Talk By

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economy would be better off without. Legitimately concerned with these wrenching, disproportionate effects on the different sectors of the economy, Congress moved discretely last September, when it passed an interest ceiling bill. There is, however, no assurance that this will be the case next time around. Legislative remedies may cure the patient--but they sometimes shorten his life.

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If ~~I have spent a good deal of time~~ talking about 1966, it is only in ~~part because I believe we have just come through a time pregnant with meaning for the future~~. I~~t is also in part because~~ I dread talking about the unknown, 1967, which, though, is what I foolishly promised I would do at the time of invitation ~~outset of these remarks~~. The truth is that I know no more about what is left of 1967 than you do. I sometimes get the uncomfortable feeling that, as a Federal Reserve official, I am endowed by my friends (and enemies) with a great gift of prophecy and that my casual remarks about coming economic events are given great weight. If you knew me as I do, you would appreciate why this makes me acutely nervous. Like the above, an economic guess about this year is in the wind--no one knows good.

For some little while now, as you know, the Federal Reserve has been working toward greater monetary ease. And for the obvious reason. Inflationary pressures have become less strong. Of course, the recent marked decline in interest rates is not entirely the System's doing. The private sector's appraisal of 1967 has changed. Most importantly, the President's call for a tax rate increase triggered expectations of greater monetary ease and, in consequence, interest rates declined. Still, the System has done its part. And happily, I would add. Whatever our critics may say, we did not enjoy 1966. This is most clearly revealed by the promptness with which the System moved to a policy of greater monetary ease.

But it would be quite wrong to interpret the recent decline of interest rates and the increase in credit availability as signaling a recession. In the Federal Reserve anyway, the dominant expectation would seem to be that the end of 1967 will find the economy growing more rapidly again. This is what Chairman Martin told the Joint Economic Committee of Congress in his appearance of a couple of weeks ago. And apparently the Administration is also expecting the present slow-down to be only temporary. Otherwise the President would hardly have proposed his 6 per cent surtax.

With an economic outlook more optimistic than pessimistic, it is perhaps not to be expected that interest rates will decline a whole lot further. As I have emphasized, we have already had a dramatic decline in rates. But beyond this, what can one say. The difficulty, apparent enough, is that what the Federal Reserve does in coming months must depend largely on what the Congress does and what monetary authorities in other countries do. In matters of taxation, the President proposes, but the Congress disposes. And since the President has made his proposal, it is up to the Congress how much freedom for maneuver the System is going to have.

In some lesser measure, it is also up to the monetary authorities in other countries to decide how much freedom the System shall have. Our government could go further than it has in directly controlling international flows of funds, but our present network of controls allows for the free movement of short-term funds. In consequence, the differential between monetary conditions here and abroad still influences considerably our balance of payments position. Witness what happened in 1966, when a massive inflow of Euro-dollars gave us a slight official settlements surplus.

Actually, the dollar has never enjoyed greater confidence than it does today. But to maintain confidence, we have got to be watchful of our

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international payments position. It could dissolve in a return to larger deficits.

For good or bad, the Federal Reserve is therefore limited by world monetary conditions. We have lately witnessed a marvelous instance in monetary cooperation. In concert, Germany, the U.K. and the U.S. have worked toward lower interest rates. But whether domestic conditions in the several countries will remain such as to allow the effort to continue is not easily foretold.

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~~I am aware of having been of little help on what the future holds. For this, I have already offered my apologies. I do hope, though, that I have made some small contribution to your understanding of why the System has behaved as it has. This is what I most wanted to do, for as I indicated when I began these remarks, the Federal Reserve does need your thoughtful support. And I might add, your thoughtful criticisms. Both, though, require understanding of what the System has been trying to do and why.~~

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Declines in orders are widespread among durable manufacturers, including machinery, and especially orders for metal cutting and forming tools which in January were 40 per cent below a year ago.

Autos. Daily average sales of new domestic automobiles continued to weaken in the first 20 days of February. Assuming this tendency continues through the remainder of the month, the seasonally adjusted annual rate for February will likely be about 7.3 million units, 7 per cent below the 7.8 million unit rate for January and about one-fifth below the 9.2 million unit rate a year earlier.

The automobile industry's planned output curtailments in February, along with severe snowstorms and a wildcat strike at the General Motor's Fisher body plant, seem to have stopped the recent expansion of inventories of new cars at about 1.5 million units. Output for the entire month of February is expected to be at a seasonally adjusted annual rate of about 6.5 million units, down at least 10 per cent from the preceding month and 30 per cent below a year ago. With a sales rate of 7.3 million units, the seasonally adjusted inventory level at the end of February would be slightly less than at the end of January. In relation to this year's lower sales rate, of course, stocks are considerably above a year ago.

