# The Business Situation

After several months of sustained advance, the economy's upward movement appears to have slowed in late summer, although fragmentary September data suggest the possibility of a renewed pickup. Industrial production and manufacturers' new orders for durable goods declined a bit in August, while nonfarm employment and retail sales showed little change and personal income posted the smallest gain in six months. In almost every case, these signs of hesitation could be traced in significant part to the operation of special factors in the auto and steel industries. These factors were also operating in July, and there was thus an element of surprise in the buoyancy of the economy in that month. As it turned out, production declines in the steel and auto industries were more pronounced in August than in the earlier month. And, with car makers retooling for the 1964 models in August, shortages of some lines were apparently responsible for a slackening in the pace of sales and new orders.

As the new car models began to come off the assembly lines in September, auto output received a more-than-seasonal boost. Steel production, moreover, turned slightly upward, following the three-month decline that had occurred in the aftermath of the industry's labor settlement. Auto sales continued to be adversely affected by shortages of some new models, however, and department store sales declined somewhat from the record August rate.

The broader questions with regard to the performance of the economy over the balance of the year of course remain—including the reception to be accorded the new auto models and the outcome of proposed tax legislation. Two positive factors are the anticipated rise in government spending—reflecting the recently enacted military-pay hike and a resumption of the uptrend in state and local government outlays—and the planned step-up in business plant and equipment spending. In any case, there continues to be little prospect of a significant near-term reduction of the current unemployment rate. In September, the rate edged up to 5.6 per cent of the civilian labor force (seasonally adjusted) and was just as high as the year-earlier figure.

## PRODUCTION, EMPLOYMENT, AND SALES

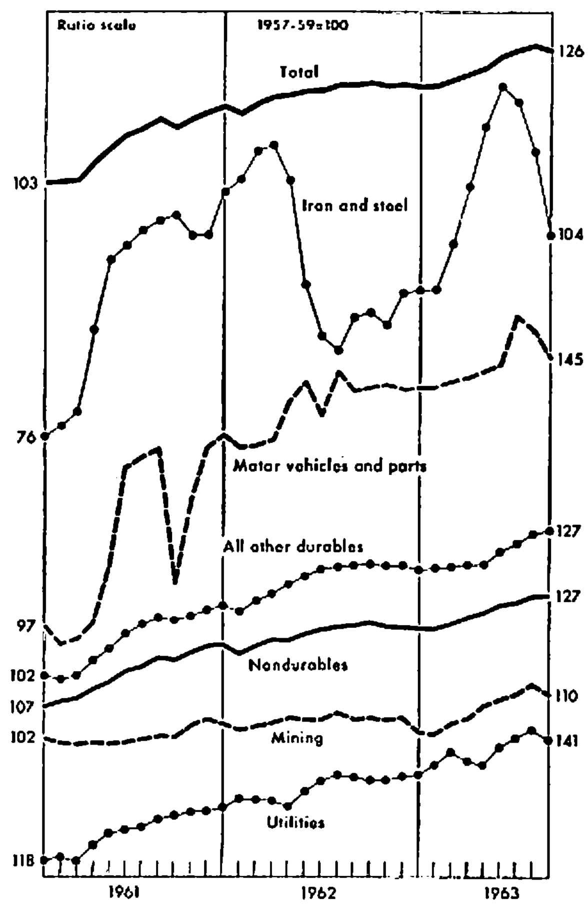
After advancing by more than 7 percentage points in the previous six months, the Federal Reserve's seasonally adjusted index of industrial production fell by nearly a point in August to 125.6 per cent of the 1957-59 average (see Chart I). Most of the decline was attributable to a 12 per cent reduction in iron and steel output, the sharpest of the year, but production of motor vehicles and parts also dipped significantly from the unusually high July rate. Outside these two industries, rises and declines were generally small and just about offsetting, whereas in previous months there had been sizable gains on balance. Early data for September point to a moderate advance in automobile output (seasonally adjusted), with preliminary schedules suggesting the possibility of a more substantial gain in October. Data on steel output for September indicate a small increase, after seasonal adjustment, from the August level. In the June-August period, declines in the iron and steel component cost the total industrial production index about 1.1 points, and a bottoming-out in the steel industry would thus remove a significant drag on over-all production. The strength of the industry for the near term, of course, depends in part upon how much longer it will take steel users to reduce their inventories to desired levels.

Reflecting dampened industrial production, nonfarm payroll employment (seasonally adjusted) showed a small decline in August, the first since February 1961. Gains in service and government employment failed to offset a reduction in manufacturing payrolls which was concentrated mainly in the transportation and primary metals fields and was therefore related to cutbacks in steel and autos. In other areas of the economy, however, payroll employment, like production, showed less buoyancy than in earlier months. In September, according to the Census Bureau's household survey, total employment moved up again, after seasonal adjustment, but a proportionately greater rise in the labor force resulted in a small increase in the unemployment rate.

