

REMARKS OF
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THE GERMAN-AMERICAN CHAMBER OF COMMERCE
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PRICE STABILITY FOR ECONOMIC GROWTH

I AM PLEASED AND HONORED TO MEET WITH YOU TODAY IN FRANKFURT. IT GIVES ME A WELCOME OPPORTUNITY TO REAFFIRM THE IMPORTANT TIES OF FRIENDSHIP AND COMMON INTEREST BETWEEN OUR TWO COUNTRIES.

DURING THE PAST FEW YEARS BOTH OF OUR SOCIETIES AND BOTH OF OUR ECONOMIES HAVE UNDERGONE MANY CHANGES AND EXPERIENCED MANY DIFFICULTIES. BUT WE HAVE BOTH EMERGED FROM THE ECONOMIC SETBACKS OF THE FIRST HALF OF THE 1970'S STRONGER THAN EVER IN OUR ABILITY AND IN OUR WILLINGNESS TO LEAD THE WAY TO A HEALTHY WORLD ECONOMY, WITHOUT LOSS TO OUR DEMOCRATIC VALUES AND THE PRINCIPLES OF A FREE ENTERPRISE SYSTEM.

THIS HAS BEEN NO SMALL ACCOMPLISHMENT. IN THE UNITED STATES, WE SUFFERED THE WORST ECONOMIC DOWNTURN SINCE THE 1930 S. SOME OF OUR PESSIMISTS ARGUED WITH VEHEMENCE THAT THIS DEMONSTRATED THE NEED FOR A SIGNIFICANT RESTRUCTURING OF OUR BASIC INSTITUTIONS AND OF OUR ECONOMIC SYSTEM. BUT WITHOUT ALTERATION, OUR ECONOMIC SYSTEM HAS PRODUCED A STRONG RECOVERY AND HAS PLACED US ON THE ROAD TO RENEWED ECONOMIC EXPANSION. THE REVERSAL DEMONSTRATED THE VERY STRENGTH AND RESILIENCY OF THE SYSTEM THAT WAS IN QUESTION. THAT DEMONSTRATION MUST NOT BE FORGOTTEN AS WE SET OUR ECONOMIC COURSE TO ACHIEVE HIGHER LEVELS OF ECONOMIC PERFORMANCE AND HUMAN WELL-BEING.

WHEN I LEFT THE UNITED STATES THREE WEEKS AGO, THE AMERICAN ECONOMY HAD EXCEEDED ITS EARLIER PEAKS OF PERFORMANCE IN SOME IMPORTANT AREAS.

THE OUTPUT OF GOODS AND SERVICES IN CONSTANT PRICES WAS 1 1/2 PERCENT ABOVE ITS PREVIOUS PEAK OF THE FOURTH QUARTER OF 1973. TOTAL EMPLOYMENT WAS MORE THAN A HALF-MILLION ABOVE ITS SEPTEMBER 1974 PEAK. WE WERE ABOUT TO LEAVE THE RECOVERY STAGE OF THE CYCLE AND MOVE INTO THE EXPANSION PHASE. I HAVE NO REASON TO MODIFY MY OPTIMISTIC VIEW ON THE COURSE OF THE AMERICAN ECONOMY.

THE RECOVERY IS NOT COMPLETE FOR ALL SECTORS, OF COURSE. INDUSTRIAL CONSTRUCTION AND MULTI-FAMILY BUILDING CONTINUES TO LAG. INDUSTRIAL PRODUCTION ACTIVITY IN THE DURABLE GOODS' AREAS IS STILL BELOW THE EARLIER PEAKS. REVIVAL OF THE IMPORTANT BUSINESS CAPITAL SPENDING SECTOR HAS BEEN DELAYED.

THE SLACKENING IN THE PACE OF RETAIL SALES IN RECENT MONTHS, AS WELL AS THE SOMEWHAT LACKLUSTER PERFORMANCE IN BUSINESS SPENDING AND DURABLE GOODS' PRODUCTION, HAS BEEN INTERPRETED BY SOME RATHER PESSIMISTICALLY. IN THEIR RELENTLESS SEARCH FOR "NEWS" MANY OF THE NEWSPAPERS AND TV NETWORKS, BOTH IN THE U.S. AND IN EUROPE, HAVE, I AM AFRAID, ADDED TO THIS EMPHASIS OF A HESITATION. IN LARGE PART, HOWEVER, I THINK THE CONCERN HAS BEEN FOSTERED BY SIMPLY THE BAD MEMORY OF THE ANALYSTS.

