L63-20

Copy No. 1 of 2

THE INTERPRETATION OF ECONOMIC INDICATORS

Professor Martin R. Gainsbrugh

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Reviewed by: Colonel J. H. M. Smith, 10 December 1962

INDUSTRIAL COLLEGE OF THE ARMED FORCES

WASHINGTON, D. C.

1962 — 1963

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11 September 1962

CONTENTS

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INDUSTRIAL COLLEGE OF THE ARMED FORCES

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DR. POPPE: General Stoughton, Gentlemen:

This morning's lecture is very important. It deals with the economic statistics prepared by the President's Council of Economic Advisers. These statistics are extensively used by the President's advisers, the Joint Economic Committee, Congress, and the business community in general.

We have requested Professor Gainsbrugh, Vice President and Chief Economist of the National Industrial Conference Board and a member of the Board of Advisers of the Industrial College, to bring these cold figures to life and to analyze and interpret them for us in a meaningful way.

It is my pleasure to welcome Professor Gainsbrugh for his tenth presentation to the College and to introduce him to the Class of 1963.

Professor Gainsbrugh.

PROFESSOR GAINSBRUGH: That was a good introduction.

It is my purpose this morning to explore with you our system of economic intelligence. As the results of that system are contained in the document that has been placed before you, I suggest you keep it handy with a pen or pencil, so that we can underscore some of the pertinent statistics and add some of the later figures that have become available since this document was printed.

We will use it to explore the three questions that are involved in appraising the outlook. Notice I said three questions, and not one. This document is set up to throw light on all three questions.

The first question involved in the outlook, whether it be the outlook for the Nation, for an individual enterprise, or for a community, is the question the President of the United States was exploring with his people not so long ago. That question is the determination of our current position. On the basis of the system of economic intelligence that we have set up, what is the current position of the economy? Specifically, question No. 1 is: Where are we? What is the state of business, as best it can be determined, using our system of statistical indicators to help us answer that question on the determination of our current position?

If you will look at the Table of Contents of this document, you will find therein quite a few economic indicators that are primarily of importance as measures of current position. We will explore some of these measures of current position. You might check off on your outline about five of these thermometers as distinct from the second battery of indicators that we will be exploring, namely, barometers.

Here we are exploring current position . Some of the best measures of current position were those that our President was using. We, too, will be looking at the same body of data, and in some instances perhaps even later data than the President had at his command.

One such indicator is the index of industrial production. This is shown as being on page 14. At a later time we will turn to page 14. But at the moment, mark the letter T next to the index of industrial production, signifying that as one of the thermometers, worthy of your constant and regular study.

Next is the body of data that you will grow painfully familiar with before you have completed your course here--gross national product. It is shown as being on page 1 here--gross national product or gross national expenditure. This is the second thermometer we will be exploring.

The third is the status of the labor force, shown as being on page 9--employment and unemployment of our people.

The fourth--and here I come close to your own pocketbook nerve—personal income, is shown as being on page 3—the income of our people.

And, last, but by no means least, is sales--trade sales and inventories, shown as being down around page 19--and particularly retail trade.

Those are five good measures of current position. If time permits we may get around to the sixth, and that is the price position of the economy, as shown either by the consumer price index or by the wholesale price index. These are measures that economists over the years have set up, placed on a current basis, and that we use increasingly to determine our current position, to answer our first question about the shape of the economy.

The second series of questions that we will be exploring extensively relate to the factors that have shaped our current position. Why are we where we are? The first question is: Where are we? The second question we will be exploring is: Why are we where we are? How did we get there? If that sounds somewhat academic, let me put it in more homespun fashion. What are the elements of strength in our current position? What are the elements of weakness? Why have we grown concerned, as we have, about the shape of the economy currently?

As we move from one measure to another, we will be using those measures not only to determine our current position but to throw light upon why we reached that particular position.

And last, but by no means least, are the indicators that we have been developing of future position. We call some of these the foreshadowing statistics, bodies of data which, when organized, throw light upon the future operations of the economy--foreshadowing statistics. Another graphic name for this series is leading indicators. I prefer to refer to them as barometers, telling us something not only about current but about prospective position. On your sheet again you might check off some of the barometers, using the letter B for this particular designation, as distinct from the letter T for the thermometers.

I suspect that your individual interests are more in the B's than in the T's, but we have far fewer B's than we have T's, and some of those B's can be as misleading at times as they are leading indicators.

One of those barometers is corporate profits, on page 6. Put the letter B after corporate profits. Another is private investment in new plant and equipment, on page 8. That's another B. Still a third B, and the one that has the value that you can usually secure these data for your own local community as well as nationally, is perhaps one of the most sensitive of statistics, of all of the thousands of series that we have--weekly hours of work, on page 12.

Once a business man or a manufacturer starts having some degree of hesitancy about his future order position, he will do his utmost to avoid paying premium overtime, and that will in turn be reflected in the hours of work figures.

Another is housing starts, or heavy engineering awards, pages 17 and 18--construction contracts. Another B.

And the fifth and last of the barometers--and by that time we will have more than exhausted the period available to us for this initial review--new orders, one of the earliest forms of foreshadowing statistics, on page 20. This is the type of foreshadowing statistic that you would very quickly develop if you were running your own shop--your order book. You would be constantly comparing your order book with your rate of production. When your orders were coming in faster than your rate of production you would begin to develop a feeling of euphoria, or well-being about your future position. The minute your orders started falling below your rate of production, you would have more and more concern about your future position.

