

MONTHLY *Business Review*

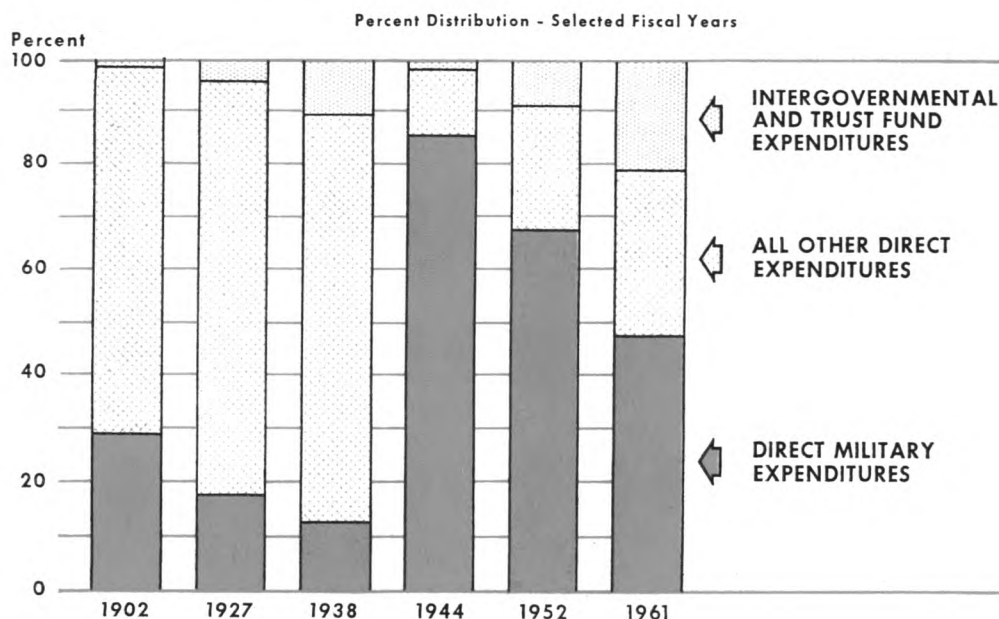
— FEDERAL RESERVE BANK of CLEVELAND —

June 1963

IN THIS ISSUE

Patterns in Federal Spending: 1900 - 1962.....	2
Current Trends in Retail Sales.....	12

Military outlays have accounted for a substantial part of total Federal spending since 1940, and intergovernmental and trust fund expenditures have accounted for larger proportions of total spending since 1952.



Source of data: U.S. Bureau of the Census.

Patterns in Federal Spending: 1900-1962

EACH January the President of the United States sends a Budget Message to Congress in which he outlines projected Federal income and spending for the coming fiscal year.⁽¹⁾ The Budget usually creates considerable interest in Congress and among the general public. The reaction from some people is favorable; from others, disapproving. In either event, the introduction of the Budget is often followed by a lengthy debate concerning Federal spending plans. At times, the ensuing discussions may conceal the basic purposes and value of some Federal expenditures. In the following review of Government spending from 1900 to the present, an attempt will be made to define and categorize the expenditures, as well as to place budget programs in historical perspective. In addition, some comments are offered on the economic objectives of Federal spending.

Level of Spending

In fiscal year 1962, the United States Government paid out to the public a cash amount of almost \$108 billion.⁽²⁾ At this level, gross Federal cash outlays reached a record volume that exceeded even the unusually high rate of spending that was necessary during the Second World War. The tremendous expansion and increasing importance of this sector of the economy is more apparent when the recent all-time high is contrasted with total budget expenditures of just half a billion dollars in 1900. In other words, in sixty-two years Federal spending has shown an increase of more than two-hundred-fold, attaining a

level that cannot be easily put into perspective by the average individual.

The climb in Government outlays has not been continuous since the turn of the century. Between fiscal years 1900 and 1915, expenditures increased gradually, reaching a level close to \$1 billion. Two years later, Federal spending jumped as a result of the U. S. entrance into World War I, reaching, by fiscal 1919, a total of approximately \$18 billion. (This was a record amount in the history of the country up to that time.) In accordance with fiscal policy of the time, however, postwar spending was cut back sharply in 1920 and then continued to decline very gradually until 1928. Budget expenditures in fiscal 1928 totaled about \$2.9 billion, revealing that the economy and Federal spending grew beyond the prewar levels of 1900-15.

In order to comprehend the relative economic importance of Federal spending, it is useful to compare the total dollar amount with the aggregate measure of spending in the entire economy, Gross National Product (GNP). Some estimates of GNP have been made for the years prior to 1930, although the early decades are represented only by averages for five-year periods. Using these figures, one can estimate that Government expenditures in fiscal 1900 amounted to about 3 percent of total spending in the economy.⁽³⁾ The proportion actually declined slightly until 1917. In other words, the activities of the Federal Government were not a major factor in the business and financial activity of the United States between the turn of the century and the First World War. This situation was changed sharply by the entrance of

(1) A fiscal year is the twelve-month period from July 1 through June 30, and is designated by the June calendar year date.

(2) See Appendix to this article for a description of the different accounting concepts of Federal spending and for an explanation of the statistics used in the following pages.

(3) The relation of Federal spending to GNP is approximate because of the time lag between calendar and fiscal years.

the nation into the war and the concentration of economic output into defense needs. By 1919, Federal spending had increased to the extent of accounting for about one-fourth of GNP. With the decrease of Government outlays following the war, the proportion of such spending to total GNP dropped back to 3 percent by the end of the 1920's.

