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THE WHITE HOUSE

PRESS CONFERENCE
OF
ALAN GREENSPAN, CHAIRMAN
AND
BURTON MALKIEL, MEMBER
COUNCIL OF ECONOMIC ADVISERS

EXECUTIVE CONFERENCE ROOM

11:20 A.M. EST

MR. GREENSPAN: I think we better get started.

Good morning, ladies and gentlemen. This is our last report of the Council of Economic Advisers. This is certainly my last full press conference as Chairman of the Council of Economic Advisers, and there are no maybes.

What I would like to do, to begin, is to point out a few things which are either immediately newsworthy or not directly in the report and are newsworthy.

First of all, I point out that, as we do every year, on page 221 in the report we introduce for the first time the revised unemployment rates; that is, the revised seasonals which were applied to the same unadjusted unemployment rates. The changes this year are quite small; however, they do indicate, as you can see, that in November and December the new seasonal adjustment factors have revised down those two months by .1, and are now 8.0 and 7.8. Our previous seasonals showed them in the official reports, as you know, as 8.1 and 7.9.

What I would like to do this morning is to briefly go over the outlook, and then have Burt spell out in summary form some of the key elements in the report and then open the meeting to questions for as long as you are willing to stay here and listen to us answer them. So just let me get a few pieces of paper.

I think it is fairly apparent now, looking at the movement of weekly data, monthly data, quarterly data, that we are reaccelerating, and that it looks as though we may end up with a rather sharp increase in GNP growth for the first quarter of 1977. It looks to be about double or more the 3.0 reported rate for GNP which was released this morning.

However, let me caution you a bit about that figure. I don't have the transcript of what Commerce discussed in detail at their briefing this morning, but we have, as we often do in these GNP figures, a problem with the price indexes. I won't go into the technical analysis of what the problem is, but periodically, for those of you who are aware of what the issue is, we have a spread between prices calculated using current quarter rates and prices calculated in the official base period. There is a huge difference this fourth quarter of about a half a percentage point in the growth rate.

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The more accurate statistic is the figure on the so-called chain index which is reported in the Economic Report for the fourth quarter and shows approximately a half a percentage point less in inflation than the official so-called implicit price index.

What this, in effect, means is that the real growth in the fourth quarter is really more accurately describable in terms of not 3.0 but 3-1/2 percent, and that the price inflation was approximately a half a point less, depending upon which of the various indexes you want to use.

Starting off from that base point, there are certain interesting data which I think tells something about the state of the recovery.

For example, if you get very crude monthly data, which we can create, it shows that we have approximately a 5 percent annual rate of growth between September and December of last year, and if you go from October to December, it is approximately an 8 percent annual rate of growth. These numbers are consistent with the 3.0 figure, which is the official published number.

Finally, the month of December itself is already well above the quarterly average, and one way of describing it is if, in fact, January, February and March -- that is, the first quarter -- were exactly equal in real terms to the December level, we already have almost a 3 percent annual growth rate for the first quarter, so that in a sense we are starting off the quarter with 3 percentage points in the bank and if nothing happens from here -- meaning it is absolutely flat -- we are already equal to the growth rate in the fourth quarter.

The reasons for this, I think, are fairly apparent. The strike at Ford had a rather significant effect on the numbers of the data. It was particularly depressing in the areas of non-residential fixed investment, and if one looks at the various components, it is fairly obvious that the October rate in the GNP was clearly depressed, and that is the major reason for this particular problem.

You also can come up with a fairly significant figure for the first quarter if you recognize that the published final sales figure in the GNP for the fourth quarter is 4.8 percent of annual growth rate, and if you adjust for this price problem I mentioned before, a more accurate estimate of real final sales in the fourth quarter is approximately 5.2 percent.

Since we have got such a depressed inventory figure in the fourth quarter, any return to normality will create again a rate of increase for the first quarter, which is fairly significant.

The reason I dwell on the first quarter is that whenever you do a projection for the year, it is very important that you start your forecast from the best observable observations for where you are at this current period.

The figures which we reported, as you know, in the budget at 5.2 percent for the year imply an average of 5-1/2 to 6 percent annual growth from the fourth quarter of 1976 to the fourth quarter of 1977. This obviously implies that the growth rates will be somewhat higher in the early part of the year because of the acceleration out of the fourth quarter and then simmer down a bit, although so far as we can judge at this stage we have a fairly solid, sustained type of forecast, using all of the assumptions and various governmental policies which we discuss within our Economic Report, and I won't repeat a number of those things because I assume that most of you have at least scanned or read it in some detail.

Having gone through this, what Iwould like to do is to turn the microphone over to Burt Malkiel and let him give you some general review of the contents of the report itself, and then we will open up to questions.

Q Alan, before you do, just to make it clear, when you say the first quarter might be double or more the fourth quarter, is it double or more the 3 percent as announced or double or more the 3-1/2 percent?

MR. GREENSPAN: Double or more the 3 percent as announced. In other words, the officially reported figure is likely to be that.

Q Six percent or better.

MR. GREENSPAN: Yes. Now remember, we are talking as of mid-January, and the only way in which we can evaluate is to try to capture as best we can where we are right at this moment and then extrapolate for the rest of the quarter.

