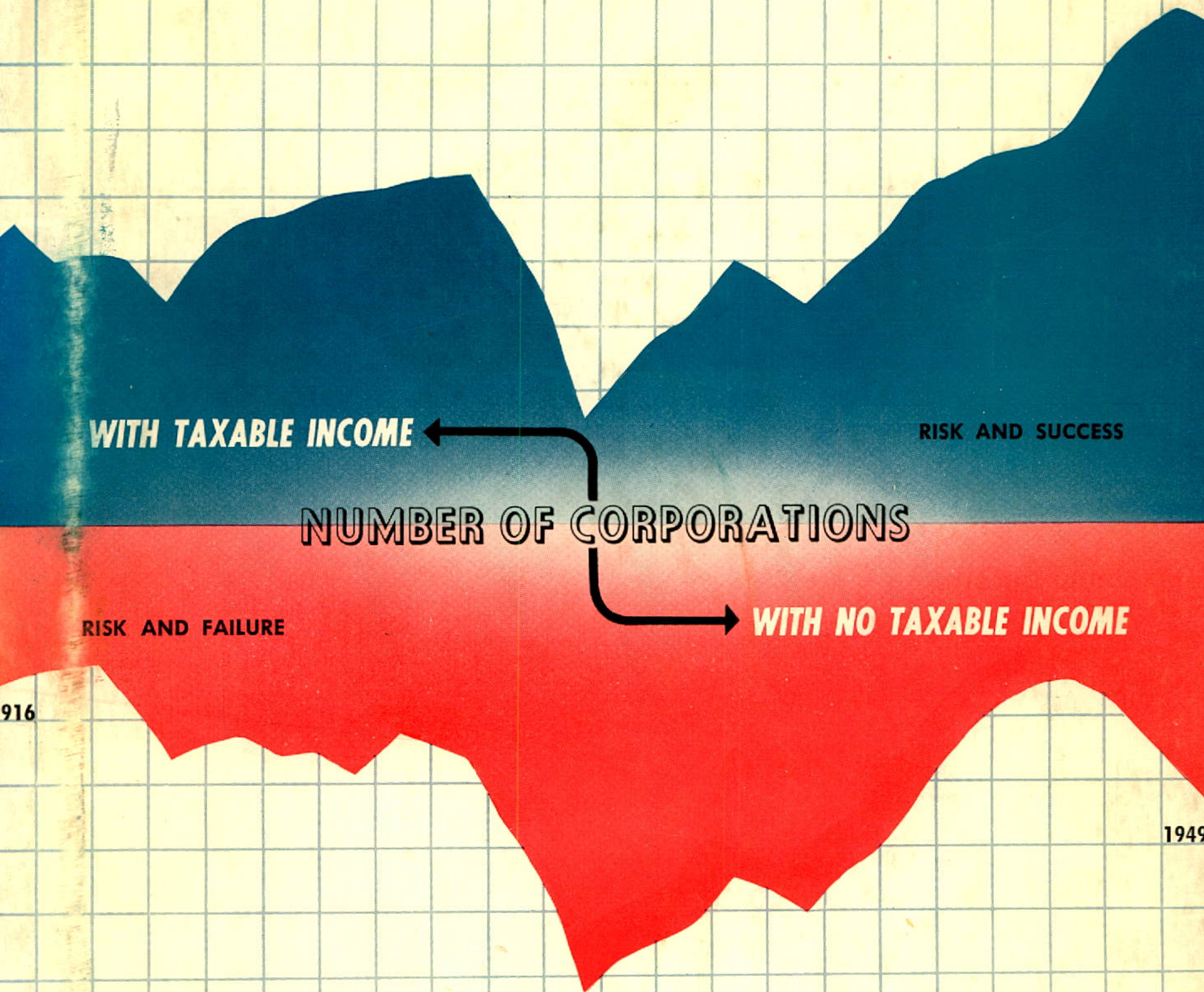
no. 37

National industrial conference board
Annual meeting [chartsurvey]

PROFITS IN PERSPECTIVE



A Graphic Analysis Prepared for the
37th ANNUAL MEETING
The Conference Board

CONTENTS

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PROFITS
IN PERSPECTIVE

Prepared for the

37th

ANNUAL MEETING

of

THE CONFERENCE BOARD

May 21-22, 1953

FOUNDED 1916

NATIONAL INDUSTRIAL CONFERENCE BOARD, INC.
247 Park Avenue, New York 17, N. Y.

FOREWORD

WE SEEM to be emerging slowly from an era in which profits and our profit-making system were subject to violent criticism, if not moral condemnation, and to much restrictive legislation.

In part, these criticisms and punitive actions stemmed from industry's inability or reluctance to put the solid facts about profits before the workers, shareholders, and public in general, in a form which could be understood and believed. In part, such antipathy stemmed from public ignorance of the vital economic functions performed by profits in making our enterprise system work. Some looked at profits as evidence of the concentration of control. It is only in recent years that unprejudiced studies have highlighted the competitive battle for markets that goes on even among the giants, as well as the wider distribution of corporate ownership throughout the income pyramid.

This Chart Study is designed to deepen the knowledge of both the dimensions and the functions of profits. One public opinion poll after another reveals that the general public still believes that profits are far higher than they really are. Paradoxically, the same polls reveal that the public impression of what would constitute a "fair" profit is close to, and in many cases considerably above, the rate that is actually earned by corporations. Profits, too, are rarely looked at in the perspective developed in this analysis—as a share over the years of national output, sales, and as a share of the total contribution of the corporate economy to national income—and distorted views still prevail and are embellished by those who are opposed to the profit system.

This Chart Study was prepared for the 37th Annual Meeting of THE CONFERENCE BOARD by Martin R. Gainsbrugh, the Board's Chief Economist, and Gertrude Deutsch, with the assistance of other members of the Division of Business Economics. The Board's Chart Department, under the direction of Paulette LeCorre Lydon, prepared the charts.

JOHN S. SINCLAIR,
President

May, 1953

Against the Background

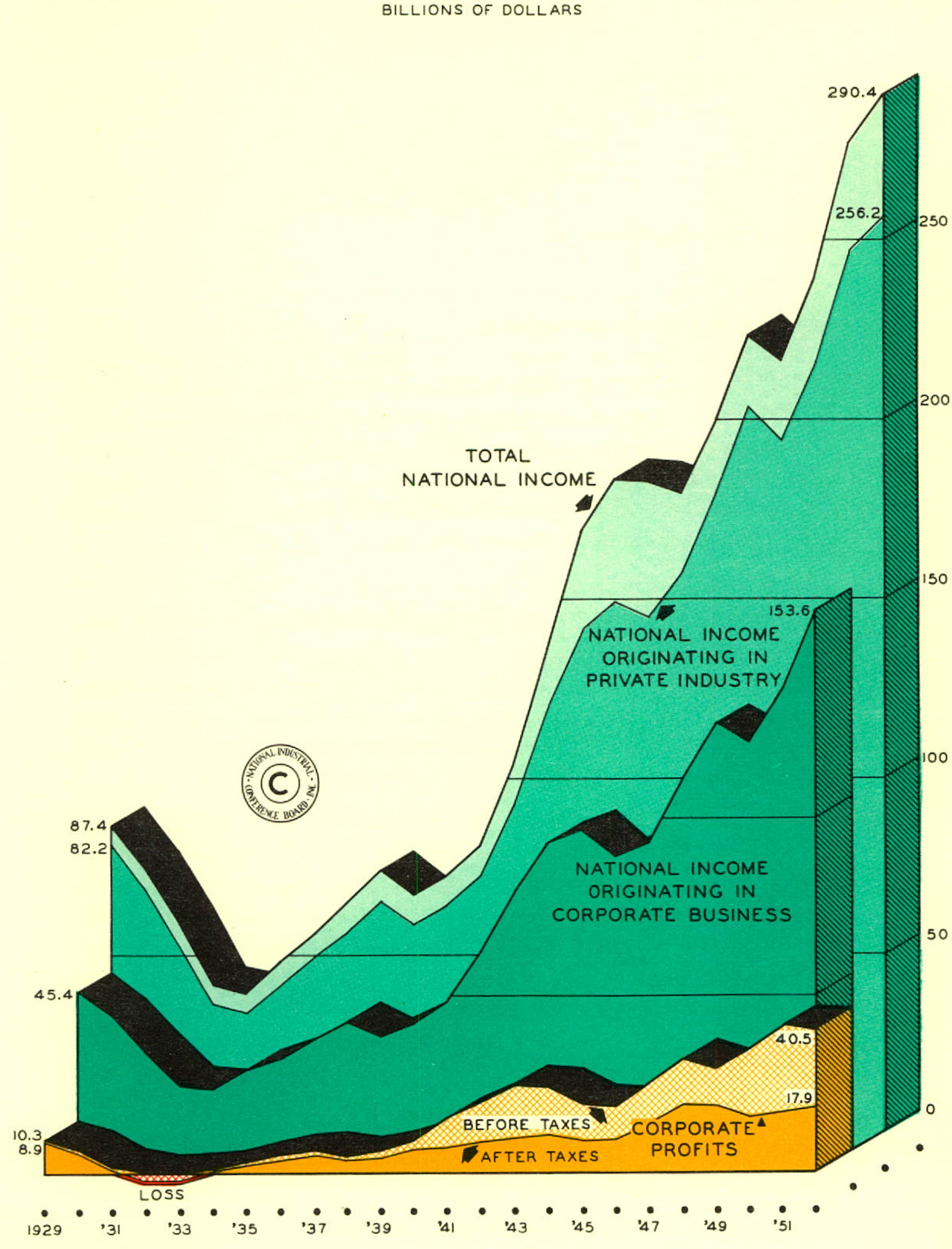
THE AVERAGE citizen who reads about new peaks in corporate earnings year after year must think that profits are soaring. Last year, for example, total corporate earnings were officially reported at more than $40 billion. Even in 1929 they were only $10 billion, and they were greatly below that figure just before the war. But this is far from being the whole story. The huge dollar total does not tell about the even greater expansion of national output, or about the greater investment needed to finance this mounting production. While the profit total has expanded rapidly over the decade of inflation, it has increased less than the national income.

Profits must be viewed against the total national output which they help to bring into being if they are to be seen in perspective. When this is done it is found that only a minor fraction of our annual production is allowed to flow into profits. The bulk of the nation's output is paid out in wages and salaries, in interest and rent, and to the farmers and other self-employed.

Over the past twenty-four years, profits after taxes have averaged only about 6% of the total national income. It is this 6% that provides the incentive to risk—the willingness to put savings into the expansion of tool power and creation of jobs which together have made our nation the world's industrial colossus. It is to corporate profits that government looks as an almost inexhaustible source of tax revenue. Wage earners look to profits as a source from which their earnings can be miraculously increased. Shareholders look to corporate profits for greater dividends as a return for the risk they take. Consumers see in them the possibility of lower prices and better goods. Despite the modest share of the nation's output left for corporate profits, they are expected to do all these things. If they disappoint the expectations of any one of the claimants, the whole profit system is blamed.

Sources: Department of Commerce; THE CONFERENCE BOARD.

