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SUSTAINING ECONOMIC RECOVERY:
REMOVING THE OBSTACLES

Remarks by
Roger Guffey

President, Federal Reserve Bank of Kansas City

Harvard Graduate School of Business
Administration
68th AMP 6th Continuing Education
and Reunion Meeting
May 5-8, 1983
Dorado, Puerto Rico

Against the backdrop of historically high inflation and a stubborn recession in these recent months, we have seen quite a varied menu of economic developments. On the one hand there have been continuing declines in production and high levels of unemployment, which contributed to a 2 percent decline in GNP for last year. On the other hand, we've seen vigorous upsurges in stock and bond markets, and a major lessening of inflationary pressures. (Good News - Bad News)

To be sure, the economic headlines in 1982 made disappointing reading, tracing as they did the economy's dismal performance. As you know, high interest rates brought on by years of inflation affected many key sectors of the economy. The bellwether housing and auto industries declined further, and business capital spending was extremely weak as the second recession in three years rippled through the economy.

The human dimensions of the business downturn were reflected in the rise in unemployment throughout the year. ~~Even~~ *which we have thought in the past to have* ~~communities like Wichita, with traditions of stable divorce~~ *as a nation,* ~~operation, were not exposed.~~ *Price* We were paying a high ~~cost~~ to wring inflation from the economy.

Yet, in the face of such a deep recession, some long-awaited indications of economic recovery have recently ~~become~~ *begin to appear.* apparent.

Among these welcome signs are the so-called leading economic indicators--including the stock market--which have been positive nearly every month since mid-1982. Underlying trends suggested by these indicators were confirmed when declining inflation, together with weakness in business activity, prompted a general decline in interest rates during the second half of 1982.

Declining ^{interest} rates, in turn, have encouraged a rebound in housing and auto sales, (two of the most interest-sensitive ~~parts~~ *sectors* of the economy. January housing starts were up 38 per cent, and auto sales have remained fairly strong ^{up 16% in april over a year ago.} Furthermore, industrial production grew strongly last month, retail sales were positive, and the unemployment rate ^{begin to} declined.

Although these favorable economic developments certainly brighten the prospects for business recovery, many people are understandably ^{rather} gun-shy ~~now~~. Many question the economy's ability to sustain ~~the~~ ^a recovery through 1983 and into future years. Given the critical importance of sustained economic growth to the nation,

would like I ~~want~~ to discuss this question with you briefly today from two *different* perspectives. First, I want to consider the near-term outlook, (1983 *& into* 1984)

and indeed to the world

and second, I want to examine ^{the} prospects for sustaining U.S. economic health over the longer term. — *through the 1980s*

In assessing the economy's staying power in 1983, I believe one of the most encouraging trends is the substantial progress that has been made in restraining inflation. As you know, the 3.9 per cent rise in the ^{*Consumer Price Index*} CPI in 1982 was the smallest annual increase in a decade. In January, ^{*and again in March*} the producer price index actually declined, and in real terms, the price of oil—a most important economic ingredient—^{*also*} has been declining.

These welcome trends on the price front also are having a favorable effect on cost structures throughout the economy. We have seen lately that a significant byproduct of slower inflation — is a slower rise in labor costs and an increase in labor productivity. (*up 4.8% in Q1 1983*)

These price and productivity trends, in my judgement, are helping ^{*To*} establish a healthy ^{*foundation*} ~~base~~ for ^{*the*} 1983 economy. So, too, is the generally lower level of interest rates. Reflecting these lower rates, ^{*/*} interest-sensitive industries like homebuilding and automobiles and other durable goods, are likely to show additional gains this year. With increasing sales, ^{*/*} businesses are likely to rebuild inventories, ^{*/*} spurring production levels and ^{*hopefully*} employment. Additional stimulus also will ^{*come*} ~~flow~~ from Federal government spending, particularly for defense goods.

