The 1958 Survey of the Economy

The 1958 Survey of the economy issued by the Commonwealth Government in May achieves the same high standards of reasonableness and clarity as its two predecessors. The authors, commendably, maintain an air of intellectual humility. They concede that the surveys do no more than put forward a point of view and that "it is likely that, both generally and in detail, many will disagree with that point of view. It can only be for good if they do in that way succeed in promoting intelligent controversy on matters which have so many aspects and which affect people in so many different ways". But although of considerable educational value, the new Survey is the least satisfying of the three. Analysis too frequently stops short just when it is becoming really interesting; problems are confronted but not always grappled with.

It would be unfair, however, to lay the deficiencies of the Survey at the door of the government officers chiefly responsible for its preparation. The defects are inherent in the nature of the document itself. The ultimate responsibility for its contents does not rest with the departmental experts; it rests with the Commonwealth Government. The annual Survey must therefore be a document with more or less strong political overtones, not an independent, economic appraisal made by experts untrammelled by political considerations. Unless this is understood, the contents of the Survey cannot be properly assessed and interpreted. What is inferred is sometimes more significant than what is directly stated; what can be read between the lines is often more important than the lines themselves.
Nor can the Government be entirely blamed for the deficiencies of the Survey. The Government must, perforce, defer to the dictates of politics, and the experts must, perforce, defer to the Government. And if the 1958 Survey is less venturesome in some respects than the Surveys preceding it, this is understandable (1958 is after all an election year). It is hardly to be expected, for instance, that it would exhibit the same degree of frankness (and even bluntness), the same readiness to say the unpopular thing, as the recent report on the British economy by the Cohen Committee, an independent body of experts with freedom to say what it wished.

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The key to the approach taken in the 1958 Survey is to be found in a phrase which appears on page 21: "... it is important for confidence to be sustained and asserted". Here, of course, is the old dilemma of the economist and of spokesmen for the reigning government. How far is it wise for them to go in saying what they really think? If dark clouds are looming, is it best to ignore them, or, at the most to suggest that they will probably result only in a mild shower or two, on the grounds that to do otherwise could give rise to a loss of confidence which would itself precipitate an economic storm? It is the dilemma whether, in economic matters, it is wise for the full story to be told or whether some concealment, at least of unpleasant possibilities, is justified lest confidence be shattered.

The Survey clearly takes the stand that confidence is all-important. In face of an overseas situation less than reassuring it contrives, therefore, to throw the rosier possible glow over the Australian economy. It achieves this both by its treatment of the immediate past and its approach to the problems of the future.

By selecting early-1956 as a basis for comparison it is able to show an economy which has gained notably in strength and stability over the past two years. The balance-of-payments position has improved out of recognition—there has been a vast accretion to overseas reserves of some £200 million. Import restrictions have, as a consequence, been considerably relaxed. The finances of the Commonwealth Government are in much better condition. Population has
increased by the best part of half a million. Employment—
although not at boom-time levels—is still high. Praiseworthy
advances both in industrial output and productive capacity
have been achieved. The rate of home building has been
rising in recent months although, in 1957, other forms of
building declined somewhat. Expenditure on public works
has expanded not merely in money terms but also in the
volume of activity undertaken. The picture presented is
altogether one of substantial industrial development and of
enhanced economic strength.

But all this is scarcely surprising, since in early 1956—
the base for comparison—the economy was moving in dan-
gerous waters. Indeed, the threat of a major crisis induced
the Government to appoint a special economic committee
and later to introduce an emergency budget. The Survey
thus chooses one of the lowest points touched by the economy
since the war to provide a contrast with the present situation.
But all this happens to be of no great significance at the
moment. Following the tremendous and unexpected bounty
of the 1956/7 wool season, the improvement over the last
two years was as inevitable as day after night. Common-
wealth Government policy in its recent fight against cost
and price increases contributed something of value. The
abolition of the quarterly wage adjustments by the Common-
wealth Arbitration Authority as far back as 1953 was also
helpful. But the preponderant reason for the recovery since
1956 need be sought no further than the wool market. In
the delayed effects of the 1956/7 wool season is also to be
found the main reason for the buoyant state of the economy
in the financial year just ending.

W hat is significant for the economy at the moment is
the present and prospective state of the external balance
of payments. On this over-riding topic the new Survey
rather conspicuously fails to reach the high standard of
analysis and appraisal achieved in 1957. The Survey, ad-
mittedly, does not shrink from enumerating the gathering
clouds in the external scene—the fall in world commodity
prices (wool down 35%, metals 30% and butter 20%), the
flattening out of world production and trade and the American
recession—and the impact on our balance of payments and
international reserves. Exports for 1957/8, the Survey points
out, will not be much above £800 million compared with £980 million in the previous year. International reserves could fall by £70 million which would leave us with around £500 million at the 30th June as compared with £567 million a year previously. This leads the authors of the Survey to say: "Australia is therefore, in that respect, still in a not uncomfortable position and the Government has announced that import licensing is being continued on the basis of imports at approximately £800 million in 1958/9."

But the important thing is what is likely to happen in 1958/59. Here the Survey, perhaps wisely, refrains from indulging in arithmetical forecasts—although there can be no doubt that forecasts of the course of events must be a leading preoccupation in departmental circles at the moment. But published predictions are dangerous, not only because, in the Australian context, there is a high degree of probability that they will be wrong; but because cautionary thoughts about the future in these days of boom psychology are not merely unpopular, but are regarded as little short of treasonable. The Survey, however, does say bluntly: "Externally it has been apparent for some months that the world economic context has become less favourable to us and, whilst this trend has not had any major impact on our local situation so far, there should be no mistaking the possibilities of trouble it could hold for the future." And it points out that "we require an export income of at least £900 million a year, together with a fair amount of capital inflow, if we are to keep up a reasonable flow of imports without using up our reserves at a hazardous rate. Exports, however, have lately been running at much less than £900 million a year." (Earlier the Survey states that export income for 1957/8 is not likely to be much above £800 million.)

The crucial question then is the prospect for 1958/9. Unless there is a quite solid recovery in wool prices, and if improvement in America continues to be slow (as seems probable at the moment) export income is unlikely to reach the 1957/8 estimate of around £800 million. In these circumstances (which represent, it must be stressed, a possibility, not a prediction) we could face a drop in reserves of close to £150 million in 1958/9. This is clearly the sort of situation the Survey has in mind when it says: "... ordinary
prudence requires that we should think ahead to the kind of problem that could arise if recovery abroad were unduly slow and that we should try to assess candidly the courses of action which, under these circumstances, it would be practicable and wise to take.”

This is the critical point of the entire Survey, but it is just the point at which the Survey falters badly. The Survey fails to do what it says it is going to do—that is “assess candidly the courses of action which it would be wise and practicable to take.” All it does is to affirm that our main objective must be to keep expansion moving at a steady rate and to keep up the flow of migrants. In that objective everyone would concur. The vital thing, however, is not the objective, but its feasibility in face of a balance-of-payments position which is assumed to be deteriorating rapidly. The objective is, of course, wholly desirable. The only question is: “Is it practicable?”

It is surely a delusion to suppose that a certain rate of economic expansion can be established and that this can be maintained, through thick and thin, irrespective of external influences on the economy and consequent changes in internal prosperity.

