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Statement of

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before the

Joint Economic Committee

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A YEAR OF RECESSION AND RECOVERY

Mr. Chairman:

When I testified before your Committee last year, on behalf of the Federal Reserve Board, economic activity in this country was receding. Contraction in output and employment was general. Unemployment was rising at a disturbing pace. No one could be sure how far downward adjustment would go, or how long it would last.

We pointed out then that, with the exception of the catastrophic recession of the thirties, every moderate cyclical decline since World War I had been checked in the course of a year. It was further emphasized that many forces were present in the economy that were favorable to eventual recovery. But at that time we did not know, nor did we then expect, that vigorous recovery would so soon be in full swing, and that contraction from 1957 levels of activity would be shorter in duration than most preceding economic recessions.

Even while the Committee's Hearings were going on, some were beginning to view the outlook more optimistically. In January, corporations, taking advantage of easier conditions and lower interest costs in financial markets, were offering an increasing volume of new issues in anticipation of future needs for funds, and to refund shorter-term debt. State and local governments were bringing to market bond issues that were deferred earlier, and were stepping up the pace of bond offerings to provide for public works.

Farmers continued to foresee favorable output and price conditions in agriculture and were bidding up further the prices of farm land. Bankers, with slackened customer demand for credit and with strengthened reserve positions, were bidding more aggressively for assets. By February, bankers were accelerating expansion of the assets and deposits of their institutions, thus increasing more rapidly the economy's stock of cash balances and raising its over-all liquidity.

Within a matter of weeks following last year's hearings, personal income and consumer spending had ceased to decline and, in fact, showed modest recovery. Production and employment soon after resumed an upward trend. Whether these developments, though encouraging, foreshadowed wide revival in activity was not known at the time; not until the June-July period did the current flow of information and reports provide substantial confirmation that general economic recovery was actually under way.

From that stage on, currently available data, reflecting trends in markets, production, and employment, showed that recovery was both broadly based and vigorous. Pickup in employment, however, lagged behind that of output as is usual in early phases of cyclical upswing. At the year end, eight months after recovery set in, the level of total output in the economy approximated that prevailing at the output peak of 1957.

Recovery has been so rapid and widespread as to indicate that the revival phase of the economic cycle has by this time probably run its course.

The economy has reattained its prerecession level and now appears to be entering a phase of resumed economic growth.

Federal Reserve Action to Combat Recession

This brief review of changing levels of economic activity during 1958 provides a backdrop for specific comments about Federal Reserve policy and action over the past 16-month period of recession and recovery.

As reported to you last year, Federal Reserve policy began to shift in a counter-recession direction in late October and early November of 1957. About that time, the System directed its open market operations to supplying reserves more liberally to the banking system. It also reduced the discount rates on member bank borrowings from the Reserve Banks. As the stream of factual information verified the emergence of recessionary trends, Federal Reserve actions and policies became more aggressive and discount rate, open market, and reserve requirement instruments were actively applied in complementary fashion to foster ease in credit markets and encourage bank credit and monetary expansion.

From late fall 1957 through April 1958, there were four reductions in Federal Reserve Bank discount rates, from 3-1/2 per cent to 1-3/4 per cent. Through continuing open market operations from late fall of 1957 to early last summer, the Reserve System supplied the commercial banks with some $2 billion of reserve funds. Through three successive reserve requirement reductions in late winter and early spring of last year, the System released for the use of member banks about $1.5 billion of their required reserves.

The total amount of reserve funds supplied by the System to commercial banks over the nine months, November 1957-July 1958, was enough to enable member banks to reduce their discounts at the Reserve Banks from $800 million to about $100 million, to offset sales of gold to foreign countries amounting to about $1.5 billion, and to finance a commercial bank credit expansion of almost $8 billion. Monetary expansion from February through July stimulated by this Federal Reserve action was at an exceptionally rapid rate--at an annual rate of 13 per cent for all deposits, including time and demand deposits. For the active money supply; that is, demand deposits and currency seasonally adjusted, the rise was at an annual rate of 8 per cent. After the shift in Federal Reserve policy in the summer, expansion in the active money supply slackened, and for the year as a whole it amounted to about 3-1/2 per cent.

