49

JANUARY 1952 ECONOMIC REPORT OF THE PRESIDENT

HEARINGS

BEFORE THE

JOINT COMMITTEE ON THE ECONOMIC REPORT

CONGRESS OF THE UNITED STATES

EIGHTY-SECOND CONGRESS

SECOND SESSION

PURSUANT TO

Sec. 5 (A) of Public Law 304

(79th Congress)

JANUARY 23, 24, 25, 26, 28, 30, 31, FEBRUARY 1, 1952

Printed for the use of the Joint Committee on the Economic Report

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JOINT COMMITTEE ON THE ECONOMIC REPORT

(Created pursuant to sec. 5 (a) of Public Law 304, 79th Cong.)

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JANUARY 1952 ECONOMIC REPORT OF THE PRESIDENT

WEDNESDAY, JANUARY 23, 1952

(This hearing was held in executive session of the committee, but is made a part of the printed record by mutual consent.)

CONGRESS OF THE UNITED STATES,
JOINT COMMITTEE ON THE ECONOMIC REPORT,
Washington, D. C.

The joint committee met, pursuant to call, at 10:15 a. m., in room 224, Senate Office Building, Senator Joseph C. O'Mahoney (chairman) presiding.

Present: Senators O'Mahoney (chairman) and Flanders; Representatives Patman and McKinnon.

Also present: Grover W. Ensley, staff director; John W. Lehman, clerk, and staff members of the Joint Committee and the Council of Economic Advisers.

The CHAIRMAN. The committee will please come to order.

This session of the Joint Committee on the Economic Report is called in accordance with the provisions of the Employment Act of 1946 to review the President's Economic Report.

The Chair will insert in the record at this point a memorandum which was directed to each member of the committee with respect to the nature and plan of the hearing.

(The memorandum dated January 16, 1952, is as follows:)

CONGRESS OF THE UNITED STATES—JOINT COMMITTEE ON THE ECONOMIC REPORT

MEMORANDUM

January 16, 1952.

To: Members of the Joint Committee on the Economic Report.
From: Joseph C. O'Mahoney, chairman.
Subject: Plan for committee hearings on the President's Economic Report.

The President has transmitted his Economic Report to the Congress and this report has been referred to the Joint Economic Committee. As all members of the Joint Economic Committee are aware, the Employment Act of 1946 directs the committee "as a guide to the several committees of the Congress * * * not later than March 1 of each year * * * to file a report with the Senate and the House of Representatives containing its findings and recommendations with respect to each of the main recommendations made by the President in the Economic Report * * *."

In accordance with customary procedure the committee, preliminary to the preparation of its report, will seek to broaden the basis for its report by obtaining additional facts and analyses bearing on the materials contained in the President's Economic Report from the three following sources: (1) executive and open hearings with the heads of appropriate executive agencies of the Federal Government; (2) round-table sessions with non-Government technicians; and (3) questionnaire returns from representatives of the leading economic interest groups.

The transcript of these committee sessions, together with the comments from economic interest groups, should be available before February 6 so that the committee may proceed with preparation of its report which according to statute is to be filed on or before March 1, 1952.

The subcommittee on General Credit Control and Debt Management of the Joint Economic Committee is making an intensive study of monetary policy. The subcommittee's chairman, Wright Patman, of Texas, is publishing a compendium of materials on this subject and has announced that the subcommittee's hearings will begin about March 1. The subcommittee will be reporting to the full committee before Congress adjourns this summer. The full committee, therefore, in considering the President's Economic Report, will not call witnesses to discuss the monetary problem.

SCHEDULE OF HEARINGS ON THE PRESIDENT'S ECONOMIC REPORT AND AGENDA FOR PANEL DISCUSSIONS

Wednesday, January 23, executive session, room 224, Senate Office Building:
- 10 a. m.: Leon Keyserling, Chairman
  John D. Clark
  Roy Blough
  Council of Economic Advisers, Executive Office of the President

Thursday, January 24, executive session, room 224, Senate Office Building:
- 10 a.m.: Frederick J. Lawton, Director, Bureau of the Budget

Friday, January 25, open to the public, room 362, Old House Office Building:
- 10 a. m.: Roger L. Putnam, Administrator, Economic Stabilization Agency

Saturday, January 26:
- 10 a. m.: Charles E. Wilson, Director Office of Defense Mobilization

Monday, January 28, open to the public, room 362, Old House Office Building
- 10 a. m.: Michael V. DiSalle, Director, Office of Price Stabilization
  Nathan Feinsinger, Chairman, Wage Stabilization Board

Wednesday, January 30, open to the public, room G-16, Senate wing, Capitol:
- 10 a. m.: Panel discussion on the nature and magnitude of the problem of mobilization and economic stabilization:
  - Participants:
    - Thomas Blaisdell, University of California
    - Roy F. Foulke, Dun & Bradstreet
    - Martin Gainsbrugh, National Industrial Conference Board
    - Edwin G. Nourse, consultant economist, Washington, D. C.
    - Boris Shishkin, American Federation of Labor
    - Caroline F. Ware, chairman, Consumers Clearing House, Washington, D. C.
    - Donald Woodward, Mutual Life Insurance Co. of New York
  - Suggested topics for discusion:
    1. What are the general economic implications, short-run and long-run of a "gradual" versus a "quick" military build-up?
    2. What is the outlook, short-run and long-run, for production—manpower utilization, hours of work, and productivity? What is the outlook for demand for this output—Government, foreign, business investment, and consumer? What are the resulting inflationary and deflationary forces?
    3. What are some of the regional and special industry problems?
    4. Can the economy support and maintain, over the long run, an armed force of the size contemplated?
    5. What will be the impact of the mutual security program and other foreign assistance programs on our domestic economy? What consideration should the Congress give to the impact of the defense program on the economies of other free nations?
    6. In general what should be the role of Government economic policy—fiscal, monetary, and regulatory—in light of the nature and magnitude of the mobilization and stabilization problem?

Thursday, January 31, open to the public, G-16, Senate wing, Capitol:
- 10 a. m.: Panel discussion on Federal fiscal policy:
  - Participants:
    - Alfred G. Buehler, University of Pennsylvania
    - H. Van B. Cleveland, Committee for Economic Development
    - Milton Friedman, University of Chicago

Walter W. Heller, University of Minnesota
John P. Miller, Yale University
Richard Musgrave, University of Michigan
Carl S. Shoup, Columbia University
Arthur Smithies, Harvard University

Suggested topics for discussion:

1. What is the outlook, short-run and long-run, for Federal expenditures, receipts (present tax legislation), and balanced budgets? What would be the economic results of substantial deficit financing?
2. Specifically, what can be done to increase the efficiency and economy of the Federal Government: (*a*) in the defense area; and (*b*) in the other areas? What programs should be cut back? How important is our foreign-aid program from a fiscal standpoint?
3. Should taxes be increased to achieve a balanced budget? What taxes? What are the practical limits to increasing taxes under present conditions? What about Colin Clark's 25 percent of national income rule?

Friday, February 1, open to public, G-16, Senate wing, Capitol:

10 a. m.: Panel discussion on Federal direct controls:

Participants:

Jules Backman, New York University
Kenneth Galbraith, Harvard University
Griffith Johnson, Motion Picture Association of America, Inc.
Richard Lester, Princeton University
Edward Mason, Harvard University
Lloyd B. Reynolds, Yale University
Stanley Ruttenberg, Congress of Industrial Organizations

Suggested topics for discussion:

1. What is happening to the structure of American business as a result of the current mobilization and stabilization program?
2. Do we have the human and material resources to support and maintain, over the long-run, an armed force of the size contemplated?
3. What is the outlook, short-run and long-run, for Federal direct controls—price, wage, and materials allocation? How are these controls working today? What controls are required, under present conditions, to halt the "inflationary wage-price spiral"? Will wage increases result in price increases? Should the Defense Production Act be extended and amended?

The CHAIRMAN. We have this morning before us the members of the Council of Economic Advisers whose printed economic review is available to the committee in the document which also included the President's Economic Report.

May I ask how many copies of this were printed?

Mr. KEYSERLING. There were 15,000 copies printed for sale by the Superintendent of Documents, Government Printing Office, and 9,000 for distribution by the Council.

The CHAIRMAN. I am advised that the report is automatically printed as a House document and is available from the Government Printing Office for all persons who care to purchase a copy.

Mr. KEYSERLING. We have greatly reduced our distribution by shifting to the interested parties an even larger share of the responsibility for buying than before. To take one example, in the past we had distributed a couple of hundred copies to members of the Business Advisory Council, which services the Department of Commerce and in part meets with us. This year we arranged to have them buy in bulk from the Government Printing Office. We do have to make a substantial distribution because it contains the President's Economic Report, and its distribution to the press alone on the day of issuance runs into several thousands.

The CHAIRMAN. Now may I say, in opening the session, that the economic aspects of war and preparation for war seem to be growing in importance. War now is an industrial effort as well as a military effort more than it ever was at any time in history, so that the impact falls upon those who are on the home front as well as those who may go to any fighting front.

Inflation seems to be an inseparable factor from military efforts, particularly from military preparation.

There have been available to this committee reports from abroad indicating that military expenditures in Western Europe are having an inflationary effect there.

Of course, the struggle at home here is in part, at least, affected by the effort that the Congress must make to prevent inflation, so that the cost of living and the cost of defense will not get out of hand.

The problem, therefore, seems to be what will this Congress do to preserve a sound economy, since the President's report on the budget clearly indicates that expenditures during the next fiscal year, upon the basis envisaged in the budget, will produce a deficit of almost $15,000,000,000. Such a deficit is clearly very different from the deficits that were incurred when the national debt was so much lower than it is now. Although the economy is growing, and that is a fact in which we can all take a great deal of satisfaction, it still remains a primary problem in the public mind as to how much we should spend, not only for defense but for the normal activities of Government.

The committee felt that it was only proper that the Council of Economic Advisers should initiate the hearing by stating to the committee in summary fashion the reasoning upon which the economic review is based and the policies which it felt ought to be carried out to preserve the American economy during this very critical situation.

Dr. Keyserling, you have the floor.

STATEMENT OF LEON H. KEYSERLING, CHAIRMAN, COUNCIL OF ECONOMIC ADVISERS, EXECUTIVE OFFICE OF THE PRESIDENT

Mr. KEYSERLING. Mr. Chairman and members of the committee, I have no written statement. What I have to say will follow in logic and organization the structure of the published material which begins with a description of the real economy in operation, what is happening to its resources, how they are being used under the impact of the defense program, and then moves on to some more specialized problems.

Our arangement, as we indicated in our communication to the chairman, is that I shall attempt to set forth the underlying factors in a general way; that my colleague, Mr. Blough, will discuss the aspects of fiscal policy which the chairman has identified as being of such great importance, and then Mr. Clark will discuss the general outlook for inflation, the complex of policies to deal with it aside from fiscal policy and, I believe, will want to make some remarks about the longer run-out look.

One of the things that you gentlemen may have noticed in many discusssions of economic problems, particularly by working economists, is that they sometimes start with one aspect of the economy, such as what is happening to prices, or what is happening to inflation, or what is happening to the Federal budget, and then try to trace back from that to the effect—past, present, or assumed—upon the economy. Yet, they all admit that, in the final analysis, they are interested in those segmental problems in terms of how, why, and to what extent they affect the whole economy. How does taxation affect production? How does inflation affect the distribution of resources?

From the point of view of production, and from the point of view of equity, how does a defense program in the final analysis affect the rest of the economy, whether the ability of people to consume and remain contended or the ability of business to get the materials and the manpower that it needs for building up that productive strength which, of course, is the ultimate reliance of the whole economy.

