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The Interpretation of Economic Indicators

Professor Martin R. Gainsbrugh

NOTICE

Reviewed by Col R. W. Bergamyer, USAF on 25 September 1963

INDUSTRIAL COLLEGE OF THE ARMED FORCES

WASHINGTON, D. C.

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12 September 1963

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Reporter--Grace R. O'Toole

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ADMIRAL ROSE: This morning it is my pleasure to introduce a great friend of the College and a member of our Board of Advisers. Also, aside from such pleasant tasks, he is the Vice President and Chief Economist of the National Industrial Conference Board.

We have been fortunate in having him for several years to give a talk similar to this. This morning he will talk to us again on the evaluation of the Economic Indicators.

Dr. Martin R. Gainsbrugh.

PROFESSOR GAINSBRUGH: Good morning. It is awfully good to be back again. I think by this time, Admiral, I have been become almost a two-digit speaker. At least the impact seems to grow cumulatively over the time.

I have three youngsters at home. I will be referring to them from time to time in terms of their economic significance. One of the ways they date their own calendar as to I is by this appearance. With this appearance they know that the summer has come to an end and that I am back in harness .

I am going to be speaking to you about the state of the economy, using the document with which I believe you have all been supplied, Economic Indicators for August 1963. I would suggest that you keep a pen or a pencil handy so that you can post some earlier statistics that I will be supplying for purposes of a long-term perspective, and in a few instances some later statistics that have already emerged, that give us a little bit more insight into our current position.

I have said this to classes in the past. I say it again, that today this is perhaps the most difficult time of the year in which to have an economist speak to you about current and prospective position of the economy. The months of July and August typically are the period of the summer doldrums, and we never know how much significance to read into trends in the months of July and August. It is not until the summer ends and the fall begins that we really get an accurate fix on our economic position, and yet the month of September is the month of budget making in American industry.

So it is a real challenge to the economist to overcome the seasonal deficiencies of the data, and it becomes sufficiently accurate to assure himself tenure, if he happens to be a private economist, with his employer, unlike some of my academic and, may I even add, governmental friends.

For reasons perhaps best known to the authors, there is an index to Economic Indicators. It is on the back page. I suggest you turn to it. We will be using these economic indicators to answer three questions that are involved in the appraisal of the economic scene. I commend all three questions to you. Let's explore the three in the time available to me, using this system of economic intelligence that we have developed as the framework of our analysis. May I add parenthetically that we have the best system of economic intelligence in the world. Good as it is, it isn't good enough, and I will at times be talking about its imperfections. But we have made marked improvement in this flow of economic intelligence to business, to government, to our citizenry, and I think this is in turn improving our ability to deal with the problems of the business cycle.

The three questions we will be exploring are these: The first one: Where are we when the summer ends, on the basis of the readings that can be taken from our economic thermometers? I will be exploring specifically with you about 4 or 5 of those economic thermometers. You might check them off on your Table of Contents as the types of economic thermometers that receive the maximum consideration in the front office of American business. This I say on the basis of 25 years of experience with the type of economic analysis that goes on in the front office of American industry.

Thermometer No. 1--and we will begin with this shortly--is the index of industrial production. So put T on page 16, the index of industrial production, on your index, the Table of Contents. That will be the first thermometer we will explore.

Thermometer No. 2--and by this time you have already become painfully aware of its existence--is the most important economic statistic of our times, gross national product, on page 2. That is the second T.

The third thermometer, determinant of current position, full of not only economic but political significance, is our labor force statistics, on page 10. That's the third T, status of the labor force.

The fourth, of direct personal interest to you, is personal income, on page 4, the flow of income to the American people.

The fifth--and with that I will cease reciting to you what it is we will be talking about--is the battery of price indexes, and particularly our consumer and wholesale prices, pages 26 and 27.

We will use these 5 or 6 measures to explore the first question: Where are we? In that exploration we will be dealing not only with that question but with its corallary or companion question: How did we get where we are? What are the forces which, since February of 1961, have given us 31 months of recovery? Can you identify them? Are they waning? Are they still of an expansionary type?

This, then, is the second question. The first question is: Where are we? The second is: How did we get where we are? Then, the third, and within the limits of our science, and on the basis of the answers to the first two questions we will devote a little attention to the third question: Where do we go from here?

There, then, is the framework of analysis. Where are we? How did we get where we are? Where do we go from here? In connection with the third question, our system of economic intelligence is beginning to provide a whole body of organized data. I have labeled this "foreshadowing statistics," statistics which, when assembled, throw light on the future position of the economy. You are all interested in the future position of the economy and so, on the Table of Contents, I suggest you tick off 4 or 5 business barometers. Previously we will be exploring thermometers and now we will be looking at a few of the business barometers that we are building into our system of economic intelligence.

Barometer No. 1, and I commend this one to you, not only on a national basis but for the insight it will give you in your own local communities, is average hours of work, on page 14. This is one of the most sensitive of business barometers. Any manufacturer who begins to grow uncertain about his future position starts examining that penalty payment for overtime intensively. Watch that figure in the months immediately ahead for such foreshadowing significance as it may have.

Barometer No. 2--and again I think you will see in homespun fashion how barometric this one is--is new order position, on page 22. This is another important barometer. New orders are, in a sense, the woodpile of American industry. All you need to do is look at new order position compared with current rate of production and you get some indication as to future courses of activity in major sectors of American industry.

Barometer No. 3--and extremely important in influencing the investment positions of American industry--corporate profits. This is what makes the mare go in our society, and grow, too, I might add. It's on page 7. Right along with it is the series that we have helped pioneer, and I will be talking about our latest readings from this particular barometer. This is anticipation to spend for new plant and equipment, on page 9.

Last but by no means of least interest to this particular audience, and to other audiences, is the barometer, stock prices, the barometer shown on page 34, and appearing on the front pages of newspapers across the country these days.

