FINANCING PRIVATE PRODUCTION

It was assumed earlier that the government contractor can obtain financing and thus, once facilities and materials are available, can effectively carry on government-ordered production.

In a report to the Hoover Commission it was observed that the need for short- or long-term borrowing to finance current operations becomes much greater when a firm takes on government contracts:

> Capital borrowings in the performance of Government contracts are frequently made necessary because of common delays in obtaining payment such as the slow processing of invoices, delays encountered in obtaining definitive contractual instruments authorizing payment, Government revisions of delivery schedules which delay or stretch out deliveries over a longer period, thereby prolonging investments in inventories, and other Government action * * * [50]

Retained earnings are often a firm's prime internal source of working capital while bank credit is a major external source. Here can be seen the possible ramifications and interrelations of fiscal and monetary policies. A liberal money market would tend to quicken and ease the expansion of business credit while a tight one might tend to have an adverse effect. In this connection, taxation which impinges on savings and thus reduces the supply of loanable funds would tend to have a tightening effect on the availability of external business financing. Also, such fiscal measures as changes in the level of corporate taxation and in the treatment of undistributed profits could strongly affect the extent of internal financing.

The liberalization of advance and progress payments tends to ease the financing problems of government contractors. Other governmental devices to ease the demand of government contractors for working capital are the delivery of government-owned raw materials and of semifabricated items for processing or for assembly and the utilization of government-owned inventories. All of these methods result in increasing the current assets controlled by business firms working under government contracts. To the extent, consequently, that these financial arrangements are carried on, business concerns do not have to rely solely on their own resources to find the capital and the credit necessary to support current production.

In the absence of governmental assistance, there may be financial as well as technological limits to expansion of production on government orders. As can be seen by the large array of governmental devices designed to ease the financing problems of government contractors and by the performance of the American economy during wartime, these financial limitations have generally not been controlling.

FINANCING THE GOVERNMENT EXPENDITURES

In the simple situation examined in the previous chapter, it was assumed that the government payments to contractors would be financed by borrowing idle funds. It would be more usual for the Government to finance a large increase in the level of expenditures through raising the level of taxation or through borrowing active investment funds or by means of a combination of the two. In the short run, some increases in expenditures could be financed by drawing down the government's cash balances.

[50] National Security Industrial Association, *Report to Commission on Organization of the Executive Branch of the Government Regarding Military Procurement*, Washington, 1954, p. 57.