Slowdowns and Recessions: What's Been Government's Role?

By Donald L. Raiff

All industrialized countries have their economic ups and downs, and the United States has had its share. Between 1950 and 1970 we went through seven slowdowns and the best guess of the experts is that the eighth one ended this spring. This latest experience turned out to be the deepest drop-off since World War II.

Are these fluctuations inherent in our economic system or has some outside force caused them? Some economists have suggested that changes in Government policy may be a cause of this instability or, at least, be aggravating the swings. Analyzing the severity of slowdowns and Government policy actions which accompanied them provides some insight into this question.

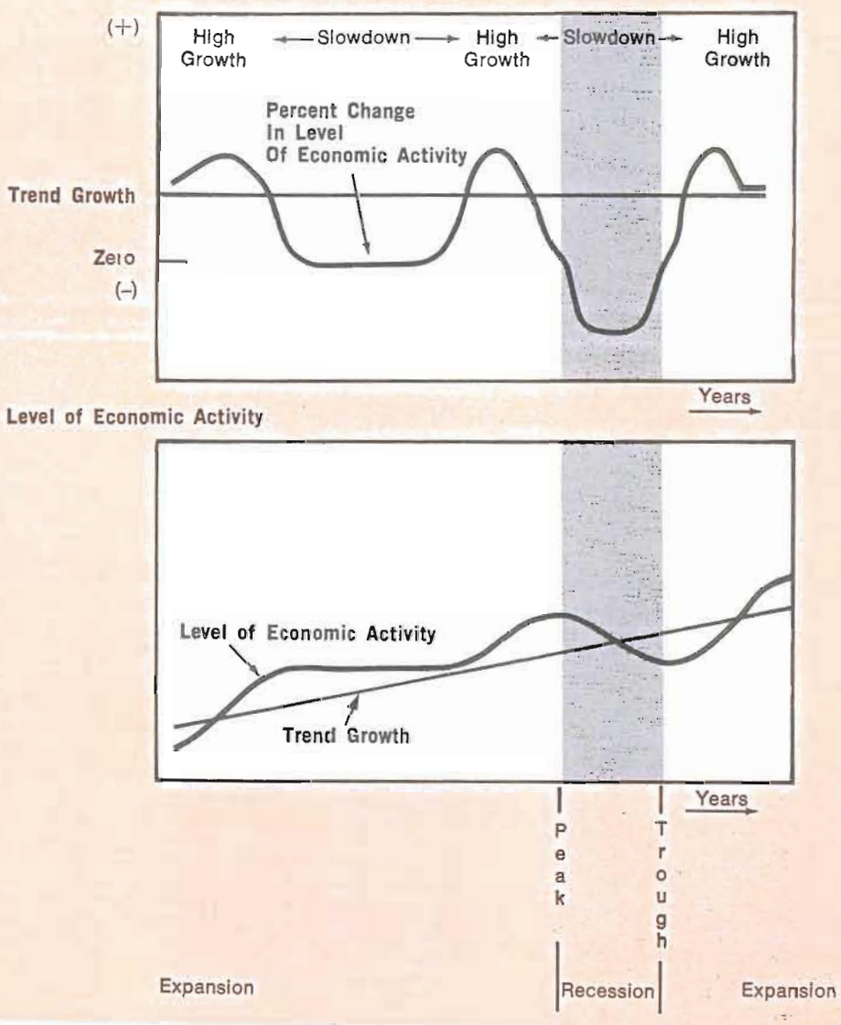
SLOWDOWNS AND RECESSIONS: SEVERITY IS THE ISSUE

In technical jargon, economic slowdowns are deviations *below* the trend of long-term growth. They include periods of *slow positive growth* as well as actual declines in economic activity. (For an illustration, see Figure).[1] The severity of these slowdowns varies greatly. Some "slowdowns" are worse than others, and the business declines are tagged "recessions" (a really bad downturn, like in the 1930s, is labeled a depression). For example, of the seven slowdowns between 1950 and 1970 three weren't serious enough to qualify as recessions and four were. Accord-

[1]For a long time the National Bureau of Economic Research has produced and studied a chronology of business cycles. This effort distinguished *only* between periods of positive growth (lumping together periods of high and low growth) and declines in the level of economic activity—recessions. For an introduction to a more recent and general framework used in this article, see Ilse Mintz, "Dating United States Growth Cycles," *Explorations in Economic Research* 1 (1974): 1-113.

