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THE *Business* SITUATION



By the Office of Business Economics

THE BASIC trend in economic activity continues upward, but there has been a definite easing in market demand during the past 2 months. The frenzied buying which developed during the summer months has now abated and has been followed by a more orderly flow of both consumer and business purchasing. The major factor in this change has been that the fears of immediate shortages of civilian goods have proven to be unfounded. Production has expanded, and armament procurement has not as yet been large enough to curtail the flow of goods for civilian use. In addition, during the past month the tempo of consumer demand has been subject to the dampening influence of the higher tax rates effective October 1 and the more stringent control of consumer and housing credit.

Nevertheless, the volume of consumer demand at the present time remains appreciably above that prevailing before the outbreak of the Korean incident. This is a reflection of a significant expansion in employment and of sizable wage increases affecting large groups of employees.

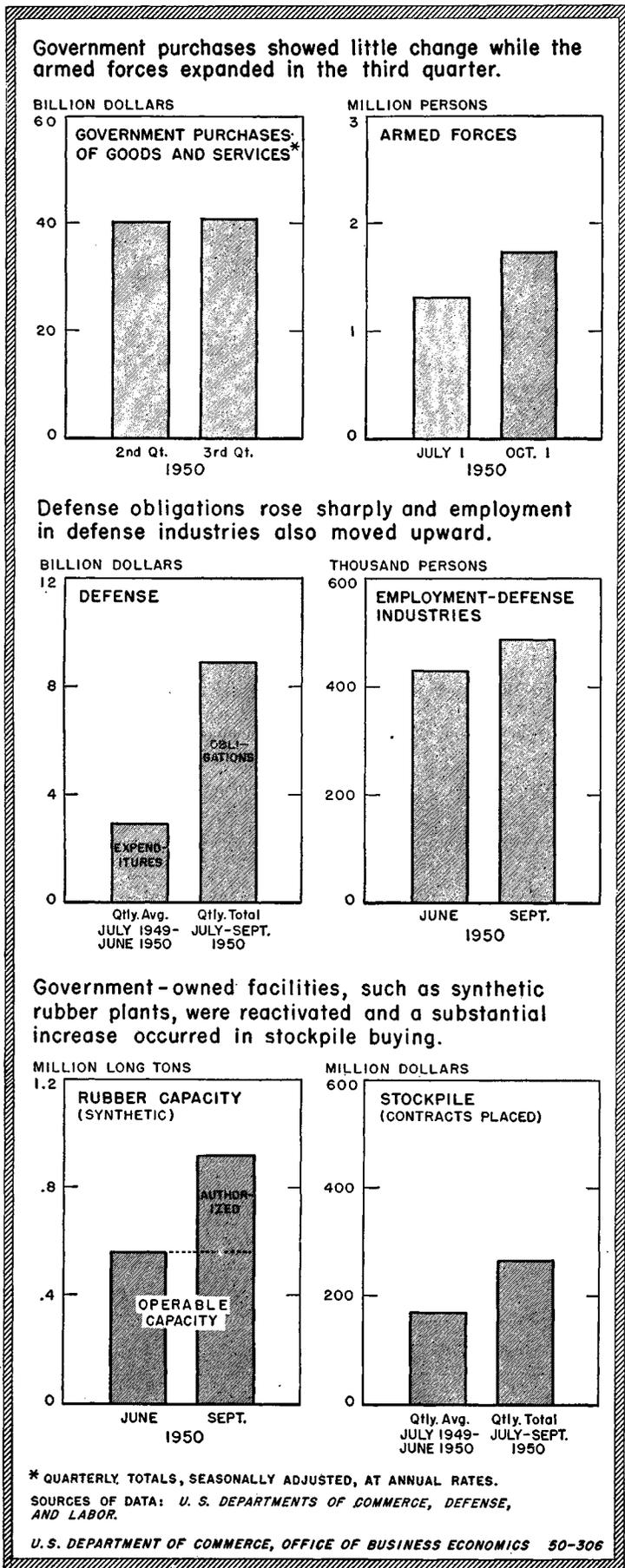
Since the Korean attack, the stepped-up defense program has been the basic influence in the expansion of business activity. For the most part the principal effects have been anticipatory, however, growing out of the projected expansion in Government spending in the year ahead. As shown in the top panel of the accompanying chart, actual Government expenditures, showed little change from the second to the third quarter as the rise in military expenditures was offset by a decline in nonmilitary foreign aid and in farm price support.