Well, so much, then, for the framework of our discussion, drawn from the context of what I regard as one of the most valuable contributions made by the economic fraternity, the development of this monthly bit of information that was originally designed when the Employment Act of 1946 was passed and the Council of Economic Advisers was set up. A few simple charts and statistics were assembled by the Council and sent over to the President of the United States for his inspection. Members of Congress heard of this and asked if they couldn't see these charts and statistics, and so the audience was broadened from the Executive Office to the Congress. As Congress saw the value of this information, it decided to make this a public document. I think it's one of the best buys in the American marketplace for $2.50 per year. Using this document, in a few simple sentences you can read what it is the Council of Economic Advisers is telling the President about any particular measure. You will get from the charts some historic perspective, and if you are a figure filbert you can dig the underlying statistical detail very readily from the statistical data that are assembled here, not only for the current period but in most instances spanning a decade.

Let's turn first to the first thermometer, on page 16, and see what insight it gives us into our current position. Very quickly, for reasons of time, this is a measure that is particularly noteworthy, because it deals with the volume--there is the key word in your document--of output in the Nation's factories--you see the column there labeled "manufacturing"--the Nation's mines, and the Nation's public utilities. We take the production of steel, the yards of cloth, the pounds of paper, the gallons of petroleum and combine this into one single, meaningful figure, called the index of industrial production, and this measure is available monthly.

Very quickly, on page 16, you can discern what has been happening to the economy in 1962 and 1963. Toward the middle of 1962 there was considerable concern about the future course of the economy. You will note from the figures before you that we struck a plateau in this particular measure. It was at 118.3 and that means that in the month of May, 1962, the physical output of the Nation's factories, mines, and public utilities was 18.3 percent higher than the base period, the base period being 1957-59.

For month after month, from July on, there was considerable concern as to the future cyclical position of the American economy. Without being unkind, I might recall for you that in late January and early February some eminent authorities in Washington were taking the position that we needed a massive tax cut as an anti-recessionary measure. You see there the particular warrant for that statement. They were of the belief that this recovery, which was no longer young, was maturing and might conceivably break out of the plateau on the down side.

Well, the good news of the second quarter of 1963 was that we did break out of the plateau. It is evident. But we broke out of it on the up side rather than on the down side. Now, initially, in the months of February and March the members of the jitters axis were inclined to say, "Well, that's simply a temporary upsurge reflecting the build up of steel inventory--participation of difficulties in the steel industry." So we lived with that uncertainty. But note, by May the steel issue was pretty well resolved, and yet, with steel production descending rather than ascending in June and July, the physical volume of output in the Nation's factories, mines, and public utilities continued to rise--so much so that by June and July of 1963 these measures were above the year-end forecast that most conservative business economists had made at the end of calendar year 1962.

Business economists ever since have been busy revising their forecast for the balance of 1963 and early 1964 upward. One conclusion which emerges, then, from this analysis of this particular measure is that a broad, general breakthrough occurred across a wide industrial front in the spring of 1963, and as late as September of 1963 the course of that movement is still upward.

We shift from that to a second thermometer that can be read with even more significance. This is the gross national product measure. You see the degree of priority it is given, and rightfully so, on page 2. It is perhaps, to repeat, the most important single economic statistic of our times and the greatest contribution of the economic fraternity in the past quarter-century. It is a system of national accounts.

Let me highlight this for you in quite another way. No business worth its salt can be run without an operating statement and a balance sheet. Every business man knows this. These are the financial controls that he has over his particular enterprise. Until very recently we lacked both for the U.S.A. You see on page 2 and the pages that follow, the national operating statement, now assembled after years of effort. So that quarter by quarter we can now follow this particular measure and get insight into at what rate we are producing. This is important. But also we can get insight into what is happening to what we are producing. This is what a business man wants to know relative to his own enterprise. This is what we can now deal with on an informed basis relative to our national economy.

There again the same point I was making earlier becomes clearly evident. You might jot down on this page that when this recovery began, back in the first quarter of 1961, the gross national product was $500 billion. See where it stood as of the second quarter of 1963, and note that, despite the uncerties that were prevailing in the second half of 1962, the gross national product was rising in the third quarter and again in the fourth, and continued up throughout the first half of 1963. It's up again in the third quarter of 1963, despite the low levels of output in the steel industry and despite the summer doldrums, so much so that my first guess, my first approximation of the third-quarter figure, when it emerges, is that it will be around #585 billion.

I have just come from the annual meeting of the American Statistical Association where, at the outlook session, we took an immediate consensus of the group. Every man was supplied with a card, a sensitized cars. On it there was a series of questions about the outlook. Each man also had a sensitized pencil. There were blips on the sensitized card, and he had to enter the figure that he thought most likely for the gross national product, for the index of industrial production, year end 1963, mid-year 1964, and end of 1964. We resorted to the democratic process. He couldn't get his lunch unless he completed all the blips on the card. We had 175 people in attendance, and we had 175 cards submitted. The consensus of the group was that by year end 1963 this gross national product figure would be at a minimum of $590 and more likely in the $590-to-$595 billion range, approaching the $600 billion mark by the end of 1963. By mid 1964 the most common figure, the motal figure, was somewhere around $610 or $620 billion.

What is this figure? It is the dollar value of the Nation's output of goods and services. Herein it differs from our first measure. Our first measure related to the output of goods. Tuck away in your memory machine the fact that we have become increasingly a service-oriented society. You are part of that service-oriented society. Your industry is part of the service industry. We are the first nation in the world's history to have more people in the service industry than in all the primary and secondary industries combined--more people at work in medical care, education, and the whole public utilities, the whole gamut of services, than ever before.