Q Alan, before you drop this, you were mentioning and I got a little confused -- you said first if you went from September to December you would have a 5 percent annual rate of growth and if you went from October you got 8 percent. Is that correct? I thought we just had a 3 percent annual rate of growth from October to December.

MR. GREENSPAN: No. The 3 percent is the average of the fourth quarter of 1976 over the average of the third quarter of 1976.

MR. MALKIEL: What I would like to do is take a few minutes to highlight some aspects of the report, and I think particularly those dealing with somewhat longer term problems.

I think one of the aspects of the recovery that has been particularly troublesome from a longer term perspective is the weakness that we have seen in business fixed investment. Investment is weaker than usual at this stage of the cycle. You sort of look at past cycles and you find that we have really not come up as much as one might have expected. It is also weaker than expected if you take into account the cash flow of business, the state of excess capacity and the strong sales gains that we have had.

In other words, you sort of crank this into the models. Every one of the models that you use these variables, these sort of standard accelerated models and the ones with excess capacity, invariably are predicting more investment than we are actually getting.

This has been a very troublesome aspect of the recovery and we suggest in the report that risk factors are an important element now for restraining capital investment. We, in fact, present some evidence in the report why we think this is so.

You will recall when we had this press conference a year ago we indicated at that point the capital needs study that the Council had done, where we specifically argued that if full employment was to be reached in 1980 and we were to reach our environmental and energy goals that we would have to have a much larger share of investment devoted to GNP. Specifically, we said we would need 12 percent of GNP devoted to fixed business investment for the last half of this decade.

The investment last year was just over 9 percent of GNP, and, even with the recovery that we are forecasting, it is still going to be well below 10 percent next year.

It is quite possible we overestimated our investment needs. For one thing, it seems very clear that we are not moving rapidly to meeting our energy goals. And you may say, "Okay, maybe it isn't 12 percent that we need. Maybe it is a bit less, and, in fact, the energy goals might take off a couple of tenths of 1 percent, maybe even three-tenths of 1 percent." But no matter how you slice it -- I mean making the adjustments -- it seems very clear that perhaps it is even only 11-1/2 and not 12 percent that we need.

The study that we have done -- and in fact this is confirmed by Brookings studies and other studies that have been done -- show that we really do need a larger share of business fixed investment in the years ahead, and if we don't provide the economic environment that is conducive to getting this business fixed investment, we are not going to have a capital shortage in the sense that we have now got a natural gas shortage, but, rather, what is going to happen if we don't get the adequate investment is that we are going to run into capacity constraints, not in 1977 but well before full employment is reached, or we may fail to meet our environmental and other goals.

Perhaps most importantly, a slow growth in productivity is going to result, and with it a slow growth in living standards. I think this is really what the key is. Continued low investment is really a problem because along with continued low investment is going to go a very slow growth in productivity; and with a slow growth in productivity is going to go a slow growth in living standards.

In the report we present a detailed analysis of what I think can be really called a striking decline in productivity growth. We show, for example, from 1948 to 1966 private productivity increases were proceeding at an annual rate of 3.3 percent. From 1966 to 1973 the rate went down to 2.1 percent, and the trend rate has undoubtedly declined in the years since 1973.

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To some extent our analysis indicates that the changing composition of the labor force may have something to do with that decline in productivity because what has happened, is that, as we all know, the composition of the labor force has changed so that a larger percentage of the labor force is now younger and less experienced.

To the extent that youth is a problem, there is, fortunately, an automatic solution for that problem, namely, the passage of time, because as time proceeds, all the young people who have entered the labor force in the last few years will become older and more experienced.

There is another major determinant, though, of the productivity slowdown that will not have an automatic solution, and that element is this sluggish investment. Because of the very slow rates of investment in the last several years, coupled with the large increases we have had in the labor force, what has happened is that you have had really a striking decline in the growth of the capital -labor ratio, which simply means the capital and tools which each worker has to work with.

We have shown in our analysis that this is intimately related to the productivity slowdown, and this productivity slowdown is the major reason why the Council has revised downward its estimates of potential Gross National Product. By "potential GNP" I mean the GNP we could have if we were operating at full utilization of our labor and capital resources.

Previous estimates of the CEA suggested that the gap between actual output and potential output was 11 percent. With our new estimates incorporating the effects of the slower productivity growth, the gap is now reduced to 7 percent. We present a number of reasons in the report why we have really been conservative, and we suspect that the gap may be even lower.

While these new estimates certainly still indicate that a strong economic recovery is necessary to eliminate the waste of unused capacity and the hardships of unemployment, they also provide a note of caution: that we probably don't have the slack that I think a number of people have estimated.

In talking about potential, there is one other aspect I think I ought to mention. There are really two elements that enter into the calculation of potential output. The most important is the growth of productivity, which I have just discussed. By and large, the major reason that we have reduced our estimates of potential is the slower growth in productivity. I mean, our estimates before assumed that there was not a slowdown in productivity growth, and it is quite clear there has been.

But there is another aspect of it. That is, the other element of this is the growth of the potential labor force. Associated with this is an estimate of what is called the full employment-unemployment rate.