Approaching it in this way, I start here with a chart which shows what I call, for lack of a better term, the real economy, the picture of how our economy has changed and is in process of changing under the impact of the defense program.

And for this purpose the economy might be visualized as a triangle which usually has three sides, although the chart is not in the form of a triangle, and these three sides are the following:

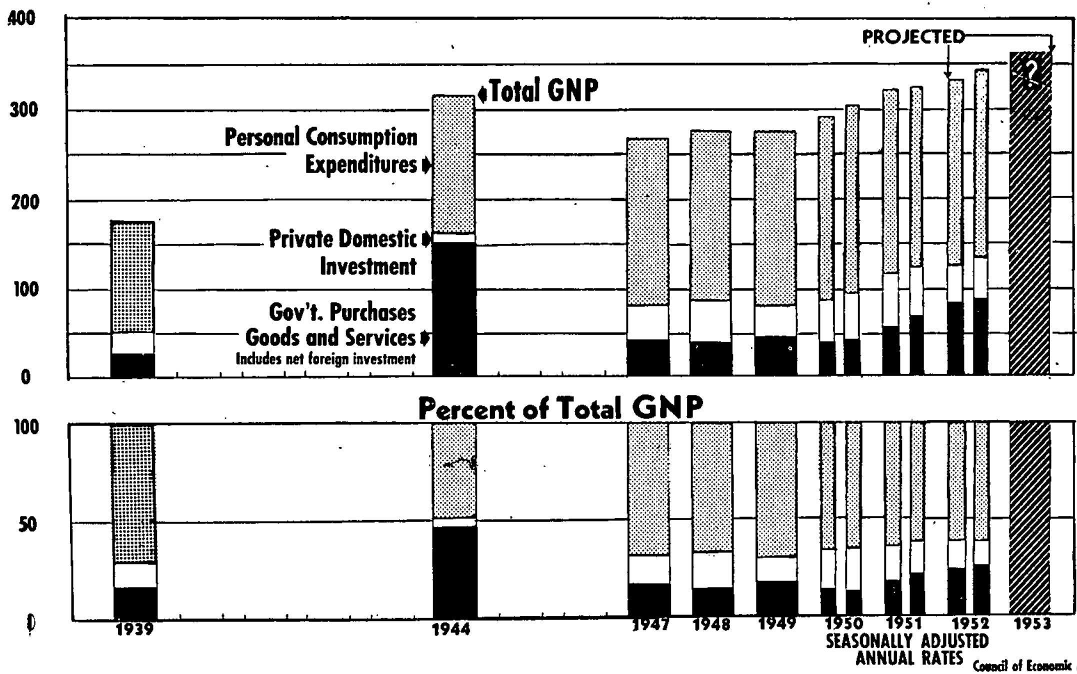
How much of our resources are being taken by the security program, measuring it in dollars as against our total output. And by the security program in this context we mean the whole security program, the American defense build-up, aid to other nations, both economic and military, atomic energy, stockpiling, and so forth. And, obviously, this is a noneconomic undertaking. Nobody claims that a security program in the main upbilds our resources or adds to our strength. It is a drain upon our strength, undertaken for other reasons.

The second side of the triangle is how much of our resources are going into the build-up of productive strength. And the simplest measurement of that, although not a completely accurate one, is business investment. It becomes more accurate when you divide it into segments or components. How much of our resources of materials and manpower and output are going into building plant, in building tools and sharpening tools in the factory and on the farm, which includes fertilizer as well as tools, raw materials as well as finished products? And this, of course, is in one sense the most important part of the triangle, because in the final analysis this is the side which services the other two sides. Both the defense program and the civilian enjoyment side of the triangle are serviced from our productive strength.

The third side of the triangle, as I have just now referred to it, represents ultimate consumer supplies and enjoyments and necessities.

GROSS NATIONAL PRODUCT

BILLIONS OF DOLLARS - 1951 PRICES



Council of Economic Advisers
Graphics by Exos-Navy

This chart undertakes to show what is happening to the economy in terms of these three purposes. The expression is all in terms of a uniform price level. Any price level could be taken for that purpose. We have taken 1951 prices. This is to show not what has happened to the dollar value of the product, but what has happened to the actual product.

The black parts at the bottom of the bars are the Government purchases of goods and services—Federal, State, and local. Of course, the bulk of that, as I shall show shortly, are security outlays.

The white part of the bars is the second side of the triangle, business investment, gross private domestic investment. And I will give something of a breakdown on that in a little bit.

And the third part of the bar, the top part, is personal consumption expenditures, which is the exact reflection of what 155 million consumers more or less are getting by way of goods and services. I have carried this back to 1939.

The CHAIRMAN. Are getting or expending?

Mr. KEYSERLING. Well, the expenditure is the measure of getting, because these are shown at a uniform price level; in other words, if this shows that they are spending so many billion dollars more than in 1939, Senator, it is not in terms of a different price level—it is adjusted for the changes in prices.

The CHAIRMAN. In other words, do I understand that the top part of the bar indicates not only the dollars which are expended, but the commodities which are received in return therefor?

Mr. KEYSERLING. Yes, sir. In other words, this part is bigger than this one. It does not mean that the prices are higher. It means that there are more goods flowing to the civilian economy. There is an adjustment for changes in prices. The simplest illustration of this is that the total national product in 1939 is shown at $179 billion. That is in 1951 prices.

In 1939 prices, it was lower by the amount that there has been a price change since then.

The CHAIRMAN. So that this chart is prepared to eliminate the so-called fall in the value of the dollar?

Mr. KEYSERLING. Yes, sir.

The CHAIRMAN. And show the exact comparison between 1939 and now in terms of 1951 dollars?

Mr. KEYSERLING. Yes, sir.

The CHAIRMAN. You could have done the same thing in terms of 1939 dollars?

Mr. KEYSERLING. Yes.

The CHAIRMAN. And the proportions would have been the same?

Mr. KEYSERLING. The proportions would be the same. It is not exact, because there are, of course, technical difficulties in translating dollars into goods at different price levels, but substantially I think it shows what I do regard as the most important central aspect of the economy, what it is actually producing, and what is actually happening to the things that it produces in terms of how the three sides of the triangle fit together into the whole picture.

The only current interest of the 1939 and 1944 comparison is to show that in 1944 there was an enormous increase in the black bar, representing public outlays and, of course, they were almost entirely national defense. In 1951 prices, public outlays were $151 billion in 1944. And it is perfectly obvious, since this black bar in 1944 is so near the total size of the 1939 bar, that the main way by which in 1944 we maintained a necessary level of business investment and a very ample level of civilian supplies was by increasing the total length of the bar, in other words, increasing total production. And it was an observed phenomenon of World War II that, despite the diversion of enormous resources to the fighting of the war, there was an expansion of real output to the point where in 1944, although the distribution was somewhat different, the general level of civilian supply was, allowing for population change and stating it moderately, about as good as in 1939 though we were carrying an enormously heavier defense burden.

Another interesting thing in this connection, and I do not want to carry it too far because of limitations of time, and it will be dealt with more extensively by Mr. Clark, broadly speaking in the years between 1944 and 1950 the increased productivity capacity created during World War II was reabsorbed in domestic uses and not left languishing or idle. So that by 1950, the last year before the impact of the Korean outbreak, the total output was, approximately, the same as in the war year 1944, but with an enormously different composition. The black part, Government having swung way down, from here to here, the white part, business investment, having greatly risen, and the top part, personal consumption, of course, having risen, so that even on a per capita basis the availability of civilian supplies was greater.

The CHAIRMAN. As I look at that chart, the second column, which is for the year 1944, it would indicate that the Government at that time was expending practically 50 percent of the total.

Mr. KEYSERLING. Just about that, $150 billion out of $320 billion, that is, Government—Federal, State and local. Most of it was Federal.

The CHAIRMAN. That business expenditures were very slight, percentagewise.

Mr. KEYSERLING. Yes, sir.

The CHAIRMAN. And that consumer expenditures, ordinary individual expenditures, were practically the same as Government expenditures?

Mr. KEYSERLING. Just about.

The CHAIRMAN. How do you compute the amount of business expenditures—what factors go into that?

Mr. KEYSERLING. I have a chart which shows gross private domestic investment in more detail. It shows the level of private business investment in construction, in residential construction, in tools, plant, and equipment. There is a breakdown in appendix table B-3 of the Economic Report which shows the exact composition of gross private domestic investment. It is the total investment of the business community, in 1951 prices on an annual basis, in plant expansion, in inventory accumulation, and in the building and improvement of tools and equipment, and in other construction, all of the things that it consumes for the purpose of ultimately producing goods for others to consume.

The CHAIRMAN. If I can judge the length of these columns from this distance I would come to the conclusion that while ordinary consumer or individual expenditures in 1952 are less, percentagewise, than they were in 1947, they are actually in dollar value greater than they were in 1947.

Mr. KEYSERLING. In goods value greater; yes, sir. The reason for the very small size of the business investment bar during World War II, although there were enormous expansion programs, is that during World War II for a variety of reasons most of those expansion programs were financed by Government and, therefore, enter into the black bar. And the plant and capacity which was added and built was mostly disposed of to industry after the war.

The CHAIRMAN. Then do I understand that the white bar on the first chart represents only investment?

Mr. KEYSERLING. Private outlays. In other words, if the plant was built by the Government and financed by the Government, as many were during World War II, it would enter into the black bar.

The CHAIRMAN. It does not include expenditures privately made for labor, or does it?

Mr. KEYSERLING. It includes the labor cost factor in the private outlays of an investment character.

The main point I want to discuss in connection with these later bars is this, that the essence of the mobilization effort is to try to find what balance among these three bars, in other words, among the part of our resources devoted to the security build-up, the part devoted to the industrial or productive build-up, and the part devoted to consumption, will give us the greatest strength in the long run in the face of a situation which is uncertain, in the sense that World War II situation was certain. Then, while we could not know for sure who would win, we knew the die was cast. The philosophy of the effort now is to try to undertake a vigorous and substantial security build-up, but at the same time maintain a high enough level of civilian supplies, not only to satisfy the necessities of life, and even they are in part subjective, because what we regard as the necessities of life, people in China or even in Great Britain would regard as fantastic luxuries—but also to sustain a level of civilian supplies which in a free democracy under current conditions will keep the people feeling that there is hope as well as life, and that they are not being so sharply cut back by a defense program as to undermine support for that program while the program remains necessary.

You might call that a political consideration. I do not care much what you call it. It is a factor in the life of our economy under current conditions.

Moreover, the purpose is to keep a very high level of business investment, because in the long run since production is the ultimate source of all wealth and all economic strength. We must keep building the essential parts of the industrial mobilization base as it is sometimes called, so that if the defense burden does last for a long time it can be supported with relatively less strain on other parts of the economy, whether measured by resource strain, or by the taxes that reflect that strain if they are enacted, or whether measured by pressure upon supplies which translate themselves into inflation. The strain becomes less as the productive power of the economy increases.

Of course, I cannot here talk either to validate or invalidate the size of these black bars in the later years, because the Council has taken the position that we cannot possibly be expert in what the size of the primary security program should be from the viewpoint of national protection. We have views on it as citizens, everybody does. We believe that whatever is undertaken should be undertaken as economically as possible.

We do not pose as experts or quasi-experts as to what the size of the defense outlay should be unless it should reach the point where we felt that it could be demonstrated that it was impoverishing the other two sides of the triangle to the degree that it weakened our general economic strength.

Looking candidly at the depiction of what actually has happened in the economy, we have not yet been prepared to say that a program of the current or projected size has reached that point of danger. It is burdensome, it involves cut-backs and hardships; it raises difficult financing problems, but we cannot say, at least we cannot say as of now, that it threatens to impoverish the industrial mobilization base or weaken it, or cut civilian supplies to an intolerable level.