All too frequently we judge the Nation by what is happening to the goods-producing sector and forget about the stability or the expansion that is taking place in the service sector. What was happening in the second half of 1962 was that, while the goods-producing sector was marking time, the service sectors were still continuing to expand.

The gross national product tells us first, the rate at which we are producing goods and services in dollar terms. That's important in and of itself. But far more important to the American business man is what it tells us about the demand side of the equation. First it tells us the rate at which we are producing. That's the supply side of the equation, but it also tells us what is happening to the $580 billion worth of goods and services that we are producing. It begins to provide us with answers to the questions: Why did we get where we are? What has given us 31 months of unbroken recovery? Tick them off on your sheets as we review them.

The first force making for this recovery has been the strength of consumption. Look at that column labeled "personal consumption expenditures." Note its growth. It's the third column on page 2. It has grown throughout this entire period of our recovery. This has not been the sluggish sector of our society. Why has consumption been rising as markedly as it has? The answer is to be found a little bit later on. We look at it in personal income. We've given American consumers the highest income they have ever had in the months of June, July, and August, and the same will be true in September.

Here's a bit of homespun arithmetic. Give my wife additional dollars of income and she will find ways and means of spending or saving. It's mostly on the spending side. Spending has been going on freely in the months of June, July, and August, and will again in September.

This is strength No. 1. In the first 2-½ years of recovery and in prospect for the balance of 1963 and 1964, consumer confidence is high, as best we can measure it. Consumer intentions to buy are high, as best those can be measured.

We ask these questions of American consumers, 1500 of them, every week. There is no diminution in the index of confidence of American consumers as best that measure can be summarized for you. There is confidence in employment in the future, confidence in the future rise in their income. We will explore that one perhaps a bit more in the discussion period. That is strength No. 1, one of our major sector accounts.

In passing, notice how much of our output is devoted to the aggrandizement and satisfaction of the individual. Of the $580 billion of output, nearly two-thirds is taken off the marketplace by consumers. Not so in other societies but so in ours. I could devote an hour to that thesis.

This is one new sector of demand. It has been strong in the first 2½ years of recovery, strong in the third quarter of 1963, and promises to continue strong in the balance of 1963 and 1964, insofar as we have foreshadowing statistics for that particular area.

The next area of demand is government purchase of goods and services, the column in nearly the middle of the page. Look at the total--$123.8 billion worth of goods and services taken off the marketplace by government. And here's the break-up: Much by the Federal Government--$56.7 billion at an annual rate for national defense. But catalog in your mind again for future reference the fact that the overhead at the state and local level is in excess of our total defense take. It has grown far faster than our national rate of economic growth over the past decade. And, since there has been so much talk in certain quarters of the United States about private affluence and public squalor, may I suggest that you post on this sheet what that figure was for the year 1939. This is an official statistic. You have experienced this phenomenon in your lifetime. The corresponding figure for the year 1939 was $23 billion. I'll put that growth curve against any growth curve you can offer in the way of a counterpart. It's the world's biggest business.

Again, we have foreshadowing statistics for this particular sector of our society. We can look at the budgets of the Federal Government and we are organizing more and more the information about the future spending plans of the state and local units of the Government. It is a virtually ironclad forecast that this figure by year-end will be higher than it was at mid-year, and by mid-1964 it will again be higher than it was at the end of 1963. If I had to come up with a figure for you I would say that in all likelihood that figure by year end will be approaching $130 billion.

So here we have strength in demand in two major sectors of our society, in the consumer sector and in the governmental sector.

What has been ailing the American economy? What has been holding back our growth rate? Good as the figures are, they are not good enough to cure our basic domestic problem. Our basic domestic problem is sticky unemployment. We will look at the column that is so vitally related to the process of economic growth. That column is the column labeled "gross private domestic investments." Note that after a rebound from the recession low, private investment reached a total of around $77 or $78 billion and in quarter after quarter failed to move upward.

If there is any sluggish sector in the American economy, it isn't in the consumer area and it isn't in the governmental sector. It is not in our net exports of goods and services. It is primarily where it has been for nearly a decade--an inadequate rate of growth in private investment, in new tools and equipment, in new plant and machine tools, lathes, turbines, in the new technology that we depend on so much to improve our competitive position internationally or to offset rising wage costs domestically. The evidence is crystal clear.

One of the reasons why economists have grown more optimistic about the outlook for the balance of 1963 and 1964 is that finally, as you can see from the second-quarter figure shown here, the investment in new plant and equipment began to turn upward modestly. From such data as we have assembled at our shop, it becomes apparent that this modest upturn in the second quarter will continue upward at a modest pace through 1963 and well into 1964.

About a year ago we were warning the American economy that sluggishness in this particular sector of our society could bring on a recession. Fortunately, in 1962 we began to take initial steps toward stimulating that vital sector of our economy. We liberalized depreciation; we created the 7 percent investment incentive. These were small capsule pills on the investment front. Despite the widespread feeling that if you gave investment stimuli to American industry it would not respond because of a huge overhang of capacity, we found in industry after industry that, given greater incentive to invest, there was a higher degree of investment, in the automobile industry, where sales were good and profits high, but also in the steel industry, where there was a huge overhang of excess capacity. There was a massive breakthrough on the investment front in the fourth quarter of 1962 which was repeated again in the second quarter of 1963.

There are four channels of demand that you can explore, using the gross national product approach. One is consumption; the second is government demand for goods and services; the third is one you will hear more about from Howard Piquet tomorrow, the net exports of goods and services--notice that that is still a favorable item in our gross national product currently--; and, lastly, the sluggish sector, all too sluggish. It should be around 15 percent and it is only around 13.5 percent of the gross national product. It has been in a descending phase for nearly a decade. Every short fall of a percentage point sounds like a token figure. A 1 percent decline in the setaside for new plant and equipment with a $600 billion gross national product is an attrition rate of $6 billion in the rate of investment.