In the mid-1950's, the CEA used a 4 percent figure as an estimate of what the full employment-unemployment rate was. In other words, we were saying that when 96 percent of the labor force was employed it was considered full employment of our labor resources.

The point here is that there is always going to be some amount of frictional unemployment. There will always be people moving from job to job. There will be new people entering the labor force looking for a job for the first time and there is bound to be some amount of unemployment. The figure of 4 percent had been used at that time.

Since the mid-1950's, however, there has been a really dramatic shift in the composition of the labor force, and in particular the proportion of youths in the labor force has increased sharply.

By the way, we define unemployment rates in the United States when a young person enters the labor force and starts looking for work, that individual is unemployed until he or she finds a job.

We always have higher reported unemployment rates for youths, even at full employment, because of this factor -- because there will be a number of them first entering the labor force and obviously there will be more youths in the process of looking for a first job than there will be older workers. For this reason, even at full employment, you know, even in periods when we have had 4 percent unemployment or even lower unemployment than that, we have had a much higher percentage of youth unemployment.

The point is, even if at full employment then, the youth unemployment rate is higher. If you then change the composition of the labor force so that more of the labor force is young, you are bound to increase the full employment-unemployment rate.

Another thing that has probably happened is that there does seem to be a tendency now for youths more to combine schooling and work. In other words, it isn't the case that you go to school, you leave school, whether it is high school or college, and you go in and work. It is much more the case now that youths will go to school for a while, maybe take off for a while and work, and then go back and forth. In other words, there is more entering and re-entering of youths into the labor market.

Again, by the way, we define our unemployment statistics, as long as there is more entering and re-entering, you are then going to have more of these short spells of unemployment and a higher reported unemployment rate.

The point is, then, because of these compositional changes in the labor force and the increased tendency of youths -- and I might say other groups as well -- to move in and out of the labor force with greater frequency, the Council has now estimated that what would correspond to a 4 percent unemployment rate in the 1950's is now a 4.9 percent unemployment rate. In other words, just with these compositional changes and the fact that there is more movement in and out, 4.9 percent would roughly correspond to what 4 percent was in the mid-1950's.

In presenting that figure, I am not presenting this as some immutable number that represents full employment. Indeed, as the composition of the labor force changes in the future, so will the full employment-unemployment rate. Indeed, one of the aspects of our estimation procedure is that this rate is going to change from year to year.

I might also add that much of the economics profession believes that, in fact, the true employment-unemployment rate now is probably somewhere between 5 and 6 percent because there are a number of other factors that have probably pushed up unemployment rates that we have not taken account of. Again, here we have tried to err on the optimistic side. We want to set our sights and goals high for the potential reduction of unemployment rates, but I think it is very important that we warn the public that if our estimates are inaccurate, they are likely to be too low rather than too high, and signs of accelerating inflation could well occur before we get down to the 5 percent level.

Having said that, there are several policy implications that at least seem to us apparent. One is that we really do continue to need cautious demand management policies in our return to full employment. We have a great deal of uncertainty as to what that potential level of output is. It may be even considerably lower than we have estimated it at. Too rapid an expansion that got us into capacity problems early and reignited inflationary expectations would certainly in the long run be counter-productive.

We have also argued in the report that to the extent we need fiscal adjustments, they ought to be done through tax reduction rather than through government spending. What we want to do is stimulate the private economy and private initiatives, because this is the way we are going to get the productivity moving and the productivity is really the key to getting improved living standards in the country.

We have also suggested for a number of reasons that tax reduction ought to be permanent rather than temporary. Just looking at it from the investment side, permanent reductions are much more likely than temporary ones to create confidence in the future and help spur investment.

We also think the tax reduction ought to be balanced between measures that stimulate consumption and some that rely directly on investment. For the same reason that I indicated that the models suggest that a simple accelerator -- that is, you stimulate final sales and that is going to get investment going -- precisely because our analysis indicates that those models are not working terribly well now, we suggest that we are not saying there is no accelerator mechanism, but simply that it could be usefully supplemented by direct measures to help investment.

Finally, as a policy implication, it appears very certain that the so-called fiscal dividend, the extra revenues that we are likely to have from getting to full employment, are going to be lower than had previously been estimated in terms of a 4 percent full employment-unemployment rate, and the old potential numbers. In other words, moving the potential down still means there is going to be a fiscal dividend, but it just is not nearly as great as we had estimated before. The difference is something like $30 billion in 1980 from our change in the full employment-unemployment rate, and more particularly from our recognition that productivity just hasn't been growing so quickly.

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Let me just say a couple more words about the international economy. The recovery here is now in its second year and, I think, as is not atypical at this stage of a recovery, there are, as you know, sufficiently mixed signs so that questions have been raised as to whether the worldwide economic recovery is in trouble.

There is no doubt that there has been a slowdown in the rate of growth for the industrialized economies. I think it is important to make clear that there is no real problem here. I think there is no question about economic stagnation in the world.

While the growth that is now forecast for the major industrialized economies may be slower than we might like to reduce unemployment rates sufficiently, I think it is clear that it will be near its long-term average, and the problem is not one of stagnation.

You know it has been very popular to talk about synchronization of the world economies; that we are all sort of moving up and down together in a synchronized fashion. Yet I think what we saw in 1976, and the situation is better now, is really the divergences of the things that have come up and been perhaps the big news.