THE PROFIT PROFILE



▲AFTER INVENTORY VALUATION ADJUSTMENT

Relative Stability of Profits

CORPORATE profits are highly sensitive to national economic activity. In periods of expansion they swing upward more than does national income or other related measures of business activity. They respond even more violently when national income drops and, as in 1932-1933, they may be transformed into losses. (Capital is the only factor of production that is not assured a positive return.)

Viewed in perspective over the past three decades, however, profits are found to be a highly stable percentage of national income at *comparable* stages of the business cycle.

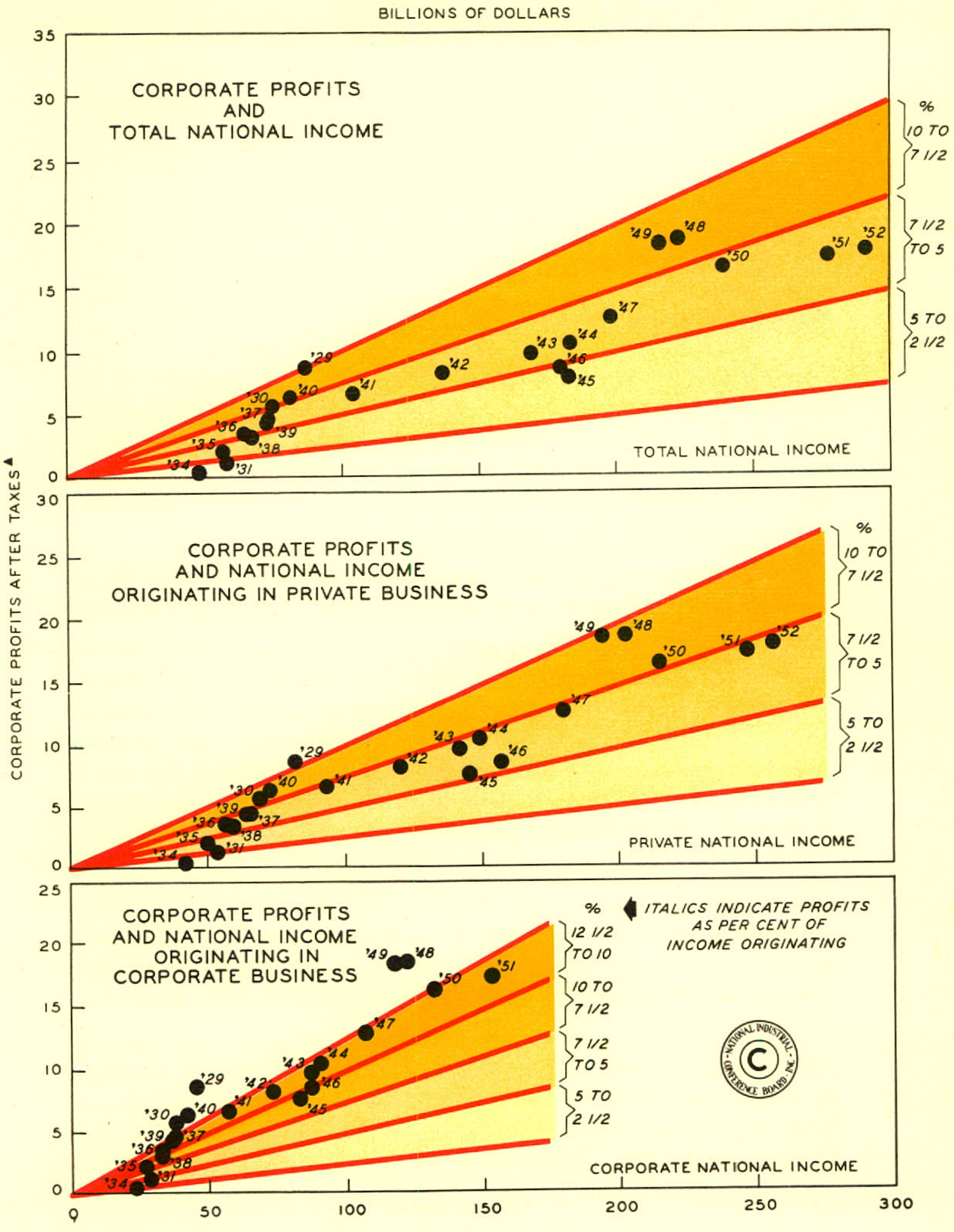
Corporate profits after taxes are correlated with three meaningful national comparatives in the accompanying chart. The first and traditional comparison is with national income. Profits in recent years fall well below their relationship to national income not only in 1948-1949, but also in 1929-1930 and 1940. They fall in the band of 5%-7.5% of national income —the most common (modal) percentage of the years under review.

A further comparison is with *private* national income. Over the past quarter century income originating in government has risen far more rapidly than national income. Restricting the comparison solely to income originating in private industry brings the stability of the profit ratio into sharp relief. Profits in 1951-1952 again fall in the 5%-7.5% band.

Finally, corporate profits are viewed against the total contribution of the corporate economy to national income. In 1951, income originated by corporations totaled nearly $154 billion. In other words, corporations paid out to the various factors of production fully 50% of the total income of the country. Once again, the chart shows the relative stability of corporate profits.

Sources: Department of Commerce; The Conference Board.

HOW BIG ARE PROFITS ?



▲*AFTER INVENTORY VALUATION ADJUSTEMENT*

NOTE: 1932 AND 1933, WHEN CORPORATIONS AS A WHOLE INCURRED A DEFICIT, ARE OMITTED.

Property's Share Declining

STOCKHOLDERS and other owners of property have received a steadily shrinking share of the national income during the past quarter century. Fully a fifth of the nation's income in 1929 went to the owners of property as dividends, rent, and interest payments. Today, their share has fallen to less than a tenth.

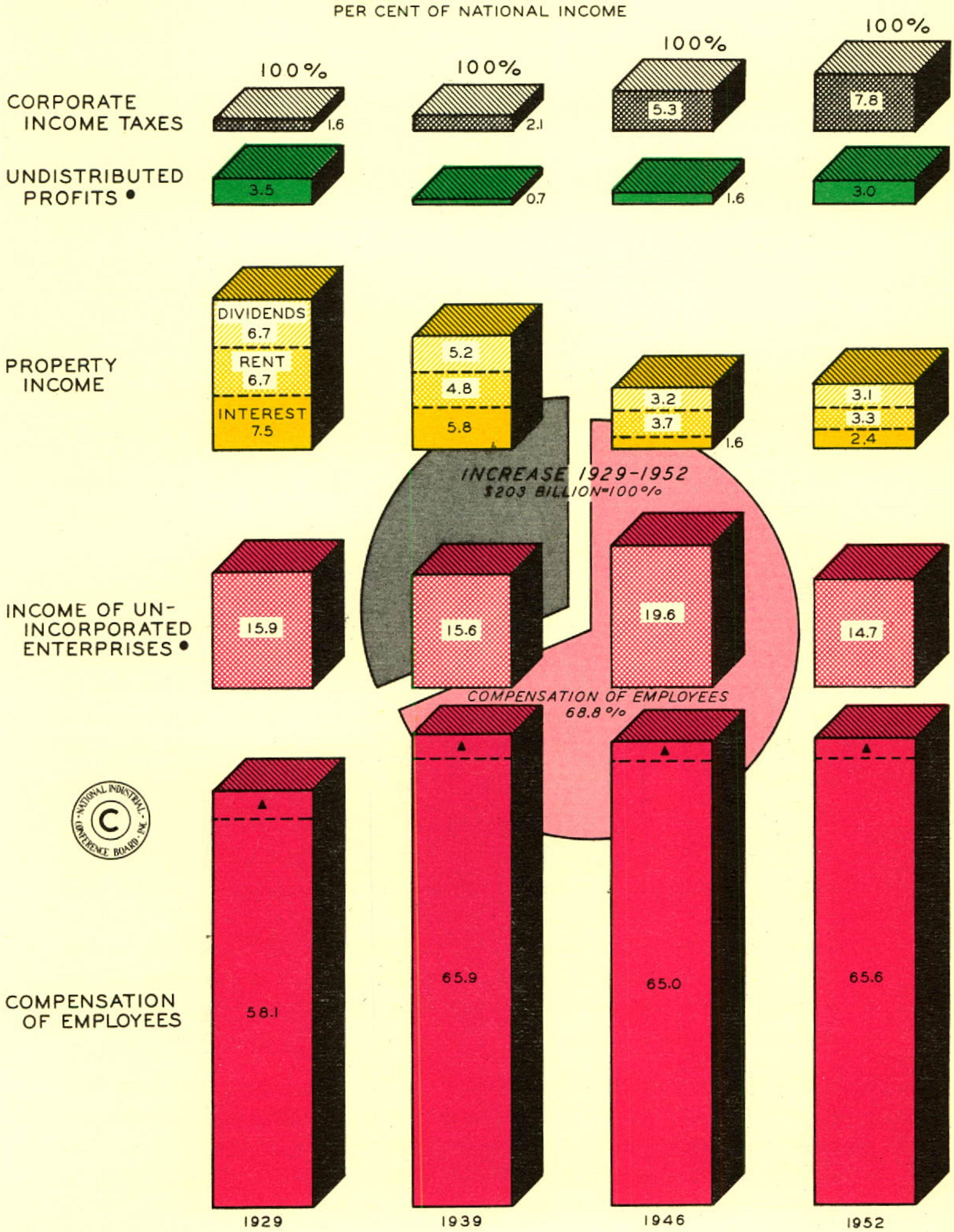
This shift is largely the result of a series of legislative measures that were designed to alter the distribution of income. Rent controls, for example, made it difficult if not impossible for rents to keep pace with the inflationary surge in other prices. Interest rates, in turn, reflected the easy money policy of the period and the desire to keep the interest burden on the huge public debt low at any cost. The growing reliance of government upon corporate taxes for current revenues has likewise reduced the share of corporate profits that is available for dividends. Steadily declining payments to stockholders have made it even more difficult for corporations to secure equity financing. This stems in good part from the attrition of savings in the higher-income groups, whose personal income taxes have been sharply increased.

Corporate taxes in 1952 accounted for nearly 8% of national income In 1929, such taxes took only 1.6%. (Data are not available on the increased burden borne by entrepreneurs, labor and other factors of production.)

In contrast to the declining share received by the owners of property, the portion of national income distributed as wages and salaries was higher in 1952—nearly 66%, as compared with 58% in 1929. And while national income rose by $203 billion from 1929 to 1952, nearly 69% of this increase was distributed in the form of wages and salaries.

Sources: Department of Commerce; THE CONFERENCE BOARD.

