and early retirement programs have allowed businesses to reduce the number of employees, causing a drop in total labor costs. Finally, many producers have closed inefficient facilities in an effort to reduce average operating costs. While some of the facilities will be called back into production when the recovery gains momentum, many of these closings are part of a long-term adjustment to declining demand for domestic steel. For the near term, producers will probably have to rely on cost-reduction efforts until financial positions (i.e., profits) improve.

The machine-tool industry has been severely hampered by the recent contraction in capital spending. Orders declined by 87 percent from early 1979 to the trough in the third quarter of 1982, compared with a 73 percent peak-to-trough reduction in the 1974-75 recession. Because of the unusual length and depth of the latest contraction, order backlogs declined from their usual one-year level to five months, as shipments outpaced orders. Although orders were expected to stabilize in 1983 and improve this year, shipments could decline another 30 percent to 40 percent from their 1982 levels.

The automobile industry is expected to fare somewhat better than the steel and machine-tool industries in 1983, as manufacturers' incentives and weakening oil prices boost new-car sales. The Round Table's median forecast shows a pickup in domestic new-car sales to about 6.5 million units in 1983 from 5.8 million units last year. The 1983 forecast is 15 percent, however, would be about 3.5 million units below 1978 sales. Even the most optimistic forecast does not show a return to 1978 levels until 1984 at the earliest. One economist noted, however, that incentives offered during the 1981-82 recession prevented automobile sales from declining as much as they could have, given the steep drop in income and employment mix. He suggested that the shallower drop in automobile sales could have been bought at the expense of a steeper gain during the recovery period.

Monetary Policy and Inflation

Monetary policy will play a key role in shaping the 1983 outlook and in determining whether the expansion will continue into 1984 and beyond, according to the Fourth District economists. The liquidity built into the economy during the latter half of 1982 and early 1983 is expected to support at least moderate economic growth over the year ahead. Moreover, it is anticipated that this expansion will be achieved with little or no acceleration in inflation in 1983. Price increases probably will occur in some key industries as firms attempt to restore profit margins, but other factors will moderate upward price pressures. Weakening oil prices, for example, have led several economists to scale downward their 1983 inflation forecasts, even though they expect increases in natural gas prices to offset partially the drop in oil prices. Moreover, a sharp rise in productivity usually slows the pace of price increases. Weakening oil prices could prove to be an important factor in shaping the 1983 outlook and in influencing price expectations, according to several of the group's members. They were concerned that monetary policymakers might interpret the business sector's efforts to restore profit margins as a resumption of inflation, triggering a rise in interest rates. The prime rate is expected to drift down to an average of 10.1 percent in the second quarter of 1983 and to remain at that level before beginning to edge back up in the fourth quarter of the year. Moody's rating on Aaa-rated corporate bonds is expected to hover around 11 percent throughout 1983 and the first half of 1984. Given this background, participants were hopeful that monetary policymakers would tread a narrow path in 1983 to prevent a stalling of the recovery. Several of the group's members were concerned that monetary policymakers might interpret the business sector's efforts to restore profit margins as a resumption of inflation, triggering a rise in interest rates. Near-term tightening in money-market conditions, according to these economists, could lead to a peaking of economic activity as early as the fourth quarter of 1983. However, other economists argued that, unless growth of money stock slows soon, double-digit inflation could return by 1985.

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Economic Commentary

Economic Outlook for 1983

by Paulette Maclin and Joanne Bronish

Twenty-nine economists met at the Federal Reserve Bank of Cleveland this March to discuss the economy. Known as the Fourth District Economists' Round Table, this meeting produced a rather subdued economic outlook, indicating that 1983 would be a year of relatively slow recovery. The median of 29 forecasts anticipated real gross national product (GNP) growth of 4.1 percent over the year (fourth quarter to fourth quarter, compared with an average 6 percent increase in the first year of the six previous postwar recoveries). The expected growth, however, will not be distributed evenly among sectors; some industries that are important to the Fourth District economy, such as capital goods and primary metals, will recuperate more slowly. The Round Table economists also expressed concerns about the viability of the recovery beyond 1983. Monetary policy, interest rates, and inflation psychology are variables that add a great deal of uncertainty to the economic outlook. This Economic Commentary reviews the major factors shaping the Round Table's 1983 forecast, touching on some of the uncertainties for 1984 and beyond.