The setbacks of 1929 coupled with the succeeding depression that gripped the economy in the 1930's led to substantial changes in theories of government and in the emphasis placed on Federal spending. As a result, cash outlays by the U. S. Government rose to a little over \$8 billion in fiscal 1937, a peacetime spending record up to that time. At that level, expenditures amounted to 9 percent of GNP. Spending then slipped in the following year, until the advent of the Second World War resulted in a skyrocketing volume of funds paid out to the private economy. Between 1940 and 1945, Federal cash outlays showed a 1,000 percent increase to a total that had been virtually undreamed of in any previous wartime period. Total cash payments exceeded \$90 billion in both fiscal 1944 and 1945. Although there was a concurrent rise in national income during the war years, Government expenditures at these record heights accounted for nearly half (45 percent) of GNP.

In the next three years, following the end of hostilities in 1945, Federal spending declined very sharply as cash payments for military defense were cut back. Starting in 1949, however, and continuing to the present, expenditures have increased on balance. A substantial rise was apparent in fiscal year 1952 partly as a result of the involvement of the United States in the Korean War. It is noteworthy that succeeding Federal spending has never dropped back to the pre-1952 level, although absolute declines in outpayments were recorded in 1954, 1955, and 1960. What is more important is the fact that the private sector of the American economy has grown so rapidly in the postwar period that even at the record 1962 level, Government expenditures accounted for only one-fifth of total

GNP. From fiscal 1948 to 1962, Federal cash payments nearly tripled in dollar volume, but as a proportion of GNP, Government expenditures increased moderately from 14 percent to 19 percent. This means that the rise in Government outlays since World War II has proceeded at a pace only moderately faster than that for the economy as a whole.

There could be objections to evaluating Federal Government expenditures in this way in that much of the increase in Federal spending has been due to rising prices since 1900 (with some major interruptions). To evaluate this criticism, it is first necessary to "deflate" statistics for Government outlays. Since the national Government purchases goods and services at both wholesale and retail levels, a price deflator has been used that represents both aspects of the general economy. The implicit price deflator for the GNP series was used with a 1929 base period—roughly halfway through the time span under review.

On an adjusted basis, the pattern of Federal cash spending since 1900 is roughly the same as on an unadjusted basis, with one important exception. That is, if Federal outlays are put in terms of 1929 dollars, it is still apparent that spending was low between fiscal 1900 and 1917, that it climbed during World War I and again during the 1930's, and that it increased very sharply at the start of the Second World War. The important exception is the experience since 1942, when the changes in the volume of Federal spending represented price behavior to a more important extent than previously. From the end of that fiscal year until the present, Government expenditures on a 1929 base are much smaller than in terms of current dollars, so much so, that deflated outlays in fiscal 1962 are roughly half as large as the unadjusted dollar volume.⁽⁴⁾ After this price adjustment is made, cash spending in 1962 becomes the highest *peacetime* amount on record but falls some \$26 billion below the wartime record of fiscal 1944.

(4) The GNP implicit price deflator (1929 base) increased from 103 in 1942 to 192 in 1962.

To summarize the description of the growth in total Federal payments, the greatest stimulus during this century has been the expense of wars in which the United States has taken an active part. While the record spending volume of fiscal 1962 is also due in large part to military outlays, analysis of the expenditures by changing type of function provides further insight in this study.

Purposes for Spending

The objective of Federal spending is to meet the financial obligations of the Federal Government assigned to it by law and custom. From this basic objective, it follows that if the scope and activity of the national Government increases, operating expenses and cash outlays will also increase (barring a sharp decline in the price level).

The magnitude of the operations of the Government, in turn, increases partly as a result of the growth in population, territory, and national income of the United States. For example, part of the rise in expenses of the House of Representatives in this century has been due to the increase in the number of Congressmen, reflecting increases in population. In addition, in fiscal 1908 salaries paid to employees of the Internal Revenue Service amounted to \$4.4 million; by fiscal 1962, the amount was 100 times higher, reflecting in part the increase in staff necessary to accommodate a larger tax-paying population as well as changes in tax legislation. The acquisition of additional land or facilities, such as the Panama Canal, also causes a rise in Federal spending. The Canal land was purchased in 1904 for a little more than \$50 million, and the operating costs and costs of improvements have ranged from \$4 million to \$72 million in the succeeding fiscal years.

Some fiscal outlays reflect changes in the stage of economic and political development of the nation. Thus, a few of the accounts listed in the summary of disbursements made in fiscal year 1908 now seem like early American history. Examples are "payments for public schools in the territory of Oklahoma", some aspects of "Steamboat-Inspection Serv-

ice", and in 1909, "payments to the State of Kansas for suppressing Indian hostilities". In contrast, the following accounts appeared in 1962: National Aeronautics and Space Council, Subscriptions to International Financial Institutions, Southeastern Power Administration, and the Subversive Activities Control Board. In recent years, the increased emphasis on scientific research and knowledge has led to higher Federal costs for specialized equipment and highly-trained workers.

A third, and undoubtedly the most important, factor that currently influences the volume of Government expenditures is the increasing role of the Federal Government in both the domestic and world economies. Earlier in this article, it was demonstrated that prior to the 1930's Federal spending was held down to low levels in peacetime. It was also mentioned that a basic change in fiscal policy occurred in the 1930's. The change may be said to have taken two forms simultaneously. First, the usefulness of Government spending as an anticyclical weapon was tested, and secondly, the Federal Government assumed chief responsibility in providing economic relief to large segments of society. Modern economic theory recognizes that Federal spending can be used to stimulate the economy at times when consumer spending and business investment are weak. This approach was adopted and applied during the world-wide depression of the 1930's. At the same time, the deep slump produced such human hardship and economic want in the United States that the Federal Government intervened to prevent further deterioration in living standards of wide segments of the population. As a result, in fiscal 1934, while total budget expenditures amounted to \$7.1 billion, expenditures for both recovery and relief accounted for \$4.0 billion of the total.

