"INVESTMENT AS A NATIONAL PROBLEM"

ADDRESS

of

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During the past few years we have been told repeatedly that we must stimulate the capital goods industries. The reason is clear enough. The greatest volume of unemployment has been found in this part of our industrial life. The construction industry, the steel, cement, machine tool, and other industries concerned with the manufacture of those heavy durable machines and buildings which are such an important part of our productive equipment have all been seemingly laggard.

Strangely enough, if we measure the production of capital goods, we find that they expanded at an extremely rapid rate from 1933 to 1937. In 1937 the gross production of these goods was \$17.5 billions while in 1929 it was \$20.3 billions. In other words, our rate of investment in 1937 was almost as high as at any previous time in our history. On the other hand, our securities markets were not nearly so active as in 1928 or 1929. This suggests that we have confused our ideas of the volume of investment with our ideas concerning the volume of trading in stocks and bonds.

A few weeks ago these apparently academic and theoretical questions of savings and investment were rudely dragged from their places in books and financial pages. For the moment they were front-page news. From the standpoint of the well-being of our people, this is where they belong. They are a number-one problem.

On the one hand we are told that the economy is suffering from over-saving or underinvestment; on the other hand we are told that this is impossible because saving must always be equal to investment. Some think that a high level of national income is impossible without a high level of investment; while others think that a high level of the national income induces a high level of investment. Similar differences of opinion prevail with regard to the relationship of the level of investment to the level of consumption: Must we have a high level of investment in order to have enough to consume, or is the level of consumption to a certain extent independent of the level of investment?

To throw some light on these questions let us examine, first, the process of savings, second, the process of investment, and third, the relationship of savings and investment to the volume of goods and services available for consumption.

The savings process at the present time has three outstanding aspects. First, the data indicate that as a nation we are probably saving more in proportion to our income now than at any time since the great War. Secondly, the data indicate that we are transferring the management of our savings to a group of institutions. In other words, the control over the use of savings is being rapidly shifted from the individual saver to the institution that invests his money. Thirdly, the evidence indicates that the process of saving is becoming increasingly automatic and that it is losing that element of deliberateness, of individual choice, of that combination of moral elements which we have characterized in the past as thrift and initiative.

It may be worth while briefly to examine these present-day characteristics of the process of saving. First, the volume of savings:

Individuals save; corporations save; governments save. No one knows how much we save.

The best available measure of individual saving is the increase in the assets of our major savings institutions. The increase in the assets of life insurance companies, mutual savings banks, building and loan associations, and postal savings banks, and changes in the time deposits of commercial banks, individual holdings of baby bonds, and Federal, State, and local trust and pension funds surely account for the overwhelming bulk of the individual savings. In 1937 the assets of all these savings processes increased by \$4.7 billions; in 1938, by \$3.1 billions. Except for the increase of \$5.1 billions in 1928, the increase in their assets in 1937 was greater than in any year since 1921. The measure of our effort to save is not, however, the absolute amount of savings but rather the relationship of savings to the national income. It is significant that the ratio of the increase in assets to the national income was greater in 1937 than in any year since 1921.

Just as individuals save so do corporations. They are an important factor in determining the total volume of saving. Undistributed profits, although substantial for some corporations, are less than they were before 1929. For all business enterprises (considered collectively) they have been negative throughout the decade. Nevertheless, productive capacity has been maintained and in some industries materially expanded. This seeming paradox is explained by (1) the high volume of depreciation and depletion funds available, (2) the level of replacement costs, and (3) increased efficiency.

Likewise the governments of the United States have added their share to the total savings of the community. This volume of savings is more difficult to measure than that of individuals or corporations. The goods, the equipment, and the organizations operated by Government are not valued in the market. How much is the Post Office worth? How much is a school system worth? How much is a local sewer system worth? How much is a State Department of Conservation worth? In spite of these difficulties we shall make a conservative guess. Since 1931 the Federal, State and local governments combined have added to their assets properties having a "value" of about \$28.1 billions. Of this, \$16.5 billions represents net construction, \$3.3 billions represents investments in government corporations, and \$6.3 billions represents increases in general fund balances. These are simply estimates on a conservative basis of the extent to which our governments have been saving and investing.

Thus there is little indication that we have stopped saving or that we are living on our fat.

Secondly, an examination of the ways in which we save demonstrates clearly that the individual saver tends more and more to lose control of the use of his funds. The only ways an individual can save and still retain control over his savings are through the purchase of a home, an automobile, or other personally used durable goods, or through putting his savings into a business which he will help to administer. Whenever

saving takes place through life insurance, savings banks and pension, trust and Social Security funds, the individual exchanges his own control for a claim against an institution or a government body. A corporation saves by retaining its profits to expand its business, and substitutes corporate judgment for individual judgment. When governments save, they obviously do not directly consult the individual citizens.