It is true—as the Survey claims—that the threatening situation which developed early in 1956 did not compel a drastic reduction of the development programme. In that respect it may, at first sight, seem that the Government’s bold determination at that time to proceed with large-scale immigration and development proved, in the event, to be right. Even so there has been, over the last few years, a noticeable easing off in migration. In 1955 the net migrant intake in round figures was 97,000. In 1956 it fell to 94,000 and in 1957 to 79,000. This fall has taken place despite the Government’s declared objective of maintaining a stable level of migration and despite the great improvement in the external position in 1956/7 when exports reached an all-time record level, higher even than that achieved in the Korean boom year.

What would have been the position if 1956/7 had turned out as the Government had anticipated in early 1956 (i.e. exports at around £770 million instead of the actual figure of £980)? There is no shadow of doubt that the net migration target of 1% (equal to 95,000 in 1956/7) would
have been unattainable. As it was 1956/7 proved to be infinitely more favourable than the Government or, for that matter, anyone else expected, and yet the actual figure still fell 10,000 short of the target.

* * * *

The hard truth is that it is impracticable to maintain a steady rate of development and migration in an economy subject to such wide and precipitous swings in external income as the Australian, and in light of the difficulties of obtaining an even flow of acceptable migrants. The year-by-year graph of the migrant intake since the war confirms this indisputably. The figures of net migrant intake since the launching of the migration programme in 1947 are as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Intake</th>
</tr>
</thead>
<tbody>
<tr>
<td>1947</td>
<td>10,611</td>
</tr>
<tr>
<td>1948</td>
<td>55,115</td>
</tr>
<tr>
<td>1949</td>
<td>150,001</td>
</tr>
<tr>
<td>1950</td>
<td>152,505</td>
</tr>
<tr>
<td>1951</td>
<td>111,433</td>
</tr>
<tr>
<td>1952</td>
<td>94,032</td>
</tr>
<tr>
<td>1953</td>
<td>42,897</td>
</tr>
<tr>
<td>1954</td>
<td>68,207</td>
</tr>
<tr>
<td>1955</td>
<td>97,255</td>
</tr>
<tr>
<td>1956</td>
<td>93,998</td>
</tr>
<tr>
<td>1957</td>
<td>78,732</td>
</tr>
</tbody>
</table>

The story is one of an intake fluctuating widely in response to changing economic conditions.

The rate of economic expansion possible for Australia can never be divorced from the state of its external finances. Should there be a rapid drain on international reserves through the coming financial year, with no early recovery in sight—and this is the assumption made in the Survey—the Government would be forced to retreat from the objective it has so boldly set itself.

Economic policy is concerned not so much with what we would like to do; it is concerned with what we can do in light of all the circumstances in which we are placed. A high rate of development and a weak external financial position are incompatibles, both economically and politically.

But, to use the words of the Survey itself, “this is not, in any sense, a forecast of accumulating difficulties. Developments may not take such a turn at all. Recovery abroad may occur well ahead of the stage at which our difficulties start to become critical.” It remains to be seen. At present nobody knows.
Tax Reductions!

It seems likely that some reductions in taxation will be made in this year's Commonwealth Government Budget.

The reasons for this presumption are mainly political. But economic considerations also play some part.

1958 is an election year and the Government will therefore be more favourably disposed toward tax reductions than it would be in other years. The understandably natural desire to please in the forthcoming Budget is reinforced by one or two important facts in the economic picture.

For the time being, the inflationary tendencies in the economy appear to have moderated. Prices generally over the last twelve months have been steadier than in almost any year since the war. The employment position is better balanced than for some time past and business generally more healthily competitive. There are even some strong deflationary forces in the economy, which, though at present largely latent, could become active in the fiscal year 1958/9 and that is the year the Government must have in mind in framing its budget.

The main one is the substantial falling away in farm income due partly to near-drought conditions, but largely to the slide in export prices for major commodities, chiefly wool. It would be foolish to attempt to predict what will happen next year in a field of such uncertainty as export production, but present indications are not favourable. Dry conditions are continuing throughout important parts of the country, whilst the pace of recovery from the American recession, with its vital significance for the level of commodity price levels, seems certain to be gradual (see article by Professor Condliffe on page 56). On a pessimistic assessment, 1958/9 could conceivably be a bad year for primary production and exports.

All in all, in order to maintain business activity and employment in the months ahead, it may be necessary to
give a stimulus to spending. One way of doing this would be through a reduction in the tax burden, even if this compelled some mild recourse to Treasury Bills.

It is true, of course, that the Government would be most unwise to jeopardise the newly won stability in the economy, especially in view of the decline in world commodity prices, but at least it can be said that, from the strict standpoint of economic policy, conditions are more propitious for tax reductions this year than for quite a time past. On the other hand the high hopes held earlier in the year of sweeping tax cuts now seem hardly likely to be realised because of the accumulation of budgetary difficulties facing the Government. The steep fall in farm incomes and in exports, taken in conjunction with the inevitable increase in the cost of social services and the large maturing debt in 1958/9, pose an unenviable financial problem for the Government.

As tax concessions are not likely to be unlimited, it is of special importance that the concessions should be made where they will do the most good. In this respect, two main considerations must enter into the Government’s calculations. The first is the effect of any cuts on the economy; this simply means that the taxes which should be reduced are those that weigh most heavily against the basic objectives of economic efficiency and industrial productivity. The second consideration which the Government must take into account is that of social justice. In other words the opportunity should be taken to provide relief for those sections of the community which have benefited least—or suffered most—in recent years from relative movements in incomes and the arbitrary redistribution of wealth brought about by the inflationary process. In determining the nature of the concessions to be made, there is a clear obligation on the Government to do something—even though a little—to restore a measure of financial justice as between different sections of the community.

Fortunately, at the present time, the two criteria of economic policy and social equity point in the same direction: Namely, that any tax reductions granted in the forthcoming Budget should be concentrated mainly in the field of personal income tax.

* * * * *
In last year's Budget business received the major benefit from the limited concessions that were made. Company tax was lowered by 6d. in the £; depreciation allowances were liberalised; and the exemption limit for liability to payroll tax was raised. Some reductions were also made in sales taxes. The total cost to revenue of the tax concessions granted was estimated to be nearly £57 million in a full year.

Only minor concessions, involving mainly an increase in allowances for dependants, were made in the personal income tax field. These concessions amounted to about £8½ million.

What is to be done this year? A strong argument can, of course, be made out for the reduction of certain business taxes. Payroll tax is a case in point. Probably there is no other tax so unpopular in business circles. It certainly possesses many weaknesses and no one, probably not even the Treasury experts, would be sorry to see it abolished in its entirety. It is inequitable as between different businesses in that it falls most heavily on those with a high labour content in their costs; it has a peculiarly snowballing impact on prices; and it could be construed in a sense as a tax on employment since, from the businessman's standpoint, it amounts in effect to an addition to wages. The great obstacle to its abolition at one fell swoop is that it is a prolific source of revenue (this year it will probably produce some £50 million).

For various reasons, the abolition of the tax would result in the loss of less than this amount in revenue. But the loss would certainly be substantial and would seriously narrow the scope available to the Government for tax concessions in other directions. It is clearly impossible to have everything. Realism compels us to recognise that what we are faced with is, at best, a series of choices. There are priorities in tax reductions, as with most things in life, and whilst the payroll tax is undoubtedly high on the list, there are others which rank above it. But one would hope that a further step towards its ultimate abolition will be possible in the forthcoming Budget.