Chart I

DEVELOPMENTS IN INDUSTRIAL PRODUCTION

January 1961 - August 1963; seasonally adjusted




Source: Board of Governors of the Federal Reserve System.

Total retail sales were about unchanged in August (seasonally adjusted), after climbing appreciably in the two preceding months. Excepting autos, however, sales continued to rise significantly, with advances posted particularly by stores featuring back-to-school and other fall items. Incomplete data for September suggest that over-all retail sales moved downward, in part reflecting continued limitations on new-car availabilities in some popular lines. Public response to the 1964 models cannot as yet be assessed with any confidence. Industry spokesmen have suggested that auto sales may reach or exceed 7 million units for the third successive year.

Since the statistics on new orders received by the automobile industry reflect mainly deliveries of new cars to dealers, the August decline in automobile sales also had a marked impact on new orders data. Thus, despite little net change in orders outside the motor vehicle industry, total new orders received by manufacturers of durable goods declined by 2 per cent in August (seasonally adjusted) to the lowest level since January. Total unfilled orders of durables manufacturers (seasonally adjusted) were virtually unchanged in August.

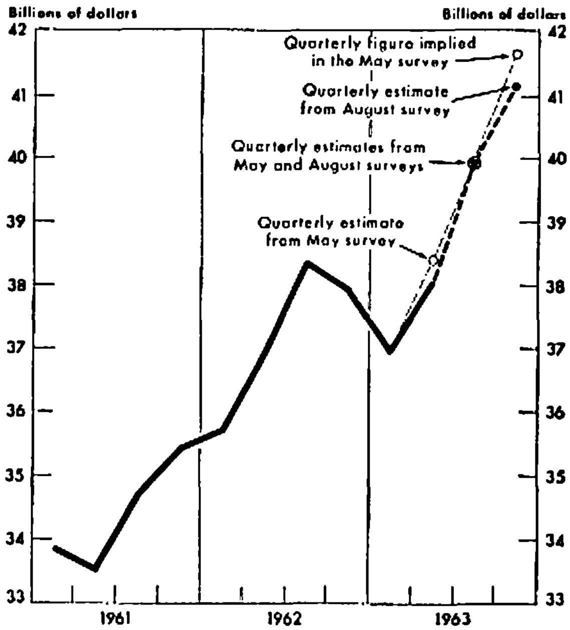
## FIXED INVESTMENT

The latest survey of businessmen's plans for plant and equipment spending, taken in August by the Commerce Department and the Securities and Exchange Commission, points to substantial gains over the balance of the year (see Chart II). After declining in the first quarter, business fixed capital outlays rose by \$1.1 billion in the April-June period to \$38.1 billion (seasonally adjusted annual rate). While this was a bit below the levels businessmen were planning in May—mainly because of a shortfall in nonmanufacturing industries—the latest survey indicates no change from the earlier report in outlays planned for the third quarter. As a result, the second-quarter to third-quarter gain of \$1.9 billion indicated in the latest survey is somewhat greater than had been suggested previously. Although the latest plans for the final quarter of the year indicate a somewhat lower level of spending than was

Chart II

**RECENT DEVELOPMENTS IN PLANT AND EQUIPMENT SPENDING**

Seasonally adjusted, annual rates




Sources: United States Department of Commerce; Securities and Exchange Commission.

implied in the May survey, they nevertheless call for a further $1.2 billion advance from the third quarter. In appraising the likelihood that spending plans for the rest of the year may be realized, it is noteworthy that corporate profits (after taxes) rose to a twelve-year high in the second quarter of the year. Such a level of profits should help provide the financial resources and the incentive for a further expansion of plant and equipment spending.

Indicators of residential construction activity are continuing to ease off from their earlier exceptionally high levels. Private nonfarm housing starts moved slightly lower in August, marking the third consecutive setback in this monthly series. These movements appear to be in line with the Commerce Department's revised forecast for 1963, which implied a moderate reduction in housing starts over the last half of the year from their high spring levels. Although the backlog of unused permits remains substantial, new home building permits also moved down further in August, following an initial decline in July. Against the background of these declines in leading indicators, private residential construction outlays edged down slightly in September. Despite these declines, new home construction is still proceeding at a rapid pace. Moreover, the underlying demand for housing continues to be bolstered by a number of factors, including rising family incomes, an upward trend in new household formations, and the ready availability of mortgage credit at relatively low rates.

## SECOND DISTRICT DEVELOPMENTS

In comparison with the many available indicators of national economic trends, statistical data for analysis of activity in the Second District are somewhat limited.[1] Data on employment and unemployment, sales, personal income, and construction activity are available for the region, however, and these series provide a fairly reliable measure of over-all developments within the District.