I have spent a considerable amount of time exploring the gross national product as it relates to two questions: Where are we? How did we get there? It is in my judgment the best analytical tool that has thus far been devised for dealing with those two questions.

Now very quickly let me move on to the other thermometers. On page 10, I have underscored this one as our most serious domestic problem. It deals with employment and unemployment in our society. I had the good fortune to be a member of President Kennedy's Committee to Review the Adequacy of our Employment and Unemployment Statistics. We spent 9 months on this problem. I have been telling business audiences and I now repeat it to you: Don't minimize this problem on the basis of what you believe to be the inadequacy of the statistics. Every business man has his own horror exhibit about someone who is counted as unemployed and really ought not to be a member of the unemployed.

As best we can define these statistics these figures are meaningful. It is not just the problem of the baby sitters, who don't find employment. It's not just a problem of the teenagers. It is not just a problem of the married women who really ought not to be in the labor force, according to some. One of my graduate students said when that charge was made, "She doesn't work for pleasure." It is not just a problem of the superannuated trying to find employment. It cuts across the whole gamut of America's population.

We told the President of the United States in our report of 400 pages--available from the Government Printing Office if you would like to examine it--

that unemployment was growing stickier with each passing peak of the business cycle. It is still true on page 10. You might jot down what the seasonally adjusted unemployment rate was for the month of August. We've had 21 months of recovery and nearly $600 billion of gross national product, and yet 5.5 percent of our people are unemployed in the month of August, at a peak of the business cycle.

Ponder the significance of that rate should contraction develop as compared with the peak rates of output. With each passing peak of the business cycle the unemployment rate has been higher. It was around 4.5 percent at the last peak and 3.5 percent at the preceding peak. That's conclusion No. 1.

Conclusion No. 2: We have the highest rate of unemployment of any industrialized society. I wrote that particular chapter of the report. I know all about the bugs that exist in international comparisons. We have a higher rate of unemployment than Western Europe, than Japan, and than Italy. One nation did have a higher rate than ours. That was Canada, but it has dipped below ours.

The third conclusion is the most sobering one of the lot. Our unemployed have the highest option to remain unemployed of any unemployed in the world history. This, too, is a problem that we as a people should be concerned with: How do you motivate the unemployed?

There is another part of the problem you may wish me to explore in the discussion period. I told a congressional committee just 2 or 3 weeks ago that, as good as our system of economic intelligence is, we can't tell at the moment whether we have more jobs going unfilled than we have unemployed. Across the country help-wanted ads are mounting and at the same time unemployment rates are large. Employer after employer in many instances would like to have more employees, but can't find people with the particular skills that they need. We have no measure of job vacancy in our society. I, for one, will not be satisfied until we know whether we have unemployment because jobs are not to be had or whether we have unemployment because there is a failure to mesh the skill requirements of opening a job vacancy with the job training of the young.

That's another measure that's worthy of your consideration. I have looked at the whole in the doughnut, but now here is the doughnut itself--the highest level of civilian employment this country has ever known, in the months of July and August. The August figure, seasonally corrected, that civilian employment figure, is 68.9 million in the month of August, nearly 70 million. At one time we came close to this, in fact, without seasonal adjustments. It is still true. Nearly 70 million people are at work.

Remember when Henry Wallace was concerned about finding jobs for 60 million Americans. Here we have created jobs for 70 million. But this is still not good enough. We have created a million and a quarter jobs over the past year. Despite that fact the unemployment figures are larger than they were a year ago. It reminds me of Alice in Wonderland and the Red Queen, who had to run awfully fast to stand still.

If you think I am spending too much time on this problem, I refer to my three youngsters at home to give you a bit of homespun economic arithmetic. Add 18 to 46. Eighteen is the average age of entrance of a youngster into the labor force. Our unemployment problems are as nothing today compared with the problems of creating employment in 1964, 1965, and 1966. If the Golden 1960's are to come into being, and I still believe they will, despite the first third of the 1960's, which had a somewhat slower pace, what we must do is create a job explosion first, to have the consumption explosion that will follow thereafter. We have been too slow to recognize the need for this job explosion and to deal with it where it must be basically dealt with, at the grass-roots level rather than at the national level.

We are still on our thermometers. We have looked at strengths and weaknesses. In quite a few of these hastily again I move from the employment one to the one that is of such interest to you--on page 4. I have already cited it. One of the underlying strengths in our economy is personal income, the flow of personal income to the American people. You will see that in every month of the second quarter personal income was higher than any preceding month. The good news in July was that the personal income of July was higher than that in June. I can assure you that when the August figures are released they will be higher than the July figures. Behind it--and again all I can do is give you a fleeting reference to it--is the day and age of the $100 pay check.

That is shown on page 15. You can examine it at your leisure. I am not talking any longer about the pay check of the steel worker or the automobile worker. The average pay check of a factory worker in the U.S.A. was on the verge of the $100 mark, the weekly pay check, in summer. I can recall--again you see how one draws on personal experience--back in 1939 the pay check of the average factor worker was $23.65. It has risen from less than $25 per week to today's $100 plus.

And remember, there are many supplementary breadwinners in the American wage-earner's family, so that literally we have lifted millions of wage-earner families from the subsistence levels or below at which they were prior to World War II to today's middle-income class with all the significance that has for consumption and market potentials.

Lastly, and again so that you will know where the data are, pages 25 and 27 give the readings on our price thermometers. There has been some concern about the resumption of inflation. I suggest to you that you study carefully the statistics on pages 26 and 27 to appraise the merit of that argument. I said to, I believe it was, the New York Times in a review they will publish on Sunday that I do not see a resumption of inflationary pressures from three traditional causes. Cause No. 1 would be the wage-cost price pressures in our wage settlements of late, which have been entirely in keeping, particularly in the steel industry, with the gains in productivity.