Defense activities expand

Other aspects of the defense program showed more substantial increases. Defense obligations reached \$9 billion in the quarter, of which nearly \$6 billion represented procurement orders and letters of intent. Employment increased in defense industries, some war plant facilities were reopened, and stockpile buying showed a further rise.

The timing of the indirect effects of the rise in defense spending is particularly uncertain. As the general magnitude of defense planning became apparent in advance of large-scale Government expenditures, the immediate effect was a surge in private spending by both consumers and business. This forward buying was financed by liberal credit terms and the drawing down of liquid assets, which in turn brought interacting advances in prices, profits, wage rates, and employment.

Some catching up in anticipatory buying by consumers began in September even before the imposition of credit controls. This together with a high rate of shipments from manufacturers to distributors brought trade stocks more into line with current consumer buying and reduced the incentive to increase commitments further.



Production edges upward

The continued strong demand has led to further rises in production. Industrial output advanced somewhat more slowly in October, however, than in other recent months. For the most part, capacity operations continued to be maintained in industries producing raw and semifinished materials, and output of most manufactured goods was sustained at or close to the high rate of the third quarter.

New production peaks were recorded for steel and paper-board. Steel mills in October operated at 102 percent of available capacity—up over 2 percent from September—turning out more than 8.7 million tons of steel ingots and castings. Output of bituminous coal advanced further, averaging 11.5 million tons weekly, with total output for the year to date exceeding last year's volume during the same period by nearly 60 million tons. While consumer buying of bituminous coal has increased, the higher level of production has permitted a sizable accumulation of stocks during the summer months. Since last March when the miners returned to the pits, the additions to coal stocks have averaged approximately 6 million tons per month and total stocks at the end of September were only 10 million tons below the peak of 74 million reached in July 1949. Crude petroleum output held steady at the September record rate.

Output of manufactured goods was paced by the record output of television receivers and a further increase in freight car deliveries to the railroads. Television receivers rolled off the assembly lines at an average weekly rate of over 200,000 units in October which compares with the previous peak rate of 175,000 in August. For the fourth consecutive month assemblies of passenger cars and trucks in United States plants averaged around 35,000 units per day.

On the whole, defense output continues to represent a small fraction of the volume of total production. Even the limited flexibility in industrial potential at the time of the Korean invasion has permitted the stepping up in defense activity which has occurred to date without interfering with civilian production schedules. New orders for war materials are increasing, however, and tightening supplies of a broad range of raw materials presage cutbacks in civilian supplies in order to fill defense contracts.

Regulations affecting basic materials

The National Production Authority initiated action during October to implement its broad program of priorities and allocations of scarce materials. The first of these orders, issued October 12, is on steel. The primary purpose of this directive is to spread evenly Defense Order (DO) ratings among all producers so that they may continue to take care of civilian orders with the least possible market disruption. A similar directive dealing with aluminum was issued on October 27. Steel producers were also asked to set aside approximately 310,000 tons of steel products to provide for the production of 10,000 freight cars per month in the first quarter of 1951, as well as for adequate repair and maintenance of used freight cars. More recently, regular allotments of steel products to warehouses were established in order to insure supplies for small business. Furthermore, NPA announced that orders will be issued cutting supplies of copper, aluminum and nickel for civilian use possibly as much as 20 to 35 percent. These orders will tend to curtail output of most consumer durable goods.

