The Business Situation

The full impact of the change in the Presidency on November 22 cannot, of course, be assessed as yet. Nevertheless, it appears that at the time of the change the economy had already developed sufficient momentum to assure further expansion over the months ahead. The reaction of various economic groups to the change in the Presidency conveys the impression of continued confidence in the working of our institutions, in the strength of the economy, and in the prospect for future economic gains.

This confidence partly reflects the fact that, with the final quarter of the year well under way, most measures of activity were continuing to post new advances. In October, industrial production, nonfarm payroll employment, personal income, and retail sales each rose more than seasonally. Among the various leading indicators, both housing starts and building permits rose sharply from already high levels, while new orders for durable goods also scored a good gain. Fragmentary data for November show a modest pickup in steel ingot production and a further rise in the rate of automobile assemblies. Retail sales appear to have held up well, except for a few days following President Kennedy's death.

On the other hand, assessments of the longer term picture had been somewhat mixed even before the President's assassination, with uncertainties relating particularly to the timing of a Congressional decision on tax legislation. It is thus heartening that President Johnson in his November 27 address to a joint session of Congress announced his full support of an early enactment of the proposed tax cut.

One recent study bearing on the prospects for next year, the McGraw-Hill October survey of businessmen's capital spending intentions for 1964, suggests that current plans call for no further increase in outlays beyond the annual rate of spending estimated for the final quarter of 1963 in the August survey of the Department of Commerce-Securities and Exchange Commission. On the other hand, the National Industrial Conference Board reports that capital appropriations by large manufacturing corporations were higher in the third quarter of 1963 than at any time since the first quarter of 1956. Capital appropriations for these firms have tended to lead capital outlays by six to nine months. The high third-quarter level of appropriations, following a substantial rise the quarter before, would seem to indicate more strength in capital outlays during 1964 than is suggested by the McGraw-Hill survey. The likelihood that actual spending will exceed this survey's levels would be further increased if other forces continued to push the economy upward. In this regard, it is encouraging that the Census Bureau's latest survey of consumer buying intentions, taken in October, shows that plans to purchase durable goods within six months are above the relatively high levels of a year earlier.

PRODUCTION, EMPLOYMENT, AND CONSUMER SPENDING

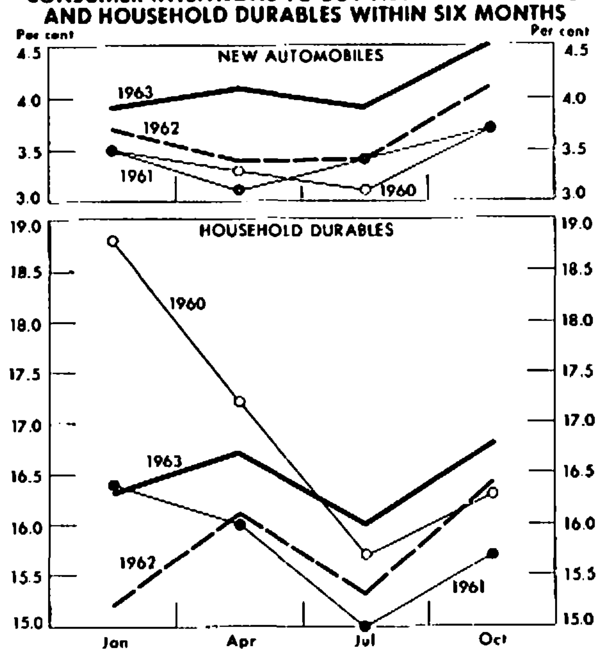
After declining in August and showing little change in September, the Federal Reserve's index of industrial production moved up by 0.7 percentage points in October to reach 126.6 per cent (seasonally adjusted) of the 1957-59 average. This figure very slightly surpasses the previous all-time high, reached in July. The automobile industry provided the largest single source of strength in October, as assembly of the new models moved into full swing. At the same time, producers of business equipment posted their sixth consecutive increase in output (see Chart I). It is also worth noting that iron and steel production was essentially unchanged in October, following the appreciable declines registered in the previous several months. Although steel users apparently still have some surplus inventories of finished steel products, which probably will be worked down over the balance of the year, recent reports from the trade suggest that new orders are being placed in sufficient volume to support a moderate increase in steel production in the near term (on a seasonally adjusted basis). Ingot production in November did indeed score about a 6 per cent advance over October. Auto production also posted a modest rise in November, despite a series of work stoppages.