In the Big Three economies -- the United States, Germany and Japan -- the main policy aim has been to assure a broadening out of the recovery and to make sure that it is sustained without an acceleration of inflation. I think that will be accomplished.

In contrast, though, in the major European economies and in Canada, the policy swing has now gone much more toward containing inflationary pressures, in part because only insufficient actions had been instituted earlier. As a result, the people in these economies are now looking to the Big Three nations and the rest of the developed world to help them achieve an export lead growth. To be sure, the U.S., Germany and Japan do need to enjoy a healthy recovery to help the rest of the world. It is important for us. It is important for the rest of the world. We are very much an interdependent world.

In the analysis that we have done, if, let's say, you add another percentage point to our growth rate -- instead of 5-1/2 to 6 percent over the next 4 quarters, let's say it was 1 percentage point more -- if you go through the analysis and see what that is going to do for the individual countries, you find that you are talking about a decimal point or so, and it is not going to make the crucial difference. We do need a healthy recovery, and it is important that we keep it going.

The most important thing for the rest of the world is, in fact, that we get a sustainable, non-inflationary recovery. It would surely be counter-productive if we were to institute expansionary policies that were so expansionary that they started inflation rolling and then we shifted abruptly to restraint.

But it surely is important that we do maintain a healthy recovery. I think it is particularly important because, so long as the OPEC members continue to accumulate large current account surpluses, to the extent that they do that there are then going to be unavoidable deficits in the rest of the world and increases in the external debt of the oil importing countries. So in that sense, the need for international economic cooperation is, if anything, greater than ever.

I think the two things we really have to watch out for in the next year are (1) that we do not adopt a divisive policy, such as trade restrictions because of external financial pressures; and for that reason it is equally important that the countries that have adopted satisfactory adjustment measures to deal with their external disequilibrium and their large increase in debt, that they do have access to international financial resources to carry them through the adjustment period. That is why in our international chapter we do have a considerable discussion about international financial resources and the need to insure that they are available.

MR. GREENSPAN: Thank you very much, Burt.

Q Alan, in your forecast for '77, you based your forecast, I assume, on the President's economic program. Did you make any calculations on how real growth and inflation might be affected if Congress should, by chance, adopt Mr. Carter's program?

Q What was the question, Alan?

MR. GREENSPAN: The question is whether we have made any alternate estimates embodying into our forecast mechanism President-elect Carter's proposals rather than ours.

I would say you raise that question with Charlie, because I think I would like to stay with what ours is, what we are doing, and let him answer questions with respect to that. So you direct that to him.

Q The reason I asked is not to tie you to one program or the other, but assuming the realities of life.

MR. GREENSPAN: Are you asking if it's going to make a very significant difference? Is that the question?

Q Yes.

MR. GREENSPAN: It will not, no.

Q Carter's program will not make a significant difference?

MR. GREENSPAN: It will not, as far as we can judge. Its economic impact is not in the short run significantly different. I use the word "significantly" as a term which economists love because it can mean almost anything to most anybody. In my view, it is not a major difference. That doesn't mean, incidentally, that we subscribe to the particular policies, obviously.

Q Coming back to this question of this new full employment-unemployment concept, if there is indeed, as Burt said, so much debate and discussion about the exact point, if

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it is such an imprecise thing, was it for political reasons that you didn't take, say, 5 percent, which is an even number like 4 percent, and instead took 4.9 percent?

MR. GREENSPAN: No. We took 4.9 percent because that is where the statistical calculations came out. I don't see any distinction at this particular stage between 4.9 and 5.0. In fact, I think, as Burt indicated, it's quite likely if we embodied into these calculations the factors, other than the demographic forces which we have, we would get something above that.

But you do recall that this is a very fluid concept, that in a sense there is no specific rate which adheres throughout time and it does change depending upon the characteristics. The definition itself is rather fuzzy. It's trying to capture a particular level or quality of the labor market which would begin to change the pattern of wage determination. There isn't a number which all of a sudden you get to and then the whole structure of the labor market changes. It is a gradual sort of thing.

As a consequence of that, it's important to recognize what I think is the qualitative nature of these analyses, namely, more the absolute urgency that we abandon as statistically indefensible the old 4 percent figure. We had the choice obviously of spending a great deal of time and refining these numbers down perhaps far beyond which they could. In fact, I don't think we can until the actual unemployment rate gets much closer to those levels so we can see the responses. So our choice was really to do nothing, stay with the old figures, or to do an interim or even a very approximate interim upward revision in that number. In other words, we think less violence is done to reality by re-estimating the number in the crude way, admittedly crude way, in which we have, rather than stay with something which we think at this stage is not quite defensible.

Q Did you use the 4.9 in your budget calculations?

MR. GREENSPAN: Yes, we do.

Q So that the President's fiscal dividend, or margin or whatever you call it, that he projected for 1980 is based on the 4.9? In other words, we don't have to chop $30 billion off?

MR. GREENSPAN: Yes, that is correct.

Q In other words, the $53 billion in surplus or margin that is estimated in the President's budget for fiscal 1981 I guess on a continuing services basis is based on this new full employment concept? You're not saying it's $30 billion less than the $53 billion?

