

## The Business Situation

Economic activity was continuing a rise of almost four years' duration as 1964 drew to a close, and most forecasts pointed to further gains in 1965. Production, employment, and personal income all recovered in November from the depressing effects of widespread strikes in the automobile industry in the preceding months, and output in both the auto and steel industries continued to climb in December. Unusually heavy Christmas shopping resulted in an appreciably greater than seasonal rise in retail sales in December, and businessmen's outlays for new plant and equipment apparently were also increasing. On the other hand, residential construction still showed some weakness. Price developments continued to be a cause for some concern. Both consumer and industrial wholesale prices rose slightly in November, and some additional rise in the industrial component of the wholesale price index apparently occurred in December. Moreover, a number of further price rises announced by the steel industry in late December undoubtedly added to the recently emerging climate in which businessmen seem to be less reluctant to probe markets to determine whether price increases can be made to stick.

Assessment of the economic outlook for the new year is, of course, beset with the usual collection of complicating uncertainties, not the least of which is the possibility of disruptions as a result of labor disputes. The strike of East and Gulf Coast dock workers will have serious effects unless it proves to be of short duration. There are also the lingering possibilities of a nationwide railroad tie-up during the winter as well as of a strike in the steel industry on or after May 1. Another determinant of the course of over-all activity in the months ahead is likely to be business spending. A Commerce Department survey taken in November, which may not fully reflect the possible hedge buying of steel, indicated that manufacturers already anticipated a substantial increase in their inventory holdings in the final quarter of 1964 and a somewhat more moderate expan-

sion in the first quarter of 1965. Capital spending plans for 1965, on the other hand, appear to have strengthened since the initial surveys early last fall.

Economic developments in the months ahead will, of course, also be influenced heavily by the Administration's budgetary decisions that are about to be revealed. Most business analysts seem to believe that these decisions will result in some net expansionary impact on the economy and thus will help extend further the current over-all advance.

### RECENT INDICATORS

After a strike-induced dip in October, industrial production rose strongly in November: the Federal Reserve Board's seasonally adjusted index advanced by more than 3 full percentage points to 134.9 per cent of the 1957-59 average (see Chart 1). The bulk of this advance was attributable to the return of most automobile workers to their assembly lines, though final settlement of issues at a number of local Ford Motor Company plants was not reached until late in November. In addition, most other industries—including primary metals, furniture and fixtures, and machinery—registered moderate increases in output in the month. In December, most of the automotive industry mustered everything at its command in an effort to work down the backlog in consumer orders and to restock dealers' showrooms. December data indicate that assemblies rose about 6 per cent above the pre-strike level and 12 per cent over December 1963. The stepped-up pace of activity in the automobile industry also influenced steel ingot production, which continued to rise in December. Steel ingot output for the year as a whole is now estimated at 127 million tons, 9 per cent more than the previous record reached in 1955 and 16 per cent above 1963. Strength in over-all production during the months ahead is suggested by the high level of unfilled orders on