In a general way, the year 1951 showed that, due to the security build-up, total public outlays rose from $41 billion in the first half of 1950, to $71 billion at an annual rate in the second half of 1951.

Meanwhile, the changes in the level of consumer supplies were small, from about $204½ billion to $203 billion. Now allowing for population growth, that represents a slight per capita decrease, but it is still a very heavy level of consumer supplies, and that will be borne out by current popular observation of the level of food supply, clothing, automobile supply, television supply, radio supply—all kinds of supply—in 1951.

As to the industrial mobilization base or the broad base of our productive capacity which, I think, is the most important of the three for the reasons given, although it is an intermediate step between production and consumption, in 1951 there was a level of investment for the year as a whole of approximately $59 billion, 63 in the first half and 55 in the second half.

This level of business investment contrasts with $48 billion in the very high level year 1948 and, of course, is enormously higher than in prewar years. The high significance of this will be shown a little more clearly in a later chart, which breaks it down, and shows just what was accomplished and is in process of accomplishing during the course of 1951 and on into 1952 in expansion of certain basic or vital elements in the production base such as steel, aluminum, electric power, transport, copper and the like.

Running on into 1952, I have here some computations which I would like to ask permission not to have inserted in the record in exact detail, because we do not like to make predictions of future years, since they are problematical, but roughly speaking, we make the best estimate we can.

The CHAIRMAN. This is off the record.

Mr. KEYSERLING. It may go on the record. I want to get the gist of it in the record, but not the exact figures.

The CHAIRMAN. All right.

Mr. KEYSERLING. Not because they are secret, but because they are estimates.

The estimate of public outlays, of course, is based upon the projected size of the defense program which is fairly clear, at least, for the next calendar year, rather independent of the exact size of the appropriations for the fiscal year 1953.

The computation is that the now projected defense program will lift the level of spending or take of the economy for that purpose by about $20 billion between the annual rate now and the annual rate at the end of next year.

Mr. CLARK. This year.

Mr. KEYSERLING. The end of this year, calendar 1952.

The estimate of business investment is based upon current expansion programs now under way, commitments already made, and the declared investment intentions of business, which are pretty well rounded out, at least two or three quarters ahead, by a process of accumulating of individual business intentions.

The estimate of consumer expenditures is somewhat more problematical, from the viewpoint of what they will actually spend as against what they will save, and that will enter into the estimate of the inflationary outlook which Mr. Clark is going to discuss, but these estimates in any event are consistent with the available supplies of consumer goods, assuming an expanding defense program and a large investment program.

What it shows in broad outline, moving on into 1952, is that there would be, with the expanded defense program a high and rewarding level of investment in plant and equipment, not so high as over this past year, but that the decline would occur in part because of a lower inventory investment and in part through the weeding out of the less essential forms of investment. For example, housing, of course, is essential in peacetime, but the estimate contemplates a considerably lower level of residential construction, somewhere in the neighborhood of 750,000 or 800,000 in 1952, contrasted with about 1,100,000 in 1951. It also contemplates a lower level of automobile output, moving downward toward about 4 million, as against 5.3 million in 1951, and so forth.

But it nonetheless shows, measured against the need for the security program, that the economy can move ahead under this program with good servicing to the other two sides of the triangle. Further, if total war is prevented, by a couple of years from now (with the basic expansion programs more or less completed, thus relieving the shortages of critical points of the economy, and with the defense program leveling off at what might be called a maintenance level or even at the now projected level) we would move again to a level of civilian supplies and a level of available resources for business investment higher than currently and, of course, a priori higher than past years.

That is the broad picture. I do not want you to think that these other charts are going to take as much of your time as this first one. I have concentrated on this first one because it seems to me to be rather central to the whole course of our presentation.

The CHAIRMAN. And easier for the committee to understand.

Mr. KEYSERLING. Well, I think that is a prime requirement. I think it is easy to understand, because it does try to put on one chart a whole picture of what is happening in the economy in real terms.

Senator FLANDERS. May I inquire whether at any point you will have the personal consumption expenditures on a per capita basis?

Mr. KEYSERLING. I do not have it in any of these charts, but we have the figures and can readily make them available to you.

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Senator FLANDERS. I think it would be interesting to see what is happening to the persons in that blue area.

Mr. KEYSERLING. Yes. The Economic Report does contain, Senator, at one point a comparison that does not go year by year, but compares the gains in living standards since pre-World War II. That is chart 3 on page 7. We could very easily show you what has happened over the intervening years.

The basic point of it is that in 1951, with the security program, the living standard was through more ample supply of goods very much higher than in the prewar period, and the first two bars on that page show it on a per capita basis adjusted for price changes.

Senator FLANDERS. It would be interesting, however, to see what the defense program is doing to that item.

Mr. KEYSERLING. Yes, and that can readily be shown.

The CHAIRMAN. May I ask, with respect to chart 3 in the report, in what dollar is that computation made?

Senator FLANDERS. Based on the 1951 prices, the index?

Mr. KEYSERLING. Yes. Further in answer to your question, from this large chart with which I have opened my discussion, although I will supply you with the additional information, since the change in population from year to year is not great these bars do indicate in a way that there has not been much change in the per capita availability of supplies in 1951 contrasted with 1950. I do think that inflation has tended to make some nondesirable redistribution of the availability of supplies.

Total and per capita personal consumption expenditures in current and 1951 prices, 1939–51

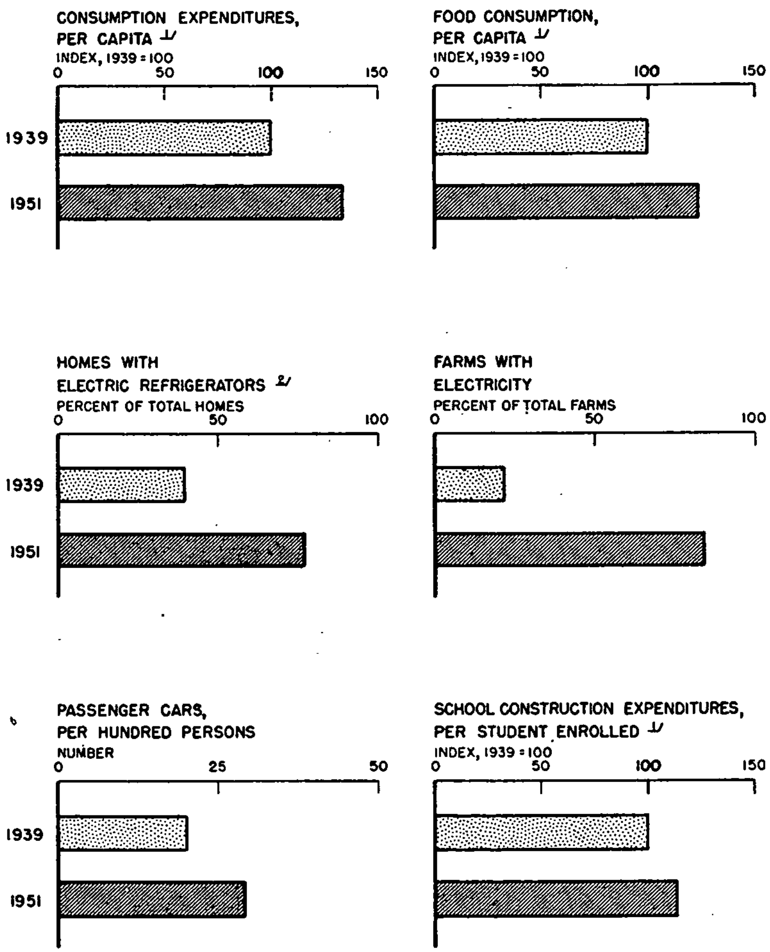
Period	Total personal consumption expenditures (billions of dollars)		Per capita personal consumption expenditures (dollars)		Population (thousands)
	Current prices	1951 prices	Current prices	1951 prices	
1939	67.5	129.4	516	989	130,880
1940	72.1	137.0	546	1,037	132,114
1941	82.3	147.6	617	1,107	133,377
1942	91.2	145.5	676	1,079	134,831
1943	102.2	149.3	748	1,092	136,719
1944	111.6	155.3	806	1,122	138,390
1945	123.1	165.6	880	1,183	139,934
1946	146.9	184.1	1,039	1,302	141,398
1947	165.6	188.6	1,149	1,309	144,129
1948	177.9	191.9	1,213	1,309	146,621
1949	180.2	196.6	1,203	1,318	149,149
1950	193.6	207.5	1,276	1,368	151,689
1951 [1]	204.4	204.4	1,324	1,324	154,353
	Seasonally adjusted annual rates				
1950: First half	186.7	204.4	1,235	1,352	151,132
Second half	200.4	210.6	1,315	1,382	152,438
1951: First half	205.0	205.5	1,334	1,337	153,699
Second half [1]	203.8	203.2	1,314	1,310	155,107
1950: First quarter	184.7	203.5	1,224	1,349	150,847
Second quarter	188.7	205.2	1,246	1,355	151,390
Third quarter	202.5	214.4	1,332	1,410	152,068
Fourth quarter	198.4	206.9	1,299	1,354	152,774
1951: First quarter	208.2	209.4	1,357	1,365	153,396
Second quarter	201.7	201.6	1,310	1,309	154,011
Third quarter	202.5	203.1	1,309	1,313	154,724
Fourth quarter [1]	205.0	203.4	1,319	1,308	155,469

[1] Estimates based on incomplete data; fourth quarter by Council of Economic Advisers.

Source: Department of Commerce and Council of Economic Advisers.

GAINS IN LIVING STANDARDS

By almost any measure, the standard of living has improved markedly since the pre-World War II period.

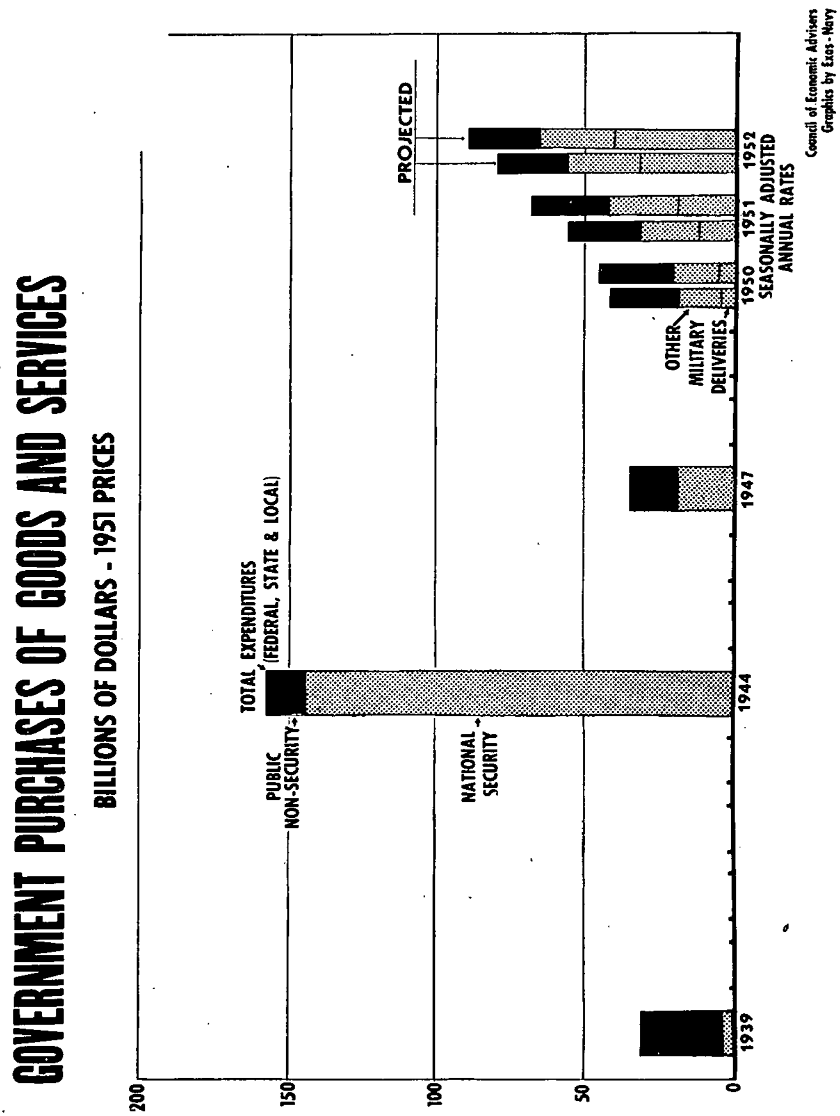


1/ INDEXES BASED ON EXPENDITURES IN 1951 PRICES. SCHOOL CONSTRUCTION EXPENDITURES FOR 1939 INCLUDE WORKS PROGRESS ADMINISTRATION PROJECTS, AND ARE ADJUSTED FOR PROBABLE LOWER PRODUCTIVITY.