Since the first quarter of this year most measures of business activity in the Second District have kept pace with their national counterparts. Thus, both personal income and nonfarm employment advanced in the District during the April-July period at the same rate as in the nation, while department store sales, which had been adversely affected by the first-quarter New York City newspaper strike, showed a greater than national improvement. Unemployment in two of the District's three states—New York and Connecticut—averaged somewhat below the national rate during the recent period. The only notable exception to this generally good record is activity in the District's construction industry. While recent gains in construction employment have paralleled the national rate of advance, District employment in the industry is below a year ago. To a substantial degree, this reflects the combined effect of several large-scale construction strikes in upstate New York and the aftermath of last year's surge of activity in New York City, during which many builders "borrowed" from future projects in order to beat the deadline set under the City's new, more stringent, zoning law.[2] At the same time, however, several areas outside New York City also continue to report disappointing levels of building activity.

Total nonfarm employment in the District increased at the national rate of 1 per cent during the April-July period. Some divergences from the national pattern are noteworthy, however. Thus, in the apparel industry, which

[1] The Second District includes all of New York State, twelve primarily industrial counties of northern New Jersey (Sussex, Passaic, Bergen, Hudson, Essex, Warren, Morris, Union, Hunterdon, Somerset, Middlesex, and Monmouth), and Fairfield County, Connecticut.

[2] Although the actual deadline is not until the end of 1963, the surge in activity prompted by this deadline came in 1962.

employs more of the District's manufacturing labor force than any other, the employment increase was larger than in the nation as a whole. Trade sources, moreover, suggest the prospect of further gains during the fall and winter seasons. Employment in the transportation equipment industry, however, showed a smaller rise in the District than in the nation. The automotive segment of the industry apparently is still performing well, but shipbuilding and aircraft producers have been reducing work forces. An exception in the aircraft industry is Fairfield County, Connecticut, which has shown rising employment in recent months.

District employment in primary metals, particularly steel and wire production, also has shown slower than national growth since the first quarter—in part reflecting the temporary shutdown of some upstate operations and the closing of a plant in western New York that was attributed by the company to the impact of foreign competition. As a result of this closing and an over-all reduction in steel demand since just before the settlement of the industry's labor dispute, the Buffalo index of steel production during July and August averaged 80.7 per cent of its 1957-59 base, compared with a United States average of 99.7 per cent.

Unemployment in the District as a whole showed about the usual seasonal decline during the April-July period. In both New York and Connecticut, however, the total unemployment rate averaged lower than the national figure, while the New Jersey total unemployment rate was higher. As was true of the country as a whole, the unemployment rates in each of the District's three states were slightly above their year-earlier levels. Two of the District's major labor market areas—Newark and New Brunswick-Perth Amboy—have been removed from the national list of areas with "substantial" unemployment (6.0 per cent or more) and reclassified to the category of "moderate" unemployment (3.0 to 5.9 per cent). Heightened activity in the transportation equipment industry and the expansion of employment in the chemical and electrical equipment industries were the major factors bringing about the reclassification. As a result of these changes, only three of the District's thirteen major areas remain in the substantial unemployment category. In Rochester a reduction in unemployment, largely attributable to employment gains in the photo-optical industry, resulted in a reclassification of that area to the category of "relatively low" unemployment (1.5 to 2.9 per cent). Only fifteen other major areas out of 150 in the country currently are classified in this category.

District store sales advanced more rapidly during the April-July period than nationally, with notable gains recorded in New York City and Rochester. Much of the recent New York City gain represents merely a return to a more normal sales level following termination of the newspaper strike in March. The Rochester situation, however, reflects a generally expanding local economy, as measured by a local index of business activity which is now at a record high. District sales during the April-July period were 6 per cent higher than a year earlier. Nationally, the gain was 4 per cent.

Construction activity in the District, measured in terms of the average level of employment in the April-July period, equaled the national gain of 3 per cent over the first-quarter average. Nevertheless, construction employment and contract awards showed a decline from the year-earlier level, while nationally there was an increase. Some over-the-year decline in construction activity in the District, of course, reflects the slowing-down from an exceptionally high level of activity in the New York City area during 1962, when, as already noted, builders rushed work on projects in anticipation of the effective date for more stringent building regulations. During recent months, however, District construction has also suffered from several strikes in upstate areas—the largest one involving some 11,000 workers in twenty-eight New York State counties.

Reflecting these and other developments, the value of total construction contract awards in the April-July period was 9 per cent below the record 1962 level, while for the nation as a whole contract awards during the period were 12 per cent greater than a year ago. The District's volume of nonresidential building awards, which in the first quarter was still above the corresponding period of 1962, has recently joined the residential and heavy engineering categories in showing an over-the-year drop as a result of slackened activity in New York City. Through the first seven months of 1963, however, District awards have remained above their 1961 level and that of earlier years.