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College of Business Administration

ECONOMIC FORECAST FOR 1979

SUMMARY

National Economy

In 1979:

- Gross National Product will increase 2 percent or less in real terms.
- Inflation will approximate 8 percent on average.
- Employment will increase to near 97 million by the end of the year.
- Unemployment will average 6.5 percent.
- Food prices will increase 8 to 10 percent.

Nebraska Economy

In 1979:

- Nonagricultural employment will increase to 760,000 (place of residence).
- Personal income will rise 8 to 10 percent in current dollars, 0 to 2 percent in real or deflated dollars.
- Unemployment will average 3.3 percent, well below national levels.

The economic outlook for 1979 indicates a slowdown in real growth and continuation of an unacceptably high rate of inflation. There is a good chance of avoiding a recession in 1979, and the excessive pessimism so evident in some quarters is not held here. Never has an anticipated recession been so well advertised in advance. With each month's survey, economists have shifted more toward expecting a recession month after month.

Wide public recognition of selected policy measures by the Federal Reserve Board has increased the public awareness and interest in the current economic situation. These recent policy changes include the Federal Reserve Board's full percentage point increase in the discount rate, an unprecedented action. Simultaneously, the Federal Reserve Board raised reserve requirements an estimated \$3 billion. These moves were calculated to increase interest rates, and rising interest rates have historically been associated with a slowdown in the rate of economic activity.

These policy moves will likely slow real economic growth but not bring on a recession. One of the most closely watched indicators of future economic activity is the composite of leading economic indicators. This index represents twelve indices which tend to move in advance of economic trends. If this index is rising, it is an indication that the expansion will continue. If the composite of leading economic indicators declines and continues to do so for an extended period, this frequently signals a slowdown in growth or even a recession.

A review of the leading economic indicators does not support the widely held contention that there will be a recession in 1979. There are several tests that can be applied to the composite index

of leading economic indicators to assess the prospects for a recession. One widely applied test is the three-consecutive-months-decline rule. This contention holds that if the series of leading indicators declines for three consecutive months, a recession is imminent. Another less widely used but trustworthy interpretation of the leading economic indicators suggests that if the composite series does not make a new high in a four-month period, this may be a harbinger of a slowdown in growth or a recession. Applying these two rules to the composite of leading indicators provides no definitive evidence of a recession in 1979. (Recessions are defined as two consecutive quarters in which there is no real growth in the gross national product. Note, however, that a negative growth one quarter of -1.1% followed by a 0.2% increase the next quarter followed by a third quarter of negative growth, say -1.7%, would not be classified as a recession if real growth were resumed.)

While there are conflicting opinions about the prospects for a recession in 1979 (Chase Econometrics, Inc., for instance, is forecasting a recession), it is our judgment that there are insufficient reasons at this time for suggesting that it will occur in 1979. While a recession appears doubtful, there is ample evidence that the economy's rate of growth is slowing. The economy expanded in real terms by approximately 3.8% in 1978, a rate which is about the equivalent of long-term real rate of expansion for the economy, and it now appears that real economic growth in 1979 will be below the long-term rate, averaging slightly above 2%.

The forecast for 1979 calls for a modest expansion in real output. Gross National Product in (Continued on page 2)

(Continued from page 1) 1972 dollars (real) is forecast to increase to \$1,423 billion, up \$22 billion from the estimated fourth quarter of 1978 (Table 1). The best quarters of the year will be the first and second quarters, with growth slowing considerably in the third and fourth quarters. While no recession is forecast, real growth in the third and fourth quarters was projected at the annual rate of less than 1% a year. (See Chart 1, p. 6.)

The 1979 forecast is based upon some important assumptions. It is assumed that interest rates will not be boosted to the extent that severe restriction is placed upon economic activity. The course of interest rates in 1979 is quite uncertain. A case can be made for higher rates on the basis of the Federal Reserve applying strong monetary pressure to stop inflation. On the other hand, interest rates may peak and decline in 1979 if the economy slows and inflation moderates.

Finally, it should be noted that the forecast assumes no large increase (over 15%) in the price of oil or another oil embargo. No serious petroleum shortage is anticipated in 1979.