Similar outlays were necessary throughout the decade until the Second World War brought an improvement in levels of employment and income in the United States. The

newer types of Federal spending that arose with the Depression have continued. It is current policy to increase spending during recessions. In addition, it is the policy to continue many of the social programs begun in the 1930's, often in expanded form.

A final development that has contributed to the expansion in the operations of the Federal Government occurred first in the Depression. Since that time there has been an increasing dependence on the national administration as a source of funds. The Federal Government became involved in many local projects during the 1930's because state and municipal governments suffered from a sharp loss in revenue and, in turn, curtailed services. As a result, construction of highways, public buildings, and parks was carried out with Federal financing. The payment of national funds to state and local governments rose sharply during this period, amounting to 9 percent of total Federal outlays by fiscal 1938. In the past decade, state and local governments have depended heavily upon Federal funds to aid in financing such projects as urban renewal, conservation, welfare, airports, college housing, highways, and perhaps mass transit. In fiscal 1961, intergovernmental expenditures made up nearly 7 percent of total Federal spending.

The national Government has also served as a source of credit in recent years. Loans are made directly to small businesses, manufacturers of defense equipment, veterans of the U. S. armed forces, and farmers. Direct loans in fiscal 1962 (excluding those to international agencies or other nations) amounted to \$15 billion. In addition, the Government has an extensive program of insuring and guaranteeing loans made by private sources, primarily in the area of housing. Total guarantees and insurance on domestic loans equaled almost \$76 billion in fiscal 1962. The rationale for both direct loans and guarantees is that the Government provides credit that is not otherwise available or assumes risks that private financial institutions would not undertake.

Types of Spending

There are several ways of grouping Federal expenditures by functions. To illustrate the diversity of fiscal projects, the functional classifications developed by the Bureau of the Census are used here.

Some functions of administration have always been considered the natural "domain" of the Federal Government. There is little doubt, for example, that the national government is the logical and capable choice to handle the defense of the country. Spending for military equipment, personnel, and administration has accounted consistently for a large part of total Federal expenditures. Even in 1902, military outlays amounted to 29 percent of "direct general expenditures".⁽⁵⁾ The proportion rose sharply in World War I but dropped in the period between the wars. A low point was reached in 1934 when the ratio for military spending sank to 11 percent. In contrast, a high of 76 percent was recorded in 1944. It is important to note that defense outlays have equaled more than half of "direct general expenditures" since 1951, with the actual share ranging from 60 percent in fiscal 1952 to 51 percent in fiscal 1962. The present emphasis on military expenditures reflects international defense commitments such as U. S. obligations to NATO and the United Nations, as well as the high cost of armaments and the continual search for new weapons. Outlays for these purposes are judged to be vital in the present-day world; they account for the major portion of Federal spending, but it is a slightly declining proportion. In other words, the volume of military expenditures explains the current high *level* of total Federal spending, but not the rising *trend* of such spending.

Other expenditures of the Government are closely related to current or past defense programs. For example, benefits and services for veterans of the armed forces are a result of previous wars. In addition, one could

(5) As defined by the U. S. Bureau of the Census, direct general expenditures exclude trust fund and intergovernmental spending.

count in civil defense, interest costs on debt issued to finance wars, and even the current space exploration program. Other expenses related to defense efforts fall in the area of international relations, i.e., foreign aid and assistance and subscriptions to international organizations. The cost of research and development in atomic energy is also included in this broad grouping. The classifications of international affairs and military science are among the most rapidly increasing expense units in total Federal spending. To illustrate, cash payments to the public for space research and technology rose from \$71 million in fiscal 1956 to \$1,257 million in fiscal 1962. In the same period, payments connected with international relations increased from \$1.6 billion to \$2.5 billion. While most of the increasing expenditures just mentioned stem from U. S. efforts to fulfill its current and future responsibilities to the free world, the subject of veterans' benefits and services is related to the past. (A further discussion of these services is given later.)

Some nondefense programs have always been considered within the province of the Federal Government. A number of these functions seem best handled by the national administration because the operations cut across state boundaries. Postal service for the United States has been a Federal function since the eighteenth century. In the early part of this century, the Post Office Department accounted for a large proportion of fiscal spending (about 20 percent). With the increased diversification of Government programs, however, expenses for postal service have recently accounted for only 5 percent of total direct expenditures.

The Federal debt is, of course, a national function. The ratio of interest expense on the debt to total Government spending becomes larger in peacetime when the bulk of spending is nondefense; it also increases following periods of heavy Federal borrowing. Since fiscal 1952, the ratio for interest expense has held within a narrow range around 8 percent of direct expenditures. Other Gov-

ernment operations carried on without regard to area or group identity include the Weather Bureau, the Coast Guard, the St. Lawrence Seaway, and air traffic agencies. The proportion of spending for these functions has declined since the early 1900's. Finally, the United States has been fortunate to keep spending for "police" supervision (FBI, Secret Service, and Immigration) at fractional levels in the twentieth century. Expenditures for all these "customary" Government services make up a much smaller share of total spending today than prior to the Second World War, even though the share has been increasing slightly since 1944 because of improvements and additions to established programs.

The remaining types of Federal spending, while heterogeneous, have an underlying factor in common. The outlays generally are aimed at improving the standard of living of certain groups of people or in specific areas of the country. Spending of this sort is not a new development; in the budget accounts for fiscal 1908, the following expenditures appear: "funds for epidemic diseases", "expenses of cotton-boll weevil investigations", "wagon roads in Alaska fund", and "money for the relief of sufferers from cyclone in the Southern States". Nevertheless, the relative growth and widening impact of Federal social programs since the early 1930's has been a major factor in the transition of Government spending. The reasons for this spending were explained earlier; the evidence is presented in the accompanying tables.