Sources of Recovery

According to the Round Table's median forecast, a swing in business inventories from liquidation to accumulation is expected to be a prime source of renewed economic expansion in early 1983. The Round Table's current forecast of inventory accumulation is greater than it could have grown during the October 1982 Round Table, largely because of the unanticipated record inventory liquidation that took place in the fourth quarter of 1982. The buildup in stocks in 1983 is expected to amount to about $10.5 billion, compared with liquidation of twice that size last year (see table 1).

Housing is another major sector of the economy that is expected to provide impetus to economic activity in the first half of the year. Residential construction expenditures could increase approximately 7 percent in each of the first two quarters, with overall growth of 23 percent for the year. While this is a stronger expansion than the group's median forecast last October, it

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remains within the bounds of past experience. Although recent declines in mortgage interest rates to about 12.8 percent have contributed to the improved housing outlook, several elements are still seen as constraining a housing recovery. Some forecasters believe further reductions in mortgage rates are necessary if the rebond in housing is to continue. Sluggish income growth, for example, will constrain housing demand. The Round Table economists view consumer spending as a moderately positive factor in the 1983 recovery. Real personal consumption expenditures (PCE) rose sharply in the final quarter of 1982, to a large extent reflecting lower interest rates and price incentives in the automobile industry. Similarly, the below-market automobile installment loan rates offered by major automakers testify to consumer costs to their highest annual rate since the third quarter of 1981. The improvement in housing sales also caused an increase in spending for household furniture and equipment, and, consequently, for consumer durable goods. This greater willingness to spend for apparel and other "soft" goods and services. Expenditures for fuel oil, however, weakened over the period because of unusually mild weather.

Because of atypically slow growth in real disposable income, the Round Table economists do not expect the large fourth-quarter 1982 increase in consumer spending to continue throughout 1983. Growth in real disposable income, which struck a floor at the final period of 1982, is expected to be about 3 percent (fourth quarter to fourth quarter in 1983). The projected incremental growth is similar to that achieved in the year following the 1980 cyclical trough, but it is well below the average 5.6 percent gain posted in the first year of previous postwar recoveries. The unusually slow growth expected in personal consumption expenditures and real disposable income in part reflects the persistently high rates of unemployment forecast for 1983. The Round Table economists, however, have been stronger than anticipated. In the first quarter of 1983, for example, new housing starts rose to nearly a 1.7 million unit annual rate. The Round Table economists view consumer spending as a moderately positive factor in the 1983 recovery. Real personal consumption expenditures (PCE) rose sharply in the final quarter of 1982, to a large extent reflecting lower interest rates and price incentives in the automobile industry. Similarly, the below-market automobile installment loan rates offered by major automakers testify to consumer costs to their highest annual rate since the third quarter of 1981. The improvement in housing sales also caused an increase in spending for household furniture and equipment, and, consequently, for consumer durable goods. This greater willingness to spend for apparel and other "soft" goods and services.

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remains within the bounds of past experience. Although recent declines in mortgage interest rates to about 12.8 percent have contributed to the housing recovery. Some forecasters noted that lingering doubts about the recovery, and about job security, combined with historically high real interest rates, could result in further increases in the personal saving rate and dampen the recovery in consumer durable-goods spending.