Thirdly, saving as a national process is becoming increasingly automatic. Business savings, for the greater part, are matters of corporate policy and go on independently of the decisions of individual stockholders. In this sense, practically the whole of the saving of our larger corporations is automatic. Likewise, the growth of governmental pension and trust funds has the same characteristics. The newer developments in social insurance have actually put into operation the greatest program of automatic saving in the history of the United States. Old-age insurance taxes, unemployment insurance taxes, and other taxes and deductions have increased these pension and trust funds with startling rapidity in recent years. Between 1936 and 1938, for example, governmental trust and pension funds increased by \$2.6 billions.

If we consider those elements in the savings process where individuals set aside savings in the first instance, later to deliver these savings to the control of institutions, we discover automatic elements similar to those already discussed. The largest single element in the individual savings process consists of the life insurance companies. Between 1936 and 1938 the assets of all life insurance companies increased by \$2.9 billions. Individuals saved at least this amount through life insurance companies in these years. Yet individuals do not ordinarily consider their life insurance premium payments as savings. They rather consider them as expenses, to be met in some cases ahead of expenses for consumption. One of the most interesting problems faced by social case workers is the person on relief who is trying to save his life insurance policy. Still another interesting case is the man who is always pleading poverty and then suddenly realizes that his insurance premiums are taking a large share of his income. He is saving without knowing it.

In short, we now have a streamlined savings machine, a machine which operates quietly, automatically, and painlessly, a machine increasingly independent of those conscious choices called thrift. Control over this machine is more and more leaving the hands of individuals, leaving the hands of savers, and being transferred to institutions: financial institutions, business enterprises, and governmental agencies.

What happens to these savings? Are they all invested? Must all savings be invested? The answer to this last question is "yes".

Any community that saves must find investment outlets for its savings. In the broadest terms, a community can maintain a given level of income and employment only by using these incomes to buy the products of its employment. In this sense there is no difference between investment and consumption. Consumption is spending, and investment is

spending. The difference between consumption and investment lies in the direction of the spending. When we consume, we spend our incomes for one type of goods and services; when we invest, we spend our incomes for another type of goods and services. When we save and do not invest, we cause unemployment in those industries producing investment or capital goods; when we save and do not consume, we cause unemployment in those industries producing consumers goods. In both cases, the unemployment tends to spread. But in the very nature of the case spending for consumption tends to be steadier than spending for investment.

Savings may be used by the saver or by someone else entrusted with these savings in any of the following four ways:

- (1) To purchase goods which have relatively long lives, such as dams, steel plants, power plants, houses, automobiles and electric refrigerators:
- (2) To finance the current spending of someone else, as when your cousin borrows from you to take a trip around the world;
 - (3) To pay off bank loans or add to bank balances:
 - (4) By hoarding money.

I shall speak only of the first two. The last two would lead me to a complicated discussion of money and credit.

First, the financing of the purchase or production of new machinery, plant, houses, automobiles, and other types of goods having relatively long lives. This use of savings we may term investment, in distinction to the process whereby one person buys property, tangible or intangible, from another person. Such an exchange swaps one asset for another asset and leaves untouched the problem of the ultimate use of the saving.

It may be noted that the commonly accepted notion that business enterprises expand plant and equipment by obtaining savings through the securities markets is greatly exaggerated. Business enterprises rely upon the securities markets, that is, upon the savings of individuals, for only a small part of the new funds which they invest in plant and equipment and their going businesses. For example, during 1938 there were sold in the securities markets approximately \$2 billions worth of securities. Of these only \$428 millions were used to expand plant and equipment. Since 1923 there has never been a year when as much as \$2 billions of savings were taken from the public markets to add to capacity. In 1929 more than \$10 billions of securities were sold, but only \$1.8 billions were used to expand capacity.

If these corporations do not get their funds for expansion from the public financial markets, where do they get them? Primarily from earnings, that is, from undistributed profits, depreciation and depletion. For example, seven major automobile companies (having assets of \$1.6 billion in 1938) spent \$430 millions on plant and equipment during the years 1930 through 1938. They had \$560 millions available from gross earnings. These companies were completely independent of

the savings of individuals to finance their investment program. Eleven oil companies during the same period spent \$2.1 billions for plant and equipment. They were able to finance 95 per cent of these expenditures from earnings.

(2) Secondly, savings may be used to pay for current consumption. Mr. A loans Mr. B \$100, to buy groceries or to pay for travel expenses. Mr. B intends to repay the loan; that is, he intends to curtail his consumption some time in the future in favor of Mr. A. This is an important type of savings outlet. It is indispensable to note, however, that this employment of savings does not increase the capital equipment at the disposal of the community. It merely redistributes the existing income. This is essentially what happens when a government borrows from you and pays me direct relief. Some part of current savings has always been used to redistribute income. Sometimes the redistributions are voluntary and sometimes they are involuntary.

Now let us consider the case where these savings are "lost," that is, where the debt (and the saving) disappears. Mr. B finds himself for one reason or another unable to repay the loan. This means simply that Mr. A cannot expand his consumption at the expense of Mr. B. There is no recovery of income through the payment of the loan.