Another business tax for which a logical case for relief might be argued is company tax. This was raised by 1/- in the £ of taxable income in the interim Budget of March, 1956, to help counter the threatening economic situation developing
Inflation was galloping ahead internally and overseas reserves were sinking perilously close to rock bottom. The 1957 Budget made some recognition of the remarkable and unexpected economic improvement achieved in 1956/7 by reducing the tax by 6d. to its present rate of 7/6 in the £. It could be argued that the conditions which made the tax necessary as a restraint on activity in early 1956—though everyone did not concede its necessity—have vanished and that the addition made at that time should now be entirely removed. Whether this will be done may depend on the cost to revenue of such a measure and the total scope available for tax reductions. The first is not likely to be less than £10 million. The second is unknown—at any rate outside government circles. If it is reasonably substantial then the Government should seize the opportunity to restore company tax to the level preceding the interim Budget of March, 1956, namely 7/- in the £. If the scope for tax concessions is limited, then a wise policy might prefer to concentrate them on the personal income tax field and defer the 6d. reduction in company tax for another occasion. Something here, however, will depend on prognostications of the business outlook for 1958/9. If it is believed that a further fall-away in farm incomes is likely, and that this may react adversely on business prospects, then it may rightly be felt that companies should be assisted and business stimulated through lightening the burden on profits.

There is a great deal of dissatisfaction among business people with the taxation of private companies, chiefly on the grounds that the 10/- in the £ levy on profits not distributed, gravely restricts the opportunities of natural growth and expansion of the smaller business, particularly by comparison with the well-established public company with much readier access to outside sources for its capital requirements. This matter deserves serious consideration by the Government. The one thing that the free-enterprise economy should avoid at all costs is to hamper the rise of the virile, enterprising businessman. It has been suggested by some tax experts that a private company above a certain size should be free to choose whether it should be treated for tax purposes as a public or private company. Consideration might also be given to increasing the scale of retention allowances (i.e. amount not taxable) applying to undistributed profits.
Should the economy be threatened with a deflationary down-turn, it might also be desirable to consider a further increase in permissible depreciation allowances in order to stimulate capital investment. Last year's Budget went part of the way to meet the recommendations of the Hulme Committee in 1955. Australian depreciation provisions, however, remain among the least generous of the Western countries, and the trend must be toward further liberalisation. In previous years arguments advanced in favour of faster depreciation write-offs have usually been rejected on the grounds that in a time of inflation and over-full employment it was undesirable to give an additional stimulus to investment. The crux of the case against higher depreciation loses some of its force under the new policy of "stabilisation" and would vanish entirely should economic conditions threaten to become deflationary.

ONE additional point might be given consideration in the coming Budget. Many of the optimistic hopes held about the economic future of Australia are based on the discovery of rich mineral deposits in recent years and the belief that further important discoveries are certain to be made. It is undoubtedly vital to our development that they should be. It might be desirable for the Government to give special encouragement to mineral exploration, perhaps along the lines of Canadian tax laws which permit a tax-free period of three years in the initial production stage of any new mine.

There remains the field of indirect taxation represented by sales taxes and excise duties. In the 1957 Budget a small, but commonsense, reduction was made in rates of sales tax on household furniture and appliances. With the costs of establishing or improving a home representing such a frightening burden on the family man, a further move in the same direction would be widely applauded. But it would be hard to justify any great or general reduction in sales taxes, as this could only seriously narrow the scope of easing the load of personal taxation. Indirect taxation does not have the same frustrating effect on incentives as does personal income tax, and if a choice has to be made between the two, the decision must be strongly in favour of the latter.
It would be nice to see rates of general sales tax cut back sharply, but the room for tax concessions is not likely to be sufficiently extensive to permit this to be done. Australia, after all, raises a smaller proportion of its governmental revenues by means of indirect taxes than other Western countries, and the case for widespread reductions in sales taxes may have to give way to the stronger need for lightening the load of personal income tax. This would not necessarily rule out the possibility of selective cuts designed to relieve difficulties in particular industries.

* * * * *

The need for relief in personal income tax is most urgent in the middle range of incomes occupied mainly by professional men of high educational qualifications and salaried business executives carrying positions of more-than-ordinary responsibility. In recent years these sections of the community have been frustrated by inflation which has not only made serious inroads into their real earnings but which has also hoisted them into a higher income bracket where any extra earnings attract an extremely heavy tax burden.

In 1948/9 the man in a £1,000-a-year job was able to keep 13/6 of every £ he received by way of, say, a Christmas bonus; today the man in an equivalent job returning say £2,000 a year would only be permitted to keep 12/11. The marginal tax rate becomes much more severe as incomes increase. For instance, on a £5,000-a-year income, the rate becomes 11/-; on £6,000-a-year, 11/7; on £8,000, 12/1; on £16,000, 13/4.

If only because of the effect of inflation on the level of money incomes over the last decade, it would seem that the personal income tax structure is due for a general overhaul. For instance, a million and a quarter Australians now earn over £1,000 a year, compared with only 63,000 in 1946/47.

In the past the middle income-earners have been strong savers. For many of them in recent years, savings, apart perhaps for ultimate retirement, have been out of the question. They have been forced to virtually utilise the whole of their
current income to meet their current expenses. No matter how hard they work, or what moderate increases in their money incomes they are able to achieve, their economic position appears to remain “as you were”. Attempts to achieve even modest additions to their capital resources have been generally frustrated by rising prices, increasing commitments, and the heavy subtractions from additions to their income made by high additional amounts of tax.

At present many of the middle income-earners are unable to regard their financial future with much optimism. Yet the community, and more narrowly the businesses which they serve, are greatly dependent upon the drive, enthusiasm and ambition which they bring to their daily tasks. If there are to be just rewards and proper incentives for education, for professional skills, for organising talents, and for qualities of enterprise and leadership, then something should be done to improve their prospects. It is not within the competence of one Budget to do the trick entirely, but at least the Government can show that it is not unaware of their difficulties and is prepared to give them some ray of hope.

Neglect to do so by a free enterprise Government would amount to a negation of the basic principles which it professes and would sow the seeds of serious trouble for itself in the future. The man of talents and ambition must have reasonable opportunity to advance and to make his way in life. At present opportunity is for many much too restricted. If justice is to be done the 1958 Budget must above all be a “middle class” Budget.
The rapid increase in personal debt (i.e. debt incurred by people in a private capacity for the purchase of homes, cars and other durable consumer goods) is one of the most striking economic developments of recent years. It represents almost a revolutionary break from past habits of consumer buying. Its wider significance for the economy has yet to be assessed; surprisingly, economists have devoted little attention to it. In the short space of five years the total of personal debt on housing and durable consumer goods has more than doubled. As a proportion of all incomes (after tax), hire-purchase outstandings on consumer goods have grown from approximately 4½% in 1955 to over 6% in 1958. In 1939 the comparable percentage was 2. Including housing, personal debt has increased from 14% of incomes in 1947 to 30% in 1955, to 36% in 1957. It is clear that a large section of the community are now mortgaging a far greater share of their future income than they were accustomed to in the past.