A further ruling issued October 24, tightens the previous rubber control order by limiting total new rubber consumption to 90,000 tons a month in November and December, with more severe restrictions on the consumption of natural rubber in the latter month.

Manufacturers' new orders ease in early fall

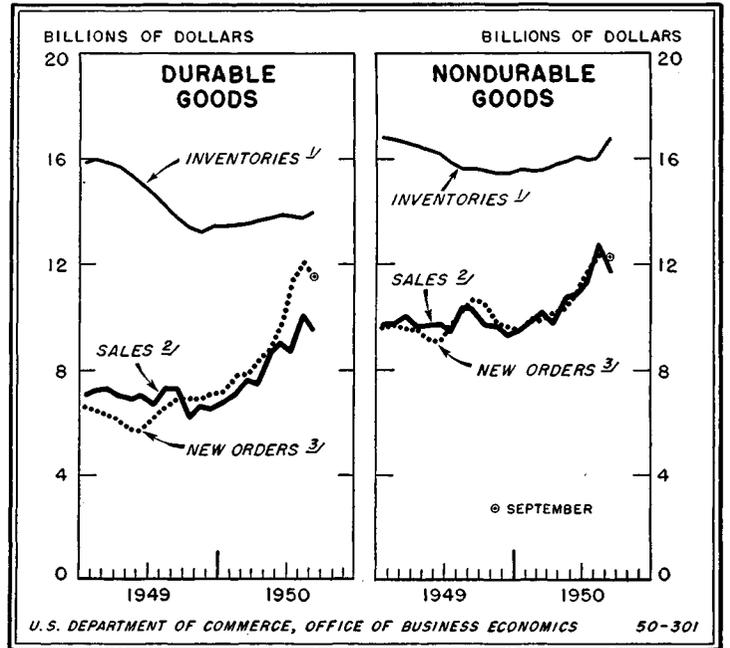
The effects of the easing in buying after the post-Korean surge were reflected in the early fall trend of manufacturers' new orders. Incoming business, though substantially above the rate of the early part of 1950, was down from its August peak.

Manufacturers' new orders in September amounted to \$24 billion, about 12 percent below August. Despite the drop, new orders remained higher than shipments, and backlogs continued to advance. Preliminary information for October indicates some further decline in the rate of new business, with unfiled orders still increasing.

Consumer demand important in third quarter surge of orders

The flow of new business, which soared from \$57 billion in the second quarter to nearly \$73 billion in the third, derived its impetus from three sources. The first was the consumer rush to obtain goods whose supply might be affected by the increase in defense requirements. Although the direct impact of this demand had largely subsided by the end of August, the high rate of retail sales and the drain on stocks stimulated forward buying by retailers. The rate of placement of department store orders, as indicated by the Federal Reserve Board series on orders outstanding, was running 35 percent ahead of year-ago rates in the third quarter of 1950; the corresponding gain in the second quarter was 5 percent.