TWO VIEWS OF THE SAME HYPOTHETICAL ECONOMIC ACTIVITY

The top graph is the percentage change representation of the lower one. Together they illustrate the occurrence of two slowdowns, the first one displaying a period of mostly zero growth. The second experience shows a slowdown becoming a recession, as below-trend growth yields to a period of decline in the level of economic activity.



ing to the percentage change in output, the worst recession was in 1957-58 and the mildest slowdown was the mini-recession of 1966-67. (See Appendix Table A for a complete ordering, 1950-70).

Analyzing "slowdowns" rather than just recessions allows us to distinguish between periods of sluggish growth and those characterized by actual declines in business activity. This separation of "plateaus" from "valleys" may provide insights into stabilization efforts, especially if the severity of the slowdown is related to differences in the accompanying Government policy. (See Box 1.)

BOX 1

INGREDIENTS FOR A COMPLETE EVALUATION OF STABILIZATION POLICY DECISIONS

An in-depth look into the quality of stabilization policy would need to identify three things: the goals of the policy actions, the information available at the time of each decision, and the thrust of any policy changes. The ideas and data in this article present only a "first glance" at such a complete evaluation.

The evaluation in the article is limited to the goal of preventing severe slowdowns in the rate of economic growth. A thorough appraisal of policy would also consider other legitimate goals of policymakers—for example, reducing the rate of inflation.

Also, we make no mention of the forecasts existing at the time of relevant policy changes. It is possible that errors in the forecast are an important force leading policymakers astray in charting their course. Even though there is some evidence that the shapers of monetary policy can recognize impending slowdowns and recessions before they arrive, there is no documented evidence that these officials—nor their counterparts in fiscal policy—can accurately predict the magnitude of the impending slowdowns.* Their decisions should be assessed in light of the information available at the time.

To complete an evaluation, the thrust of policy actions must be carefully mapped. Yet, there is no widespread agreement about which variables best measure the thrusts of each policy, or about the time-lags between a policy move and the result.** Each of these issues must be confronted and the "best" available indicators used to reach conclusions. For example, evaluating monetary policy may involve a decision of whether to use interest-rate movements or changes in the growth rate of money as an indicator. Even if the latter indicator is accepted, one must then select the most appropriate definition of money.***

The tests presented in the article do not demonstrate all of the successes and failures of stabilization policy. However, they do provide some insight into one of the issues raised by its critics—the role of policy in aggravating slowdowns.

*See C. Elton Hinshaw, "The Recognition Pattern of the Federal Open Market Committee," Rendigs Fels and C. Elton Hinshaw, *Forecasting and Recognizing Business Cycle Turning Points*, National Bureau of Economic Research Studies in Business Cycles No. 17 (New York: Columbia University Press, 1968), pp. 61-128.

**For examples of the professional disputes about fiscal and monetary indicators respectively, see Michael E. Levy, *Fiscal Policy, Cycles and Growth*, The Conference Board Studies in Business Economics No. 81 (New York: National Industrial Conference Board, Inc., 1963), and Karl Brunner, ed., *Targets and Indicators of Monetary Policy* (San Francisco: Chandler Publishing Company, 1969). Policy lags are discussed in Mark H. Willes, "Lags in Monetary and Fiscal Policy," *Business Review* of the Federal Reserve Bank of Philadelphia, March 1968, pp. 3-10.

***For an explanation of the information value of using some other aggregates, see Myron B. Slovin, "On the Relationship among Monetary Aggregates," *Journal of Money, Credit and Banking* 6 (1974): 353.

Of course, before getting too deep into the numbers, it's important to review what some economists think may cause economic fluctuations.

Causes of Slowdowns: Tough to Isolate. One explanation of business cycles popular since the 1930s suggests that the economy is inherently unstable. This means that the economy, if left alone, will move along a path of positive growth on average but is likely to experience ups and downs along the way. This inherent instability of the economic system produces something like the following scenario. Consumers and businessmen *allegedly* spend rapidly for a period, then slow their purchasing for a while. Next, adjustments in inventories play a critical role. Optimistic businessmen overstock during prosperous times, but when spending slows, they're caught with too many goods on hand. So, to avoid mounting inventories, businesses curtail production and lay off workers; current sales are met out of existing stocks of merchandise. The laid-off workers buy fewer goods, inventories rise still further, and another round of layoffs ensues. The process repeats itself and what starts off as a mild slowdown tailspins into a recession.

