The American Economy . .

THE eyes of the world have, in recent months, turned increasingly toward the United States. The American economy, which, toward the end of 1948, had achieved an unprecedentedly high level of activity and an unprecedentedly low level of peace-time unemployment, has shown unmistakable signs of slowing down. Fears of inflation, which were rampant at the time of the Presidential elections last year, were almost overnight replaced by fears of deflation, as the prices of basic commodities, which had been running at record levels, turned suddenly downward. Throughout the first half of this year the recession in American activity gathered way—production continued to decline, prices and incomes continued to fall, unemployment continued to rise. Overseas press cables were anxiously scanned almost daily for some sign that the downward drift was abating. In July the picture improved slightly as some prices steadied and others moved upward. It is difficult, at the time of writing, to say to what extent seasonal influences were responsible.

So far the actual magnitude of the decline in economic activity is of minor proportions. Like other countries, the United States had been riding on the crest of a post-war boom, stimulated by abnormal world shortages created by the war; and some recession, sooner or later, was inevitable, as the post-war re-stocking demand in homes, shops, factories and public utilities began to be satisfied. The unemployment figure of four millions, however, is still much below the average of the pre-war years, and the level of economic activity still much above anything previously regarded as normal. It is not what has already happened, but what may happen, that is giving rise to concern and anxiety. In practically everyone's mind is the question: Is the break in American activity the beginning of another large-scale depression in the United States, and indeed in the world?

So far there is no reason at all to believe that it is; but the question may not be definitely answered for another six to twelve months. Until then the uncertainty will continue, and the eyes of the economic world will remain uneasily fixed on the United States.

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World economics are dominated by the United States. In resources and productive capacity, in world trade, in foreign investment (if free grants are included) and world commodity markets, the United States easily leads the rest of the world.

With only 6% of the world's population, her production amounts to over 40% of total world output. In 1939 the production of industrial minerals in the United States was almost four times greater than that of the second largest producer—the U.S.S.R. The United States runs away with the production race, partly because of her abounding natural resources and massive population, but basically because of her great superiority in productive efficiency. In real national income per head she far surpasses any other country. This is a magnificent vindication of the virtues of the free enterprise way of life to which she is firmly wedded.

Her influence in world trade is also decisive—though overseas trade represents only about 6% to 7% of her national income. During the prosperous 'twenties, the United States was the world's greatest exporter (comprising 16% of the total of all exports as compared with Great Britain—11%). Her imports amounted to 12% of the world total, and she was second only to Great Britain with 15%. As a consequence of the economic collapse in 1929, U.S. imports and exports for 1931-35 declined to about half of the level in 1921-25. Since what the people of the United States spend on imports is directly related to the level of their internal economic activity, world prosperity is largely dependent upon the ability of America to maintain a high domestic demand for her own products. If she fails, repercussions in every important trading nation are sure to follow.

WORLD FINANCIER

The United States is replacing Britain as the world financier. The magnitude of British long-term investments abroad was greatly reduced during the war by the sale of British assets to finance war supplies; on the other hand, the United States financed the war requirements of the allied powers through Lend-Lease to the tune of $46 billion. Since the war U.S. long-term loans and investments have steadily increased, and now, for the first time in her history, exceed those of Great Britain. She has also provided vast sums through free grants-in-aid, and plans to spend in all $16 billion in the Marshall Aid Programme. The United States is now obliged to undertake the responsibilities, borne mainly by

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Britain in the 19th Century, for the supply of capital to the rest of the world to raise living standards and purchasing-power, and hence help to provide an outlet for her own massive productive capacity. From a long-term standpoint, the continuance of a large capital outflow from the United States is imperative for the maintenance of demand throughout the world and for her own internal prosperity.

COMMODITY PRICES

The United States exerts a determining influence on world prices for basic commodities. The U.S.A. is now virtually the only major free market in the world; the operations of British and other markets have been closed, or severely curtailed, as a consequence of bulk purchasing arrangements made directly between governments. World prices tend to follow U.S. futures' quotations. U.S. consumption constitutes so large a part of total world consumption that world prices are to a great extent determined by the intensity of American demand. The United States consumes about one-third of the world's cotton, one-quarter of its wool, one-eighth of its wheat, two-fifths of its rubber, and about one-third to one-half of basic minerals such as iron, coal, zinc, tin and lead.

