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The Expansion Begins to Slow

By John O. Bornhofen

In mid-June, it appeared that the U.S. economy might be on the verge of an all-out boom. As of mid-September, however, that boom has yet to materialize, and a moderation in the growth of the economy looks more likely. Nevertheless, the strength of the current expansion has been extraordinary. Since the 1981-82 recession ended, real GNP (gross national product adjusted for inflation) has risen at an annual rate of $7\frac{1}{3}$ percent. This is stronger than the average of the post-World War II expansion and possibly the strongest since World War II.

In its wake, the expansion has added six million jobs. Total employment was at a near record 105 million in August. In addition, the overall unemployment rate has dropped as quickly as it rose earlier during the recession.

Yet, despite this torrid growth, inflation has not yet been reignited. All three of the major measures of prices show inflation running at or under 4 percent, not much different from the rate of the Consumer Price Index in 1982 and 1983.

At this point, there are signs that the economy's red hot growth is slowing, as it eventually must. To the extent that growth slows to a lower, more sustainable rate, the expansion and prosperity can continue. This would be most desirable. Despite the alarms of some, there is no danger of deflation; if anything, inflationary pressures are building, not disappearing.

The latest figures indicate very strong growth in the first half of 1984. The best overall measure of the economy—real GNP—grew at seasonally adjusted annual rates of 10.1 percent and 7.5 percent in the first and second quarters respectively. It was this performance that converted this expansion from average to well above average. The "flash estimate" for the third quarter just completed shows that growth is slowing. It shows a gain in real GNP of 3.6 percent. This estimate is subject to wide revisions when complete data become available, however.

This has been a good year for the labor market. The number of people working has risen three million, and unemployment has dropped 700,000 to 8.5 million for an overall rate of 7.5 percent of the civilian work force. Even though the unemployment rate has risen in recent months from 7.1 percent to 7.5 percent, the labor market still appears to be tightening. Surveys of future hiring and help-wanted ads both point to more hiring in the near future.

Buoyed by rising employment, rising incomes, and improved consumer confidence, consumer expenditures on nondurable and durable goods and on services have been strong since early 1983. Real consumption expenditures by the household sector in-

creased by 8.7 percent in the past year and a half.

From almost the beginning, however, this expansion has been driven by investment expenditures, primarily purchases of new equipment by business and by new housing production. So far, fixed investment by business and households has increased 30 percent since the recovery began. By contrast, government expenditures (federal, state, and local) on goods and services have been flat, and net exports were down during that same period.

The extraordinary performance of investment expenditures in this expansion has occurred in spite of the very high interest rates and moderate level of stock prices that make for high capital costs. The strength of business investment reflects, among other things, the tax incentives in the Economic Recovery Tax Act (ERTA) of 1981, the strength of the recovery, the belief that the expansion is real and durable, the expected profitability of new investment, and the attempt to increase productivity by replacing obsolete and high-cost equipment. Demand for new housing has been very strong until just recently. Now it appears to be backing off in the face of high mortgage interest rates.

Net exports—the difference between U.S. sales of goods and services to the rest of the world minus our purchases from them—is now at record lows. Our second quarter net export figure of -\$58 billion in current dollar terms and -\$10 billion in real terms reflects the extremely rapid growth in our imported goods and services relative to the much slower rise in our exports. This condition reflects the high value of the American dollar in the foreign exchange markets, the rapid growth in American incomes during the expansion, and the decline in exports to parts of the Third World. The decline in exports reflects belt-tightening by developing Third World countries in return for International Monetary Fund assistance in restructuring their debt to the international, mainly American, banks.

Net exports have been worsening every quarter for over a year and a half but may stabilize now that the economies of some of our major trading partners are recovering more rapidly from their recession.

Consistent with the strong increase in GNP, industrial production by factories, mines, and utilities has been increasing strongly—at a 10 percent annual rate so far this year. Demand has been so strong that capacity utilization in manufacturing is now over 82 percent. This is the area where we typically encounter increasing cost pressures. But since productivity is still rising in a healthy fashion, unit labor costs are still under control. Productivity per hour worked is up at a 4 percent annual rate so far this year, and unit labor costs are up just over one percent, about in line with last year.

In the financial markets, long-term rates have drifted down over the last two or three months and stock prices rose sharply in late July and early August as a result of the falling long-term rates. Short-term rates, however, have continued to rise unabated since the beginning of the year. One alarming fact is the rapid rise in long-term interest rates so far in the expansion. Even with the latest downward movements, long-term rates are still two percentage points higher than at the beginning of the expansion. Typically, long rates hold steady during the early years of an expansion. The exceptions have been the very short recoveries of 1958 and 1980.

All in all, though, the overall level of interest rates is still very high, and the financial markets continue to reflect the effects of the large Federal deficits plus the tightening of the stock of money in the summer. Although the monetary policy of the Federal Reserve is essentially unchanged, the M_1 measure of the money stock is back to where it was at the beginning of the summer. This appears to be the result of a decline in the "money multiplier" rather than any reduction in reserves or monetary base available to support the stock of money. Since M_1 is at the lower end of the Federal Reserves target range, it should grow in the near future.