Government stabilization efforts are supposed to moderate the downward spiral by offsetting the downswing in private demand. Increasing Government spending and/or cutting taxes to spur consumer and business spending would be the standard fiscal policy response. Either of these actions would shrink a Federal budget surplus or would widen an existing deficit. Increasing the growth of the money stock would be an appropriate monetary policy response. This would stimulate spending by initially lowering interest rates and increasing wealth.[2]

[2]The increasing wealth can come about as the fall of interest rates raises the price of assets yielding fixed incomes (bonds) or through the increased money balances themselves. For further development, see Laurence H. Meyer, "Wealth Effects and the Effectiveness of Monetary and Fiscal Policies," *Journal of Money, Credit and Banking* 6 (1974): 481.

However, not all students of business cycles see the policy choices and their consequences in such a neat scenario. First, some argue that the economy is more inherently stable than implied in this scenario. Second, they believe Government actions in practice tend more often to aggravate rather than moderate slowdowns in economic activity. In their view, Government does not set out to do mischief, but policymakers simply don't know enough about the economy to do more good than harm, or policymakers may have other goals in mind than smoothing out business cycles.

Destabilizing changes in Government policy could occur, for example, because of ignorance about the timing and magnitude of the effects created by policy changes. For example, how much of a tax cut will people spend and when? Alternatively, destabilizing changes might result from Government responding to another problem, such as a high inflation rate. A tax cut may stimulate the economy, but it could also stimulate inflation, for instance. Thus, some business cycle scholars caution against using Government policy to "fine tune" the economy because they think too little is really known about how Government stabilization policies impact on the economy.

HAS STABILIZATION POLICY WORKED?

Applying statistical analysis to business fluctuations cannot *prove* the effectiveness (or lack of effectiveness) of Government stabilization policies in cushioning business slowdowns, but it can provide some clues.[3] Clearly, stabilization policy has *not* prevented observed slowdowns. But have policy changes occurred (for whatever reason) which discouraged slowdowns from snowballing into recessions? Or, have restrictive policy moves aggravated slowdowns?

[3]The tests here involve the thrust of policy and do not necessarily represent the actual desires of policymakers. (See Box 1 for the ingredients of an evaluation of policy decisions).

Congressional Decision-Making: Fiscal Policy. The simplest notion of fiscal policy is that the Federal deficit should be enlarged during slowdowns either by lowering taxes, raising expenditures, or a combination of both.[4] Unfortunately, to look simply at changes in the size of the standard deficit as a measure of policymakers' response to a slowdown can be misleading. The reason is that the size of the budget deficit can change during a slowdown either *automatically* or because of conscious decisions by policymakers to increase spending programs or to lower tax rates. Revenues, for example, will automatically decline during slowdowns because, among other reasons, corporate profits slip and thus corporate income taxes diminish. Similarly, there are automatic increases in expenditures—unemployment compensation payments, for example, which rise during slowdowns. These passive or automatic changes in spending and revenues have to be filtered out to isolate the conscious or active changes in policy, like a tax cut, that are made to cushion downturns.

The "high-employment" surplus or deficit attempts to isolate policy actions which are independent of the current state of the economy.[5] To do this both spending and revenue are adjusted to the levels that would have resulted if the unemployment rate hovered around 4 percent—sometimes referred to as the high-employment level. To the extent this adjustment is successful, increases in the high-employment budget deficit or decreases in its surplus mean that fiscal policy is stimulating the economy with more than just the use of economic stabilizers. The Government is increasing overall demand for goods and services through a new spending program or making more income available for others to spend by way of tax-rate reductions. If such a policy is well-timed, it could offset a slowdown in economic activity. The opposite is also true. A high-employment budget deficit that has shrunk or a surplus that has increased means that Government fiscal policies are becoming more restrictive and reducing overall demand. During a slowdown, this would aggravate rather than alleviate the downturn.

Not all economists are convinced that fiscal policy changes affect the economy immediately, but many believe that the lags are quite short. It is estimated that a substantial part, say at a minimum 30 percent, of the total effect occurs within three months of the policy change.[6] If so, then sorting out the influence of fiscal policy on slowdowns should be done with data from the same time periods as the slowdowns themselves. Such a comparison is shown in Table 1. The comparison suggests that Government policy, as reflected by changes in the high-employment budget, was on net injecting purchasing power into the spending stream during the three mild slowdowns. However, during the slowdowns which became recessions, changes in the high-employment budget indicate that fiscal policy was a drain on the economy.