Broader Effects of Monetary Action

Although the immediate impact of Federal Reserve policy was on commercial banks, it clearly had broader effects upon the economy generally. For one thing, since commercial banks are direct participants in some degree in all important credit markets, expansion in bank lending and investing activities intensified competition among all lenders for the acquisition of the available supply of credit-worthy loans and securities. This worked to reduce the cost of financing to borrowers generally -- businesses, farmers, consumers and home buyers, and all levels of government. It also widened access of all potential borrowers to credit funds.

Another effect of the credit ease was a greater willingness on the part of banks and other lenders to make new loans to business customers and to renew outstanding credits. This facilitated the orderly run-off of excess business inventories accumulated in the preceding boom. It also furthered the completion of business programs of plant and equipment expansion begun in that period. With a $6 billion reduction in business inventory holdings and a significant cutback in fixed investment programs since recession began, it is perhaps remarkable that business loans outstanding declined only $1 1/2 billion in the year ending September 1958. The ability of businesses to maintain their bank borrowing and also to borrow more readily in capital markets not only cushioned downward pressures on investment spending but helped many companies to minimize cutbacks in their working force and payrolls, to maintain dividends, and to strengthen liquidity positions.

In housing markets, the easier conditions broadened the availability of mortgage funds. Discounts were reduced on FHA and VA mortgages subject to ceiling interest rates, and interest rates on new conventional mortgages also fell. As bank credit expansion gained in momentum, banks participated in mortgage investment more actively than at any time since the boom housing year of 1955. The increased availability of mortgage funds at lower cost, together with the maintenance of personal income, was promptly reflected in a step-up of builder activity in constructing new houses.

In the consumer instalment credit area, the increased availability of funds made it possible for lenders to meet sound demands for credit more readily, thus bolstering lagging demand for consumer durable goods. On some transactions, terms were eased and, in addition, new credit plans were developed and extended. Easier credit conditions permitted lenders to be more liberal in granting renewals and extensions of time for repayment of outstanding credit. Thus, the volume of repossessions and credit losses was less than would otherwise have been the case, with benefits to both borrowers and lenders.

Increased availability of funds also had an important impact on State and local government financing and spending. In many cases, the lower cost of financing encouraged States and municipalities to borrow in order to finance capital projects. In a few cases, lower market rates enabled local governments that had a legal ceiling on permissible interest rates to return to the market. The increase in spending by State and local governments from the summer of 1957 to the summer of 1958 was a billion dollars more than in the corresponding period of the preceding year.

These observable effects of easier monetary conditions which developed from efforts to combat recession were, of course, important and salutary. They are not to be overly stressed, however, for monetary action is always only one element in Government counter-recession policy. In turn, Government policy is always only one element in the total economic scene. Businesses, individuals, and State and local governments, in the light of their own circumstances, were taking actions to adjust and adapt their situations and to redirect their energies. Their actions undoubtedly shaped the recovery and gave it momentum.

Changing Expectations

Achievement of monetary ease to combat recession so promptly and amply was not without its problems. One of the most acute was the build-up of prices in the bond market as speculators counted on continuing business recession, credit ease, and still higher bond prices. Psychological reactions and expectations always play a role in swings in economic and financial developments, but were of particular importance in financial markets last summer as the economic outlook changed from one of a continuing recession to one of early, vigorous recovery.

At that time, the improved economic outlook led to a sharp change in expectations in regard to renewed inflationary pressures and a turnabout in the trend of interest rates. A much larger Federal deficit loomed up than had been estimated, as well as the crisis and threat of military action in the Middle East. Concern about the drain of gold from the nation's monetary reserves through sales of gold to the industrial nations of Europe was a further cause of uncertainty. The fact that the Canadian Government announced a major refunding operation at sharply higher interest rates was also a complicating factor.

In these circumstances, heavy market sales by holders of U. S. Government securities in anticipation of higher interest rates sharply depressed bond prices. Initially, this selling stemmed from temporary holders who had bought in anticipation of a continued rise in Government security prices. Some of these holdings had been acquired with funds borrowed on thin margins in connection with the Treasury's June financing operations. In many cases, selling was forced because the margins vanished as security prices declined.

Prices of Government securities continued to decline under pressure of steady liquidation and the reluctance of investors to purchase market offerings in view of changed prospects for credit demands and inflationary threats. On July 18, the Federal Open Market Committee concluded that the market situation had become disorderly and decided to intervene temporarily in the medium- and long-term sectors of the Government securities market. This action was within the framework of the Committee's established operating rules. From July 18 to July 23 the System purchased $1.2 billion of securities involved in a Treasury refinancing and a small amount of other notes and bonds.