While these factors certainly will work in favor of sustaining the economic recovery in 1983, there are indeed, some question marks. ^{*For example,*} Some observers suggest that continued high

unemployment and weak personal income prospects cloud the outlook for ^asustained recovery. I ^{would} agree that consumer spending may not be overly strong under these circumstances. Another concern is that business capital investment may continue to be weak and ^{therefore} provide little economic stimulus in 1983.

Another problem area for 1983 is ^{the} U.S. exports. ^{picture,} The worldwide recession and a strong dollar resulted in a major deterioration in the nation's ~~net exports~~ ^{markets} during 1982. Given the current weakness in foreign economies, and the still high value of the dollar, [/]export demand is not likely to turn around quickly.

Many of you undoubtedly have been concerned about the health of the international financial system. Widespread public attention has been focused in recent months on the deteriorating financial positions of many international borrowers--particularly ^{the} developing countries. Slowing worldwide economic growth left many of these borrowers exposed [/]and raised questions about their ability to repay ^{their} debt. Despite the high visibility of this problem, ^a ~~I believe that~~ ^{many have} official efforts now under way are serving to ease this problem considerably.

Through responsible cooperation with the International Monetary Fund, a number of countries are taking ^{the} necessary steps to put their affairs in order. As a result, major international lenders are developing confidence that orderly economic adjustments will occur.

Moreover, lower worldwide interest rates and improving economic conditions should ease pressures on both lenders and

*That are
in place or*

borrowers. In my judgement, the programs now on stream are likely to bring needed confidence to international financial ~~affairs~~ ^{markets} and diminish the effects of international financial problems on ~~the~~ ^{our} domestic economy in 1983.

A key ingredient in the 1983 outlook and for the sustainability of economic recovery through the year is Federal Reserve monetary policy. What are the Federal Reserve's intentions in 1983? Should the public be concerned that--as one former Fed chairman put it--the Federal Reserve will take away the punch bowl just as the party really gets going?

As background for understanding the Federal Reserve's policy intentions, you should know that the Federal Open Market Committee looks for about 4 per cent real economic growth ^{to be sure & slow rate} this year. Moreover, we believe, as a group, that the 1983 inflation rate will be below the 5.6 per cent rate in the GNP deflator anticipated by the Administration.

*This is historically the case
for the first year of recovery.*

The Federal Reserve's intentions for 1983 were set forth in mid-February when Paul Volcker met with the Congress to discuss the FOMC's agreed-upon targets for money and credit growth. He reaffirmed the Federal Reserve's objectives ^{- that is -} to maintain progress toward price stability while providing the money and liquidity necessary to support continued economic growth.

To achieve the objective of moderate noninflationary expansion in 1983, it is clear that the Federal Reserve cannot be bound by rigid rules of monetary growth, but rather must pursue these goals with a ^{more} flexible policy. Such a policy will permit us to

look beyond the varied impact of financial deregulation on money growth, for example / and to deal more realistically with unusual or unanticipated financial developments. The 1983 monetary target ranges established in connection with such a flexible policy are in some cases wider and higher than in 1982 ~~targets~~, particularly for the widely followed and distortion-prone aggregate, -M-1.

In my view, the Federal Reserve's intended approach to monetary policy in 1983 will help to insure that an appropriate level of money and credit will be available to support moderate noninflationary expansion in business activity.

On balance, then, after weighing the most significant economic variables, I believe that the economy's forward momentum can and will be sustained through 1983.

Against the background of these optimistic assumptions for 1983, I want to turn now to consider the economic outlook over the longer-term perspective. What can be done to insure that the current favorable developments in the economy can be translated into sustainable economic performance over the longer run?

I believe the answer to that question might read like this: The chances for sustained expansion are certainly good if we remember the painful lessons of inflation and also address the major obstacle to long-term economic progress, ^{that} ~~which~~ is the massive deficit position for years to come in the Federal government's budget.

