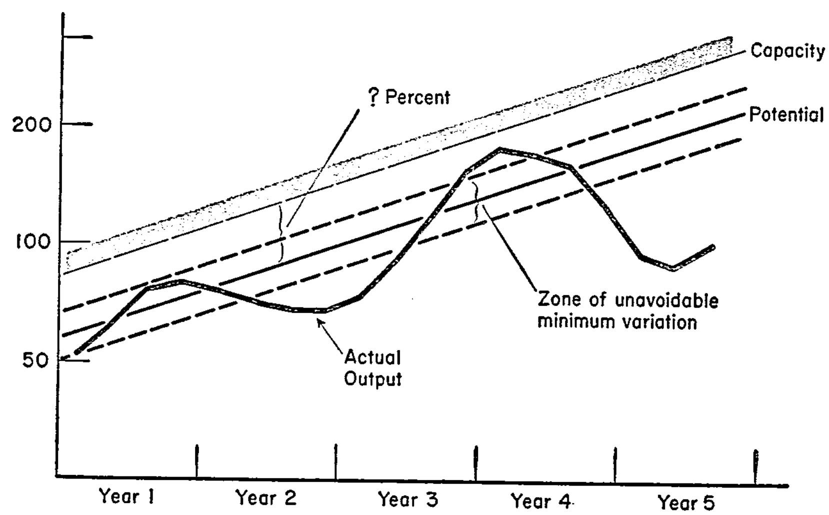
Potential output versus capacity

At the outset of this chapter, the term "potential" was used and reference was made to the Nation's potential for economic growth. Now we refer to economic growth in terms of an increase in the Nation's capacity to produce goods and services as well as leisure.

In the analysis that follows, the distinction between capacity and the output potential for which a measure is developed, is of critical importance. To make the relationship clear, chart I was developed.

CHART I

CAPACITY, OUTPUT, AND POTENTIAL
an EXPLANATORY SKETCH



It will be noted that the topmost line, labeled "capacity," is above the "potential" by some unspecified percentage, though the two lines are shown parallel. The potential is a measure of the optimum or best practice which it is believed the economy is capable of sustaining on the average, year after year, without running into serious instability of employment, output, or prices. It is, in a word, a measure of what would be reasonably good performance of the economy, maintaining a stable relationship between output and capacity. Around this line of potential, lines have been dotted which represent what may be termed tolerance zones. Within these limits, the economy is fluctuating by so little that it cannot be regarded as being a serious challenge to the objectives of the Employment Act though certainly a matter of concern. Over time, it might be possible to reduce this type of variation. In fact, one of the objectives of economic research, both pure and applied, should be to determine what these limits of variation are and how much they can be narrowed in practice.

No attempt to determine them quantitatively has been made in this study.