The Business Situation

As is frequently the case, economic activity got off to a relatively slow start in the new year. In January, industrial production, payroll employment, and retail sales were virtually unchanged, while housing starts dropped sharply. The lackluster performance was at least in part, however, attributable to unusually severe weather and to several major strikes. The more encouraging developments in January—a rise in new orders for durable goods following two months of decline and continued strength in consumer buying intentions—were registered in indicators that normally are not particularly sensitive to weather conditions. For February, fragmentary data suggest some rise in steel ingot production, a continued high level of automobile assemblies, and little change in retail sales.

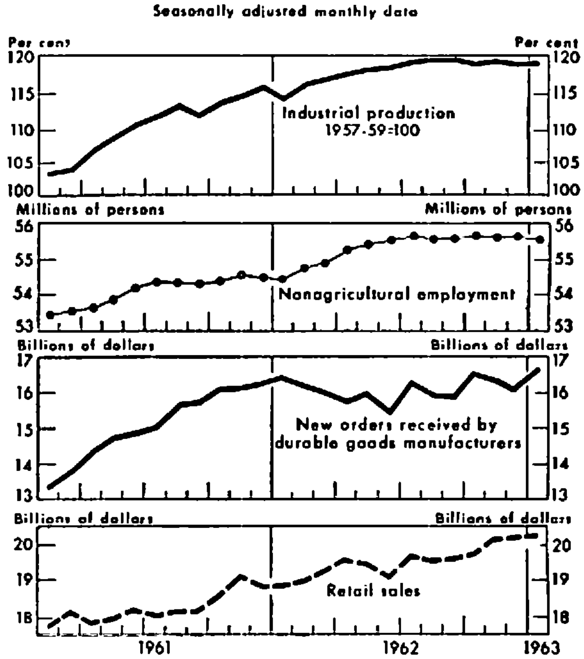
The prospects for tax reduction continue to dominate most appraisals of the over-all economic outlook. Although the Administration has continued to emphasize that it is not predicting an economic downturn for 1963 or even for 1964, the President noted in a recent speech he was "willing to venture" that without a tax cut the country would "in the not-too-far-distant future be struck by its fifth postwar recession". For this reason he indicated that he considers "the important thing" is to get a tax bill this year that would provide for a tax reduction of at least $10 billion over the next three years, even if this meant substantial modifications in the tax proposals he submitted to the Congress in January.

PRODUCTION AND EMPLOYMENT

The Federal Reserve's index of industrial production remained at 119 per cent of the 1957-59 average in January, continuing at the level which has prevailed since June of last year (see Chart I). Relatively little change in production levels was also the characteristic pattern for most major industries, with the only sizable gains being shown by producers of consumer home goods and of electricity and gas. Of course, unusually severe weather probably accounted for much of the advance in the output of electricity and gas. On the other hand, part of the lack of vigor in over-all production was due to unusually cold weather and severe snow storms that blanketed large sections of the country in the latter days of the month and prevented some workers from getting to their jobs. Moreover, there is some evidence that the East and Gulf Coast dock strike, which was not settled until late in January, tended to curtail production in industries that depend on imports for their raw materials.

Weekly production figures for February suggest that new cars are continuing to come off the assembly line at a seasonally adjusted annual rate of about seven million units, close to the level that has prevailed since last July. The industry planned to have a record of slightly more than one million cars in dealers' inventories by the beginning of March, in preparation for the spring sales push. In the steel industry, ingot production continued upward in February and substantial bookings are said to be already in for March. While these orders undoubtedly included some destined for protective inventories being built up in anticipation of a possible steel strike or price rise, the amount

Chart I
CURRENT ECONOMIC INDICATORS
Seasonally adjusted monthly data



Sources: Board of Governors of the Federal Reserve System; United States Departments of Commerce and Labor.

was believed to be relatively small. A more substantial protective build-up does seem in prospect, however, unless labor and management reach a noninflationary settlement in the not-too-far-distant future.

