

The Business Environment  
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It is a pleasure for me to be here today to open your meeting on "The Consumer Market: The Second Half of the Seventies." I am particularly glad the opportunity was given to me this year rather than a year ago. We have come a long way from the days when a royal tyrant might punish a messenger who brought him bad news, but we all still have a tendency to give a friendlier reception to the bearer of good news. And this year, the economic news about the business climate is generally good.

By almost any measure, the economy is now recovering from the most severe set-back it has experienced since the Great Depression of the 30's. While some were concerned even after the decline in business activity was reversed that we could be slipping into another such great Depression, there was clearly no resemblance between 1974-75 and the early 1930's. But so much appeared in the media, particularly while the unemployment level was rising, that I do want to give you one point of reference to keep the events of the last two years in perspective. Throughout the 1930's the civilian labor force stayed around 43 million and the number of unemployed averaged close to 10 million persons. In 1974-75 the civilian labor force was more than twice as large, but unemployment even in the peak month was one million less than in the 1930's.

Now this does not mean that I view with complacency the present level of seven million unemployed today or a projected level of about 6.5 million

unemployed at year-end, I do not. But, I do feel that it is important that we recognize the true size of the problems we faced rather than succumb to the kind of emotional doomsaying that has been too common during the past two years.

Not only haven't we not been through a Depression, but virtually each new statistic which has been released in recent months adds to the evidence that the economy is now undergoing a vigorous recovery; one which, if sustained, can eventually bring us back to reasonable levels of growth and employment, with a lower rate of inflation than we have experienced in our most recent history.

The severity of the decline during 1974 and 1975 followed a series of almost unprecedented shocks to the economy of the entire world. There was the series of monetary crises which led eventually to the abandonment of the Bretton Woods fixed-rate monetary system. Then came the oil embargo and subsequent run-up of all energy prices, the severe pressure on world food supplies, and the parallel overbuilding of inventories of other commodities and the fear of still more shortages. These shocks combined to produce economic downturns not just in the United States, but in every industrialized country in the world, and severely squeezed those lesser developed countries that were not fortunate enough to be part of OPEC. The fact that the cumulative effect of these shocks did not produce an even sharper and longer lasting recession than they did I attribute to two major factors: the structure of built-in Government stabilizers such as unemployment insurance, social security, and similar programs which maintained consumer purchasing power despite the rapid drop in production; and the effective balanced use of both monetary and fiscal policy to meet the situation.

As a result of the progress that has already occurred, there is a much broader consensus among economists about the future course of the economy than existed just a few months ago. Virtually all of the current forecasts are for rates of growth in real GNP well into 1977 above the long-term average. There is general agreement that this broad measure of total economic activity will grow about 6 percent in 1976 and show slower but still substantial growth in 1977.

There also seems to be rather general agreement that inflation, as measured by the GNP deflator, will decline from the nearly nine percent rate in 1975 to about 6 percent in 1976. For 1977 there is less agreement about inflation than about growth. Some foresee further decline in 1977, while others foresee an increase in the inflation rate as business activity becomes progressively brisker.

Until a few months ago a small group of forecasters were saying that the recovery would grind to a halt in late 1976. But with the evidence of strength in the recovery increasing, even they have now shifted forward their expected slowdown to mid-1977 or even into 1978. I personally suspect that, as the year progresses, the pessimists will be pushing their forecasts of a slowdown further and further ahead in time. The economy should not only make up some of the ground which has been lost, but should continue to grow faster than the long-term average for quite a while. My reasons are several. First of all, this has been a consumer-led recovery. Despite the tremendous drop in consumer confidence as measured by the various surveys--and savings rates at levels well above the long-term trends--the consumer has been the key force which has turned the economy around. We have now reached a point in the recovery where the consumer sector is well placed to continue its strong contribution to recovery.

Personal income has been rising at a rapid rate at a time when the consumer is very liquid, and slowing price increases are raising confidence levels.

Second, the housing industry has typically led recoveries after past recessions. This time, although housing starts have climbed substantially from their very low levels of late last year, housing is still lagging general recovery. We are entering an extended period when family formations are going to climb. The growing pressure for new housing could therefore become a factor contributing to the recovery later than has normally been the case.

Third, despite strong retail sales, inventories are very lean; there is going to have to be a growth in business inventories to parallel the growth in sales.

Fourth, although the immediate outlook for capital goods sales, based both on order rates and surveys, is not very promising for most of this year, corporate capital appropriations are rising rapidly. This suggests that a rapid expansion of the capital goods sector could begin in late 1976 or early 1977, and add one more factor necessary to growth.

Finally, I feel that Government economic policy is likely to be reasonably well executed. The new budgeting process in the Congress worked well during the trial period for fiscal 1976. I am anticipating good results from the deliberations which will set fiscal policy for 1977. It is possible that the Congress will decide on more spending and less tax reduction than the Administration has proposed. However, the resulting fiscal policy will still be based on a thought-out total plan formulated by a Congress which is getting expert advice, rather than the old haphazard result of the accumulation of individual appropriations and tax actions.

I have even more confidence in the likely course of monetary policy--biased though I may be. It is now nearly a year since Chairman Burns, in testimony before the Congress, publicly reaffirmed the policy that monetary policy would be conducted with a view of supplying sufficient monetary growth to assure recovery without rekindling accelerating inflation. The evidence indicates that this is just what has happened thus far. I see no reason to expect that either that policy goal or our record in achieving it will not continue. This does not mean that the presently announced goals for money supply growth are immutable. It does mean that the adjustments which will be made in those goals will be consistent with the more basic goals of sound economic growth with declining inflation.