Chart 3.—Manufacturers' Sales, New Orders, and Inventories



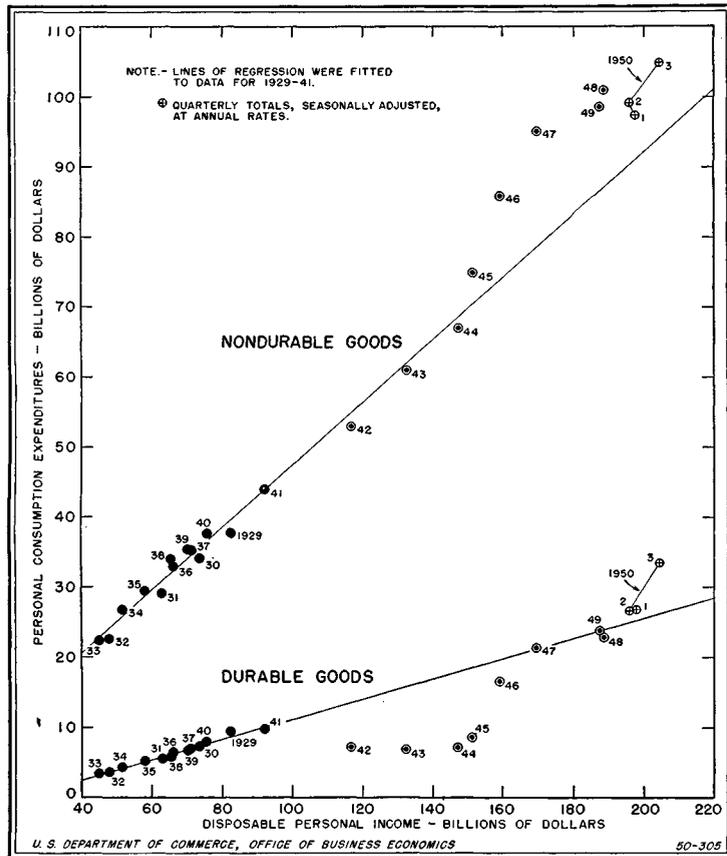
¹ Seasonally adjusted book values, end of month.
² Monthly totals, seasonally adjusted.
³ Three-month moving average, centered at middle month, except for September 1950.
Source of data: U. S. Department of Commerce, Office of Business Economics. 50-301

Military procurement was the second factor in the high rate of manufacturers' new business. A substantial part of the third quarter defense obligations represented commitments to purchase goods, which are directly reflected in manufacturers' new orders figures.

The third source of forward buying represented in manufacturers' bookings was the indirect stimulation of the stepped-up defense program. Orders placed by businessmen in expectation that Government contracts would be forthcoming constituted an important part of this.

restrictions on durables into increased nondurable-goods spending, the shift to less expensive durable-goods buying, disposition of current holdings of liquid assets, changes in the rate of income and saving, and a variety of other factors. A simplified illustration of the effects of credit restrictions under given assumptions may, however, place into focus the range of magnitudes involved.

Chart 8.—Personal Consumption Expenditures Related to Disposable Personal Income



Source of data: U. S. Department of Commerce, Office of Business Economics.

The volume of consumer purchases of major durable goods made on terms more liberal than Regulation W requirements is estimated at \$5.5 billion a year at spending rates in the third quarter of 1950 under the simplified assumptions of table 6.³ If it is arbitrarily assumed these purchases will be reduced by one-half under the regulation, consumer spending will be cut by \$2.5 to \$3 billion a year below the level which would have prevailed in the absence of the recent credit restrictions. This represents about 13 percent of the annual rate of third quarter 1950 consumer expenditures on major durable-goods items, 8 percent of total outlays for all durable goods and more than 1 percent of all consumer expenditures.

More than half of the total potential reduction of \$2.5-\$3.0 billion reflects the dampening effect of the controls on new automobile purchases, associated with a 15 percent reduction in these outlays at the third quarter of 1950 rate. Household durable goods on the basis of the above assumptions may tend to be reduced by a proportion in the neighborhood of 10 percent.

The procedure followed in obtaining these figures, as given in the illustrative example of table 6, was to calculate

³ Credit sales may be overestimated insofar as they are used as a base from which to measure the restrictive effect of Regulation W, since they include sales not affected by consumer credit controls, e. g., household appliances included in the purchase price of a house. In addition, it may be noted that third quarter credit sales were unusually high because of scare buying noted above.

the proportion of consumer expenditures bought on credit terms less restrictive than those imposed by Regulation W, and then to assume as a first approximation that one-half of these sales might be affected by the stiffer contract terms. This rough procedure measures only the direct effect involved and does not take into account changes in spending due to housing credit restrictions, in personal incomes, and in the trends in credit terms had controls not been imposed, as well as other qualifications noted above.