Because of atypically slow growth in real disposable income, the Round Table economists do not expect the large fourth-quarter 1982 increase in consumer spending to continue throughout 1983. Growth in real disposable income, which was negative in the final period of 1982, is expected to be about 3 percent (fourth quarter to fourth quarter) in 1983. The projected increase is similar to that achieved in the year following the 1980 cyclical trough, but it is well below the average 5.6 percent gain posted in the first year of previous postwar recoveries. The unusually slow growth expected in personal consumption expenditures and real disposable income in part reflects the persistently high rates of unemployment found in 1982, which some Round Table economists. Although most participants projected slow, but appreciable, gains in employment, they expected the unemployment rate to remain around 10 percent during 1983 and therefore to constrain consumer confi- dence.

In the first quarter of 1983, for example, new housing starts rose to their highest annual rate since the third quarter of 1981. The improvement in housing sales also caused an increase in spending for household furniture and equipment, and consumer durable goods. Expenditures for fuel oil, however, were flat over the period because of unusually mild weather.

The Round Table economists view consumer spending as a moderately positive factor in the 1983 forecast. Real personal consumption expenditures (PCE) rose sharply in the final quarter of 1982, to a large extent reflecting lower interest rates and price incentives in the automobile industry. Similarly, the below-market automobile installment loan rates offered by major automobile manufacturers decreased to the 9.5 percent range, which is typical for the first year of a new model. In their view, this liquid-ity that built into the money supply. In their view, this liquidity could result in further increases in the personal saving rate and dampen the recovery in consumer durable-goods spending.

The Round Table economists. Steel shipments expected for 1983 because of the strong recovery, according to the Round Table economists. Steel shipments were at their lowest levels since 1958, with an 18 percent to 20 percent increase in ship-ments expected for 1983 because of minimal growth in domestic steel consumption. The relatively mild increase in steel prices (currently, well below published prices), could result in another unprofitable year in 1983, according to some Round Table participants.

Three developments, however, could affect the cost-price relationship in the steel industry. First, the recent contract settlement with the United Steelworkers of America will aid producers in efforts to hold down production costs. Major concessions ap-pound the wage bill for union steel workers, including a freeze in cost-of-living payments until July 1984, and reduced vacation time. Second, various other cost-containment pro-grams also have been instituted. Administrative workers have taken a pay cut, and a persistently strong dollar in foreign-exchange markets are the major factors that will continue to provide strength to U.S. imports but weakness to U.S. exports. According to one Round Table participant, recent oil price declines also could weaken U.S. exports of capital goods to oil-producing countries.

Fourth District Industries

Steel, machine tools, and automobiles are three industries whose well-being is particularly important to the Fourth District. Some forecasters of these industries experienced severe declines in business during the recent recession; and each should experience an upturn according to the Round Table economists. Steel shipments were at their lowest levels since 1958, with an 18 percent to 20 percent increase in shipments expected for 1983 because of minimal growth in domestic steel consumption.

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remains within the bounds of past experience. Although recent declines in mortgage interest rates to about 10 percent during 1983 and throughout 1984 have a negative impact on domestic economic growth in 1983. The median fourth quarter forecast is PCE growth at about a 3 percent rate in the first half of 1983, accelerating slightly to nearly 4 percent over the second half. The Round Table economists expect PCE to expand approximately 3.5 percent from the fourth quarter of 1982 to the fourth quarter of 1983, compared with 4.5 percent to 7.0 percent in the first year of past recoveries. Some Round Table participants, however, expect an almost typical recovery in PCE, basing their forecast on the large real increase in consumer spending for household furniture and other "soft" goods and services. The unusually slow growth expected in personal consumption expenditures and real disposable income in part reflects the persistently high rates of unemployment forecast for 1983 by the Round Table economists. Although most participants projected slow, but appreciable, gains in employment, they expect the unemployment rate to remain around 10 percent during 1983 and therefore to constrain consumer confidence and spending.
and early retirement programs have allowed businesses to reduce the number of employees, causing a drop in total labor costs. Finally, many producers have focused on reducing the number of employees, causing a drop in costs. As a result of these efforts, businesses have been able to reduce their overall costs.

