pstau001165001.wav / Tape 183 - Outlook at midyear / Duke Digital Repository

---

- Welcome once again as MIT professor Paul Samuelson discusses the current economic scene. This series is produced by Intstructoral Dynamics Incorporated. Professor Samuelson, we're now past the midpoint of the year the time when many economists have predicted the turnaround would come. How is that turn around coming?

- In the middle of 1975, the outlook certainly is less gloomy than it was at the beginning of the year. One of the reasons perhaps is the fact that all over the world there's been an increase in stock prices, common stock prices. Which country do you suppose has been the best place for an American to invest his money? Taking account what the appreciation has been in dollar terms, In other words, if the German mark has gone up or the Swiss frank has gone up, then that might be an extra source of remuneration for the investor who on New Year's Eve put in his money into one country or another. This is a good time to take stock because 6 months and 10 days so to speak, have passed that you can now cash in your long-term capital gains. Or if the spirit moves you, you can let your profits ride. It is a case of profits without exception. Well I don't suppose anyone would be able to guess but it is the Hong Kong stock market. It's a very volatile market. It's a good place to make a lot of money. It's also a good place to lose a lot of money. That's gone up 96% in the first half of 1975. Converted into dollars. Dollars at the beginning and dollars at the end. Any change in the floating exchange rates being allowed for. Not surprising you say, because Hong Kong is a citerdo of three private enterprise. It shows what can happen when laissez faire is allowed to do its best or its worst. But you may be surprised to know what the second best stock market of the world has been. It's been the United Kingdom. 73%. And this despite the weakness of the pound. A pound that has gone down. In fact, if you had put your money in pounds in the UK stock market, you'd have the highest rate of profit of all. You'd have 83%. But looking at it selfishly from a dollar standpoint, the depreciation of the pound that has finally come. Most of us thought it was on its way. Even before it was on its way. You'd still have 73%. Perhaps it shows that equities at some states of the game do become something of a hedge against inflation. Or perhaps it shows that in a directed world or an over-directed world, you might as well have an interest in an equity. As in depreciating currency or fix principal investment. Well, third you may be happy to learn is the US. The Dow Jones average, if you use that particular average, is 41.7% up from January 1st to June 30th. No need to convert that into dollars. It's already in dollars. And that perhaps gives us slightly exaggerated notion of what the whole market in America has been doing. Because 38.3% and the standard import is 500, is perhaps a more even-handed comprehensive average. You'd have done better than that I should say though if you'd been in risky over-the-counter stocks. Just those in an NASDQ index, would've shown an appreciation of 61%. And the AMEX, American Stock Exchange Index, has gone up 54%. As usually happens and it's interesting to speculate as to why this happens, an unweighted average of stocks like the value line index of 1,500 stocks, which industrials, which is a very biased index is biased downward being a geometric mean. The fact though that it gives equal weight to a General Motors and to American Motors, even though there's a heck of a lot more dollars out of value in General Motors than in American Motors. It shows a 60% increase in this period. You pay for this on the downside because a, an unweighted average, just an average of every stock by name, not by, weighted by value, goes down a lot more. And went down a lot more from 19, say 68 to 1973 than did the Dow Jones average or the S&P 500. Well, after that comes