2/ END OF YEAR DATA.

SOURCES: DEPARTMENT OF COMMERCE, McGRAW-HILL PUBLISHING COMPANY, DEPARTMENT OF AGRICULTURE, FEDERAL SECURITY AGENCY, AND COUNCIL OF ECONOMIC ADVISERS.

The CHAIRMAN. Are there any questions with respect to this first chart? Apparently not.



Mr. KEYSERLING. This chart I shall not cover in detail because you are having a presentation from the Budget Bureau tomorrow or the next day. In brief, it just breaks down the black line on the first chart, the public outlay sector, and shows what part of the total of Federal, State, and local expenditures is involved in defense programs. And because you will go into that in detail tomorrow, I would rather skip it if it is agreeable to the committee.

The dark part shows the public nonsecurity outlays. The lighter part shows security outlays for the various years.

The CHAIRMAN. And Federal, State, and local are all combined in one?

Mr. KEYSERLING. They are not segregated here, because we are looking at it from the viewpoint of the national economy, and the relative drain upon our resources encompassed in public programs, security programs, and private outlays.

The CHAIRMAN. What year is represented by the second column?

Mr. KEYSERLING. 1944.

One of the interesting things in this last bar, and I am not saying it argumentatively in any way, is that the lighter portion in 1951 and 1952—this is $26 billion here in the second half of 1952—happens to be about the same as the $26.1 billion in 1939.

The CHAIRMAN. That is to say, the amount expended for nonsecurity objectives in 1952 was approximately the same as in 1939?

Mr. KEYSERLING. Yes, despite a much larger population and a much bigger country. I am not saying that to advance the argument that further economies could not be achieved. It is just an observation that the growth both absolutely and relative to the size of the economy has reflected the world burden. It does not necessarily mean that this bar should not be still shorter, because you can say that, because of the world burden being so much greater, you have to cut down even more on the other part of the bar.

This breaks down the second part of the bars on the first chart. You remember the white part dealing with business investment. It shows more specifically, partly responsive to the question that the Senator asked, the precise nature of gross private domestic investment over these various years. And it is broken down into residential nonfarm construction, other construction, producers' durable equipment, which is the heart of the mobilization base, and changes in business inventories.

What this shows, broadly speaking, is the line of development, contrasting the late forties and early fifties with the prewar period. It shows that we may reasonably look forward in 1952 to a further contraction in residential construction as I had indicated, as shown by this black part of the bar, a further contraction in other construction and the maintenance of a very high level of outlays in durable equipment, which is the heart of the mobilization base. Here the estimate is, roughly speaking, for the first half of 1952 at an annual rate of $25 to $28 billion, contrasted with $27 billion and $29 billion for the two halves of 1951, or relatively about the same.

Representative MCKINNON. Do those changes in the projection on the business inventory indicate an increase in inventories in 1951 and 1952?

Mr. KEYSERLING. In 1951 or 1952.

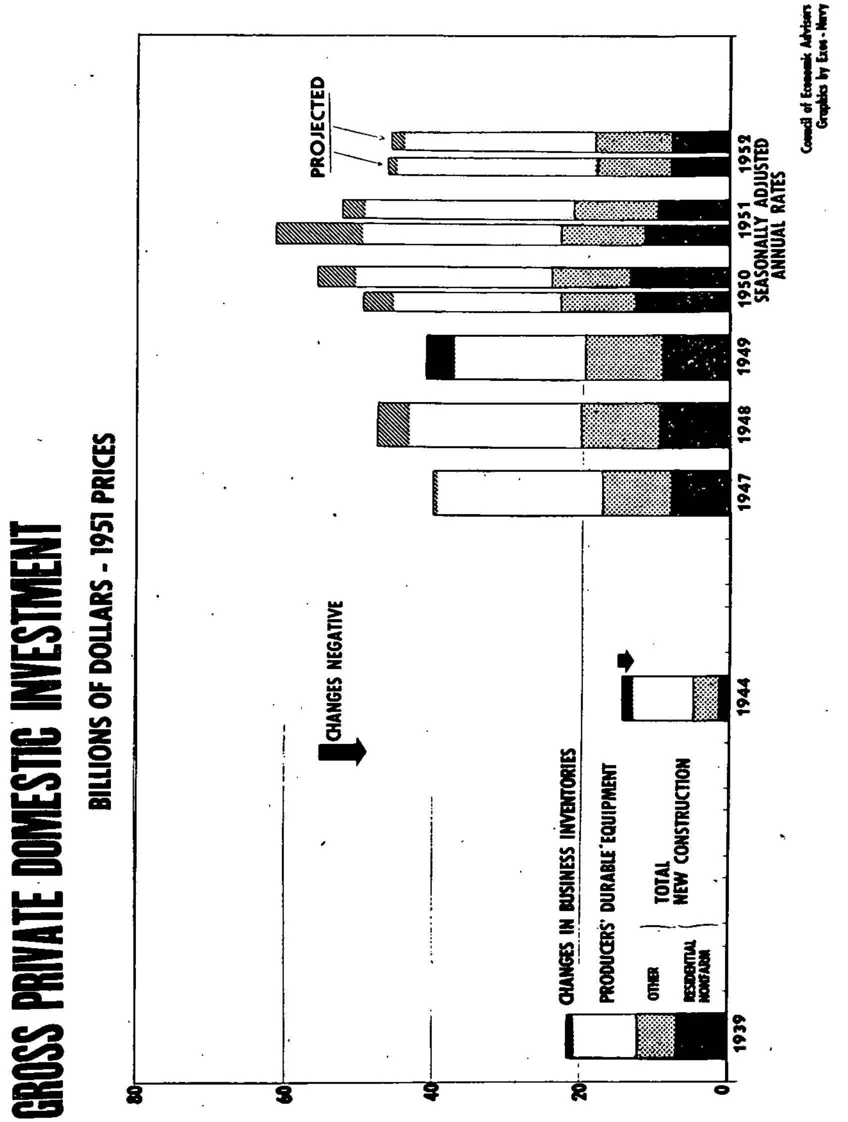
Representative MCKINNON. At least, you are cutting down 1952 over 1951?

Mr. KEYSERLING. Very much so, as to the rate of increase.

Representative MCKINNON. But the size indicates an increase; does it not?

Mr. KEYSERLING. Yes, some increase. The only negative figure is shown in 1944.

I think all of the members of the committee, and I think you particularly, Senator Flanders, will be interested in this lighter part of



the bars here which relate to investment in producers' durable equipment. I think that is so important—in fact, I think it comes so close to the whole heart of the effort for this kind of period—that I just want to run off briefly these figures.

In 1948, $23 billion. That was considered a very high investment year.

In 1949, the year of partial and limited recession, $21 billion, still a high level. I think, as a matter of fact, one of the reasons that the recession did not prolong was that this was reasonably well maintained.

In 1950, at an annual rate of $26 billion in the second half of the year and moving sharply upward; and as high as $22 billion in the first half of the year even before the impact of the Korean aggression. In other words, there was an upward movement in that very important segment of the economy even before Korea.

Senator FLANDERS. I think that is worthy of note, because the suggestion is so often made that we went into the Korean war in order to prevent a depression. We were already coming out. That is, you hear from radical sources that remark made over and over again. Yet, we were on our way out before the Korean thing struck.

Mr. KEYSERLING. I think so. I think that one of the greatest potential areas for the development of our strength in other parts of the free world would be much more information than they are not getting in answer to just that line of propaganda, because it is very much used by the Russians and others, and it is even used by some anti-Russian and free economists and others in some of these countries, who really think that the nature of the American economy is depression-ridden, as it was at some times in the past. But I think the facts are enormously significant for our own strength and the strength of the free world.

By 1951, the second half of 1951, the producers' durable goods and equipment investment figure was up to $29 billion at an annual rate. The average for the year as a whole was about 27, 27, and 29 for the two halves of the year.

The contemplation for 1952 is that this type of investment can be estimated somewhere in the neighborhood of a $26 to $28 billion annual rate in the first half of the year and something like $24 to $26 billion in the second, maintaining a very high level of investment in that sector.

And this is very important as to our capacity to bear the burden of defense, and very important as to the ultimate implications for the inflationary burden and also for when we will arrive at a stage where, with leveling off of the burden in some places and expansion of output in others, the budgetary problem will be more manageable later on than it seems to be over the next year.

Senator FLANDERS. Is there any significance to the different shading of that top sector for 1949—that is darker than in the other.

Mr. KEYSERLING. That indicates a negative change in inventories; in other words, in 1949 you had a disaccumulation or decumulation of inventories, just as in 1944. That is the significance of that.

Representative PATMAN. How much was from earnings of corporations?

Mr. KEYSERLING. That I could not answer from this chart. I could supply that for you.

Representative PATMAN. Do you have that information in any chart?

Mr. KEYSERLING. I do not believe it is in a chart. I do not think so. We could easily supply it for you.

Representative PATMAN. Will you supply it for the record at this point?

Mr. KEYSERLING. Certainly, I will.

(The information to be furnished is as follows:)

Net change in nonfarm inventories

[Millions of dollars]

Year	Total	Corporate	Noncorporate	Year	Total	Corporate	Noncorporate
1939	344	251	93	1946	6,334	6,037	297
1940	2,035	1,633	402	1947	1,408	1,383	25
1941	3,416	3,165	251	1948	3,717	2,153	1,564
1942	756	470	286	1949	−2,493	−2,176	−317
1943	−502	−457	−45	1950	3,586	2,402	1,184
1944	−264	−1,070	806	1951 [1]	8,036	7,713	323
1945	−598	−1,027	429				

[1] Preliminary estimate.

Source: Department of Commerce.

The CHAIRMAN. Would you state again what the different segments mean?

Mr. KEYSERLING. The black one is the residential nonfarm construction, housing.

The next one is the other new construction. That would include the construction of a theater, the construction of a building of some kind or other.

The white is producers' durable equipment, which is your tools, broadly speaking, tools of production.

And the segment with diagonal lines is changes in business inventory.

The CHAIRMAN. Have you any answer to the question as to whether or not the expenditures and investments which are made in expanding plant capacity are so great that if the national-security program were stopped there would be no outlet, no market outlet for the production of which such plants would be capable of producing?