Traditional cause No. 2 is the excess of demand over supply. As best I could read the thermometers, our American industry is still operating at around 87 to 90 percent of capacity.

Third is the monetization of the public debt. Again there you see very little impact, and some degree of restraint being exercised by the Federal Reserve on that particular front.

Back up and look at page 27 and you will find our wholesale price index. It hasn't changed despite the recent bulge as late as August 13 of 124. Back in 1960 it was 100.7. On the prices of goods, some goods have gone up and some others have gone down. In general there has been very little growth, very little price pressure on the manufactured goods front.

If you look at commodities other than farm products and food--all industrials--you will actually find a decline. On the consumer price index front there has been a rise. The July figure is up, a very sharp bulge, half a point. That is significant as consumer prices go, from 106.6 to 107.1. Examine it carefully, as we have done, and you will find that the growth came primarily in the food area. The commodities less than food have virtually the same price in July as in June. I think this has been more a seasonal bulge than any other factor, in part reflecting a poor season for the citrus crops.

All that has been happening is that the service sectors have shown some degree of increase, as they have in the past. This is the familiar price creep which has characterized this index, rather than an outbreak of inflationary pressures.

Moving on from a review of the thermometers to summarize that review, we have had a broad breakthrough across a wide industrial front. I think I have demonstrated that, at least to my own satisfaction. On the demand side we have had strength in the demand for consumer goods, with rising trends in government expenditures for goods and services. We have had a sluggish tendency on the part of private investment, primarily because of our excessive reliance on the corporate tax rate, which is higher than virtually any other in the world. We draw more of our central government revenues from corporate taxation and in fact from income taxation in general than does any other system.

By way of a footnote, we put 10 points into our corporate tax rate a little more than 10 years ago to fight the Korean War, to help finance the Korean War. We put in 5 points at that time for emergency revenue purposes. Do you know what we put in the other 5 points for? I am quoting: "To restrain an incipient capital goods boom." We still have those 5 points left in the corporate tax rate when we have been suffering from sluggishness and anemia on the private industry front.

Now to the barometers for what they are worth--first, the weekly hours of work, on page 14. As you can see there, the hours of work in May, June, and July were pretty close to a postwar high--40.6 or 40.7, particularly in the durable goods industries. There was some seasonal letdown in the months of August and September, but I believe that Ford, among others, has indicated that a resort to overtime will be more intensive in the fourth quarter of 1963 than in any earlier quarter since this recovery began. While you are on that page you can see that $100 figure on page 15, on the opposite page, $99.88 average weekly earnings, for manufacturing. In the durable goods industries it has crossed $100. It is up to $108.77

If you think that these have been largely a reflection of the cost of living adjustments, notice in the column over there where the price factor has been removed and you will see that from 1953 to 1963 the pay check in terms of constant dollars has gone from $80 to $99. Do you wonder that more and more the American labor leaders are growing more concerned with preserving what they have than with fighting, as Hoffa described it, for a few lousy cents more per hour.

That is still a positive reading. The second barometer is the new order position, on page 22. This measure inordinately bulged in the opening months of 1963. You will find it reaches a peak around April. It tailed off a bit in May and June, and again the jitters axis grew a little bit concerned. There is some relief in sight in the July figure which is now available. It shows the figure for manufacturers' new orders to have improved above the June position. It is 35.5 as compared with 35.2, particularly in the soft goods sector of our society. I think it will show further improvement in the fourth quarter as the process of steel liquidation ends and inventory accumulation begins, of steel.

Profits are on page 7. Again this is something that merits much more attention than I am able to give to it. Look particularly at the figure of undistributed profits. See how little remains. This is the primary incentive to investment, far more so than cash flow. We wrote a rather devastating critique of the illusion of cash flow. Some of you may want to refer to it. Liberalization of depreciation gives a more rapid return of past investment. It is not a return on past investment.

The corporate profits figure after taxes is around 4 percent of our gross national product today. It used to be around 9 percent. We have sharply reduced the proportion of the national output that is available to the corporation, either as a reward to its shareholders or for purposes of future growth. There is no sign of improvement in the relative position of corporate profits, even in the second quarter of 1963.

This is closely related to the phenomenon on page 9, expenditures for new plant and equipment. I commend this series to your particular attention because here is the series that is shot full of future significance. The U. S. Department of Commerce and the SEC asked American industry across the board, "What are you spending for plant and equipment? Or what do you propose to spend for plant and equipment in the months immediately ahead?" What they found in their latest survey just a week or two weeks ago is that by the fourth quarter of 1963--you see your figures break off with the third quarter and we can now begin to foreshadow the fourth quarter--the rate of expenditures for new plant and equipment will be as high as 41.7. It would be around 40 in the third, and 41.7 in the fourth.

We have just completed our own survey of the capital appropriations of the thousand largest manufacturing corporations--General Motors, U. S. Steel. We do this every quarter. We found in the second quarter of 1963, in the latest reading, perhaps, of this whole foreshadowing area, that the investment intentions of American industry are still rising. But they are still not good enough to give us the rate of expansion we need to create sufficient jobs in the capital goods industry and to step up our of economic growth. Nevertherless there are positive readings on the barometric front in many instances.

The last, for reasons of time, that I will refer to, because it is common knowledge, I think, on everyone's part, on page 34, is the stock price index which recently broke through the previous high, and from day to day we have been reading about new highs, with the prospect of the Dow Jones index going beyond 800, et cetera.

Well, here, then, is the framework of analysis as best I can present it to you on which business economists have built their model for the next 6 to 12 months, after appraising the three questions with which we started: Where we are, how we got there, and where we are going.

We have many problem areas. We have a whole catalog of uncertainties. We have the unemployment problem, to which I referred, as our largest single domestic problem. The largest and gravest international problem is our balance of payments difficulties. We have an integration problem. You can build up your own catalog of worries. We have them. The burden of proof lies on the economist who is as optimistic as I seem to be. I don't believe I am. If anything I am restraining my optimism in my analysis to you, because I am fearful of excessive optimism on the part of American industry.