# Monthly Review

FEDERAL RESERVE BANK OF NEW YORK

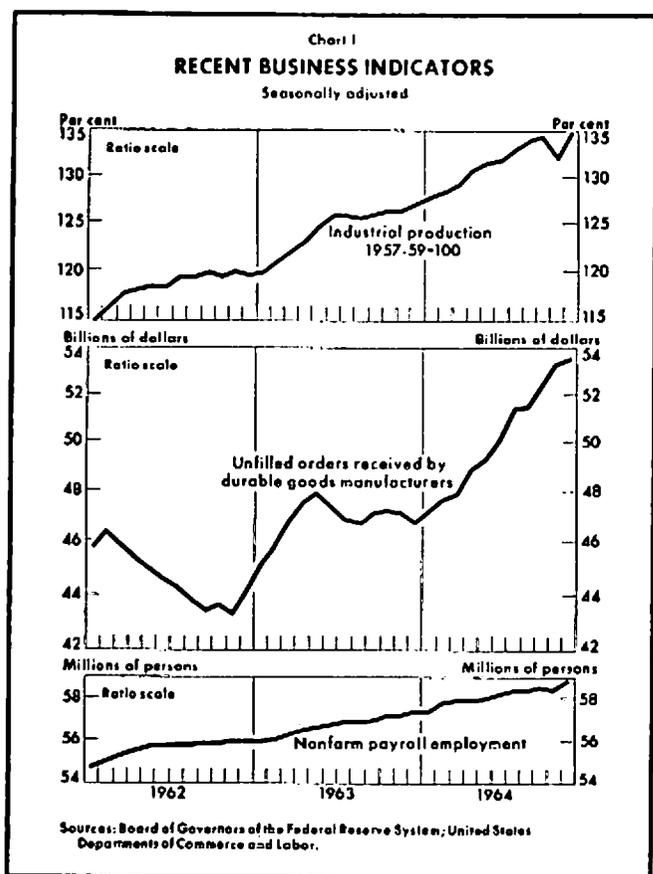
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the books of durables manufacturers. Such backlogs rose for the eleventh consecutive month in November, to a level 13 per cent higher than a year ago.

Reflecting the turnabout in production, nonfarm payroll employment also turned sharply upward in November, following a decline the month before (see Chart I). Employment gains were scored by all major industry groups, though the return to work in the automobile industry accounted for two thirds of the over-all rise. Total employment expanded further in December, according to the Census Bureau's household survey, and the rise was somewhat greater than the expansion in the civilian labor force. As a result, the over-all unemployment rate (seasonally adjusted) fell to 4.9 per cent, a substantial improvement over the 5.5 per cent figure for the final month of 1963. For one of the most important groups in the labor force, the improvement has been relatively even more substantial: the jobless rate for married men stood at only 2.7 per cent in December, as against 3.3 per cent a year ago.

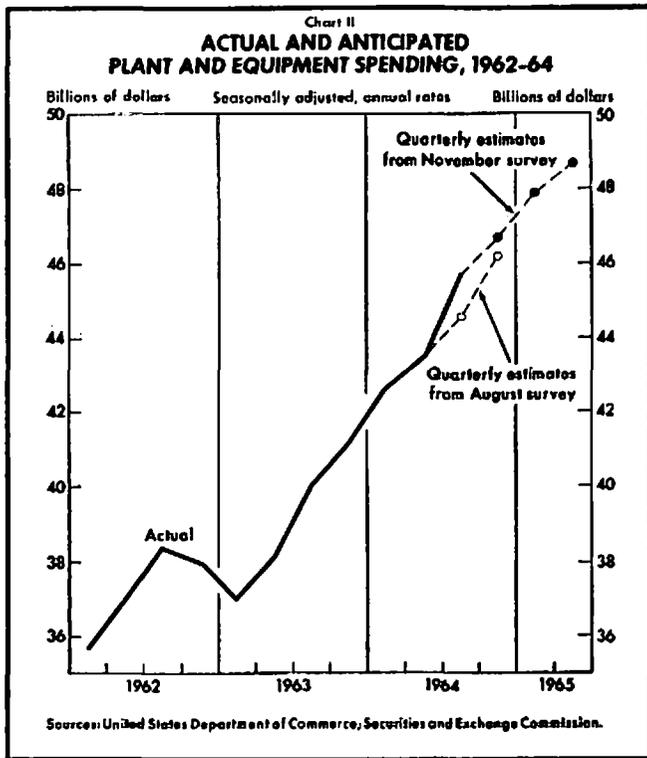
Retail sales declined in November, the third successive month of slippage, as unusually warm weather apparently

sharply curtailed sales of winter apparel. Personal income, however, recorded a considerable advance in November, with the result that Christmas shoppers were in good financial shape to carry out the buoyant buying plans that had shown up in recent surveys. Glowing trade reports suggest that heavy consumer spending did in fact occur. Indeed, according to the advance report, retail sales in December rose to a record \$22.8 billion (seasonally adjusted), 5 per cent higher than in November and 9 per cent above December 1963. The substantial gain reflected largely a marked pickup in durable goods sales. These, in turn, were sparked by a very considerable advance in automobile sales as new-model cars were in better supply.