Spending for social welfare was relatively large during the 1930's, as the Government made efforts to alleviate the effects of the Depression. The amount of such expenditures in fiscal 1938, however, was only one-fifth of the amount spent in fiscal 1961.⁽⁶⁾ The reference in Table I to the rise in the proportion of Federal spending made by the trust funds and to political subdivisions (primarily states) is important in this context because most of these funds go to improve social welfare. To

(6) Latest data available.

TABLE I
Percentage Distribution of Total Federal Expenditures
for Selected Fiscal Years

	<u>1902</u>	<u>1922</u>	<u>1938</u>	<u>1954</u>	<u>1961</u>
Total	100.0	100.0	100.0	100.0	100.0
Direct general expenditures	98.8	96.7	89.0	89.7	79.1
Trust fund expenditures	—	0.2	2.0	6.5	14.2
Intergovernmental expenses	1.2	3.1	9.0	3.8	6.7

TABLE II
Percentage Distribution of Federal Spending for "Social Programs"
for Selected Fiscal Years

As percent of direct general expenditures (including defense):

Type of Spending	<u>1902</u>	<u>1922</u>	<u>1938</u>	<u>1954</u>	<u>1961</u>
Total	28.2	17.0	46.8	14.8	20.6
Farm subsidies	—	—	4.3	5.5	8.8
Veterans' services	25.0	11.7	7.9	4.0	4.8
Natural resources	1.4	2.2	20.5	2.6	3.4
Hospitals	0.4	2.4	1.3	1.0	1.3
Education	0.5	0.2	2.2	0.9	0.8
Health	0.2	0.2	0.4	0.4	0.7
Housing and urban renewal	—	*	1.4	0.2	0.5
Highways	—	0.1	6.6	0.1	0.2
Public welfare	0.7	0.2	2.2	0.1	0.1

* Less than 0.05 percent.

illustrate, in fiscal 1961, nearly one-third of Federal payments to other governments was for welfare purposes, while slightly more than half was for the improvement of educational systems and highways. Similarly, of the total spending accounted for by Federal trust funds, almost 80 percent was in the form of social security payments.

Within the category of *direct* expenditures for programs to improve living standards (Table II), farm subsidies made up the largest share in fiscal 1961. This Federal program began in 1933, with the ratio of such outlays to total spending remaining high until World War II and then again increasing steadily since 1952. The rise in this spending is directly related to Federal farm legislation but is also affected by the increasing productivity of American agriculture. On the other hand, payments for veterans' benefits and pensions

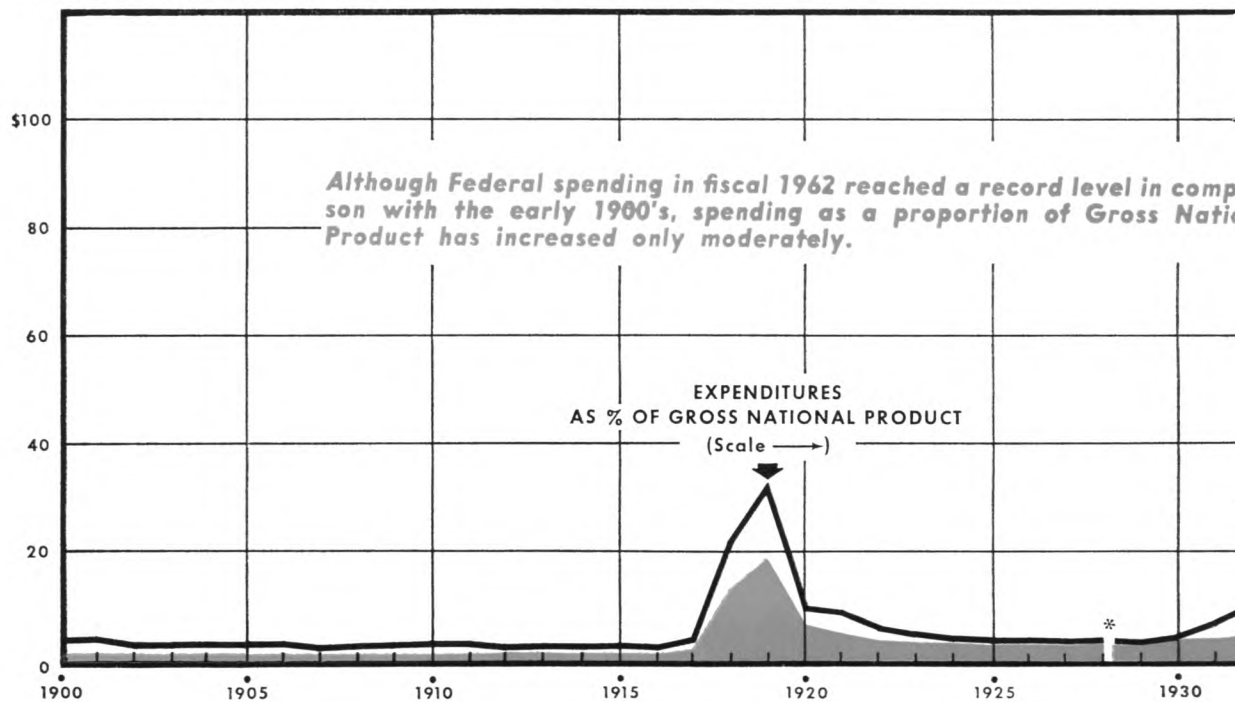
comprise a declining proportion of total direct spending. The ratio for this category has hovered just under 5 percent since fiscal 1954, in contrast to the early years of the century when almost all social programs were for the benefit of veterans.