It is unfortunate that only the most rudimentary information is available on a subject of such economic and social importance. To go into any detail it is necessary to make estimates which are little better than informed guesses.

By contrast, in the United States, the fullest particulars are collected on the various aspects of private debt—both for housing and for consumer durables. This data is of some help in attempting to appraise the position in Australia. Two in every three American families are now in debt against little more than one in every three in 1941 (the pre-war high) and in 1948. The people most responsible for the increase in debt are young couples in the middle-income brackets. 80% of middle-income families are in debt against 50% in 1948. Fixed payments on instalment debt, insurance and housing now absorb 30% of all American incomes (excluding those of farmers) as against 20% in 1948.

Owing to paucity of statistical information it is impossible to make similar comparisons for Australia. But there can be no doubt from the total figures that debt is also grow-
ing rapidly in this country. The table below endeavours to trace, within the limitations of the material available, the history of debt in relation to disposable personal income—i.e. income after tax—since 1939 in Australia and United States.

**Personal Debt as a Percentage of Personal Income after Tax United States and Australia.**

<table>
<thead>
<tr>
<th></th>
<th>U.S.A.</th>
<th></th>
<th></th>
<th>Aust.</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>%</td>
<td>%</td>
<td>%</td>
<td>%</td>
<td>%</td>
<td>%</td>
</tr>
<tr>
<td>Family Housing</td>
<td>23</td>
<td>17</td>
<td>33</td>
<td>36</td>
<td>20</td>
<td>12½</td>
</tr>
<tr>
<td>H.P. Debt on Cars</td>
<td>2</td>
<td>1</td>
<td>5</td>
<td>5</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Other H.P. &amp; Instalment Debt</td>
<td>4</td>
<td>3</td>
<td>6</td>
<td>6</td>
<td>1</td>
<td>1½</td>
</tr>
<tr>
<td>Total Debt</td>
<td>29</td>
<td>21</td>
<td>44</td>
<td>47</td>
<td>22</td>
<td>14</td>
</tr>
</tbody>
</table>

**Notes and Sources:**

1. Australian figures end June 30th.
3. As complete information on personal debt in Australia is unobtainable, the Australian figures above are to indicate broad trends and not exact magnitudes.
4. Mr. M. Hill of the Commonwealth Bank has assembled statistics of advances for housing by major lenders, i.e. building societies, the War Service Homes Commission, the banks and the life offices; but practically nothing is known about advances by a variety of small lenders such as individuals, solicitors and investment and finance companies. On Mr. Hill's figures, outstanding advances by major lenders appear to have risen, in round figures, from £100 million in 1945 to £400 million in 1952, to £800 million in 1957. Total housing debt in 1957 could be £1,200 million. Victorian statistics suggest that in 1957 major lenders accounted for about 2/3 of new mortgages.
5. The Commonwealth Statistician has been collecting statistics of balances outstanding on hire-purchase agreements made with finance companies (including subsidiaries of retailers) since 1953. This figure has risen from £89 million in June, 1953, to £276 million as at 31st March, 1958 (£236 million at 30th June, 1957). In addition, there are hire-purchase debts owing to sundry retailers, currently estimated at over £50 million. Portion of hire-purchase outstandings relate to producers' goods such as farm and industrial machinery, commercial equipment, trucks, vans and business cars. These have been excluded from the table above to make the figures comparable with United States.
6. The figures in the table relate the total amount of debt outstanding in any one year to the total of all personal incomes (after tax) earned in that year. Thus, the percentages shown do not represent the proportion of personal income (after tax) devoted to the repayment of debts. It should also be emphasised that the proportions refer to the nation as a whole.

Although housing debt appears to be slightly larger relative to income in the United States, the rate of growth seems to have been more rapid in Australia, particularly over the last few years. Hire-purchase debt also seems to be expanding at a faster rate in Australia, notably since 1955. In the United States the upward trend in home mortgage debt has slackened and, in the case of consumer credit, has completely flattened out. (Latest information is that total consumer debt in United States has commenced to decline.)

* * * * *

Rapid Trend to Home Ownership

The accelerated trend to home ownership has been similar in the two countries because of high incomes, shortage of rentable housing and liberal mortgage lending policies. The proportion of owner-occupied dwellings in United States has grown from 44% in 1940 to over 60% in 1956. In Australia 65% of homes are now occupied by their owners as compared with 55% in 1947, 47% in 1933, 45% in 1921 and 36% in 1911. In the United States, the Federal Housing Administration and the Veterans' Housing Administration, by guaranteeing advances from private investors on extremely liberal terms, have been mainly responsible for the rapid upward surge in home mortgage finance. Very little of the money has, however, been furnished directly by the U.S. Federal Government itself. It has come mostly from savings banks and savings loan associations, life assurance companies and the commercial or trading banks.

In Australia, the increased tempo of home ownership (and, with it, mortgage debt) over the past decade has arisen from three basic causes. First, booming export prices and a sustained development programme have meant full employment and high incomes, with a growing demand for home
ownership as part of the over-all improvement in living standards. Second, rent control and high costs have brought about a dearth of rental housing. The erection of new properties has ceased to be attractive to investors and, furthermore, the sale of existing houses to tenants has often proved to be a better proposition for the owner than letting at controlled rents. Because of the shortage of rental housing, people who may have preferred to be tenants have been forced to become home-owners in order to secure accommodation.

Third, finance has been made available, as a deliberate act of policy, on a far greater scale and on easier terms than in former years. As in the United States, ex-servicemen especially have been assisted by the Federal Government in securing their own homes through small deposits and extended terms at low rates of interest. Advances by the War Service Homes Commission have risen from £10 million in 1947 to £200 million in 1957. Since 1955 tenants in Housing Commission homes have been encouraged to buy them on terms. State Governments have also been particularly active over the post-war period both in facilitating the flow of money to home-owners from their own resources and through guaranteeing loans made to co-operative building societies by banks, life assurance companies and other institutions. The co-operative building society movement has made massive strides since the war, especially in N.S.W. and Victoria. The 1956 Commonwealth-State Housing Agreement gave a boost to co-operative housing by providing that 20% of Commonwealth funds for housing have to be allocated to co-operative housing societies—the proportion is to rise to 30% in 1959/60. Traditional lenders, such as the Commonwealth Bank, State Savings Banks and Life Assurance Societies, have been able to step up advances for housing purposes both to building societies and to individuals because of the great growth in deposits and in life policies.

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Hire-purchase

THE rapid rise in hire-purchase credit, which began in Australia only five or six years ago, has been associated with a surging demand for motor cars, electrical appliances
The Growth of Personal Debt (continued)

such as refrigerators, washing machines, radios and, recently, T.V. sets. Bearing in mind the higher potential demand for consumer durables in United States—due to larger incomes and also relatively cheaper prices (because of mass production economies)—the rise in consumers' hire-purchase debt in Australia from 1% of personal income (after tax) in 1947 to 54% in 1957 is remarkable. In United States the rise in consumer debt has been from 4% of disposable personal income in 1947 to 11% in 1957.

Over the last few years there has been a great expansion in the activities of finance companies which handle most hire-purchase business in Australia. Some of these companies have assumed giant proportions. In addition to the moneys provided by their shareholders, through short-term note issues they now mobilise vast funds from companies, superannuation trustees and individuals for the financing of hire-purchase operations.

