

## The Business Situation

The economy came through the summer months with few of the signs of hesitation that had marked that season in 1962 and 1963, and in spite of unsettled labor disputes in some sectors business was continuing its brisk advance as the autumn began. Industrial production and retail sales moved ahead in August, and although nonagricultural employment held at about the July level, hours worked in manufacturing—particularly in durable goods industries—moved up. Weekly data for September suggest that steel production continued to rise, while auto production and retail sales edged down from their August levels.

It is probably too early to assess the eventual impact on the economy of the conclusion of labor negotiations between the United Auto Workers and Chrysler and Ford in September and the signing of a national agreement with General Motors early in October. The terms of these agreements, to be sure, included increases in wages and fringe benefits in excess of the economy's average productivity gain in recent years, but the current exceptionally good level of profits in the auto industry, together with the industry's above-average rate of productivity increase, provides a cushion with which to meet the cost increases. Hence, the labor settlement apparently raises no immediate threat to the stability of automobile prices. Yet, there is the possibility that similar wage adjustments may spread to other industries, including those less able to absorb higher costs. The agreements also have a potential psychological impact on pricing decisions and could become an inducement to increased inventory building. On the other hand, productivity growth over the past two years has been unusually rapid for an expansion more than a year old. The continuation of such rapid growth, while it should not be taken for granted, would of course be of substantial help in offsetting the cost-price pressures arising from wage settlements.

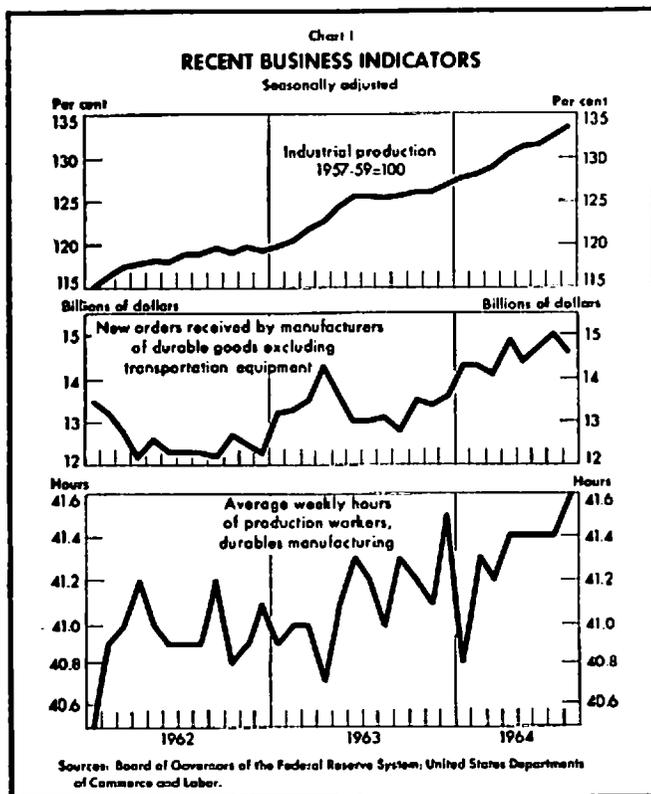
While the auto settlements and the sustained economic advance have served to focus attention on the behavior of prices, there is still no sign of any immediate change in the relative stability that has generally characterized broad indexes of price behavior for several years. The consumer price index held virtually steady in August, and the increase in percentage terms so far this year has been

somewhat smaller than the moderate rises in the first eight months of 1962 and 1963. A decline in food prices was too small to cause any significant movement in the overall wholesale price index in August, as average prices of commodities other than farm and food products held steady at a level about equal to those prevailing at the end of 1963 and the beginning of 1964. Weekly data indicate little change in this broad indicator of industrial commodity prices in September. At the same time, however, prices of some sensitive industrial commodities, particularly nonferrous metals, pushed up the Bureau of Labor Statistics index of thirteen raw industrial commodities in September. The advances in this index in recent months, which have totaled about 11 per cent since the beginning of the year, partly reflect special supply situations in individual commodities, but may also indicate some tendency toward generally increased demand pressures both in the United States and abroad.

### PRODUCTION AND EMPLOYMENT

Industrial production (as measured by the Federal Reserve's seasonally adjusted index) rose by 0.8 percentage point in August, the ninth consecutive monthly gain, to reach 133.5 per cent of the 1957-59 average (see Chart I). So far in 1964 industrial production has risen 5 per cent, about equal to the advance during the comparable months of 1963. The August gains were widespread; equipment production registered a rise of 1 per cent, while output of both durable and nondurable materials advanced. Automobile production—drastically curtailed by the model change-over and the lack of any continuation of 1964 model production—actually recorded a small increase, after a necessarily rough allowance for these seasonal influences. Steel production showed a less-than-seasonal rise in August, but weekly data point to some seasonally adjusted advance in September. Auto output declined somewhat in September, reflecting the General Motors' strike during the last days of the month.