THEY SEEM TO HAVE FORGOTTEN THAT WE ARE NOW WELL INTO THE SECOND YEAR OF ECONOMIC EXPANSION. THE RATE OF GROWTH OF ECONOMIC ACTIVITY TYPICALLY SLOWS AFTER THE FIRST YEAR OF RECOVERY. THE PACE OF EXPANSION CANNOT BE PERFECTLY SMOOTH IN ECONOMIES THAT ARE AS COMPLEX AND INTERRELATED AS OURS.

THOSE WITH A SKEPTICAL ATTITUDE ALSO SEEM TO BE FORGETTING THAT OUR WEEKLY OR MONTHLY MEASURES OF ACTIVITY SHOULD BE APPROACHED WITH CAUTION. IN SPITE OF OUR EXTENSIVE EFFORTS, MEASUREMENT FOR SHORT

TIME PERIODS IS FREQUENTLY HAMPERED BY REPORTING INCOMPLETENESS OR ERROR AND PROBLEMS OF SEASONAL ADJUSTMENT. TOO QUICK AN INTERPRETATION IS USUALLY MISLEADING -- AND OFTEN DANGEROUS.

WHILE SOME OF THE ANALYSTS' MEMORIES MAY BE BAD, THE MEMORIES OF DECISION MAKERS ARE NOT. THE EARLIER EXCESSES AND THE HORRENDOUS RATES OF INFLATION HAVE LEFT THEIR MARK IN CAUTIOUSNESS. THE PESSIMISTS HAVE MISINTERPRETED THAT CAUTIOUSNESS AS APPREHENSION. IT ISN'T.

THE RECOVERY PROCESS IN THE U.S. HAS BEEN RELATIVELY WELL-BALANCED -- NOT IN THE SENSE THAT ALL SECTORS ARE RESPONDING AT THE SAME RATE BUT IN THE SENSE THAT THE PATTERN OR SEQUENCE OF EVENTS IS BUILDING APPROPRIATELY FOR A LONGER PERIOD OF EXPANSION.

THE SLACKENING IN THE PACE OF CONSUMER SPENDING WHICH HAD LED ~~THE UPTURN~~ IS NOT LIKELY TO LAST. REAL INCOMES ARE RISING, LABOR MARKET CONDITIONS ARE IMPROVING, AND THE CONSUMER HAS BECOME INCREASINGLY LIQUID IN OUR SOCIETY.

SINGLE-FAMILY HOME CONSTRUCTION IS MAKING A SIGNIFICANT CONTRIBUTION TO EXPANSION, AND, WITH MORTGAGE CREDIT IN AMPLE SUPPLY, THE PROSPECTS ARE GOOD HERE, TOO.

THE MAJOR FUTURE THRUST OR STIMULUS FOR SUSTAINABLE ECONOMIC EXPANSION MUST COME, HOWEVER, FROM BUSINESS OUTLAYS FOR NEW PLANTS, MACHINERY, AND OTHER EQUIPMENT. THIS THRUST HAS BEEN DELAYED SOMEWHAT IN THIS EXPANSION BECAUSE OF THE CAUTION GENERATED BY THE RECENT EXPERIENCE. BUT THE TRADITIONAL PATTERN OF EXPANSION IS EMERGING. THE SALE OF SOME PRODUCERS' GOODS, ESPECIALLY TRUCKS AND FARM EQUIPMENT, IS STRONG. CAPITAL SPENDING PROGRAMS SHELVED BY THE AUTO AND STEEL COMPANIES IN 1974 ARE BEING REVIVED. ORDERS FOR LOCOMOTIVES AND FREIGHT CARS HAVE

INCREASED. A NUMBER OF AIRLINES ARE ORDERING NEW AIRCRAFT. ORDERS FOR INDUSTRIAL DRIVES, CONTROLS, AND MOTORS HAVE IMPROVED.

UNUSED CAPACITY IS ONE OF THE CONSTRAINTS ON BUSINESS SPENDING. AS THE EXPANSION CONTINUES, HOWEVER, THE IMPORTANCE OF THAT CONSTRAINT WILL CONTINUE TO DIMINISH, PARTICULARLY SINCE MUCH SO-CALLED UNUSED CAPACITY IS OUTDATED AND INEFFICIENT.