Outlays for nonfarm residential construction in December were off by less than 1 per cent. Such outlays edged downward in the closing months of 1964 but for the year as a whole amounted to \$26.6 billion, compared with \$25.8 billion in 1963. Building permits issued rose by 3 per cent in November and the dollar value of residential construction awards was up by 12 per cent, although nonfarm housing starts declined after moving up in the preceding two months. A recent forecast by the Commerce Department places nonfarm housing outlays in 1965 slightly above the 1964 figure.

#### BUSINESS SPENDING PLANS

As the new year began, most business analysts were increasingly focusing attention on the probable course of business spending in 1965. One area of immediate interest is investment in inventories, especially in view of indications that steel users have already begun to stockpile finished products in anticipation of a possible strike. A Commerce Department survey taken in November—which may not fully reflect the possible hedge buying of steel—indicated that manufacturers already anticipated a substantial \$1.2 billion increase in their inventory holdings in the final quarter of 1964 and a somewhat more moderate expansion of \$0.6 billion in the first quarter of 1965. At the same time, manufacturers expected their sales in the final quarter of 1964 to remain unchanged from the quarter before, but did anticipate a considerable rise in sales in the first quarter of 1965. In October and November inventories held by manufacturers recorded the two largest monthly advances in the current upswing, which suggests that manufacturers would actually carry out fourth-quarter inventory building plans. If inventory and sales expectations for the first quarter of 1965 are realized, the inventory-sales ratio for manufacturers at the end of the first quarter will be no higher than the reading for the third quarter of 1964, a figure that was relatively low by historical standards.



As in previous years, business capital spending in 1965 will be an important determinant of the course of business activity. Such outlays, of course, tend to increase productivity and to accelerate real economic growth, in addition to their immediate influence on aggregate economic activity. The first clue with regard to the course of plant and equipment spending in 1965 was provided by the fall 1964 McGraw-Hill survey of businessmen's capital spending plans, which pointed to about a 5 per cent over-the-year gain for 1965. When this projected 1965 level of plant and equipment spending is compared with the \$46.7 billion annual rate of spending now expected in the final quarter of 1964 (see Chart II), the advance amounts to only 0.3 per cent. However, the fall McGraw-Hill survey has in past years of uninterrupted business expansion tended to understate the mark on average by about 7 percentage points. For example, the 1963 fall McGraw-Hill survey had called

for a 4.2 per cent advance in 1964, compared with the 13.9 per cent increase over 1963 now expected for 1964.

There are now other indications that capital spending will show strength through the first half of the new year. According to a Commerce Department-Securities and Exchange Commission survey taken in November—i.e., somewhat later than the McGraw-Hill survey—businessmen's spending plans for the first quarter of 1965 were \$1.2 billion above the expected figure for the final quarter of 1964. At the same time, businessmen expected their spending for plant and equipment to expand by an additional \$0.8 billion in the second quarter of 1965. The indicated advance in the first half of the year was projected to come largely from the manufacturing sector. If the expected average gain in the first and second quarters were to be extended over the rest of the year, the estimated year-to-year gain for 1965 would be approximately 10 per cent.

The National Industrial Conference Board has recently reported that, according to its survey, capital appropriations by manufacturers were up strongly in the third quarter. Such appropriations tend to lead capital spending by two to three quarters. Thus, manufacturers' plans for enlarged capital spending through the first half of 1965 may well be firm.

#### PERSPECTIVE ON 1964

Early each year the Federal Reserve Bank of New York publishes *Perspective*, a nine-page review of the course of the economy during the preceding year. Many businessmen find the booklet useful as a layman's summary of the economic highlights treated more fully in the Bank's *Annual Report*, available in mid-March. If you would like to receive without charge *Perspective on 1964*—it is available now—write to Public Information Department, Federal Reserve Bank of New York, 33 Liberty Street, New York, N. Y., 10045.