Thereafter, as market conditions became more orderly, no further Federal Reserve open market transactions were effected outside the usual area of short-term Government securities. During late July and early August, sales of Treasury bills by the System together with other factors that absorb reserves more than offset the large volume of reserves supplied to the market by Federal Reserve intervention in the Government bond market.

Shift in Federal Reserve Policy

By this time, there was clear evidence in current statistics that recovery in economic activity and production, though not yet in employment, had gained considerable momentum and was likely to go forward without serious setback. Moreover, in view of the strength of consumer demand, further decline in business inventory holdings and capital outlays was no longer likely. Monetary policy was now reinforcing the existing foundation of productive activity and preparing the economy for a new advance.

About this time, inflationary expectations began to spread. The abrupt upward shift of interest levels in central money markets, while precipitated by liquidation of speculative positions in Government securities, reflected investor demand for an interest premium to cover the risk of a depreciating purchasing power of invested funds. It was accompanied by a significant shift in investor allocation of newly available funds to common stocks instead of fixed interest obligations, with hedging against inflation a frequent explanation of the change in investor policy. Large current and prospective demands for credit by the Federal Government, State and local governments, and home purchasers, also influenced the rising cost of borrowed funds. In the stock market, the volume of trading was expanding rapidly and the rise in stock prices carried the yields on common stocks below the yields on bonds of the same companies.

Developments in our financial markets, as well as the very large deficit which the Federal Government was facing, were occasioning concern, abroad as well as at home, about the future of the dollar. The extent of concern among foreign financial leaders was clearly evident last fall at the annual meeting of the International Bank and Monetary Fund at New Delhi, India.

In the light of the rapidly changing economic situation, in many ways highly encouraging but with inflationary and speculative psychology spreading, the Federal Reserve, during the summer, began to moderate the policy of credit ease with a view to tempering the rate of bank credit and monetary expansion.

System open market operations after midsummer supplied only a portion of the reserves needed to meet rising credit demands and to offset the reserve drain of a continued gold outflow. As a result, member banks were obliged to draw down their excess reserves and to increase their borrowings from the Federal Reserve Banks. Such borrowing was made more costly when Reserve Bank discount rates were raised in the late summer from 1-3/4 per cent to 2 per cent, and at mid-fall when they were again raised to a level of 2-1/2 per cent.

Since last summer, bank credit and the money supply have continued to expand but at a rate much reduced from earlier in the year. Some seasonal expansion in business loans was supplemented by a rapid growth of real estate loans. On the other hand, bank holdings of short-term U. S. Government securities rose only moderately despite a substantial increase in their supply to finance the Treasury's deficit. With business sales and liquidity showing rapid rise, the higher interest rates that developed in the market helped to attract a substantial volume of funds of nonbank investors, especially business corporations, into the purchase of the new short-term Treasury issues. As a consequence, the Treasury was able to finance most of its deficit outside the banking system, and at the same time banks were able to meet private credit demands accompanying economic recovery, with only a moderate further growth in total bank credit and money.

Regulation of Margin Requirements

In addition to its broader monetary responsibilities, the Federal Reserve is directed by law to prescribe margin requirements to guard against excessive use of credit for purchasing or carrying stock market securities. By providing a means of dealing directly with this volatile type of credit, margin requirements serve as a special-purpose supplement to the general instruments of Federal Reserve action. Since the flow of credit into the stock market fluctuates with general business conditions, changes in margin requirements are usually correlated with policy actions that affect general credit availability.

Following the stock market decline in the early fall of 1957, total credit to customers for purchasing and carrying stock market securities declined by about 5 per cent and was back to about the level outstanding in mid-1955. With this indication of abatement of credit use in the stock market, the Board of Governors, early in January 1958, reduced the required margin from 70 to 50 per cent.

With the increasing activity and rise in stock prices accompanying economic recovery, stock market credit rose sharply, reaching by July a level about 20 per cent above the volume at the beginning of the year. In view of the rapid rise in credit to finance trading in or temporary ownership of stocks and the emerging investment psychology favoring purchase of stocks as an inflation hedge, the Board, early last August, restored the required margin to 70 per cent. As outstanding stock market credit continued to rise following this action, the Board, in mid-October, raised the required margin to 90 per cent.