Government expenditures on the nation's natural resources go for a multitude of projects. Such spending was the major vehicle for combating economic conditions in the 1930's, with most public works projects classed in this group. Included now are outlays for the Tennessee Valley Authority, the Army Engineers, reclamation projects, and the National Park and Forest Systems. The remaining categories in the table have smaller relative importance, although the total dollar amount spent for these functions has been increasing. The emphasis on direct spending for highways and education has declined since the 1930's because funds of this nature are now

FEDERAL EXPENDITURES

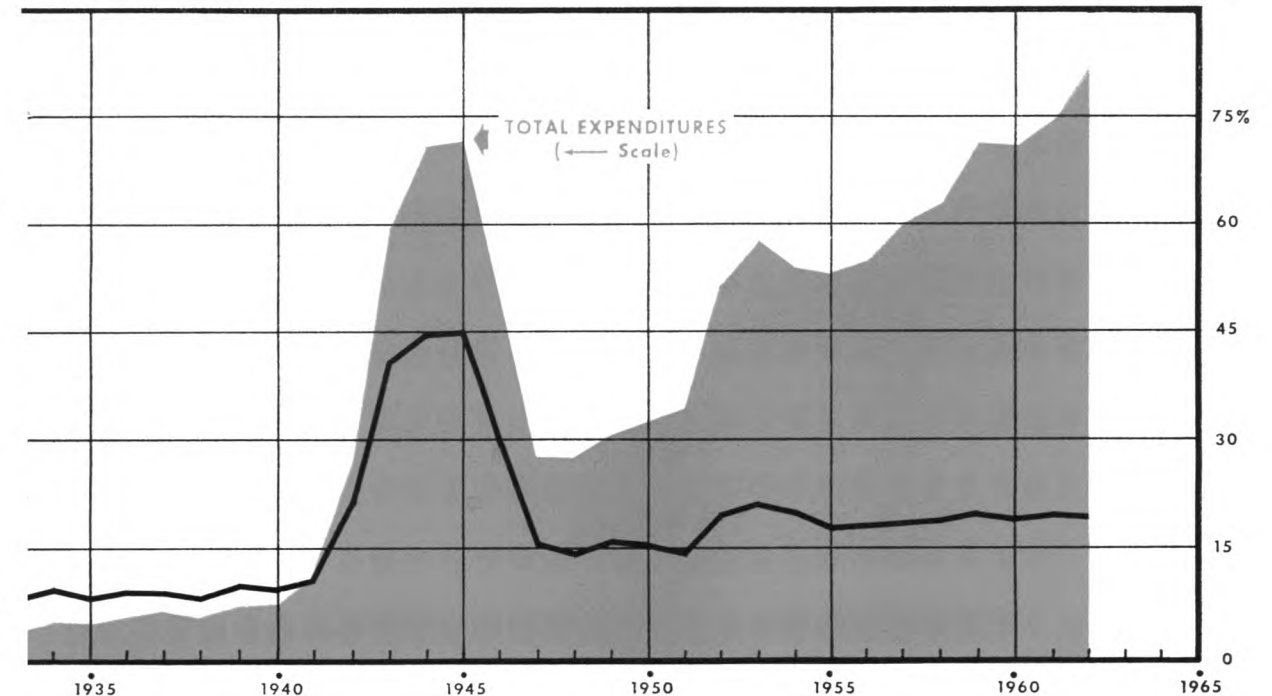
Fig. 1

Billions of dollars



* See Appendix.
Source of data: U.S. Treasury Department.

Percent of GNP



channeled through intergovernmental payments. Expenditures for hospitals and health (primarily for veterans) have been increasing a little faster than total outlays in recent years, and the share of spending for housing and urban renewal has risen since 1957.

Conclusions

Federal spending is currently at a record level, with cash payments to the public reaching an all-time high in the past fiscal year. Since the world situation has saddled the United States with heavy expenses, about half of the total outlays are for national defense, with a much smaller but growing proportion budgeted for military research and international affairs.

An increasing share of Government expen-

ditures has gone for domestic programs of a social nature. Most programs were begun in the Depression, but their coverage has widened, and the demand for new Federal services has grown. There are many reasons for the increased participation of the national Government in the economy: to combat the extremes of the business cycle, to provide for social needs too severe or too widespread to be countered on regional or local levels, and to provide credit that has not or could not come from private financial sources.

Given the current environment and role of the Federal Government, it appears that Federal spending will continue to grow in future years. Spending could be cut, but only if wide segments of the American public were

willing to give up the assistance that they receive in so many forms from the Federal Government. It would also be necessary for state and local governments to take over some of the functions which they relinquished thirty years ago, perhaps by regaining part of the taxing power now concentrated on a national basis. In addition, the private financial sector of the economy would have to assume some of the credit functions now performed on the Federal level.

There are probably some weaknesses in spending programs at all levels of government. Some projects may cost more than is necessary, while others may represent unneeded duplication. Often the need is stressed for a complete re-evaluation of Federal ex-

penditures, with the suggestion that some functions would be better handled on a local level. (Examples that have been mentioned by several observers are unemployment compensation and urban renewal.) In many instances, the entire budgetary process has come under attack, including the method of approving fiscal outlays and the motives underlying many spending decisions.

Nevertheless, both the level and nature of Federal spending have undoubtedly contributed to the nation's economic growth. While Federal spending has been implicitly approved by the people of the United States, wider public awareness and understanding of government operations may help to provide improvements in government fiscal activities.

APPENDIX

Data on U. S. Government expenditures, like the Budget as a whole, are presented in several different formats. For example, spending plans which are submitted to Congress for approval make up part of the *administrative budget*. This budget has certain disadvantages in use, chiefly because the non-substantial income and spending by trust and deposit funds and Government-sponsored enterprises are omitted.⁽¹⁾ As a result, expenditures on an administrative budget basis do not disclose the complete scope of Federal activity nor do they help in tracing the impact of total Government spending on the U. S. economy. In the past few years, emphasis has been placed instead on expenditures as forming a part of the *national income accounts*. Such statistics seek to measure the direct impact of Government purchases on the national economy by recording the purchases at the time of delivery rather than at the time of payment. Federal outlays on a national income basis, however, exclude purely financial transactions and District of Columbia expenditures. Thus, this approach still does not measure the full flow of funds from the Federal Government to the economy.

