Prime Rate Hits Record; Output Drops

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A number of the nation's largest banks yesterday increased their prime lending rate to 8.75 per cent, the highest that key interest charge has ever been.

In other economic developments, the Labor Department reported that output per man-hour declined slightly in the second three months of the year, while the Commerce Department reported a 1.9 per cent increase in its leading indicators index. Steady increases in this index are supposed to portend upturns in business activity while decreases foreshadow downturns.

Taken together, the economic reports provide contradictory evidence as to whether the economy is braking hard.

If the productivity slowdown is as severe as the statistics indicate, it is yet another heavy impetus to inflation.

Rising productivity has dampened some price rises that might otherwise have occurred, although prices have been skyrocketing, especially at the farm level, since January.

The boost in the prime lending rate was initiated by New York's largest bank, First National City Bank, and quickly followed by a number of other large banks including Bankers Trust and Marine Midland in New York and First Pennsylvania, Philadelphia National and Girard of Philadelphia.

The prime rate is the interest a bank charges its best corporate customers for a short-term loan. During the severe credit crunch of 1969-70, the

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prime rate was at 8.5 per cent for nine months.

The latest increase, which is expected to be followed by most banks throughout the nation, came as the Federal Reserve Board is pursuing an increasingly tight monetary policy but one which is failing to slow the growth in the money supply.

The Fed's discount rate, the rate it charges member banks to borrow from it, matches a 1921 record of 7 per cent.

A spokesman for the administration's Committee on Interest and Dividends said it would have no comment on the prime rate increase.

Earlier in the year the committee, which is headed by Federal Reserve Board Chairman Arthur F. Burns, had been pressuring banks to hold down the prime rate. In April, however, the committee told banks to raise that rate flexibly to respond to other interest charges in the money market. At the same time, it asked banks to restrain increases in consumer and small business loan rates.

Most consumer rates have held fairly steady, while small business rates have increased — although hardly as sharply as the 2.25 per cent increase in the prime rate.

The Labor Department said output per man-hour (productivity) declined at a seasonally adjusted annual rate of 0.2 per cent in the second quarter, after a 4.1 per cent gain in the first quarter. The department said real output increased 2.7 per cent in the recond quarter, while the number of man-hours worked increased 4.1 per cent.

Coupled with a 7.2 per cent increase in compensation per man-hour, the increase in labor costs per unit of output rose at an annual rate of 7.4 per cent. Real compensation per man-hour, which adjusts pay and benedit increases for price and tax increases, fell, however, at an annual rate of 1.5 per cent.

The Bureau of Labor Statistics bases its productivity statistics on the Gross National Product data compiled by the Commerce Department and the bureau's own compilation of man-hours worked.

A number of economists are convinced that real growth in the economy was much faster than the 2.7 per cesnt reported by Commerce last week. If that is the case, then the productivity decline would probably be overstated.

Productivity normally declines somewhat when industries approach full capacity, for a variety of reasons: business must put less efficient machinery in production to satisfy demand, workers may have to work more overtime hours, machinery may need more repairs at higher use rates.

The Treasury's top career economist, Herman I. Liebling, said technical questions which involve adjusting raw statistical data to account for usual seasonal changes caused the Commerce Depertment to understate real output. He calculates real growth at 5.5 per cent and productivity increases at 2.5 per cent.

Because the economy was already operating at such high capacity in the second quarter, the normal huge upswing could not occur. But the seasonal factor adjusted for it anyway and thus understated output, he said.