Let's start, then, with one of our first determinants of current position, turning to page 14, our index of industrial production, and let's see where this stands as late as the month of July, and speculate productively a bit about where it may be in the month of August. This is on page 14.

On that page, for purposes of identification, you might post the word, volume. This is a measure of the physical volume--not dollars, no, but volume--output of the Nation's factories. If you look at the headings of the columns you'll see there the word, manufacturing, in the Nation's factories, the Nation's mines, and the Nation's public utilities--all combined into a single, meaningful figure. We take tons of steel, yards of cloth, gallons of oil, and, weighting them on the basis of their relative economic importance, we combine all of this output into one, single, meaningful figure. Catalog immediately in your minds the figure for July that provided such comfort to the President when he reported it. The figure for July 1962 indicated that as late as that particular month that very vital measure was still rising. As you see, the figure was 118.7 as compared with 117.9. Just so that this measure is crystal clear in your minds, what that means is that in the month of July 1962 we were turning out 18.7 percent more in physical volume than we were in the base period 1957, and 1957 was a good year in and of itself.

That's the good news. Now for some of the disconcerting aspects of this particular measure insofar as they are revealed. You might post on your sheet that at the trough of the last cycle, or when this recovery began in February of 1961, that measure stood at 102.1. The reason I am commending that figure to your attention is so that we can contrast performance in the opening phases of this recovery with current performance.

Against the figure that I have given you, note the December 1961 figure. In the first 10 months of this recovery that index rose by over 12 points. Am I right? It rose 12.7. In the first seven months of this year, in contrast, that index rose but by 4 points. There was less momentum with each passing month of this recovery, a sluggish recovery, ever since we moved into 1962. It is still rising, but with far less zip than previous postwar recoveries. There are some guesses hazarded that the August figure may be no higher than the July figure when it is released.

So I make two points, then, about this particular measure--one, that it was still rising in the month of July, but, two, that the rates of gain have been lower than in previous postwar recoveries, and far slower than in the first 10 months of this recovery.

Before we leave this page we might make a third point. Where is this sluggishness most pronounced? If you look at this page 1 a conclusion begins to emerge, and you will hear me underscore it time and time again. This recovery has been plagued by sluggish capital goods activity ever since it began--sluggish capital goods activity.

Notice that we break this measure into its components. In about the third column there is a group of statistics, labeled, durable production--production of machinery, production of capital goods, of goods used in the production of more goods. That particular measure, as late as July 1962, was only 15 percent higher. Do you see it there--115? It was only 15 percent higher than it had been in the year 1957.

In striking contrast thereto, encircle the next figure for soft goods--24.8 percent higher than it had been in the year 1957. Since 1957 the general pattern of the capital goods industry has been less expansionary than all of manufacturing. All of manufacturing, as you see, is up by 19 percent; the capital goods sector, 15 percent; the soft goods sector, 25 percent.

See in striking contrast if you will the production of energy--41 percent--the utilities group--41 percent greater than in the year 1957. Or, notice how we break the series in the second half of the page, into the type of good, as distinct from an industrial classification. There again the same conclusion leaps off the page:

Equipment so vital to our society in maintaining our international competitive position, in offsetting higher wage costs, and in giving us increased productivity, is only 16 percent higher than it had been back in the year 1957. Consumer goods, in contrast--24.5 percent.

If you are puzzled by this, you can find some further detail on page 15. You will see there that the primary metals output was 86 in the month of July as compared with 100 in 1957, turning out less steel, 14 percentage points less, than in the year 1957. Or transportation equipment--and this will come as a surprise to many of you, in the light of the high rate of activity in the automotive industry--the whole transportation-equipment complex is only 13 percent more than in the year 1957.

Contrast to that chemicals, petroleum, and rubber--38 percent.

You see how this particular measure, then, can be used to throw light on current position and can also begin to answer some of the questions as to Why? in addition to answering the question Where?.

Well, we shift from that to the second thermometer that I suggested we explore. This one is the gross national product, on page 1. Perhaps in many ways this is the most sought-after single statistic by business men of all of the statistics put out by our Federal Government. Page 1, gross national product--this is the dollar figure, instead of the volume figure. It is the most impressive dollar figure that we have. It embraces all forms of activity in our society, not only manufacturing, mining, and public utilities, but construction, agriculture--every form of activity gets into this particular measure. As you will learn, it is the total dollar value of the Nation's output of goods and services--market value.

What this measure tells you on page 1, second column, total gross national product, is that as late as the second quarter of 1962 the total national output of goods and services was still rising. On an annual basis we were turning goods out in the second quarter of 1962 at an annual rate of $552 billion. Do you see the figure there? This is the second quarter, total gross national product.

In the first quarter the comparable rate was $545 billion. This is an important measure, not only because it gives us the figure as to total aggregate economic activity but note the composition of such activity. This is one of the greatest economic discoveries of our time, made by the late Lord Keynes, who said that once a good has entered the market place there are only four things that can happen to it--we eat it up or wear it out for our own individual satisfaction--personal consumption, expenditures. I suggest you put a (1) over that one. That's one thing that can happen to a good. That in our society is the largest single outlet for the goods we produce--the consumer, the individual. In a sense, that's the purpose of our society--the aggrandizement of the individual in every way possible, including providing him with more goods and services.

