The 1980s have been especially difficult years for industrial areas of the country. We have experienced an enormous transformation in our economies. Once-prominent industries have declined in absolute and relative importance. Under the pressures of competition, firms have been forced to alter operations and restructure facilities. Change of this sort is usually painful for the people and the communities involved, but if change is inevitable and leads to a better world, then much has been accomplished.

Here in the Fourth Federal Reserve District, the results of change are emerging, and two observations can be made concerning the future of our economy. First, the manufacturing sector will continue to be important, but will employ a smaller proportion of the labor force. Second, the service sector will continue to grow, as measured both by employment and output.

The service sector’s dramatic rise has not meant the deindustrialization of our region or the country, any more than the massive shift of employment from agriculture to industry at the turn of the century led to a loss of output in agriculture. Manufacturing will continue to be a basic component of our economy and the nation’s economy. In fact, it still claims roughly the same percentage of GNP that it did after World War II—a share that may well rise somewhat in the next several years as we close the trade deficit—even though its employment share has declined sharply.

Nineteen eighty-seven has been heralded as the “Year of Manufacturing.” Nationally, manufacturing output in 1987 rose by 5.7 percent over 1986, and manufacturing employment also rebounded. Last year, over 300,000 factory jobs were added, an increase of 1.6 percent. Although the increase last year was the largest since the early part of this expansion, it comprises only 11 percent of the 2.8 million jobs created between October 1986 and October 1987. The service sector, which claims 24 percent of the economy’s jobs, generated 1,045,000 jobs, or 37 percent of the total new jobs, over the same period.

These statistics tell us that manufacturing output continues to expand, but with fewer workers. The general shakeout in manufacturing experienced over the last eight years has resulted in a leaner, more competitive manufacturing sector. Productivity in the manufacturing sector has been rising at a rate of 3.5 percent per year since 1980—twice the rate of growth of productivity in the total business sector. Industries have made conscious efforts to modernize their facilities. According to recent surveys, new plant investment is being targeted more toward modernization than toward expansion. We expect the structural change that has been underway in our local economy to continue. In order to see continued positive results from this restructuring, we will have to see continued improvement in the productivity of our manufacturing sector and of our service sector. We are after all going to be forced to compete with other regions and countries in export markets for services.

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months are symptomatic of a deeper problem—a problem that I might characterize as growing uncertainty about the direction the market's inability to perceive a commi-
ment by economic policymakers to achieve a noninflationary economic growth.

The growth of federal debt slowed in 1987, but this reflected only a tempo-
rary change in the direction of fiscal policy. Following World War II, governments
reached consensus and made basic economic choices that included the
trade and open borders. Over the inter-
vening four decades, progress was
slow, to say the least. The revolution in
budgeting–monetary policy and the
trade deficit, however, was not driven by
to the point of affecting the pricing
of the entire range of domestic and
international financial assets.

From fiscal year to fiscal year, the fed-
eral debt in the hands of the public
swelled at about 15 percent annually
about twice as fast as national income.
The growth of federal debt slowed in 1987, but this reflected only a tempo-
rary change in the direction of fiscal policy. Whether the political budget
improvement in 1986 and foreign
exchange rates began to correct and
continue progress. Closing ourselves
off from foreign markets would produce
significant adverse impacts in capital
markets as well. While economic
growth remains a concern, it can and
will reflect the difficulties of action by
marking down prices of those
markets that remain unresolved.

A second issue contributing to uncer-
tainty in the economy is the risk of a
trade policy, and our trade imbalance.
Early in this decade, we reached a
workable consensus that the value of
the dollar was a matter best left to
the markets. We recognized that we did not know what the equilibrium
rate was and, mindful of the damage
done in the 1970s with inappropriate exchange rates, we also recognize
the dangers of attempts to control
prices designed to maintain an inap-
propriate exchange rate were detrimen-
tal to our domestic economy.

To meaningfully influence exchange
rates, policymakers have to make fun-
damental changes in monetary and fis-
cal policies. Surely we are moving
toward a more global economy. Never-
thless, international financial mar-
tests they perceive to be in their best
interest, regardless of prior commit-
ments. The political process through
which countries define and implement
policies is not a priority in international
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months are symptomatic of a deeper underlying problem—a problem that I might characterize as growing uncertainty over the stability of the dollar and the market’s inability to perceive a commitment by economic policymakers to achieve a noninflationary growth rate. After all, consumer prices did rise last year by 4 percent.

It seems to me that there are several major sources of uncertainty about economic policies. It is also obvious that many uncertainty issues were not resolved or even alleviated without resolving several fundamental issues—issues that have been long debated but that remain unresolved.

At the top of any list is the federal budget issue. Simply put, how large should government be and how will the services we demand of our government be paid for? It may well be that in some technical or theoretical sense the budget issue is not the root of some of our problems. For example, can be counted on to achieve and maintain price stability regardless of the budget. But where government becomes larger, it has, and government services are paid for with debt. If current issues have been less obscured by some market participants may suspect that pressures on the Federal Reserve to inflate that debt is now changing. The Federal Reserve has resisted such pressures over the past eight years of disinflation. But the political stance does change in any case. The Federal Reserve has been able to achieve more of its programs when it desires to financial markets, the issue of the day for policymakers. Setting and Stating Monetary Policy Objectives

Clarity of objectives and obtaining some degree of market support is the key to the success of the monetary policy process. The Federal Reserve should make its goals clear to the public. Setting, achieving, and maintaining clear objectives is necessary for policymakers to establish the clear objectives are necessary for policymakers to establish confidence in the market expectations, which is conducive to monetary policy success. The Federal Reserve can make a material contribution to the underlying problems will reemerge. In the long run. At the moment, the monetary policy impact on and response to short-run market conditions is foremost in our thoughts, but long-term challenges of the current policy process will require some thought. Markets will not allow us to forget these problems. They are assessing the likelihood of continued policy mistakes.

The October 19 crash reemphasized the reality that markets serve as a constraining force on economic policies. Ultimately, policymakers have little choice but to reexamine policies and attempt to alleviate some uncertainties. As policymakers reexamine policies, I recommend that they keep in mind two prongs to their policy decision. The first: inflation is a problem, not a solution. The second principle is as familiar as the underlying problems will reemerge. In the long run. At the moment, the monetary policy impact on and response to short-run market conditions is foremost in our thoughts, but long-term challenges of the current policy process will require some thought. Markets will not allow us to forget these problems. They are assessing the likelihood of continued policy mistakes.

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ECONOMIC COMMENTARY

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These statistics tell us that manufacturing output continues to expand, but with fewer workers. The general shakeout in manufacturing experienced over the last eight years has resulted in a recovery. Last year, over 300,000 factory jobs were added, an increase of 1.6 percent. Although the increase last year was the largest since the early part of the expansion, it comprises only 11 percent of the 2.9 million jobs created between October 1986 and October 1987. The service sector, which claims 24 percent of the economy’s jobs, generated 1,045,000 jobs, or 37 percent of the total new jobs, over the same period.

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by W. Lee Hoskins

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