

concentrated in the consumer sector. Demand for consumer goods has risen rapidly and has been supplemented by retailers' desires to add to their inventories after the heavy sales of the first quarter. Production of materials has been feeling the stimulus of steel stockpiling as well as the rebound after the end of the copper and glass strikes.

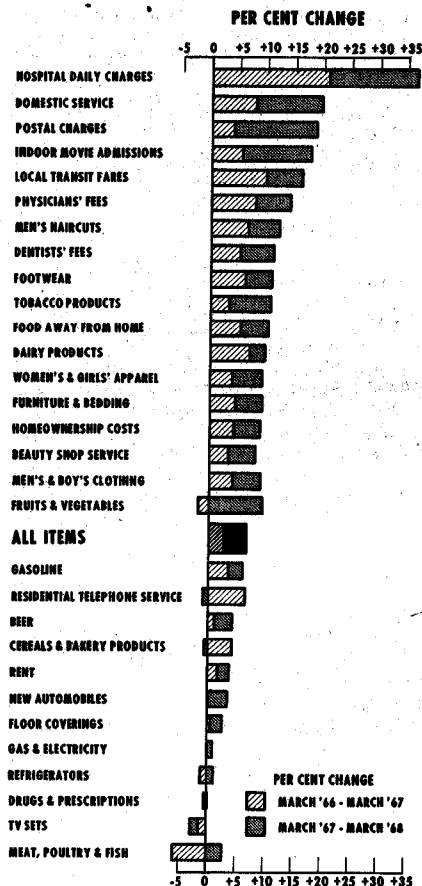
Wages, Prices, and Profits

The rising volume of activity has helped boost corporate earnings to a new high. Pretax profits reached a seasonally adjusted annual rate of \$88.8 billion in the first quarter, a gain of \$3.7 billion from the fourth quarter of 1967. However, more than half of this rise—\$2.2 billion—was the result of inflation, reflecting the upward revaluation of inventories. The remainder of the gain was attributable to increased sales volume. Profit margins have not shown the improvement which is usual in the early stages of an upswing in sales. Rising wages have far outstripped the increase in productivity of labor.

The U.S. Department of Labor estimates that hourly wage costs in the private economy were climbing during the first quarter at a 10 per cent annual rate. Consequently, although productivity increased at a 4 per cent annual rate—double the gain in the previous quarter—unit labor costs were escalating at 6 per cent per year. Commerce Department calculations indicate that a similar upswing in unit labor costs at nonfinancial corporations more than cancelled out a rise in prices and left profit margins after taxes and allowance for inventory markups well below both the fourth quarter and year earlier levels.

The increasing pressure of rising wage costs following a period of monetary inflation has set the stage for a renewed burst of price increases. In turn, the advance in living costs and anticipation of further rapid increases have stiffened labor's wage demands. The first chart highlights the wide disparity in movements of prices at different stages of production. Spot prices of most of the 22 selected basic commodities have trended downward in the past year, and the preliminary May index is the lowest in over four years. Currently, the index is 17 per cent below its February 1966 peak. Prices of wheat, cotton and metals, among others, have drifted lower since the first of this year, as increasing supplies have, in some cases, encountered declining demand.

The wholesale price index not only encompasses a far broader range of commodities, but also includes a greater degree of processing and manufacturing costs, and thus a higher proportion of labor costs. This comprehensive index has risen steadily since last October at an average



Changes in Selected Items in the Consumer Price Index, March 1966-March 1968

Source: U.S. Bureau of Labor Statistics. Items are ranked according to the overall change from March 1966 to March 1968.

annual rate of about 3½ per cent. A resurgence in prices of farm products and processed foods contributed to the latest rise, but the broad-based advance in prices of industrial commodities has been of deeper concern. In the seven months ended March 1968, the industrial price index rose more than it had in the seven years 1957-64. However, the pace of the rise appears to have slowed somewhat in the second quarter,