In matters economic the United States bestrides the world like a colossus. Because of its dominant position in world production and consumption, in trade and finance, the tempo of American activity largely sets the tempo of economic activity throughout the world. Few countries could remain unaffected by an American depression or even a severe recession, although something can be done through internal domestic policies by individual countries to lessen the shock of an American decline on their own economies.

ELEMENTS OF INSTABILITY

Nevertheless, a reasonable measure of stability in the United States is vital to stability throughout the world. Economic tremors in the United States are felt in practically every country, and often give rise to consternation and fear. But the very size and vigour and wealth of America create latent elements of instability. To some extent this instability is part of the price that she pays for her extraordinarily rapid rate of progress. Technical change and improvement take place almost at breakneck speed, and the annual rate of increase of productivity—production per manhour—in the States greatly exceeds that of any other nation. The huge American capacity for production requires, if it is to be kept fully employed, a correspondingly rapid increase in the consumption standards and habits of the people. But this is not easily achieved. Even in the United States, there are limits to the flexibility of probably the most adaptable and flexible people in the world. With their genius for technological innovation, the components of production fluctuate widely. Great national advertising programmes often precede the production of new products. Resources of manpower and materials are drawn to and fro, in response to changing demands as reflected in prices. In an economy as vigorous, inventive and dynamic as the United States, some degree of instability must be accepted as inevitable. In the past much hardship has been imposed on sections of the American people by the shifting stresses and strains in the American economy, but there is now very good reason to hope that this will be greatly alleviated in the future by U.S. federal government action.

EFFECT OF U.S. RECESSION ON AUSTRALIA

Australia, along with other countries, is supremely concerned in the ability of the United States to maintain itself in stable prosperity, and hence to sustain the flow and volume of world trade. The recession now taking place in the United States is being, and will continue to be, felt by Australia directly in the prices of its own basic exports. World wheat and metal prices have already responded to the price decline in the United States, and wool may shortly follow suit.

Moreover, falling prices and costs in the United States imply increasing competition in world markets. A vigorous drive by the United States to sell surplus production abroad at cut rates would greatly aggravate the British export problem, and would tend to deprive Britain of much-needed export income to pay for her essential imports from sterling countries as well as from America. Britain is Australia's greatest market for exports of foodstuffs and raw materials. A decline in British demand and employment would react unfavourably on Australia's own export prices and income, and would thus, in the absence of counter-balancing factors, reduce the level of spending within Australia.

The countries of Western Europe are also very large consumers of Australian primary products and raw materials. A serious recession in the United States would almost certainly intensify the economic difficulties of European countries in their struggle back to prosperity and solvency, and would thus tend to reduce their purchases of Australian goods.

PROSPECTS OF PREVENTING DEPRESSION

Whether the United States will be able to control the recession now taking place, and prevent the development of a major depression, is thus a question of critical importance to Australia. What are the prospects of this? No definite answer can be given. In economics, as in other things, the United States is more or less unpredictable. Generally, informed American opinion is that there will be no large-scale depression; and, that if a serious slump should occur, there is no reason why it should be other than short-lived. How far this view is founded on solid conviction, how far it amounts to "whistling to keep their courage up," is not easy to tell. Generally, however, cold analysis would suggest that a serious depression will be avoided, and that the adjustment from post-war boom conditions to a lower price level, and to a more normal state of internal demand, can be achieved without an intervening collapse.

In the first place, some retreat from the dizzy heights of 1948, attained partly under the upward pressure of the post-war restocking process by businesses, private individuals and governments, was, sooner or later, inevitable. In fact, the decline which is now taking place can, in part, be attributed to the phenomenal success of the American post-war production drive in overtaking war-caused shortages. To take an example—a year ago steel was a bottle-neck holding back production in many fields; on latest indications it has not only caught up with demand, but has passed it to such an extent that the steel industry is now operating at only 80% capacity.

In a financial sense the American economy is fundamentally sound. There is no reason why an economic crisis should occur because of financial reasons. In this respect the situation is wholly different from 1929. The 1929 depression was primarily a consequence of "boom headedness" in the nineteen-twenties. Great developments in the mass production of manufactured goods, such as motor cars and electrical appliances, generated a wave of borrowing and speculation, which culminated in frenzied gambling in stock exchange securities. Money could be obtained almost for the asking, and caution was thrown to the winds. The banking system was completely immature in the matter of currency and credit control.