EMPLOYMENT AND UNEMPLOYMENT

The civilian labor force expanded by 3 million in 1978 (all 1978 employment data refer to the period October, 1977, to October, 1978, unless otherwise specified). Employment, however, expanded more rapidly than the civilian labor force, thereby contributing toward a reduction in unemployment. Employment increased 3.8 million persons in 1978, which permitted a reduction in unemployment of approximately 818,000 persons. The unemployment rate for October, 1978, was 5.8%, a full percentage point below the October, 1977, rate of 6.8%.

The prospects for a further reduction in unemployment in 1979 are not encouraging. The anticipated slowdown in the rate of economic expansion will make employment gains more difficult to attain. Present trends suggest a 2% increase in employment in 1979, which means nearly 97 million employed by the end of 1979 (household survey basis). The civilian labor force will likely rise more rapidly, however, than the increase in employment. If the civilian labor force rises a total of 2½% during 1979, unemployment will rise to nearly 6.6 million, or approximately 6.4% of the labor force. If the increase in the labor force should occur at a slightly more rapid rate, say 3%, unemployment will likely exceed 7 million persons, or 6.8% of the labor force, by the end of 1979. The rise in unemployment will be modest in 1979 and should average about 6.5% of the labor force.

Once again in 1978 more females were added to the ranks of

the employed than males. Employed females increased from 33.5 million to 35.8 million, while male employment increased by 1.4 million (rounded). The employment ratio for females (civilian employment as a percent of the total noninstitutional population) was 47.0, October, 1978, compared to 44.9 a year previous. In other words, nearly one of every two women over 20 was employed in October, 1978.

INFLATION

Inflation will remain the major economic problem in 1979. There are several reasons for believing that inflation will continue in 1979. Among the more often mentioned factors associated with inflation are the expanding money supply, the depreciation of the dollar abroad, and continued increases in wholesale food items.

After modest expansions in the money supply in 1973-75, the rate of increase accelerated in 1976-78. M_1 expanded by little more than 4% through 1975, but this rate was stepped up to 6.2% in 1976, 8.0% in 1977, and 9.2% in 1978 (Table 2). (M_1 is checking deposits and currency in circulation.) If the popular M_2 measure of the money supply is used as the criterion, the rate of increase was 8.6% in 1975, 11.4% in 1976, 9.3% in 1977, and 9.3% in 1978. (M_2 is M_1 plus time deposits at banks and savings and loans.) If one accepts a monetarist's framework, the growth in M_1 and M_2 substantially improves the prospects for more inflation in 1979.

Contributing to the inflationary pressures is the dramatic decline in the value of the dollar in international currency markets. It appears that Americans are underestimating the inflationary impact of the dollar devaluation. Depending upon the time frame or the currency used for reference, the dollar has declined 25 to 35% against major foreign currencies. The dollar's devaluation takes the edge off foreign products' price competition in American markets. Foreign producers find it increasingly difficult to maintain U.S. price lists when their costs are escalating. A devaluation of the dollar increases foreign producer costs of conducting business in the United States. Foreign goods rise in price reflecting changes in exchange rates, and domestic producers find that price competition is lessening and can therefore raise their prices. Domestic prices consequently begin to rise at a more rapid rate than would have been the case had the foreign competition remained keen. This is particularly valid for such products as automobiles, televisions, radios, and component parts, where there are foreign substitutes. As the price of foreign goods rises, reflecting

Table 1
GROSS NATIONAL PRODUCT
IN CURRENT AND CONSTANT (1972) DOLLARS
(in billions of dollars)

	1978:1	1978:2	1978:3	1978:4
GNP Current	1,992	2,087	2,114 ^e	2,185 ^e
GNP Constant	1,354	1,382	1,394 ^e	1,401 ^e
	1979:1	1979:2	1979:3	1979:4
GNP Current ^f	2,241	2,289	2,338	2,391
GNP Constant ^f	1,410	1,417	1,420	1,423

^e Estimate for 1978.

^f Forecast.

Table 2
ANNUAL PERCENTAGE RATES
OF INCREASE IN
MONEY STOCK MEASURES

Year End	M_1	M_2
1975	4.3	8.6
1976	6.2	11.4
1977	8.0	9.3
1978 ^a	9.2	9.3

^a Annualized rate through August, 1978.

Source: *Federal Reserve Bulletin* 64, No. 10, October, 1978, p. A14.