The effects of controls depend on several estimates which—though partly based on incomplete data—are considered as conforming to prevailing economic trends. In table 6, 50 percent of expenditures on the selected products is assumed to be bought on time. Consumer finance studies in 1949 indicated that 43 percent of new cars and 54 percent of other durables were bought on credit. Buying plans early in 1950 indicated a substantial increase in the proportion of credit purchases of new cars. Credit buying plans were not available for other durable goods, although a continuation of the upward trend of the past 3 years is probable.

The table also presents estimates of credit sales made on terms more liberal than Regulation W requirements, based on credit conditions prevailing in the spring of 1949. On the basis of an analysis of installment credit terms at that time, it would appear that the proportion of contracts carrying terms more stringent than those of Regulation W were approximately as follows:⁴

Contracts with down payments of 22 percent or less and maturities exceeding 15 months, April 27-June 30, 1949

[Percent of all contracts]

Refrigerators.....	55
Washing machines.....	40
Television sets.....	45
Console radios.....	30

Trends to easier terms since the summer of 1949 were used as the basis of estimating the somewhat higher proportion of credit sales made on terms more liberal than Regulation W used in table 6.

Table 6.—Total Credit Purchases of Selected Consumer Durable Goods and Volume Bought on Terms Less Restrictive Than Regulation W Requirements¹

[Dollar figures in billions]

Item	Consumer durable expenditures, 3d quarter, 1950 ²		Proportion or credit to total sales		Credit sales ³		Credit sales made on terms more liberal than Regulation W requirements	
	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	
New automobiles.....	2.5	50	1.25	60	0.75	60	0.75	
Major appliances.....	1.0	50	.50	50	.50	50	.25	
Radios, televisions, etc.....	1.1	50	.55	40	.55	40	.22	
Furniture.....	.9	50	.45	33 1/4	.45	33 1/4	.15	
Total.....	5.5	50	2.75	50	2.75	50	1.37	

¹ Proportions of nonautomotive goods purchased on credit terms less restrictive than Regulation W include the volume for which both the initial and the monthly payments were less restrictive than required by the regulation. For automobiles the proportion used also includes an allowance for credit sales made on contracts with maturities of 24 months or more, even when down payments were in excess of Regulation W requirements.

² Seasonally adjusted.
³ Credit sales may be overestimated insofar as they are used as a base from which to measure the restrictive effect of Regulation W, since they include some sales not affected by consumer credit controls. This is offset to some extent by an understatement of the proportions of credit sales made on less restrictive terms by Regulation W.

Source: U. S. Department of Commerce, Office of Business Economics.

For new cars bought on credit in this period, approximately one-fourth of the contracts in 1949 involved one-third down and more than 15 months to pay. Incomplete information for 1950 indicates a substantial easing of terms

⁴ See "A Study of Installment Credit Terms," Federal Reserve Bulletin, December 1949.

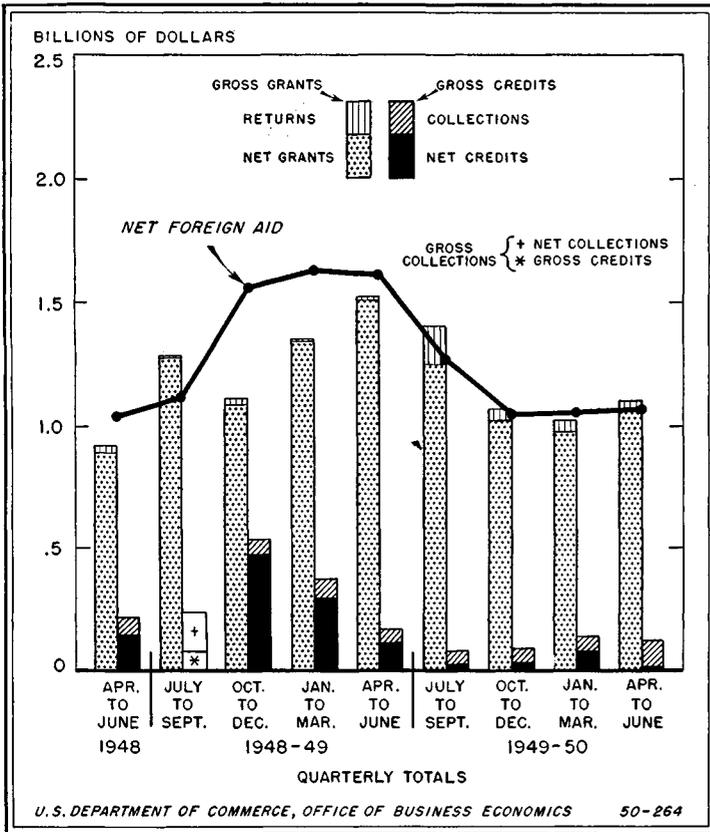
(Continued on p. 20)