We can eat it up or wear it out for our own satisfaction--that's one. Use No. 2 is that business can take it off the market place--that column labeled, gross private domestic investment.

Third, foreign countries can take our goods off our market place or send goods to our market place. File away in your memory machine the fact that as late as the second quarter of 1962 we still had a positive balance of $3.7 billion in terms of the goods that were shipped abroad as contrasted with the goods that came to our market place. We had a net balance of goods and services of $3.7 billion.

Individuals can take goods off the market place, business can take goods off the market place, foreign countries can take goods off the market place, and last, but by no means least, the world's biggest business, the Government, acting as our intermediary, acting in our behalf, can take goods off the market place. That's the column labeled Government purchase of goods and services.

What this measure, then, enables business men to do quarter by quarter is to observe, first, the rate at which goods are entering the market place. That's the total gross national product. That's of intereat to all business men. But even of greater interest to the business men is: Who on earth is chewing up $552 billion worth of goods and services in our society? Where is the demand coming from to equal the supply? Unless the demand equals the supply we are in trouble.

Here again we get insight into where are the elements of strength and where are the elements of weakness. Notice under personal consumption expenditures that it isn't weakness in consumption that is causing concern about our current position. Your wife and mine were spending even more freely in the second quarter than in the first quarter, and they have ever since this recovery began. Look back to the trough in the first quarter of 1961 and see the pattern of consumption emerge, from $330 billion to $355 billion, and still going up.

The sluggishness becomes more and more apparent again in the same area of concern that we noted earlier--business investment. Fourth quarter of 1961, a $76 billion annual rate; first quarter of 1962, a $75.9 billion annual rate; second quarter, a $77.4 billion annual rate.

That's the inert, the semi-active, component of this particular recovery. Foreign demand is holding up right well through the second quarter and continuing into the third quarter.

Lastly, it has not been failure of government spending that has retarded this recovery, if there's any question about that in your minds. Notice how much, from the trough in the recovery in the first quarter of 1961, $104.8 billion, to $116 billion. That's the increase in demand for goods and services that has arisen in the governmental sector. Some of my colleagues refer to this as the skimp sector--the one that we hold down.

It's from this set of figures that we get the data on the cost of national defense. You see it there. May I commend to your attention another figure that is greater than the total cost of defense-- state and local expenditures for goods and services are already in excess of our national defense expenditures. So much of our concern is in the direction of the burden of defense, with very little recognition of how high that state and local expenditure has come and the extent to which it has outstripped economic growth over the past decade. Those expenditures at one time, following World War II, in the first postwar decade, were around, as I remember it, 6.5 or 7 percent of the gross national product. Now they are up to around 10 percent.

The basic point I have made here, the same as the point I made earlier--growth is still apparent in the economy through the second quarter of 1962--less growth with each passing quarter. It's evident again in the second-quarter figures. And the most sluggish sector of that growth again is found to be the capital goods area.

We move from that to the third measure of current position. This is on page 9--employment--nonemployment. Again, now that you have grown familier with procedures, you will find that in the month of July the figures, particularly for employment, make for good reading. The latest figure shown here is 67.7 million people at work in civilian pursuits. Even more important in many ways, the unemployment figure--encircle, if you like, the figure for 3.8 million unemployed in the month of July. Contrast that with the 4.9 million unemployed in July of 1961. At the trough of the cycle we had 5 million people unemployed. We have reduced the number of unemployed, from the 5 million that it was at the trough, to 3.8 million. And for the seasonally adjusted unemployment rate, if you take the number of unemployed and divide it by the labor force you will get the rate of unemployment seasonally corrected. It is shown for the month of July as you see it there as 5.3 percent. It had been as high--look at the top of the column--as 6.9 percent. We have markedly reduced the number of unemployed. We have raised the level of employment.

These are all positives. Now, on the negative side, post, if you like, the figure for August, just released. Seasonally adjusted, the unemployment rate is 5.8 percent. It has moved up again. It's too high for this state of the recovery. This has been a sluggish recovery in terms of the employment that it has generated. Our unemployment rate is higher than in any previous recovery, with 18 months of recovery elapsed. It's a sluggish response of the economy so far as employment is concerned. Again, if you look at the figures on page 11 you will see where the sluggishness is most pronounced--the same old problem--in manufacturing, back in

1956, we had over 17.25 million people at work; in manufacturing if we had the 1953 figures it would be 17.5 million. There is a corresponding figure today, with a far higher output. Remember, I demonstrated to you initially that in 1957 there was a figure of only 16.9 million.

Then, driving the point home, how many workers in durable goods, manufacturing? Currently 9.5 million, with 9.8 million in 1956, and over 10 million in 1953, in the durable goods employment sector.

In contrast with that, encircle, if you like, the gratifying figures for nonmanufacturing employment, particularly since this is private in character--29.5 million people at work in nonmanufacturing, as compared with 28 million back around 1956.

Remember President Kennedy's Committee studied the employment-unemployment statistics. We have spent six months at it, and we have just submitted our report to the President. It will be off the press shortly. One of our major findings relates to this particular phenomenon. The shrinkage that has taken place in job opportunities for the blue collar workers and the marked growth in employment opportunities in the service sectors--the white collar as distinct from the blue collar--is apparent. But in all too many instances the skill requirements in the expanding service sectors of our economy are different from the job training the individual has had in manufacturing and elsewhere. We are not getting a happy blend of skill requirements on the part of openings and skills of the job applicants, so much so that the unemployment rate has grown stickier with each passing peak of the business cycle.