WHO GETS NATIONAL INCOME



▲CORPORATE OFFICERS

●AFTER INVENTORY VALUATION ADJUSTMENT

Profit Dimensions

How Industries Share the Profits

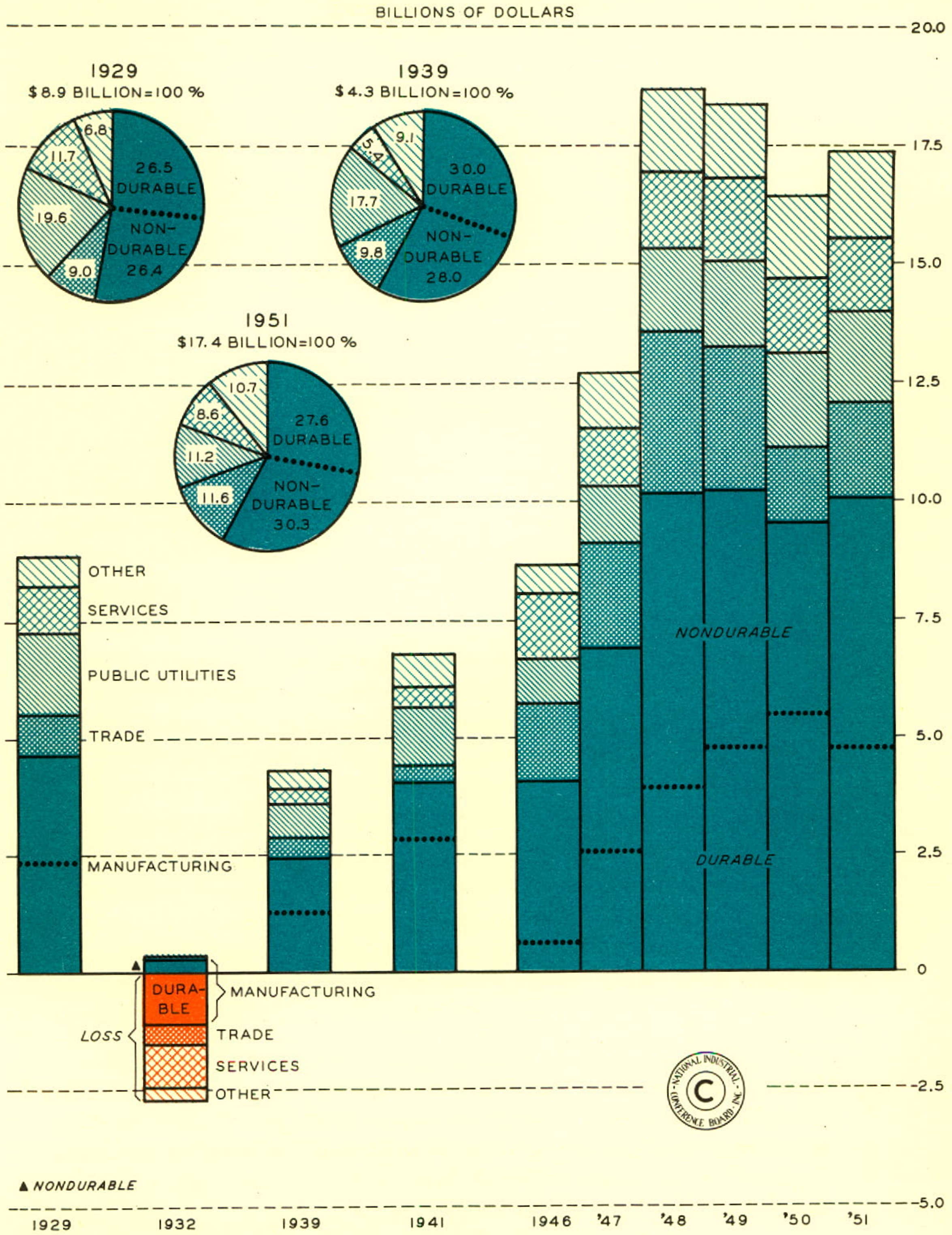
IN THE early postwar years the distribution of corporate profits among industries was markedly different from the prewar distribution. The late Forties, however, saw a return toward the pattern of the late Thirties. In 1946, for example, the manufacturing corporations accounted for slightly less than half of total corporate profits. Since 1950, the manufacturing share has run at a little less than three fifths of the total, or about its 1939 share.

The tendency to return to the prewar pattern of profit distribution is also evident within manufacturing. Immediately following the war, non-durables producers enjoyed a considerably larger share of profits than the producers of hard goods. But since 1950 the two sectors have returned to the rough balance that prevailed in 1939. Similarly, profits of wholesale and retail trade corporations, which accounted for as much as one fifth of total corporate earnings in 1946, have returned to their prewar share of about one tenth.

Service corporations (including financial, real estate, and insurance companies) still have a larger share than in 1939. But the portion going to public utilities (including communication and transportation) is much smaller than it was prewar. This industry accounted for barely a tenth of all profits in 1951, as compared with nearly a fifth in 1929 and 1939.

Sources: Department of Commerce; The Conference Board.

CORPORATE PROFITS BY INDUSTRY



NOTE: "SERVICE" INCLUDES FINANCE, INSURANCE AND REAL ESTATE.
"OTHER" CONSISTS OF AGRICULTURE, MINING, CONTRACT CONSTRUCTION
PROFITS ARE AFTER INCOME TAXES AND INVENTORY VALUATION ADJUSTMENT

Profitability: How Do You Measure It?

"HOW profitable is business?" is an easy question to pose, but extremely difficult to answer. Profits are frequently viewed in perspective by relating them to sales or to net worth. In recent years these measures have given different and often conflicting answers.

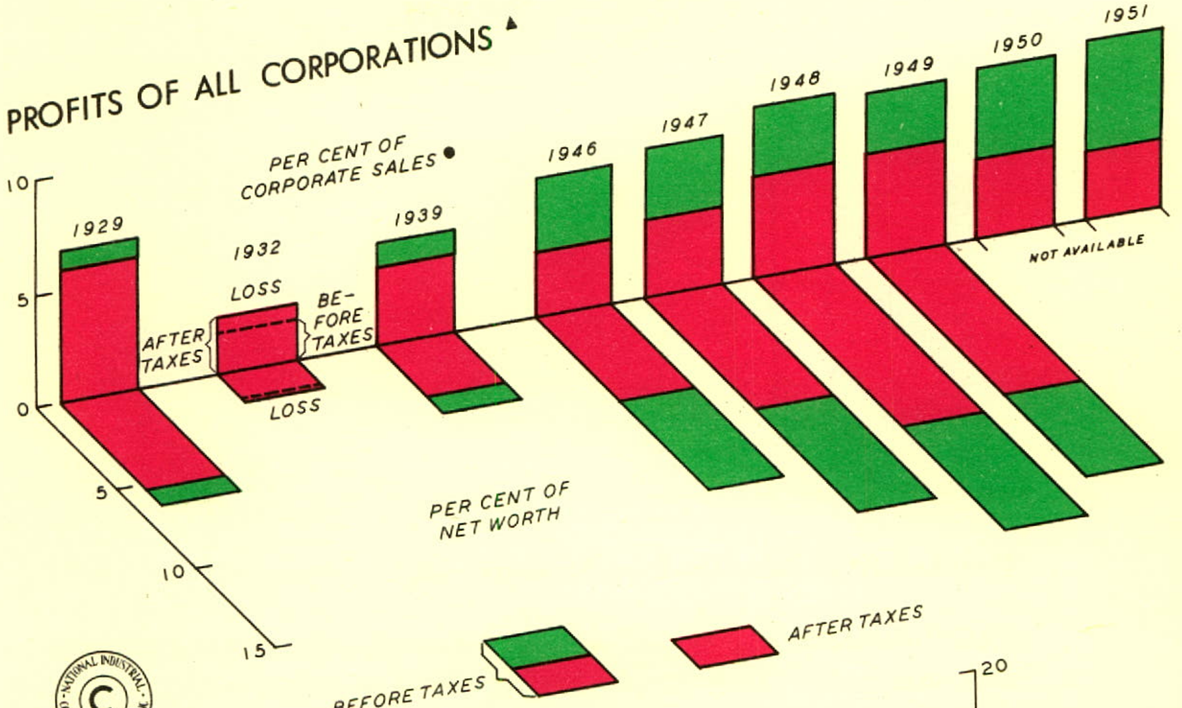
The profit-sales ratio throws considerable light on the extent to which profits affect selling prices. In 1951, for example, nonfinancial concerns earned $16 billion after taxes and adjustments for inventory profit and loss. This was equivalent to only 3.3% of sales. (Preliminary figures for 1952 show about the same margin as in 1951.) This "service charge" of business was no higher than in 1939 and considerably less than in 1929.

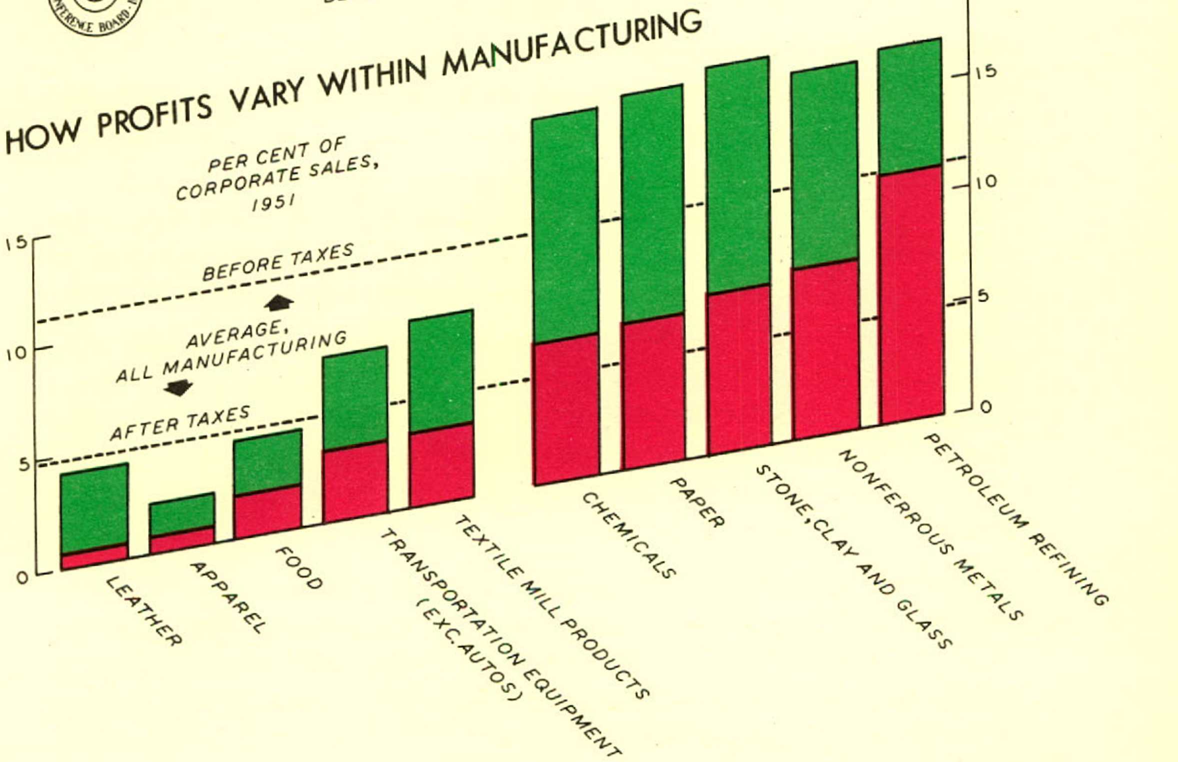
When net worth is used for perspective, the profit margin is higher than it was in 1929 and 1939. After-tax profit amounted to nearly 10% of net worth in 1949 (the latest data available), compared with only 4% in 1939 and 6% in 1929. The primary reason for this divergence is that much of the net worth of business reflects prewar prices, while sales are in current dollars.

