The economy in the past year has provided both good and bad news. The good news is that inflation has slowed markedly from the double-digit levels that had prevailed in recent years. At the end of the year inflation was generally believed to be in the five to six percent range rather than over ten percent. The decline in interest rates during 1982 also was good news for those faced with high debts. The bad news included an unemployment increase to over ten percent and a decline in total value of goods and services from the 1981 level after correcting for inflation. The huge federal deficit continues to loom as a major problem for the economy. For Michigan residents, the level of automobile sales has been another piece of bad news.

In looking ahead there are several areas that merit discussion before attempting to project the level of economic activity. These include the level of savings, consumer attitudes concerning when to buy, the federal deficit and our federal fiscal and monetary policies, and the impact from the international economy on the U.S. economy. Each will be discussed briefly.
Consumers increased their savings as a percent of income during 1982. This reflected a consumer reluctance to incur debt to purchase housing or durable goods during a period of high unemployment and high interest rates. There are two data sources on personal savings which moved together during the 1960s and 70s. However, for 1982 the Federal Reserve Board estimate of net personal savings is four percent above the rate calculated by the U.S. Department of Commerce in its national income statistics. This large difference greatly affects one's assessment of consumers' ability to rapidly increase purchases.

Existence of savings is not sufficient to assure increased consumer spending. In recent months consumers appear to have increased their willingness to make purchases, particularly as they observed declining interest rates. Falling interest rates have contributed to the recent increase in housing starts but construction remains a depressed sector in the economy. However, interest rates on consumer loans are still a deterrent to major purchases, according to surveys conducted by the Survey Research Center of the University of Michigan.

Michigan is particularly interested in auto sales. We are driving an aging stock of automobiles. Are consumers confident enough to spend some of their savings? Will interest rates fall enough to encourage auto purchases? The outlook for 1983 auto sales hinges on how one answers these questions.
We turn now to federal economic policy. Many believe that the Federal Reserve Board has eased monetary policy and will provide funds to support growth in the economy in 1983. The evidence cited is both the rate of increase in the money supply and the decline in interest rates, in spite of the huge federal deficit. Because inflation has slowed markedly, one can argue that the real rate of interest - the rate after correcting for inflation - is still high by historical standards. If one accepts that argument, one might expect further easing of interest rates in 1983, providing some stimulus for consumers to invest in durables and making it less costly for business firms to invest in plants and equipment.

There is no doubt that the federal government will run a very large deficit in 1983. Experts disagree on the exact size of the deficit, just as they disagree on economic policy. As calculated in the national income accounts, the federal deficit for fiscal year 1982 was approximately 124 billion dollars. For the current fiscal year, this deficit is likely to be some 20 billion dollars larger, assuming there will be no major changes in tax policy and that the rate of increase in federal expenditures will slow somewhat. The deficit might be reduced if the increase in gasoline and diesel fuel taxes flows into the treasury faster than the road repair expenditures are increased. Financing the large deficit will affect credit markets and interest rates, thus affecting consumer spending and business borrowing.
The United States is a major part of an international economic community. Other nations also have been experiencing recession with increased unemployment. There is increasing concern that major bankruptcies overseas might impact the international financial community, including U.S. banks. This concern was highlighted by the difficulties Mexico faced in 1982. Another aspect of the international economy is the strength of the dollar which has increased in value relative to that of other currencies during 1982. The increasing value of the dollar makes our exports more expensive to importers in Europe or Japan and makes imports less expensive for Americans to buy. If net exports in the third quarter of 1982 had remained at the same level as in the previous quarter, the real output of goods and services in the U.S. would have grown at a 2.5 percent annual rate rather than being constant. This is of particular interest to agriculture because of the large portion of agricultural output that is exported. Because of the increased value of the dollar, its price to many foreign buyers in their currency has increased by 35 percent over the last two years, although the price of U.S. wheat has declined. It is also important to everyone in Michigan because of the lowered price for imported automobiles relative to the price of American produced cars.

A survey of a large number of economic forecasters reveals wide disagreement on the economic outlook for 1983, probably because of the many uncertainties, some of which
were discussed above. On the average, forecasters predict an increase of about three percent in the real value of goods and services produced for 1983 compared to 1982. I see little reason to disagree with the results of this survey. There is clearly a wide range of possible outcomes depending on one's assumptions about consumer spending, federal economic policies and the behavior of the international financial markets.

My most likely scenario for the U.S. economy projects slow growth with an average increase in real output of about three percent for 1983 over 1982. Unemployment will continue high throughout 1983, perhaps averaging near ten percent and remaining above nine percent even at the end of 1983. This scenario is consistent with inflation of less than six percent for 1983 over 1982.

The Michigan economy remains more depressed than the national economy. A national growth rate of three percent would provide a small stimulus to the Michigan economy, but the annual average rate of unemployment would be on the order of 14 percent. However, the uncertainties affecting the national economy are magnified in terms of their effect on the Michigan economy. Should consumers decide to reduce savings and incur debt in a significant way, there could be a much larger decline in Michigan unemployment, or, more positively, a much larger increase in Michigan employment. On the other hand, should the national economy grow at a rate of one
percent instead of three percent, Michigan would continue in its depressed state with unemployment increasing from the 15 percent level of 1982.

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