We say in our report--and this is no secret, it's readily available data, so I am not scooping the President's report--that at the peak of the cycle in 1953 we had 3.5 percent of our people unemployed--that's at the peak. We call this frictional unemployment, or close thereto--people moving from one job to another in a flexible society such as ours, usually from one job to a better one. At the peak of the cycle in July 1957 we had 4.2 percent of our people unemployed. Notice the progression, from 3.5 percent at the peak of the cycle in 1953 to 4.2 percent at the peak of the cycle in 1957 to 5.1 percent at the peak of the cycle in May of 1960, and now in August of 1962, with peak output, peak gross national product, peak industrial production, we have 5.8 percent of our people unemployed. Unemployment is growing stickier with each passing peak of the business cycle, with less employment generated in this recovery than in previous recoveries.

Two more measures of current position and I will be moving on to the prospective position. On page 3--if you have more people employed than ever before at the highest wage rates in the Nation's history, it is not surprising, as shown on page 3, that we have the highest levels of personal income ever recorded by man, and that this increase in income was still going on as late as July of 1962. That's the figure shown in the first column--total personal income.

While you're at it, may I commend for more intensive study at your leisure the figures relating to the laborer's part of this income, in the next column, the collom labeled, labor income. From 1953 to the present just see what has happened to that flow of income. It used to be $200 billion back in 1953. It's $310 billion today. If you look at the figures on page 2 you'll get a longer historic perspective. It used to be $140 billion back in 1949. It's $322 billion today. I am stressing this because of the Marxian thesis of the exploitation of the proletariat that would characterize a capitalistic system. Let no one tell you that that is a characteristic of our society. More and more of the Nation's income has been channeled into labor compensation. It used to be as low as 60 percent of the Nation's income. Today it is 70 percent and is still rising. And it is not weakness in the flow of income to labor that has been, in my judgment, restraining economic growth.

Another column on page 3 that's worthy of your attention is the one labeled transfer payments--the increasing extent to which income is being paid by government to our people, not necessarily for a contribution to current production, to use a semantic phrase very carefully. One of the outstanding features of this table that you will discover at some later period of time is the decreasing share of the Nation's income flowing to the owners of capital, to the savers, to the risk-takers in the form of dividends, in the form of interest, in the form of rents. In my judgment there is a relationship, a nexus, between the sluggish character of capital-goods investment and the diminishing share of the Nation's income that flows to the risk-takers, to the owners of property, to the savers. This may be very closely tied to the inadequate rate of economic growth that has prevailed in our society, particularly after the lush, hyperstimulated, first postwar decade came to a close.

The immediate point I am making is that personal income was still rising as late as July.

The last current indicator at which we will look is the result of this high income, page 19, the retail trade figure. If consumers have high incomes, those high incomes are very quickly translated into the form of high expenditures. As you can see from the figures here, for the month of July retail trade was still doing right nicely in the month of July--19.5, higher than in the month of June, although it held a little bit below the April figure. The August figure has just been released, and there is some disappointment in that the August figure dipped a bit below--19.3, as I remember, seasonally adjusted--the sales for July.

Personal income is still high. Retail trade is good. But notice, there is no zip. It's displaying less growth than it did in the first 10, 12, or 15 months of this recovery.

So much, then, for our look at thermometers and for the help they give us in determining current position. The conclusion, I think, that emerges from this examination, is that we hadn't reached the turning point of the business cycle as late as July and August, that the current indicators of position were still rising. But the corallary that we also observe is that they were growing with less rapidity, that we were losing momentum with each passing month of the business cycle of this recovery.

Then, the final footnote to all of that is that as best sluggishness could be identified it was to be found in the capital-goods sector, and it appeared to be closely related to the flows of income that dictate investment, the flows of income that generate investment. The life blood of this Nation's economy in terms of the contribution made by investment is in that flow. We'll want to take another look at it if time permits.

Let's leave that to the area of more intense interest. The future--having at least diagnosed our current position--what about the future position? This is the increasing area of concern on the part of business economists. The business barometers, ever since this year began, have been suggesting cloudier weather ahead. We want to see what evidence there is in support of their concern. I might tell you that economists are paid to be fulltime worriers, but at times in 1962 we've been worrying on our own time as well as on the boss's time.

Let's look at one of these barometers, perhaps as significant as any I could direct your attention to, and that is the corporate profits, the figure on page 6. Corporate profits were rising, as you can see if you look at the first column on page 6, so much so that by the fourth quarter of 1961 they had reached an annual rate before taxes of $51 billion. As a result of that growth there were rather gratifying projections made on the levels of corporate profits in 1962. One such made by our Treasury Department was that corporate profits in the calendar year 1962 would reach $56 billion. If we are suffering from anything at all in the way of an economic ailment in September of 1962, it is from the excessive expectations that were given our people and American business men by these projections that were made in late December and early January, because, as you can see from the official figures before you, corporate profits were already turning downward in the first quarter of 1962, and at best they were no higher in the second quarter than in the first quarter. As wages rise and prices hold steady, profit margins are being squeezed. They already have been and will continue to be in this calendar year.

