

*The 1957-58 recession*

In the early autumn of 1957, more than three years after the upturn in business, expansion gave way to recession. A capital equipment boom by its very nature cannot be indefinitely prolonged. Exceptionally high rates of capacity expansion, rapid rise in equipment prices, and reduction in business liquidity eventually weaken incentives to make additional outlays. A decline in business capital spending will usually entail a period of inventory liquidation for capital goods industries, with reduced employment in these industries. Secondary effects of these developments are reductions in business inventory holdings, employment, incomes, and demands generally. The recession that began in the autumn of 1957 was of this type—although other elements were present, including cutbacks in defense ordering and contraction in foreign demands for U.S. exports.

Recession was not accompanied by widespread liquidation of credit and distress sales, however, and the basis was soon formed for recovery and renewed expansion, in part because of the increased availability and reduced cost of credit. Policy actions had operated to restrain the use of bank credit for speculative purposes during the expansion, and then operated in recession to encourage expansion in bank credit and increase the liquidity of the economy.

During the recession, prices of sensitive industrial materials declined, as the chart shows, with the average returning to the early 1954 low. While it is likely that various forms of concessions from list prices developed for other industrial commodities, list prices generally were maintained and, in fact, were raised further for some commodities. The failure of list prices to decline may be attributed in part to continuance of expectations of rising prices, to additional increases in costs arising out of commitments made during the preceding boom, and to the brevity of the recession.

*Expansion since early 1958*

When recovery in business activity began in the spring of 1958, average levels of prices were appreciably higher than in early 1954—when the previous recovery began. Expectations of continuing upward creep in prices remained widespread. The reality of expectations of inflation became obvious not so much in the behavior of commodity markets but in a further advance in common stock prices to new highs and a continued increase in land values. Moreover, interest rates turned up promptly and long-term rates which had declined only moderately in the recession, quickly approached or reattained prerecession highs.

The pattern of demands, production, productivity, prices, and profits through the first year of expansion was similar in many important respects to the comparable period of recovery from the 1954 low. Consumer buying expanded rapidly, housing starts closely paralleled the rise of 1954-55, and liquidation of inventories slowed down and then gave way to accumulation toward the end of 1958. Constant dollar gross national product reached a new high in the fourth quarter of 1958 and industrial production exceeded the 1957 prerecession peak by March 1959. Prices of sensitive industrial materials responded to expanding demands, rising about as much in the first year of economic expansion as in the comparable period of 1954-55.

However, growth in final demands was less rapid than in the comparable period of 1954-56. Consumer buying of autos rose less sharply—for a variety of reasons, including higher prices and no important further easing in credit terms on contrast to the marked liberalizing of terms in 1955. Moreover, merchandise imports rose substantially while exports changed little. In recent years, there has been a considerable improvement in the ability of other industrial nations to satisfy their own requirements and also, partly because of price advances in this country, to compete with American manufacturers of many materials and finished products in domestic markets as well as in markets abroad.

Consequently, while consumption of materials in manufacturing reached a new high in the spring of 1959 and inventories were being accumulated at a rapid rate (stimulated in part by the expectation of interruptions of supply by strikes), the margins of capacity over output for most major materials were somewhat greater than in mid-1955, and greater than during any other period of high-level activity since World War II. The margins were not large, but their importance was magnified by the fact that they existed simultaneously in several industries whose markets overlap. Government policy actions and policy pronouncements, furthermore, lessened the expectation of rising prices. Altogether, there was more uncertainty in the outlook, and prospects were for more intensive competition.