Business profitability is even more difficult to put in perspective in interindustry comparisons. Industries with rapid turnover (food, for example) tend to have lower profits-to-sales ratios than industries which have a long production cycle (steel and petroleum refining), where there is a high investment per dollar of sales.

Sources: Department of Commerce; Securities and Exchange Commission; Federal Trade Commission; THE CONFERENCE BOARD.

THE MARGIN OF PROFIT





▲ AFTER INVENTORY VALUATION ADJUSTMENT

● PROFITS AND SALES OF FINANCE, INSURANCE AND REAL ESTATE CORPORATIONS ARE EXCLUDED

Claimants to Sales Revenue

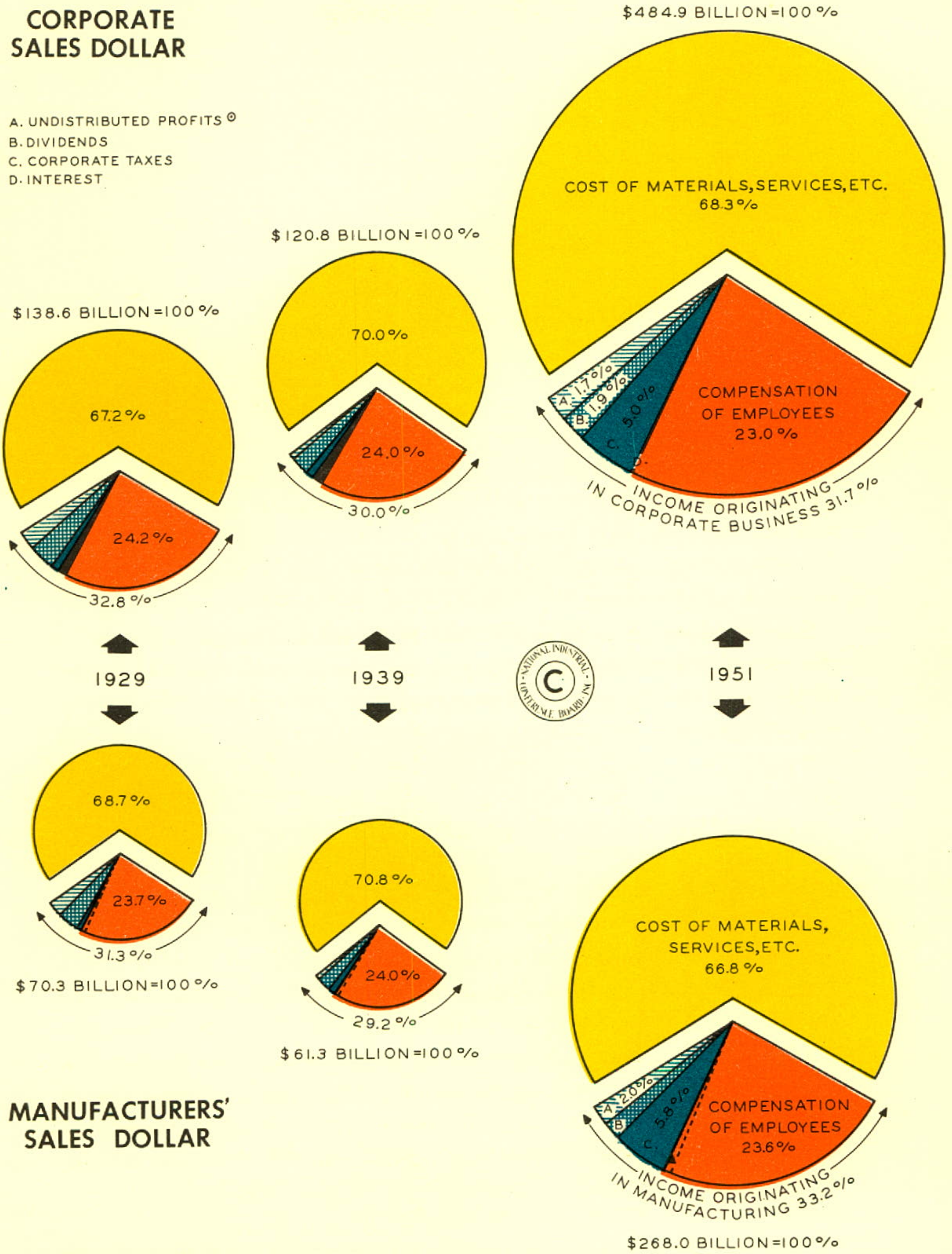
IT IS from sales that industry must derive funds for payrolls, for taxes, and for shareholders. Of the vast amount of revenues from sales, however, by far the major portion is not available to these claimants. The bulk must be paid to suppliers at market-determined prices over which the purchaser has little or no control. In 1951, nonfinancial corporations as a group paid out a third of a trillion dollars for materials and related items required to produce sales of nearly half a trillion dollars. Less than a third of the total revenues from sales represented value created within the corporate sector.

Payment for materials took a slightly larger share of the sales dollar in 1951 than in 1929. A larger percentage was set aside for taxes—five cents per dollar of sales, as compared with about one cent in 1929 and 1939. The share paid to labor remained virtually unchanged, while the relative interest burden was sharply decreased. Shareholders, too, received less per dollar of sales, and less of the sales dollar remained with corporations for purposes of future growth. The major beneficiary, then, from the change in the distribution of the corporation's sales dollar over the past two decades was government.

Manufacturing industry had sales of $268 billion in 1951, but only $73 billion remained after paying suppliers and meeting income taxes. Of this, $62 billion went to manufacturing workers. Once again, shareholders received a smaller share than prewar, and only two cents of every dollar of sales received by manufacturers remained available for future growth.

Sources: Department of Commerce; THE CONFERENCE BOARD.

WHO GETS THE SALES DOLLAR ?



⊙ AFTER INVENTORY VALUATION ADJUSTMENT

▲ INCOME OF UNINCORPORATED ENTERPRISES AFTER INVENTORY VALUATION ADJUSTMENT

NOTE: INCOME ORIGINATING IN MANUFACTURING INCLUDES NET INTEREST, A NEGLIGIBLE PER CENT, WHICH IS NOT SHOWN SEPARATELY.

The Profits Pay Envelope

GIANT numbers are always hard to understand. For example, $190 billion paid out in 1952 in employee compensation; or such related totals as the $23 billion collected in corporate income taxes, the $9 billion distributed as dividends, or the like amount which corporations retained for future growth. To the average factory employee, the more meaningful numbers are those that appear on his paycheck or weekly pay envelope. His compensation in cents per hour or dollars per week is, therefore, a yardstick against which other magnitudes can be gauged.

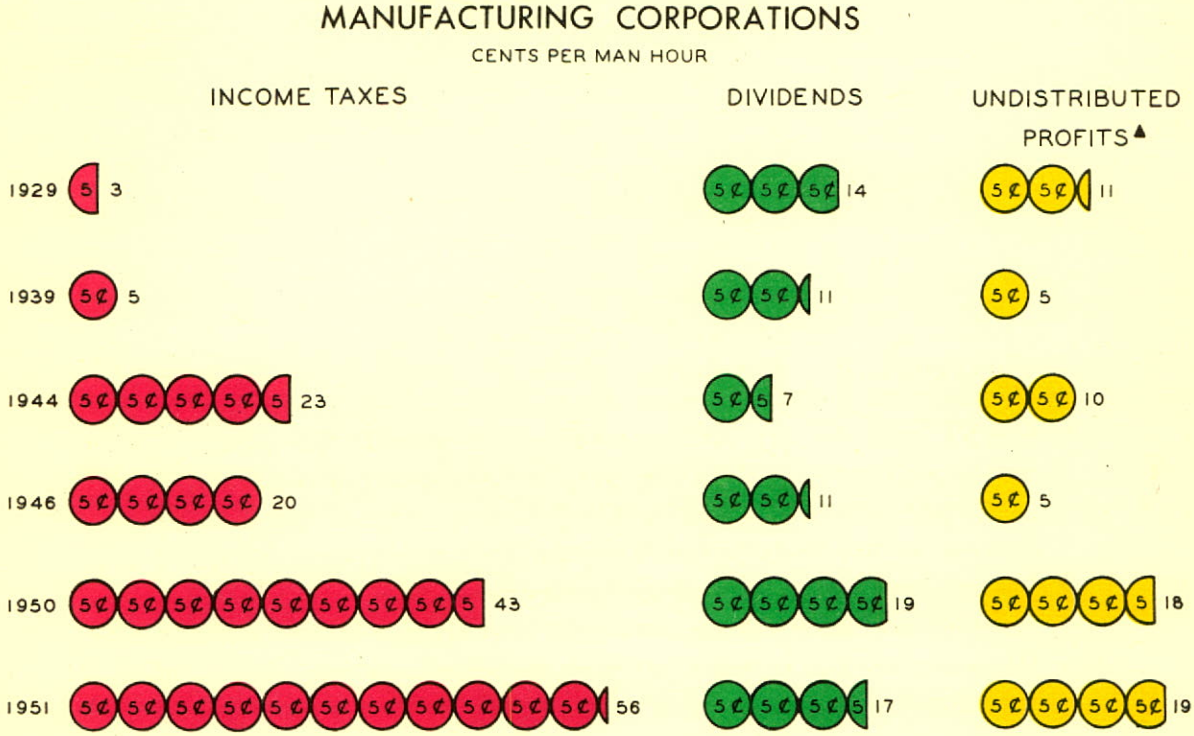
The accompanying chart puts taxes, dividends and retained profits for the manufacturing economy in just this perspective. Each of these giant dollar totals is expressed in the more familiar terms of cents per hour of work. Thus, the $16 billion of income taxes collected from manufacturing was equal to 56 cents per hour worked in manufacturing in 1951. Dividends came to 17 cents per hour, and profits retained for future growth to 19 cents. Taxes took 53 cents more per hour worked than in 1929; dividends and retained profits were only 3 and 8 cents more. Hourly earnings, meanwhile, were up more than a dollar.