This is one barometer that doesn't make for too good reading, because corporate profits and business investment are very intimately related. We have studied the manufacturing appropriations process of the Nation's thousand largest manufacturing corporations quarter by quarter. All you need have happen is shrinkage in profits and profit margins for a quarter or two quarters, and even the growth companies will start slowing down their investment plans for the future. In the second quarter of 1962 the appropriations of the thousand largest manufacturing corporations were cut by one-sixth from the rate at which they had been in the first quarter, in part because of disaffection with the profit state, in part, perhaps, because of the break in equity prices, and in part because of the civil war over steel prices. There have been various reasons. I am simply reporting the net effect.

Look at the after-tax figure. You have heard this argument in various places before. I am not going to repeat all of it for your benefit. See how little growth after taxes there has been in corporate profits from 1950 on, in the face of an increase in the gross national product in excess of $100 billion. There were very sharp increases in national growth over the past decade or more, and little, if any, of that is reflected in the corporate profits-after-taxes figure. I am underscoring for you again the close relationship between profits and investment. In my book corporate profits are not defined as a residual. This is the way they are often treated, as what's left. The question is very often raised: If profits were higher, would investments be higher? If you belong to the school that uses profits as a residual, you might answer that in the negative. In my book I define profits as the catalyst of investment. The companies with the high profits are the companies with the high rates of investment, with the high rates of expansion. Examine this in your own neighborhoods, or look at the profit performance and the investment performance of the automobile industry or the electric-appliance industry, and compare them with the profit performance and the investment performance of the textile industry and some of the other industries characterized by low profits. The life blood of expansion is profits, and we still apply the same high rates of taxation, the same 52 percent corporate tax rate, with the 10 points that we pushed into it to help finance the Korean War. It was put in as an emergency measure but was also put in to restrain a capital-goods boom. That's why 5, at least, of those 10 points were put into the corporate tax rate. We did have a capital-goods boom in the first postwar decade. But I have been pointing out to you how sluggish has been the rate of investment in the last 5 to 7 years. In my judgment, that is closely related to the 52 percent figure.

That's one barometer that does not make for good reading. Now, conceivably this may alter as the figures for the third and the fourth quarters come along. There has been a recognition of the archaic treatment of depreciation that has held back investment in this country. Business is cognizant of that. There is an investment-incentive clause in the new tax bill. Business is cognizant of that. We have been promised tax reform and tax reformulation in 1963. That may stimulate some degree of business investment. But as late as the second quarter of 1962 this barometer was not making for good reading.

The second is on page 8--expenditures for new plant and equipment. I have already commented on this enough so that I can deal summarily with it. We've had less expansion in investment in new plant and equipment, particularly in manufacturing, than in any previous recovery. Our friends in Washington had hoped that as 1962 ran its course this figure would be going up sharply as it had in previous recoveries. But it hasn't. With each passing quarter business men are holding to about the same pattern of investment. The figure for the fourth quarter has just become available. You may want to post it. They expect to invest $38 billion in total at an annual rate, fourth quarter. You see the figure there for the third quarter. Examine those figures intensively for first differences and you will see that, with each passing quarter of 1962, the rate of increase is less rather than greater, and the typical pattern in recovery is to have the first differences rise rather than diminish.

The figure for 1962 for manufacturing has been cut back rather than increased. So this is another barometer that fits into the general pattern that I have been painting for you of sluggish capital-goods industries and the relation of that sluggishness to our system of taxation.

On page 12 is the barometer that I commended to you for ease of determination locally--hours of work. Again you will find the same pattern--peaking early this year and the hours of work coming down to 40.4 in July. That will go up again another tenth in the month of August. Some of you may wonder as to why the work week is this long, since you know that the nominal work week is 40 hours in manufacturing. This is for manufacturing, but it includes overtime. The compulsions of a slow recovery are to reduce the premium pay as the recovery proves disappointing.

I might, before leaving this barometer, direct your attention to page 13, because here, in my judgment, is another one of the factors contributing toward our inadequate rate of economic growth--our extremely high wage costs. One measure of that is the hourly-earnings figure. It's hourly earnings to the employee; it's hourly cost to the employer.

I joined the Conference Board 25 years ago, and I remember what those levels of compensation then were--63 cents an hour was the average hourly earning for the skilled, the semi-skilled, and the unskilled, back then. If you look at page 13 you will see that as late as 1952 it was $1.65 an hour, and then for the month of July of 1962 the figure is $2.39 an hour. Or I direct your attention again to the weekly pay check. How many of you realize that the average pay check in manufacturing--and that is the average of the unskilled, the skilled, and the semi-skilled--was already approaching $100, as compared with the figure of $23.50 back in 1939? The pay check has risen from $23.50 to $100. If you think I am enphasizing the obvious, you can see that this is already surpassed in the hard-goods industry. The average weekly pay check is in excess of $100. The average wage-earner family in the U. S. A., with more than one breadwinner now present in the average family, has $7500 to $10,000 annual income. This is on the income side.

Visualize the cost that goes along with this and the difficulties we have competing in world markets, in which our high wage rates are so sharply in contrast with those elsewhere in the world.

Again, to repeat, here is another barometer that suggests cloudy skies ahead, on page 20, the one series that business men give great weight to--the new order position of the economy. If you study that column--it's away over on the right, the durable goods manufacturer's new orders for durable goods--you'll see the general characteristics of that series ever since this year began--peaking out in the months of January and February, in part because of the threat of the steel strike, and then the order book's getting thinner with each passing month. One gratifying bit of news for the month of July was the improvement in the new-order position in July as compared with June. You see it there. But even that improvement figure was lower than some of the figures for the earlier months of 1962.