The record in dealing with slowdowns is mixed and overall does not deserve high marks. Of the seven slowdowns observed, fiscal policy changed in the "right" direction only three times. During the other four slowdowns, fiscal policy changed either in the "wrong" direction or hardly at all. Of course, looking at slowdowns alone cannot tell us whether fiscal policy prevented some slowdowns which otherwise would have occurred. But, a reasonable conclusion from all

[4]For empirical estimates of these effects in light of concurrent monetary policy, see Nariman Behravesh and Donald L. Raiff, "Tax Cuts Seem Like a Good Idea. . .But How You Finance Them Makes a Difference," *Business Review* of the Federal Reserve Bank of Philadelphia, forthcoming.

[5]For an explanation of the general concept and further references, see Keith Carlson, "Estimates of the High-Employment Budget, 1947-1967," *Review* of the Federal Reserve Bank of St. Louis, June 1967, pp. 6-14.

[6]For an estimate of the lags involved with expansionary policy within the original FRB-MIT model, see Frank deLeeuw and Edward M. Gramlich, "The Channels of Monetary Policy," *Federal Reserve Bulletin* 55 (1969): 472. It shows that 75 percent of the maximum response in real GNP from an expenditure increase and 25 percent of the response from a tax rate cut occur within one quarter after the respective policy actions.

TABLE 1

DURING RECESSIONS FISCAL POLICY HAS NOT CHANGED TO STIMULATE AGGREGATE DEMAND

	Slowdowns (Ordered by Severity With Mildest Last)	Net Injection (+) or Drain (-) on the Economy by Changes in the Budget Position during the Slowdowns* Standard Budget** (Billions of Dollars)	High-Employment Budget*** (Billions of Dollars)
RECESSIONS	2/57-5/58	+ 6.6	- .1
	2/60-2/61	- 3.0	- 5.1
	3/53-9/54	+ 2.5	- 1.1
	6/69-12/70	+ 7.7	- 5.2
	5/51-7/52	+ 18.8	+ 13.9
	4/62-4/63	- .8	+ 1.8
	6/66-10/67	+ 8.7	+ 7.4

*Measured by subtracting the average budget position during the slowdown from the levels averaged over the two quarters before the slowdown (see Appendix Table B for support data). Because of the way the changes were computed, a positive number means that fiscal policy is moving in the right direction to offset a slowdown and vice versa. For example, during the 1951-52 slowdown, the average level of the high-employment budget surplus declined from $11.1 billion to an average deficit of $2.8 billion—a stimulative shift in the budget position of $13.9 billion.

**Budget numbers are usually presented on a Unified Budget basis or in terms of the National Income Accounts; the standard budget numbers are on a National Income Accounts basis.

***Using four rather than two quarters before the slowdown does not alter the general implications except for the 1953-54 slowdown where the change in the budget position becomes +1.1 percentage points.

of this is that fiscal policy has been largely "hit or miss" in mitigating economic slowdowns—sometimes stabilizing, sometimes destabilizing, and sometimes "neutral."

Congressional Delegation: Monetary Policy. Congress does not make the decisions involving discretionary monetary policy. Through the Federal Reserve Act and subsequent amendments Congress has delegated this power to the Federal Reserve System. The Fed's power to implement monetary policy is based on its ability to "control" (see Box 2) the U.S. money stock (the public's currency and checking account balances). Changes in the rate of growth for money can be viewed as an indicator of discretionary monetary policy changes. While this is not the only measure of monetary policy, it is commonly used by analysts.

Theoretical and empirical studies have

BOX 2

HOW THE FED CONTROLS THE MONEY STOCK

In the United States, the Federal Government and the commercial banks are the issuers of money (currency plus demand and, possibly, time deposits at commercial banks*). However, the Federal Reserve System, an agency of the Federal Government, has the responsibility for controlling the money supply. The Fed exercises control through its own liabilities—currency and reserves of member banks (so-called high-powered money). It is through injecting or withdrawing high-powered money into or from the economy that the money supply is changed.

Changing High-Powered Money. There are two methods the Fed uses to alter the amount of high-powered money in the economy. By far the most important of these is the use of "Open Market operations." Using this method the Fed buys or sells (U.S. Government) securities in the financial marketplace. When securities are bought, the sellers (individuals, corporations, and security dealers) receive payments in dollars which they either hold as currency or deposits in the bank. When securities are sold, the buyer usually pays by check and the Fed debits the reserve account of the bank on which the check was drawn. A second significant but far less important method is directly making loans to banks. Again, however, the Fed has the ultimate power to limit how much it will lend.