Foreign Transactions of the U. S. Government in Fiscal 1950

GR OSS foreign aid extended by the United States Government in the form of cash or goods and services in the fiscal year ended June 30, 1950 declined to \$5 billion from the high of \$6.4 billion in the previous year. This represented the sharpest year-to-year change during the postwar period, and brings the 1946-50 annual average to \$5.7 billion.

The decline, as chart 1 makes clear, was greater for credits than for grants. The latter accounted for 92 percent of total aid in fiscal year 1950—as against 83 percent in the preceding year.

Chart 1.—U. S. Government Foreign Grants, Credits, and Net Foreign Aid Since Inception of European Recovery Program



Source of data: U. S. Department of Commerce, Office of Business Economics.

Other transactions of the United States Government abroad, mainly cash disbursements and receipts for goods and services, were also lower than in the preceding year. Thus the excess of disbursements over receipts declined from \$1.4 billion in 1949 to \$800 million in fiscal year 1950.

Outstanding among the new developments of the past fiscal year were (a) the initiation of the Mutual Defense Assistance Program (MDAP), (b) the enactment of legislation to implement the Point Four Program which had been

NOTE: This article was prepared by the Clearing Office for Foreign Transactions, Office of Business Economics, and is a summarization of data compiled and published in detail each quarter by that Office.

stressed by the President in his inaugural address early in 1949, and (c) the establishment of a new program of economic aid for the Far East.

Gross foreign aid rendered by the United States Government in the five postwar years ended June 30, 1950 aggregated \$28.1 billion, with its composition as shown in table 1. This is exclusive of the Government's investment of \$3.4 billion in the International Bank for Reconstruction and Development and the International Monetary Fund.

Government aid has played a substantial part in financing the export surplus of the United States throughout the postwar period. The recent decline in aid has been accompanied by an even greater reduction in the margin of exports over imports.¹ Moreover, the sharp curtailment of aid in the form of long-term Government credits has contributed to the reversal in the flow of net foreign investment.

Returns to U. S. increasing

The objectives of the major foreign-aid programs in the postwar period have varied from the supplying of elementary civilian needs to economic reconstruction and development—and, more recently, to the attainment of military security. To the extent that the objectives have been achieved, the United States has also gained in economic well-being and security, although these are hardly capable of measurement in financial terms.

In addition, a number of tangible returns have been received in the form of reverse grants, and returns on grants, as well as collections of principal on credits. By deducting these from gross foreign aid for the period in which the returns were reported, the net flow of aid for any given period is derived. On this basis, net foreign aid declined from \$5.9 billion in fiscal year 1949 to \$4.4 billion in 1950, evidencing a decline somewhat larger than the reduction in gross foreign aid. The difference was the result, of course, of the small increase in aggregate returns.

To the extent that collections of principal will increase in the future on the basis of repayment schedules, returns should rise, having the effect of further reducing net foreign aid.

Three countries—the United Kingdom, Germany, and France—accounted for almost half of the total net foreign aid in fiscal 1950. As shown in chart 2, aid to China declined most sharply from 1949 to 1950, but substantial declines were recorded for almost all of the major countries.