So again we are awaiting the new figures for August and September with considerable interest to see what they may be telling us about the shape of business late in 1962 and early in 1963.

The last barometer, but one that in past years I detected was of maximum interest to this audience, is contained on page 30. It is people's capitalism. This has been a series which typically in the past has turned down well before business in general turned down, but which also has turned down frequently in the past without any downturn in general business. So there was considerable debate as to whether this was a typical or atypical performance. That debate is still unresolved, but you will note there--if I need to recall it to you--the sharp break in the second quarter. And I think you also ought to add on your memory book the fact that we have had rather a sustained recovery since that time, which has carried the Dow-Jones index back to at least 600, so that much of the initial shock is beginning to disappear. But again this is a barometer that suggests more difficult times ahead, and I think it has been borne out thus far.

Well, there in the aggregate are some of the measures that I commend to you for intensive study each month as they become available, using this particular document to throw light on the three questions that are involved in the outlook, the first question being: Where are we? I have given you a battery of measures that should be helpful to you in answering that question. The second question is: How did we get where we are? You will be in a far better position to deal with that question after you have had your exposure to our system of national accounts. But I indicated to you this morning how you could use that gross national product for sectors of demand--consumption, investment, net foreign balance, and government--to explore from quarter to quarter changes in demand. And, finally, I indicated the somewhat mechanical approach of using business barometers to throw a bit of light on the future position of the economy.

The business cycle is not unique in American history. We've had business cycles before. We are in the midst ~~of one now~~. We'll have them again. In every recovery in the past we've built stresses and strains in that recovery that ultimately brought it to an end. We have been building stresses and strains in this recovery that will ultimately bring it to an end. I have demonstrated to you one of the greatest single weaknesses that exist in our recovery pattern this time. It's the lack of zip, the lack of drive, in the capital-goods industry. No recovery has been long sustained without rising rates in capital investment.

Barometers make for disappointing reading. Now let me stress a positive in closing. I find less imbalance in this recovery, less excess in this recovery, than in any previous postwar recovery. We've had less resort to consumer credit, less pressure from inflation, less speculative fever. Tick these points off in your minds. These are the things that have typically produced recessions in the past. The greater the imbalances in the recovery the greater the dimensions of the recession and the contraction.

This time I think economists will have to agree that we have built fewer excesses into this recovery than into any previous recovery. This may very well mean that if we do encounter a recession, if we do encounter a recession, the recession pattern may well continue to be in the mold of the mild, shortlived business recessions of the past.

Find some comfort in that. I do. I am concerned, however, about the disappointing rates of economic growth that have characterized our system from 1955 on, and the fact that we haven't yet found a way back to rates of economic growth that will give us lower rates of unemployment, that will permit us to use the human resources as productively in the future as we have in the past.

Perhaps our biggest single economic problem domestically for the balance of the sixties is to increase our rate of economic growth so that the tidal wave of population that will hit the labor force shortly, the postwar baby crop, will continue to be as productive a resource in its generation as past generations have been. The problems of employment creation in the future are giant as compared with the problems of the first quarter of the 1960's. We are going to have 87 million people in our labor force before this decade is up. We have only 75 million now. We have to create netwise 12 million new jobs just to take care of the entrance into the labor force, if, to repeat, our population is to be as productive a resource in our society in the future as it has been ever since this country was founded.

DR. POPPE: Professor Gainsbrugh is ready for your questions.

QUESTION: Sir, in view of the increase in the labor force by 1970 of 12 million people, have you any comments on labor's newest proposal on the 35-hour work week in relation to that?

PROFESSOR GAINSBRUGH: This is one proposed solution that would shorten the work week and thereby employ more people in turning out the same output. That's what it would come to. I should add, if you don't, that when labor proposes to shorten the work week it also proposes to keep the weekly earnings figure unchanged. What this then implies is higher labor costs at a time when we are already plagued with extremely high labor costs relative to the rest of the world.

So that I am not inclined to view that as an ideal solution to our problem of job-creation. My emphasis is upon the creation of an environment that will expand job opportunities and give greater incentives to the risk-takers and to the job-creators, upon an exploration of the economic climate to see what is militating against job creation, and upon working down that particular road rather than down the road of shortening our work week.

Now, over the long period of time we have moved toward the shorter work week. If you examine American history you will see that we have curtailed our work week by about one-half of 1 percent per year. I think it is possible to take a shorter work week of that evolving character in stride without creating pressures upon the wage-cost-price equation. If we are going down the road of a shorter work week, I would view that evolutionary progress toward a shorter work week as far more desirable than a very drastic, sharp alteration in the length of the work week, designed primarily to disguise unemployment. This has been done in the past. It may again be resorted to in the future. But let's recognize it for what it then is. It's a ruse, really, to disguise unemployment, rather than a way to create more jobs.

QUESTION: With our net exports totalling $3.7 billion, why get excited about the high cost of labor?

PROFESSOR GAINSBRUGH: Because our capital movements are far greater than our net exports. If we want to keep on aiding the underdeveloped countries, quartering our troops abroad, and permitting an even greater flow of investment abroad in the future than we have had in the past, we need conceivably an export balance of $5 to $6 billion rather than $3.7 billion. Good as is the figure it isn't good enough in terms of the demands that are being made upon it. As the world leader, I think, viewed against this context, the pattern isn't quite as favorable as the absolute figures would suggest.