A third format for reporting fiscal spending is on the basis of *cash payments to the public*. Expenditures on a cash basis most nearly approximate the actual flow of funds from the Treasury Department to the public. Included are spending by the Federal trust and deposit funds and by Government corporations; missing are all intragovernmental transactions which do not involve payments to the public (e.g., payments to Federal employee retirement funds). In addition, accrued items such as interest on Government securities are shifted to a checks-paid basis.

Another method of compiling cash figures on fiscal expenditures is used by the U. S.

(1) Government-sponsored enterprises include the Federal Deposit Insurance Corporation, the Federal land banks, the Federal Home Loan banks, banks for cooperatives, and the Federal intermediate credit banks.

Bureau of the Census. Here, some additional financial transactions are excluded (loan repayments and mortgage purchases), while expenditures of Government enterprises are reported on a gross basis, rather than net, as in cash payments to the public. The Census method also counts in employee contributions to Federal retirement funds. This approach performs a useful service by grouping Federal expenditures into functional classes; such information is available for selected years from fiscal 1902 through fiscal 1961.

Confining the use of statistics to those on a cash basis has the added advantage of eliminating confusion among funds "authorized", "appropriated", and "obligated". Plans for Government expenditures must first be authorized by Congress, but the actual outlays can not be made until Congress also appropriates the necessary funds. While the authorization for certain projects can continue indefinitely, appropriations usually have a time limit of one year. In addition, obligations to spend from the appropriations must be made within the original year, even though the checks may be written in future years. Thus, the existence of obligated but unspent funds often has the effect of boosting Federal spending above the levels proposed for an individual year in the Budget Message from the President.

In this article, an attempt was made to report Federal spending, wherever possible, on the basis of checks paid and cash payments made. Because of the difficulties of obtaining a consistent series with both historical length and descriptive detail, however, some leeway was taken. Annual totals for expenditures from 1929 to the present time represent cash payments to the public. Prior to 1929, expenditures from the administrative budget were used, since data on a cash basis are not available. (The average annual discrepancy between the two series is estimated to be less than \$0.2 billion in these early years.) In the

discussion of Federal spending by type or function, the chief source was the data published by the Bureau of the Census in its releases "Summary of Governmental Finances."

The Federal budget system has always been set up on a current basis, i.e., projects which will absorb funds over a period of time longer than one year (and thus do not need to be paid for within one year) are not isolated in a separate grouping. A number of observers believe that the United States should adopt the system used by many European countries of a separate capital budget. Such an accounting statement would include expenditures for construction, capital equipment, and the purchase of land and existing buildings, as opposed to expenses for current operations. While various estimates are available for Federal capital expenditures, there is substantial disagreement about the types of spending to be included. For example, the Bureau of the Census lists capital spending in a range of \$16.2 billion to \$18.5 billion in each fiscal year since 1952, with most of the outlays going into defense equipment. (Data for previous years are not available.) N. H. Jacoby would include expenditures for research and education in a capital budget, and accordingly, estimates Federal capital spending in fiscal 1962 at \$35.3 billion.⁽²⁾

The Government itself, in the 1964 Budget, presented a special analysis of expenditures by an investment *versus* operating division. The accounts included "not only outlays to increase physical capital and intangible as-

sets, but also developmental expenditures which represent an investment in human capital. It does not distinguish precisely between capital and current items, although it does provide useful general magnitudes. . . . This analysis does not purport to be a capital budget in the sense of a long-range program for the acquisition of assets. Nor is it a plan for separate financing of capital expenditures."⁽³⁾ In this presentation, total expenditures of an investment or developmental nature in fiscal 1962 amounted to \$38.4 billion. The outlays falling in this classification were loans for home building and improvements, grants to states, spending for public works, commodity inventories, buildings, land, and major equipment, and the expenses of research and development in science and health. Some 65 percent of the total for 1962 was for defense purposes (68 percent if research spending by the National Aeronautics and Space Administration is included). In addition, it is of interest to note that 25 percent of the total investment outlays fell in the categories of "social" spending presented in the table accompanying the article. The major nondefense item was Federal grants to states for highway construction; other large proportions of funds were spent for improvement and conservation of natural resources and for housing and urban renewal.

This brief description of the intricacies of statistics on Federal spending should not give the impression that all the figures are exact to the cent. It is hoped, however, that the magnitudes involved in this article are accurate enough for the purpose at hand.

(2) Neil H. Jacoby, "The Analysis of Fiscal Policies — Past and Present", *Quarterly Review*, Banca Nazionale Del Lavoro, March 1962.

(3) U. S. Bureau of the Budget, "Special Analysis D", *The Budget of the United States Government* for the fiscal year ending June 30, 1964.

Current Trends in Retail Sales

RETAIL sales have received considerable attention in recent months as dollar volume, seasonally adjusted, pushed into all-time high levels during the first quarter of this year, easing only slightly in April, and in May returned to March's record-high level. The retail sales series, which reflects sales of all retail stores including department store sales, automotive sales, food sales, and others, is closely watched by businessmen and economists as one of the indicators of current economic activity.⁽¹⁾

As is the case with numerous business indicators, it is characteristic for retail sales to increase over the long run, partly because of the continuing growth of the population. Changes in the general price level also affect the level of retail sales as well as other business indicators which are measured in terms of current dollars. Therefore, in order to evaluate the significance of current developments in retail trade, it will be helpful to compare recent rates of expansion with past experience and to relate changes in the level of retail sales with changes in the level of other business statistics associated with consumer spending, such as disposable personal income and expenditures for services.