1978 SUMMARY AND EVALUATION OF THE 1978 FORECAST

Accelerating inflation accompanied by marginal declines in the unemployment rate characterized the U.S. economy in 1978. Real GNP advanced more slowly than in 1977, posting a 3.8% increase over the annual period ending in the third quarter of 1978. This increase was slightly below the forecasted value of 4%, a result which is consistent with the actual inflation rate of 7.7% being above the forecasted value of 7%. Many forecasters were not anticipating such a strong surge in the rate. Continued large increases in the money supply, coupled with deficit spending, were principal factors in the price situation.

Interest rates were affected by the inflation rate's rise, with the prime rate on bank loans increasing by

almost 250 points over October, 1978, to October, 1979. The Treasury bill rate advanced nearly 200 points over the same time period, while rates on large certificates of deposits also showed a gain of 250 points. These actual increases were substantially above the forecasted increases of 50 to 100 points. Credit demands remained strong despite the higher rates, possibly reflecting public expectations of continued high inflation.

Employment was forecast to increase to more than 93 million in 1978. As of October, 1978, employment stood at 95.2 million, an all-time high. Unemployment declined to 5.8% in the same month, below the forecasted value of 7½ to 8%.

COMPARISON OF 1978 FORECAST WITH ACTUAL

<u>Indicator</u>	<u>Actual</u>	<u>Forecast</u>
GNP, in 1972 dollars	3.8% ¹	4%
Prices	7.7% ¹	6-7%
Interest Rates	up 2.3% ²	up ½ to 1%
Employment	95.2 million ²	93+
Unemployment	5.8% ²	7½-8%

¹ Compares 3rd quarter, 1977, with 3rd quarter, 1978.

² Through October, 1978.

the dollar devaluation, domestic producers find it easier to up their price lists accordingly. The effects of the dollar devaluation will be accentuated by the inflated money supply, making price stability most difficult to achieve.

To understand inflation and the role that devaluation can play, economists should examine the experiences of countries where the disease has reached epidemic proportions. During a recent inflationary interval in the United Kingdom, it has been estimated that devaluation had a very direct impact upon their price level. The 10% decline in sterling's value has been associated with a corresponding 10% increase in the price index. This, it should be noted, does not account for all the inflation, only the contribution made by devaluation.

The impact of the devaluation of the American dollar may take longer to work through our economic system than it did in the U.K., because our economy is larger and more complex. If, however, inflation were to follow roughly the same pattern as that observed in the U.K., devaluation of the dollar is going to work one substantial inflationary factor into our economic structure. Unfortunately, this inflationary bias can be expected to persist well into the 1980s.

Food prices, a highly visible component of consumer prices are rising rapidly. Food prices increased 6.4% 1974-75 (December to December), 0.6% 1975-76, and 8.0% 1976-77. Consumer food prices have continued to increase, rising another 12% in 1978 (annualized rate through October).

Food prices will likely increase 8 to 10% in 1979 because of rising producer prices (formerly wholesale prices). The finished consumer foods index (wholesale) was up 11.9% in October, 1978, compared with a year earlier. This double-digit increase in

producer prices for food will influence consumer food prices well into 1979.

The outlook for prices in 1979 unfortunately is not substantially different from 1978. Food and housing costs will probably continue to increase at annual rates of 8% or more. American consumers were fortunate that gasoline prices rose by slightly more than 2% in 1978, but it is unlikely that this situation will persist in 1979.

For 1979 the price level is forecast to increase 8%, using the Consumer Price Index (CPI) as a guide. Some prices will undoubtedly increase more than 8% and others less than 8%. Those items showing the largest price increases in 1978 will probably continue to lead other price increases in 1979. Food and housing costs will probably continue to lead the overall index.

Price increases will again likely be concentrated in the first quarter when changes in the minimum wage and social security tax levels go into effect. Inflation may show signs of moderating during the second and third quarters of 1979 if the economy does begin to lose momentum and if real growth rates decline. This small deceleration of prices may persist into the fourth quarter of 1979, at which time the inflation rate may moderate to approximately 6% on an annualized basis. Although the inflation rate may approximate 6% by the end of 1979, this should not be taken as an indication that our inflation problem has been solved.

THE NEBRASKA ECONOMY

Economic prospects for Nebraska in 1979 are slightly more optimistic than those for the nation. This slightly more optimistic outlook is attributable to Nebraska's employment base and rising beef prices. Employment in Nebraska is evenly distributed across many industries and is not subject

(Continued on page 6)

Review and Outlook

Real output in Nebraska increased in September, with the physical volume index for the state recording a gain of 0.9 percent during the month. This marks the second consecutive monthly rise in the index, resulting in a value of the index which was 42.0 percent above its 1967 base-period level.