MR. GREENSPAN: No. If, however, it turns out that the figure is not 4.9 percent but actually somewhat higher, then you would have to make that sort of adjustment.

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Q Don't you have a 4.7 for some years ahead?

MR. GREENSPAN: I am saying that the concept remains the same.

MR. MALKIEL: Could I just add one point on that. In terms of the potential GNP, the 4.9 to 4.7 or 5.5 does not make very much difference. The major factor is the productive decline.

Q But that was reflected in those budget figures.

MR. MALKIEL: It is reflected, but again I want to emphasize in terms of our estimates, we have in a sense been very optimistic. We have not wanted to put the potential number as low as we might get it.

I think what we ought to warn you about is that there is probably, in terms of the uncertainty that we have, undoubtedly the chances of the potential being lower are much greater than the chances that, in fact, the potential is higher.

Therefore, there may well be some slippage in there. The $30 billion was simply to where we went, but it may be that we ought to go a bit further.

Q It is not 30 off the budget figures?

MR. MALKIEL: No.

Q What is the gross number from which you did take the $30 billion off?

Burt said it is not as great by about $30 billion as it would have been in fiscal 1980, the fiscal dividends.

MR. MALKIEL: Just compared with our previous potential series --

Q What was that number?

MR. MALKIEL: I don't have that particular number.

MR. GREENSPAN: It is in the book.

MR. MALKIEL: I think we have a table, don't we, with the old and the new?

Q It is not the revenues?

MR. MALKIEL: No. It is not the revenues, but we do have the potential GNP. The potential GNP, I guess we have here just through 1976.

Q I think it would be useful to have that number so we know what you are really talking about because there have been all sorts of fiscal dividend numbers thrown around like sixty.

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MR. GREENSPAN: You mean what is the difference between the full employment revenues at the old potential and what it would be under the new one?

Q No.

Q When you said the $30 billion, what were you referring to?

Q He said fiscal dividend.

Q Fiscal dividends?

MR. MALKIEL: Right. That was the fiscal dividend based on the old potential series which incorporated a four percent full employment-unemployment rate but, more importantly, that there had been no slow-down in productivity.

Q Could we get somebody to give us that number so that we would be able to compare this with what we had before?

Q The specific question --

Q Aren't you mixing -- You're using fiscal dividends to mean GNP output. I think there is confusion here.

MR. MALKIEL: No. No, I'm not. I am using -- no.

Q Budget surplus or margin.

MR. GREENSPAN: It is a margin difference.

MR. MALKIEL: That's right.

MR. GREENSPAN: It is a difference in a particular year in the budget margin at full employment revenues and expenditures.

Q What is that number?

MR. GREENSPAN: The number, as I recall, the difference is $30 billion.

Q No. What would the old number have been?

MR. GREENSPAN: You mean the absolute amount?

Q Yes.

MR. GREENSPAN: Somebody has that.

MR. MALKIEL: We certainly can get that for you.

Q All right.

Q Whatever the full unemployment rate may be at a given time, are you saying that getting below that would accelerate inflation, in other words? Or are you saying that you can't use macro-policies to get below it, which is what Charlie Schultze says?

MR. GREENSPAN: First of all, let's define it specifically in terms. There is an existing institutional structure, rigidities and elements within the labor market at this stage which indicate, irrespective of how you get there, that at that particular point you begin to get pressure on wages. It is not a question of a particular economic policy because if you get there from strong, say, investment demand or a very large element of demand in the private sector, you will get the same effect. It is not a consequence of policies.

Obviously, to the extent that the elements which are structural in that sense can be altered, the answer is yes, the pressure on wages at a particular unemployment rate will change.

Q Well, can we try to clarify this? Shultze testified the other day that broad aggregate measures could, he thought, get unemployment down to 5 or 5.5 percent. Then he says you could get perhaps to the neighborhood -- he was pressed, he didn't want to give a number, but he finally said maybe in the neighborhood of 4 percent through structural policies. Do you agree with that general approach?

MR. GREENSPAN: I think it is an extremely difficult calculation to make, largely because we have enough trouble coming up with this type of number. To try to translate any particular list of micro or structural measures that you can into specific effects on the labor market, any attempt to do that is fraught with extraordinarily analytical difficulties. So I would hesitate to put a specific number on what is potentially available.

Q Alan, when you were writing the chapters, the first chapter especially in which you spell out the principles, did you at some point when you were still working on it have in hand the Carter or at least the reports of the Carter stimulus package, after the Charlie Schultze briefing?

MR. GREENSPAN: No. They came out in a very late stage. The answer in general is no.

Q So these principles were laid down and put in galley form before those had it?

MR. GREENSPAN: Yes.

Q Alan, what are the risks that you referred to that are discouraging the businessmen from investment? Can you elaborate a bit?

MR. GREENSPAN: First of all, let me just point out that this is a phenomenon which is really worldwide. It is not indigenous to the United States in and of itself. What we do observe by a number of direct and indirect measures is that the required rate of return on a new facility has apparently risen in recent years.

It may well have actually peaked in late 1974 or early 1975 and it has come down since. But there is no question that the underlying risk involved in longer term investments

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has clearly increased.