Switzerland, helped, you may be sure by the appreciation of the Swiss frank in dollars terms you'da made 33% in the Swiss market. In other words, you've benefited, well not so much. The Swiss frank has only gone up by about 2% in this particular period. After Switzerland comes Australia. Australia has its ups and downs and last year I recollect that it had its downs. Well it's up 23%. Even Japan, with all of the travail it has been going through is up by 23%. The Netherlands to a dollar investor 21.6%. The German market, lagged really in the sweepstakes, up 19 and a half percent. This despite the fact that it was helped by a 2 and a half percent appreciation of the mark against the dollar. In the case of the Belgian stock exchange, it's 19%. The Canadian stock exchange, 16.2%. Interesting. That lagged behind the American recovery. Italy, which goes from distress, to distress, to triumph, to distress, had an increase of 12 and a half percent. And then perhaps because of some Emersonian law of compensation, alas on this particular list that I have is Austria. Which went up only by about 5%. However, it was Austria that you may recall which last year lead the sweepstakes. So the story would be quite a different matter if you'd taken a 2 year time span. Of course, you could've invested in other things than common stocks. For example, you might have invested in gold. Where would you stand at mid-year in comparison with the beginning of the year? Well you'd be 12% out on your, on your money. That's in addition to having to pay storage costs and various other fees. And of course there are no dividends on a simple gold holding. Still, that's better than if you'd put your money in the Dow Jones commodity index in a long position, thinking of that as a hedge against inflation. Because sensitive prices have on the hold been coming down. You'd be out 30% in such an investment. Silver, that's a perineal favorite with the, not the ribbon clerks, but with the MD's and the professional people. 5% is what you'd have made. A Dow Jones index of 40 bonds, case you wanna take a flyer in the bond market, would be up 5%. And since I suppose those bonds put on the hold give you long term bonds, about 8%. We might increase that to a 13% rate. Not, not very bad. Well, you can believe that sentiment among the establishment classes is better with this kind of a stock market rise just behind us. It's amazing how much of the animal spirits and the degree of optimism and pessimism of the middle classes and the upper-middle classes, I suppose there are no upper classes anymore, is a just reflection of what's been happening in the last 18 months to their stock market holding. THere's many a happy home, balance-sheet wise, at the mid year in comparison with the beginning of the year in terms of stock market. And this means, of course, billions of dollars of net worth in the aggregate. Most sophisticated analysts of consumer spending take as the first approximation of consumer spending. The flow of income available to spend. But to a second approximation, they do take into account the stock of wealth or net worth of individuals. And that net worth number had been decimated. It had lost at least 1 in 10 in the recession, but by the same token, it's what has been coming back. Although trips to Europe I understand are languishing this year except for cheap group charter flights. It's this sort of appreciation which gives rise to purchase of big-ticket items. To Mercedes, and small Cadillacs. And trips around the world. This could all be made quantitative by that kind of metric investigation. But let me pass on to another aspect of the problem. A high price for stocks relative to the dividends that have to be paid, and a rising price of stocks, means that the availability of equity capital to corporations desirous of increasing their liquidity by floating new stock issues becomes more favorable. And that indeed has been the case. We've seen a whole rash of new issues brought to the market in the first half of the year. It of course has long been awaited by the investment bankers, by First Boston Corporation, by Morgan Stanley, because there were some pretty lean days for such investment bankers during the worst of the recession last year. Fortunately, they would say, there was a need and a desire of firms to issue debt securities that kept them paying their overhead. And so two, another part of the moral of the story, the analysts who do the best job, I won't say at predicting the future of GNP, but the best job at describing and understanding what's happening in the GNP models like that of Professor Modeliani and his colleagues at MIT pan, former federal reserve board model. They also build into their investment equation a favorable availability and favorable cost of capital component when the stock market goes up. It's curious that we economist fight the conclusion that an increase in the stock market has a causal association with the buoyancy of business. It's what every vulgar non-economist, and for that matter, every refined non-economist, believes he absorbs that with his mother's milk so to speak, but the economist tend to resist that conclusion and yet as Professor James Tobin of Yale pointed out at a conference of economist a couple of years ago, it's one of the simplest positive correlations that stands out in the economic time series of this country and of many other countries and cross-sectional analysis. Somewhat substantiates what the Times or Series story seems to be telling us. Well consumer sentiment as measured by the various polls, and here we're now sampling by telephone or by scientific sample interrogation and interview, a much wider class of people than those who own any appreciable amount of common stocks. Consumer sentiment is way up from the trough of despair of last Christmas to Valentine's Day. The index of consumer sentiment that anabor group survey records, or that the conference board records, or various private organizations are still by no means telling a rosy story. They're no where near their previous optimistic peaks but they're a good deal up from the trough of despair which characterized the American economy and I dare say an economist from Western Europe or from Japan could have told pretty much the same story last Winter about consumer sentiment in those countries. I've read somewhere that the Japanese recovery which has been slow in coming and getting underway, has in part been the slow down by a wave of extra thrift, or thriftiness, that has swept over the Japanese consumer. For the first time in a long time, he's not spending as if money were going out of use. It's because I suppose, for the first time in a long time, the money income of the Japanese family cannot be expected to rise by 15 or 20% and prices are still rising I think in Japan on double-digit bases. For the first time in a long time, a Japanese family cannot look ahead to the next ten years and expect to have an improvement factor in real terms of perhaps something like 7 to 10 to 12 percent. The Japanese government doesn't know how fast it can grow prudently or even how fast it's likely, actually, to grow. And