The September increase in state economic activity was felt throughout the economy, with all of the five sectors registering gains for the month. This is the first time during 1978 that such an event has occurred. The sectors and their August-to-September increases were: agriculture, +2.7 percent; distributive, +0.9 percent; construction, +0.4 percent; manufacturing, +0.2 percent; and government, +0.1 percent.

Despite recent improvements, the Nebraska physical volume index has not fully rebounded from losses incurred earlier in the year. September's value was still below 1978's peak of 144.2 which was recorded in January. The pattern of movement of the index appears to follow closely changes in the agricultural component of the index. The index of agricultural output (as measured by price-adjusted cash farm marketings) recorded its high for the year in January, fell to its low for the year in July, but has shown some improvement during the last two months.

In sharp contrast, the index for nonagricultural output recorded its lowest value of the year in January. Its current value of 146.4 is the highest value ever recorded (Continued on page 5)

Notes for Tables 1 and 2: (1) The "distributive" indicator represents a composite of wholesale and retail trade; transportation, communication and utilities; finance, insurance, and real estate; and selected services. (2) The "physical volume" indicator and its components represent the dollar volume indicator and its components adjusted for price changes using appropriate price indexes—see Table 5, page 5.

ECONOMIC INDICATORS: NEBRASKA AND UNITED STATES

1. CHANGE FROM PREVIOUS YEAR

September, 1978	Current Month as Percent of Same Month Previous Year		1978 Year to Date as Percent of 1977 Year to Date	
	Nebraska	U.S.	Nebraska	U.S.
Dollar Volume	109.4	112.3	109.4	111.3
Agricultural	106.7	116.8	112.7	109.5
Nonagricultural	109.8	112.2	109.0	111.3
Construction	111.8	116.4	109.2	115.5
Manufacturing	118.7	113.5	113.2	111.6
Distributive	108.4	112.3	108.4	111.7
Government	101.4	107.2	104.8	107.9
Physical Volume	99.1	103.6	101.1	103.9
Agricultural	82.5	94.6	96.4	97.5
Nonagricultural	101.9	103.9	101.9	104.1
Construction	100.9	105.1	98.6	104.4
Manufacturing	109.1	105.2	105.5	104.3
Distributive	100.1	103.7	101.1	104.2
Government	99.5	101.6	101.5	103.1

2. CHANGE FROM 1967

Indicator	Percent of 1967 Average	
	Nebraska	U.S.
Dollar Volume	288.6	269.6
Agricultural	236.7	250.9
Nonagricultural	297.5	270.2
Construction	321.9	258.0
Manufacturing	332.2	260.2
Distributive	290.0	279.3
Government	271.0	261.1
Physical Volume	142.0	133.8
Agricultural	116.6	119.5
Nonagricultural	146.4	134.3
Construction	135.8	108.9
Manufacturing	158.2	125.6
Distributive	145.5	140.1
Government	137.4	139.8