Congressional authorizations mount

Gross foreign aid is measured largely on the basis of cash disbursements for commodities purchased through private channels of trade, or actual shipments of Government-procured items. Realization of this aid in the foreign economy normally lags behind the procurement authorizations or the obligation of funds for budget purposes. There is therefore a substantial carry-over from one year to the next under most foreign-aid programs.

Largely as a consequence of this lag, \$5.4 billion of aid

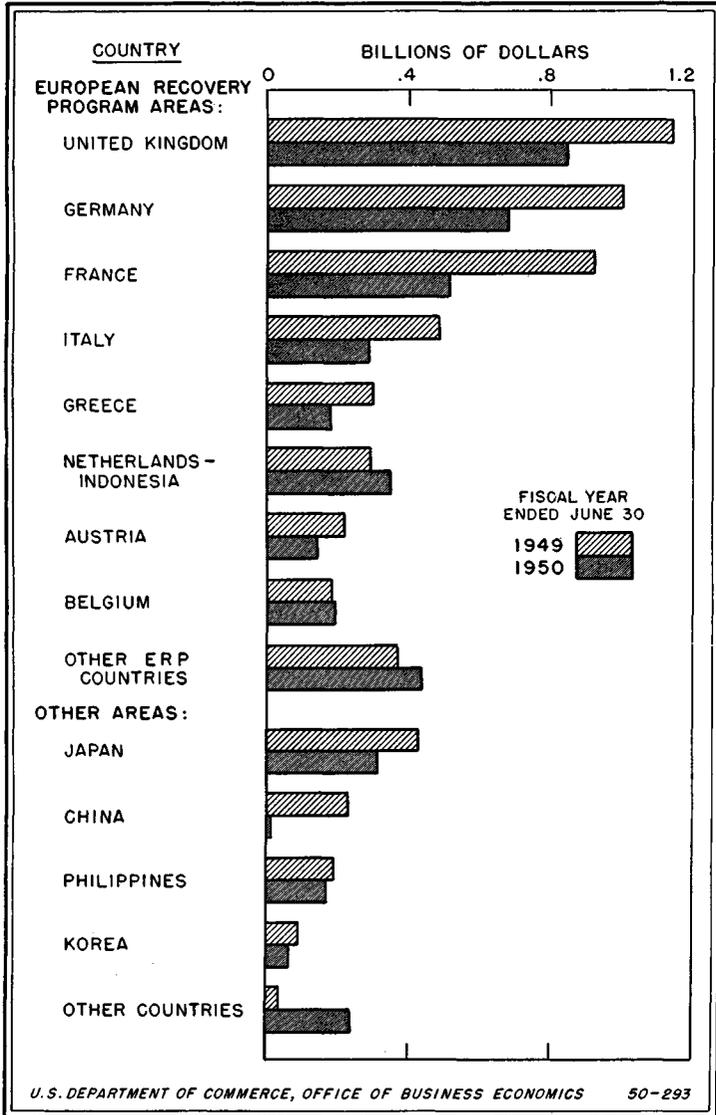
¹ See SURVEY OF CURRENT BUSINESS, September 1950, "Balance of International Payments, Second Quarter of 1950" by Walter Lederer.

authorized earlier was available after the end of the 1950 fiscal year for the continuance of foreign-aid programs. About two-thirds was designated for grants and the remainder for credits.

Developments touched off by the invasion of South Korea on June 25, 1950, have greatly altered the outlook for additional new foreign aid and other activities abroad.

New authorizations and appropriations by Congress from July through September 1950 will provide \$8.7 billion in addition to the carry-over—making a total of \$14.1 billion now available for grants and credits after July 1, 1950. Almost all of the new funds are for grants; the only new credit authority is that of \$62.5 million for a loan to Spain.