Along with an increased demand for houses and consumer durables and the greater willingness and ability of financial institutions to lend money for these purposes, there has been a marked change in the national psychology towards the incurring of debt. People are now much more prepared to enter into financial obligations which they can only expect to repay out of future income spread over a number of years. Indeed, because of a succession of new purchases, some borrowers probably never anticipate getting out of debt. There is perhaps a grain of truth in the saying that many car users never see car ownership papers because they trade in their old car for a new one before the final instalment is paid.

This attitude to debt has probably been engendered, in the main, by the greater financial security brought about by continued full employment and high earnings over the post-war years. People now have much more confidence in their long-term financial future. This is in striking contrast with pre-war times when the threat of unemployment and of short-time or reduced earnings hung over the heads of many people. Conscious of this threat, large numbers of people were more disposed to curb their spending impulses because of the rainy day which they believed was pretty certain to
come sooner or later. Memories of the depression were still vivid. There were few families that had escaped its impact. But the depression is now a quarter of a century away and a whole generation has grown up accustomed to the full employment economy, with no experience of either the fact or the threat of economic insecurity.

Ethical attitudes to hire-purchase debt have also changed. Buying on terms no longer carries the stigma of financial irresponsibility. Indeed, inflation has made it good business to borrow while prices are rising, and to repay in depreciated currency. More and more people have become in a way indifferent to the arithmetical size of their debts and are concerned only with the down-payment and the weekly or monthly instalments on their purchases.

While, on the one side, the improvement in all-round financial security has made people more disposed to borrow on their future earnings, on the other side there is today a far greater incentive, almost a need, to incur debt. Apart from the virtual compulsion of buying a home, modern living demands an array of home gadgets and appliances. The luxuries of the 1930’s have become the necessities of the 1950’s.

The decline of domestic help in middle-class homes and the increasing tendency of married women to take up employment have accelerated the demand for all kinds of time and labour saving devices. The place of the weekly laundress has been taken by the automatic washer; the vacuum cleaner and electric floor polisher have replaced the casual help; and the ice-chest has given way to the refrigerator. The decline in home deliveries and the rise of the self-service store have made the motor car necessary for shopping as well as for business and recreational purposes.

A higher average level of real incomes, a greater sense of financial security, a widening variety of wants and a constantly changing array of attractive new products and gadgets have revolutionised consumer spending. A large part of this spending is directed at relatively expensive durable goods, which most people can finance only on hire-purchase terms.

* * * * *
The widespread use of hire-purchase (and the astonishing growth in personal indebtedness accompanying it) has become an integral feature of the modern free enterprise system. It needs no great imagination to see that this development has come to stay and that personal debt is destined to retain the larger place it now occupies in our economic arrangements, compared with ten or twenty years ago.

Consumer credit performs an indispensable service in enabling the majority of people to acquire what have come to be regarded as the essential accoutrements of modern living. The great capital investment in factories making cars, T.V. sets and electrical appliances, and employing tens of thousands, would not have been possible had finance not been available to provide a mass market.

It is, however, a fair question—and one that enters the minds of many people—whether the continued rapid growth in personal indebtedness is entirely sound. Does it contain elements of weakness, that might, in certain circumstances, prove a grave embarrassment not only to the borrowers and lenders indulging in it, but also to national economic and financial stability? Perhaps only time alone will provide the answer to this question.

It can be said broadly that the increase in personal debt, great as it is, should not prove to be unsound so long as reasonable prosperity continues. This is not to say that some people have not already found that they have built up their debts to the point where they are suffering serious financial inconvenience and where they must make hurtful sacrifices in order to meet the recurrent payments. Debt is never unsound so long as borrowers have the continued means to liquidate it. A heavy burden of debt, incurred under conditions of prosperity when incomes are high, requires a continuance of those conditions if financial stability is to be maintained. Should prosperity be succeeded by conditions that are less-than-prosperous, or even depressed, then the debt burden could clearly prove a source of embarrassment to debtors and creditors and to the economy as a whole. Many people might find that debts which they had incurred in better times had become beyond their capacity to carry or
at least to carry without great financial inconvenience. Some might be forced to default, with loss both to themselves and to lenders.

The effects of a fall in incomes arising from depressive external influences on the economy, could be greatly aggravated by a high level of personal indebtedness. The rate of demand for the durable consumer goods which figure so largely in the modern economy can obviously be sustained only if buyers as a whole have both the financial capacity and the willingness to incur new financial obligations. To maintain the volume of time-payment selling, a stream of fresh debt must be constantly coming forward. But, in the event of a general decline in incomes, people could find themselves already over-committed on their existing purchases and reluctant or unable to contemplate new obligations. Sales of durable goods would clearly suffer. But the downward trend could extend also to non-durables such as food and clothing if the loss in income necessitated a cut in expenditure on those items in order to meet debt repayments. The initial fall in spending caused by a general recession could thus be magnified by a too-rapid expansion of hire-purchase debt in times of prosperity.

Several years ago the eminent journal "Fortune" warned American business that personal debt was growing too rapidly and that an eventual slow-down with painful consequences for the economy was inevitable: "Debt may continue for a time to mount furiously, until it has reached a level where it has heavily over-loaded consumers with fixed-debt payments and over-expanded industries depending on these consumers. Then it could go into an abrupt decline, and if this happened at a juncture when other critical components of the economy were turning downward, the turn in consumer credit would powerfully accelerate a general recession." The American recession which has been felt most strongly in the automobile and durable consumer goods industries suggests that this estimate of the future was remarkably astute.

Risk, of course, can never be eliminated from the economic scene. Indeed, risk-taking is indispensable to the functioning of free enterprise. This applies equally to con-
sumers as well as to entrepreneurs. But risk-taking should be prudent and calculated. When incurring debt there are virtues in erring on the side of caution.

* * * * *

APPENDIX

I. Hiring Charges on Hire-Purchase Contracts.

* United States: The most common rate on new cars is 6% to 6½%; on late model used cars 8½%, and on older used cars 12%. In individual cases the rates may be much higher. Rates for household goods are usually above the rates charged on new cars.

* United Kingdom: Charges range from 7% on new cars to a maximum of 12% for most household goods.

* Australia: Most large finance companies charge 6% to 7% on new motor vehicles and 8% to 9% on used vehicles. Rates charged by large companies on new tractors and machinery are 6% to 7%.

Medium companies usually add another 1% or 2% to these rates, but in the case of smaller concerns rates can reach 15% on used cars and household goods. Some retailers charge only 5% or 6% on household goods in order to attract custom. It should be noted that the great bulk of hire-purchase business is on new and used vehicles, and is mainly handled by the large companies.

As hiring rates are charged flat on the initial debt, the interest portion of the monthly instalment remains the same until the debt is discharged, i.e. the actual rate of interest rises progressively on the diminishing balance of the debt.

The effective rate of interest works out at slightly less than double the flat rate.

In comparing hire-purchase charges with bank overdraft rates the following points should be borne in mind:—

i. Hire-purchase companies have to pay higher rates of interest for their money than do the banks. Compared with 2¼% on money at call with savings banks,
large finance companies pay 3½% (smaller companies up to 5%).

