

RISE IN UNEMPLOYMENT BUT PRICE INCREASES TO CONTINUE

The forecast growth in gross national product is too slow to absorb the expected new entrants into the labor force and still compensate for rising productivity, and will be accompanied by rising unemployment that we expect to reach 4.5 percent of the labor force by the end of the year.

Despite slower growth and rising unemployment, however, prices will continue to rise at almost the same pace as during 1968. The reason for this is the backlog of undigested costs now in the economy. Producers cannot respond instantly to changed conditions, and there is necessarily a delay between the time a firm finds its costs rising and the time it can make appropriate price adjustments. Moreover, higher output prices of material producing firms represent higher input costs to their customers, and there is further delay before prices rise at the next stage of production. Our calculations indicate that it takes an average of 3 years before an initial increase in unit cost fully emerges in prices of final output, and for this reason any slowdown in the rate of economic growth has its first impact on jobs rather than on non-farm prices.

UNDERLYING COST PRESSURES REDUCED

Although the rate of price increase will be largely maintained through the year, underlying cost pressures will diminish and less inflationary steam will be generated beneath the surface than has been true in the recent past. Employee compensation per man-hour is forecast to rise only 5.5 percent this year, in contrast to recent rates of increase of almost 7 percent. With normal productivity increases, this implies a rise in unit labor cost of only 3.5 percent, a decline from rates of increase of 4 and 5 percent recently experienced. In other words, although rapid price increases can be expected to continue through this year, we are slowing the buildup of costs on which prices during 1970 and 1971 are going to depend. If slow growth in total output is maintained, the rate of inflation will be substantially abated by that time.

DIRECT MEASURES ARE NEEDED TO CHANGE THE TRADEOFF BETWEEN INFLATION AND UNEMPLOYMENT

Although maintaining slow growth through 1970 can bring the rate of price increase back to something like 2 percent per year, our analysis indicates that this slow growth will be accompanied by rising unemployment which will take us back to the rates of joblessness in excess of 5 percent that characterized the years from 1958 to 1964. During that period, prices as measured by the implicit deflator for the gross national product rose from their 1958 base of 100 to only 108.8, an average annual growth of only 1.4 percent. But this price stability was purchased at the cost of unemployment that never involved fewer than 5 percent of the labor force, and during 2 years averaged over 6 percent.

To put the matter another way, the present rate of price inflation is not the result of special economic "distortions" that can somehow be untangled to yield stable prices without loss of jobs. Rapid price infla-