Changes in High-Powered Money Change the Money Supply. Adding high-powered money to individuals' currency holdings directly adds to the money stock. However, since individuals and businesses keep only a small part of their total money holdings in currency form (about a fourth), most of the high-powered money goes into reserves in the commercial banks. With an increase in reserves, a bank is able to increase its checking (or savings) account liabilities—in part by crediting the account of the depositor of high-powered money and in part by making more loans and, hence, crediting the borrower's account by the amount of the loan. Thus, by changing banks' reserves, the money supply is also changed. In fact, since banks keep less than a dollar in reserves for every dollar of deposits issued, a change in bank reserves of a dollar results in a change in deposits and, hence the money stock, of more than one dollar.

The Fed's control over the money stock is by no means absolute, especially within the space of a month or even one to two quarters. For example, the Fed cannot be sure exactly how much the money stock will change every time it puts in or takes out a given amount of high-powered money. Nonetheless, as long as the Fed controls the reserve base, the relationship is fairly predictable over several quarters, and over the space of, say, six months, Fed actions become the major determinant of changes in the money stock.

*The criterion for including time deposits in the money supply is whether individuals regard this asset as a close substitute for assets accepted as a means of payment—that is, for currency or demand deposits. For policy matters, current practice is often to consider both the narrower and more inclusive definition. Because movements in the money stock according to one definition tend to parallel movements according to the other, the use of either definition usually leads to similar policy implications or conclusions.

suggested that people get used to the growth rate in money over the long haul.[7] To make a long story short, the past record of money growth gets built into current and future inflation rates, interest rates, and spending patterns. However, if there are substantial deviations (that is, lasting six months or so) from the recent experiences in terms of money growth, individuals and firms will be surprised and adjust accordingly. For example, if for six months the growth rate for money exceeds what people have become accustomed to, economic activity (either in terms of output, inflation, or both) would tend to speed up. This occurs as people and firms increase spending and investment in financial assets as a response to their higher than previously anticipated balances of money. Thus, if monetary policy is to be used to offset slowdowns, the money growth rate should increase to offset a weakening economy. Conversely, downward movements in money growth would represent a policy which exacerbates a weakening of economic activity.

The actual time between monetary policy shifts and the impact of those changes on economic activity is not known with certainty. If the time-lags were quite short, isolating the influence of monetary policy on slowdowns could be accomplished with data from the same periods as the slowdowns themselves.[8] Then the time periods used in the analysis would be similar to those used for testing fiscal policy. However, economists have made a case for using longer time-lags in analyzing the effects of changing monetary policy. If monetary policy takes between two and three quarters to alter the course of economic activity substantially (for example, 30 percent of the total effect),[9] it would be necessary to compare the growth rate of the money stock before the slowdown with its longer term average rate of growth.

Going into the milder slowdowns, money-stock growth increased relative to the long-term average rate of growth (see Table 2). However, this wasn't true prior to the recessions. A decline in the growth rate of money preceded each of these periods. Three of these four decelerations were substantial. Similar judgments about money growth also emerge from studying changes in the growth rate of money *during* the slowdowns.

Using the growth rate change just before the slowdowns as the main criterion, monetary policy, like fiscal policy, appears to have a mixed record between 1950 and 1970. Growth in the money stock rose substantially before only two of the seven slowdowns. Of the other five slowdowns of which four turned into recessions, money growth slowed appreciably in three and changed little in two.

From these observations alone, it would be difficult to blame every recession on monetary policy. Nonetheless, these data along with other more sophisticated forms of analysis provide the backdrop for concern that slowdowns in money-stock growth can happen at the wrong time with destabilizing effects on economic activity.[10] Of course,

[7]For example, see Milton Friedman and Anna J. Schwartz, "Money and Business Cycles," *Review of Economics and Statistics* 45, Part 2 supplement (1963): 32-64, as well as Friedman's recent summary, "Rediscovery of Money: A Discussion," *American Economic Review* 65 (1975): 176-79.

[8]Some economists would argue that this concurrent measure does not signal the thrust of policy since the money stock growth might be dominated by a declining demand and not reflect supply changes. Others would argue, just as ardently, that the end result is still important. If the Fed allows money growth to slow relative to established averages, it is accepting the depressing effects on economic activity (although perhaps out of unwillingness to alter credit market conditions).

[9]The original FRB-MIT model showed 30 percent of the maximum response in real GNP from a change in bank reserves occurs over the first three quarters. See de Leeuw and Gramlich, "The Channels of Monetary Policy," pp. 472-91.