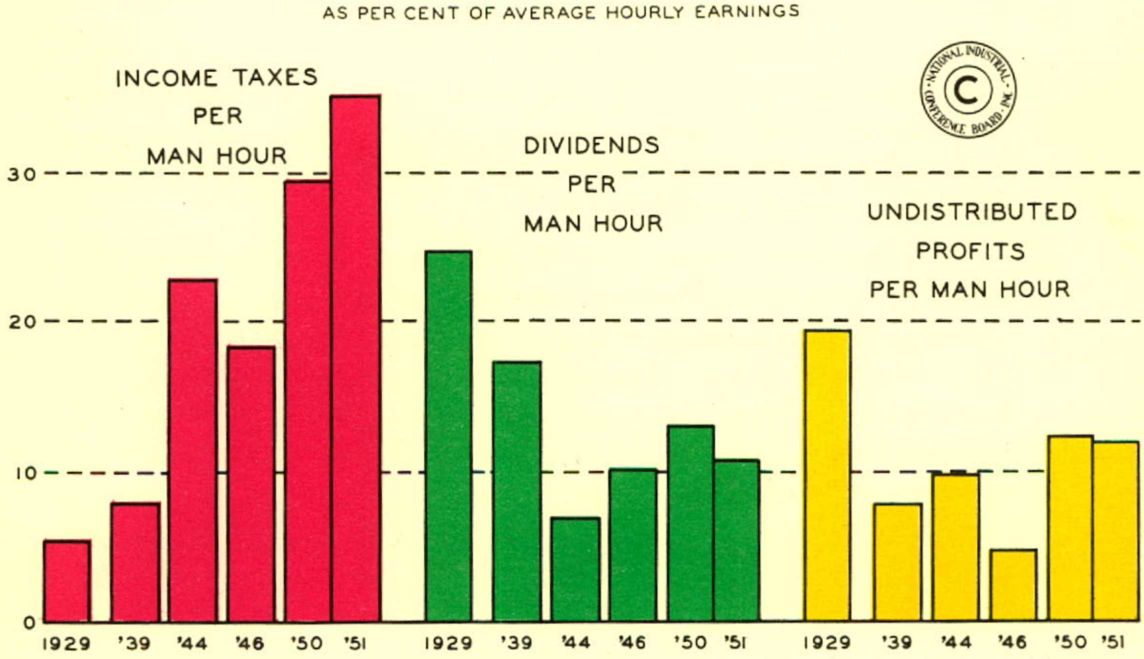
The federal and state governments took as much in taxes per man hour in 1951 as the average factory worker received for his hour's work in 1929.

Average hourly earnings in manufacturing have nearly tripled since 1929 and this, of course, affects their *relative* relationship to taxes, dividends and profits. Income taxes per man hour increased nine times as fast as earnings per hour; profits after taxes about one fourth as fast. So taxes, which equaled only 5% of hourly earnings in 1929, came to 35% of hourly earnings in 1951. Dividends and profits retained for future growth were jointly equivalent to about 23% of hourly earnings in 1951; in 1929 they represented almost twice that proportion.

Sources: Department of Commerce; Bureau of Labor Statistics; THE CONFERENCE BOARD.

PROFITS PER HOUR WORKED





▲ *AFTER INVENTORY VALUATION ADJUSTMENT*

Profits *and* Losses

IN GOOD years as well as bad, the record of the corporate economy clearly portrays the profit and *loss* characteristic of capitalism. Losses predominate in periods of recession or deep depression, but even in good times there is no assurance of reward for risk. Changes in consumer wants, technological innovations, geographic shifts of population, wars, fires, droughts and other natural hazards can and do produce a vast underlay of red ink even with more favorable market conditions. During the third of the century covered by the chart, a minimum of 27% and a maximum of 82% of active corporations reported operations in the red to the Bureau of Internal Revenue. At the predepression peak of 1929, some 41% of all active corporations wound up their operations with a deficit. At the trough of the depression, four of every five corporations could not report net income, while as late as 1939 the number of loss corporations was substantially greater than those reporting taxable income.

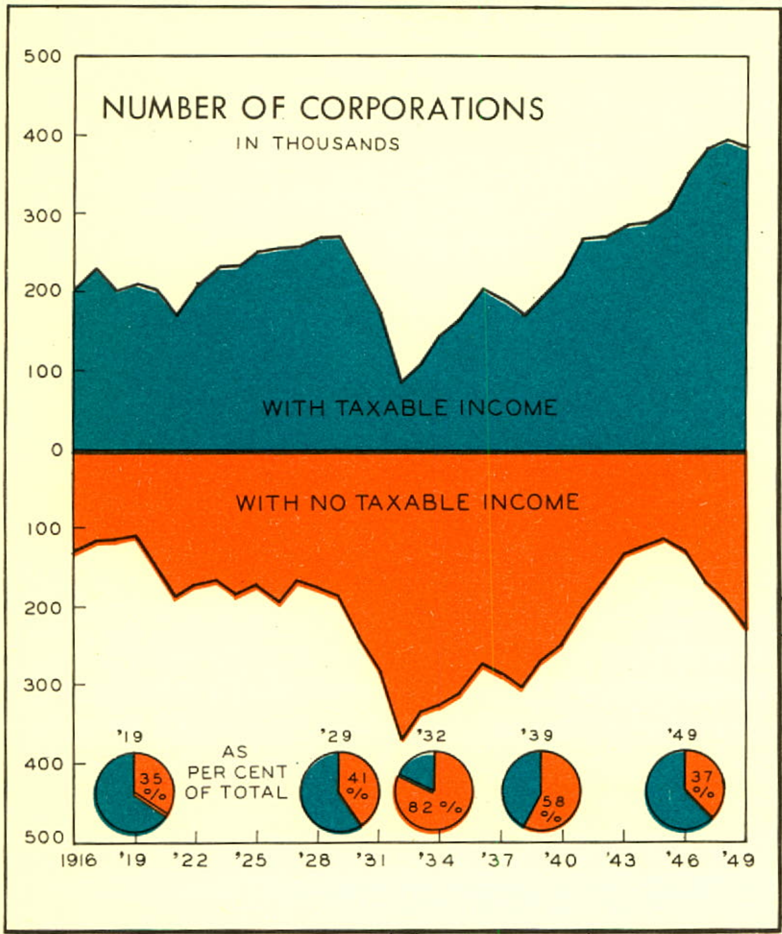
In the mild recession of 1949, nearly four of every ten corporations were again without net income.

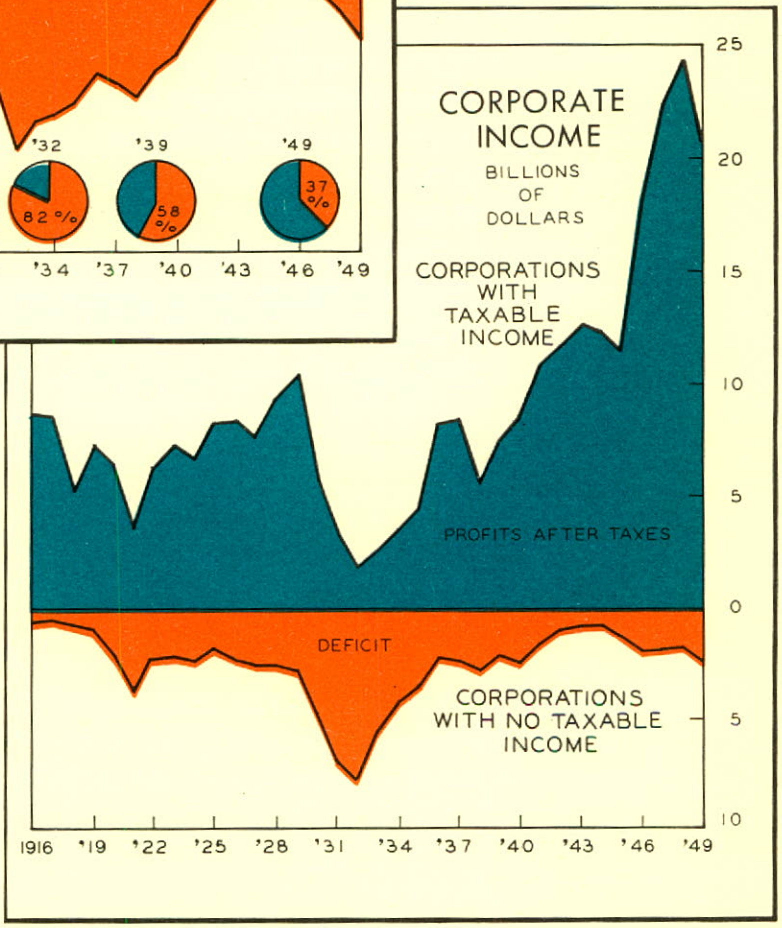
The same pattern emerges, although in less dramatic form, when the magnitude of corporate loss is contrasted with profits earned by the successful enterprises. Deficits of loss corporations even in the prosperity of 1929 were nearly 30% of all profits earned by money makers. In 1941, another highly active year, losses totaled $1.8 billion, a sixth of all reported profits. Again, in 1949, the total deficit reported was $2.4 billion, or 11½% of the reported profit.

Losses have been severe in the manufacturing and retailing sectors even in years of high activity, but no industrial sector is immune to the loss hazard.

Sources: "Statistics of Income"; THE CONFERENCE BOARD.

OUR PROFIT AND LOSS SYSTEM





Broadening the Shareholder Base

A CORPORATION is only one way of doing business; other ways include sole proprietorships, partnerships and cooperatives. Under the corporate form, individuals, by pooling their financial resources, can gain the advantage of economies of large-scale production while limiting their financial liabilities in the event of failure. The corporate form of organization has grown steadily more popular and today does over half the nation's business.

These corporate enterprises are in turn the property of the shareholders from whom their financial resources are originally obtained. Six million families have invested in, and thus own, the nation's corporations. Four fifths of the shareowning families hold publicly offered common and preferred shares. The remaining fifth hold shares in closed or family-held corporations, or in both types.

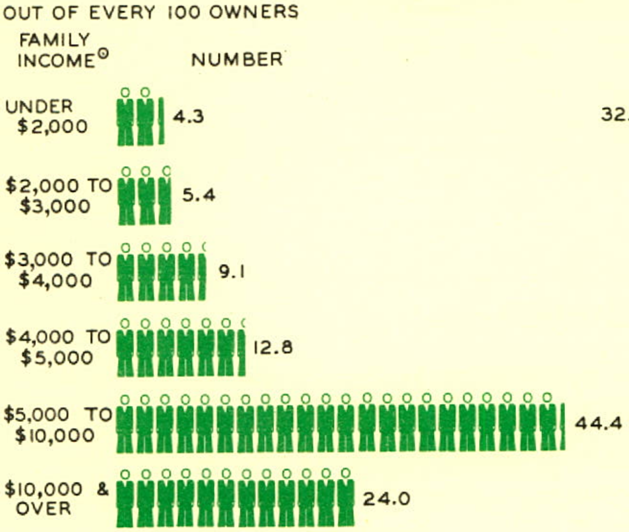
Nearly two million shareholders have invested in three of the largest corporations—American Telephone and Telegraph Company, General Motors Corporation, and the United States Steel Corporation. In all three instances, shareholders with small holdings predominate. In the case of A T & T, fully a fifth of all shares is held by investors with less than twenty-five shares, and more than half by those with less than 100 shares. Many of the holders of large blocks are insurance companies, investment trusts and the like who, in turn, were acting as investors, directly or indirectly, for numerous small savers.

As the chart indicates, three fourths of all *individuals* holding publicly offered shares have a family income of less than $10,000 a year, while nearly a third have an income of less than $5,000. One of every three is a nonemployed housewife. Clerical workers make up nearly one tenth of all shareholders, while skilled and other workers comprise almost a like proportion.

