

Economic Growth in 2nd Quarter Slowed To 1.7% Rate, Easing Fears of Inflation

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WASHINGTON—The growth of the U.S. economy slowed considerably in the second quarter, the Commerce Department said, easing fears of inflation but stopping short of indicating a downturn.

Second-quarter estimates showed that real gross national product—the total output of goods and services, adjusted for inflation—rose at a 1.7% annual rate.

That is much smaller than the revised 3.7% rate of the first quarter, but the slowdown isn't as drastic as the numbers suggest. The government attributes 2.2 percentage points of the first-quarter growth to a return to near-normal output levels for crops and livestock affected by last year's drought.

"It is not a knockdown blow for the economy," said Campbell Harvey, an economist with Duke University. Other economists agreed, and many said that this latest measure of the economy is a direct effect of the Federal Reserve's economic restraint policies initiated over a year ago.

The Fed recently relaxed its clamp on credit amid concern that the economy might slow to the point where it could topple into a recession.

Some have worried that the central bank reversed course too late. But many economists seemed to regard the latest GNP report as solid evidence that the economy is headed for a "soft landing," a period of slow but sustained growth that will ease inflation without bringing on a recession.

Michael Boskin, President Bush's chief economic adviser, told reporters: "We believe the economy will continue to do well. We believe that modest growth will continue."

But for now, inflation remains high. The annual rate of inflation, as measured by a broad GNP-based index that gauges the prices of a fixed basket of goods and services, increased to 5.2% annual rate during the second quarter, up from a 4.6% rate in the first quarter. Increases in food and energy prices accounted for much of the rise, the report said.

At the same time, another measure of inflation that reflects changes in the mixture of goods and services in the GNP grew at an annual rate of 4.9% compared with 4.0% in the first quarter.

Economists say there is often a substantial lag from when the economy slows to when inflation begins to taper.

But Michael Darby, undersecretary of commerce for economic affairs, was optimistic about reducing inflationary pressure very soon. "Recent monthly price data . . . strongly suggests that the peak rate of inflation is now behind us. From here on, we expect that inflation will slow," he said.

Some other economists weren't as optimistic as Mr. Darby. "I think that is a bit bold," said Donald Straszheim, chief economist of Merrill Lynch Capital Markets in New York. "We could in fact see the infla-

tion numbers a little bit higher."

But while a slowing economy bodes well for inflation—because it relaxes demand and other pressures that drive up prices—it could be devastating for the budget deficit. The Bush administration is counting on the economy to grow 2.9% this year so that the government can bring in enough tax revenue to meet deficit-reduction targets required by the Gramm-Rudman law. But many economists expect the economy's pace to be even weaker in the second half of the year than the first.

In the second quarter, growth in personal consumption continued to slow, increasing at a \$7.2 billion annual rate after growing at a \$13.3 billion pace in the first period. Personal income also grew more slowly, as did exports. But imports jumped, fueled by larger oil shipments.

Business inventories rose at a \$22 billion annual rate, but that was \$2.5 billion less than the first-quarter rise. "We have got a lot better handle . . . on inventory management," said Moncure Crowder, executive vice president at First National Bank in Atlanta. Keeping inventories lean helps protect against recession by lessening the likelihood that businesses will have to cut back on orders—and factories on production—to get rid of stock.

In a separate report, the department said GNP growth between 1985 and 1988 was stronger than previously estimated, averaging 3.6% a year rather than 3.3%. A major factor in the revision was that exports averaged 2.1% higher over the period than previously estimated, good news for the nation's trade deficit.

"The combination of those things leaves the level of GNP substantially above where we thought it was," Mr. Boskin said.

One of the most striking revisions in the GNP numbers was the one for 1988, a year when economists were concerned that the economy was growing too rapidly to head off inflation. Growth during the year was revised to 4.4% from the initial calculation of 3.9%, the strongest annual rate of expansion since 1984. Lesser increases in imports, decreases in nonfarm inventory investment and increased nondefense purchases were mainly responsible.

But to some, the revisions were mainly historical footnotes. "There is little importance in these numbers being released except to make the current slowdown that much more dramatic," said Alan Gayle, chief economist at Crestar Financial Corp.

No changes were made in the inflation estimates for the period, which averaged 3.7%.

GROSS NATIONAL PRODUCT

Here are some of the major components of the gross national product expressed in seasonally adjusted annual rates in billions of constant (1982) dollars:

	Qtr. 1989	Qtr. 1988
GNP	4,123.9	4,106.8
less: inventory chng	22.0	24.5
equals: final sales	4,101.9	4,082.3
Components of Final Sales		
Personal Consumption	2648.2	2641.0
Nonresidential Invest.	510.2	501.0
Residential Invest.	188.6	195.6
Net Exports	-52.6	-55.0
Gov't Purchases	807.6	799.7

In the second quarter, the implicit price deflator rose to 4.9% of the 1982 average, from 4.0% in the previous quarter.