"FRB"--A TALK ON THE NATIONAL ECONOMY

An Address to the

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by

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I take great personal pleasure in meeting with you here today. As you know, I am an old farm lending official at heart and have always felt a great deal of affection for the farmer and for those who help him make this the greatest agricultural country in the world.

For several years now, I have been part of the Federal Reserve Bank. Therefore, it is rather appropriate that I talk to you on the topic of FRB, except that these initials will not stand for Federal Reserve Bank but, as you'll see, are the first letters of three strands of thought which I wish to share with you.

The first letter "F" stands for forecasting the possible course of economic events in the near future. It's always important to look where you are going, as long as you know where you are. Fortunately, we now see an end of the recession in sight. Economic recovery is in the offing; it may even have started.

There are many signs pointing to an improvement in the economy. Employment has turned the corner. Businessmen report an increase in their orders. Consumer confidence has improved, and retail sales have turned upward. True, the unemployment rate is still close to its peak; and in some parts of this country and in certain industries, the recession is not over. But for the economy in general, the worst is behind us, and we seem to be on the road to recovery.

At the same time, we appear to have reached the point where inflation is no longer the overriding problem it was earlier. The inflation rate, while still high, has been significantly reduced. Last year, for example, consumer prices rose at a 12-percent rate, whereas this year the rise in the Consumer Price Index has been at a 6-percent rate.
The recession has helped wring inflation out of the economy; and, while price stability and prosperity may not yet be within sight, we are definitely on the right track.

While this is where we are now, the more important question is: Where are we going? And this involves the art of forecasting, which is rarely accurate. But, on the other hand, we must all plan for the future, and this challenges us to develop visions of where we might be headed.

What kind of an economic recovery will we have? Will it be strong, modest, or weak? Are we at the brink of an unbridled boom, or is this recovery more likely to be sluggish? As I look at various key sectors, I certainly see gains ahead. In housing, for example, we already see some improvement. Homebuilding starts and permits have increased after many months of decline, and buyer interest has picked up. But if you consider the number of unsold homes on the market today and that the price of a house has gotten out of reach for many people, I am not confident of a boom in this sector in the foreseeable future.

Or consider, if you will, the automobile sector which, while still depressed, has also reported a rise in sales. I recognize that consumers have saved a great deal lately, repaid part of their debts, and can afford a car better than a few months ago. But if you consider that cars carry a 50-percent higher price tag than four years ago, that gasoline and other operating costs have gone up appreciably, and one out of every five persons prefers an import to a Detroit product, it's pretty difficult to be ebullient about the prospects for domestic automobiles.
Or consider the level of capital spending—the money going for new machinery and industrial construction. A rise in new orders for capital goods suggests a turnaround of this important economic sector may not be far away. But with manufacturers in general now operating at only a fraction of their capacity and excess capacity also existing in office buildings and shopping centers, there is little grounds for optimism here.

Mind you, I am confident of the future and am usually something of an optimist by nature. But I am hard put to find signs indicating the economy will soon be moving in the direction of another boom.

That's about all I'll want to say on the subject of forecasting—the letter "F" in the FRB initials.

Now let me turn to the letter "R," which stands for responsibility. Let us suppose the economy does, in fact, not get back on a course of rapid growth and unemployment stays high for a long time. Does it then become the responsibility of Congress to spend much more than it does now or the responsibility of the Federal Reserve to provide a still heavier dose of monetary stimulus?

I have always felt that fiscal and monetary policies should be directed toward promoting jobs and production. That, in fact, is what, under the Employment Act of 1946, the Congress and the Federal Reserve are supposed to do. Besides, all of us want to see unemployment reduced as quickly as possible. But the trouble with excessive fiscal and monetary stimulation is that the consequences of these actions are felt mostly in the future. The danger is that the economy is closer to full capacity when these policies take hold. Under these conditions, oversized deficit spending and monetary stimulus contribute to inflation.
Furthermore, past experience has taught us that government programs are hard, if not impossible, to stop even if they are no longer necessary. And we have found highly stimulative monetary policies also hard to stop, especially when unemployment stays intolerably high.

Consequently, there is a danger in adopting fiscal or monetary policies that, while they may help overcome the recession, make for more rather than less inflation. In retrospect, we have learned that monetary and fiscal policies in 1971 and 1972, for example, were overly stimulative. And while they were not the only factors behind the virulent inflation--there was the wheat deal, the oil price hike, and others--we would have been better off if fiscal and monetary policies then had been less stimulative.

Today, we hear much talk that we don't have to worry about inflation. But let me tell you: Inflation is not dead. If we do much more than set the stage for recovery, the deficits of today will haunt us a year or two from now. And when one ponders about the ability of some industries to raise prices, even while their sales are depressed, and some unions to demand enormous wage increases, even while many people are out of work, I am hard put to dismiss the continued threats of inflation.

I am not predicting that inflation will be as bad in 1975 as it was in 1974. Rather, I am warning that the threat of a fairly high rate of inflation cannot be dismissed. When you further consider the likelihood that energy costs have only one way to go--namely, upward--it is hard to be overly optimistic about inflationary problems in the future. Thus, the prospects I have outlined for you today are a slow road back to prosperity and a tough struggle to hold down inflation.
And in this struggle, let me make yet another observation. When we develop government policies to deal with this problem, let us not overlook the fact that there are many forms of government policies. The government possesses much power that it can bring to bear on the problems of inflation and recession besides monetary and fiscal programs. For example, the government could become a lot more active in combating price fixing. The Congress could lower the minimum wage for teenagers, which would encourage more employment of youngsters and thus reduce unemployment. And, as it has been recently suggested, the Congress could ease the regulation of the airlines, thereby encouraging competition and lower air fares. This, obviously, is a very incomplete list of what government can do. But the main thrust of what I am saying is that we don't have to rely solely on monetary and fiscal policies when we want to influence the economy. In fact, it is important that we don't do that, because monetary and fiscal stimulus usually have inflationary consequences.

This brings me to the third and final aspect of where we may be headed. The "F," or forecast, and the "R," or responsibility, may be obvious. What is not so obvious is the significance of the last letter of my acronym, the letter "B." By that, I mean the question: Would it be all that bad should our economy over the next couple of years not get back to boom proportions?

I rather think not. We all want people to find work and prosperity. Yet, at the same time, we know that what is true for an individual is equally true for the economy. A pace too fast to be sustainable leads to excesses. There is a limit to how quickly we can pick ourselves up
and run. Similarly, there is a limit to how rapidly an economy can pick itself up and gather momentum. Should the pickup in our economic situation develop too quickly, we may all too soon face the possibility of yet another recession. Let me tell you: A slow, gradual, sustainable recovery is far better than boom and bust conditions.

Therefore, I would not be disappointed if the slow business recovery now in prospect were to materialize, despite universal hope that we can move in the direction of greater prosperity as quickly as possible. The "B" in the FRB story is a consolation that the prospect of this taking a little longer than we might want at first glance may not be all that bad.