Retail Sales in Three Business Cycles

A comparison of retail sales trends in three business recovery periods is illustrated in Chart 1. On the chart, expansion in retail sales is measured at two-month intervals over a span of 26 months starting from the lowest sales month of each of the last three business recessions.

As the chart shows, each of the three recovery periods has been accompanied by ex-

pansion in retail sales. The over-all percentage increase from the beginning to the end of each 26-month period was much the same, i.e., 14.6 percent in the latest period (January, 1961 through March, 1963) as compared with 15.5 percent in the January, 1954 to March, 1956 period, and 14.6 percent in the March, 1958 to May, 1960 period. Part of this expansion represents shifts in retail price levels rather than increased physical volume. In the two latest recovery periods, retail prices increased one percent; however, in the earlier 1954 to 1956 recovery period, retail prices declined two percent thus understating the expansion in retail sales.⁽²⁾

A difference is apparent, however, in the rapidity with which a pickup in retail sales got under way after the trough month of each recession was passed; the current expansionary period in retail sales was the slowest in starting.

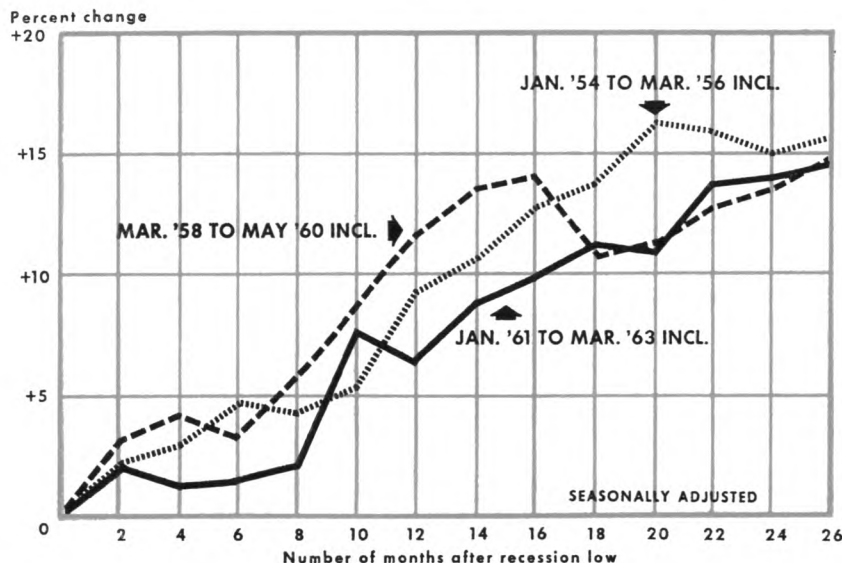
The importance of the sluggish rate of post-recession expansion in retail sales in the latest period is pointed up by the fact that monthly retail sales in the entire 26-month period averaged only 7.5 percent above the level of sales at the beginning of the recovery period, whereas similar calculations for the two earlier periods under review show that monthly sales averaged 9.6 percent and 9.7 percent, respectively, above the level of sales at the start of the 1954-56 and the 1958-60 periods. On an over-all cumulative basis, therefore, expansion of total retail sales in the most recent business recovery has been proportionately smaller than it was in the previous two periods of post-recession expansion, although retraction of retail sales in the last two cycles was comparable and exceeded the 1953-54 contraction.

On the other hand, expansion in the latter half of the present recovery has progressed somewhat more evenly than was the case in

(1) The retail sales series is compiled by the Bureau of the Census of the U. S. Department of Commerce from a representative cross-section of approximately 2000 business firms which, in total, operate some 40,000 retail stores in the United States. It is designated by the National Bureau of Economic Research as one of the fifteen coincident indicators of economic activity. Other coincident indicators include nonagricultural employment, industrial production, and personal income.

(2) As measured by the "all commodities" component of the Consumer Price Index, Bureau of Labor Statistics.

Chart 1.



A comparison of the expansion in retail trade in the last three recovery periods measured from the low month in each respective cycle provides evidence of a steady expansion of sales in the last half of the most recent period. It should be noted, however, that the trough months in retail sales do not necessarily coincide with the trough months in over-all economic activity.

Source of data:
U.S. Department of Commerce

earlier recoveries. In the current expansion, increases have continued with little interruption for 26 months, through March of this year. Expansion is now halted on a new, high plateau for, as was noted above, there was a slight easing of retail sales in April of this year which was regained in May. It remains to be seen whether the April-May experience signified a peaking out of current expansion in retail sales.

Long-Term Growth:

Durable Vs. Nondurable Goods

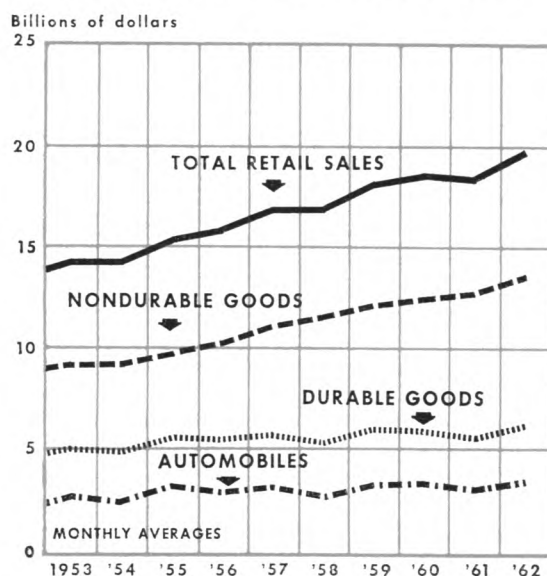
There is some popular tendency to concentrate on the vicissitudes of the automotive sales sector, or even on retail sales of durable goods as a group, as being representative of over-all retail sales activity. Over the short run, this may be a valid assumption since it is a well-known fact that retail sales of durable goods, and of new autos in particular, tend to fluctuate with the ups and downs of the

business cycle while sales of nondurables maintain a much steadier pace. During the past eight or ten years, however, retail sales of nondurable goods have provided most of the growth in total retail sales, not only in terms of the larger dollar volume involved, but also in terms of rates of gain.