The employment situation showed further improvement in October, as the number of persons on nonfarm payrolls rose by 92,000 (seasonally adjusted). Most of this rise was centered in the government sector—particularly at the state and local levels—with some increases in employment in the trade and service industries as well. In contrast, employment in the manufacturing sector showed relatively little change, despite the increase in output in the month. In November total employment remained about unchanged, according to the Census Bureau's household survey. Because of an increase in the number of persons looking for work, however, the unemployment rate rose to 5.9 per cent of the civilian labor force. The number of unemployed persons has remained at 4 million or more for thirteen consecutive months.

Recent indicators of consumer spending, on balance, are more encouraging than was the case several weeks ago. Thus, after faltering in August and September, retail sales turned around in October and rose to a new record. Fragmentary data for November suggest a possible weakening of total sales. This apparent slippage, however, was probably in some part related to a few weak shopping days following the assassination of the late President Kennedy. (Most retail outlets, of course, did not open for business November 25, a day of national mourning for the late President.) Also, sales of new automobiles probably fell slightly during November. Dealers reported that the new models have been well received but that sales had been held up early in the month by shortages in popular lines. These reports on continued strength in the market for automobiles seem to be corroborated by the Census Bureau's October survey of consumer buying intentions (see Chart II). To be sure, consumer intentions surveys do not correlate very precisely with later data on actual purchases—an imprecision that appears to be even more marked for the October surveys than for those taken in other months of the year. Nevertheless, it is noteworthy that plans to buy new cars within six months were in October significantly above the level recorded in the fall of 1962 and only slightly below the all-time high reached in October 1959, while intentions to purchase used cars also showed strength. Plans to buy household durables and new homes likewise continued at a high level.

Chart II

CONSUMER INTENTIONS TO BUY NEW AUTOMOBILES AND HOUSEHOLD DURABLES WITHIN SIX MONTHS



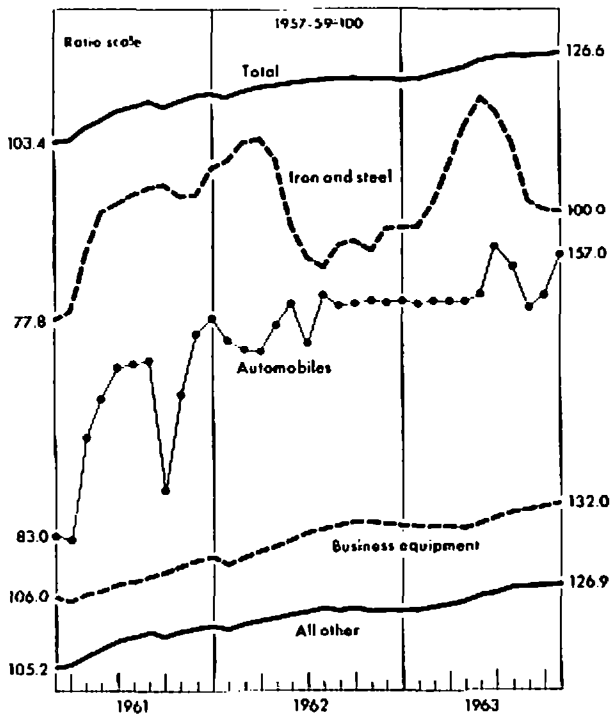
Note: Buying plans are expressed as the ratio of the number of families who indicate they intend to buy to the total number of families in the survey.

