

LOCAL, NATIONAL, AND INTERNATIONAL ECONOMIC OUTLOOK

**Remarks by Robert P. Forrestal
President and Chief Executive Officer
Federal Reserve Bank of Atlanta
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It is a pleasure to be here tonight to discuss with you my local, national, and international economic outlook. To say that these are eventful times on the international stage is an understatement. The signing last month of an agreement between the Israelis and the Palestinians is only the most stunning of a number of events that seem to be dramatically changing the world.

Besides the political changes, there have also been some economic events whose consequences may be significant in the near term. For instance, the recent lowering of the discount rate by the Bank of Japan may bring about a needed rejuvenation of the economy in Japan. Also, the widening of the European rate mechanism (ERM) bands should give some European Community countries more freedom to stimulate growth in their economies.

Here in the United States, we have begun to deal with two of our longest-running problems: the increasing budget deficits and health care costs. In that one has helped to feed the other, Congress will serve the nation well if it can bring about reforms in our health care system that make it possible to rein in the cost of this very expensive item. Notwithstanding these hurdles, the U.S. economy remains the strongest major economy on the world scene. So as a prelude to my discussion of international economic conditions, let me begin with an economic overview of the United States and the Southeast.

The U.S. Economy

For the near term, that is, the remainder of 1993, I expect the overall U.S. economy to do about the same as it did last year. The gross domestic product number for 1992 was recently revised upward by the Department of Commerce from nearly 2 percent to around 2-1/2 percent. Around 2-1/2 percent is where I believe economic growth is likely to end up on an annual average basis in 1993 also.

Inflation still remains under control. Despite a brief run-up in prices earlier this year, the consumer price index should rise about 3 percent, on an annual average basis--close to the rate of 2.9 percent last year. The unemployment rate has moved down from 7.1 percent at the beginning of the year to 6.7 percent in August. Nonetheless, with still-sluggish job growth, I expect this number to average out about where it currently is at a little under 7 percent for the year.

The main sources of strength underlying the U.S. economy will continue to be consumer spending (particularly on durables), residential construction, and capital investment by businesses, especially on computers and other equipment. Lower interest rates, which have been engineered largely by the monetary policy actions of the Federal Reserve over the last two years, are a factor in all of these areas. The main reason is that they have enabled households and businesses to restructure their balance sheets. As a result, households are in a better position to purchase goods that are typically financed with credit, and the cost of doing so is much lower than before. Thus, consumer spending should remain fairly healthy--even at moderate rates of income growth.

At the same time, however, the aging evident in most of our population, despite the recent uptick in births, is an underlying factor that tempers growth in the U.S. economy. Logically, an aging population would constrain any jump in demand for either housing or consumer durables. In turn, the demand for cars, household appliances, and the like might not rebound as sharply as it did during other post-recession expansions in the past two decades. In fact, the modest rebound from the recession seems to confirm this analysis.

On the business side, capital spending will continue to be enhanced by the reduction in borrowing costs. Also, businesses are focusing on purchasing efficiency-promoting equipment like computers. Demand for industrial equipment has been hurt somewhat by a sluggish manufacturing sector, but is beginning to pick up. In the commercial construction area, office construction is not likely to turn around this year because it still suffers from a glut of office space on the market. Retail store construction, however, is beginning to show a healthy increase based on construction contracts, which should carry into next year.

Areas of weakness in the economy include not only office construction but also government spending and, for the first time in many years, international trade. Federal government spending continues to decline not only because of defense cuts but also because of the deficit reduction measures. Although states and local government purchases are rising slowly, they have not replaced the cuts in spending by the federal government. On balance, then, I believe that in 1993, as in 1992, this constraint in government spending will be a slight drag on growth.

I find more worrisome the shift in international trade from the positive to the negative side of the growth ledger. The main reason for this change is the worsened economic conditions most of our major trading partners are experiencing. This worldwide weakness is not likely to be reversed in the immediate future, but the western European economies should begin to round the corner in 1994. In turn, the United States stands to gain on the export side. In the meantime, fortunately, our largest trading partner, Canada, is recovering at a moderately healthy pace. Also, the outlook for Mexico, our third largest trading partner, and many other Latin American countries remains bright. Demand for capital goods--an area in which the United States has a substantial advantage--is especially strong. Overall, however, imports will continue to outpace exports as U.S. growth remains stronger than that of many of our trading partners until next year.

To recap, the outlook for the nation for the rest of 1993 is one of modest growth with some promise for increased consumer spending and business investment thanks in the main to lower interest rates. The proposals made by the Administration to reduce the deficit have not caused me to make any major changes in my overall economic outlook for the nation. However, they do make some areas of the outlook less certain. For instance, spending may shift among the consumer, government, and investment categories.

Southeastern Outlook

Turning to the Southeast, I am pleased to say that the outlook for 1993 continues to be brighter than it has been in several years, even though growth has slowed to a more moderate rate

compared with earlier in the year. In the area of employment growth, the Southeast has been ahead of the nation and should remain so with Florida, Georgia, and Tennessee leading the Southeast in the second quarter. During 1992 the region added nearly 300,000 new jobs. This figure represents more than a 2 percent growth rate, which is at least twice the national gain. On an average annual basis, the Southeast could add almost 400,000 jobs this year to the economy, which is certainly not bad. As good as that number sounds, it also shows, though, how moderate this rebound is. During the recovery in the early 1980s, by contrast, the Southeast added around 700,000 jobs--and it did so from a smaller base.

