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Accountants and Economics with Reference to the Business Cycle*

By WESLEY C. MITCHELL

One of the little noticed developments of the industrial revolution has been the rise of new professions, which render service not to persons but to business enterprises. The number of these business professions is already considerable and it will doubtless grow still larger; for the differentiation of new specialties within old occupations is merely one phase of that process of dividing labor which accompanies the growth and application of science. But there are only four of the new professions which need concern us to-night, accountancy and three others which are in some measure its competitors for the work of advising business men.

Of these four professions accountancy itself and engineering are the best established. Business statisticians are rapidly making a place for themselves, however, and advertising men are acquiring professional standards and technique. Each of the four has a central field within which it is undisputed master; but no one of the four has definite outer boundaries. On the contrary there is much overlapping around the edges. For example, an enterprising advertising agency called in by a manufacturing concern to advise about a sales campaign is likely to give its client's affairs a thorough examination, and to make suggestions which might have come from a production engineer, an accountant or a statistician. Again, when a specialist is called in to organize a statistical department for the benefit of a corporation's executives, he is likely to recommend changes which affect the engineering, accounting, or advertising policy of the firm.

*An address to the New York State Society of Certified Public Accountants, delivered at New York, January 8, 1923.

I shall not elaborate examples of such overlapping of the fields covered by the various professions serving business, because as practising accountants you must know many more instances than I do. My point is this: There are considerable strips of "no-man's land" between the territory in which the accountants are firmly entrenched and the other territories which are firmly held by the engineers, the statisticians, or the advertisers, and accountants must have some policy regarding the occupation of this "no-man's land" around their territory.

Perhaps the best policy for your profession is to confine its attention strictly to its own technical work, and let the other professions in question fight for their shares of the "no-man's land." You may prefer to content yourselves with making the most perfect records of what business has done in the past, and let other people make all the constructive suggestions about what businesses should do in the future—apart from advice about how to keep their books. That may, I repeat, be your wisest policy as a profession. But as an economist I hope you will prefer to take a more aggressive line. For I think that the accountant is in some ways better fitted to give constructive advice to business men than the engineer, the statistician, or the advertising man.

An economist is not interested in business as an organization for making money. His interest lies rather in the industrial process of making and distributing the kind of goods and services which meet our needs. His viewpoint is that of the consumer who wants an abundant supply of wholesome goods, at moderate prices, convenient of access. Hence the economist has peculiar interest in the work of engineers, for they are the profession which plans and supervises the actual processes of extracting raw materials, of fabricating and transporting them. And it is on the ingenuity of scientific men and engineers that rest our chief hopes for further conquests over nature and for further increases in production.

But the economist knows that in modern society the scope of the engineer's activities depends upon the business man. Improvements in production, however admirable from an engineering viewpoint, will not be adopted unless the business men see a profit in changing their methods. No matter how well equipped a factory and how well organized its personnel, the men and machines will stand idle unless the business executives can see a market for their wares. As the great nations of the world are organized now, the business man is the man in authority, and the engineer is his servant.

In many ways this situation is unfortunate for society. It means that our supply of food, clothing, fuel, housing, transportation and the like is frequently disturbed by purely technical considerations of profit. We want coal this winter. We have coal mines in superabundance. The miners would like to do more work each year than they are offered. We have an adequate supply of mining engineers and perhaps the most efficient railways in the world. We have invested hundreds of millions of dollars in opening and equipping our mines, and as investors we want dividends on our securities. But this vital industry has not done the work which as consumers we needed to have done and which the miners, engineers and investors were eager to do, because for several months the operators thought they could not make profits at the prices they were asked to pay for labor. That profit margin was the crucial problem. And because of this technical problem of profits, thousands of us are chilly this winter and doubtless a good many of us will die prematurely.

I am not saying that the system of economic organization which makes profit margins the crucial factor in determining what we shall get to eat, wear and burn is vicious. On the contrary, I think it is the best system of economic organization which the wit of man has so far devised. But I am saying that this system has serious shortcomings, and that if we have courage and initiative we should set ourselves to remedy the shortcomings as rapidly as possible.