Other deposit interest rates for various terms are—

<table>
<thead>
<tr>
<th>Term</th>
<th>Trading Banks</th>
<th>Commonwealth Bonds</th>
<th>Finance Co’s.</th>
</tr>
</thead>
<tbody>
<tr>
<td>3 months</td>
<td>%</td>
<td>%</td>
<td>%</td>
</tr>
<tr>
<td>1 year</td>
<td>%</td>
<td>%</td>
<td>%</td>
</tr>
<tr>
<td>2 years</td>
<td>%</td>
<td>%</td>
<td>%</td>
</tr>
<tr>
<td>3 years</td>
<td>%</td>
<td>%</td>
<td>%</td>
</tr>
<tr>
<td>5 years and over</td>
<td>%</td>
<td>%</td>
<td>%</td>
</tr>
</tbody>
</table>

Trading Banks ... 2½ 2½ 3½ — —
Commonwealth Bonds ... — — — 4 5
Finance Co’s.—
Large ... 3½ 5 5½ 6 6–7
Medium ... 3½–5 5–6 5½–7 6–7½ 7–8

ii. Administrative costs, as well as risk of loss through default, are much higher on small personal loans secured on goods which quickly depreciate in value.


<table>
<thead>
<tr>
<th>As at 30th June</th>
<th>Finance Companies £m.</th>
<th>H.P. handled direct by Retailers £m.</th>
<th>Total £m.</th>
<th>% Increase per annum</th>
</tr>
</thead>
<tbody>
<tr>
<td>1947</td>
<td>13</td>
<td>6</td>
<td>19</td>
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<tr>
<td>1948</td>
<td>22</td>
<td>10</td>
<td>32</td>
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</tr>
<tr>
<td>1956</td>
<td>212</td>
<td>40</td>
<td>252</td>
<td>15</td>
</tr>
<tr>
<td>1957</td>
<td>236</td>
<td>45</td>
<td>281</td>
<td>12</td>
</tr>
<tr>
<td>Mar., 1958</td>
<td>276</td>
<td>52</td>
<td>328</td>
<td>—</td>
</tr>
</tbody>
</table>

Sources: Commonwealth Statistician—finance companies from 1953 onwards and retailers’ debt for 1954. All other figures are very approximate estimates largely based on the work of Messrs. Rowan & Runcie, Sydney and a survey by the Victorian Government Statist for 1956.

III. Hire-Purchase Repayments.

No information is available on this subject but hire-purchase instalments (including producers’ goods) could be now running at 6% or 7% of personal incomes after tax compared with around 4% in 1953/4. In United States consumer instalment credit repayments have declined from 13% of incomes after tax in 1955 to 11% in March 1958.
The American Recession—Too Much, Too Late

by

J. B. CONDLIFFE
Professor of Economics
University of California

Professor Condliffe is an Australian-born economist of international repute. He previously wrote for "Review" in 1953 at the time of the 1953/4 recession in the United States.

We are privileged now to publish his views on the current recession in America which is proving more obstinate and prolonged than many observers expected.

The recession drags on in the United States; though it is hard to discover in most areas. The fall in national income, or more strictly in gross national product, larger and steeper than in any of the preceding postwar recessions, is still only about four per cent. The decline in production and therefore employment is largely concentrated in the heavy manufacturing industries—automobiles, steel, appliances, and other durable goods—with consequential declines in materials and parts. The worst centres of unemployment are towns such as Detroit, Pittsburgh, the steel cities around Chicago, and some of the older manufacturing areas in New England, and the mining areas of the Rocky Mountain states. The decline can also be seen in the statistics of other industries, but not as badly. The reason for the general decline seems to be not so much a fall in purchasing power as increasing caution on the part of consumers. The first quarter of 1958 shows, on the average, a very heavy decline of corporation earnings, mainly but by no means entirely, in the heavy industries. In face of these reports, the stock mar-
ket in recent weeks has staged a fairly considerable rally, the basis of which may be partly technical; but which seems to depend largely on the steady buying policy followed by institutional investors such as insurance companies, investment trusts and pension funds. One of the many reasons why a relapse into a spiralling recession which could get out of control seems unlikely is the maintenance of purchasing power and therefore of both consumption and saving. The food chain stores have stood up very well and the farming industries are prospering, with farm income higher than it has been for years. To some extent, this is the result of the so-called "built-in stabilisers"—mainly unemployment insurance—preventing a short fall of consumer income. But, it is also the result of lower debt and higher levels of savings. There is no oppressive burden of farm mortgages. Time payment liabilities have been and are being reduced. The stock exchange does not depend on heavy speculative purchases on slim margins. On the other hand, there is a continuous growth of savings which are more or less automatic, which must be invested regularly and the returns on which have helped to sustain purchasing power. Few dividends have been passed or reduced so far.

There is no doubt, however, that this is the most serious of the postwar recessions and likely to be the longest. It is greater in magnitude and more concentrated in strategic sections of the economy. It, therefore, exercises a cautionary, if not yet a depressing, influence over the economy of the United States as a whole. Curiously, however, it does not seem as yet to have exercised the same baleful influence on the manufacturing countries of Europe as did the recession of 1949. Rather, its international effects resemble those of 1953-54 which were mild. The United Kingdom, for example, is selling more in the United States and benefiting temporarily from improved terms of trade—buying its imported materials at lower prices and maintaining its manufactured export prices. The result is that the gold which flowed into the United States in 1957 has almost all gone out again—much of it to the Bank of England. This righting of the international balances of payments continues—partly because interest rates have been sharply lowered in New York below London levels, partly because of restored confidence in sterling, but mainly because of the improved terms of trade. How long this situation will last depends not only on the resolution of other countries to keep their interest rates above New York; but also upon the repercussions of the recession in third markets. As the reception of Vice-President Nixon in Latin-America has shown, many countries producing minerals and other raw materials are suffering heavily and blaming the United States. Malaya and the dollar-earning members of the sterling area in Africa as well as India do not offer good markets for British exports at the moment. Canada's recession is worse than that of the United States. Australia was able to build up her reserves in London in 1956/7 and these are at present serving her well in face of lower export prices and dry seasonal conditions; but New Zealand has had to impose severe import controls. All these developments overseas must react on the United Kingdom; but their impact will depend very much on how long the American re-
The American Recession — Too Much, Too Late (continued)

cession and, therefore, low export prices of the sterling area countries' last.

Here were great hopes in the United States of a recovery this spring. The President himself predicted that March would prove a turning-point. The recovery has in fact been weak, even in what Americans call the "overall picture". Unemployment has declined slightly; but has grown worse in the heavy industries, the seasonal increase in farming, construction and outdoor jobs being just about enough to counteract the continued layoffs in manufacturing. There is a good deal of optimism in business as well as government circles. Mr. Stephen D. Bechtel, the chairman of the Business Advisory Committee of the Commerce Department and himself a great construction engineer, reported more construction contracts signed. There is a definite increase in housing starts following a liberalisation of mortgage terms and the cheapening of credit. Machine-tool orders though still at a low level have increased for three months in succession. The association of purchasing agents reports better orders. Department store sales show a slight gain. Steel production is up slightly and the index of manufacturing production seems to have stopped falling. New appropriations for defence and also for highway construction are beginning to reach the stage of firm contracts. The steepness of the decline in the defence industries had been partly due to inadequate budgeting so that the appropriations began to run out in the latter part of 1957 and expenditure was sharply curtailed, causing layoffs in such industries as airplane manufacture and electronics. This has been, or soon will be, remedied by new appropria-

tions which will unbalance the budget somewhat this fiscal year and more in 1958-59.