It is, of course, perilous to forecast for the rest of the decade. Even with the best planned policies, unexpected events--like the oil embargo or disappointing crops--can occur again. However, I don't believe there is anything fundamental in the structure of the economy which precludes good performance over the next several years. It does seem likely that the real growth rate, on average, will be slightly lower than in the past, primarily because of the slowdown in population growth which seems to be occurring. But it should be born in mind that even today's lower specific birthrate can be viewed as an unexpected event when we look back at demographic forecasts made just five years ago. The birthrate could rise just as rapidly as it fell. Taking all the things I can into account, I am inclined to place myself on the side of the more optimistic forecasters--those who expect the present expansion phase of economic recovery to last beyond 1977.

I am somewhat more concerned about the impact of some non-economic aspects in the business environment for the longer-term future than I

am about our economic fundamentals. The first of these is the touchy subject of business ethics. For about six months now it has been virtually impossible to pick up a newspaper without coming upon a story revealing some use of corporate funds called into question. These practices have ranged from clearly illegal political contributions within the United States to apparently legal, although previously concealed, political contributions abroad, from bribes which were probably illegal in the countries where they were made, to large but legal and customary "payments" in other instances. Beyond saying that no one could possibly condone the illegal use of corporate funds, it is impossible to pass honest judgment on many of these revelations in any broad fashion. The ethical questions are, in many cases, very difficult to resolve, and I think each company, whether involved thus far or not, is going to have to rethink its policies and how those policies are to be enforced.

My purpose here is not to suggest any specific rules, but to focus attention on the problems for business as a whole. It seems to me that the entire business community is faced with a massive problem of reestablishing its good name, both with the general public and with the political leadership. Steps must be taken not only to put things back in order, to clarify and properly disclose continued actions of the type that has received recent publicity but also to convince the public that the necessary steps have been taken and restore public faith that the business community does operate in a consistently honest way. I suspect that the task of restoring order, ethics, and control may be an easier assignment than convincing the public that the proper effective controls have been installed. For reasons I have never really understood, business seems much more adept at convincing the public of the merits of a new toothpaste than it is in convincing the public of the

merits of business itself. We have somehow created the general concept that the products are great, but the producers are not to be trusted. I certainly don't have any solutions to offer. I can only pose the problem and suggest that, unless it is solved--and unless the role of business profits in capital formation is explained--the chances for long-term survival of our free enterprise system, as we have known it, are diminished.

The second concern as I see it, is the question of government regulation. It has become virtually as popular to call for less governmental regulation as it is to extol apple pie and motherhood. Everywhere one turns, whether within government or business, talk focuses on the high cost of government regulation. The popular press has been full of articles explaining to the consumer how some specific kind of regulation adds to the cost of a specific service or product. We are told that the regulatory agencies get so close to the industries they regulate that the rules are often designed to protect the industry from the public and from competition rather than the reverse. If there is such great agreement that over-regulation is so harmful, why hasn't there been any progress toward its elimination? In fact, it would appear that just the opposite is occurring, there is actually a trend toward more regulation. Temporary regulations get favorable treatment in the Congress, while everyone talks deregulation. I think it is true that in many areas the costs of regulation exceeds the benefits, and the economy as a whole would gain from less regulatory oversight. However, what I see behind much of the talk in favor of deregulation amounts to saying--"let's get rid of the regulations on that industry because I will benefit, but don't deregulate my industry, we're too fragile". "Deregulate natural gas prices, but don't let the price go up." "Deregulate water carriers but not trucking." "We're for free trade generally, but our industry needs

import quotas." Again I don't pretend to have a solution, I can only remind you of the problem. It is clear, however, that deregulation will remain only a slogan--while the trend toward more regulation will continue--until the business community is willing to accept some of the readjustments needed to operate in a more competitive environment.

The third element in the climate of the Seventies I call "consumerism," for want of a better word. I am not using the term in any derogatory sense--we are all consumers and fundamentally each of you makes his living from meeting the wants and needs of consumers. Indeed, your success or failure is strongly dependent on how well you read and predict the consumer's collective mind. In recent years, however, a new phenomenon has arisen. The consumer advocate organizations, stepping up to represent the consumer, have achieved a prominent place among those attempting to influence legislation, business practices, and related questions. The problem that I see is that the voice of the consumer advocate can be so loud and piercing that it is taken for the voice of the consumer, either by those who make our laws or those who make our business decisions. Sometimes, of course, the consumer advocate is correctly voicing consumer judgments and views--but sometimes not. Legislators, regulators, and business decision makers can be misled. The auto seatbelt interlock is a classic example of something the advocate wanted but the marketplace did not, and it was an expensive regulatory mistake. But, lest you think only the government can blunder, I would refer you to the problems the auto industry has experienced in adjusting its product mix and inventory to supply the cars consumers wanted to buy. The high gas user protestors had the auto companies convinced that only fuel economy mattered this year. Production was aimed at the



highest possible volume of small cars but the buying public has reacted quite differently. In other instances such as the demand for clear, "plain English" warranties, and for equal credit treatment for women, I think the consumer advocates' voices were representative of the public's wishes. Business must solve the riddle of distinguishing consumer opinion from consumer advocate position. You are going to have to find out how to tell them apart when they differ and to recognize them when they coincide.

There is no conflict between my optimism on the economic side of the business climate and my concern with ethical, regulatory, and consumer matters. My sketch of the business environment might simply be characterized as a rose with some thorns. But that is always the picture of the future. The specific problems businesses must solve may change, but the environment will bring an endless supply of new problems. The outstanding performance of American business enterprise over history convinces me that today's problems will be successfully met, and that your firms will all be represented at a meeting like this five years from now to face up to the problems of the Eighties.