To effect improvements we must work through the controlling factor, the business man. Many business men see as clearly as anybody the points at which their methods need improvements; many regard themselves primarily as servants of the common welfare and do the very best they can to supply the community with wholesome products at reasonable prices. But not all business men take this attitude. And those who do take it need a great deal of skilled assistance to do their jobs aright. As a class they have not attained a high level of professional knowledge. Perhaps the great variety of tasks which they have to perform or to supervise will always prevent any large proportion of business executives from becoming professional men in their attitude of mind or in their accomplishments. It is almost certain that they will rely even more in the future than they have relied in the past upon the advice of men highly trained in various specialties.

To make a money-making form of organization serve society more efficiently, then, we must rely quite as much on the professions which serve business as on the business men themselves. And each of these business professions has its part to play in the game—accountants, engineers, advertisers, statisticians, and others. But your profession has an especially important part to play in guiding business men, because you are especially concerned with ascertaining the facts that are of crucial importance in guiding their decisions—the facts relative to profits.

If your policy as a profession is merely to draw up good statements about past results you will continue to render a modest but valuable service to business and through business to the public. But if you venture upon a somewhat more constructive policy by aiding business men with your counsel, you may play a much larger role in the world of affairs and in the life of the community. For by your intimate knowledge of business details, by your prestige with business men, you stand a chance of contributing as much to the orderly conduct of business, to the reduction of waste and the increase of efficiency, as any other profession can contribute. Your position is a strategic one, and it lies with you to decide whether or not to make it larger and stronger. Once more let me say as an economist that I hope you will pursue an aggressive course, that you will occupy a goodly share of the "no-man's land" between your present stronghold and the strongholds of the engineers, statisticians and advertisers, and that above all you will use your growing power to make the business mechanism render better service to the community.

To accomplish much for the benefit of the community, however, accountants must make their services profitable to business men. My chief purpose this evening is to suggest one way in which you can make your work more valuable to business enterprises and at the same time more beneficial to the common welfare. The suggestion is one which I submit with diffidence, because I do not know enough about your work and your relations with your clients to be sure of its feasibility. But if you are minded as a profession to develop a constructive policy, it is a suggesion which merits at least one evening's attention.

Every few years the United States has a business crisis. That crisis is followed by a period of business depression. The depression yields at last to a revival, and the revival usually grows into a period of prosperity. But the prosperous period never lasts more than three or four years at the most, and it ends in a new crisis.

This round of events is what is called a business cycle. Such cycles have been running their course in this country ever since the eighteen-twenties at least. And they are not peculiar to the United States. On the contrary, they occur in much the same fashion in every country which has attained a highly developed commercial organization—in England, France, Holland, Belgium, Germany, Austria, Italy, the Scandinavian countries, in Canada, Argentina, Australia, South Africa and Japan.

From the viewpoint of society booms are wasteful, crises are costly, and depressions are periods of wide-spread suffering. A recent attempt has been made to measure what we lose by the business cycle. Approximate estimates can be based both on figures concerning the physical output of staple commodities and on figures showing the size of the national income. Both methods yield about the same results. They indicate that the worst years in the United States fall some 15 to 20 per cent. behind our best years in the amount of wealth produced and in the amount of income received. The worst years also fall some 8 to 12 per cent. behind moderately good years. The values represented by these percentages run of course in the billions of dollars. Even so they take account neither of the wastes which mount so high in "booms," nor of the disorganization produced by crises, nor of the deterioration and unrest bred by unemployment in depressions. The business cycle, indeed, is one of the outstanding defects of economic organization based upon money-making. How to control this cycle is one of the great world problems.

What is true from the public viewpoint is in this case true also from the viewpoint of private business. There is no need to remind a group of accountants of the costly mistakes into which individual business men are betrayed by "booms," of the losses which they suffer in crises nor of the further losses and discouragement produced by depressions. Of course the story has its other side. Some concerns which are managed with uncommon skill and some which enjoy especial good fortune escape the dangers, avoid the losses, or even increase their gains while the vast majority are suffering. But such cases are rather rare exceptions. It is no less a problem of private business than a problem of public economy to achieve mastery over the business cycle.