3. NET TAXABLE RETAIL SALES OF NEBRASKA REGIONS AND CITIES (Adjusted for Price Changes)

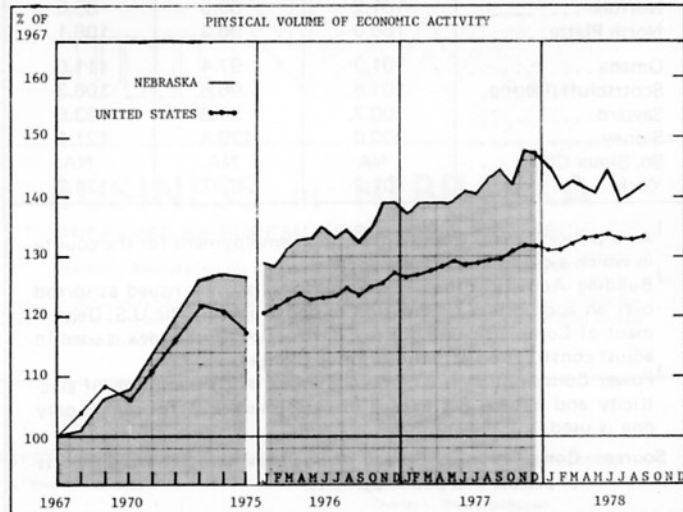
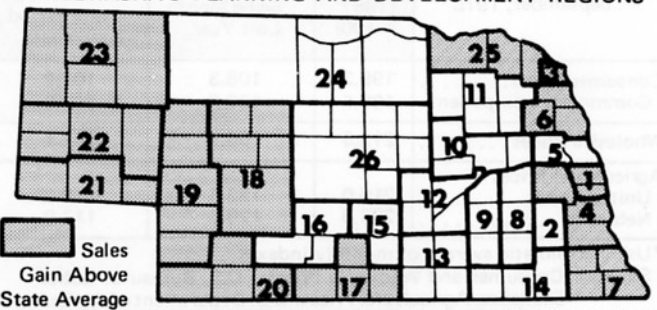
Region Number ¹ and City	City Sales ²	Sales in Region ²	
	Sept. 1978 as percent of Sept. 1977	Sept. 1978 as percent of Sept. 1977	Year to date '78 as percent of Year to date '77
<i>The State</i>	105.3	105.6	102.5
1 Omaha	107.3	107.6	104.8
Bellevue	122.4		
2 Lincoln	99.3	98.6	98.7
3 So. Sioux City	112.7	118.7	107.8
4 Nebraska City	141.0	121.3	110.4
5 Fremont	103.1	104.1	101.8
Blair	109.5		
6 West Point	119.4	114.8	106.6
7 Falls City	111.1	115.3	104.0
8 Seward	114.2	99.4	97.2
9 York	102.9	110.3	94.1
10 Columbus	100.7	105.2	101.2
11 Norfolk	101.7	106.7	100.8
12 Grand Island	102.9	104.7	102.0
13 Hastings	104.0	107.2	98.6
14 Beatrice	95.4	104.0	100.2
Fairbury	102.6		
15 Kearney	101.8	102.2	98.1
16 Lexington	109.2	105.9	96.1
17 Holdrege	92.8	105.3	104.7
18 North Platte	106.5	107.4	103.8
19 Ogallala	100.3	103.6	106.1
20 McCook	105.1	107.7	103.9
21 Sidney	98.5	98.9	108.5
Kimball	96.2		
22 Scottsbluff/Gering	94.6	100.4	105.1
23 Alliance	96.4	95.5	112.6
Chadron	82.4		
24 O'Neill	111.9	114.6	95.0
25 Hartington	98.6	106.0	104.5
26 Broken Bow	98.4	105.4	99.0

¹ See region map below.

² Sales on which sales taxes are collected by retailers located in the state. Region totals include motor vehicle sales; city totals exclude motor vehicle sales.

Compiled from data provided by Nebraska Department of Revenue.

1978 YEAR TO DATE AS PERCENT OF 1977 YEAR TO DATE IN NEBRASKA'S PLANNING AND DEVELOPMENT REGIONS



(Continued from page 4)

for the index. This indicates that in spite of the slow pace of Nebraska's economic activity so far in 1978, the composite of the nonagricultural sectors in the economy has exhibited some strength. This strength, however, has been overshadowed by the weakness in the agricultural sector.

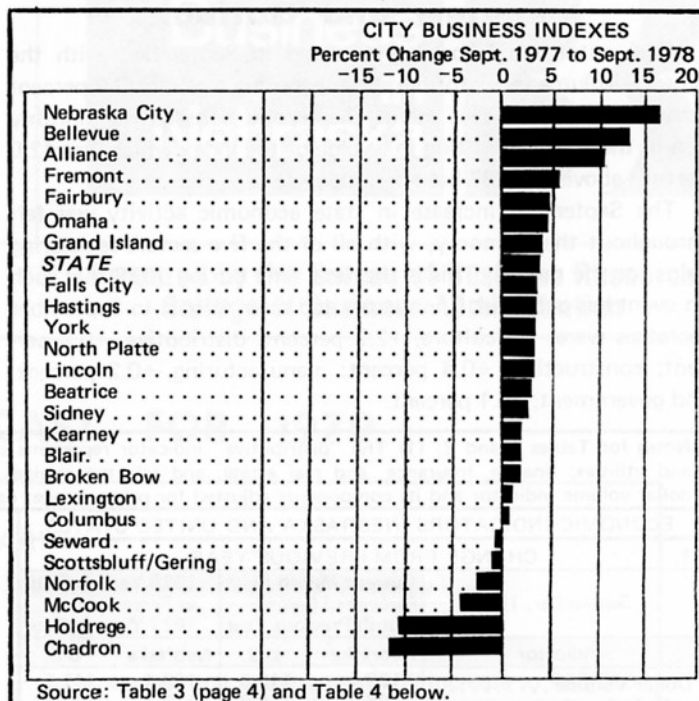
Year-to-date data also indicate the sluggishness in the Nebraska economy during the first three quarters of 1978 when compared to the first three quarters of 1977. The physical volume of output for the state was only 1.1 percent above the level for the comparable period last year. Three of the five sectors recorded increases (manufacturing, +5.5 percent; government, +1.5 percent; and distributive, +1.1 percent), while the two remaining sectors recorded decreases (agriculture, -3.6 percent; and construction, -1.4 percent).