ALL IN ALL, IT SEEMS TO ME THAT DEVELOPMENTS IN THE U.S. ECONOMY GIVE GOOD PROMISE FOR A SOLID PERIOD OF EXPANSION AHEAD.

BUT HOW DO WE SUSTAIN THIS ADVANCE IN ECONOMIC ACTIVITY. THIS LEADS ME TO THE MAJOR MESSAGE I WANT TO BRING TODAY:

--IT IS A MESSAGE OFTEN REPEATED BUT SELDOM HEEDED.

--IT IS A MESSAGE SIMPLE IN STATEMENT BUT DIFFICULT IN IMPLEMENTATION.

THE ESSENTIAL INGREDIENT OF LONG-TERM ECONOMIC EXPANSION IS PRICE STABILITY.

WE HAVE A GREAT DEAL OF EVIDENCE THAT INFLATION IS AN ENDEMIC DISEASE OF DEMOCRATIC SOCIETIES. THE AMERICAN ECONOMY, LIKE MOST OF THE INDUSTRIAL ECONOMIES OF THE WORLD, HAS A BUILT-IN INFLATIONARY BIAS. THE LEGITIMATE CONCERN WITH THE WASTE OF RESOURCES THROUGH UNEMPLOYMENT, A FAILURE TO RECOGNIZE THE SIZABLE COSTS OF INFLATION, A STRONG FAITH THAT STIMULATIVE GOVERNMENT ECONOMIC ACTIONS HAVE SIGNIFICANTLY LARGER IMPACTS ON UNEMPLOYMENT THAN ON PRICES, AND PUBLIC EXPECTATIONS THAT OUTRUN OUR CAPACITY TO ACHIEVE THEM -- AT LEAST IN THE TIME FRAME DESIRED -- HAVE ALL PLAYED A ROLE IN CREATING THE BIAS.

BUT EVEN IF IT IS AN ENDEMIC DISEASE, YOU DON'T ALLOW THE DISEASE TO DESTROY. NOR SHOULD YOU ATTEMPT TO TREAT IT ONLY WHEN IT FLAIRS UP TO THE POINT OF DISRUPTING THE ECONOMY AND EVEN THE SOCIETY. YOU ATTEMPT TO CURE IT, AND, IF YOU CAN'T, AT LEAST TO CONTROL IT, WATCHING

AND DEALING WITH IT EVEN DURING ITS PERIODS OF APPARENT QUIESCENCE.

IN MOVING FROM TWO-DIGIT INFLATION RATES TO SOMETHING ON THE ORDER OF 6 PERCENT OR A LITTLE LESS AT AN ANNUAL RATE, WE HAVE MADE GOOD PROGRESS IN THE UNITED STATES. BUT THIS PROGRESS IS NOT SUFFICIENT. WHAT WOULD REPRESENT ADEQUATE PROGRESS? IN THE ABSTRACT, A ZERO RATE OF INCREASE WOULD SEEM GREAT. PRAGMATICALLY, HOWEVER, WE WILL PROBABLY HAVE TO SETTLE FOR MORE THAN THAT. WHY?

NEITHER I NOR YOU CAN HOLD ABSOLUTELY TO THE CONVICTION THAT A ZERO RATE OF PRICE INCREASE, IF HELD, WILL BE ACCOMPANIED BY THE LEVEL OF UNEMPLOYMENT ACCEPTABLE TO SOCIETY. IF IT IS NOT, PEOPLE IN A DEMOCRATIC SOCIETY DO HAVE A RIGHT TO EXPECT THAT THEIR GOVERNMENT WILL SET LIMITS ON UNEMPLOYMENT. WHAT WE ALL MUST RECOGNIZE IS THAT THERE IS A PROVISIO CLAUSE TO THE EXPECTATION -- PROVIDED WE ARE WILLING TO PAY THE PRICE.

THIS IS THE TRADE-OFF THAT MUST BE MADE. THIS IS THE ECONOMIC POLICY DECISION THAT MUST BE MADE.

WE GET NOWHERE IN SOLVING THE UNEMPLOYMENT-INFLATION DILEMMA IF FULL EMPLOYMENT AND PRICE STABILITY, AS GOALS, ARE IN CONFLICT; THAT IS, WHEN THERE IS NO OPTIMUM COMBINATION OF THE TWO THAT CAN BE ACHIEVED. EXPERIENCE IN THE UNITED STATES AND ELSEWHERE SUGGESTS THAT THERE MAY BE A CONFLICT.