Prices of used cars remained virtually unchanged in January at the lowest point in the last four years.

Consumer credit. Consumer instalment credit continued to grow at a slow rate in early 1967. Preliminary January data for

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commercial banks, however, suggest a little faster rate than in December but slower than in the fourth quarter as a whole. ~~On this~~ basis, and in ~~light of recent auto and~~ other sales information, we project the ~~first quarter expansion at $4.0 billion, annual rate.~~

INCREASES IN CONSUMER INSTALMENT CREDIT
(Seasonally adjusted annual rate, billions of dollars)

	Extensions	Repayments	Net Change
1965			
Q1	72.5	65.1	7.4
Q2	74.4	66.4	8.0
Q3	76.8	68.5	8.3
Q4	77.8	70.0	7.8
1966			
Q1	78.9	71.7	7.1
Q2	78.6	72.3	6.3
Q3	80.0	73.4	6.6
Q4	78.4	73.9	4.6
1967			
Q1 (est.)	~~78.0~~	~~74.0~~	4.0

To a large extent, the pattern of credit use last year paralleled developments in consumption expenditures. The second and fourth quarters of 1966, for example, were periods of relative slack in consumer spending, especially for autos and other durable goods, and they were periods of slow growth in consumer credit as well. The low point for the year was reached in December when the increase in outstanding credit was at the lowest annual rate in four years ~~when the increase in outstanding credit was at an annual rate of $3.9 billion, the smallest in more than four years~~. For 1966 as a whole, t~~he increase in instalment~~

~~credit amounted to $6.1 billion, sharply less than the record $8 billion for 1965.~~ Expressed in percentage terms, last year's increase was a little less than 9 per cent, compared with a rise of more than 13 per cent in 1965 and increases of 10 per cent or more for all previous years of the current expansion.

Much of the sluggishness in consumer credit has been and continues to be associated with slow sales of autos. But demand for personal loans and repair and modernization loans also has been slow. The only area of strength has been in "other consumer goods", and this probably reflects the inclusion in this category of an ever-widening group of consumer items purchased on revolving credit plans.

The gap between new credit extensions and repayments on old debt has narrowed. Credit extensions were running at a $79 billion annual rate early in 1966, they topped $80 billion briefly in the summer months, and then they backed off again toward the end of the year and apparently are continuing downward in the current quarter. In the meantime, repayments expanded from an annual rate of just under $72 billion in the first quarter to nearly $74 billion in the last and are estimated at about that rate in the current quarter.

Consumer buying plans. Consumer buying intentions have continued to weaken in recent months according to the Census quarterly survey in mid-January. The proportion of households expecting to purchase new automobiles, household durables, and houses were all below a year ago. Declines in intentions to purchase new automobiles and houses began to show up in the surveys in the third quarter of last year, a quarter later than the initial downturn in actual reported purchases.

Intentions to purchase new automobiles within the next 12 months fell to 9.4 perccent of reporting households from 9.8 per cent a year earlier. Intentions to buy used cars, however, were 8.0 per cent in mid-January as compared with 7.4 per cent a year ago.

Reported intentions to purchase new or previously occupied houses within 12 months decreased to 4.6 per cent in the current survey from 5.3 per cent in January 1966. There was also a decline in intentions to purchase one or more of 7 major household durables: from 23.7 per cent to 22.7 per cent, with plans to buy television sets down the most.

The proportion of households with higher incomes than last year declined for the second successive quarter. Expectations for higher incomes in the next year, however, were up sharply: 27.3 per cent expected their incomes to be higher, as compared with 25.8 per cent a year ago. These optimistic income expectations appear to contradict the restraint indicated in buying plans, since respondents with higher income expectations also typically report higher intentions to purchase new automobiles.

Nat'l Park forecasts
travel [illegible] is + 7%
3% price
4 1/2 % real.
no change in spending habits
Yosemite
travel is up - especially off-season -
Oct to 2/28 - up 7% in unit
spring bookings substantial
Yellowstone -

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THE ECONOMIC PICTURE IN DETAIL

The Nonfinancial Scene

~~Gross national product. We have revised downward our projection of GNP for the first half of the year--estimating increases of only $5 billion in the current and second quarters, as compared with gains of $14 billion in the fourth quarter and, on average, throughout 1966. Despite a projected slowing in prices from last year's large advance, real growth during the first half would be negligible--at an annual rate of only 0.5 per cent a year.~~