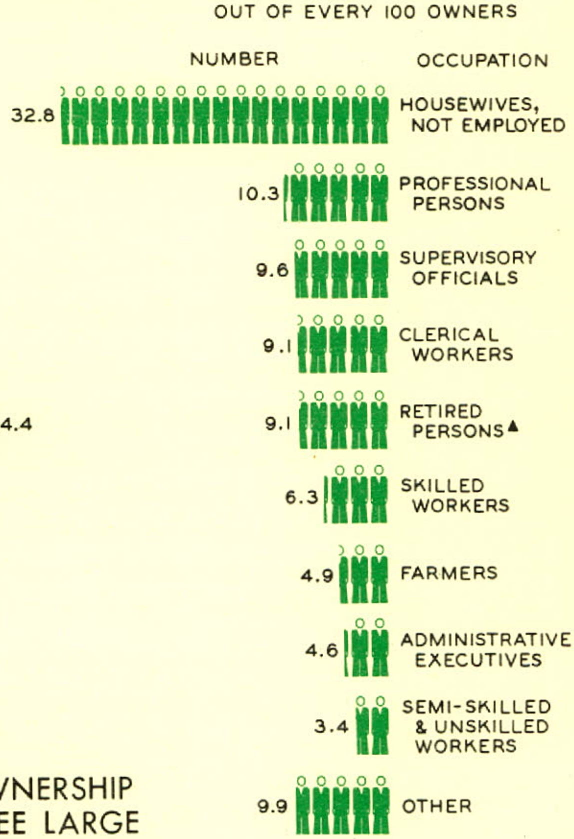
Sources: The Brookings Institution; American Telephone and Telegraph Company; General Motors Corporation; United States Steel Corporation; THE CONFERENCE BOARD.

WHO OWNS CORPORATIONS ?

THERE ARE 6.5 MILLION INDIVIDUAL SHAREOWNERS

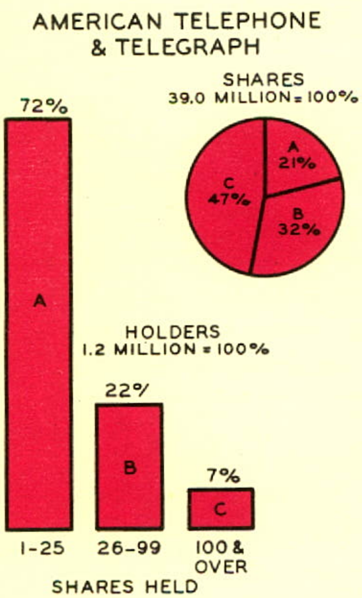


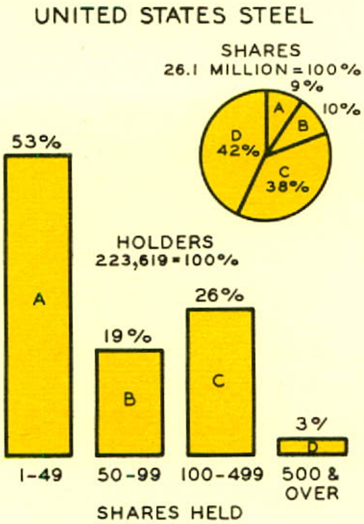
NOTE: EACH SYMBOL EQUALS 2 PERSONS

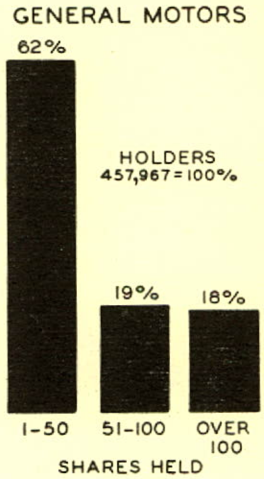


OWNERSHIP THREE LARGE CORPORATIONS

(COMMON STOCK)







⊙ BASED ON ANTICIPATED 1952 INCOME BEFORE TAXES

▲ INCLUDES NON-EMPLOYED AND DEPENDENT ADULTS

Forty Years of Corporate Income Taxes

WHEN the income tax became the law of the land just forty years ago, the initial corporate tax rate was one cent per dollar of corporate income. The yield of this tax in its first year was $39 million. One of the Senators voting for this tax had voiced the hope that the corporation tax:

> "... at the end of two years, if my estimate (of revenue) should be correct, should be reduced to a nominal amount or repealed."

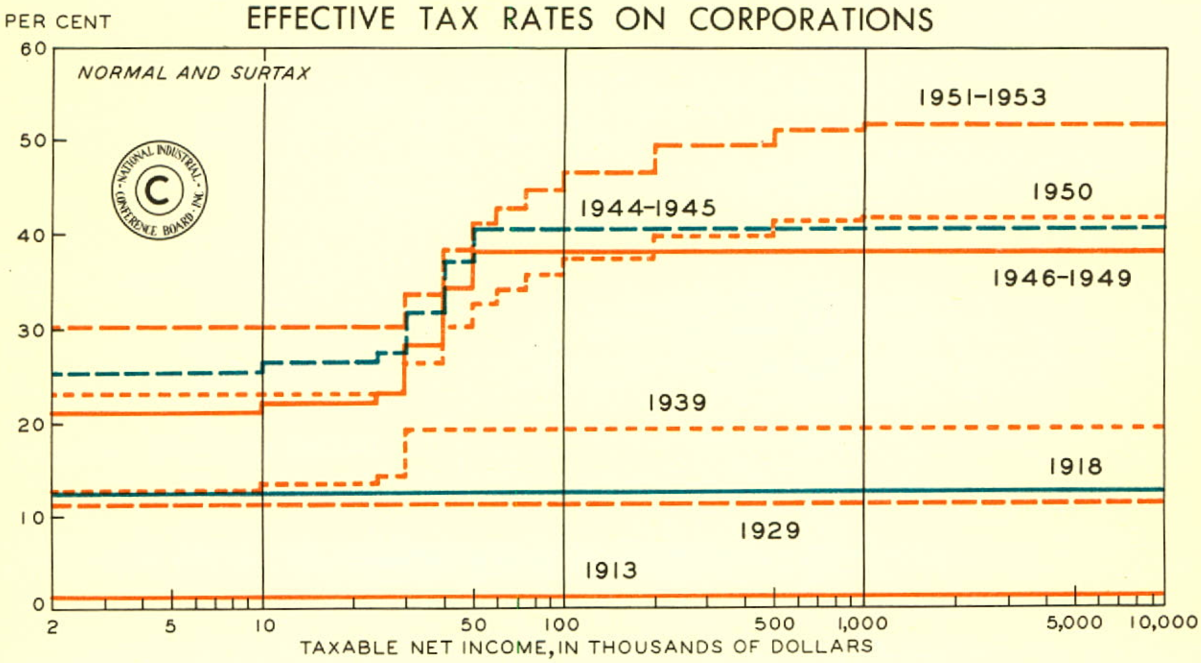
Since the historic 1913 date, nearly $200 billion has been paid into the Treasury as corporate income taxes. Under the highest bracket of excess-profits taxes, five of every six dollars of corporate net income are now siphoned off for revenue purposes. And the effective normal and surtax rates alone (excluding EPT) are such that a corporation with a taxable net income of $500,000 pays somewhat more than half of this amount to the Federal Government alone.

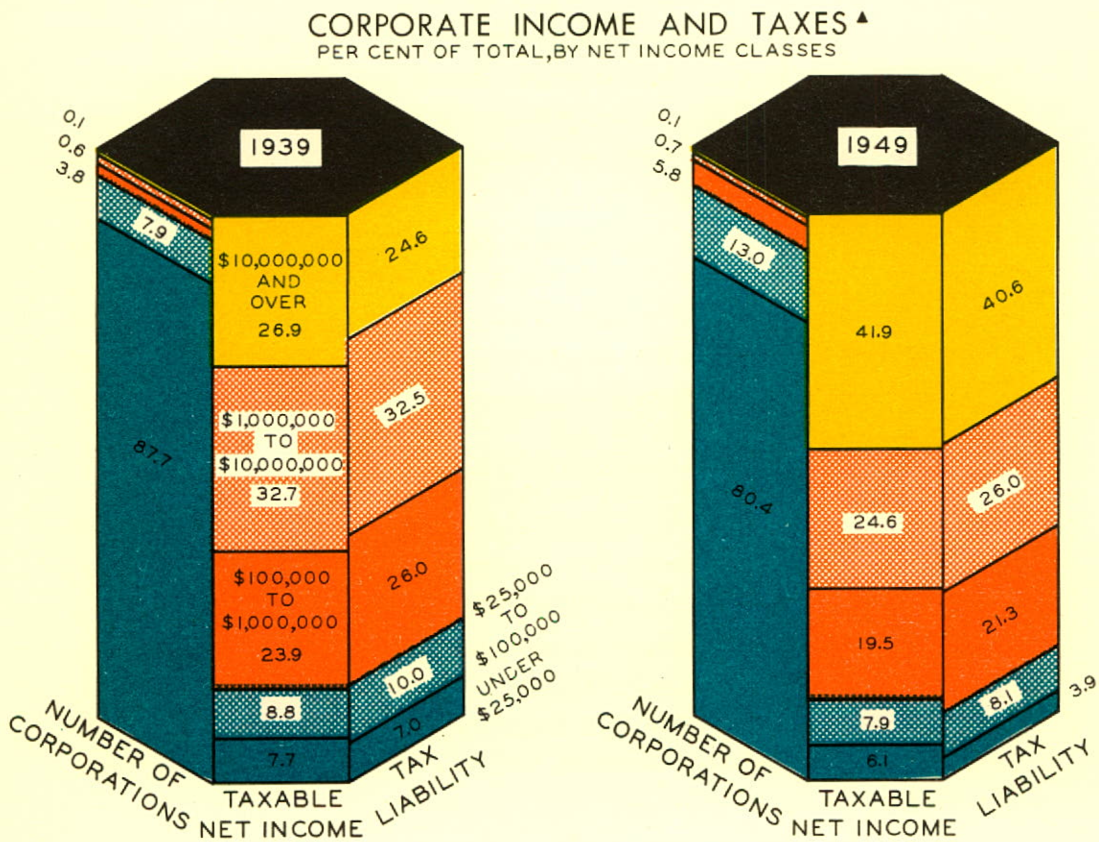
At the peak of World War II the total yield from direct corporate taxes was about $16.4 billion. Today, the corresponding amount collected from such federal taxes is nearly $7 billion above that wartime peak.

About two fifths of all federal corporate taxes in 1949 (latest available data) were paid by corporations with taxable net income of $10 million or more. Corporations with income less than $1 million also carry a heavy tax load. They contributed about $3.3 billion, or fully a third of all such taxes in that recession year.

Sources: Treasury Department; "Statistics of Income"; THE CONFERENCE BOARD.

THE TAX BITE





▲ *OF CORPORATIONS WITH TAXABLE INCOME*

Government as Senior Partner

GOVERNMENT is today the senior partner in whatever income remains with corporations after meeting all costs of operations, other than direct taxes. It now collects as much from the corporate economy in income and excess-profits taxes as is left for the stockholders and expansion together.

The full extent to which government has enlarged its share as senior partner in corporate earnings over the past seven years is highlighted in the upper half of the chart.