This is a problem which the country at large and the business public in particular are just beginning to grasp. For three or four generations we accepted business panics and depressions as visitations of providence, or charged them up as retribution for the sins of statesmen of the other party, or attributed them to the mistakes of foolish speculators. Between panics we forgot about the whole subject and acted as if we expected good times, once they had returned, to last forever. Of late however we have become wiser. Instead of thinking merely about crises and depressions, we have begun to think about the whole business cycle. Instead of taking the ills as occasional disasters, we have begun to see them as recurrent phenomena to be expected in the future if we go on behaving as we have behaved in the past. Instead of bewailing our fate and blaming each other for what has happened, we have begun to consider how we can prevent similar disasters from happening again.

The lead in this constructive direction of trying to devise preventive measures has been taken by Secretary Hoover. As chairman of the president's conference on unemployment which met in September, 1921, he asked that body first to decide on plans for meeting the emergency which threatened that winter, and second to authorize the appointment of a committee to consider how similar emergencies could be prevented from recurring in the future. The conference on unemployment followed the chairman's advice. Mr. Hoover appointed a business cycle committee including two eminent business men, a lawyer who was then president of the Chamber of Commerce of the United States, an active social worker of long experience in making investigations and one of the vice-presidents of the American Federation of Labor. This committee asked the national bureau of economic research to prepare for its use a report upon the character of business cycles, the extent of cyclical unemployment, and the leading suggestions for investigating the violence of the swings in business activity. The report has been completed, the business cycle committee has nearly finished the draft of its recommendations, and within perhaps a month the whole matter will be put before the public.

Meanwhile the business men of the country have begun to talk about business cycles to an extent never before known. Most of the newspapers which appeal to the business public have articles on the business outlook which are based tacitly or explicitly on the idea that business moves in cycles. The numerous agencies engaged in preparing forecasts have made large gains in circulation. And all this interest will doubtless be heightened within a month or two when the business cycle committee comes out with its recommendations and report.

I do not wish to decry or belittle all this sudden interest in the business cycle and all the talk about how to control it in the future. On the contrary I think the movement salutary, I have done what I could to promote it, and I shall devote more effort to it in the future. But into almost every idea taken over by the general public from the discussion of specialists, there creep misunderstandings and exaggerations. Certainly that is happening now in popular discussions of business cycles. Many a business man is developing the precipitate zeal of a new convert and talking about business cycles as if they came around with the regularity of presidential elections. Not a few forecasting agencies are publishing prophecies as if they had the certainty of history. Many a would-be reformer is pushing his cure for crises and depressions as if it were a social panacea. There is, indeed, more need than ever before of clear and sober thinking on the subject, by men of trained minds, conversant with actual business experience.

Need I say that the accountants constitute such a group and that the possession of these qualities confers upon them an obligation to take an active share in the effort to control the business cycle? There are, it seems to me, two distinct services which you can render better than any other group of men, and render with profit to yourselves, your clients and to the whole community. The first service is to complete our knowledge of the business cycle on a side about which we have very few data. What we know about the cycle at present rests primarily upon a foundation of statistics. These statistics relate to business transactions but to business transactions taken in vast aggregates. We have, for instance, index numbers of wholesale prices, retail prices, stock prices, bond prices, wages, employment, production and the like. We have also aggregates showing the volume of bank clearings, bank loans, bank deposits, exports and imports, stocks of certain commodities, car loadings, new building, security issues, unfilled orders, sales of department stores and mail-order houses, bankruptcies and so on. These statistical series are of inestimable value. We need more of them but we must improve their quality. We must get them published more promptly and we must condense their meaning by more skilful analysis. But when we have learned all we can from this type of investigation, we shall still know little about a matter of primary importance, that is, just how prosperity, crisis, depression and revival affect the inner workings of the business enterprise. We are in the position of knowing a good deal about the forest, but very little about the individual trees. Indeed we can scarcely see the trees at all; the statistics show us only the forest.

How does a depression affect the collections of a business enterprise? How much does it reduce the working capital required? What proportion of loans is "frozen" in the successive phases of the cycle? How are losses really met? Is the physical condition of a manufacturing plant allowed to run down in active times? Is the depreciation account used to carry enlarged stocks of raw materials and finished products? How low do cancelations of orders drop in depressions when buying is from hand to mouth? How early in the revival do they begin to mount? When do they reach their peak and how high is it? Do total pay-roll disbursements grow more slowly than gross receipts during "booms"? How do business enterprises use funds not required as working capital when times are very dull? Do they commonly carry out or even plan extensions and betterments before revival has made considerable headway? Do they write up and write down their fixed capital to balance unusual losses and gains? How far do business men take the business cycle into account in formulating their plans?