~~We still are expecting a sharp fall-off in the rate of inventory accumulation--reversing last year's large run-up--but there is not much evidence that it has begun to any great extent. The projected moderate strengthening in final sales also is not yet evident and, in fact, final sales now appear a little weaker than was estimated four weeks ago, particularly consumer demands for goods.~~

Retail sales in January and February appear to have shown little change from the reduced December level, with new domestic car sales declining from an annual rate of 8 million units in December to about 7.3 million in February (a fifth below the exceptionally high year-earlier level). Sales of household durable goods also appear to have edged down over the period. In mid-January, consumers' future buying plans for durable goods, as reported by the Census Bureau, remained on the weak side, although the intentions data do not necessarily imply further decreases in consumer takings from recent reduced levels. Altogether, we are now estimating a decline of $2 billion in the annual rate of consumer purchases of durable goods in the current quarter, and with nondurable goods estimated to rise only $1 billion, consumers' total dollar spending for goods--which was virtually unchanged between the third and fourth quarters--is expected to decline slightly in this quarter. In real terms, consumer takings of goods appear to have declined moderately since last fall--after showing only a moderate increase after early 1966. Consumer spending on services, however, apparently continues to expand rapidly--although much of the dollar gain is being accounted for by price increases. ~~Total consumption expenditures are projected to rise $3.3 billion in the current quarter--as compared with a little more than $4 billion in the fourth quarter.~~

They have the money -

Meanwhile, consumer income showed a surprisingly large rise in January--with wages and salaries, transfer payments and other income up by sizable amounts; despite the boost in social insurance contributions effective January 1, the January rise in personal income was the largest since last August.

Manufacturing employment and wages and salaries rose further in January. However, in February manufacturing employment is expected to decline. With weakness in manufacturing, a distinct slowing of the rise in total employment is projected. The increase in minimum wage rates effective February 1 is presumably adding about $1 billion to wage and salary disbursements and sizable wage rate increases are expected to continue, but, with employment gains slowing markedly, the rise in total wages and salaries is projected at a much slower rate in coming months. ~~Moreover, the rise in transfer payments, which has~~ been very sharp ~~since the~~ institution of ~~Medicare last July, is likely to taper off.~~

Reflecting mainly the larger than anticipated January rise in wages and salaries, the estimated levels of personal and disposable income have been revised upward appreciably for the first quarter. Disposable income now is estimated to show an increase of $10.5 billion in the first quarter, and with consumer spending projected as rising only about $3.5 billion, the saving rate is projected to rise sharply further to 7.0 per cent--the highest rate since late 1958.

A further increase of only $5.5 billion--about half the first quarter rise--is projected for disposable income in the second quarter, and consumer spending is believed likely to rise about in line with the increase in income. The projected rise in consumer spending--while smaller than was estimated four weeks ago--is somewhat larger than the increase now estimated for the current quarter, owing mainly to the likelihood that durable goods purchases will tend to level off following earlier declines. Nondurable goods purchases are expected to continue upward at a slow rate, while service outlays should show a large further gain. It now seems likely that the saving rate will remain high, probably at about the 7.0 per cent level.

In the second quarter, we are now anticipating some upturn in residential construction activity--in line with gains in seasonally adjusted housing permits and starts reported through January--and we

Some specific numbers might be useful to you -

~~Autos~~

~~Consumer credit~~

What does all this add up to for 1967? At this point in the year, no one can speak authoritatively. Key to this year will be the American consumer. If it ever stops snowing, raining, or flooding depending on where you live in the northern half of the U.S., and the American consumer returns to his old spending habits, we may see ~~vigorous~~ an ~~year~~ ~~in the~~ upward trend in the business indices that will take us out of the year 1967 at growth rates designed to please everyone.

Residential construction and autos will be the indicators of consumer changes - ~~Let~~ us hope that warm weather will arouse either the nesting urge or the travel desire again in the American consumer — but ~~not~~

in deference to your credit men — not simultaneously, in the same individuals.