I am convinced that we have the opportunity now to make the current turnaround a long-lasting period of expansion because the

harsh lessons of inflation have become apparent to the American public. ^{The public} ~~We all~~ understand, now that the inflationary excesses of the past two decades distorted our economic decisions and led to recurring recessions. Even worse, -lost jobs and lost production undermined faith in our system and weakened confidence in the future. Some repairs ^{to the public's} confidence have been made recently, but there is much more to do.

Thus, as we consider the sustainability of long-term expansion, we can draw strength from recent evidence of fundamental lessening of inflationary pressures. This development is extremely important because diminished inflation is a necessary precondition for permanent recovery. Precisely because the nation has come so far in the battle with inflation, resolving the problem of the large and growing federal budget deficits has become ^{absolutely} critical. In my judgement, this is the most serious obstacle to our nation's long-term economic health.

The dimensions of the prospective deficits for 1983 and beyond are staggering and may not be fully understood by the American public. As you may know, the Office of Management and Budget now is forecasting a \$208 billion deficit this fiscal year. Even greater deficits may occur in future years unless significant adjustments are made. A major portion of the deficit this year will be related to recession-caused shortfalls in revenue / or / increases in spending. But a significant part of the deficit ^{that} this year will be structural in nature; ^{I mean by that term, a portion of} ~~it~~ would exist even ^{the deficit} if the economy were operating at full employment. What disturbs

me most is that the structural deficit is expected to grow in future years, given existing spending and revenue laws now on the books. This will happen even if the economy recovers and the recession-related part of the deficit narrows.

Not only are the prospective deficits large by absolute standards, they are growing larger relative to GNP. To illustrate, back in the Eisenhower years, the deficits--when they occurred--averaged about 1/3 of one per cent of GNP. Twenty years later, during the Carter administration, the deficit averaged about 2 per cent of GNP. Current administration projections show deficits at 6-7 per cent of GNP, or ^{Perhaps} slightly less with a strong economic recovery.

But it is not simply the scale of the prospective deficits which is ~~the~~ ^{at} issue, but rather the potentially negative impacts on business growth, the financial markets, and the public psychology.

Because budget deficits must be financed by borrowing in credit markets, massive ongoing deficits pose a serious threat to prospects for sustained economic expansion ^{over the longer term.} As business expands, private sector credit demands from businesses, farmers, and home buyers may well collide with the government's financing needs, raising again the specter of "crowding out." Moreover, as both public and private credit demand grows, the likelihood of rising interest rates increases, as well. Although credit demands appear manageable this year, rising interest rates later on might discourage ^{Private} the borrowing needed ^{required} to finance a continuing recovery. Another very important negative factor related to

financing the deficit is that potential "crowding out" problems and rising interest rates--if they occur--would raise public fears about renewed inflation. Such rising inflationary expectations would surely weaken the foundation for recovery which has been laid.

As we all know, fundamental solutions to the deficit dilemma are developing very slowly in Washington because of sincere differences about the nation's priorities. Until those differences are resolved, the deficit issue will remain front page news. ^{also,} ~~Too~~, so long as the stalemate persists, we probably will hear ideas which ^{tend to act as} ~~are~~ smokescreen and ^{thereby} delay the decisions which must be made.

For example, some observers have suggested that the Federal Reserve could solve the deficit financing problem--and help the economy sidestep possible "crowding out"--by simply creating more money. This solution, which is tantamount to monetizing the government debt, will only add to public concern about future inflation and rising interest rates. It is quite clear to me that excessive expansion of money is not the answer to massive federal deficits--or to any economic problem, for that matter. While excessive money growth may bring temporary short term, ^{short term} benefits, such as lower ^{short term} interest rates, such action will ^{inevitably} ~~almost~~ contribute to higher inflationary pressures and higher interest rates over the long run.

We in the Federal Reserve believe that the economy has come ^{too} far in the fight against inflation, and has paid such a high

price to reach this point, that it would be irresponsible for the Federal Reserve to foresake such important gains in order to to ~~validate~~ ^{monetize the} federal budget deficits.