The other two methods of employing savings are important, but I shall refer to them only briefly. Savings may be employed either (3) to pay off bank loans or to build up bank balances, or (4) to build up monetary hoards. But bank deposits are our most important form of money supply. Since the supply of money and of its counterpart, bank credit, have an effect on both the volume of purchasing power and on prices, the way in which these bank balances and hoardings are used or withheld from use affects business activity. Such savings withheld from the purchasing power stream retard business activity.

While this is an important problem it is not the subject under discussion. Likewise, the closely related and equally important problem of price relationships is beyond the scope of this paper. I am talking about the problem of savings and investment and wish to emphasize that it is closely related to these other problems. It cannot be kept in a water-tight compartment.

So far we have been talking about the way in which savings take place, the way in which investment is carried on, and the relationship between savings and investment. However, from the standpoint of our national life, the important question is, Have we been investing enough to give us the means of increasing our standard of living? It is commonly assumed that during the decade of the twenties we did pretty well but that during the last decade we have been unable to duplicate that performance, and that in the presence of depression long continued our standards of living have sharply fallen. Let us look at the facts.

We know the national income was \$83 billions in 1929 and \$72 billions in 1937; we know that the national income was 13 per cent less in 1937 than in 1929. Many of us have therefore assumed that the amounts of goods and services available for consumption were also 13 per cent less in 1937 than in 1929. If we add the further consideration that the population increased by about 6 1/2 per cent during the same

period it would seem obvious that the living standards must have declined. Two factors must be considered in determining the effect of these changes. The first is the shift in prices, which are still below those of 1929. But even if we compared these national income figures, adjusted for price changes, we would be misled. Our standard of living depends upon the volume of goods and services which we consume. To determine what changes in the standard of living have taken place we must use data showing the goods which people have consumed. Fortunately, these data have recently been made available by the National Bureau of Economic Research.

The annual production of goods and services is divided into those used for consumption and those used for capital formation (investment). The volume of goods and services available for consumption has been in turn subdivided into four groups: perishable commodities, semi-durable commodities, durable commodities, and services.

The volume of perishable commodities (such as food, beverages and drugs) was 2 per cent larger in 1937 than in 1929 (and 11 per cent larger in 1938 than in 1929).

The volume of semi-durable goods (such as clothing, dry goods, and general merchandise) was 3 per cent smaller (7 per cent smaller in 1938).

The volume of durable commodities (such as furniture, automobiles, and jewelry) was 17 per cent smaller (43 per cent in 1938).

Data for the volume of services available during 1937 and 1938 are not available.

On the whole these data indicate that, measured statistically, the total volume of the different types of commodities and services available to the American people for consumption in 1937 was slightly below the volume available in 1929. The average for all consumers' commodities for 1936 to 1938 was equal to that for 1928 to 1930 (1 per cent below that for 1927 to 1929), and of course 1936-1938 was above that for any other three years in the decade of the twenties.

If we consider the increase in population since 1929, the results are somewhat less favorable. But, other changes have taken place in the same period. The age distribution of our population has changed. The distribution of the volume of employment has changed. Concerning these we know little. We do know, however, we have been saving and consuming only slightly less than we did during our so-called prosperity. We know now that that isn't enough. We still have savings which we must learn to use.

If we learn to use these savings, we shall have found one way for the lower third of our community to produce the goods and services which it needs.

To find ways to use these savings in productive activity is one part of our investment problem. Somehow we backslide just when our productive machine begins to work at a high level. We did in 1929, as you all know, and we did in 1937. There is a growing suspicion that our attempts to

save more than we can spend for new productive equipment and durable consumers goods has something to do with stopping the upward movement of our economy.

Where do we really need more investment? Is it in New England? The great industrial area of the Middle Atlantic and Middle Western States? The Southwest? Or the West Coast? In what industries do we need investment? And in what industries is there difficulty in securing capital? Is it the great area of mining and manufacturing? Is it in the construction field? Is it in railroads or other means of transportation? Is it in public utilities? Or are there a whole series of new industries just being born which will require large volumes of investment? Some analysis of this problem has been made. We know for example that in recent years the Southwest has been absorbing funds. We know that the Northwest has been developing its industries. We know that in spite of all drawbacks public utilities have been expanding their productive capacity and using investment funds although the rate is not as great as that of the expansion period during the twenties. We know that the area of residential construction is crying for a higher rate of investment. We know that public construction has regained the levels which were achieved during the middle of the decade of the twenties. However, on close examination, when private industry and Government have used all of these possible outlets to the full, we still seem to need more outlets. If we fail to find them, then the danger is that our savings will be lost.

If they are not to be lost, then they must be used currently. If we cannot invest all our savings and do not want to lose them, then we must find ways to consume them. This would mean that a larger proportion of our income must be consumed. Here is the second part of our investment problem. How can we divert these would-be savings to consumption? Such diversion means higher standards of living. It means fuller use of existing investment. It may create higher levels of investment. Thus we can come closer to achieving the good life for all of our people.