The Current Situation

The shift in monetary policy during the fall aligned monetary expansion more closely with the developing potential of the economy. Consumer spending on durable goods and housing continued to expand and was reflected in high levels of output of household durables, in a pickup in production of 1959 autos, and in a rise in new housing starts to one of the highest levels in recent years. Business inventory policies were switching from liquidation towards accumulation, and there was a widespread, though small, upturn in capital expenditures. At the same time, Federal, as well as State and local government spending, was expanding rapidly in accordance with budgetary authorizations adopted earlier.

In financial markets moderate curtailment of credit availability and higher interest rates served to dampen speculative excesses then developing, to restrain and spread out the volume of new corporate and municipal security financing, and to facilitate the financing of the large Federal deficit outside the banking system. The restraint of corporate and municipal security financing followed some anticipatory borrowing by these issuers earlier in the year when long-term interest rates were lower. At the turn of the year, business capital financing was again rising, and there was a large calendar of authorized but unissued State and local government securities.

Total economic activity, measured in real terms, has regained its earlier peak. The active money supply has increased by about 2-1/2 per cent above the prerecession level, and holdings of other liquid assets, including time deposits, are up sharply. The financial basis for further growth is established. While economic prospects are generally favorable, there are several areas -- unemployment, exports, prices, and Federal finance -- that are matters for continuing concern.

Despite the rapid recovery in production and sales, unemployment remains disquietingly high. The lag in employment is in part the result of a marked increase in productivity. The present availability of capital and manpower resources represents a potential for near-term growth of the economy without inflation. As output of goods and services expands in response to growing demands, opportunities for employment should increase as they have in past periods of economic expansion.

In exports, which declined sharply until early last year, recovery has not yet set in. The export decline was largely in materials and fuels and was due in part to the ending of boom conditions abroad; resumption of economic expansion is now beginning in industrial countries abroad and eventually there should be some improvement in foreign demand for our exports. It is significant, however, that the European countries which announced a broader convertibility for their currencies at the end of 1958--and other countries too--are giving our exports of manufactures stiff competition in price and quality, and these countries are now able to devote a larger share of their resources to their own exports than they could in earlier postwar years. While this reflects progress towards international balance, our producers need to adjust to these competitive forces abroad if they are to share in growing world markets.

Prospects for our international payments position thus merge with the third problem; that is, our price system. A market economy such as ours depends upon the price mechanism to allocate resources by reflecting the interplay of demand and supply. The price mechanism cannot do its job of efficient resource allocation in accordance with the changing demands of consumers unless there is some flexibility in individual prices. This does not mean that wide swings in the general price level are desirable. The price paid by Smith represents the income of Jones. But there is cause for concern when, in spite of a decline in the demand for his product, Jones raises his price, and an opportunity to stimulate both output and employment is thwarted. This is particularly disturbing when it comes on top of a price rise that Jones made when the demand for his product increased. Such a one-way movement of prices--whether it is explained as demand-pull, cost-push, or both -- is not compatible with an efficient market system. If it were to be continued, it would pose a serious threat to the otherwise favorable prospects for healthy growth in consumption and production.

Now as to Federal finances, it is essential at this stage of the economic cycle that the Government should attain a balanced budget and then achieve some surplus as economic advance continues. Whatever the desirable level of expenditures, deficits, while justified in time of recession, should be avoided when economy is at a high level of activity.

It is also of vital importance to have a healthy, broad-based Government securities market that enables the Treasury to lodge its debt outside the banking system. In other words, the Treasury must be able to compete effectively and flexibly with other borrowers for the available supply of savings.

Appropriate debt management policies, while contributing to financial stability, are in turn dependent on such stability. Investors cannot be induced to purchase fixed income securities if they fear a steady erosion of the purchasing power of the dollar.

The banking system has an important role to play in aiding the Treasury's financing. This role involves assistance in the broad distribution of securities and, in accordance with the volume of reserves made available and the meeting of essential private credit demands, the retention by banks of that portion of the Government debt that is consistent with stability of the dollar. Resort to financing Government deficits through the banking system entails the creation of new supplies of money rather than the use of existing funds. In a period of high economic activity, this is a high road to monetary inflation. There can be no effective control of inflation if the banking system is made the major source of funds to finance government deficits.

Government Policies and Economic Growth

As the United States economy emerges from the recession of 1957-58, it seems likely, if past experience is a guide, that we are on the threshold of a new period of economic growth. This is an opportune occasion, therefore, to consider the question of appropriate public and private policies to foster steady expansion of the economy.