A somewhat different picture of the Nebraska economy emerges, however, when September data are compared to data reported at the end of 1977. Since the end of 1977, the state physical volume index has fallen 3.6 percent, primarily as a result of a 26.6 percent drop in the index of agricultural output. Changes in the indexes for the nonagricultural sectors in 1978 were: manufacturing, +8.5 percent; construction, +2.2 percent; government, -0.3 percent; and distributive, -1.6 percent.

The data for the first three quarters of 1978 imply that unless economic activity in Nebraska increases considerably during the remainder of 1978 (particularly in the agricultural sector), there will be very little, if any, improvement in the Nebraska economy during 1978 when compared to 1977.

The September gain in the state's economy carried over to the indicators of city business activity. Nebraska cities experienced increases in price-adjusted retail sales, employment, and power consumption relative to September, 1977. This higher level of economic activity in September was reflected in the composite city business indexes, with nineteen of the twenty-five reporting cities experiencing increases relative to September, 1977. Nebraska City posted the largest gain in activity, with an increase of 16.8 percent. Other cities with September-to-September increases in business activity were: Bellevue (+13.8 percent), Alliance (+10.1 percent), Fremont (+5.4 percent), Fairbury (+4.7 percent), Omaha (+4.4 percent), and Grand Island (+3.8 percent). It is interesting to note that in September most of the leading cities were located in the eastern and east central parts of the state, whereas in previous months the leading cities were predominately located in the western and west central parts of the state.

The physical volume index for the U.S. economy was unchanged during September. J. A. D.



Source: Table 3 (page 4) and Table 4 below.

The State and Its Trading Centers	Percent of Same Month a Year Ago		
	Employment ¹	Building Activity ²	Power Consumption ³
<i>The State</i>	101.3	97.6	109.9
Alliance	124.4	149.3	100.6
Beatrice	102.1	112.0	133.9
Bellevue	101.3	131.9	131.3*
Blair	99.7	51.3	108.2
Broken Bow	98.9	164.2	105.2
Chadron	91.1	99.8	88.5
Columbus	101.5	69.6	112.2
Fairbury	103.7	105.7	119.0*
Falls City	100.3	55.5	114.2
Fremont	101.6	139.4	120.8*
Grand Island	101.1	119.8	113.9
Hastings	100.9	135.9	100.0
Holdrege	99.9	27.6	81.7
Kearney	99.9	118.6	102.6
Lexington	101.2	44.9	104.9
Lincoln	102.3	123.9	116.0
McCook	92.9	54.9	90.6
Nebraska City	100.2	65.6	121.9
Norfolk	101.2	55.5	89.0
North Platte	100.0	96.3	108.1
Omaha	101.3	97.4	111.0
Scottsbluff/Gering ..	101.6	96.6	106.3
Seward	100.7	20.2	103.6
Sidney	100.0	129.4	121.1
So. Sioux City	NA	NA	NA
York	101.2	82.7	124.7

¹As a proxy for city employment, total employment for the county in which a city is located is used.

²Building Activity is the value of building permits issued as spread over an appropriate time period of construction. The U.S. Department of Commerce Composite Construction Cost Index is used to adjust construction activity for price changes.

³Power Consumption is a combined index of consumption of electricity and natural gas except in cases marked * for which only one is used.

Source: Compilation by Bureau of Business Research from reports of private and public agencies.

September, 1978	Index (1967 = 100)	Percent of Same Month Last Year	Year to Date as Percent of Same Period Last Year*
Consumer Prices	199.3	108.3	107.2
Commodity component	190.5	107.9	106.6
Wholesale Prices	212.3	108.7	107.1
Agricultural Prices			
United States	210.0	123.5	112.2
Nebraska	203.0	129.3	117.0

*Using arithmetic average of monthly indexes.
Sources: Consumer and Wholesale Prices: U.S. Bureau of Labor Statistics; Agricultural Prices: U.S. Department of Agriculture.