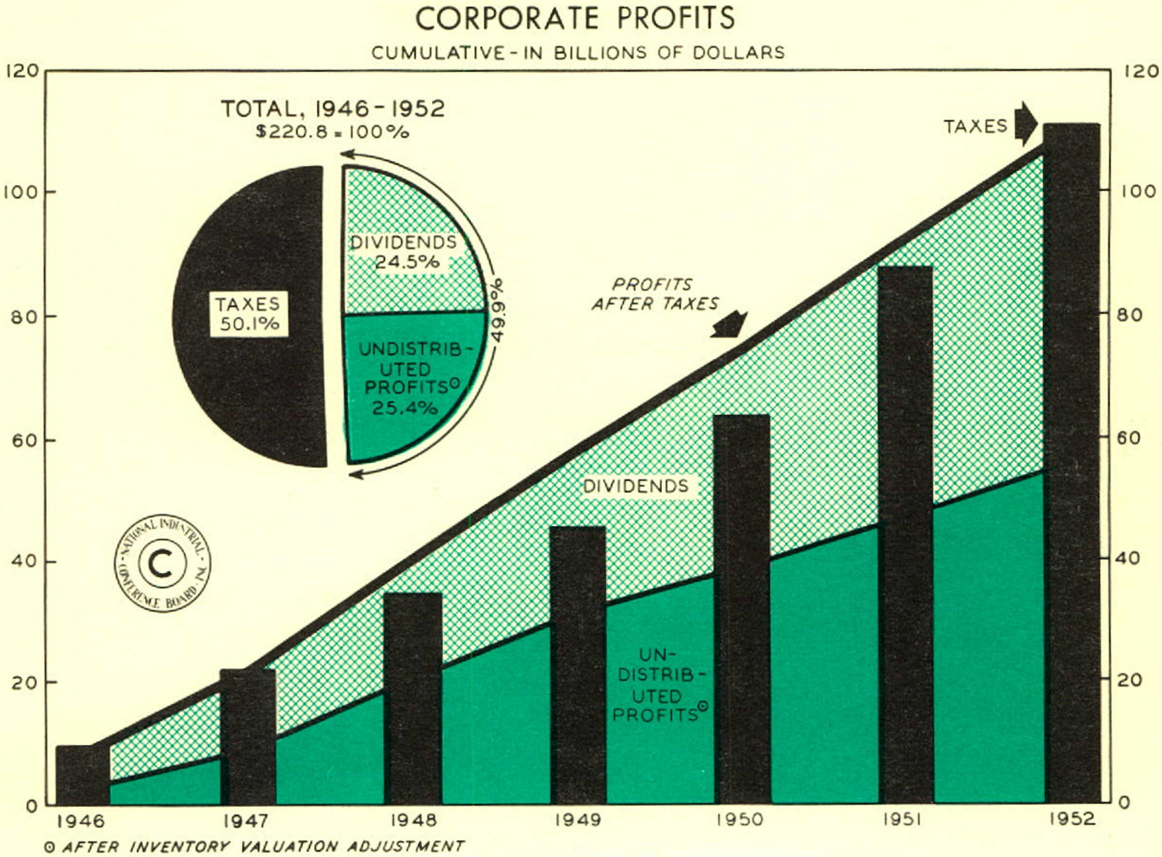
Corporations earned $221 billion before taxes over the years 1946-1952. During these years the federal and state governments levied $111 billion of income taxes on their earnings. Thus, every dollar made available to stockholders or retained for expansion was matched by an equal payment to the tax collector.

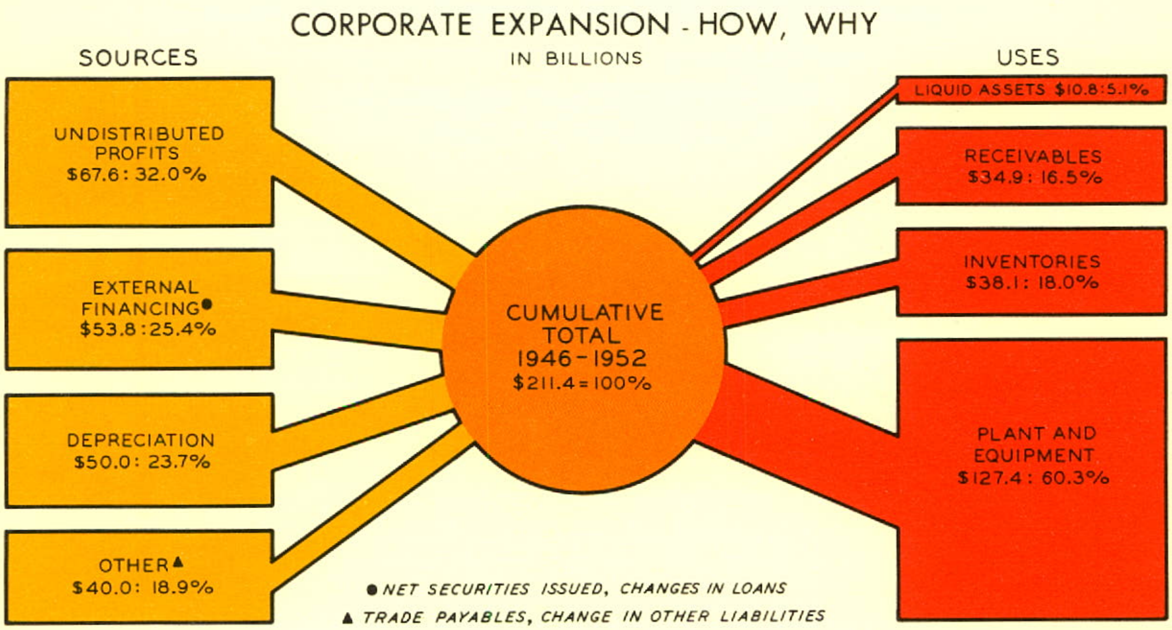
Shareholders received a somewhat higher proportion of profits after taxes in 1952 than in the immediate pre-Korean years. In 1952, dividends represented about 50% of profits after taxes, as compared with about 40% in 1948-1949. Undistributed profits were fully twice as large as direct corporate taxes in 1929; the ratio was reversed in 1952, with tax payments more than double retained earnings.

Since the war's end, corporations have needed more than $200 billion to finance the modernization and expansion required for their plant and equipment, to rebuild inventories, and increase working capital (see lower half of chart). Less than a third of this amount was available from retained earnings. In fact, the total of all corporate internal funds (depreciation reserves and retained earnings) approached only 56% of the requirements for postwar corporate growth. The remaining 44% was obtained largely through borrowing and only secondarily through equity financing.

Sources: Department of Commerce; THE CONFERENCE BOARD.

THE PROFIT-TAX RACE





Business Faces a High Cost of Living

INFLATION has clipped the purchasing power of the dollars spent by business as much, if not more, than those spent by individuals. The cost of doing business has soared since prewar, with a steep rise in the prices paid for raw and semifinished materials, labor, transportation, and other expense items. Fortunately, the greatly expanded volume of output has made for economies of scale so that unit costs, on the whole, have not risen quite as strikingly as total costs.

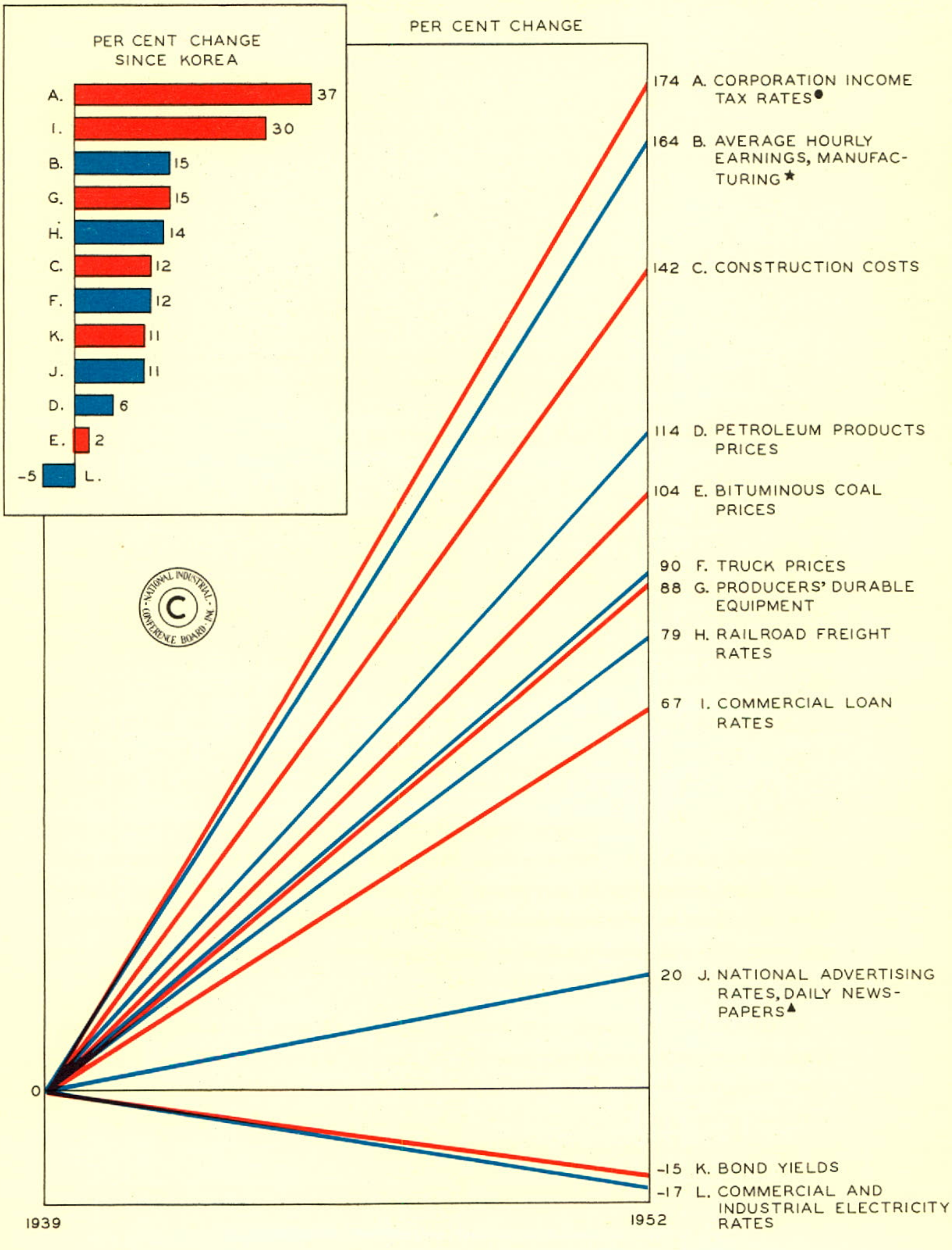
The profit dollar has been particularly impaired by the inflationary jump in the cost of plant and equipment. Construction costs have risen to such an extent that it takes almost $2.50 today to buy what $1.00 commanded prewar.

Federal taxes bite deeper than they did prewar, and there have also been sharp increases in property taxes and other state and local levies. The cost of an hour's work has about tripled. Included in such costs today are more liberal pension and welfare programs, extended vacations, and other fringe benefits for employees.

While industry's costs rose rather steadily during the war years, they tended to mount even more rapidly in the early postwar period. Business costs began to level off in 1948, but the Korean hostilities set off a new wave of price and wage increases which has brought the "cost of living" of business enterprises to an all-time high.

Sources: Department of Commerce; Treasury Department; Interstate Commerce Commission; Engineering News-Record; Marshall & Stevens; Edison Electric Institute; Federal Reserve; Bureau of Labor Statistics; American Newspaper Publishers Association; THE CONFERENCE BOARD.

