food and industrial raw materials,
fluctuate far more than prices of manufactured goods. Their dollar re-
ceipts from current exports, therefore, have been subject to marked fluc-
tuations. This instability in dollar and other foreign exchange receipts is
largely explained by the fact that supplies of raw materials cannot be ex-

tended or contracted to accord with sudden changes in demand. Shifts
in demand are consequently reflected in prices to a much larger degree than
is the case with manufactured goods. This instability is the greater, the
more dependent the economy is on the production of one or a few com-
modities for its income. The smaller the foreign exchange reserves of the
raw material producing countries, the more complete is the transmission of
this instability to manufacturing countries. As was pointed out above,
only if foreign countries have adequate gold and foreign exchange re-
serves can they absorb the effects of temporary variations in their export
receipts. To acquire adequate reserves, they must husband foreign ex-
change receipts during periods of high earnings, and draw upon them dur-
ing periods of low income.

Thus, in the case of the economically underdeveloped countries, the
insufficiency of dollar earnings is largely a reflection of the fact of their
underdevelopment. Provided that they are able to progress with their
development programs, their economies will become more diversified, they
will become less dependent on the production of a few commodities, and
their aggregate income will thereby become more stable. And if indus-

trialized countries, especially the United States, succeed in maintaining
a high and stable level of economic activity, the demand for raw materials
will also be high. Under such conditions, with reserves sizable enough
to enable the raw material producers to sustain temporary declines in
their export receipts, and with appropriate internal policies to neutralize
partially the effects of excessive rises, the injurious effects of price changes
can be minimized. Meanwhile, however, while they are in the process
of development, they are very much in need of investment funds and

technical knowledge from abroad. Continuation and expansion of activities
under the Point Four program can be of tremendous aid in bringing about
a sizable increase in their volume of production.

Conclusions Regarding International Economic Policy

The United States has marked advantages in world trade. Yet there are
real prospects that other countries will in due course under appropriate pol-

cies be able to earn sufficient dollars to pay for what they import and thus
to reduce and finally eliminate the need for aid.

The main part of this task lies in these countries' hands in the long run.
This requires the avoidance of internal inflation, the development of greater volume and efficiency in production, and the broadening of free-trade areas so that maximum economies in production may be realized. Market-widening arrangements of the type illustrated by the European Coal and Steel Community offer much hope. It is possible that fewer restrictions on the free operation of the market mechanism would contribute to the solution, by enabling countries to produce those commodities in which they are relatively most efficient, and to buy where the goods they need are cheapest. As the European countries succeed in producing an expanding volume of exports at competitive prices, the size of the problem will diminish. It seems probable that a major opportunity for balancing dollar accounts of industrialized countries may lie in their expanded exports to raw material producing countries, as United States purchases from these countries increase. If producers of manufactured goods can compete with United States producers in the markets of developing countries, their payments problems will lessen with the expansion of world trade following on development.

An expanded volume of world trade sufficient to enable foreign countries to build up their gold and dollar reserves, would have the additional advantage of helping to stabilize the demand for United States exports. With present reserves, any temporary decline in dollar earnings forces an almost immediate curtailment of foreign buying in the United States. Possession of sufficient reserves abroad would, through stabilizing the United States exports, prevent the domestic effects of a temporary movement such as an inventory cycle from being accelerated by a decline in the volume of exports, as well as avoiding the impact which any sudden cessation of purchases from the United States inevitably has upon the economies of the countries concerned.

The United States, with the largest single market in the world, and with a dynamic and highly progressive production system, also has an important role to play. An expansion of long-term investments in underdeveloped areas would help finance the foreign demand for our goods, while expanding the supply of raw materials in which we are deficient. These investments together with the Point Four program can contribute in an important way to balanced economic development, which in the longer run should assist in the solution of the world’s dollar earning problem through an expansion and diversification of production and trade of these areas. By maintaining a steady rate of economic growth, we shall help to stabilize the demand for many raw materials, thus helping to stabilize raw material prices and foreign dollar earnings and facilitating the growth of adequate foreign gold and dollar reserves.

In the field of trade policy, we can make a very significant contribution. We should eliminate as many import quotas as possible. Where import quotas are essential to the carrying-out of important domestic programs, we should make them as liberal as possible. The “Buy American” requirement
with respect to foreign purchases by the Federal Government should also be liberalized or eliminated. We should also reduce tariffs and simplify our trade-restricting and uncertainty-breeding customs procedures, so that foreign producers will have increased incentives to use mass selling techniques in our market.

This combination of improved volume and efficiency abroad, increased United States foreign investment, and reduced trade barriers should gradually enable the world to earn the dollars it needs to pay for its imports from the dollar area. In the meantime, we must continue to readjust, but not to scuttle, those programs of transition from conditions at the end of World War II to conditions in the years ahead when the peace and prosperity of the free world may be more firmly founded upon more permanent measures.

And finally, economic stability and adherence to a permanent full employment policy in the United States will prove profoundly important. Price stability here relieves other economies from the severe impact of sharp changes in the American price level. And a permanent full employment policy in this country relieves other countries of the fear of seeking to enter excessively volatile markets, and of the fear that economic reverses here would cause abrupt shifts in our attitude toward imports.