Mr. KEYSERLING. May I ask my colleague, Mr. Clark, to discuss that either now or when he comes on, because at your suggestion we had a certain division of the "spoils" here. I have my views on that subject, which I think are well known to the committee.

I think that the record of what happened after 1944 indicates that our business system has the capacity to beat the swords back into plowshares. If we had not, we would be sunk, because we have the productive power. And, if we ever do not learn how to use it, we will be sunk in any event. However, Mr. Clark is going to cover that.

The CHAIRMAN. We will have Mr. Clark do that then.

Representative PATMAN. I would like this broken down a little more, the gross private domestic investment, not only the amount of this from earnings of corporations, but where else it came from.

Mr. KEYSERLING. Well, that, I believe, we have in our published materials. At least, we did in previous years, as to the sources and uses of funds.

Representative PATMAN. That is right.

Mr. KEYSERLING. Which shows which part of the investment comes from internal financing, and what part comes from borrowings.

Representative PATMAN. Yes, and what type of borrowings.

Mr. KEYSERLING. We have had charts on that in the reports in the past. I believe there is a chart in there this year, but if there is not it is certainly shown in the tabular column materials.

There are a lot on page 203.

Mr. CLARK. On page 203 of the Economic Report.

Mr. ENSLEY. And a chart on page 83.

Representative PATMAN. Thank you very much.

Mr. KEYSERLING. I am sure that you will find that it does supply the information. If not, we will be glad to supplement that.

The CHAIRMAN. Would you care to have that inserted?

Representative PATMAN. Yes, sir.

The CHAIRMAN. Very well, the table on page 203, table B-37, will be inserted in the record.

(Table B-37, p. 203 of the Economic Report, is as follows:)

TABLE B-37.—*Sources and uses of corporate funds, 1947-51* [1]

[Billions of dollars]

Source or use of funds	1947	1948	1949	1950	1951 [2]
Uses:					
Plant and equipment outlays	16.2	18.0	16.1	16.6	21.7
Inventories (change in book value)	7.1	4.2	-4.3	7.5	8.6
Change in customer receivables	7.6	4.0	-.5	10.0	5.0
Cash and U. S. Government securities	1.2	1.9	3.0	5.0	3.0
Other current assets	-.1	.1	-.2	.3	.5
Total uses	32.0	28.2	14.1	39.4	38.8
Sources:					
Internal:					
Retained profits and depletion allowances	11.6	12.8	9.1	12.9	8.0
Depreciation allowances	5.2	6.2	7.0	7.5	8.5
Total internal sources	16.8	19.0	16.1	20.4	16.5
External:					
Change in trade debt	4.6	1.2	-2.9	5.9	3.5
Change in Federal income tax liability	2.3	.8	-2.1	7.1	8.5
Other current liabilities	1.0	(3)	-.1	.3	1.0
Change in bank loans	2.6	1.1	-1.9	2.5	3.5
Change in mortgages	.6	.7	.7	.9	1.0
Net new issues	4.4	5.9	4.9	3.7	5.8
Total external sources	15.5	9.7	-1.4	20.4	23.3
Total sources	32.3	28.7	14.7	40.8	39.8
Discrepancy (sources less uses)	-.3	-.5	-.6	-1.4	-1.0

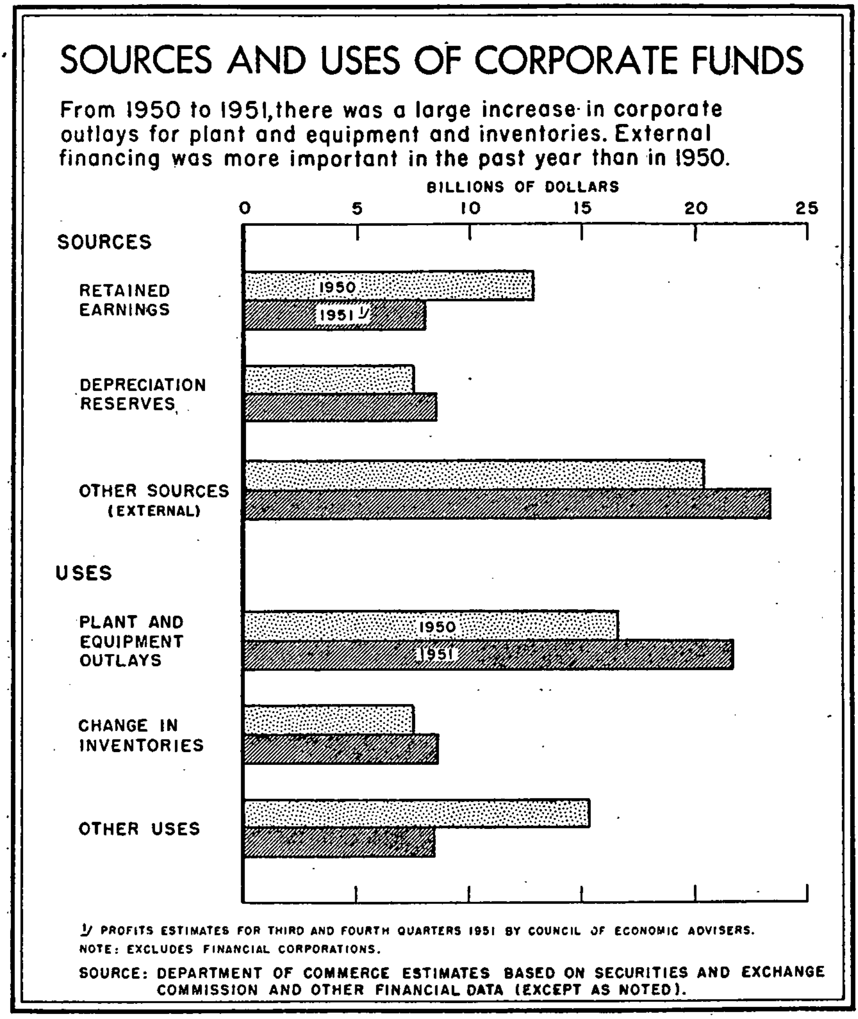
[1] Excludes banks and insurance companies.
[2] Estimates based on incomplete data; by Council of Economic Advisers.
[3] Less than $50 million.

Source: Department of Commerce estimates based on Securities and Exchange Commission and other financial data (except as noted).

Representative PATMAN. Also, chart 23 on page 83.

The CHAIRMAN. It may be difficult for us to get that chart on that page, because it is a diagram; but, if possible, we will.

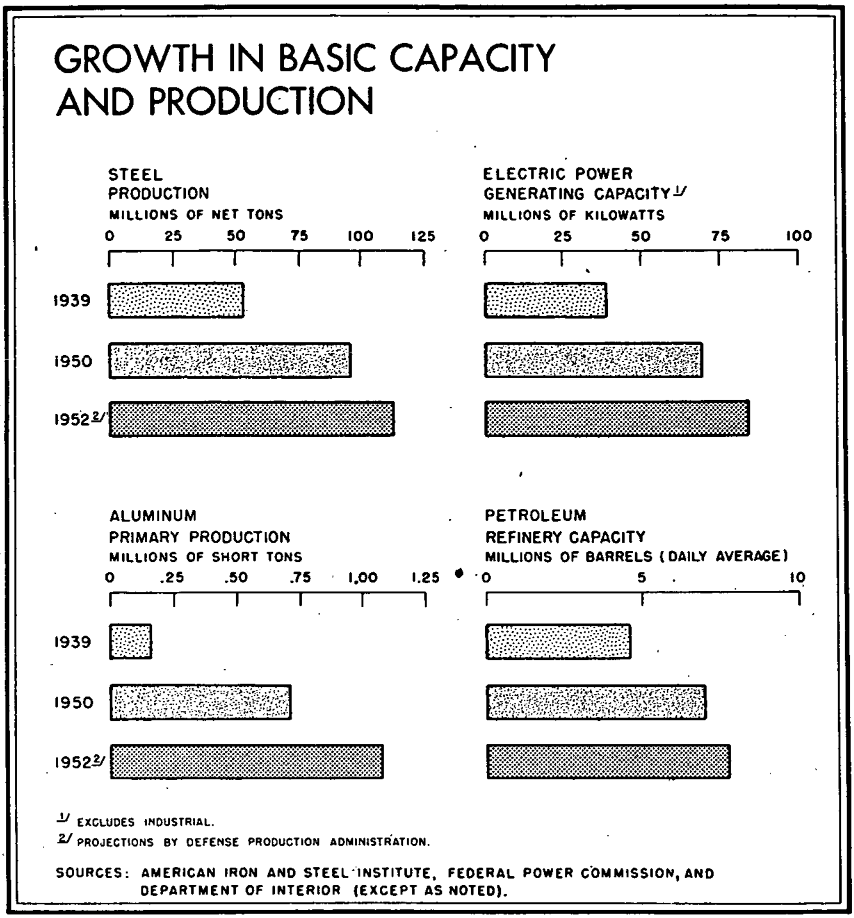
Mr. KEYSERLING. This chart, which is a blow-up of one of the charts in the Economic Report, shows in terms of basic capacity certain vital sectors of the economy, what this growth of the industrial mobilization base means, showing it for steel, aluminum, petroleum, and electric power, and contrasting the pre-World War II situation with the 1950 situation and with the 1952 situation. All of these programs are in very short run to a degree of inflationary, and thus reveal the complexity of the problem, because any program which absorbs manpower and resources before it translates them into the production of goods is a strain upon resources and adds to inflationary pressures. But these programs are a calculated balance, trying to



solve the longer-run problem effectively at the cost of some short-run strain.

As you will see in the Economic Report itself, some of the programs of expansion have really been terrific, which is the word for them. Some people think they have been too great. I do not think so, but there is a division of opinion on that. In any event, these programs reflect an enormous accomplishment on the part of the business community, which is itself doing a job that in large part was Government-financed during World War II. There have been some stimuli through tax amortizations and the like, but they have been a small fractional part of the investment cost, contrasted with the public construction of such facilities during World War II.

The CHAIRMAN. Are you saying that the evidence before the economic advisers indicate that private capital is doing a larger propor-



tion of the industrial expansion now than it did during World War II?

Mr. KEYSERLING. Enormously larger—really almost incomparably larger—enormously larger.

The CHAIRMAN. How much larger?

Mr. KEYSERLING. You get it a little bit from the first chart, gross national product, which shows that tiny white segment, contrasted with the larger white segments in 1950 and 1951. To get exactly how much larger, you would have to contrast not only the proportion but also the actual figures. We could give you that contrast.

The CHAIRMAN. I think it would be very interesting.

Mr. KEYSERLING. Almost incomparably larger, if anything can be incomparable, but enormously large. We will furnish the information.

(The information is as follows:)

Gross national product

Period	Total gross national product	Government purchases of goods and services, including net foreign investment: Total	Government	Net foreign investment	Gross private domestic investment	Personal consumption expenditures
	Billions of dollars, 1951 prices, seasonally adjusted annual rates					
1939	179.3	28.3	28.8	−0.5	21.6	129.4
1944	320.0	151.4	159.5	−8.1	13.3	155.3
1947	271.5	42.7	35.5	7.2	40.2	188.6
1948	280.4	40.9	42.4	−1.5	47.6	191.9
1949	280.1	46.1	49.1	−3.0	37.4	196.6
1950:						
First half	294.2	40.6	45.2	−4.6	49.2	204.4
Second half	307.9	41.6	46.2	−4.6	55.6	210.6
1951:						
First half	323.8	55.3	56.9	−1.6	63.0	205.5
Second half	329.8	71.8	70.0	1.8	54.6	203.2
	Percent of total gross national product					
1939	100	16	16	(1)	12	72
1944	100	47	50	−3	4	49
1947	100	16	13	3	15	69
1948	100	15	15	(1)	17	68
1949	100	17	18	−1	13	70
1950:						
First half	100	14	15	−1	17	69
Second half	100	14	15	−1	18	68
1951:						
First half	100	17	18	−1	19	64
Second half	100	22	21	1	17	61

[1] Less than 1 percent of total.