Prospects for further production gains remain good, although a 9 per cent August decline from the record July level in new orders received by manufacturers of durable



goods does provide a cautionary note. Most of the August fall in orders reflected a sharp drop in the erratic aircraft orders series; new orders for durable goods excluding transportation equipment fell only 2.9 per cent in August (see Chart I). Even at the reduced August level, new orders continued to run ahead of shipments, and the backlog of orders on the books of durables manufacturers thus climbed for the eighth month in a row.

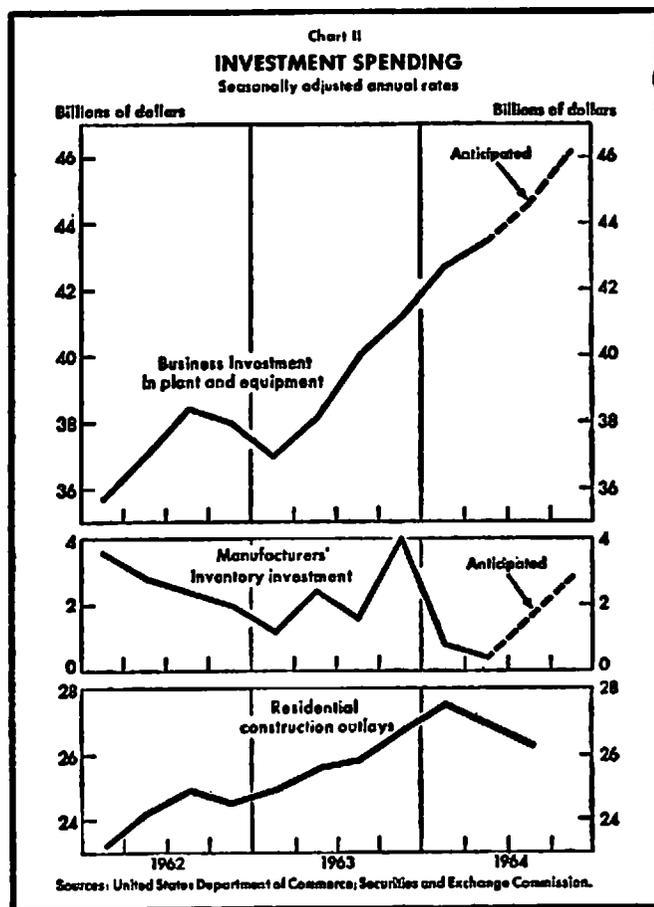
Total nonagricultural employment in August held at about the July level, although in the manufacturing sector employment (along with mining and construction employment) showed a small decline. Average hours worked per week by manufacturing production workers, however, moved up by about ½ per cent to 40.7 hours, seasonally adjusted. Average hours in the durable goods industries—at 41.6 hours (see Chart I)—in fact reached a peak for the current expansion. The increases in average hours worked may indicate that employers are utilizing existing employees to the fullest before hiring new workers and also that the sustained pace of the expansion has quite possibly now come close to creating labor shortages in some lines.

According to the Census Bureau's household survey, total farm and nonfarm employment moved down a bit in

August while unemployment edged up, reflecting primarily a failure of unemployment among teen-agers to show the normal seasonal drop. As a result, the over-all unemployment rate increased to 5.1 per cent from 4.9 per cent in July. In September, a fractional advance nudged the rounded unemployment rate up to 5.2 per cent. Unemployment among teen-agers registered some drop, but the rate for married men rose to 2.9 per cent. On a quarterly average basis, the unemployment rate in the third quarter was at its lowest level since October-December 1957.

**BUSINESS AND CONSUMER SPENDING**

While spending for plant and equipment is strong and expected to show a good advance at least through the remainder of the year (see Chart II), business spending for additions to inventories remains moderate. According to an August Commerce Department survey, manufacturers estimate that stocks of goods on hand will rise at a seasonally adjusted annual rate of \$1.6 billion in the third



quarter of the year and by \$2.8 billion in the final quarter (see Chart II). According to the same survey, however, shipments are also expected to advance over the remainder of the year at such a rate that the inventory build-up will serve only to maintain the generally tight relationship between stocks and sales that has characterized the current economic expansion.

Residential construction activity continues to slip back from the advanced levels reached earlier in the year. With some further decline in September, outlays for the third quarter as a whole—at a seasonally adjusted annual rate of \$26.3 billion—were about 4 per cent below the advanced first-quarter rate (see Chart II) and 2 per cent below the second quarter. Housing starts declined again in August, putting the July-August average of starts 14 per cent below the first-quarter rate, while new housing

permits issued moved up only slightly from the relatively low July level.

Apart from housing, the consumer continues to provide a major push to economic activity. Retail sales, rising almost 1 per cent in August, reached a record high of \$22.1 billion, seasonally adjusted. Sales of automobiles contributed substantially to the advance, and dealers substantially cut their inventories of 1964 model cars. Nondurables sales, particularly apparel, also contributed to the August advance. Data for the early weeks in September suggest that retail sales declined somewhat from their August record. As noted in last month's *Review*, consumer intentions to buy are reported to be strong and, with the March tax cut continuing to provide an incentive for increased spending, further strength in the consumer sector can indeed be expected.