Why is the Southeast doing better than the nation? The main reason is that this region produces the goods that people have been buying since the recession ended and the recovery began. For instance, with lower interest rates, more people have been able to purchase homes. Fortuitously, the Southeast is a major nationwide supplier of lumber and related building products used in residential construction. In addition to lumber, the large textile industry in the Southeast tends to fare well when the residential building industry is doing well since many textile products are turned into draperies and other home furnishings. New home building also increases the demand for home appliances that are produced in several southeastern states. In addition, the rebuilding going on in south Florida and Louisiana as a result of Hurricane Andrew and in the Midwest due to flooding has temporarily boosted these purchases. As the rebuilding effort from Hurricane Andrew peaks and diminishes, the increased demands from the midwestern flooding should take over for another nine months.

Aside from construction-related spending, the expected nationwide increase in demand for consumer durables is good news for the numerous auto and auto-related manufacturers in the Southeast. Textile mills should also gain from this development since some textile products are destined for automobiles. On balance, regional manufacturing should continue to lend strength to the economy of the Southeast, although the growth in manufacturing jobs has begun to taper off. This development is contributing to a narrowing of the gap between the rate of growth in the Southeast and the United States.

Another sector adding strength to the regional expansion is construction, which is likely to continue the growth begun in 1991. Most building activity will be concentrated in single-family housing, as in the nation. New home sales remain strong. A good part of this activity is due to the many young home-buying people who live in or who have moved to this region of the country. While apartment and condominium building will remain weak, the long slide in multifamily and nonresidential construction appears to be over.

The good news extends even to banking and financial services employment, which is slowly edging higher. This turnaround may be attributed to the increased refinancing activity from both households and business. The level of business loans also is improving slowly and should gain momentum through the year. In addition, tourism has been doing well in the Southeast, thanks in part to the flourishing of foreign tourism, although the effects of stories about the perils of foreign tourists in Florida are yet to be determined.

There are, to be sure, certain areas of weakness. Industries that specialize in nondurable goods, most prominently apparel, will contribute less than they did during the initial recovery period, and this difference in output will have an effect on the regional economy. These producers began to experience weaker demand by the end of last year. In the longer term, apparel producers face increasing competition from countries where unskilled and semi-skilled workers are willing to work for less. That competition will be unrelenting as time goes on.

Moreover, there are other areas of potential weakness. The region is not a major capital goods producer. Thus, the expected strength in capital spending by businesses on equipment will be less of an advantage. It also remains to be seen whether the trend toward consolidation and layoffs in communication, transportation, and other professional and business services has hit bottom. This dynamic has been a blow to several large southeastern cities, just as it has been nationally.

The decline in defense spending nationally will also certainly have an adverse impact on the Southeast. For the most part, defense-related manufacturing is less important in this region than in areas like the Northeast and the Far West. Nonetheless, while the region depends less on defense contracting than other parts of the nation, the Southeast does have a greater proportion of military personnel. Therefore, the proposed military base closures will affect this region through job losses.

Overall, then, the Southeast is in reasonably good shape in terms of growth, with automobiles, housing, and consumers leading the parade. Although the rate of growth is slowing

a bit and the gap between the United States and the region is narrowing, the Southeast should continue to outperform the nation.

International Economic Outlook

Now let me briefly give an overview of my international economic outlook. At the beginning of this year when I addressed the German-American Chamber of Commerce, I said that overall growth for the Group of Seven industrialized nations would continue to be modest during 1993. It may be that, like many others, I was a bit optimistic, since it now looks as though overall growth in output for the G-7 should come in somewhere near 1 percent. The bright spots are Canada and the United States. The weakest performance looks like it will belong to Germany with France not too far behind.

The German GDP performance, which should be down about 2 percent for the year, is no surprise since it was clear that Germany would face difficulties in its effort to incorporate East Germany. The same cannot be said for the performance of Japan. At the beginning of 1993, it was not obvious that Japan would be struggling with a stagnant--and even contracting--economy through the second quarter. The government has recently announced fiscal stimulus programs that should help to improve output.

With Italy coming in at the top end of the inflation rates with 4.6 percent, the G-7 countries should hold inflation in check at an average 2.7 percent through 1993.

Generally speaking, the poor performance of the industrialized nations is depressing global economic growth in 1993. That situation should change in 1994, though, as Europe and Japan move out of recession. The Asia and Pacific nations may slip back from their moderate growth rate of more than 2 percent last year to end up at less than 2 percent growth for 1993.

The most robust growth in output for 1993 will belong to the Latin American countries, which should end up with about a 3.4 percent growth rate. To take a look at our next-door neighbor: The economy of Mexico has begun to grow more slowly recently--growth for the first half of the year was 1.3 percent, the slowest rate in six years. However, inflation news is good, with the annual rate pegged to come in at between 9 percent and 10 percent. Uncertainty about the fate of NAFTA, the North American Free Trade Agreement, is taking a toll on the Mexican economy. I would like to go on record yet again about how important it is for the U.S. Congress to approve NAFTA. In a real sense, by signing the agreement, the United States has made a promise to the Mexican government that it would carry through on its end of the bargain. The Mexican government has proceeded with many serious changes to the economy on that basis. Now would indeed be a bad time to pull back from the democratic ideal of free trade, not least of all because it makes good sense economically. Nations cannot grow if they restrict their markets. Free trade is the fastest road to economic growth for both Mexico and the United States.

Conclusion

In conclusion, the U.S. economy is likely to grow modestly in 1993, and the Southeast will do better than the United States. The international outlook is more modest still, due mainly to the

stagnation of the two other economic engines of the world: Germany and Japan. I believe, however, that the strides many countries have taken to hold inflation in check and to cut their budget deficits--including, *mirabile dictu*, the United States--should hold out great promise for increased growth in the longer term.