In many instances the additional finance created was not channelled into solid productive activity, but used for private speculation and excessive personal expenditure through hire purchase and other consumer credit arrangements. Once the boom collapsed and banks and financial institutions were forced to reverse their excessive lending policies, total demand fell precipitously, and, despite the efforts to revive activity and spending through the New Deal, recovery was slow and laborious. It has been estimated that the national income lost as a consequence of the depression exceeded the entire cost of the last war to the United States.

Fortunately this time the situation is very different. There has been no excessive lending or speculation. Generally the debt situation is extremely sound. The Federal Reserve Bank, which was reconstituted in 1935, with greatly increased powers of financial direction, has exercised much more stringent control over member banks, has curtailed unwise credit expansion, and virtually eliminated excessive speculation on the Stock Exchange. Though, for instance, there are now twice as many stocks listed on the New York Stock Exchange as in 1929, and the American public has three times as much money, the aggregate value of all listed common stock to-day is about one-quarter less than just before the great crisis twenty years ago.

Bank reserves in liquid form are now regarded as adequate to tide over a difficult period, whereas in 1929 the banks were unable to prevent a collapse of confidence in their own solvency; nor were they in a position to obtain much-needed assistance from the central banking authority. Restraints have been exercised over consumer spending, through credit and hire purchase restrictions, and over investment in corporation securities; these restraints are now being

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relaxed with the advent of recession. To-day the American public has personal savings of $200 billion to fall back on in the event of a decline in personal incomes. Generally, both business and the community have been much more cautious than in 1929, and, having prevented the emergency of runaway boom conditions, are much better placed to avoid a severe down-turn.

In addition, the Federal Government of the United States, along with other governments, has developed a much broader conception of its reponsibilities in the control of inflation and deflation, and the maintenance of economic stability and employment. The Employment Act, passed by Congress in 1946, formally declares the responsibility of the Federal Government to maintain high employment by appropriate fiscal, monetary and other policies. Under the Act, a Council of Economic Advisers to the President has been established, the main purpose of which is to continuously review national economic trends and to advise the President on anti-recession measures. Counter-deflationary action proposed by the Council includes large-scale public works projects such as conservation of resources, river planning and community development to stabilise employment in the constructional and allied industries; support prices for primary products to maintain farm incomes; measures to bolster consumer spending such as cuts in excise taxes and increased unemployment and social security benefits; and large-scale housing programmes subsidised where necessary by public funds.

INTERNATIONAL RESPONSIBILITY

In the sphere of international economics, the U.S.A. now seems set to accept a far greater measure of responsibility for the promotion of world trade and the economic welfare of other nations than during the 'twenties and 'thirties, when American political sentiment was predominantly isolationist. The United States has taken a leading part in the trade and monetary conferences held during and since the war, and in the formation of the proposed International Trade Organisation—all of which are designed to restore and expand world trade on a multilateral basis. In the renowned "point four" of his inaugural address last January, President Truman stated that the United States should make available American scientific and technical knowledge to under-developed areas of the world, and should encourage capital investment in those areas to help achieve peace, plenty and freedom. With this greater conception of its role of leadership in furthering economic co-operation between the nations, the U.S.A. would appear to be far more strongly placed than in 1929 to prevent a dangerous depression internally and an economic catastrophe such as that which overwhelmed the world twenty years ago.

BUSINESS PSYCHOLOGY

The United States is thus much more powerfully armed to cope with economic recession on both the monetary and fiscal fronts, and on the plane of international co-operation and responsibility, than in 1929. An advance in economic understanding has been accompanied by a more sober and responsible attitude on the part of business and of the community generally. Nevertheless, the unpredictable factor of American business psychology may eventually be the decisive force in determining the course of economic activity in the United States over the coming months and years. A high degree of business confidence in the future, and the maintenance of business investment in expanding and modernising plant and equipment is essential to continued prosperity and stability. The huge productive capacity of the United States, and the extraordinarily rapid tempo of activity and progress of American industry, raise problems that are virtually absent in other countries where progress is, by comparison, snail-like. These problems demand an exceptionally high order of economic intelligence and leadership. The faster the car, the more alert and intelligent needs to be the driver.