Economic growth is a principal objective of governmental policy in every country of the world. The rate of growth is widely accepted as an indicator of the performance of an economy. A word of caution is in order, however, regarding the very difficult task of measuring growth. Growth measurements, particularly when they cover long periods of time and comparisons of one country with another, are necessarily approximations. They vary with a host of factors, including the scope of activities covered, both public and private; the character of such activities; quality as contrasted to quantity of output; and many others. Nevertheless, regardless of these measurement difficulties, growth estimates, properly constructed and interpreted, can be useful aids in appraising economic performance.

Desirable economic growth goes beyond increases in line with a growing population and labor force. It involves a rate that makes possible rising living standards through increasing consumption per capita for present and future generations. This requires increasing output per worker; that is, higher productivity through advancing technology.

In our economy, consumption takes the form mainly of consumer purchases of the goods and services supplied in free markets by private producers and merchants. Our living standards also encompass services provided by the various levels of government. Fundamentally, economic growth at a more rapid rate than population increase is the response of men to their ever-increasing wants.

Among the other reasons for seeking economic growth is the importance of demonstrating to the world that free economies under democratic political systems can outperform regimented economies under dictatorial political systems in providing high and rising living standards for all of the people.

Economic progress, however, cannot be measured merely by percentage increases in the quantity of output. Also at stake is the opportunity to live as free men, the responsiveness of the productive system to the desires and tastes of consumers, the quality of goods and services, the degree of leisure and opportunities for using it in a satisfying way, and our willingness to aid other nations seeking similar advantages. These aspects of our economic performance will have a great influence on how the rest of the world judges the merits of free versus regimented economies.

Economic Growth Without Inflation

When we consider the influence of governmental policies on economic growth, it is useful to distinguish between two related aspects of the process. First, growth involves expanding capacity to produce goods and services. Second, it involves expanding demands for goods and services at a rate sufficient to utilize the expanded capacity.

The first aspect of growth--an expanding output potential--depends upon such basic factors as additions to the labor force, advancing technology, and a flow of savings combined with a desire and ability on the part of producers to use them in the creation of a growing stock of modern plant and equipment. The other aspect of growth depends upon a balanced expansion in demands for final product by the major sectors of the economy--households, businesses, governments at the State and local as well as the Federal level, and demands from abroad.

For growth to be sustainable, an equilibrium between these two sides of growth must be maintained. If total demands do not keep up with the output potential, over-all growth will slacken, for the inducement to business to add to productive capacity will lessen. If total demands tend to run ahead of the output potential, the general price level will begin to rise and this, in turn, will have an adverse impact both on growth of demands and on means of financing increased and improved capacity. It will also have adverse effects on the efficiency with which resources are utilized; likewise, the equity or fairness with which final products are distributed in markets among consumers, businesses, and savers.

What then is the function of monetary policy in relation to these two aspects of growth? In general, it is to attempt to provide credit and monetary resources and an atmosphere in financial markets conducive to the basic growth factors. At the same time, aggregate demand for goods and services should expand in close relation to the capacity to produce.

On the demand side, growth basically depends on spending out of incomes earned in the production of goods and supplying of services. Monetary policy facilitates the expansion of money holdings, through sound credit expansion, consistent with the growing capacity of the economy to produce without inflation.

On the supply side, basic growth factors are the labor force, technology, and investment of savings. Growth of the labor force is to some extent influenced by over-all demands, but more generally by population growth, age distribution, and social customs. Technological progress and the desire to save and invest savings productively are influenced by the monetary environment. An atmosphere of price and financial stability in general is necessary both to the incentive to save and to rapid technological advance. Thus, through continuous efforts to safeguard the value of the dollar and to create a climate of financial stability in which savers can have confidence in the future value of their investments, monetary policy makes a contribution to economic growth quite apart from its influence on demands for goods and services.

It is for these reasons that price and financial stability is essential to the achievement of maximum economic growth. We have had a fairly good growth record over our history, but we have had too much instability in our levels of employment and prices. A major problem is to moderate this instability so that the losses in employment and output of recession periods will not depress our longer-term rate of growth. Currently there is widespread concern about the danger of renewal of inflationary trends. The Federal Reserve shares that concern. To point to dangers in this situation is not to forecast inflation. Public and private actions appropriate to present circumstances can prevent these dangers from materializing.