[10]For some references and a recent study which searches to see if deceleration in money-stock growth is both necessary and sufficient for the occurrence of a recession, see William Poole, "The Relationship of Monetary Decelerations of Business Cycle Peaks: Another Look at the Evidence," *Journal of Finance* 30 (1974): 697.

TABLE 2

THE MONETARY GROWTH RATE HAS TYPICALLY DECELERATED PRIOR TO RECESSIONS

	Growth Slowdowns (Ordered by Severity With the Mildest Last)	Net Injection (+) or Drain (-) on the Economy By Changes in the Growth Rate of Money (M_1)* During Slowdowns** (Percentage Points)	Before Slowdowns*** (Percentage Points)
RECESSIONS	2/57-5/58	− 1.5	− .3
	2/60-2/61	−1.3	− 4.9
	3/53-9/54	− 3.4	− 2.4
	6/69-12/70	− 2.7	− 2.5
	5/51-7/52	+ 3.4	+ 2.2
	4/62-4/63	+ .5	+ 1.3
	6/66-10/67	− .3	+ .1

*M_1 is demand deposits plus currency in the hands of the public. Using a broader measure of money, M_2 (M_1 plus time deposits at commercial banks) in the "before slowdown" calculation, changes the general implications for only the extremes in slowdowns: 1957-58 is preceded by an increase in M_2 growth by .9 percentage point and 1966-67 is preceded by a decline in M_2 growth of 1 percentage point.

**Measured by subtracting the growth rate (annual basis) over 24 months ending six months before the slowdown from the growth rate (annual basis) occurring during the slowdown period (see Appendix Table C for support data).

***Measured by subtracting the growth rate (annual basis) over the 24 months ending six months before the slowdown from the growth rate (annual basis) occurring before the slowdown period (see Appendix Table C for support data).

monetary authorities may have been focusing on goals other than offsetting slowdowns, like fighting inflation. Also monetary policymakers may have been looking at other policy targets such as interest rates rather than the money stock.

THE LATEST SLOWDOWN: A TWO-PART SCENARIO

Going into 1974, many forecasters saw a period of continuing slow growth. Economic activity was supposed to show an average growth rate of 1.2 percent with declines in the first half offset by growth in the second half.[11] Actually, the economy posted a 2.2-percent decline, with business deteriorating in varying degrees throughout the year. Instead of a

[11] *Business Forecasts 1974*, Federal Reserve Bank of Richmond, February 1974.

short, shallow downturn, the economy kept slipping. What happened?

What happened was an unusual sequence of events—a two-part scenario.[12] During the first part, from July 1973 through October 1974, *supply* constraints dominated the slump. Shortages related to price controls and the oil embargo dominated the supply problem. Not until November 1974 did the economy begin to resemble past recessions with weakening *demand*. (See Box 3.) By this time the slowdown was also being given a further downward shove by restrictive Government policies.

Slowdown... In mid-1973, the economy was

[12]For further development of this idea, see N. Bowsher, "Two Stages to the Current Recession," *Review* of the Federal Reserve Bank of St. Louis, June 1975, pp. 2-8. For a longer cycle approach, see Arthur F. Burns, "The Current Recession in Perspective," *Economic Review* of the Federal Reserve Bank of Richmond, May/June 1975, pp. 2-7.

BOX 3

WHEN IS A RECESSION THE REAL THING?

The National Bureau of Economic Research has long used a rather flexible procedure in deciding upon the reference dates for contractions and expansions.* Deciding whether or not we have had a recession requires more than just scanning the rates of change in any one economic series. In its concern to study the amplitude, duration, and scope of past business cycles, the NBER staff has assembled lists of business indicators to watch. However, there has been no assumption that each variable should have a fixed weight in decisions or that the current list will not be added to next time.

In an effort to improve the list of indicators, diffusion indices are becoming more important to the NBER's efforts. These indices indicate the percentage of expanding firms. For example, a value of 75 for the diffusion index on industrial production means that 75 percent of the industries covered are expanding output this period.

Despite the availability of diffusion indices and other indicators, many financial writers called the current period a recession on the basis of a simple rule of thumb involving only one economic variable—real GNP. The rule implies that if two quarters of negative movement in real GNP occur, we have been through part of an "official" NBER recession.

The "official" NBER pronouncement has supported this rule of thumb by dating the peak at November 1973. However, one could argue that the current slowdown only qualified as a recession after the downturn worsened at the end of 1974.** Yet this worsened portion of the downturn is three to six months after the rule of thumb implied that we were in a recession. As such, this rule of thumb may not prove to be an adequate measure in the future.

