

## Capital Deepening

One of the remarkable features of the present economic expansion is the sustained strength of investment spending. Figures recently released by the U.S. Department of Commerce highlight the effect of this spending on the growth rate of the nation's capital stock.

At the end of 1998 (the most recent year for which data are available), the total stock of private nonresidential fixed assets stood at nearly \$9.5 trillion. In real terms, the stock of capital grew at a rate of 4.0% in 1998, up from a 3.3% average over the previous two years. Data on investment suggest an even higher growth-rate projection for 1999.

Not surprisingly, much of the increase in capital growth in recent years has been associated with investment in high-technology equipment. Growth in the stock of information processing equipment and software rose by 7.0% in 1998, after having increased at a 5.6% average rate during 1996 and 1997. This component accounts for over 40 percent of the growth rate of total private nonresidential fixed assets since 1995.

An expanding capital stock is an essential feature of economic growth. In an economy with population growth, the stock of capital tends to rise with the labor force in order to maintain adequate capital per worker—a process known as *capital widening*. Recent capital stock growth rates have far outpaced labor force growth, however, implying that available capital per worker has been increasing sharply. This process, known as *capital deepening*, generally is associated with increases in labor productivity.

As the chart shows, capital stock growth followed a slowing trend during the 1970s and 1980s—a period that has been widely noted for its low productivity growth compared with previous decades. After averaging about 2.0% from 1960 through 1972, the gap between capital growth and labor growth (the rate of capital deepening) declined to about 1.2% from 1973 through 1995. For the same two periods, non-farm business sector productivity growth declined from 2.9% to 1.5%.

Since the mid-1990s, capital growth has been rising steadily above average labor force growth, with the rate of capital deepening averaging over 2% since 1995. This increase in productive resources per worker has coincided with the recent increase in the growth rate of economic activity, facilitating gains in both employment and productivity over the latter part of the 1990s.

—Michael R. Pakko