Going a bit beyond that, some of that favorable balance is induced by our capital movement. The economic aid we give abroad generates demands for American exports. Private investment abroad generates demand for American exports. If because of balance-of-payments difficulties we at some later period of time find it difficult to finance our capital movements, this in turn would lead to a contraction in our balance-of-trade position. So this is another reason for saying, "Let's, if possible, further improve our competitive posture."

One final point that I would underscore is that our high wage rate can be and has been in the past offset by our technological superiority. This is the way we have been able to maintain our favorable balance-of-trade position. You see how that then meshes in with the emphasis that I placed upon the need to stimulate our capital-goods sector. Unless we do, then we may find our high wage rate increasingly oppressive relative to the competition of the rest of the world.

So that all of this, I think, fits into a general framework of theory similar to that which I have been expounding.

QUESTION: What can we do about stimulating the output per man, say, per hour, per day, in our labor force today? It has steadily decreased over the years.

PROFESSOR GAINSBRUGH: No, I am afraid that you and I don't read the same body of facts. Output per man hour has been rising steadily over the years rather than decreasing.

STUDENT: The rate of rise has decreased.

ORIFESSIR GAINSBRUGH: Even that, I think, would come into question. There has been some evidence that the increase in output per man hour following World War II has been somewhat greater than the increase between World War I and World War II. Nevertheless there is something to be gained through getting greater labor cooperation in this drive toward greater productivity. I think American labor has been more receptive to capital investment and to mechanization, and to automation, than have some of our foreign competitors. This has enabled us to increase output per man hour. I think labor and management relations in the main have worked toward greater productivity in recent years rather than less.

I detect less of the class struggle between labor and management currently than was true in the late thirties and the early forties.

One other factor that I would mention, and it is getting more and more attention from economists, is that investment in education would also contribute markedly toward improving our record of output per man hour. We are going to have greater and greater need for skilled people in this process of job creation, and, hence, if we can get a better mesh between the educational requirements of the future in terms of job skill and the current educational training, our record of output per man hour will be improved in the balance of this decade.

The reason I am stressing that is that I would like to see this problem explored at the grass-roots level. What I am concerned about is that people feel that we will resolve this problem somehow through national efforts. Every community, really, ought to have a program under way to determine what its size of labor force will be by the end of this decade, what job opportunities will arise within the community, what additional jobs will be required within the community, and how such jobs can be created or attracted, also what changes in local regulations or state taxation might contribute toward job creation.

In much this way we resolved the problem of creating jobs for people following World War II. I can remember at the closing stages of World War II, when Leon Henderson and Dick Gilbert and Isadore Lubin were saying that we were faced with the prospect of 15 or 20 million people unemployed when the Government stepped out of the market place, and yet, through the efforts of CED and other groups at the grass roots we expanded business investment, stepped up consumer spending, and held our unemployment to something resembling a peacetime minimum. If only we could begin to recognize that this is a problem almost as acute in terms of its dimentions, a problem that isn't away down the road. The baby crop of 1946 will be entering the labor force in increasing numbers in 1964. I time this by my own "one man's family." We've got three of these at home. The product of 1946 is just entering college. The other two will be coming along shortly. And about half of the high-school graduates in our community--and this is a high-income community--will not be going on to further education. They are knocking on the doors of employers right now.

I am convinced that we will resolve this problem in terms of employment generation. That's a confession of faith. I think we'll find productive pursuits for these youngsters. What is bothering me is under whose auspices. My friends who believe in government creation of employment opportunities have a long agenda for rebuilding our central cities, rebuilding our highways, removing air pollution, desalinization of water. You can go down the list and see things that remain to be done. We have as yet failed to develop an agenda over in the private sector that will even begin to match the agenda of activities that are already being suggested in the public sector.

So I think business men and those who are concerned about further changes in the structure of our society would be well advised to think their way through this problem of job creation and to give it far more attention than it has received thus far, particularly at the local and the grass-roots level.

Now, I have talked all about your question, but I meant to. That was a deeply rooted question.

QUESTION: I wonder why you did not use a chart on page 7, gross private domestic investment, with its several subindices, in preference to expenditures for new plant and equipment, as a barometer.

PROFESSOR GAINSBRUGH: In part, if you look at page 7, the reason why is that home building is included therein, and government intervention in the home-building area is such that perhaps it is no longer the cyclical barometer that it used to be, whereas the table I was using, on plant and equipment, is strictly a producer's capital good. In that sense I think it is a far more important area relative to economic growth than is home building.

Let me put it to you another way. One of the most historic studies ever made was made by Simon Kuznitz of the National Bureau of Economic Research. He has studied capital formation in the U.S.A. for the past century, and from that study he concluded that our rate of savings was inadequate for purposes of achieving the same rates of high economic growth that we had prior to World War II. In part he said that one of the reasons for this is that too much of our savings is now going into "nonproductive" forms of capital formation. Now, that's using the term very carefully. A form of nonproductive capital formation would be home building. It will throw out goods and services to the person who lives in said home, but it will not necessarily increase our ability to turn out goods per man hour at a greater rate in the future than in the past. Capital formation in the way of public buildings may not necessarily contribute as much to expanded output per man hour as investment in machine tools, et cetera. One of his conclusions was that we ought to be giving more thought to the shapes of capital formation in our society as those various types of capital formation are related to economic growth.