As Chart 2 shows, all automotive sales, including both new and used cars and accessories, form only about one-fifth of total retail sales. More importantly, however, the chart shows that sales of automotive goods, and even sales of all durable goods at retail, have shown much less growth in the past decade than have retail sales of nondurable goods. In terms of percentage increase, the annual volume of nondurable retail sales expanded 48 percent between 1953 and 1962 while retail sales of all durable goods, including automotive sales, rose only half as fast with an increase of but 24 percent in the same period. Automotive sales taken separately increased

Chart 2.

COMPONENTS OF RETAIL TRADE



Source of data: U.S. Department of Commerce,
Bureau of the Census.

28 percent, or just a little more than durable goods as a group, but increased far less than nondurable goods.

Increase in Expenditures for
Consumer Services

Retail sales volume is only one of a number of statistical series that measures, in one way or another, the key role played by the consumer in the economy. Other pertinent series are those reflecting disposable personal income, total personal consumption expenditures, and expenditures for consumer services.⁽³⁾ Growth rates of these three measures are summarized in the accompanying table for comparison with corresponding changes in retail sales volume (total retail sales are not directly comparable with the more inclusive GNP total of expenditures for durable and nondurable goods).

While retail sales trends show some correlation from year to year with disposable personal income fluctuations, the expansion of retail trade in the ten-year period 1953 to 1962 has not kept pace with the expansion in disposable personal income. In the ten-year

Comparison of Growth Rates

Period	Disposable Personal Income	Personal Consumption Expenditures	Consumer Services	Retail Sales
1953-1962 annual average	4.7%	4.7%	6.7%	3.7%
1954	1.7	1.2	5.5	0.0
1955	6.8	7.9	7.2	8.7
1956	6.7	5.1	8.1	3.2
1957	5.4	5.7	7.1	5.4
1958	2.9	2.8	6.7	0.2
1959	6.0	6.9	7.4	7.5
1960	3.6	4.8	7.4	1.9
1961	4.1	2.9	5.5	-0.3
1962	5.3	5.5	5.8	7.6

Source of data: U. S. Department of Commerce

(3) Total disposable personal income (as a part of Gross National Product) is the income remaining with individuals after deductions of personal tax and nontax payments to government. This is a more meaningful measure for comparison purposes as it disregards changes in tax levels over the 10-year period.

Personal Consumption Expenditures (as a part of Gross National Product) consist of the market value of goods and services purchased by individuals and nonprofit institutions and the value of food.

Consumer services (Expenditures for Services as a part of Gross National Product) include the expenditures for household operation, housing, transportation, personal services and recreation.

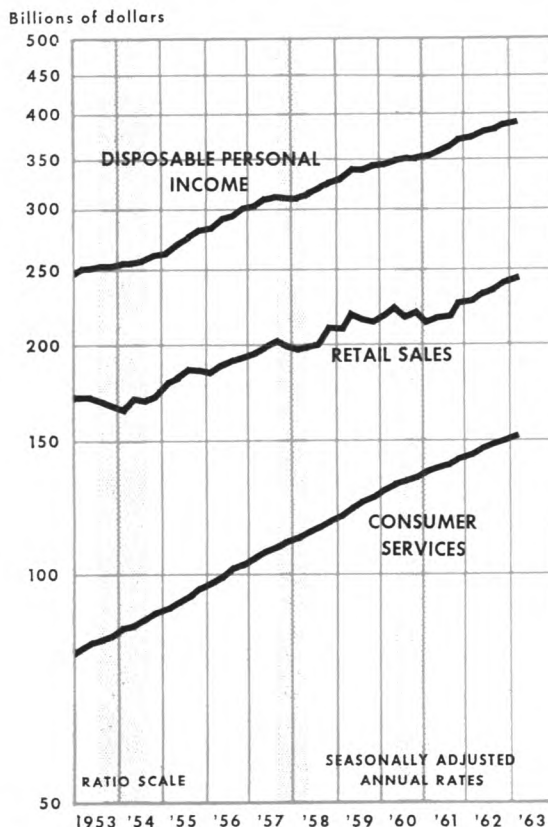
period 1953-1962, retail sales registered an average annual increase of only 3.7 percent per year in comparison with the 4.7 percent increase per year for disposable personal income. At the same time, total personal consumption expenditures matched the 4.7 percent growth in disposable personal income, indicating that consumers were using more and more of their disposable income for purposes not included in retail sales. By 1962, consumer service expenditures' share of disposable personal income had grown to 40 percent from 35 percent in 1953.

As shown on the table, expenditures for services have shown consistently high rates of growth throughout the ten-year period. Year-to-year increases ranged from 5.5 percent in 1954 and 1961 to 8.1 percent in 1956. Costs of consumer services have spiraled upward in the last decade, increasing 25 percent in comparison with a seven percent in all other consumer prices.

The relationship among disposable personal income, retail sales, and expenditures for consumer services is also shown graphically in Chart 3. The shaded areas on the chart indicate the three postwar recession periods from peak to trough. In both the disposable personal income series and the retail sales series, the levels shift coincidentally with the recession contractions and recovery expansions; however, expenditures for services were noticeably unaffected by setbacks in over-all economic activity and show almost a straight-line increase during this period.

Chart 3.

Consumer service expenditures continue to outpace the growth of retail sales and are little affected by fluctuations in economic activity.



Source of data: U.S. Department of Commerce



FOURTH FEDERAL RESERVE DISTRICT