Indeed, there is no reason for Federal Reserve policy to tighten. Inflation has been under control, and until it begins to flare up again, policy should remain unchanged. It also goes almost without saying that with the economy growing as fast as it has, neither has there been a reason to move to an easier money policy.

The fiscal policy of the Federal government continues to be very stimulative in the direct sense. Although they are declining, the big deficits still mean that Federal spending is putting more demand into the income-expenditure stream than Federal taxes are taking out. The deficit is currently running at about \$165 billion for fiscal year 1984. And even worse, the projections are for future deficits in the "out years" to be even higher.

Since the deficit must be financed, additional pressure is put on interest rates, and the high rates, in turn, have adverse but uneven effects throughout the overall economic system. The high rates are holding down new housing production, American exports to the rest of the world, and American lending to foreign countries. The U.S. is now in the rather unfamiliar position of being a net capital importer. This makes capital formation more difficult for the rest of the world.

While the deficit is receiving a lot of attention in the media and from politicians lately, no one has proposed a program of bringing it down substantially in the near term. The politicians are all looking for painless solutions,

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Conclusion and Implications

Our findings suggest that educators and marketing executives are in solid agreement on the relative desirability of the stated marketing curriculum objectives. In addition, both appear to be in reasonable accord on the "core" marketing courses needed in the curriculum to achieve these objectives. However, with the exception of case analysis, the groups differ on the educational techniques that should be used in presenting these materials to the students. Clearly, the practitioner groups would like to see more "hands-on" techniques used, e.g., internships, computer simulation, and field trips.

The implications of this study for educators suggest that a core marketing curriculum should include: (1) marketing research, (2) marketing management, (3) marketing problems, and (4) advertising/communications. Further, to reflect practitioner concerns, marketing electives should be offered that emphasize quantitative analysis, e.g., quantitative

marketing methods and models, forecasting, etc. This study also suggests that the consumer behavior course be an elective rather than a requirement.

Finally, our study suggests the need for marketing educators to integrate additional educational techniques in teaching their courses. Clearly, practitioners want more experienced students, and educators are challenged to meet this need. Not only may this integration of teaching techniques be pedagogically superior to less integrated formats, but such experience may also provide students with a decided advantage in the entry-level employment marketplace.

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The Grand Rapids Economics Index

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index, compiled for the Grand Rapids area, shows that Grand Rapids is continuing to move toward good times. Not all of us feel that. Prosperity is not shared uniformly by all. But it can be said that more people are working and more paychecks are being received and spent on goods distributed by Grand Rapids retailers. The worst of the recent years were 1980 and 1982. It looks as though 1984 will be another good year.

The composite index is made up of a weighted average of five economic indicators: bank debits, retail sales, residential and non-residential construction, industrial power consumption and employment, all of which are adjusted for seasonal variations and for the effects of inflation.

An index has been prepared for the United States which makes use of approximately the same components that make up the index for Kent and Ottawa Counties. The movements of this index are shown on an accompanying chart, which gives some evidence of how local economic activity compares with national economic activity. The composite U.S. index is correlated with real U.S. Gross National Product movements. These movements reflect changes in the general economic health of the U.S.

The index and its components are prepared by Dr. William Peterson, Professor of Economics at GVSC. Inquiries and detailed facts about the index can be obtained by writing to Dr. Marvin G. DeVries, F.E. Seidman College.

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but there aren't any. Taxing the "rich" (translation: upper income) and business corporations will close only part of the deficit and will have only minimal impact on interest rates because it will cut private saving more than would even-handed tax increases and expenditure cuts.

The major clouds on the horizon are the effects that still higher interest rates would have on Third World borrowers, some of whom might declare a moratorium on their debt service payments to big American banks if rates rise further. This is a potentially explosive problem with possible disastrous implications for all of us if it is mishandled.

The other problem stemming from our high level of interest rates is that they could cut the expansion short. Although this does not ap-

pear to be the case for the near future, the slowdown appears to be beginning. The other major cloud—the auto strike and its effects on the economy—appears to have been cleared up. At this writing, the strike has been settled and there is optimism over worker ratification. Its effects should be made up shortly and the economy's progress hardly impeded. It is unclear, though, what the effect of the settlement will be. That could be worse for the economy than the strike itself.

The outlook for the rest of 1984 and the first part of 1985 is still pretty good. Although the expansion appears to be slowing, there should be no imminent danger of recession. But a perusal of economic indicators—leading, coincident, and lagging—does show that, at minimum, a slowdown in growth is occurring. Thus, real GNP is expected to in-

crease around 3-4 percent over the next six months. Incomes and employment should continue to rise but more slowly than in the recent past, and unemployment could fall to near 7 percent in early 1985.

Inflation, which has been remarkably subdued, could start accelerating slowly in early 1985, but double digits are not imminent. Interest rates, then, will depend on what happens at the Federal level to reduce the deficit. Without meaningful moves in the direction of lower deficits, it is difficult to find credible reasons why rates will decline.

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