The reason I hesitate to give you a specific list for the United States is that, since it is a worldwide phenomenon, there is no question that if I were to tell you, for example, that there are problems and uncertainties with pollution regulation and other forms of regulation, and there is no question that the near uncertainty itself of potential future changes in regulation does effectively increase the cost of capital -- or let me put it another way, the required rate of return to cover these uncertainties, as we point out in the report, if we could find ways to lower the uncertainties with respect to future regulations, it in and of itself, would improve the investment outlook. It is not, as far as we can judge, so much the costs of the pollution control and the like -- although they are obviously relevant and I wouldn't want to dismiss them because they do get embodied in the cost structure and eventually they are largely passed through into the price level -- they are certain in the sense that there is no uncertainty about what they are or what they will be, other than most business uncertainties.

The major problem is the rate of change of regulations, where things are in a state of alteration year in and year out. If you build a plant which might, say, have a 25-year life expectancy, you have to recognize that you have sunk the capital, so to speak, and there is apparently some reluctance, from what we can judge, there is more reluctance on longer lived assets than on shorter ones. That does sort of confirm the type of problem, which I do think is a problem, which is probably largely a worldwide issue of uncertainty.

Having said that, let me go back to what I think is implicit in it in one respect. There is no doubt that the inflation which has been worldwide, and the huge instability that has occurred as a consequence of that, is the prime cause of the basic uncertainty. But it is not the only cause. It is the major element. This is one of the reasons why we think it is so essential to maintain stable policies, policies which will remove the degree of volatility and inflationary imbalances as a major policy to encourage investment, which we think is so essential in the long run.

Q When you earlier said that Carter's programs wouldn't make any significant impact on your forecast, are you talking about just the first quarter forecast for GNP? Or how far in advance are you going?

MR. GREENSPAN: I would emphasize short run. By that I don't know whether it would be one year, 18 months -- I don't know. I would not --

Q I have a follow-up question to that, that being that if Carter's economic package won't have that much impact, why is the report so critical of it in your section on philosophy, critical of Carter's program?

MR. GREENSPAN: We are not specifically critical of Carter's programs.

Q I understand that, but you can read between the lines very easily.

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MR. GREENSPAN: Let me tell you what I think the differences are, as best I can judge.

I want to also emphasize, incidentally, while there are differences, I think it is important -- I don't think we emphasize this enough -- that the difference amongst the economists tends to be really at the margin. That is, it is very likely that if one were to really spell out in full detail all of the underlying attitudes towards policy, you are going to find that, just to pick a number, 95 percent of the time we are in absolute agreement. The differences are where all of the press coverage occurs and all of the focal analysis. While I will tell you there are differences, I want to emphasize that these are really not what I would call very substantial differences.

Having said that, let me tell you where I think we come out. We believe that at this stage and for the foreseeable future, the major problem in the United States is going to be to create an adequate level of capital investment, to create jobs, to meet our environmental and energy goals and, in fact, to do the many things which we outlined in our report a year ago. I won't go into them.

You can look at a number of different ways of doing this. I think that one of the points which Burt made, and I just want to emphasize it, is that we don't believe it is enough merely to create an increase in short-term consumption, to remove the elements which still impede investment.

If, in fact, the simple accelerator models -- which really is largely where this particular point of view comes from -- were working, actually were correctly describing the immediate past, then I think we would probably say it is clear that what is missing is a specific shortfall in final demand currently.

We do believe that that is clearly an element and that, as we see final demand evolving at this stage, we think that it is clearly accelerating at least in this immediate term -- although, as I pointed out earlier, it will slow down after we get beyond this immediate short-term hump. Even after you have gotten to that point, I think it is the experience, both of this country in the most recent period and certainly that of the other major industrial countries of the world, that merely enhancing consumption or short-term demand in and of itself is inadequate to create the underlying investment incentives, the underlying needs for the type of investment that both the United States, and the rest of the world needs to maintain its necessary long-term growth rates, to create raising standards of living, job opportunities and to bring down the abnormally and intolerably high unemployment rates.

Q Alan, you project unemployment to come down close to 7 percent at the end of the year. Would you say the Carter program will make no significant difference? Are you saying it can't bring it down below 7 percent?

MR. GREENSPAN: No. George, I emphasized the word

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"significant" because I do not wish to get involved in very specific characteristics.

I think that the unemployment rate is heading down. Our ability to forecast it, as we have demonstrated with great emphasis in the last few years, is less than we would like. To pinpoint specific numbers, I would just as soon stay away from.

All I will say is this, that we have reviewed a large number of alternate programs. The basic principles that underscore them were outlined in the report. Our major concern is the longer-term investment outlook. We think that any economic policy must consider not only the immediate short-term period but to trace its consequences much beyond. In this case I am delighted that we are all getting to the point where we are trying to project the implications of our policies throughout the next three or four years.

As I have said to you and others, I think Charlie Schultze is one of the best economists in the country. I have great respect for his judgment and, as a consequence, if I disagree with him, I often ask myself why, to make sure that I know why. Fortunately, the disagreements have been in the past not very substantial, and I don't want to get to nit-picking on little differentials between how he would forecast or I would forecast, because it is very likely I might disagree with myself more between the way I was looking at the world six months ago or three months ago and now than the way I would be looking at the world now and Charlie Schultze would be looking at the world now.