This view does not signify Federal Reserve insensitivity to broad public needs. Rather, I mean to emphasize and reinforce the Federal Reserve's long standing commitment to a credible course of ~~moderate~~ ^{Moderate} ~~growth~~ growth in money and credit which will support a continuing noninflationary economic expansion.

As for making the difficult but absolutely critical decisions that will resolve the budget stalemate, I have no easy answers, ~~though~~ ^{the} alternatives seem clear. We can cut spending or we can increase revenues, or we can do some of both. Deciding where to cut spending or how to increase revenues is not ^{within} the province of the Federal Reserve. Such decisions are political in both the partisan sense and as related to the will of all Americans. At its heart, it seems to me, the budget deficit issue is a referendum on the ^{size and the} role of government in our society. And the sooner this issue is resolved, the clearer will be the economic outlook.

In closing, I am encouraged about the sincerity and intensity of the public debate over the budget deficits. Given this debate, I am very hopeful that our political processes will soon produce the appropriate solution--one which will enable our economy to move forward with renewed confidence on a path of sustainable growth. ^{for years into the future - the 1980's}
^{and beyond.}

Non Farm Sector - productivity
QI 1983 - 4.8%

- ∴ Downward pressure
on Unit labor cost & prices

- Collective Bargaining Contracts
negotiated QI - 1st year
wages fell (-1.4%)
- down from 7.3%

- Annual wage gain over
life of K 2.2% down
from 5.4%

QI Real Emp. - 3.1%

(as result of reduced rate of ^{unemployment} liquidation

- QI - Currency increased
at 13.2% annual rate

CPI - LAST 12 mos - 3.5%

unemployment ^{march} 10.1% - 10.3%

Retail Sales
Nov. 2.3
Dec -1.1
8 - -0.5
7 - -1.2
m +1.3

10.8% in Dec

Industrial production

M - +1.1
F - +0.3
J - +1.5
D - +0.2
N - -0.7

Hourly state
wage 1.6%

M - -9.2
F - +4.8
J - +33.8
D - -13.0
N - +26.5

Consumer price index

M - +0.1
F - -0.2
J - +0.2
D - -0.3
N - +0.1

Producer Price

M - -0.1
F - +0.1
J - -1.0
D - +0.2
N - +0.6

Capacity Utilization ^{march} 69.4%

HARVARD GRADUATE SCHOOL OF BUSINESS ADMINISTRATION

KIRBY CRAMER, President
CRAIG R. SMITH, Vice President
DONALD C. KORB, Treasurer
CHARLES L. LUEBBERT, Secretary

68TH AMP

SIXTH CONTINUING EDUCATION AND REUNION MEETING

DATE: May 5-8, 1983

LOCATION: Cerromar Beach Hotel, Puerto Rico

Planning Committee: Gene Branscum, Jim Morrison, Joe Deckert and Don Kipley

April 15, 1983

Saludos!

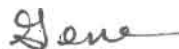
This is just a reminder about some of the arrangements for the reunion. We will be at the Cerromar Beach Hotel, Dorado, Puerto Rico. The convention manager we've been working with is Teresa Mejias. The telephone number is (809)796-1010. The Telex number is 3859758. The first planned activity is the "Welcome Cocktail Party" on May 5, at 7:00 p.m. and the last short meeting is Sunday the 8th at 9:00 a.m.

Earlier arrivals and later departures are subject to the availability of rooms at the hotel. Please call Terri Anderson at Smyer Travel Service if you have any last minute requests. The number is (316)221-4856.

There are several forms of transportation available to you from the airport to the hotel and you are on your own when you arrive.

Helen and I are certainly looking forward to seeing all of you and after a winter that's still hanging on here, we're anxious for some fun and sun!

Sincerely,



Gene Branscum

P.S. Enclosed is a pamphlet about the Cerromar.