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A repetition of the recurrent crises of the inter-war years would have disastrous political as well as economic reactions, and would certainly weaken the cause of democracy throughout the world, in the fight against the forces of totalitarianism. Of this the United States is fully aware, and in this awareness, in the new and enlarged sense of responsibility of the American people brought about by the war, and in the underlying soundness of the American economy, the peoples of other nations may with some confidence rest their hopes.

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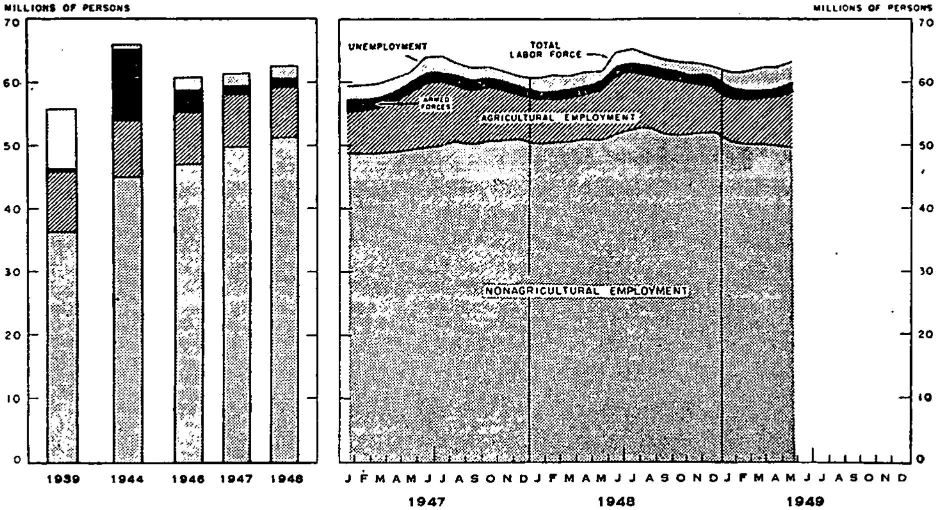
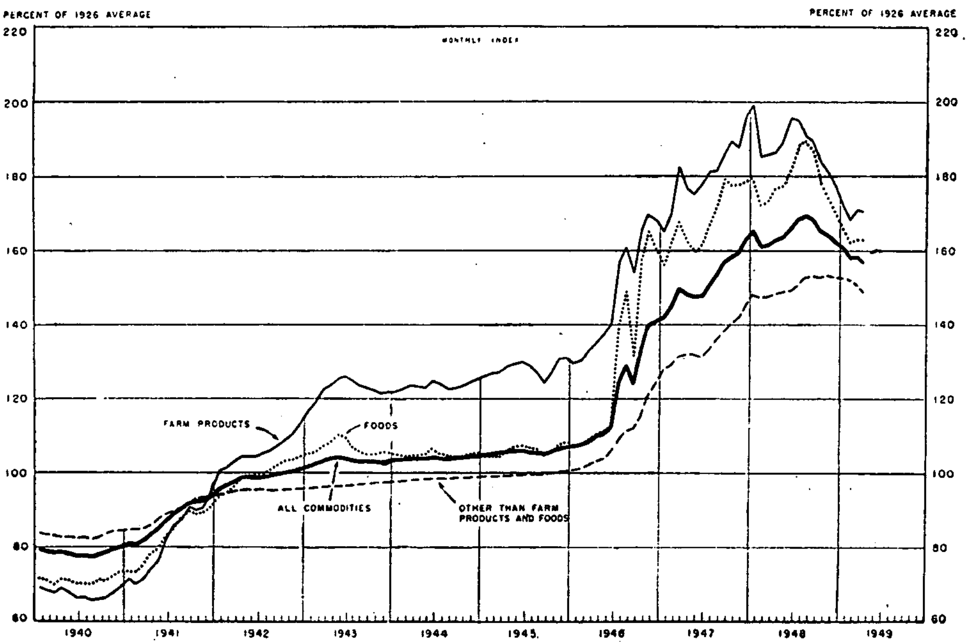
The following charts are reproduced from "Economic Indicators," June, 1949, prepared by the President's Council of Economic Advisers. They illustrate the recent down-turn in employment, prices, production and company profits which has come to be known as the "American Recession."