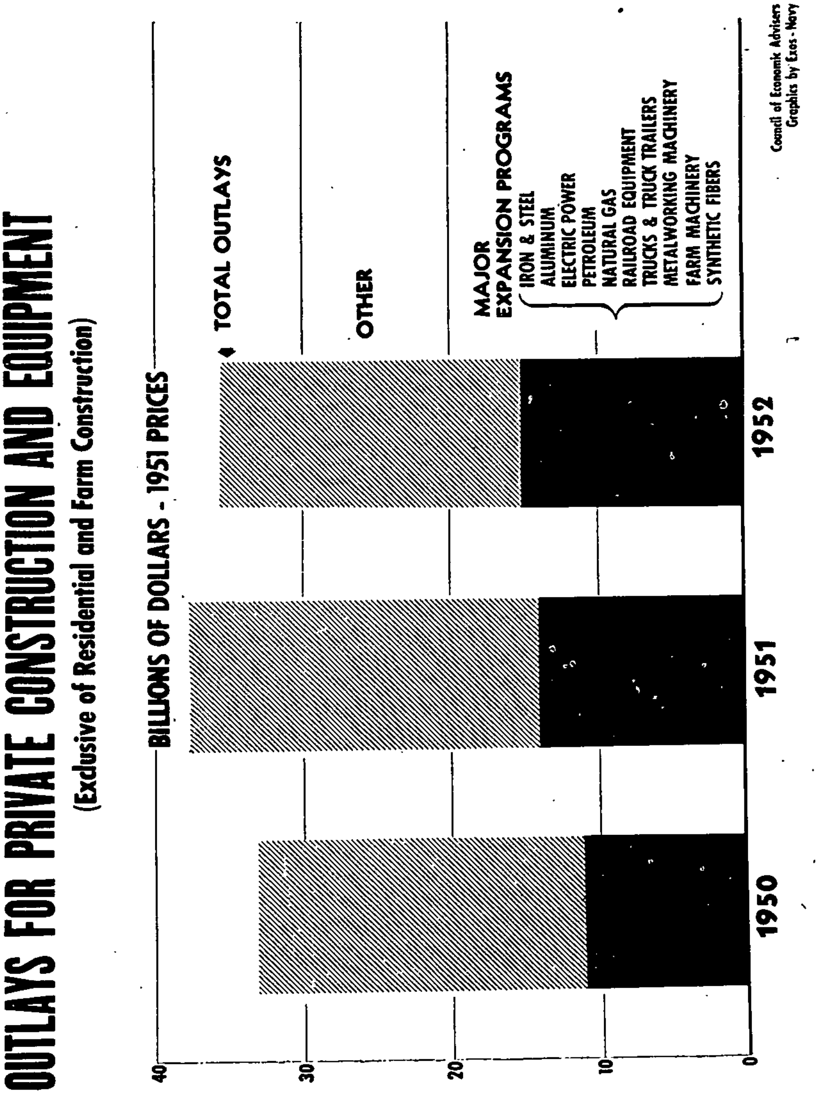
Mr. KEYSERLING. I think that this is a very good and healthy thing. I do not know that it could have been done that way in World War II.

I want to say in this connection that, while there may have been details of imperfection or even mistake in some of these stimulatory programs, such as tax amortization and the like, I personally have never shared the views of some of my good friends who have shot at the amortization program. I think that, when this whole thing is over, if it is, and we all hope it will be, when the total level of public outlays is measured against the amounts that the Government is foregoing for these stimulatory devices, it will turn out that these stimulatory devices are one of the economically most productive and most sound investments that the Government has ever made.

It can be argued that maybe $250 million less of tax amortization might have accomplished the same result, but when you set that in the framework of a $50 billion annual outlay for security and look at what is actually happening in these expansion fields, I think it has been enormously useful. This is just my personal reaction to it. I know there is a good deal of criticism of those programs.

This chart tries to show how the outlays for private construction equipment divide between what might be called the primary mobilization base and other purposes.

The total bar shows outlays for construction and equipment, exclusive of residential and farm construction.



The black bar shows the major expansions programs as listed here, iron and steel, aluminum, electric power, petroleum, natural gas, railroad equipment, trucks and truck trailers, metalworking machinery, farm machinery, and synthetic fibers.

Of course, this is private investment.

It shows that we are moving into an area now where a little less than one-half of the total of construction and equipment, aside from residential and farm construction, is going into that mobilization base. However, in a great period like the present between peace and war, this top part, with diagonal lines, is not entirely nondefense, because nobody can draw an exact line between what types of tools and equipment strengthen the security program as against what part strengthen the economy generally. Many types of tools and equipment, which would seem to be civilian supplies, nonetheless add to our strength for the long pull.

For example, other things being equal, if we have the materials to do it with, take automobiles. Well, automobiles have to be cut down now, because they are a drain upon scant resources, but nonetheless one of the factors of our strength for any kind of effort is an adequate transportation system, including automobiles running well and not burning too much gas and oil because they are not too old. So it is very hard to draw a fine line between what is defense and what is nondefense in this area. But this is an attempt to show the relative parts.

Representative PATMAN. That includes retained earnings, too, of corporations, does it not?

Mr. KEYSERLING. These are outlays.

Representative PATMAN. Oh, they are outlays?

Mr. KEYSERLING. This does not go to the question of the source, but we could give you figures on that.

Representative PATMAN. I mean that includes the outlays. You used retained earnings in order to make the expenditures.

Mr. KEYSERLING. Yes; these outlays are from retained earnings and part from borrowings.

Representative PATMAN. On page 203 of this report you have a table entitled, "Sources and Uses of Corporate Funds." Of course, that includes retained earnings, and depreciation. Together they are about $16,500,000,000. That makes a difference of only about $5 billion that was raised for plant and equipment outlays other than from retained earnings or from depreciation allowances. I think the competitive situation is bad there for the reason that the retained earnings are what might be considered costless capital, but represent three-fourths of the plant outlays of existing corporations. The additional $5 billion new capital was borrowed upon which interest was paid. That places the new capital at a disadvantage to the retained earnings, do you not agree?

Mr. KEYSERLING. Yes; it does.

Representative PATMAN. And it occurs to me that it is alarming that so much of our new plant and equipment would be from existing corporations, getting their money from increased prices, costless capital.

Mr. KEYSERLING. We have had occasion in the past, in connection with a general analysis of tax problems and whether the tax burden has borne down so heavily upon the investments as to be repressive, to discuss the issue. We have tried to analyze it partly in terms of methods of financing and what part of financing has come from retained earnings, and what part from borrowings, and we drew the conclusion in the past that while the tax level was high, and everybody hoped it could be lower if we did not have so many obligations to meet, nonetheless it could hardly be said to be generally repressive in view of the nature of the financing of corporate enterprise. This does not mean that there are not some segments of the economy which do not have adequate financing and may even be hit too hard by the incidence of taxation upon them.

Representative PATMAN. Do you not agree that under these facts that new businesses are at a great disadvantage—it is more difficult for them to get started, to compete with existing concerns?

Mr. KEYSERLING. Generally speaking, we have reached a stage in the development of the country where the established concerns, at least in our primary industries, have an advantage over the newcomer.

Representative PATMAN. On capital, specifically, you see they get their capital from increased prices. That is like Clarence Francis said one time here. He cut the phrase out in his edited testimony. He referred to it as costless capital.

How can a man across the street who borrows his money in the marketplace and pays interest on it compete with that costless capital? And according to your figures here three-fourths of the capital in new plant and equipment construction is from retained earnings.

Mr. KEYSERLING. Well, it is true—it is mathematically true there are certain advantages of that character in size. I know from my own experience in housing that when the Metropolitan Life Insurance Co. built an enormous $60 million housing project in the northern part of New York City—and I am not critical of it, I think it was a wonderful thing to do—they did have the advantage of financing with their own funds and, consequently, their rental scale could be somewhat lower, considerably lower than if they had had to borrow the money. However, I do not have a solution for that problem.

Representative PATMAN. That is not a comparable problem. I am just telling you my opinion. Possibly I am wrong about it. I do not claim to be right on everything, but part of the time.

This is for our entire economy. It is rather shocking to me that out of the expenditures for a new plant and equipment three-fourths of the money, 75 percent of the money, according to your figures here, comes from retained earnings which is costless capital of the corporations, because they got those earnings through increased prices, or prices sufficiently high to acquire them, and it places all independent concerns at a great disadvantage, or newcomers in the business, having to go into the market place and borrow their money and pay interest on it, as against a person or a corporation that has its money furnished in this costless way.

Mr. KEYSERLING. To make myself clear, I had not intended to contend that point with you.

Representative PATMAN. You went off on housing.

Mr. KEYSERLING. It may not have been good analogy, but I think there is basically a lot in what you say. In fact, some of the commentaries in our reports in earlier years, when we were addressing ourselves more to that problem, was the fact that the level of financing out of retained earnings was, probably, higher than necessary as against other types of financing, and that it was, in part, a reflection of the price problem and a lot of other problems in the economy. I am not disputing what you say.

Senator FLANDERS. I think there are questions with relation to that which are very important, but I have assumed that they would be more pertinent to the discussion which will follow than on this one, and I hope that Mr. Patman and I will both be here.

Representative PATMAN. What is that other chart? I thought that there was one about school construction that came afterward. That is the reason I asked you that.

Mr. KEYSERLING. This chart takes the personal consumption sector of the first chart, and breaks that down and gives a comparison of the as I see it here, 80 percent of the first half of the 1950 rate; electric refrigerators very much lower, passenger cars much lower, radios and television sets lower; in fact, all of them lower, ranging from 80 percent, down to about 35 percent.

The CHAIRMAN. That is what year compared with what year?

Mr. KEYSERLING. This is the index in the fourth quarter of the year just past, 1951, compared with the index in the first half of 1950 before Korea, and it shows some diminution. It still shows a high and healthy level, as I said at the beginning.

These two lines here simply show that in the first quarter 1952, steel allotments for the civilian economy for these various purposes will be a good deal less than in the fourth quarter of 1951, the conclusion being clear that there will have to be further cut-backs in these areas.

This chart amplifies that previous chart by showing different uses of steel. And this is a blow-up of one of the charts in the President's Economic Report. I will skip over that.

The CHAIRMAN. That shows the total production of steel for 1952 as compared with 1950?

Mr. KEYSERLING. Yes.

The CHAIRMAN. As being substantially greater?

Mr. KEYSERLING. Very much greater.

The CHAIRMAN. But in some instances the allocations are very much lower. For example, in the lower segment?

Mr. KEYSERLING. Consumer durables is a striking example.