The question whether the recession has yet reached bottom depends upon one's estimate of the extent to which inventories have been run down. Mainly because of the declines in output in the heavy production industries gross national product dropped by 3.6 per cent (from $440 to $424 billions) between the third quarter of 1957 and the first quarter of 1958. This was more than the 3.2 per cent. in 1949 and the 2.7 per cent. in 1953-54. But what the National City Bank calls "final demand for goods and services—total output minus the change in business inventories" fell only by $7\frac{1}{3}$ per cent. There has, therefore, been some reduction of unsold stocks of finished goods. In the first quarter of 1958 inventory reduction was at the annual rate of $7\frac{1}{3}$ billions, the highest for any quarter on record. The National City Bank cites reports of scattered indications that this is already leading to renewed orders and even to some re-employment, but concludes that the liquidation of inventories has not yet been completed and must go further. How far depends on how well final demand is maintained.

Provided it does not spiral into depression, a good case can be made for the rapid disposal of surplus stocks and this case is in the pattern of American business. Sales promotion campaigns, advertising and all the apparatus of salesmanship are in full swing except that there is little sign of lower prices for finished goods on the average. Materials are down, and metals, but finished steel is up and about to go up again when the automatic wage increase conse-
quent upon a rising cost of living comes into effect. Foodstuffs also have gone up. Indeed a long article could be written on this marked trend towards increasing costs of finished consumption goods and the extra burden of adjustment thus thrown on to the primary stages of production with the consequent clamour for government aid to agriculture, mining, and the extractive industries in general. Such aid not only distorts the economic structure, but maintains the necessity for high taxes, some of which, such as the excise tax on automobiles, reinforce the rigidity of the price structure.

Manufactured prices have a downward inelasticity partly because more fabrication, packaging and marketing costs go into them. The supermarket sells vegetables which are washed and put into cellophane bags. The automobile sprouts gadgets. All this is labour-consuming and labour is not only expensive but paid according to contracts which are often tied to living costs. There is a mutual reinforcement of the upward push of prices and resistance to any decline. This is only one aspect of the new American capitalism that cries out for further study and the devising of more adequate adjustment devices. Meantime the less organised and more individualistic enterprises tend to seek government protection.

There is therefore no certainty yet as to the length of the inventory adjustment still necessary. Optimists look for definite signs of recovery in production and employment by the late summer. Traditionalists point out that the length of recession averages twelve to fourteen months which would bring the zero hour for recovery closer to the end of 1958. There are some economists who would postpone it till well along in 1959. The consensus grows that recovery is not just around the corner. The decline is slowing up and perhaps flattening out; but there may be other hollows to traverse before the economy is again on an upward slope.

The behaviour of the stock market in recent weeks has been optimistic, though reports have circulated that insiders in some large corporations have recently been selling substantial blocks of stock. The so-called "chartists" who work on the average of past performances predict further breaks; but the stock market is neither infallible nor as closely related to the actual performance of the economy as it once was. Earnings reports for the first quarter were down 31 per cent. as compared with the good first quarter of 1957 and the second quarter of the year is not likely to be much better; but the market has gone up substantially.

Apart from inventory adjustment, the major factor in the recession has been the substantial decline of capital expenditures by the great corporations which are planned for 1958 at approximately 12 per cent. below the level of 1957, with a further reduction of 8 per cent. planned for 1959. It is this long-run factor on which the pessimists tend to dwell. New government appropriations will soon cause an expansion of defence output, highway construction, and various forms of public works mainly designed to give employment. The running down of inventories may cause the recall of men laid off in some industries. Housing is already showing considerable expansion. Consumption of non-durable goods is maintained and
even increasing. But corporate capital expenditures for new plant capacity show no signs as yet of responding either to cheap money or to reviving demand.

In my own view, this fact is significant of one of the major causes of the intensity of the present recession and also reveals one of the most troublesome aspects of the new economy into which the United States has drifted. The great corporations are long-run enterprises directed by a bureaucracy of professional managers largely motivated by pride in the enterprise and its expansion. Management is separated from ownership. The numerous stockholders are placated by regular dividends, sweetened from time to time by bonuses in the form of extra shares. Relations with the equally professional secretariats of the large trade unions are fairly co-operative because wages rise steadily and supplementary benefits are added such as pension and welfare plans. The consumer is satisfied despite the steady upward movement of prices because his income also rises as long as the credit system goes on expanding. In this situation there is little check on the natural inclination of corporation executives to expand their enterprises.

Expansion is largely self-financed and independent of the banking system and therefore of its regulation by monetary authorities. Every year a successful corporation will earn far more than it distributes as dividends. Most of them publish in their annual reports ten-year tables showing their steady growth and regular dividends. The first item in the table is apt to be net income and the next “income per share” followed by dividends, and “cash per share” which is well below the income per share. Later there is a calculation of the stockholders’ equity calculated in total and per share, both steadily growing. This growth consists of profits ploughed back into capital expansion. A strong corporation can always raise additional capital for expansion by offering to its shareholders subscription rights at prices below the market. If necessary it will borrow directly at relatively low interest on medium or long-term notes from insurance companies and other holders of funds nourished by regular savings. Very seldom need it resort to the trading banks. Indeed many corporations keep large deposits on hand which they can call upon for unexpected opportunities of development. Standard Oil of California, for example, held over $113 millions in cash at the end of 1956 and over $96 millions at the end of 1957.

In such enterprises development is planned ahead for long periods. Why should those plans be altered when the Federal Reserve Board applies a little gentle pressure to restrict the supply of credit to trading banks and their customers? It is in any case difficult to alter them quickly. And in the past such periods of credit restriction did not last long before the inflationary trend was resumed. This was of course a consequence of the fact that the monetary system, though nominally based on gold, is in fact a managed credit system in which gold is not allowed to play the role it did in the 19th century.

In the booming years of 1955 and 1956, this tendency for the great corporations to expand began to cause concern. It was symbolised by the struggle, which was
in part a personal rivalry, between General Motors and Ford for the automobile market represented by the average American's choice between a Ford and a Chevrolet. The struggle was conducted by many devices. Cars became longer, more glittering and showier. The designers held sway and perpetrated monstrosities such as tail-fins and extra rear-lights. At the same time credit terms were extended to as long as three years. Few consumers could resist the ultimate temptation of a trade-in allowance for their old car much above its book-value and often its resale value. Sometimes inducements such as free trips to Las Vegas or Honolulu were added to tempt lucky purchasers. The market was oversold and capacity was overbuilt.

The monetary authorities became concerned at the extent to which over-capacity was being built up at a time when consumers were being pinched by their obligations and by the increasing cost and tighter restrictions on credit. They had no direct means of bringing pressure to bear on the corporations which had their own sources of finance. Warnings were disregarded by men who were convinced that the credit restrictions would once again prove to be a temporary interruption in the long-term inflationary trend. The Federal Reserve Board, concerned both with the necessity of checking inflation and with the danger of continued expansion leading to a subsequent collapse based on over-investment running beyond consumption, intensified its restrictions. It is easy to see now that they were maintained long enough to cause a degree of recession and unemployment sufficient to frighten the expansionists into reducing their investment plans. They were tightened even in the third quarter of 1957 when the recession was clearly serious and not relaxed till November when it was clear that investment plans were in fact being reduced. There is much criticism by those who are concerned with the suffering caused by the Board's action in thus bringing indirect pressure on business investment through restrictions which affected not only consumers but small businesses dependent on bank credit. But the Board seems to have achieved its objective and to be unrepentant.