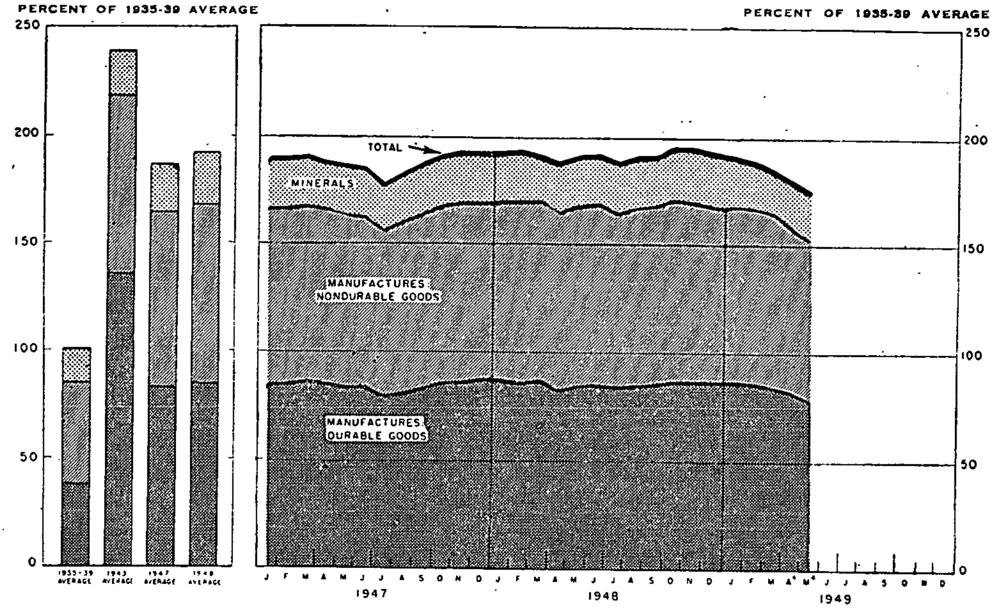
EMPLOYMENT.



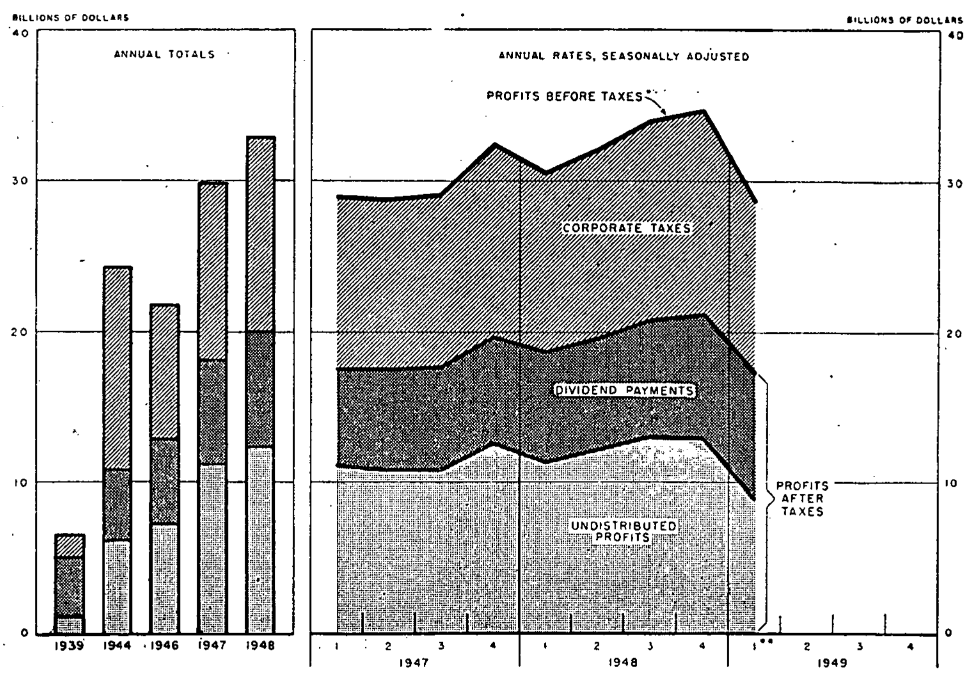
WHOLESALE PRICES.