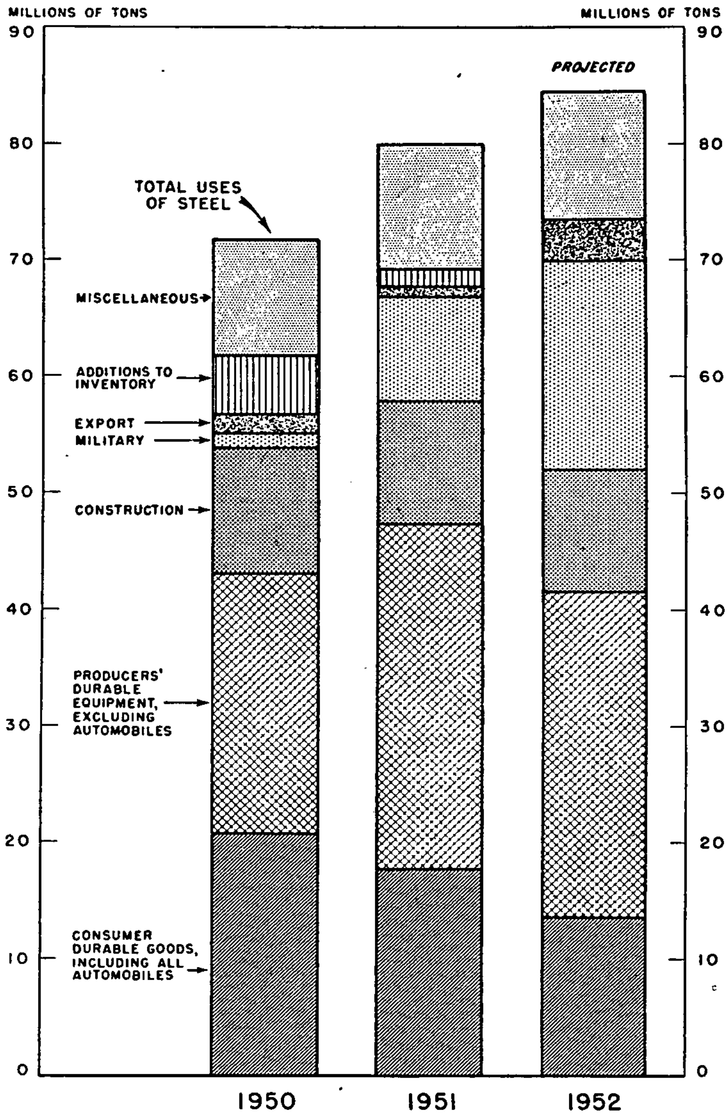
I will skip over the price charts, because, as I say, Mr. Clark is going to discuss the outlook for inflation.

They show, in main, the sharp upspurt of prices in the post-Korean period, particularly after the Chinese intervention, and a relative leveling off in the last 9 months or 8 months of 1951.

I likewise will skip over this chart, which is a blow-up of the personal savings picture which enters into the inflationary discusssion.

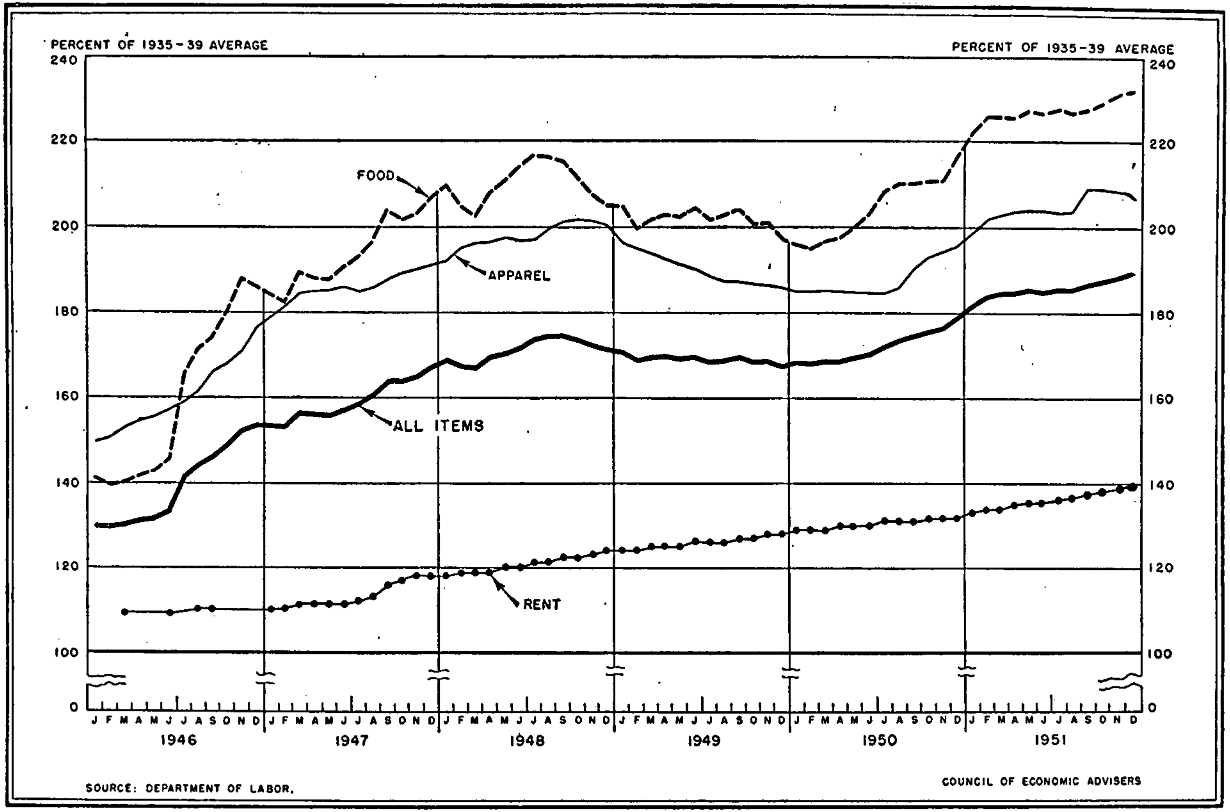
USES OF STEEL

Less steel will be available for nonmilitary use in 1952. The reduction will mainly affect automobiles, household appliances, and some types of construction.

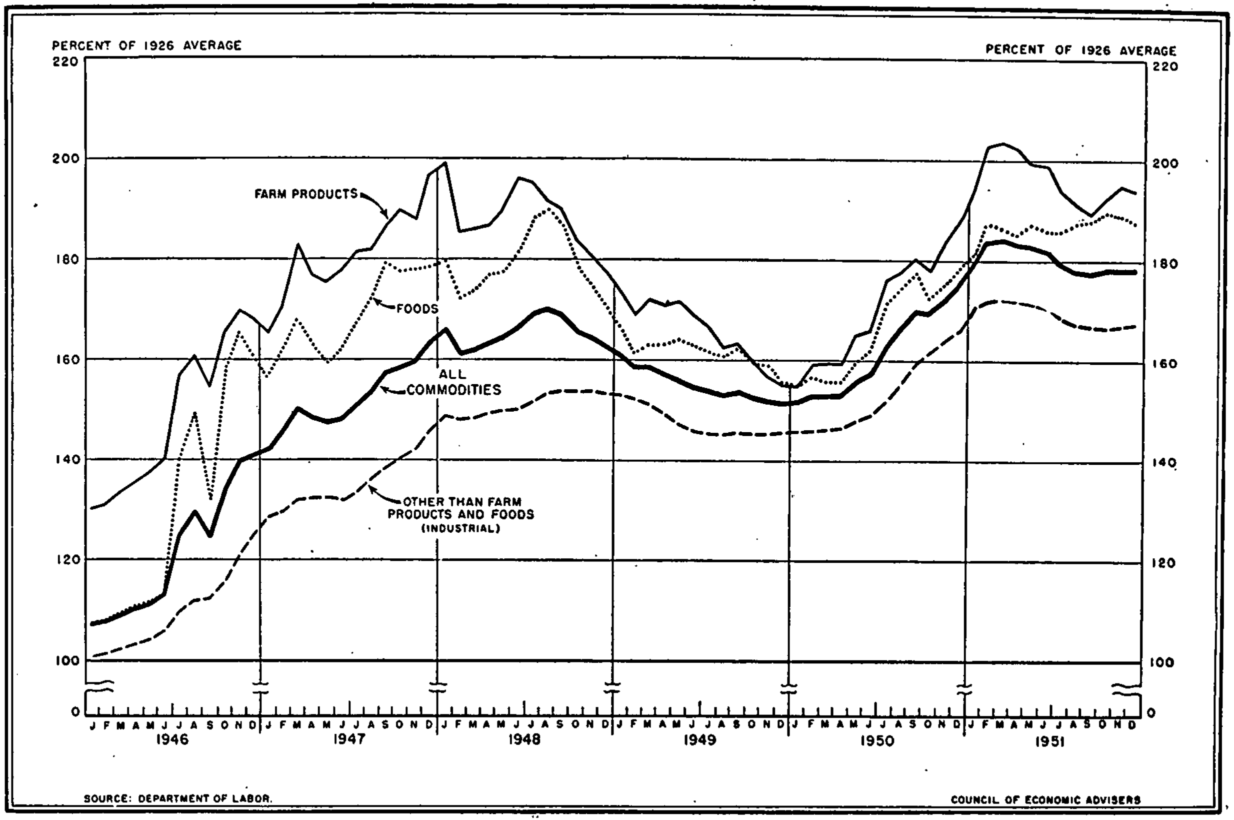


SOURCE: DEFENSE PRODUCTION ADMINISTRATION.