Q What are your estimates of the effects of the recent OPEC price split decision on the U.S. economy growth, or however you would like to characterize it, and the world economy?

MR. GREENSPAN: I think, as Burt pointed out, we have problems with the level of oil prices per se, forgetting rates of increase and the implications that that has with respect to generating a very seemingly impenetrable OPEC surplus. What that does is, because of the incapacity of a number of the OPEC countries to buy goods and services and reduce those surpluses, it must of necessity mean that there are equal and offsetting deficits, both in the industrial world and especially in the nonoil developing countries, which means we are accumulating levels of debt which I don't believe can be persistent indefinitely. As a consequence of that, we hope that this will essentially balance out in the way which Burt mentioned.

The direct impact on the United States is embodied in our forecast, and it still hasn't shaken its way down. I would just as soon stay away from specific figures on that at the moment, largely because there is a substantial element of uncertainty at this point.

Q There have been figures floated anywhere from 6 to 15 billion dollars. Can you give us something in between that or something that reflects a little more accurately what you believe or what the CEA believes?

MR. GREENSPAN: Until those figures simmer down and until we have a figure that we feel comfortable with, I would just as soon not come up with a number.

Q Alan, if Congress passes a tax rebate and tax cuts, as they undoubtedly will, why then will that not have an impact on second quarter GNP growth and thus accelerate the first quarter?

MR. GREENSPAN: Largely because, as I pointed out, we start off with an, in part, accelerated first quarter growth reflecting the inventory and effects of the Ford strike directly.

Secondly, as we learned from our experience with a similar sort of rebate in the spring of 1975, that the initial effect of that is to create large increases in savings and not in consumption, it is only later on that that filters into the consumption pattern. I would doubt very much that the effect is going to be impacted within the second quarter, should that occur, should the tax cut occur in the way you suggested.

It is more likely to have an effect not dissimilar to what occurred in 1975. I think in effect the Christmas buying season was far more impacted from that spring rebate as it filters through the system than I thought one could immediately -- in other words, the impact very immediately. What we know is that you are not going to get a quick, overall, big consumption effect. It tends to stretch its way out.

Q Alan, can I follow that up? Just following up on that, isn't the infla . situation though now so radically different since the last rebate and the people's psychology may as a result also be considered different? The willingness to spend now, the saving levels also have been building up since early 1975 and the willingness perhaps to spend, is that much greater than it was then?

MR. GREENSPAN: It might be slightly different, but remember we have far more in our history of this type of event than 1975. We go back to data which exists -- for example, we had a soldiers' bonus here in 1936. We had very large national service life insurance and dividends in the 1950's and earlier. So we have a lot of experience with these one-shot large payments to consumers. There is an extraordinary uniformity of the pattern of expenditures. That is, what you tend to get is somewhat more durable goods expenditures on an average, a larger proportion is saved and the tendency for that to spread out its impact over time is quite pronounced.

Q Alan, on your point of not being enough to merely enhance consumption, I am familiar with the differences between the President's tax program and Carter's. But isn't it true that the President's program as well, at least for calendar 1977, stresses the consumer rather than the investment side?

MR. GREENSPAN: Well, it is certainly true that the level of tax cuts within the consumer area are larger than in the corporate sector, in part because of the attempt to remove

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some of the inflation drag on particular tax rates.

We also point out in the report that, in addition to the 2 percentage point corporate tax cut which the President is recommending, and the accelerated depreciation for areas with unemployment rate of over 7 percent, that, should that appear less than adequate in terms of tax policy, that other measures should be looked at. We do go in at that point to discuss the effects of the investment tax credit.

There is a bias, as you know, towards shorter lived assets, so that we say this is a critical question which should be looked at, but for the moment we think that that type of package is about the best one that we could come up with.

Q But for this calendar year there isn't all that much difference, is there, between your package and their package in terms of the break between the consumer side and the investment side? Is that right?

MR. GREENSPAN: We don't fully know at this point what the so-called business tax effect is. I don't want to get too much involved specifically in that. I don't think that they have finalized the exact details of their business package as yet.

Q Mr. Greenspan, once again this year you predicted that unemployment was going to drop about a percentage point. Charlie Schultze has said that with great optimism it will drop down to six and a half or probably even closer to 7 percent. You have a pretty healthy program for unemployment. What do you ascribe that point drop to again?

MR. GREENSPAN: You mean in the forecast per se?

Q In the forecast and your economic package?

MR. GREENSPAN: First of all, I think that the expectation, as essentially to where employment will tend to increase, is likely to mean that the labor force growth this year will nowhere near match the extraordinary figures of last year. So that it is largely not an estimate of employment because, in fact, the employment growth this year has been quite substantial. It is the errors that were created, that we created last year, I would say, in badly missing the extraordinary rise in the labor force.

It's conceivable it could happen again this year. It is not a zero probability but it is possible. I doubt it, largely because we expect the flexibility of the labor force to be less this year , that is its growth potential. As a consequence, as you get increases in production and employment its impact on the unemployment rate will be far greater, as we see it, this year than it was last.