The employment situation in January was also influenced by strikes and inclement weather. Total payroll employment remained virtually unchanged for the eighth consecutive month (see Chart I). Cold weather continued to impede outdoor work in construction and about 70,000 transport workers, according to Labor Department estimates, were out of work as a result of the longshoremen's strike. In manufacturing, employment and average weekly hours edged off slightly, largely reflecting cutbacks in the apparel and automobile industries. A decline in the number of initial claims filed for unemployment compensation in February suggests, however, that adverse factors may not have been so significant in that month.

INDICATORS OF FUTURE DEVELOPMENTS

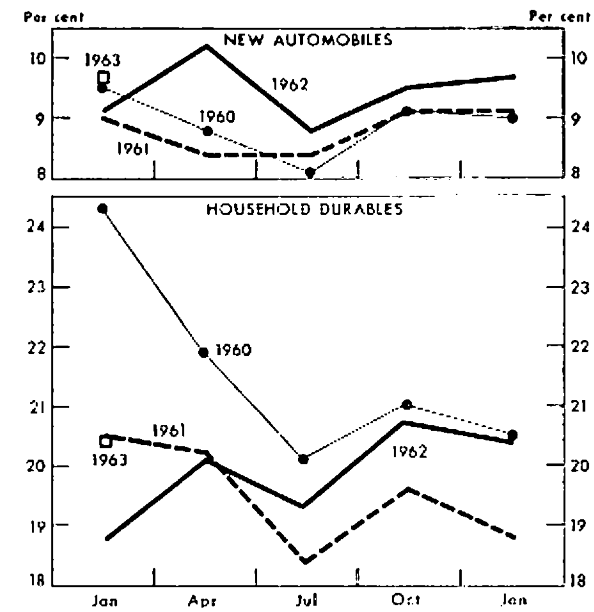
In contrast to the lack of change shown by measures of current activity, new orders received by durable goods producers rose by 4 per cent in January, following two months of decline (see Chart I). The bulk of the January advance came in the steel industry, but machinery and aircraft industries also reported modest gains. Although no conclusive data are available, there have been scattered reports that some firms are beginning to step up equipment purchases in response to the Treasury Department's revised depreciation schedules and the new investment credit legislation. Whatever the cause, however, orders for machinery and equipment have risen in three of the last five months and, in January, were 3 per cent higher than last June.

Forward-looking indicators of residential construction present a mixed picture but, on balance, imply no weakening from recent high levels. On the one hand, new building permits issued rose markedly in November and December and then held near the high December level in January. In contrast, private housing starts fell sharply in both December and January. Housing starts in January made their worst showing in the northeast and north central regions of the country where weather was particularly bad, whereas in the western region the number of new starts rose substantially. A similar siege of bad weather had curtailed starts at the beginning of 1962, but starts then spurted in the spring as weather conditions improved.

The consumer sector continues to be a major source of strength in the economy. While retail sales showed almost no change in January, they remained above $20 billion (seasonally adjusted), a level that has been exceeded in only three months since the series has been in existence (see Chart I). Moreover, this high level was maintained despite a weakening in the latter part of the month that may have been caused by adverse weather. In addition, of course, newspaper strikes in New York City and Cleveland made it difficult for stores in those cities to advertise their post-Christmas sales. Indeed, sales by New York City department stores so far this year have been about 7 per cent below the year-earlier volume in contrast to an increase in the rest of the nation. Partial data for February suggest little change in unit sales of new automobiles as well as in the volume of other retail sales.

Chart II

CONSUMER INTENTIONS TO BUY NEW AUTOMOBILES AND HOUSEHOLD DURABLES WITHIN SIX MONTHS



Note: Buying plans are expressed as the ratio of the number of families who say they intend to buy to the total number of families in the survey.

Sources: Board of Governors of the Federal Reserve System; United States Department of Commerce.

That consumer spending may continue strong in the months ahead is suggested by the Census Bureau's latest quarterly survey of consumer buying intentions. Plans to buy new automobiles in the next six months were slightly above the levels of a year earlier, while plans to purchase household durables showed significantly greater strength than at the beginning of 1962 (see Chart II). While previous experience is, of course, no certain guide to future performance, it is noteworthy that the high level of buying intentions during 1962 was accompanied by rather sharp increases in total purchases of durable goods in both the first and second halves of the year.