Among potential inflationary factors first, perhaps foremost, is the budgetary position of the Federal Government. As the economy moves up toward more intensive utilization of its productive resources, it is essential that deficits give way to surpluses. There is no mystery about this source of danger. If the will exists, the way will be found. It clearly lies in adaptation of Federal expenditure and tax policies in order to produce a budgetary surplus in prosperous times.

Second, there are the problems arising from the so-called cost-push inflation which is part of a spiral process stimulated by demand pressures. In the period ahead there is a strong prospect that demands will continue to expand. In these circumstance, we must recognize the dangers both of wage increases in excess of productivity growth and of price increases beyond what the traffic will bear. Business and labor leaders have a paramount responsibility to the general public as they make wage and price decisions over the coming year.

Then there is the easy acceptance of the idea that a little inflation is not seriously harmful. The experience in the government bond market, to which I alluded, is a vivid example of the influence of inflationary expectations in financial markets. To the extent that such attitudes come to be reflected in decisions on wages, prices, consumption, and investment, they help to bring about their own realization.

These are the major reasons for concern about the possible development of inflationary pressures. To be fully aware of a danger, and to face up to it, is not to despair or to capitulate, nor does it mean being blind to other national needs, including sustained economic growth.

The Federal Reserve System will continue to the best of its ability to contribute, so far as it can, to continuing prosperity and economic growth, without inflation. Such decisions as it must make within its particular province manifestly are not enough to assure attainment of the national objectives to which we all subscribe. What this Congress decides, what management, labor, agriculture and, indeed, the public generally decide to do will win or lose the battle against debasement of the currency with all of its perils to free institutions.

The state of the nation tomorrow -- its progress and prosperity -- rests with the decisions of today.

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ECONOMIC ADVANCE AND HIGH UNEMPLOYMENT

Employment gains have lagged output gains in this recovery, as they usually do. The lag, however, has been greater than in preceding postwar recovery periods, and the level attained by unemployment has been both higher and somewhat more sluggish in its response to rising activity. Thus, while real GNP and industrial production are currently both within striking distance of earlier highs, nonfarm employment--up 700,000 from its recession low--has regained less than a third of its recession loss of 2.4 million jobs.

Since September, there has been little evidence of any extensive general rehiring of workers other than for seasonal reasons. In the two preceding postwar recession-recoveries, employment stabilized for a number of months after the recession bottom, but once recovery set in, employment increases were not halted until a new peak was reached.

What accounts for the slower pickup in employment in this cycle than in preceding postwar cycles? Several factors may be mentioned.

(1) Productivity increases in manufacturing industry have apparently been higher this time than in the earlier recovery periods, reflecting very high modernization investment in preceding boom as well as the greatly expanded industrial research and development programs of the boom period. For instance, automobile output in December, while only 4 per cent lower than in December 1956, provided one-fifth less in production worker employment than two years earlier. The railroads, while carrying about as much freight as in late 1957, provided 10 per cent

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A Federal Reserve Board staff paper presented for the record of the Joint Economic Committee by Chairman Martin at a hearing February 6, 1959.

less employment. Similarly, the coal mines have been about equalling output levels of a year ago with about 15 per cent fewer employees.

The larger productivity gains of this recovery period may also be a factor in recent stabilizing of average hours of work per week in all manufacturing industry. Virtually all of the recession decline in hours worked had been recovered by last September and there has been no further gain since. In earlier postwar cycles, hours of work continued to increase long after this stage of recovery. It is important here to note that, since 1955, there seems to have been a downward drift in the length of the workweek.

(2) It may well be that labor cost increases of recent years have made management more cost conscious than in any earlier period and that greater efforts are now being applied to limiting employment and overtime increases in order to keep costs down. Also, postwar growth in fringe benefits now makes record-keeping costs and benefit liabilities rise rapidly as new workers are hired, and this would operate to slow down management decisions to add to work forces.

(3) In machinery and other industries associated with investment outlays, employment has shown little recovery rise because expansion in fixed investment has not yet shown marked revival. In the past, expansion of nonproduction worker employment, associated especially with research and development, has been correlated with rising investment. In the preceding two cycles, business investment had shown much more revival than has been shown up to the present point in this cycle.

(4) Nonmanufacturing employment, which had shown strong growth through the whole postwar period, with only modest slackening of expansion in the two preceding downturns, declined moderately in this recent recession and has shown little expansive tendency in recovery. Judging by the rise in nonindustrial GNP since last spring, perhaps as sharp or sharper productivity gains have been experienced in nonmanufacturing activities as in manufacturing industries during this recovery period. Presumably these nonmanufacturing activities are digesting earlier postwar increases in their working force.