CONSUMERS, who were eager for the chrome and gadgets of the new cars and willing to buy them on easy terms, now tend to blame the automobile industry for developing them. It is possible that once again those who talk of needing simple transportation at minimum cost will be able to get it. The sales of small foreign cars are up to 300,000 which is still a small percentage even of the four million cars which may be sold this year, but is a substantial help to the western European producers. The American Rambler is also selling well and its producer is the only automobile company which shows increased sales in the first quarter. It will take time for this trend to prove itself. The 1959 models are already designed and will soon be under way. To retool for smaller, simpler cars is a major operation and a major investment. Meantime corporation profits are down, dividends so far are well maintained, but there is less in the kitty for new plant investment.

Emphasis has been placed on inventories and business investment because this is above all a capital
The American Recession — Too Much, Too Late (continued)

The goods recession largely concentrated in the durable goods industries. Time payment was obviously extended in the inflationary years 1955/6 in the expectation that consumer income would continue to increase. This was in large measure an element of the struggle for the automobile and appliance markets. As long as employment and consumer income were maintained, the economic consequences of expanded consumer credit were not serious and could easily have been corrected. It is only when unemployment becomes serious that re-possessions increase to a dangerous level. The pressure on consumers through the tightening of credit was one avenue of indirect pressure on the big industrial producers. As in every recession, the argument recurs that markets are saturated, that the formation of new family needs is declining now that the war babies are growing up; but this argument is unconvincing. Population is still growing and demand is still elastic. Consumers are at the moment paying off their instalment debts faster than new ones are contracted and there are complaints that "good borrowers" are scarce. Some finance companies are tempted to take greater risks even though collections are harder and re-possessions more numerous. Repayments are stretched, downpayments lowered and less solvent clients accommodated. But these are not unfamiliar recession developments—in a period of unemployment and lowered incomes, time-payment and most other forms of debt become troublesome. It is difficult to believe that they contributed significantly to the onset of recession, even though their size complicates recovery.

Recovery is likely in consequence to be gradual and perhaps deferred. There may even be some further declines. It does not seem likely that these, if they occur, or the painful prolongation of unemployment and lowered purchasing power in the heavy industries will result in a break of confidence that might set up a downward spiral leading to a major depression. There is always the risk of some accidental happening—the failure of a major firm for example—that might shake the present feeling of confident optimism for the future. But the economy is being shored up by various forms of government action. The railroads will receive some form of help. Housing has already done so and is responding vigorously. Highway construction is well launched and defence expenditures are increasing.

The big argument in Washington continues to be whether or not to reduce taxation and how. It is inevitably complicated by politics in an election year. The Administration (except perhaps for the Secretary of Labour) is trying to hold the line against reckless action that might result in a grossly unbalanced budget next year. The danger in this view is that Congress will do too much too late. Economists, including Arthur Burns who has great prestige not only as a leading student of business cycles but as the former Chairman of the President's Council of Economic Advisers, stress that immediate tax reductions would put money into the pockets of consumers. Whether they would spend it or put it away in extra savings is a question that depends partly on the kind of reduction. If withholding from payrolls were suspended or reduced and the reduction went mainly to low-income earners, the chances of increased consumption would seem to be greater. But it would be difficult later to re-
impose this taxation and the increased spending power would certainly be inflationary as soon as the recession began to ease. It is not at all certain that the spending would help the industries that are most depressed. A worker might spend his extra dollars on food or clothing (or beer) rather than buy a new car.

There is a considerable body of conservative opinion which would concentrate any tax reduction on excise taxes such as the 10 per cent. on automobiles and at the same time set up new schedules of depreciation allowances designed to encourage new investment. The argument is by no means over, but Congress is controlled by a combination of Republicans and conservative Democrats and so far the resistance to a quick tax cut for the benefit mainly of small income-tax payers has been strong enough to beat off successive proposals. The decision must come in June since the corporation tax rates imposed to cover the Korean war expenses expire at the end of the month unless Congress extends them. If the present rather weak recovery should continue and strengthen the chances would seem to be that the Administration will gain the day and there will be no general tax reduction, though there may be some concessions, perhaps the removal of excise taxes.

Interest rates have been somewhat lowered and will come down further. The Federal Reserve Banks now charge 1½ per cent. for rediscount, but the trading banks have been slow to follow. The small borrower must still pay 5 and even 5½ per cent. on his notes. Credit has been made abundant by successive lowering of reserve requirements. But it is easier to tighten credit than to force it into circulation. The metaphor often used is that you can pull on a piece of string, but you can't push. The advocates of monetary policy, however, plead that it takes time and that its effects must before long become evident.

Meantime the Administration is cautious about the various attempts by Congress to create jobs and relieve distress. The President signed the housing and construction bills, but he vetoed a pork-barrel public works bill and threatened to veto a social security measure which would in effect have introduced an unemployment dole. The measure is still in the Senate after the House beat down attempts to add payments to unemployed who had not contributed to the social security system by past contributions. The bill now provides for federal advances to enable the states to increase the period of unemployment payments from 26 to 39 weeks in order to cover those who had used up their eligibility. This is likely to pass the Senate and be accepted by the President.

The conflict, therefore, continues between those who urge quick action to provide jobs and increase consumers' purchasing power and those who contend that the natural forces of recovery should be allowed to work so that the economy will not be further distorted in a renewed inflationary push. The chances would seem to be that the conservative view will win out even though it may bring electoral reverses to the Republicans in some areas. The calculation seems to be that the industrial areas are lost anyway and the best policy is to concentrate on getting the economy into a situation which will minimise the inflationary risks for a time. It may be reasonable to effect a slow recovery, but the
possibility of further setbacks cannot be ignored. There are optimistic expectations of substantial recovery by the end of the year, but there are many economists who do not expect full recovery till well along in 1959. There is substantial agreement that the 1960's will see further marked expansion. Estimates as to the timing of recovery depend upon the importance attached to the plans for reduced capital investment by business which are scheduled into 1959.

One footnote should perhaps be added. The worst effects of the recession are being felt in its repercussions on foreign policy. Not only are there severe consequences in many countries as the result of the sharp declines in raw material prices. In many respects the revival of protectionist sentiment is more dangerous. This article must go off as Congress faces the crucial decisions on trade policy. The extension of the Reciprocal Trade Agreements Act reported from the House Ways and Means Committee is stronger and better than most of its supporters have dared recently to hope. It is not very good, but it is not disastrous. This is the result of an impressive mobilisation of both popular and business, as well as labour, support. But there will be a suspicion of attempts on the floor of the House to write in protectionist amendments and there is a formidable combination of the mining interests (whose strength has still to be shown in the Senate), of independent oil interests, textile manufacturers in the north-east and also in the south and many other scattered groups which add up to a considerable pressure on Congressmen and Senators. The Administration will do well if it can hold the line on the bill as it stands at present.