the same uncertainty that besets the government forecasters must be shared by the ordinary person in the Japanese street. Well, where do we stand, not with respect to the stock market, but with respect to the American economy? If we have already gone through a V-recovery, it must be one of the best-kept secrets in the annals of economic history. It's possible that the GNP, if we're calculated on a real monthly basis, that it reached its trough in March or in April. The towns and greens and Greenspan Organization makes a rough calculation currently of monthly GNP. And I recollect that their estimate showed that the turn as measured by that indicator came before May of 1975. Yet, analysts are still in doubt as to whether the turn has taken place. I conclude from this that in all likelihood, the turn is a fairly gentle one, describable in its local features, that is it's March to let's say August time span as a much more of a U than of a V. The history books will still be able to resurrect the notion, fiction if you like, of a V-turn if what happens between mid-1975, just a little while ago, and one year from now, mid-1976, records an average rate of real GNP growth of the, let's say, 8%. Something over 7%. That would fit in with the notion of a longer-term V. But that kind of a V is still consistent with a local bottom that looks like a U. Those who follow inventories most carefully are not convinced that the inventory decummulation is already at an end. Particularly in the durable goods fields. Now the hero in this scenario has been consumption. Chain stores sales as measured, let's say by Crezgy's, as measured by Woolworth's, as measured by JC Penny's and a bit more disappointingly is measured by Sears Robuck, behaved well in June. The spending occasion by the tax rebates is presumably now beginning to take place and on its way. I've had occasion to comment more than once on the view that you hear so often that this term came without the help of the tax rebate and the fiscal stimulants. In the first place we don't really know for sure that the turn has come. But in the second place, what's been happening is very close to what the consensus forecasters were saying would be happening for the months that we're going through. And, I must remind all of us that those census, consensus forecasters, built into their consensus forecast the fiscal stimulants voted by Congress and not vetoed by the President. So where we are, apparently, as far as the prudent judge can tell, because of the fiscal stimulants. The fiscal stimulus actual and the fiscal stimulus anticipatable. So there's no reason to say that it's been independently of the fiscal stimulus that the Great Depression has been avoided. We shall never know what would've happened if we hadn't had the fiscal stimulus. THat's the limitation under which every economic historian must labor. You can never know what would've happened if history had not been what history turns out to be. But it's one thing to agree with what is almost a banality. Namely that in the absence of fiscal stimulus. At some point, whether it be in mid-1975, or late-1975, or mid-1976, the recession would have come to an end. But would it have come to an end with the same peak amount of unemployment that we are expecting with the fiscal stimulus. And it seems to me that the bulk of experience and plausible ways of analyzing that experience would argue against such a particular view. Since I've spoken about employment, let me say more. The numbers came in for June of only 8.6%. That looks as if we really could celebrate because it was 9.2% in May fishell number. And the fishell number is 8.6% in June. But I must congratulate the commissioner of the Bureau of Labor Statistics, Shush Shishcanow, he's been handling this particular bit of news. He pointed out in May in announcing the figures, I mean in June announcing the figures for May, that the 9.2% was spuriously high because of a faulty seasonal correction method. And that inconsequence of Mays' being so high, we would find in June, that the June number would be lower as it has turned out to be. But that would be true even if there'd been no basic improvement in the unemployment situation. The reason is not hard to describe in gross detail. About the same number of college students and high schools students pour into the labor market this year, a deep recession, as last year before we were in the deep recession. Or the year previous to that when we still were riding pretty high. If you use as your seasonal correction and assumption that there's always the same percentage increase in unemployment due to this factor, then in a year of deep depression, it turns out that there's only of the same number of people going onto the labor market. That's a smaller fraction of the higher unemployment. And so it's a poor method of seasonal correction. If you could recognize it while it's happening, the question one must ask is why couldn't you recognize in advance and have a better method of seasonal correction to allow for what is predictable, what is a predictable aberration. Now I think Dr. Shishkin was right, Mr. Shishkin was right not to change in mid-screen in May because it would look as if he was trying to cook the figures. But I think that last year there should've been thought about this, or better still, when the programs on the computer were being devised several years ago. There should be a better method of seasonal correction and let's hope that this won't happen again. We still are looking at the housing industry and there has been some improvement there. And perhaps the pessimists are being confounded just as the optimists earlier were being confounded. But it still is a picture of rather modest rate of housing rebound. In the case of automobiles, the American cars seem to be gaining a little bit at long last on the imports. For one thing, there are a lot of, there aren't so many 1974 imports anymore which were selling at competitive prices. The new imports are not all that competitive in prices in part because the dollar, until recently, had floated downward. There's also a fact that there's the biggest liar contest going on now in what our rather inflated mileage claims. The best performance that any one of your cars ever runs in an official test is used in your advertising. And so as I've been reading the newspapers and listening on the TV screens, it now appears that those same American cars, which were doing so badly in mileage compared to the foreign cars, just some months ago, are now doing almost as well. Nothing's been changed in their engines, but something has been changed in the public image. I conclude by giving my opinion that the turn is behind us, that the year ahead is not likely to show that V, right hand of the V bottom, 8% rate of growth. But something measurably less than that. And so 4 to 8% I still think is about the only sensible range that one can give for what the real growth the American economy will be in the next 12 months.

- If you have any comments or questions for Professor Samuelson, address them to Instructural Dynamics Incorporated for 50 East Ohio Street, Chicago Illinois, 60611.