*See Geoffrey H. Moore, "What Is a Recession?" *American Statistician* 21 (1967): 16, for a good layout of current procedures in dating peaks and troughs. Attempts at making the procedure more mechanical can be found in Ilse Mintz, "Dating United States Growth Cycles," *Explorations in Economic Research* 1 (1974): 1-113; and Gerhard Bry and Charlotte Boschan, eds., *Cyclical Analysis of Time Series*, National Bureau of Economic Research, Technical Paper No. 20 (New York: Columbia University Press, 1971).

**For example, see Geoffrey H. Moore, "Recession?" *Economic Outlook USA*, Summer 1974, pp. 4-5.

slowing down, following the rapid real growth experienced over the previous six months. During the first half of 1973 money-stock growth was around 7 percent—as it had been on average for about two years—and fiscal policy was still in deficit on a full-employment basis, although moving toward a surplus. Forecasters were predicting that late 1973 and 1974 would provide a breathing spell from rapid growth. The only sector expected to be strong was business investment, which would enlarge the nation's capacity to produce and possibly relieve some of the inflationary pressure. As late 1973 arrived, the economy was hit with an oil embargo by members of the Organization of Arab Petroleum Exporting Countries (OAPEC). In early '74 members of a different but similar group—the Organization of Petroleum Exporting Countries (OPEC)—hiked the price of their oil markedly. This cutback in supply fueled additional increases in the inflation rate and sparked a series of economic adjustments away from petroleum-intensive activities.

Economists expected—once they incorporated the magnitude of OPEC plans into their forecasts—that energy-intensive industries would suffer and others would benefit. The net effect of this kind of adjustment turned out to be a decline in total output in the first half of '74. As the economy moved through this period of industry-by-industry adjustment to a new supply situation for energy, Government policy became restrictive.

Then Recession. Ostensibly to curb the rapid inflation, fiscal policy tightened from a slight high-employment surplus of $3 billion averaged over mid-1973 (second and third quarters) to a surplus of $10.7 billion averaged over 1974. Money-stock growth slowed from its two-year average of around 7 percent to a level slightly below 4 percent from April through October 1974. With these Government policy changes, the latter part of 1974 witnessed an economy taking on the characteristics of past recessions. An unusual supply-induced slowdown had become the typical demand-deficient downturn. The slowdown turned into a severe recession, encouraged by a restrictive shift in Government policy.

A RECAP

The thrust of stabilization policy which accompanied economic slowdowns between 1950 and 1970 can be analyzed with some simple tests. According to these tests, the record for monetary and fiscal policy, in terms of mitigating slowdowns in the economy, has been spotty at best. True, some slowdowns—those remaining mild—were aided by policy thrusts which provided "net injections" to economic activity. But, the slowdowns that became recessions were aggravated by policy thrusts which placed drains on the economy. Possibly these "drains" upon real growth resulted from policymakers pursuing goals other than maintaining high levels of steady economic growth. This seems to have been the case in 1974, when policymakers (in an attempt to combat double-digit inflation) responded with restrictive policies. On balance, the Government's success in executing fiscal and monetary policies to smooth out business slowdowns appears to be a long way from fulfilling the dream of steady growth.

APPENDIX

TABLE A

DATES FOR SLOWDOWNS AND RECESSIONS: SINCE 1950*

Growth Downturn	Reference Peak	Reference Trough	Growth Upturn	Occurrence Of Growth Slowdown and a Recession	Percent Change In Real GNP From Downturn To Upturn Quarter	Severity Ranking**
May 1951			July 1952		+ 3.3	5
March 1953	July 1953	May 1954	September 1954	Yes	– 1.2	3
February 1957	August 1957	April 1958	May 1958	Yes	– 3.1	1
February 1960	April 1960	February 1961	February 1961	Yes	– 1.6	2
April 1962			April 1963		+ 3.5	6
June 1966			October 1967		+ 4.4	7
June 1969	December 1969	November 1970	December 1970	Yes	– .9	4
July 1973	November 1973***	June 1975		Yes	N/C	N/C

*Growth cycle dates through 1973 correspond to those set in Ilse Mintz, "Dating United States Growth Cycles," *Explorations in Economic Research* 1 (1974): 67, table 10, 12 indicators--undeflated. Peak and trough dates through 1970 are the new series announced in *Business Conditions Digest*, May 1975.