We have a whole catalog of uncertainties. The primary reason--there are two--is that our business economists are of the belief that this recovery will not come to an end in the course of 6 to 12 months, despite the fact that as recoveries go this one is already 31 months old, and the average is about 26 to 28 months--we don't place too much confidence in an average, because you can drown in a stream only 4-feet deep on the average--but will continue, because, first, even with 31 months elapsed it is difficult to find excess, and this is what brings recovery to an end--stresses and strains that are built into it, excessive inventories, an excess rate of capital accumulation. It is difficult to find excesses in the economy thus far, at least of sufficient magnitude to suggest a turning point.

Secondly, and overriding, is the strength currently and in prospect of end-product demand, strength on the consumer front, as I have indicated, strength in the governmental section, strength currently and in prospect on the private investment front. But it is still not good enough.

In closing, I would hope that we would recognize that it isn't good enough. That's why I have tried to restrain my optimism about the months immediately ahead. It isn't resolving our unemployment problem. It isn't giving us a competitive rate of growth with that of other societies. The reason I stress this is that growth and investment are closely correlated. Investment and profits are in turn closely correlated.

There is philosophical debate--you all have been exposed to it and will continue to be--about how you arrive at a higher rate of economic growth. There is one school certainly in the majority which believe that all that's wrong with us is on the demand side, that all that we need do is stimulate consumption. They say this is basically the right approach for stepping up our rate of economic growth.

When I argue as I have with this with you this morning, I put my emphasis upon the stimulation of investment rather than on the stimulation of consumption. In so arguing I am then told--and this I regard as a semantic trick--that I am endorsing the trickle-down thesis that what you do is stimulate the economy by giving a greater reward to the risk taker or the adventurer and out of this will flow higher pay checks to those at the middle of the base of the income pyramid.

If this be a warranted type of appraisal, I would suggest to you that in my argument perhaps I have logic on my side. If the emphasis is upon stimulation of demand, I think that is a trickle-up process. Mine is described as the trickle-down process. I have the law of gravity, I think, on my side.

CAPTAIN McCUSKEY: Professor Gainsbrugh will now entertain your questions.

PROFESSOR GAINSBRUGH: This is the part of the morning I really look forward to.

QUESTION: I have read recently about the increase in consumer credit and debt. I wonder if you will give us the reason for your optimistic picture in this area.

PROFESSOR GAINSBRUGH: Restrainedly optimistic. I haven't yet shifted from optimistic caution to cautious optimism, but I may. Somewhere in this Table of Contents you will find the statement on consumer credit. It is on page 32. I think there you will find warrant for some of the statistics that were recited. I didn't follow them too closely.

It is undoubtedly true that, with two good car years back to back, and with a third good car year imminent back to back to back, you will see a further increase in the personal debt figures. So far as I know, no one holds a gun to the head of an automobile dealer and tells him to sell without a credit search on his part.

As I can vouch for, on the basis of personal experience, there is a rather intensive credit search. I think, then, we ought to be looking at the quality of this credit as well as its amount. I think, too, that the amount of credit outstanding ought really to be viewed as a balance-sheet item rather than as an operating-statement item, and that, as the net-worth position of America's consumers is improved, as the average wage-earner's family income rises from where it was to the $7500-$10,000 income bracket in which more and more of them now fall, their capacity to carry debt is enlarged.

So far as I know, the figures are not out of keeping relative to the flow of income to America's consumers or to their net-worth position. This may become an increasingly restraining factor as the recovery runs its course.

Will Rogers at one time had his own definition of a recession. Some of you may remember it. Will said, "You have to stop every once in a while to pay up."

This may be a break on future credit extension, but I do not view it as an area of excess at the moment. If I were to single out a factor for more intensive consideration, it would not be the consumer installment credit. It would be the mortgage debt outstanding. The marked growth that has taken place over the past decade, as you can see from the figures in this table, and the possibility that there are weaknesses in the credit structure in the mortgage area which might conceivably grow cumulative, might perhaps compound some of our problems in the next recession.

Lenders have grown concerned about the quality of credit both in the mortgage and in the installment areas. I think they are beginning to exercise some degree of restraint. This may suggest a more modest rate of increase in this particular area, but I do not regard it as a basic weakness.

QUESTION: Doctor, would you please comment on what stress economists are giving to the fact that, while consumer prices have remained fairly stable, there has been a notable decrease in the quality of the commodity?

PROFESSOR GAINSBRUGH: I think some economists would contend to the contrary, that there has been substantial improvement in many of the items that are being produced today, as compared with their counterparts of 5 or 20 years ago. Again using a one-family example, we are today a three-car family. We used to be a one-car family. The three cars I think are the equivalent of one good one, but it is amazing to me the life span of the two that my youngsters have acquired. They are functional. This is all they ask of them.

I think I could point to many quarters in which the quality of products has been improved rather than deteriorated. Think of the life span of a tire, and the horsepower of a car. These are cases in point. There may be some offsets in terms of price. I think the improvement in medical care is another offset to the rise in price. Again there is an improvement in quality.

So I don't think the swing is all in one direction. Further I would add that American industry is growing conscious of this belief on the part of the American consumer, and is doing a better job of policing service than it used to and a better job of inspection than it used to, and is actually embracing more and more of the service sectors. There is the extension of the guarantee of 50,000 miles, for example. This is embracing in part the service sector by the goods producer. There is also, I believe, a better policing of the service sector than we have had previously.

I know that certain economists, who shall go unnamed, take a counter position. That doesn't surprise me. We are frequently at odds. This makes for full employment of economists, and I am all for that.