INFLATION AND BUSINESS COSTS



● *NORMAL AND SURTAX, EFFECTIVE RATE OF LARGE CORPORATIONS*
★ *PRODUCTION WORKERS*
▲ *PER MILLINE*

Smaller "Seed" Profits

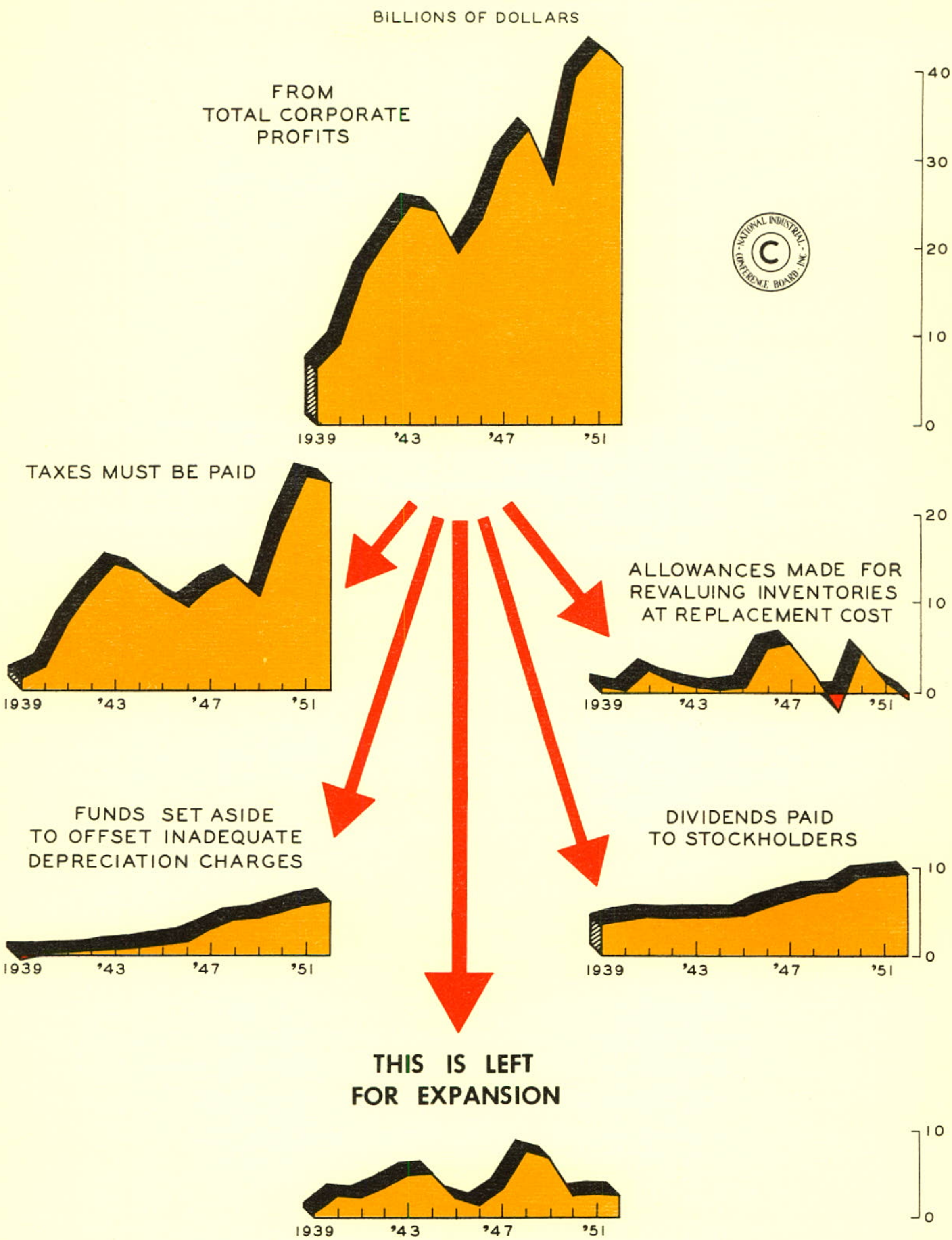
FEW figures enter the nation's economic accounts surrounded with a heavier cloud of statistical uncertainty than those on profits. Even the seemingly "hard" figures for corporate profits are officially recognized as being "soft" or infirm. The Department of Commerce warns that its allowance for depreciation is based on original rather than replacement costs. Rough estimates place the resulting overstatement of corporate profits for the past decade of inflation at more than $30 billion, assuming adequate allowance for depreciation based on prevailing market prices during this period. The official profit estimates also fail to allow for depletion and are before allowance for capital gains and losses. Finally, there are no official estimates available on the shrinkage in the purchasing power of profits in recent years.

The marked extent to which such adjustments and reductions would drastically alter popular impressions of corporate profits can be demonstrated strikingly in the table below. Thus, in 1950-1952, corporate profits before taxes totaled slightly more than $123 billion. In those three years, corporations distributed dividends of about $9 billion annually, or only 22% of earnings. Yet despite this giant profit total and modest dividend rate, only $7.5 billion remained available for expansion.

	1950-1952 (Cumulative Total) In $ Billions
Total corporate profits	123.3
Taxes	66.2
Profits after taxes	57.1
Inventory valuation adjustment	5.5
Understatement of depreciation	16.8
Dividends	27.3
Available for expansion	7.5

Sources: Department of Commerce; National Bureau of Economic Research; THE CONFERENCE BOARD.

PROFITS LEFT FOR EXPANSION



Putting People and Profits To Work

IT IS now estimated that by 1975 we will have added 36 million to our population. As the population rises, so will the number of people seeking employment. The Bureau of the Census estimates the probable increase in the number seeking employment at some 22 million by 1975. Thus, at least one new job must be created for every three now in existence.

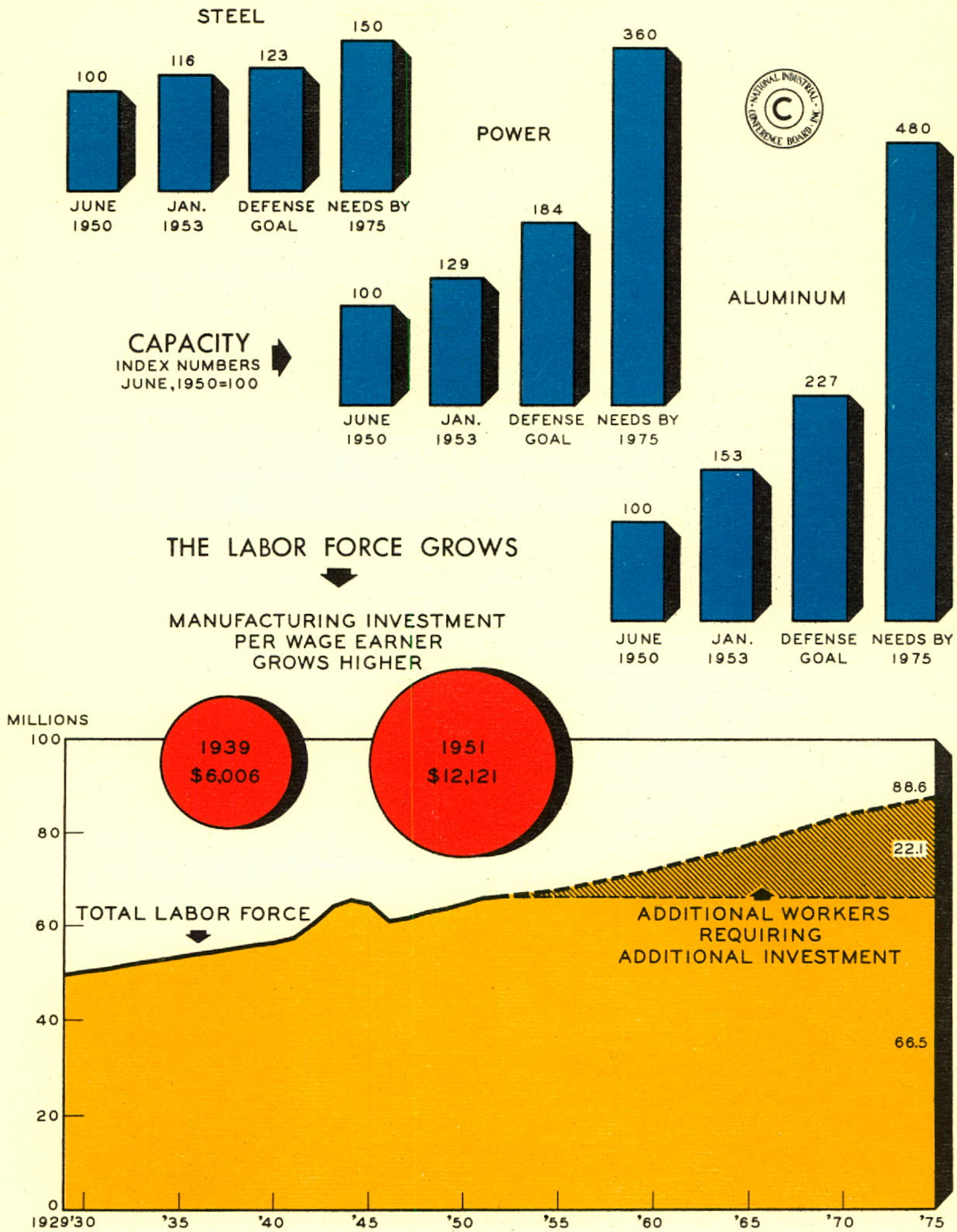
To create productive jobs for these new workers we will need sustained investment of unprecedented amounts. By 1951, an investment of about $12,000 was required for every manufacturing worker. This was already more than double prewar requirements. The projected increase in the labor force by 1975, according to one rough estimate, will call for the investment of an additional $50 billion in manufacturing alone, based on 1951 investment-worker ratios.

Future capacity requirements for which investment funds must be forthcoming were recently indicated in the Paley Report. The steel industry's output, the Report estimated, will be 50% greater by 1975. Electric power requirements will be fully three and one half times the capacity at mid-century, while for aluminum the need will be even greater. The long-term growth of all industry has averaged about 3% annually.

Retained profits and equity capital have been two traditional sources of funds for expansion in the past. Over the past two years retained earnings have been cut sharply. The flow of risk capital into industry has likewise been restrained by double taxation of dividends and steeply progressive income taxes. These policies strike deep at the savings of the higher-income groups which in the past have provided the bulk of equity capital. A good part of the postwar expansion was financed through bonded debt, so that today it is a higher percentage of total corporate liabilities (including capital) than it was in 1929. The voluntary flow of private capital to provide the funds for the industrial expansion required in the years ahead may not be forthcoming unless profit prospects are regarded as attractive and unless the economic environment and tax treatment become more favorable to investors.

Sources: Bureau of the Census; Bureau of Labor Statistics; President's Materials Policy Commission; Quarterly Reports of the Director of Defense Mobilization; The Conference Board.

THE JOB AHEAD FOR PROFITS



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To perform this function the Board maintains a large staff engaged in continuous research in economics, statistics and management technique; it operates a widely used public information bureau; it provides specific information services for individuals, organizations and business concerns; it conducts periodic conferences of business executives and others for discussion of economic and management problems; and it issues many publications presenting the results of its investigations and conferences.

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* *Out of print.*

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