**The measure chosen for severity is the percent change in real Gross National Product--current output adjusted for price changes since 1958. The 1974-75 experience is treated separately from earlier slowdowns because data from the entire recessionary period is not yet available. Also it allows us to save this observation as a "test" for the implications drawn from earlier periods. N/C--complete data for the period not available.

***The analysis in the text is based on the assumption that the economy began to resemble past recessions, starting in November 1974.

APPENDIX

TABLE B

DATA FOR THE FISCAL POLICY EVALUATION (BILLIONS OF DOLLARS—ANNUAL RATE) [Surplus (+) or Deficit (–) Position]

	Slowdowns (Ordered by Severity With Mildest Last)	National Income Accounts Budget		High-Employment Budget	
		Average over Two Quarters Before Slowdown	Average during Slowdown*	Average over Two Quarters Before Slowdown	Average during Slowdown*
RECESSIONS	2/57-5/58	+ 5.5	– 1.1	+ 6.7	+ 6.8
	2/60-2/61	– .8	+ 2.2	+ 9.5	+ 14.6
	3/53-9/54	– 5.7	– 8.2	– 6.8	– 5.7
	6/69-12/70	+ 4.2	– 3.5	+ 4.9	+ 10.1
	5/51-7/52	+ 17.6	– 1.2	+ 11.1	– 2.8
	4/62-4/63	– 3.5	– 2.7	+ 11.1	+ 9.3
	6/66-10/67	+ .2	– 8.5	– 1.5	– 8.9

SOURCE: Federal Reserve Bank of St. Louis.

*Excludes beginning and ending quarters of each slowdown because they may be only partially within the slowdown period.

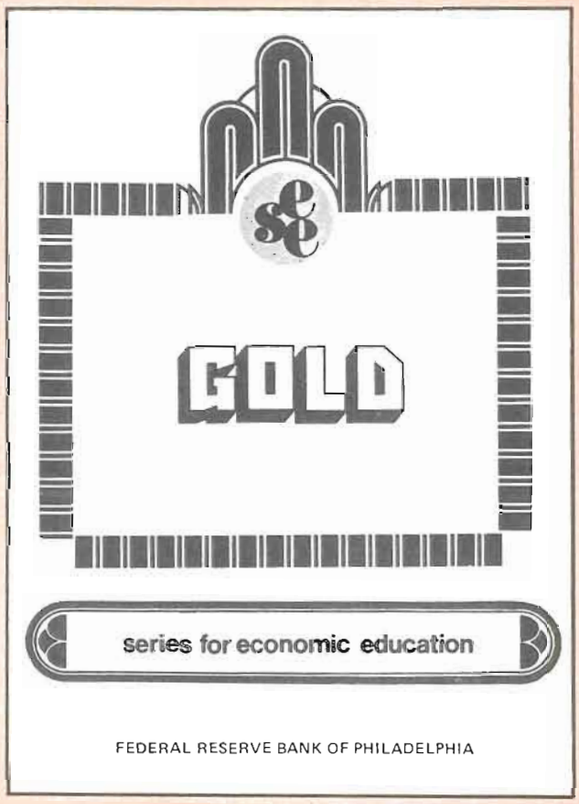
APPENDIX

TABLE C

DATA FOR THE MONETARY POLICY EVALUATION (GROWTH RATE IN M_1—ANNUAL BASIS)

	Growth Slowdowns (Ordered by Severity With Mildest Last)	Two Years Ending Six Months Before Slowdown	Six Months Before Slowdown	During Slowdown
RECESSIONS	2/57-5/58	1.9%	1.6%	.4%
	2/60-2/61	2.7	− 2.2	1.4
	3/53-9/54	4.9	2.5	1.5
	6/69-12/70	7.5	5.0	4.8
	5/51-7/52	1.8	4.0	5.2
	4/62-4/63	1.4	2.7	1.9
	6/66-10/67	4.7	4.8	4.4

SOURCE: *Federal Reserve Bulletin.*



On December 31, 1974, Americans were permitted to buy and sell gold for the first time in some 40 years. Since then questions have been raised about the once-hallowed, almighty metal's worth and importance. For example, has its status in the United States and in the international monetary system changed? If so, in what manner? A pamphlet recently produced by the Philadelphia Fed's Department of Public Information considers the role of gold—past, present, future.

Copies are available free of charge. Please address all requests to Public Services, Federal Reserve Bank of Philadelphia, Philadelphia, PA 19105.

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