Chart 2.—U. S. Government Net Foreign Aid, by Countries



Source of data: U. S. Department of Commerce, Office of Business Economics.

The Korean crisis was also largely responsible for the supplemental appropriation of \$4 billion for MDAP—almost half of the new appropriation now in prospect for fiscal year 1951. Because of the time required to procure many articles of heavy equipment, especially military items, a substantial part of these newly appropriated funds will not be translated into actual shipments by the end of the present fiscal year. However, if these available funds were to be fully utilized, cumulative postwar gross foreign aid would then exceed \$42 billion.

European Recovery Program predominates

By the end of the 1950 fiscal year the European Recovery Program had accounted for gross aid of \$7.6 billion, or 60 percent of all foreign aid extended within the 27-month period that the program had been in operation. Although the actual aid rendered declined from \$4.1 billion in fiscal year 1949 to \$3.4 billion in 1950—in accordance with the plan for its gradual reduction—it increased in relative significance in that time from 63 to 68 percent of all foreign aid. With the growing importance of military aid, the proportion of the total represented by the European Recovery Program will undoubtedly decline in fiscal year 1951.

The European Recovery Program has been essentially on a grant basis; loans and other credits have accounted for no more than an eighth of gross ERP aid through June 30, 1950. However, the decline in this aid between fiscal years 1949 and 1950 took place largely in credits; aid on a grant basis increased. There had been a growing realization that many member countries had approached the limit of their credit as evidenced by their probable capacity to repay. Thus, the proportion of gross ERP aid on a credit basis declined sharply from 21 percent in 1949 to 3 percent in fiscal year 1950.

Whereas in the first year of ERP more than half of the aid was in food, feed, fertilizer, and fuel, the proportion of such commodities declined to less than one-third in the year ended June 30, 1950. Capital goods in the form of raw materials and semifinished products, with machinery and vehicles, became the major items.

The broad economic impact of the recovery program is indicated by the fact that at the end of June only two-thirds of the total program expenditures were for commodities produced in the United States—the remainder coming primarily from Canada and the American Republics as well as directly from the participating countries. Moreover, the aid data grouped by participating member countries as in tables 2 and 3 do not indicate the broad geographical scope of other phases of the program—such as projects involving technical assistance or the development of deficiency materials for the United States stockpile.

For example, at least six ERP participants—Belgium, Denmark, France, Netherlands, Portugal, and the United Kingdom—are receiving technical assistance in the development of their dependent territories. The bulk of these approved projects have been in Africa, but others are in the Western Hemisphere and in the Far East. While only a small amount of total available aid has been allocated for this purpose, this activity represents a significant precursor to the President's Point Four Program, discussed below.

European Payments Union created

Aid under the ERP has been allotted to participating countries as a general rule on the basis of the dollars needed to balance the international accounts of each participant in the program. For the most part, aid is accounted for in terms of dollar payments for private shipments, and the cost of United States Government shipments; that is, the basis of the record shown in tables 1 and 2. However, since the program is based on the principle of mutual aid—each participant, according to its ability, being obligated to help others—part of the grant aid rendered by the United States to the various participants has been governed by the amount of their own contributions of goods supplied to other participants. As a consequence the total aid received by each participant may be more or less than that directly provided by the United States.

The effects of the operation of this procedure—known as the intra-European payments plan—are shown in table 3.

Unless otherwise stated, statistics through 1948 and descriptive notes are shown in the 1949 Statistical Supplement to the Survey

Table with columns for years: 1949 (September, October, November, December) and 1950 (January, February, March, April, May, June, July, August, September)

FOODSTUFFS AND TOBACCO

Main data table with categories: ALCOHOLIC BEVERAGES, DAIRY PRODUCTS, and FRUITS AND VEGETABLES, including various sub-items and their monthly values from 1949 to 1950.

* Revised. 1 December 1 estimate. 2 October 1 estimate. 3 Revisions prior to 1949 are shown on p. 24 of the August 1950 Survey.