QUESTION: How do you propose that industry go about the task of creating more jobs and therefore more income for American consumers?

PROFESSOR GAINSBRUGH: It is entirely possible by stimulating the investment sector. Stepping up the rate of research and development of new product development, product improvement, will in turn create jobs well before the flow of income to the American people and well before the new products themselves are coming off the wheels of American industry.

Let me put it to you this way. I think the multiplier of the dollar of investment is greater than the accelerator. The additional dollars of income that will be generated by the dollars spent for plant and equipment--and mind you those dollars are spent well before the plant is completed, well before the equipment is rolling--are feeding into the consumption stream before the goods and services will emerge. I think the multiplier of private investment is far greater than the accelerator that comes from the additional dollar of income that is spent for food and clothing, and ultimately shows up in the order books and even later in the pattern of investment.

I think there is a time-lag factor there that is definitely on the side of the investment-level dollar.

Here my biases are again showing. I think here again I am revealing that I am more a product of the old firms here than the new.

QUESTION: You stated that our unemployed have the highest option of remaining unemployed. Will you please comment on that?

PROFESSOR GAINSBRUGH: This embraces a whole field of objectives. Since our standard of living is so much higher than the standards of living in some other countries with which we drew comparisons, and since the levels of savings are higher in many instances than in other countries, it is possible for a worker to remain unemployed without having the overhand of subsistence confronting him, as, let's say, is the case of an Italian worker or a Japanese worker. The levels

~~of savings and the flow of supplementary income are greater. Our unemployment insurance is many instances is higher than that in other countries.~~

In all too many instances our people are of the belief that they have paid ~~their dues in the unemployment insurance~~ lodge for the past 10 years and that now they have an opportunity to draw those benefits for 13 to 26 weeks, so they exercise that degree of option. In many instances our workers are reluctant to take the first job that is offered, particularly if it involves downgrading. This wouldn't necessarily be true in other societies.

These are some of the overtones. Another one that bothers me no end is that in some of our surplus areas of labor force, areas of labor redundancy (grand semantics) unemployment insurance has really become a way of life. And then I must confess that I hear all too often of abuses, some of them within legal sanction and others going beyond it, abuses of the unemployment insurance feature.

I think it is time--and it is being done--that we started reexamining the warrant for inclusion of individuals in unemployment insurance at the local and state levels in the same way that there was a rather revealing examination of the warrant for relief in Washington, D. C. There are abuses developing in that particular area.

Many of these provisions were set up at the time when the levels of living were sharply different from what they are today. Unemployment insurance was designed primarily as a short-run protection against the economic hazards of dislocation that would introduce marked changes in an individual's way of life. All too often now it is an easy way to take more time before an individual is really motivated to move on to searching hard for additional employment.

One of our major findings in the Presidential Commission survey was that we don't know enough about the motivation of the unemployed, that it is no longer useful to have just the statistic of 4 or 4.5 million unemployed, and that we should make a deeper search of what actions the individual himself is taking to seek employment: Has he registered with an employment agency? Is he going back to see his future employer? Is he doing what he can to make certain that he is a mobile member of our society?

QUESTION: Doctor Gainsbrugh, many major industries today appear to have an excess of capital. The proposed tax cut would simply appear to increase this excess. Would the tax cut, therefore, mean any additional incentive to expand?

PROFESSOR GAINSBRUGH: That's the question that I am very often confronted with, that industry has more cash flow, retained earnings plus depreciation, than it did before and still it isn't spending its cash flow in terms of new plant and equipment.

What makes the mare go, to repeat, is not the cash-flow position of industry but the profits, particularly the retained earnings of American industry--current and prospective profits.

We've examined the process of investment for the past decade intensively. My rule of thumb is this: When profits and profit margins are rising, you will find investments rising. When absolute profits start to flow or to hold stable and profit margins start to decline, you will find investment declining.

I know that the counter argument is that they already have more capacity than they know what to do with and this is what motivates them. I have given you the illustration of 1962-63. I had the good fortune to participate in the American Bankers' Symposium on Economic Growth. The President addressed that particular symposium and brought along with him Secretary Dillon. Secretary

Dillon looked for an empty chair on the dais and the only one that was available was next to me. So I had his ear for a good while. This was early this year. I turned to him at that time and let him see the preliminary readings of our capital appropriations. This was when there was great indecision as to the outlook for 1963. I pointed out to him the investment intentions had risen markedly in the steel industry and across the board in the metalworking industry. We surveyed our membership and asked why, and the primary reasons why these men had changed their horizons was that liberalization of depreciation, but particularly the 7 percent investment incentive, had moved them forward.

Sure, they have excess capacity, but what they have in most instances is high-cost excessive capacity. We've got antique shop after antique shop across the country, in Youngstown and elsewhere, as compared with their counterparts abroad. Our American kndustrialists know this.

I repeat--the basic frame we have used in the past to motivate investment has been the profit motive. It worked in the past. It worked following World War II. It worked again in 1962-63, despite the feeling that it wouldn't. What happens is, if you step up profits you bring across the threshhold of investment investment that would otherwise lie dormant.

The process is a simple one. The bright boys down the line keep knocking on the door, saying "Profits look better than they were last quarter. What's holding you back now? Let's innovate. Let's modernize." They keep pressuring the front office until there is a response. If a given company doesn't do it, then its competitor across the street is moved into investment under our market-motivated determination of investment.

So you see mine is a confession of faith. This is a mechanism that has worked in the past, the incentive mechanism, the reward to the risk taker. The higher the reward, the greater the degree of investment . What companies are investing the most currently? The companies with the better profit position.

QUESTION: Dr. Gainsbrugh, on page 20 are new housing starts, which you didn't mention. I would like to know the importance of this, particularly its relationship to the matter of foreclosure. This is not mentioned on this particular page.