INDUSTRIAL PRODUCTION.



COMPANY PROFITS.



CHANGES IN THE UNITED STATES ECONOMY SINCE 1939.

	1939.	1947.	1948.	% Increase 1939-1948.	% Change Mid. 48-Mid. 49.
	Billion Dollars.				
Income and Expenditure—					
Personal Income	72.6	195.2	213.6	194	+ 3
Pers. Consumption Exp.	67.5	164.8	177.8	163	— 1
Personal Savings	2.7	8.8	13.6	404	+50
Corporate Profits	6.5	29.8	34.0	423	—13
Private Investment	9.0	30.0	39.7	341	—16
Net Foreign Investment	0.9	8.9	1.5	66	N.A.
Construction—					
Private	3.8	10.9	13.6	258	— 2
Public	2.5	3.1	4.0	60	+33
New Plant and Equipment	5.2	16.2	18.8	262	— 1
Financial—					
Vol. of Money	64.4	172.4	168.0	161	— 1
Fed. Public Debt	41.9	256.9	252.8	503	— 1
Fed. Income Tax	1.8	29.3	31.2	1,633	N.A.
Fed. Expenditure	8.9	41.1	39.8	347	+20
Internal Trade—					
Sales	133.4	394.0	435.4	226	— 5
Stocks	20.0	48.0	54.0	170	+ 5
Foreign Trade—					
Exports	3.2	15.3	12.6	294	+ 7
Imports	2.3	5.7	7.1	209	—15
	Indices: 1939 = 100.				
Foreign Trade—Q'ties—					
Exports	100	244	188	88	N.A.
Imports	100	116	131	31	N.A.
Prices—					
Retail	100	160	172	72	— 2
Wholesale	100	197	214	114	— 7
Farm Produce	100	293	302	202	—14
Shares	100	129	131	31	—16
Weekly Wages—M'fg.	100	206	223	123	— 1
Production—					
Industrial	100	172	176	76	—12
Agricultural	100	122	133	33	N.A.
All Phys. Prod.	100	164	171	71	N.A.
	Millions.				
Employment—					
Civil Labour Force	55.2	60.2	61.4	11	— 3
Agriculture	9.6	8.3	8.0	—17	+ 7
Manufacturing	10.1	15.9	16.3	61	— 6
Unemployment	9.5	2.1	2.0	—79	+73

Source: Economic Reports of the President of the U.S. and the Survey of Current Business.

NOTES ON TABLE

A comparison of the American economic position in the last three years with 1939 is shown on page 110.

Although somewhat distorted by changes in the value of the dollar, some of these business indicators reveal an astonishing increase on 1939. Personal income has trebled, and physical output nearly doubled. Personal savings in 1948 were five times their pre-war level. After allowing for currency depreciation, net income per head (after taxation) has increased by 40% since 1939. Private investment and construction and new plant expenditure reached peaks in 1948, three or four times higher than those of 1939.

Prices received by farmers have increased much more rapidly than other prices. The total amount of corporate profits (before taxation)—not rates of profit—is five times the pre-war level. Share prices are only one-third above pre-war.

Unemployment in 1948 at 3% was practically non-existent, despite the great increase in the labour force which has taken place since 1939 when unemployment amounted to 17%. Unemployment in total is even now only half the 1939 level. The decline in farm labour contrasts strongly with a 60% increase in manufacturing employment. Lay-offs in manufacturing now amount to only 5% of total manufacturing employment, and should not therefore cause undue alarm.

The vast expansion in the size of federal finances illustrates the increased responsibilities of the central government. Income tax is 17 times the pre-war level, and, if maintained as a means of redistributing income to lower income groups, should assist in the maintenance of a high level of consumer spending.

The overseas trade figures provide interesting comparisons with 1939. Although exports have quadrupled, imports have less than trebled. In physical quantities the discrepancy between exports and imports is even greater. That imports are probably at their peak gives some cause for apprehension and indicates the need of continued American capital loans to bridge the gap between exports and imports.

The great decline in net foreign investment in 1948 is mainly due to a shift in foreign aid from loans to grants.