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Q But then why did the Carter people think that it is only going to be 7 or 6-1/2 with -- I am sure they take in the same vagaries as you do -- how come they still get down to that point with a healthy stimulus for unemployment and you don't seem to be showing anything in that?

MR. GREENSPAN: Well, our decline is down to 7 percent. It could be off. I hope we are too high. It is possible.

Q Is it just a normal business cycle and you think it is just going to trail down by itself without any stimulus?

MR. GREENSPAN: I think without any stimulus there is no question, I think, that the unemployment rate would fall, because what we are getting at this particular stage is clearly a fairly solid recovery. I think that the recovery is still very much on track. As I indicated, the only thing that has been bothering me of late is the capital goods market. They are showing some marginal evidence of improvement. What we are talking about is the differential effects of policy on that particular pattern.

Q Alan, you talked about the problem of business not investing to the extent in order to keep up our productivity we are going to require. I realize that in your view it is obviously important that business take the initiative in doing the investment, but do you see any role for Government aside from sort of passive stimulation like increases in the investment tax credit? Do you see any role for direct investment by Government in some areas to boost that total, where business may be reluctant to do it itself?

MR. GREENSPAN: You know, there is a long history of that which I don't want to get involved in. A number of countries in Europe have gone in that direction and, while I scarcely would take gross statistical evidence as proving anything, I will tell you that the gross statistical evidence is highly suggestive that that is not the direction we should go.

Q Alan, you mentioned that you expected the extraordinary growth in the labor force to slow in '77, but in the report at one point you cite the civilian labor force growth in '76 at 2.3 percent. Then you say in another point that it is expected that the civilian labor force will grow at about 2.5 percent in '77. I don't see this slowing. It seems to me it has accelerated.

MR. GREENSPAN: No, it is not. The forecast is not accelerating it. You should know there is a difference. Maybe it is an annual average difference from year to year.

Q On page 23 you say the labor force grew by 2.3 percent in 1976. On page 41 you say it is expected that the civilian labor force will grow at about 2.5 percent in 1977.

Q It is at the top of page 41.

MR. GREENSPAN: No.

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MR. MALKIEL: I think that Alan has made the point that what was extraordinary is when you look at a fourth-to-fourth figure and precisely because we have had so much growth in the labor force already, it is really the same kind of point Alan was making about the first quarter.

You are starting off with an extraordinary growth in the labor force, and the question now is, fourth-to-fourth, what is going to happen, and implicit in that number is a slowing in the fourth-to-fourth growth from the labor force.

Q In reference to that, do you expect the employment gains next year to equal employment gains in the past, which were about 3 million? It seemed to cut unemployment from 2.5 percent growth in the labor force.

MR. GREENSPAN: No. I don't want to give you an employment forecast right at this moment. I think that we do see strong, continued gains in employment implicit in our forecast.

Q What are the reasons behind the 10 percent increase in OPEC investments in the U.S. between 1975 and the fourth quarter, I guess it is-- excuse me--the third quarter of 1976?

MR. GREENSPAN: I am sorry. Would you repeat that?

Q In 1974 there was a 10 percent increase in OPEC investment in the U.S. between 1974 and the third quarter of 1976.

MR. GREENSPAN: Do you have that page there?

Q Yes. It is 126, the last point in the OPEC surpluses.

Q It is the table on page 127.

MR. GREENSPAN: Are you saying an increase? My recollection was that it was a sharp decrease.

Q It has risen from 20 percent of the total investments in the United States.

MR. GREENSPAN: I see. You mean in percent.

Q Of investable surpluses, I gather.

MR. GREENSPAN: Let me read it for a second.

It seems to me that that paragraph is so self-explanatory, that there are clearly less investments in sterling assets, and if the total investable surplus remains the same and you are doing less in basically sterling and sterling-related assets, I don't know what I have to explain.

Q Is it going to rise?

Q You are talking about percentage of total volumes, are you not?

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MR. GREENSPAN: What?

Q You are talking about percentages of total volumes, are you not?

MR. GREENSPAN: Yes. In other words, we are merely describing what is in the table on page 127.

Q Is it going to move up, though? Is the percentage going to move up?

MR. GREENSPAN: You mean in the United Kingdom in sterling assets?

Q No, no. Will there be a greater percentage of OPEC surplus funds coming into the United States in this case than in the past?

MR. GREENSPAN: I do not know. I really don't.

Q Do you detect that interest rates are edging up again, or what concern, if any, do you have in that area?

MR. GREENSPAN: I am certain I have concern. I think that one should have concern that the pattern of recent days has been, I would describe, moderately sharp. Should we get into a situation where the recovery begins to show some real strength in it, which is not inconceivable to me, I think you may well find that the demand and supply of funds itself will begin to have an effect on rates.

But I will point out that the key issue on the interest rate outlook is largely inflation. If we have the capacity to keep inflation rates down, I think we will find that, even though there is an increase in the demand-supply balance, it may well be that the further unwinding of inflation expectations and, therefore, of the inflation premiums and the interest rates, will keep the interest rates relatively steady in nominal terms.

THE PRESS: Thank you.

END (AT 12:33 p.m. EST)