25 MAR 83 8:23

PRESIDENT

JAMES L. MORRISON
7348 ELDORADO STREET
MCLEAN, VIRGINIA 22102
(703) 821-3406



March 22, 1983

TO: THE SPEAKERS - 68th AMP 6th Continuing Education & Reunion Meeting
May 5-8, 1983 Cerromar Beach Hotel, Puerto Rico

Roger

Mr. Speaker:

With your indulgence I will write to you as a group - and a grand group you are. Plans are made for the upcoming meeting and we are looking forward to it with great anticipation.

As some of you know Gene has planned a welcoming "get-together" with cocktails and hors d'oeuvres for Thursday evening, May 5. There is to be a group dinner on Friday evening. Our education sessions are from 9:00 a.m. to 11:00 a.m. on Friday and Saturday and our business session will begin at 9:00 a.m. on Sunday morning. Afternoons are for the activities of your choice.

Enclosed is the flyer that went out with Gene's letter of February 18, 1983. I have just learned that David Marlow will not be able to be with us due to a recent development that presents a direct conflict in schedule. Otherwise all speakers are holding firm so far as I know.

I suggest that Jesse Markham be our keynoter and lead off Friday a.m. and be followed by Roger Guffey. On Saturday I would suggest that Jeff Smith start the ball rolling and that our panel then carry on with all that has been presented as backdrop for a free-wheeling discussion.

If you have questions and/or counter suggestions let me hear from you.

See you in Puerto Rico.

*So glad you will be with us. I am ready for a rest.
This retirement is tiring.*

Be looking for you.

Jim

ECONOMIC UPDATE.....1983

The downbeat has been given for the start of an economic recovery in the United States.....businessmen (and women) are wildly enthusiastic about the prospects for the future..... politicians are enthusiastically wild about the prospects for 1984..... and the 68th AMPers are going to learn how much of the above is true, if they attend the 6th Continuing Education and Reunion Meeting in May in Puerto Rico. Our program at that meeting is not limited to the U.S. but will provide views and opinions of the world, by the world and for the world. No small task, but then we have no small speakers.

Featured will be Professor J. W. Markham, speaking on a large blackboard. Welcome back Jesse. Our presidential timber panel will consist of financial wizards and business tycoons of the corporate and the entrepreneurial types..... Al Graf, Bud Klauser, Mac Pullon and David Marlow. And we are going to have with us a star of the Federal Reserve System, Roger Guffey. His topic will be "A View of Domestic and World Economy from the point of view of a member of the Federal Reserve System." The devil's advocate brigade roster is being made up now and will include each and every Meeting Participant, i.e. you.

*RM
to write
own
speech*

Also joining us again this year will be Jeffrey Smith who was with us in New Orleans. General Smith will update his report on the world situation as he sees it from the perspective of a career military man whose present position with the Ethyl Corporation in Washington, D.C. gives him an added dimension as a speaker to be heard today.

So that's the program.....the nuts and bolts of it, as Al Graf would say. You all come. See Al's new threads. Mercy sheiks alive it is going to be sometheeng, I theenk. Hasta la vista.

Jim Morrison

HARVARD GRADUATE SCHOOL OF BUSINESS ADMINISTRATION

22 FEB 83 AT 51

PRESIDENT

KIRBY CRAMER, President
CRAIG R. SMITH, Vice President
DONALD C. KORB, Treasurer
CHARLES L. LUEBBERT, Secretary

68TH AMP

SIXTH CONTINUING EDUCATION AND REUNION MEETING

DATE: May 5-8, 1983

LOCATION: Cerromar Beach Hotel, Puerto Rico

Planning Committee: Gene Branscum, Jim Morrison, Joe Deckert and Don Kipley

February 18, 1983

TO MEMBERS OF THE 68th AMP.....

Well, we're getting close to deadline time. Looks like it's going to be a good group, with 22 couples firm, but still some on the fence. March 5 is our cut-off date. If you have not already sent your room deposit, please send \$140.00 to Smyer Travel Service, Inc., 120 S. Summit, Arkansas City, KS 67005. After that date we can't promise we can get a reservation for you.

