End Of The Year Review Of America's Economy; Future Forecast

By Richard B. Roberts
Senior Vice President
Wachovia Band and
Trust Company, N. A.

The biggest economic news of 1981 was the philosophical change in direction characterized as Reaganomics. The basic premise of the new economic program is that lower taxes and greater savings incentives will, over time, bring about gains in investment and productivity, reduce the rate of price inflation, move interest rates downward, and increase the pace of real economic growth.

Since the first phase of the Reagan Administration's program only became effective on October 1, it cannot be blamed or credited to any significant extent with the bad or good economic developments of the year. Except for the psychological impact of tax and budget cuts scheduled for the future, the business scene over the past twelve months has been largely dominated by the momentum of entrenched forces and programs originating over many years past.

During 1981, fiscal and monetary policies continued to work at cross purposes with each other. The budget deficit remained large and stimulative. Persistent price inflation, weak money supply growth, of strong financing needs by both government and business drove interest rates to record heights. Depressed conditions existed throughout the year in the housing and automobile industries, but recent data suggests that a much broader contraction is now under way.

The tug of war between fiscal and monetary policies has caused the economy to follow an erratic up-and-down course since the fall of 1979. This is evident in the profile of real gross national product changes for 1981: first quarter up 8.6 per cent; second quarter down 1.6 per cent ; and third quarter up 0.6 per cent.

The recent fall in industrial production, rise in unemployment, and behavior of numerous other indicators suggests a decisive drop in business activity during the final period. Interestingly, the softness in holiday season retail sales seems to be as much due to cautious stocking of shelves and lack of merchandise selection in some stores and lines as to consumer spending retrenchment.

Prospects do not appear good for a quick, vigorous or clear rebound. The statistical path of economic activity is not likely to be a smooth trend or straight line in any direction. There could continue to an erratic and inconsistant pattern of quarterly starts and stops which defies rational prediction or explanation.

For this reason, the first quarter of 1982 could surprise the forecasters with another aberration and bring unexpected growth in real GNP. The overall tenor of the economy seems to be represented in statistics and media reports as a bit more gloomy than the impression one gets from talking to many individual businesses and consumers, especially in this part of the country.

The most prominent concern in the outlook is the burgeoning size of the federal deficit, which some project to exceed $100-billion. This is the result of large tax reductions without comparable decreases in spending, despite a good effort to contain the rate of increase. When government expenditures exceed revenues, the amount of funds available for productive capital formation is reduced.

If the Administration's economic program is to have the desired effect, the government must bring down the share of savings and investment funds that it preempts and denies to the private sector. A large measure of statemanship and discipline will be needed from Congress during the 1982 election year to prevent further enlargement of the deficit.

A number of major labor contracts are due for renegotiation next spring, and the outcome of these settlements will have a great influence on the cost-push element of price increases for several years. During the last twelve months, inflation has slowed encouragingly from peak levels, and a moderation of wage and benefit demands should be expected.

A continuation of the better trend in consumer prices, couples with reasonable labor demands, and a declining federal deficit would make it possible for monetary policy to operate more effectively without producing such volatile money markets. A more stable interest rate structure at much lower levels is definitely required for a healthy economy. This is not likely to occur until the budget deficit is brought under control. Meantime, rates are likely to be erratic, but in 1982 should average below 1981 levels.

Cyclical and historical turning points in economic and interest rate trends are always hard to forecast. The difficulty is compounded now by the lack of experience with the new Administration's innovative and untested economic philosophy and policy. But, looking a recent cyclical developments and underlying fundamentals, a good case can be made for modest recovery beginning sometime in the first half of 1982 and, somewhat guardedly, for even more encouragement in future years.

Lower average money costs provide hope for some improvement in interest-sensitive sectors such as housing and autos which have a broad impact on the economy and where pent-up demand is accumulating. Housing starts fell short of basic need in the first two years of this decade. Also, automobile scrappage has begun to exceed production. Fuel prices remain relatively high, but have softened. Capital investment programs should begin to expand in 1982 as the demand for goods and services strengthens.

The American consumer has consistently disappointed pessimistic forecasters by displaying amazing resiliency in coping with painful inflation, high interest rates, and erratic economy and psychological uncertainty. Sustained abatement in price inflation, additional reductions of income taxes, and further stimulation by budget deficits should boost consumer spending as 1982 progresses. However, steady monetary restraint and nagging inflationary anxieties could cause interest rates to move up again as economic activity and private sector borrowing increase. This would tend to moderate the recovery.

For the longer run, there has clearly been a fundamental and favorable shift of historical significance in national policies and priorities. Turbulence, uncertainty, and a sluggish economy will likely accompany this basic change in course as the various stages proceed. One of the most critical contingencies in the outlook is whether enough of the tax cuts will be saved to help finance a major part of the budget deficits they create. If so, the prospects will be greatly enhanced for a gradually better outlook over the years ahead.

The North Carolina economy holds good promise for continuing its above average performance. The state's industrial development and diversification efforts have during the last six years resulted in commitments for over $10-billion of added capital investment estimated to create 170,000 new jobs. Some of these projects are still in the various stages of construction, staffing, and becoming fully operational. A modest but steady pattern of additional investments, new jobs and further diversification is expected to continue.

Nevertheless, the North Carolina economy will, as in the past, mirror national trends to a substantial degree. However, the more diversified employment profile and cautious inventory positions of major consumer goods industries should enable the state to fare better than the national averages in most meaningful measures of economic well being. A favorable comparison has thus far been clearly evident in an unemployment rate which has been consistently tracking well below the nation.

The upward trend of jobless figures for the state which began during the fall seems certain to continue through December, reflecting careful inventory control, shortened production schedules, and prolonged holiday closings. The lagging unemployment statistics announced in the current month and next month will probably look progessively worse. This could prove temporary and be gradually reversed in the first quarter as 1982 comes into clearer focus, spring and summer orders firm up, and inventory building gets more earnestly under way.

As has been true for many of the past several years, the performance of the state's and nation's economy for 1982 is likely to be closer to the optimistic side of the consensus forecast than to the pessimistic extreme. This is especially true for election years when the bias of fiscal policy tends toward stimulation. With enough perservance and vision on the part of the American people and their political leaders, the next year could bring the first stage of a slow but sustainable turn-around in the country's economic fortunes.

NOTICE

Primary Election Of 1982

Pursuant to G.S. 163-104, a Primary Election will be held May 4, 1982, and the second primary, if necessary, will be held June 1, 1982, with the County of Chowan, North Carolina.

Filing period for candidates will begin at 12:00 noon on January 4, 1982, and close at 12:00 noon on February 1, 1982, at the Board of Elections Office, Chowan County Courthouse, King Street, Edenton, North Carolina.

Chairman Board of Elections

Felix F. Chambers