(Continued from page 3)

to the wide fluctuations that characterize some industries.

Employment by place of residence increased continuously during 1978 and approximated 750,000 persons by the fourth quarter of 1978. Comparing the fourth quarter of 1978 with the fourth quarter of 1977, employment was up approximately 3.1% in Nebraska. For 1979 the outlook is for continued expansion in employment, although at a slower pace than in 1978. Total employment was projected to about 760,000 by the fourth quarter 1979, up 1.2% from fourth quarter 1978.

Nebraska's unemployment rate will be lower than for the nation in 1979. Unemployment declined to 2.6% of the work force during the fourth quarter 1978. It is expected to show little change in 1979, perhaps rising by less than 1/2 of a percentage point. For the year, unemployment is expected to average 3.3%.

Personal income will continue its expansion more or less in line with the rate of inflation. Personal income expanded to \$12.3 billion during the fourth quarter of 1978, which represents a 9.7% increase over the fourth quarter level of 1977. This was largely an inflationary gain with little allowance for real growth.

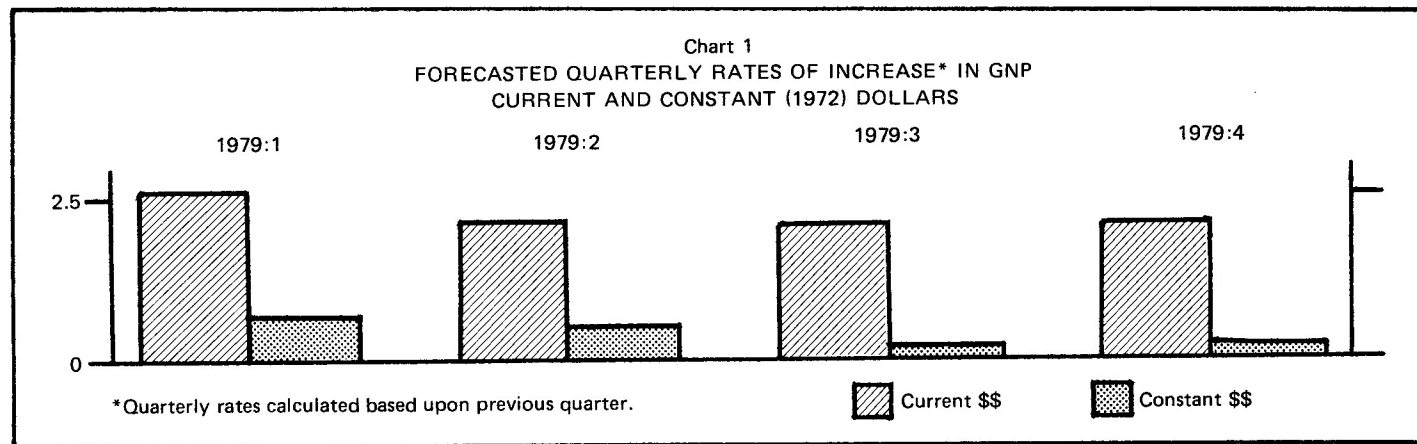
Personal income for Nebraskans will continue to expand in 1979 and the rate of increase will approximate the 9% recorded

in 1978. It is forecast to increase to \$13.2 billion by the fourth quarter of 1979. Contributing to this increase will be expanded wage and salary payments and higher prices for livestock, particularly cattle. While most Nebraskans will see higher incomes in 1979, gains will be offset by rising social security taxes and inflation. Very little progress in increasing real income will be made in 1979.

One of the pleasant surprises in 1978 was the rate of expansion in manufacturing employment in Nebraska. Fourth-quarter manufacturing employment was estimated at more than 94,000, up 4% from a year previous. The outlook for 1979 is for an additional 1,200 to 1,500 manufacturing jobs. Employment in this sector is projected to 96,000 by the fourth quarter of 1979.

Nebraska's economy and personal income will expand about on par with the national average in 1979. Deviation from this average for Nebraska may depend upon grain or livestock prices: higher than anticipated prices will boost personal income above the national average, lower than anticipated prices will likely drop Nebraska's personal income below the national average for 1979. A freeze on livestock prices would have rather adverse economic consequences for Nebraska.

D. E. P.



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