(5) The industries in which recession declines in employment have been highest and greater than in preceding recessions have been durable manufacturing, railroads, and mining. These industries have been subject to a secular decline in postwar years in employment of semi-skilled workers, with reductions in semi-skilled jobs more accentuated in each succeeding recession-recovery period. This means, of course, a sizable problem of transfer of employment to other gainful activities, a problem that can be only resolved slowly.

With the rise in employment opportunities lagging, that is to say, showing slower advance than in preceding postwar recoveries, what about the unemployment problem and prospects over the months ahead?

Unemployment has been higher all through this recession-recovery period than in earlier postwar cycles. It reached a seasonally adjusted high of 7.5 per cent of the labor force in the summer and declined to about 6 per cent subsequently. In numbers of unemployed, the decline has been about 1 million workers.

While unemployment has been higher than in preceding cyclical dips, the general pattern of rise and decline has not been dissimilar to that of preceding cycles. The seasonally adjusted unemployment did not fall below 4.5 per cent of the labor force in the 1949-50 recovery until about 12 months after recession ebb, and in the 1953-54 recovery this rate was not pierced until after 10 months. In the Korean boom, the unemployment rate fell to under 3 per cent, but in the 1955-57 boom, 4 per cent constituted a floor and most of the time the rate fluctuated just above 4 per cent.

In the two earlier postwar recoveries, employment rose and unemployment declined at the same time that sizable additions were being made to the working force. In the recent recession, part of the rise in unemployment was due to the large number of secondary earners who entered the working force when primary earners had their pay reduced or lost their jobs. The recent decline in unemployment has reflected in part withdrawal from the work force of many of these secondary earners as well as withdrawal of some older and younger workers for want of job opportunities.

Recovery in job opportunities has been uneven for different groups of workers. Younger workers have generally faired better than older workers, and females better than males. Relatively high rates of unemployment persist for durable goods workers, semi-skilled and unskilled workers, and for nonwhite workers. Among those with long duration unemployment, durable goods workers, miners, and railroad workers are numerous in relation to their role in the labor force.

Recovery re-employment has also been uneven geographically. In California, employment has returned to prerecession highs. In Michigan, it has fluctuated only seasonally and unemployment is currently well above last year's rates. At midsummer, the number of substantial surplus labor markets was 89 out of 149, and by the present month the number of such markets had declined by only 13. The concentration of substantial surplus markets continues to be in the east and midwest.

Two observations about current labor market conditions seem warranted from this review. First, on the supply side, a conjuncture of secular and cyclical forces seems to have contributed to the present volume and composition of unemployment. As we have noted, a high proportion of the unemployed is concentrated in durable goods and related industries, making the continuing unemployment problem a cluster of localized problems rather than a general problem. But this may also work to make unemployment slack linger on. The terms "technological unemployment" and "labor immobility" undoubtedly will be used more frequently again to describe a possibly slower decline in the unemployment rate than featured the earlier cycles. However, given appropriate job opportunities, the American worker has been extremely mobile in adopting to new occupations and new conditions.

Second, on the demand side, the labor market in the recent period has, on the whole, been experiencing a less vigorous demand for labor than in the comparable phase of the other postwar cycles. But as consumption expenditures rise further and as capital expenditures begin actively to expand, demand for labor will surely strengthen, and particularly in the durable goods areas where unemployment is now concentrated. Gains in worker productivity are typically high in the recovery phase of the cycle and then slow down in the expansion phase. Gains in output in the expansion phase increasingly require utilization of older facilities and these facilities take more manpower per unit of output.

How fast available manpower resources will be taken up in the period ahead depends on the pace of further expansion in aggregate demand and especially of durable goods demand and on the strength of competitive responses, especially price response, in meeting additional growth in demand. If expansion in money demand is dissipated in price advance, the employment impact will, of course, be lessened.

Taking into account the relatively larger pool of unemployed manpower at this stage of the present cycle compared with earlier postwar cycles, it seems reasonable to observe that manpower availability will not become a limiting factor on the further increase in total production nearly so soon as it did in the two preceding cycles.

If inflationary tendencies can be checked, currently available manpower resources and unused capacity can provide the basis for an extended period of economic growth.