

THE PROSPECTS FOR GENERAL BUSINESS ACTIVITY AND THE FINANCIAL MARKETS

My forecast of general business activity in 1968 is outlined in the table "Estimated Comparison of Selected Economic Indicators" attached to my statement. I expect a very strong expansion of business this year, particularly in the first half. This forecast makes three very important assumptions: (1) that Federal defense expenditures will be in accord with the budget—a very conservative assumption in view of developments in the Far East; (2) that Congress will not enact a personal and corporate tax increase; and (3) that the rate of personal savings will remain at about the same level as in 1967.

Without an increase in taxes, the Federal deficit on a national income accounts basis will run as high as last year—in the \$12–14 billion range. It will thus be a powerful force for economic expansion. In addition, although I expect that monetary policy will continue to move toward less credit ease, I believe that the authorities will nonetheless permit a very large increase in commercial bank loans and investments this year.

As shown in the table, we expect that GNP will expand from \$785 billion in 1967 to about \$850 billion this year, an increase of \$65 billion, or about 8.3 percent. A little less than 5 percent of this will be *real* and about 3.5 percent will be the result of an increase of prices. Our pattern is for a stronger first half, with GNP rising by about \$38 billion. The rate of expansion in the second half is expected to decline somewhat—to \$27 billion. We anticipate that the unemployment rate will remain below 4 percent and that the workweek will lengthen somewhat. We also expect that labor compensation will increase at 6–6.5 percent annual rate.

The higher rate of expansion in the first half is based on (1) the buildup of steel inventories in expectation of a strike on August 1; (2) a catching up of automobile sales and production after the strike of late last year; and (3) an increment of \$5–5.5 billion of personal income due to the rise of the minimum wage rate and social security benefit payments.

Turning to the components of GNP, we are estimating that personal consumption expenditures will increase from \$492 billion in 1967 to \$526 billion in 1968, or by 7 percent. As indicated earlier, we are not counting upon any significant decline in the rate of personal saving. Consumer confidence will still be affected by uncertainty about Vietnam and taxes, as well as by rising prices. In spite of a high rate of personal saving, encouraged by record interest rates, the sharp rise of personal incomes which we are estimating will produce the 7 percent increase in consumer spending.

Aside from the rise of personal income, there are two factors which explain our forecast of a 10 percent increase this year in expenditures for durable goods. One is that we think that total sales of automobiles will rise to about 9.1 million cars. The other is that we expect housing starts in 1968 to total about 1.5 million units, thus swelling the demand for durable consumer goods.

Turning to government purchases of goods and services, we are estimating that Federal defense expenditures will rise by \$5 billion, or 7 percent. This is in line with budget estimates. Our figure is likely to be far under the mark for two reasons. Even under the Federal budget there probably will be an updrift of defense spending of about \$2 billion. Beyond this, if we increase our troop commitment by as much as 100,000, we could be involved in a defense spending increase of \$3–4 billion at a minimum. The increase of "other" Federal purchases of goods and services is in line with the budget. The 12 percent increase of state and local government expenditures is in accord with the experience of the past several years, which we do not expect to change.

Under our model, gross private domestic investment is expected to increase by \$17 billion in 1968, or 15 percent. Under "fixed investment", we are estimating that the nonresidential portion will rise by 7 percent. This is somewhat higher than the 5–6 percent increase indicated by the various surveys of capital spending. In periods of general business expansion, the capital spending surveys usually undershoot the mark. We think this will be true in 1968.

Residential construction expenditures in the fourth quarter of 1967 were running at a \$28 billion annual rate. Our pattern calls for a rise to \$29 billion in the first quarter of this year and then level at a \$30 billion annual rate in the last three quarters. We expect that the total of housing starts will be somewhat higher in the first half than in the second, with the rate about 1.5 million starts for the year as a whole. Rising prices will hold up the total expenditures in the second