These are a few of the questions which students of the business cycle cannot answer with any assurance from their statistical data. They are questions that can be answered only by men who have not only free access to confidential records, but also the training to make these records tell a true story. Accountants can do this kind of work even better than the business men whose accounts they inspect. I fear that our knowledge will remain in its present imperfect state unless and until the accountants interest themselves in the business cycle, and study the materials they handle from this viewpoint.

If and when you do undertake work of this sort, you will become far more valuable advisors to your clients. That is the second service which it seems to me you are in a peculiarly advantageous position to render. Despite all their talk about the cycle, business men as a class do not understand it clearly, and they are peculiarly susceptible to an emotional bias of elation and discouragement which leads them into error. Accountants who deal with clients in several or many industries can get a better view of the business situation as a whole than most business men; they are more accustomed to using figures; they have a more objective and detached view of a client's affairs and prospects than he can gain by himself. All this should make the accountant who has studied the business cycle an exceedingly helpful advisor on problems of business policy.

If you undertake service of this kind and equip yourself properly, you should not only be able to guard your clients against making mistakes, but also to show them how to take advantage of many opportunities for profit which the business cycle offers. When to buy freely and when to go slow, when to advertise and when not, when to build extensions and when to conserve assets are problems which can be solved with a much better record of successes by a man who has trained himself to look at the future in the light of the past than by a man whose vision is colored by the haze of the business situation of the moment.

Finally, by helping the business public to take advantage of the opportunities for profit offered by the business cycle and to avoid the losses which it threatens, you will also be serving the public. For when we can all foresee the coming changes in the condition of business these changes are likely to be modified. To give an extreme example: As the close of the civil war came on, the business community expected a great crisis. Business was being done on the basis of irredeemable greenbacks; these greenbacks were notes of the federal government; their value would rise if the confederates laid down their arms; an increase in the value of the currency would produce a fall of prices, and this fall of prices would affect the position of every business concern in the country. This logic was sound and it was clear. So, as one business man put it, every business man set his house in order to be ready for a panic. Everything happened as expected—except the panic. From January, 1865, to July, when the last confederate force had surrendered, prices fell more rapidly than they had ever fallen before. Even in 1920-21 it would be hard to find any six months in which the decline was so precipitous. But since every business house was expecting just that contingency, there were almost no failures. When you read the newspapers of the day, you find few references to credit strains of any kind, few complaints of shrinking inventories, few notices of canceled orders—indeed almost none of the developments which made 1920 and 1921 such anxious years to all, such disastrous years to many.

I do not suggest that such success in foreseeing the future as circumstances made easy at the end of the civil war is likely soon to become the general rule. Nor do I suggest that prevision would always mean prevention. Indeed I think we have a long way to go before we can gain the insight which will be necessary to accomplish more than a mitigation of such disastrous experiences as we have recently suffered. But every business concern which does manage to forecast correctly the course of events which affects its operations, and to shape its plans accordingly will benefit, not only its proprietors and employes, but also every other business concern from which it buys or borrows and every concern to which it sells or lends. And it certainly benefits the general public so far as it keeps its men at work and steadies the supply of goods which it produces for consumers. If your profession can contribute to this result you will be aiding to start a process which should grow at a cumulative rate, once it gets under way.

Let me say again that this suggestion is offered in a tentative spirit for your consideration. Economists have a great deal to learn from accountants, and my eagerness to have you take up the study of business cycles may be colored by my desire to profit by what you can discover better than any other body of men. There may be reasons why you prefer not to assume the responsibility of offering constructive advice to your clients outside of your own technical field. Even so, everyone must recognize the indispensable value of your services to business and through business to the community. But if you do think it best to confine yourselves to accounting pure and simple, you must be prepared to see other professions—notably the engineers, statisticians and advertisers—winning positions of which you might occupy a share. And the rest of us must expect that progress toward stabilizing employment and production will be less rapid than it might be if you were more aggressive.