It's for that particular reason that I placed my stress on plant and equipment rather than on home building, industrial and commercial construction, and inventories. All of those items are in the gross private domestic investment table on page 7. I would rather choose to view the item on page 7 in another way, as a coincidental indicater, rather than as a leading indicator. The leading indicator is the plant and equipment expectation series.

QUESTION: Professor, in discussing the gross national product you indicated some concern with the state and local government expenditures. Since so much of of these expenses contribute to education and health, and certainly to an improved labor force, especially transportation, which improves business opportunities in general, why are you concerned?

PROFESSOR GAINSBRUGH: I will let you in on a bit of personal background there. I'm as much concerned about the growth of government in our society as I am about any other economic development of the 20th century. Ours was essentially a laissez-faire economy as late as the 20th century. Perhaps 5 percent of our income was generated in government and 5 percent of our employment was generated in government, and 5 percent of our market decisions were influenced by government. Today that figure is closer to 20 or 25 percent than to 5, in part because of the burden of defense. Defense takes a larger toll in our society than it took in the earlier decades of this century.

I recognize that. At one time Jacob Viner, who has a tart tongue, having heard me express my concerns about the growth of government, asked me if I'd be any happier if we took the men out of Army uniform and put them in the uniform of a private corporation, because they would be performing exactly the same function, we would have reduced the government toll, and the burden would still have to be borne by society.

That isn't my area of concern. My area of concern is this—that whether it be periods of peace or of war, periods of inflation or deflation, of recession or of expansion, that curve for governmental cost has been rising faster in the aggregate than the growth of our society. More and more of our people are on governmental payrolls, civilian as well as military. More and more of the goods in our market place are being taken off the market place on the basis of governmental decisions. More and more of the wealth of this society in the 20th century is in the possession of government rather than in the possession of the private sector. The costs of government in the aggregate may now be as much a restraining factor upon the growth of our society as the stimulus of government expenditure was upon our society in the depressed thirties when we needed some additional stimuli.

Basically what I am concerned about is the impact of these changes upon the structure of our society and upon its inherent basic strength. Its inherent basic strength lay in the decisions of the millions of enterprises, the millions of consumers, independent of a central government. Those decisions in the aggregate were stronger and led toward a more efficient society than any other society known to man.

Now, as we increase the scope and dimensions of government, more and more of those decisions are centralized, whether it be within the State or the local or the Federal nucleus. They are no longer being made as independently, obviously, as they were in the first century or more of our expansion.

I am therefore concerned about the longer-run implications of this growth of government. We have moved--there is no question about it--from the free, laissez-faire society we were until the 20th century to the mixed economy today. It is increasingly more and more of a mixed society. What concerns me as I look down the road further is how much more rapid growth in government than in the private sector will there be before we become a government-determined, a goal-oriented society, if you like, rather than a market-oriented society. Ours has been a market-oriented society, in which the investment decisions, the key investment decisions, and the key consumption decisions, were made by the individuals concerned.

We are competing with another society which is goal-oriented, state-oriented, rather than market-oriented, and we are being told in some instances that the goal-oriented society is far more efficient than the market-oriented society. That has not been the record of history, at least up to this point. I am concerned whether changing the shape of the orientation of our society is desirable. At least I think it is a question that we ought to be exploring more and more intensively.

I put that question at one time in a publication, called *How Much Government?* You could read the handwriting on the wall just as clearly as if I were sketching it for you now. It's there. It isn't a mythology. Government has outstripped science and technology, I think, around the world in the 20th century. It's growing more and more rapidly than the output of goods and services.

I think it's a rightful cause for debate and study, if not concern.

QUESTION: It seems to me that business thinks in a negative matter. They are always thinking about the rise of the labor rates and the rise in taxes. What positive thinking can they do to preclude this mirror you have of big government taking over the economy?

PROFESSOR GAINSBRUGH: First let me rebut, if I can, the negative versus the positive. I'll match the aspirations and the models built by the private business economist against anything that the government economist has come forward with. Their expectations for the future are just as glowing as those that have been painted by others. In addition to that, they are betting their hard dollars on that future.

I don't know whether you noticed what happened in the steel industry just 2 or 3 weeks ago, in the face of the overhang of excess capacity in the steel industry. Homer of Bethlehem Steel said, "We will spend for new capital facilities in 1963, already authorized $175 million as compared with $150 million we spent this year." And Roger Blough announced a new steel mill to cost $55 to $60 million, this in the face of the overhang of excess capacity. Both men said, "If we are going to remain competitive in world markets we must have even better facilities in the future than anything we have had in the past."

What holds them back? The restraints that have been imposed upon economic growth, particularly by our depreciation and tax policies. What has industry been doing in the way of developing a better environment? Using the process of public education and public debate leading toward greater and greater enlightenment. This is where we win problems in our society. We win them in the public arena via the process of debate, via the exchanges of points of view, sharpening up each other's intellectual tools.

I think there is emerging a greater and greater recognition of the need for profits in our society, of the functions of profits in our society, and of the relationship between profits, investment, and taxation.

I think this is the way business hopes to achieve its own goals and the national goals, respecting the roles and laws of economics, not resisting change if it is for the better, but not endorsing all change as being good, and raising the level of sophistication of the American public, the American wage-earner, the American labor leader, as well as the American business man, so that the policies that we pursue are more and more in terms of the national interest, yet without changing the basic character of our society, unless the compulsions of time necessitate that change.

DR. POPPE: Professor Gainsbrugh, you have given us an excellent presentation. On behalf of the Commandant, thank you very much, sir.