Source: United States Department of Commerce, Bureau of the Census.

Chart I

RECENT DEVELOPMENTS IN INDUSTRIAL PRODUCTION

Seasonally adjusted monthly data



Source: Board of Governors of the Federal Reserve System.

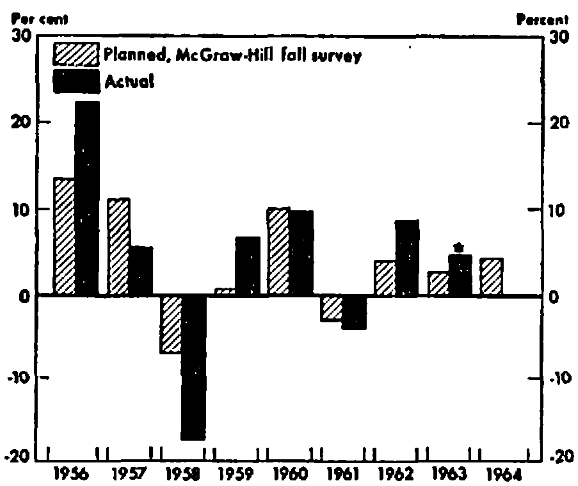
PLANT AND EQUIPMENT SPENDING IN 1964

In assessing the prospects for continued over-all economic expansion in 1964, much attention has been focused on the likely course of spending for new plant and equipment. The first impression of capital spending plans for next year, derived from the October McGraw-Hill survey, appears to have been one of disappointment to many observers. The survey indicated that businesses in the aggregate were planning to spend only about $41 billion for plant and equipment in 1964—4 per cent more than the estimated amount of such spending for 1963 as a whole, but actually slightly below the planned rate of spending for the current quarter adjusted to an annual rate basis.

Upon closer examination, however, the picture is somewhat more encouraging. Past experience suggests that the McGraw-Hill fall surveys have tended to be very reliable in predicting the direction of change in capital spending but have tended to understate the amount of increases by considerable margins. Thus, in each of the years since 1955 for which the McGraw-Hill fall survey pointed toward a rise in capital spending an increase was in fact realized (see Chart III). However, the rate of increase actually rung up in such years exceeded the projected advance by an average of about 2½ percentage points. The difference between the actual amount of gain in capital outlays, compared with that shown by the survey, is even more pronounced in years of continually rising over-all economic activity. Some respondents to the survey have already indicated that their capital outlays will probably exceed present plans if the proposed tax cut is passed. It is also worth noting that this year's survey included a much larger representation of smaller firms in the sample than had been the case in previous years. There is some evidence that small firms do not tend to make very definite long-range plans for capital spending, which suggests that the latest survey may have had an even larger downward bias than those taken in some past years.

Chart III

YEAR-TO-YEAR PERCENTAGE CHANGES IN PLANNED AND ACTUAL CAPITAL SPENDING



* Estimated by United States Commerce Department and Securities and Exchange Commission.

Sources: United States Department of Commerce, Securities and Exchange Commission, and McGraw-Hill Publishing Company.

About 80 per cent of the McGraw-Hill survey's projected increase in capital spending for 1964 is accounted for by the manufacturing sector, where the largest push is expected to come from the iron and steel industry. Although utilization of over-all capacity is relatively low in this industry at present, there may be some need for additional finishing mill capacity. Furthermore, competitive pressures—both from foreign steel producers and from alternative products—have increased the need for modernization. It is also possible that several industries which in September were already very near to their preferred operating rates—most notably textiles and petroleum and coal products—may find it necessary to revise upward their relatively modest 1964 capital spending plans should sales turn out well. The only industries that reported significant reductions in planned capital outlays in 1964, compared with 1963, were the railroads and manufacturers of transportation equipment. However, the railroads have frequently noted a shortage of modern rolling stock and other equipment, which in the past several weeks has become even more pressing. This development, in turn, could cause some upward revision in their planned 1964 capital spending.