CONFIDENTIAL -- FR

March 1, 1967

GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Expenditures and income figures are billions of dollars
seasonally adjusted annual rates)

	1965	1966	1966				1967 Projected	
			I	II	III	IV	I	II
Gross National Product	681.2	739.6	721.2	732.3	745.3	759.3	764.3	769.3
Final sales	672.1	727.7	712.3	720.0	735.4	743.1	752.8	764.3
Personal consumption expenditures	431.5	464.9	455.6	460.1	469.9	474.1	477.4	482.6
Durable goods	66.1	69.3	70.3	67.1	70.2	69.6	67.7	67.5
Nondurable goods	190.6	206.2	201.9	205.6	208.1	209.2	210.4	212.0
Services	174.8	189.4	183.4	187.4	191.5	195.3	199.3	203.1
Gross private domestic investment	106.6	117.0	114.5	118.5	115.0	120.0	115.6	110.2
Residential construction	27.8	25.8	28.6	28.0	24.8	21.9	21.9	22.4
Business fixed investment	69.7	79.3	77.0	78.2	80.3	81.6	82.2	82.8
Change in business inventories	9.1	11.9	8.9	12.3	9.9	16.4	11.5	5.0
Nonfarm	8.1	12.2	8.5	12.1	10.4	17.6	12.0	5.0
Net exports	7.0	4.8	6.0	4.7	4.2	4.1	5.0	6.0
Gov't purchases of goods & services	136.2	153.0	145.0	149.0	156.2	161.1	166.3	170.5
Federal	66.8	76.9	71.9	74.0	79.0	81.7	85.1	87.5
Defense	50.1	60.0	54.6	57.1	62.0	65.5	68.3	70.3
Other	16.7	16.9	17.4	16.9	17.0	16.2	16.8	17.2
State & local	69.4	76.2	73.1	75.0	77.2	79.4	81.2	83.0
Gross National Product in								
constant (1958) dollars	614.4	647.8	640.5	643.5	649.9	657.2	657.7	658.6
GNP Implicit deflator(1958=100)	110.9	114.2	112.6	113.8	114.7	115.5	116.2	116.8
Per cent change, annual rate								
GNP current dollars	7.8	8.6	9.5	6.2	7.1	7.4	2.6	2.6
GNP constant dollars	5.9	5.4	5.9	1.9	4.0	4.4	0.3	0.5
Implicit deflator	1.8	3.0	3.6	4.3	3.2	3.1	2.4	2.1
Personal income	535.1	580.4	564.6	573.5	585.2	598.3	610.0	616.5
Wage and salaries	358.4	392.3	380.0	387.4	396.7	405.0	413.0	418.0
Disposable income	469.1	505.3	495.1	499.9	507.8	518.4	529.0	534.5
Personal saving	25.7	27.0	26.7	26.6	24.5	30.4	37.3	37.3
Saving rate (per cent)	5.5	5.3	5.4	5.3	4.8	5.9	7.0	7.0
Total labor force (millions)	77.2	78.9	78.1	78.4	79.1	79.8	80.4	80.6
Armed forces "	2.7	3.1	2.9	3.1	3.2	3.3	3.4	3.5
Civilian labor force "	74.5	75.8	75.2	75.4	76.0	76.5	77.0	77.1
Unemployment rate (per cent)	4.5	3.8	3.8	3.8	3.8	3.7	3.8	4.0
Nonfarm payroll employment (millions)	60.8	63.8	62.8	63.6	64.1	64.8	65.3	65.5

Note: Labor force revised to exclude persons age 14 and 15. Quarterly data for 1966 also reflect new seasonal factors; projections for 1967 reflect new definitions of unemployment.

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Net Acquisition of Financial Assets by Households
(seasonally adjusted annual rates)

	1964 IV	1965 I	1965 II	1965 III	1965 IV	1966 I	1966 II	1966 III	1966 IV
Demand Deposits & Currency	13.9	6.3	.9	6.1	15.4	-1.9	-2.7	-1.6	7.9
Savings Accounts									
At commercial banks	11.2	13.5	9.8	15.8	13.9	11.3	13.0	12.4	10.9
At savings institutions	15.2	13.3	12.3	13.2	13.6	9.7	4.1	5.1	10.7
Total	26.4	26.8	22.1	29.1	27.6	20.9	17.1	17.5	21.5
Reserve -- Life Insurance & Pension Fund	16.2	15.0	16.4	16.1	15.4	17.3	15.3	17.5	17.4
Cr. & Equity Mkt. Instr.	1.0	-3.0	11.7	3.8	-1.9	13.8	18.3	15.3	-1.3
TOTAL*	52.3	39.9	47.9	51.1	52.3	45.1	43.5	44.0	40.0
Disposable Income	446.6	453.2	461.0	476.2	486.1	495.1	499.9	507.8	518.4
Ratio -- Net Acquisition of Financial Assets to Income	11.7	8.8	10.4	10.7	10.8	9.1	8.7	8.7	7.7
Ratio -- Net Acquisition of Savings Accts. to Income	5.9	5.9	4.8	6.1	5.7	4.2	3.4	3.4	4.1

* Includes net investment in noncorporate business in addition to items listed.