PROFESSOR GAINSBRUGH: One of the reasons I didn't mention the housing starts figure is that we wish they were better in terms of their statistical ability. They bounce around so much on a seasonal-adjustment basis that you never know how much stock to place in them in a given month. They have run awfully high of late. If you look at the figures you will see that they are up to around an annual rate of a million and a half or so.

Starts today foreshadow subsequent activities. This is another barometric measure that we very frequently look at--heavy contract awards and housing starts. The foreclosure figures have been running higher than in the past. They are lower than they used to be in pre-World-War-II days. This is, I think, a restraining factor that will become more and more obvious as this recovery runs its course.

This may be one of the areas in which a turning point could conceivably be reached. It is no longer easy to pick up a capital gain in the housing area. This was a favorable factor in much of the early postwar period. Quite a few of the people who have been living in heavily mortgaged homes have wondered whether they want to go on paying on the mortgage or whether they'd just as soon let someone else carry the bag, because there isn't the offset of a rise in values.

I suspect in your neighborhood, as in mine, there are more signs up on used homes for sale, and they stay up longer than they used to. In New York City we've got a different problem that affects these figures. The total looks good. It's heavily concentrated in apartment units, and, despite the fact that we had rent control as late as 1963 over certain types of facilities in New York City, concessions are just as liberal as they were prior to World War II. This is an indication of softness in the apartment area in New York City. It may not be typical across the country.

It's another item in the catalog of uncertainties, the catalog of worries. There are many. I think I could give you a baker's dozen. This would be one. The debt area would be another. The unemployment picture would be a third. The balance of payments would be a fourth. Each one of you, I think, could keep adding to the list.

In the face of all these, our foreshadowing statistics are still strong, but even more in point, so far as we can measure, end-product demand for goods and services by American people, by American government, and by business, if anything, are in the ascending phase. If you weigh these in the balance, you will still come up with the type of picture I gave you.

QUESTION: Sir, was your forecast for the increase in GNP to possibly $620 billion based on a prospective tax decrease, and, if not, will you comment on the effect of the prospective tax cut now being considered?

PROFESSOR GAINSBRUGH: The business economists in the main did not incorporate a tax cut in 1963 in their expectations for 1963. The model that I gave you for 1964 does incorporate it. In Cleveland, and in most of the other sessions that I have attended, we incorporated a tax cut, the amount in question centering around $4 billion in 1963, largely personal, maybe 75 percent personal, and 25 percent corporate--somewhere in that neighborhood.

Yes, and I would give you another bit of economic arithmetic that suggests that this is likely--64 is divisible by 4.

QUESTION: My question relates not to sweet dreams. My question relates to the tools of the trade. We've heard much about computers and what they can and can't do. Would you care to comment about what has been done in the area of predictions and the science of indicators through the use of computer simulations or models?

PROFESSOR GAINSBRUGH: I think you win the prize for the best question this morning. I have begun to speculate about the significance of developments in the field of economic intelligence of the past decade and a half, relative to the whole area of economic analysis and prediction. The vistas ahead are very glowing. We have speeded up our whole system of economic intelligence. We have moved from the day and age when most of our material was of an annual character to quarterly data, and as you saw here this morning, to monthly data.

I won't be satisfied, nor will many of my colleagues, until the GNP figures which are so essential for economic analysis are available on a monthly rather than on a quarterly basis. We have moved from annual to semi-annual to quarterly, and we'll move on to monthly. Many of our data for monthly purposes will become weekly. I am stressing this, because I think that from it will emerge a better knowledge of current position. Good as is our system of economic intelligence, time and time again we've missed out on determination of current position.

It's too late to know that profits are shrinking 3 to 6 months after the fact. It's too late to know that inventories are in excess of sales 2 to 3 months after the fact. The individual firm is going to be better informed, and we as a people are going to be better informed. Our levels of sophistication relative to the economy and its current position will be improved. The whole process of decision making will be markedly improved, I think, in the next decade, as compared with the progress we made in the past.

That is important in and of itself. Better decision making, I think, will improve even more than it already has, and our ability to deal with the problems of the business cycle. Don't minimize the improvement we have already made on the basis of our enlarged system of economic intelligence. Do you know that a quarter-century has elapsed since our last major recession--1938 was our last major recession.

I think in good part this has stemmed from the improvements we have made in our knowledge about the economy and ways and means of dealing with it.

That brings me to the second prospect, that, if we improve our capacity to diagnose the economy, we may be able to take actions to forestall and render increasingly inaccurate the economists' forecasts. What happened to our recession that was in prospect in 1963 in so many of the models that were built for 1963? We believed the diagnosis and took action upon it.

I think you recognize that business cycles are man-made. The better informed, the better the decisions, and the greater the likelihood of the right decisions. I could spend much more time on this. Time Magazine will in the next week or two, I think, be moving into a cover story dealing with the whole area of the contribution of the computer to the next decade and the next quarter-century, not just in the field of economics but in medicine and other areas.

We are beginning to to develop a model built on the past history of the old system to which we can feed data requiring millions of calculations that would otherwise have taken months, if not years, to complete, and have the machines perform many of these functions for us--so much so that, through the process of simulation, we can now begin to see, or will in the years ahead, what the effect of a tax cut would be on this, that, or the other sector of the economy, or what a rise in the new discount rate would mean.

I think this whole process of simulation began to make it possible for us to develop better public policy on a continuing basis relative to actions, and for industry to develop the same type of simulation models for itself.

All of this I think suggests a greater degree of ability to deal with the problem of the business cycle in the months immediately ahead than we had in the months past.

CAPTAIN McCUSKEY: Gentlemen, I am afraid we have run out of time on the questions you have. Professor Gainsbrugh, I extend the appreciation of the College and of the Class of 1964 for a most informative session this morning.

PROFESSOR GAINSBRUGH: You have been a most receptive audience.