A short outline of the activities planned--Thursday evening, a welcoming "get-together"--cocktails and hors h'oeuvres. Friday, the group dinner. The education sessions will be from 9:00 a.m. to 11:00 a.m. on Friday and Saturday and a very short meeting beginning at 9:00 on Sunday morning. Afternoons will be free time for tennis, the beach, golf, sight-seeing, etc.

Schedule

Enclosed is a copy of a letter from our program director, Jim Morrison, and I know you'll agree the program looks great.

Please give me a call at 316/221-2230 if you have any questions.

Sincerely,

Gene

Gene Branscum

*2-11-83
check for \$140
to Smyer
Travel Service
for reservations*

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Jim Morrison

FEDERAL RESERVE BANK OF KANSAS CITY
KANSAS CITY, MISSOURI 64198

February 11, 1983

Smyer Travel Service
120 South Summit
Arkansas City, Kansas 67005

Gentlemen:

We enclose check in the amount of \$140 for room deposit for Roger Guffey at the Cerromar Beach Hotel near San Juan, Puerto Rico in connection with the meeting of the Harvard Graduate School of Business Administration on May 5-8.

Sincerely,

A handwritten signature in cursive script that reads "Glenda Hewitt". The signature is written in dark ink and is positioned below the word "Sincerely,".

Secretary to
Mr. Guffey

3 DEC 82
- PRESIDENT

HARVARD GRADUATE SCHOOL OF BUSINESS ADMINISTRATION

KIRBY CRAMER, President
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68TH AMP

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DATE: May 5-8, 1983

LOCATION: Cerromar Beach Hotel, Puerto Rico

Planning Committee: Gene Branscum, Jim Morrison, Joe Deckert and Don Kipley

December 1, 1982

GREETINGS TO ALL MEMBERS OF THE 68th AMP

The time for our Sixth Continuing Education and Reunion is fast approaching. The hotel requires that we make a one night deposit to be assured that they will hold the rooms for us.

The 1983 room rate at the Cerromar Beach Hotel is \$140.00 per night, double occupancy, Modified American Plan (including breakfast and dinner). This rate does not include hotel service charge, bellman gratuities, and 6% Puerto Rico Government room tax. The deposit required is \$140.00. This rate is based on two people sharing a room. Cancellations are subject to a one night cancellation fee.

I am working with a travel agency who is assisting me in coordinating travel plans. Please make your deposit check in the amount of \$140.00 payable to Smyer Travel Service and mail directly to them at 120 S. Summit, Arkansas City, Kansas 67005.

In order to obtain the best schedules and airfare, I have asked the travel agency to block a number of seats both from New York and Miami to San Juan on May 5th. Return seats from San Juan to Miami and New York are blocked for May 8th.

I have enclosed a form with information needed by the travel agency if you would like them to assist you in securing transportation to San Juan. Please return this form with your deposit remittance. NO

We would appreciate your immediate attention to sending the one night deposit since we must send these deposits to the hotel by December.

Gene Branscum

Enclosure

1-3-83
will not attend
JP

no
no

Smyer Travel Service, Inc.

HEAD OFFICE:
316-442-9270
120 SOUTH SUMMIT
ARKANSAS CITY, KANSAS 67005

WINFIELD BRANCH:
316-221-4857
908 MAIN
WINFIELD, KANSAS 67156

1. Do you wish to use our block air space? NO
2. If so, which gateway city do you prefer? N/A
3. Passenger names: N/A
4. Do you wish us to book connecting flight? NO
5. If so, from what city? N/A
6. Do you wish to upgrade to 1st class travel? N/A
7. Do you wish to upgrade to Business class? N/A
8. For seating purposes, are you a smoker? N/A
9. Do you prefer window or aisle seats? N/A
10. Payment by credit card:

For those who wish to travel on their credit card, please fill out the information below:

Credit card name: _____

Name of cardholder (as imprinted): _____

Account number: _____ Expiration: _____

Signature: _____