HOW DO YOU RESOLVE IT? I DON'T HAVE THE ANSWER, BUT I DO THINK THAT THERE ARE POLICIES THAT COULD MOVE US CLOSER TO AN ACCEPTABLE SOLUTION.

THE VAST MAJORITY OF OUR ECONOMIC POLICIES ARE DESIGNED TO INFLUENCE AGGREGATE DEMAND. BUT THE PERFORMANCE OF UNEMPLOYMENT AND INFLATION, AS INFLUENCED BY AGGREGATE DEMAND, DEPENDS ON ITS DISTRIBUTION AMONG

MARKETS -- OR ON VARIOUS SUPPLY CONDITIONS. IN EFFECT, WHAT WE GET FROM A PARTICULAR AGGREGATE DEMAND POLICY DEPENDS UPON THE STRUCTURE OF INDIVIDUAL PRODUCT AND LABOR MARKETS. SIMPLY, THEN, IF WE WANT BETTER UNEMPLOYMENT AND INFLATION PERFORMANCE, POLICY SHOULD BE DESIGNED TO AFFECT BOTH DEMAND AND SUPPLY.

THE IMPORTANCE OF THE CONTRIBUTION OF SUPPLY POLICIES IS NOT WIDELY APPRECIATED IN THE UNITED STATES. HOPEFULLY, OUR RECENT PERIOD OF PRICE IMPROVEMENT WILL NOT BE A PERIOD TO RELAX BUT RATHER A PERIOD FOR ACTIVE CONSIDERATION AND IMPLEMENTATION OF POLICIES DESIGNED TO MAKE MARKETS FUNCTION MORE EFFICIENTLY AND LESS IMPERFECTLY. MANY STRUCTURAL MODIFICATIONS CAN AND HAVE BEEN SUGGESTED. ANALYSIS OF THESE MODIFICATIONS TO DEVELOP AN ADEQUATE AND COORDINATED SET OF POLICIES SHOULD BE PURSUED VIGOROUSLY. THIS, IT SEEMS TO ME, IS THE ROUTE TO FOLLOW TO DEAL EFFECTIVELY WITH THE INFLATIONARY PROBLEM.

PRICE STABILITY MUST NOT ONLY BE A NATIONAL GOAL BUT AN INTERNATIONAL GOAL AS WELL. THERE ARE MANY THEORIES ON THE TRANSMISSION OF INFLATION FROM COUNTRY TO COUNTRY. UNDERSTANDING OF THE TRANSMISSION PROCESS IS IMPORTANT, BUT THE OVERRIDING CONSIDERATION MUST BE THAT MAJOR INDUSTRIAL NATIONS CANNOT HOPE TO LIVE INSULATED LIVES -- NEITHER IN PRACTICE NOR IN TERMS OF MAXIMIZING THE WORLD'S GAINS FROM OUR PRODUCTIVE CAPACITY.

I FEEL THIS INTERDEPENDENCE KEENLY IN CHICAGO. MORE THAN ONE-QUARTER OF U.S. EXPORTS ORIGINATE IN THE MIDWEST. FROM THAT BASE, WE HAVE TAKEN ON AN EXPANDED ROLE IN INTERNATIONAL FINANCE. OUR LARGER BANKS COMPETE AROUND THE WORLD, AND THE WORLD'S LARGEST BANKS WORK WITH US IN CHICAGO. TWENTY-TWO FOREIGN BANKS HAVE BRANCHES IN CHICAGO; TWO

SUBSIDIARIES OPERATE IN THE CITY AS DO FOURTEEN OTHER FOREIGN REPRESENTATIVE OFFICES. THESE TIES ARE IMPORTANT. THEY SPAWN THE OPPORTUNITIES FOR EVEN GREATER INTERDEPENDENCE AND ECONOMIC GAINS FOR US ALL.

BUT, IN CONCLUSION, LET ME RETURN TO MY MAIN THEME. THE LONG-RUN EFFECTIVENESS OF THIS INTERDEPENDENCE, AND THE MAINTENANCE OF A HEALTHY WORLD ECONOMY, DEPENDS ON OUR ABILITY TO ACHIEVE A SOUNDLY BASED, NONINFLATIONARY ECONOMIC EXPANSION. I AM CONFIDENT THAT WE CAN.