Monetary Policy and Inflation

Monetary policy will play a key role in shaping the 1983 outlook and in determining whether the expansion will continue into 1984 and beyond. The Federal Reserve Board's current monetary policy forecast indicates that this expansion will be achieved through moderate growth. However, monetary policy uncertainty for 1984 and beyond is expected to remain high. This uncertainty is due to the possibility of sustained economic growth in the early stages of recovery.

The possibility of sustained economic growth through 1984 would allow for a gradual increase in wages and salaries. However, the possibility of a strong expansion in 1983 is expected to be limited by the possibility of inflation. The Federal Reserve Board's current forecast indicates that inflation is expected to remain low in 1984. This is due to the expectation of a gradual decrease in the rate of price increases. The Federal Reserve Board's forecast indicates that inflation is expected to remain below 3% in 1984.

Economic Commentary for 1983

The Federal Reserve Board's median forecast for 1983 indicates that the U.S. economy is expected to continue its recovery. The recovery is expected to be driven by the anticipated increase in inventory accumulation, which is expected to be greater than the buildup predicted at the beginning of the year. The Federal Reserve Board's current forecast indicates that inventory accumulation is expected to be greater than the buildup predicted at the beginning of the year. The Federal Reserve Board's forecast indicates that inventory accumulation is expected to exceed the buildup predicted at the beginning of the year. The Federal Reserve Board's forecast indicates that inventory accumulation is expected to exceed the buildup predicted at the beginning of the year.

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Monetary Policy and Inflation

Monetary policy will play a key role in shaping the 1983 outlook and in determining whether the expansion will continue into 1984 and beyond, according to the Fourth District economists. The liquidity built into the economy during the latter half of 1982 and early 1983 is expected to support at least moderate economic growth over the year ahead. Moreover, it is anticipated that this expansion will be achieved with little or no acceleration in inflation in 1983. Price increases probably will occur in some key industries as firms attempt to restore profit margins, but other factors will moderate upward pressure on prices. Weakening oil prices, for example, have led several economists to scale down their 1983 inflation forecasts, even though they expect increases in natural-gas prices to offset partially the drop in oil prices. Moreover, a sharp rise in productivity usually slows the pace of price increases. The Round Table's median forecast, however, anticipates little further decline in interest rates. The prime rate is expected to drift down to an average of 10.1 percent in the second quarter of 1983 and to remain at that level below beginning to edge back up in the fourth quarter. Moody's rate on Aaa-rated corporate bonds is expected to hover around 11 percent throughout 1983 and the first half of 1984. Given this background, participants were hopeful that monetary policymakers would tread a narrow path in 1983 to prevent a stalling of the recovery. Several of the group's members were concerned that monetary policymakers might interpret the business sector's efforts to restore profit margins as a resurgence of inflation, triggering a rise in interest rates. Near-term tightening in money-market conditions, according to these economists, could lead to a peaking of economic activity as early as the fourth quarter of 1983. However, other economists argued that, unless growth of money stock slows soon, double-digit inflation could return by 1985.

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Economic Commentary

Economic Outlook for 1983

by Paulette Maclin and Joanne Bronish

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According to the Round Table's median forecast, a swing in business inventories from liquidation to accumulation is expected to be a prime source of renewed economic expansion in early 1983. The Round Table's current forecast of inventory accumulation is greater than they could have predicted at the October 1982 Round Table, largely because of the unanticipated record inventory liquidation that took place in the fourth quarter of 1982. The buildup in stocks in 1983 is expected to account to about $10.5 billion, compared with liquidation of twice that size last year (see table 1). Housing is another major sector of the economy that is expected to provide impetus to economic activity in the first half of the year. Residential construction expenditures could increase approximately 7 percent in each of the first two quarters, with overall growth of 23 percent for the year. This is a stronger expansion than the group's median forecast last October, it