CONSUMERS' PRICES

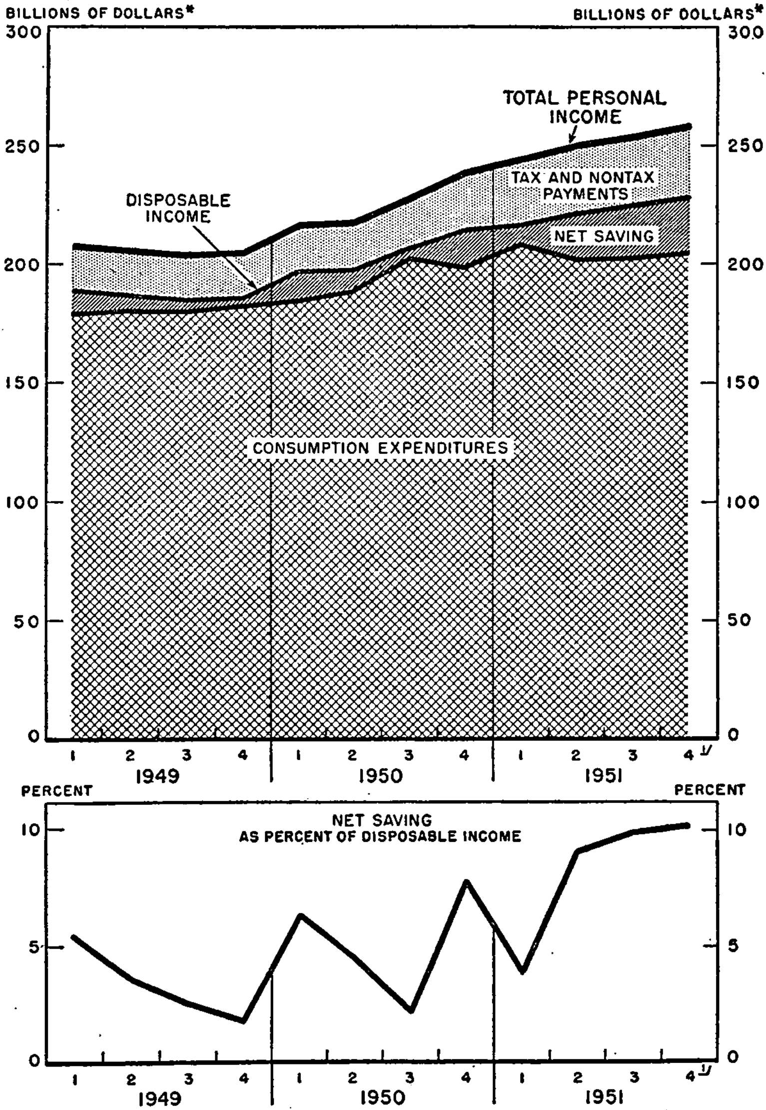


WHOLESALE PRICES



PERSONAL INCOME, SPENDING, AND SAVING

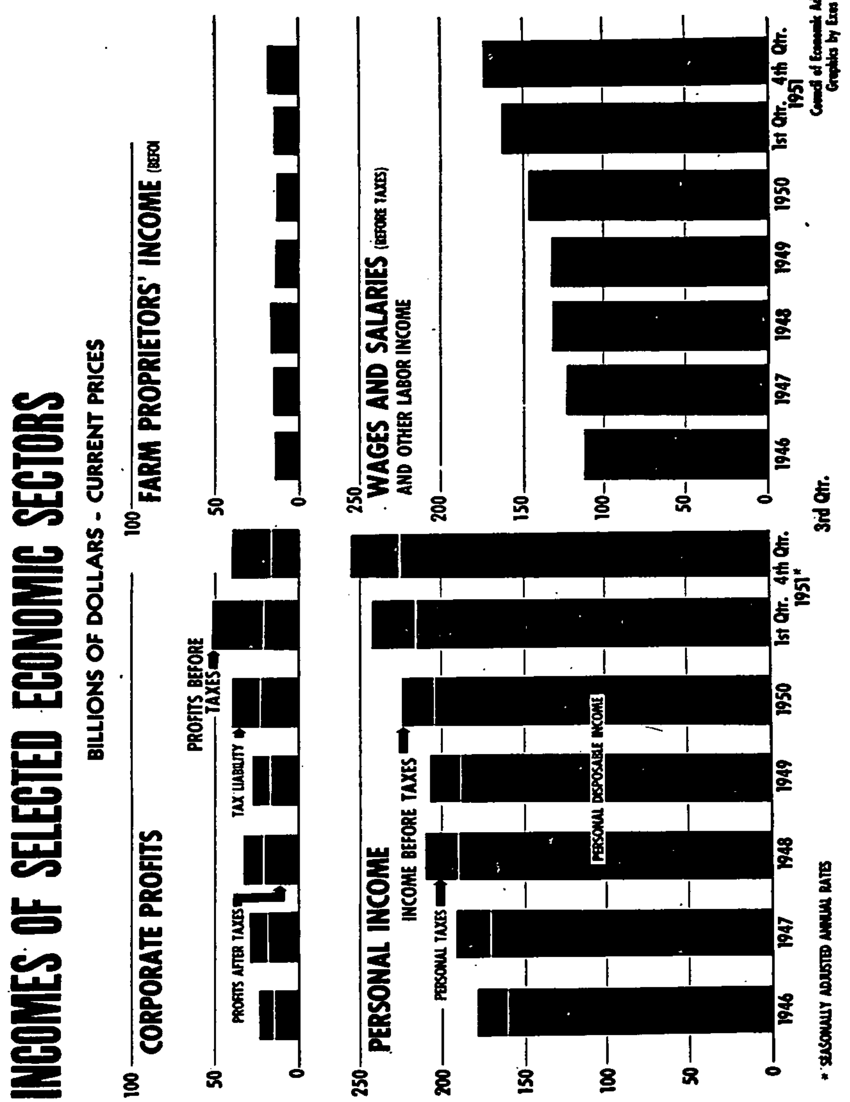
Consumption expenditures in the second half of 1951 remained below the first quarter peak despite the continued rise in income. Saving rose to 10 percent of disposable income.



*SEASONALLY ADJUSTED ANNUAL RATES.

1/ PRELIMINARY ESTIMATES BY COUNCIL OF ECONOMIC ADVISERS.

SOURCE: DEPARTMENT OF COMMERCE (EXCEPT AS NOTED).



Here is one that you may be interested in, which shows the changes in the availability of incomes during these different periods, showing it for personal disposable income, for wages and salaries, farm proprietor's income, and corporate profits, both before and after taxes.

I think there is some considerable interest in that it shows, broadly speaking, that with the economy expanding, and with employment being full, the general trend of income has been upward.

The trend of profits after taxes has been sharply downward in the latter part of 1951, mainly because of the high tax rates. And there is some significance in that.

Just a few words and then I will be through, having taken up a lot of time of the committee.

In summary, what I have tried to indicate is this: While the Council cannot appraise what the best level of security outlay, domestic and international, would be, from the viewpoint of national security, we can say that if they come anywhere within the range now proposed or talked about, then the weight of the evidence is that the economy can stand that burden, whether measured by the business picture or whether measured by the consumer picture.

If, in the judgment of those making security policy, which ultimately gets to the Congress, those security outlays are not needed in that quantity from the viewpoint of national security, then they should be reduced. Because most of them are noneconomic expenditures, they do not add to our wealth or strength.

From the general point of view of relationship to the tax picture and the inflationary picture, our general view has been that an economy of our size and strength and expansive capacity can stand the defense program as we now envisage it, with less inflationary strains than during World War II, and within the capacity of the economy to contain inflation through rounded measures less drastic than those in World War II. We think that this has been in part borne out by the experience in the latter part of 1951, although there are many reasons to believe, with savings so high and with incomes rising, that you can get serious inflationary spurts.

The CHAIRMAN. Has your presentation to the committee been based upon an assumption of increased tax revenue as recommended in the report?

Mr. KEYSERLING. These charts have not been based upon an assumption of increasing tax revenues through additional legislation, because, first of all, the projection parts of this chart have to do only with projections of assumed expansion of productive capacity.

The CHAIRMAN. I was not talking alone of the charts, but of your entire presentation.

Mr. KEYSERLING. My presentation has been based upon the current situation. It has not been based upon new tax action.

The CHAIRMAN. Then you are telling the committee that in your opinion the economy of the United States under the present revenue, under present law, is strong enough to bear the increased expenditures which have been recommended for security?

Mr. KEYSERLING. Yes, but I did not mean to intimate by that, Mr. Chairman, that the inflationary danger would be equal whether or not taxes are brought more nearly in line with expenditures.

The CHAIRMAN. Yes, I understand that.

Mr. KEYSERLING. It is not the Council's position that the inflationary danger will be increased if they are brought more nearly in line. Higher taxes would reduce inflationary pressures.

The CHAIRMAN. The reason I asked the question is that from a perfectly practical point of view the official spokesman of both the Ways and Means Committee of the House and the Finance Committee of the Senate has made it rather clear that increased taxes are not to be anticipated during this session of Congress; that we shall have to base our program upon the revenue to be derived from present tax laws. Therefore, it will be important to know what the judgment of the

Council of Economic Advisers is with respect to the soundness of the economy under such circumstances, considering the drain.

Mr. KEYSERLING. I think that should be discussed at greater length by Mr. Blough in his discussion of fiscal policy, and by Mr. Clark in his discussion of the inflationary outlook and the whole composite of measures.

In general, the position that the Council has taken, as I understand it, is revealed in the published report. We have believed it desirable, in a highly productive, high employment situation like the current situation, to pay for the program as we go by taxation. The burden of a defense program, and it is a burden, is imposed upon the economy whether you tax yourself for it or not, because it is taking things out of the economy for defense, which means noneconomic purposes.

A lot of talk by Colin Clark and others, as to what part of the economy can be devoted to taxation without paralysis, is really, at least as I have analyzed it, a discussion of what part of the resources of the economy ought to be commandeered by Government programs. Now, I am perfectly willing to go along with that in normal peacetime, a 15–20 percent figure is as high as we ought to go. But that does not seem to answer the question as to what to do about taxes if a security program, which is noneconomic and undertaken for other reasons, absorbs 20 or 25 or 50 percent of the economy. If it should be 50 percent, as it was in World War II, hardly anybody could devise any feasible way of financing it all by taxation. But the Council's position has been that, for a program of the size now contemplated, it would be better to finance it by taxation than by inflation. We recognize, however, that because of the lag in tax action last year, and the long-range outlooks, it would not be desirable now to impose enough additional taxes to achieve balance this year or next year.

Coming to the second part of your question, well, suppose the Congress is not ready to enact any new taxes. What is better under those circumstances, to cut security outlays to the level of revenues, or to run some deficit?

Part of that question I cannot answer, for the reason I have given, that the Council has never pretended to know what the security outlays ought to be. But if the security outlays as now proposed are anywhere within the range of what is desirable from the viewpoint of national security, and personally I believe they are not too high, then the position we have taken is that, if the Congress will not raise taxes, then in an economy of our size and power it would be better to labor under a Federal deficit of several billion dollars a year for a few years than to risk a cumulative deficit in the security strength requirements for facing the great forces arrayed against us.

The Council does find in the economic history of recent years that the question of the balanced position of the Federal budget is not the sole factor bearing upon inflation or noninflation. There are many other powerful factors—our record of production, the course of wages and prices and how effectively they are controlled, what is done about credit measures. Prices can be stabilized even with a Federal deficit. In fact, that happened in 1951.

The CHAIRMAN. You are, of course, aware as your statement indicates that bills have been introduced in the Congress which are designed to place a definite limit upon the amount of Federal expenditures in relation to the income, regardless of the security demand or the social demand or any other such demand, so that we are confronted with that problem.

It is, also, a fact, as the Congressman from Texas well knows, that throughout the United States there are many State legislatures that have been asking for a constitutional convention to limit, percentagewise, the rate of income taxes that can be levied upon any source.

Both of these suggestions place greatest importance upon the limitation of expenditure and relegate to secondary importance the job that the Government or the people throughout the Government have to do.

Mr. KEYSERLING. Let me try to discuss it this way, because I do not want to duck the question. I think this gets into an area where a man's economical views and his political views—using "political" in the sense of his interpretation of the world outlook—intermingle.

If a man thinks that the world outlook is as serious as many informed people think it is, and that we must play a large part in marshaling the strength of the free world and that this is in part a matter of military power, then he will incline toward the view that, while a Federal deficit is undesirable, it is more undesirable to run a deficit against Stalin in armaments. This is my own view.

On the other hand, if one thinks that the international danger has been greatly magnified and that we can afford to relax or slow down, then he will feel that the danger of that kind of relaxation is less serious than running a Federal deficit.

I do not think any economist can provide any formula which avoids getting back to fundamental appraisal of the international situation. A deficit for a few years is undesirable, but it is not going to wreck the economy. A deficit in the arms race is also bad. My personal views are well known that such a deficit is more dangerous than a deficit in the Federal budget.

I think that Stalin is a greater danger to us than inflation. If we counteract Stalin, the American economy will thrive and prosper, and the national debt has not prevented us from doing so. But if Stalin expands his sway over Western Europe, it will take more than a balanced budget to protect the United States.

I just want to make one comment in closing. While the Council cannot appraise the military aspects of what we need for our security, we can, as economists, look at conditions in some of the Western European nations. Even starting with the assumption, which I am perfectly willing to grant, that they in many respects ought to do better than they have; certainly, with respect to coal, they can do better than they have; certainly, we should not be a Santa Claus and should view what we do as against what they do; nonetheless, the fair-minded economist cannot look at the situation in France and in Italy and in England without realizing the perfectly enormous difference between their resources and their economic situation and their political situation and ours.

They set out after World War II, after enormous decimation and, in fact, after losing literally empires in the course of two World Wars, to rebuild their capital equipment. The austerity program in Great Britain, before the new rearmament program, was fundamentally a program of cutting back very sharply on their civilian standards of living in order that they might rebuild capital equipment with which to produce tools and goods that they needed, both for home use and for export at an efficient price so that they could trade with the rest of the world.

They have lifted their standard of production far above what it was before World War II. And then they get the new defense burden on top of their other problems. I think they have got to carry that burden, but it poses a problem that is really much harder than ours, much harder.

The thesis is either correct or incorrect that in the final analysis the free countries are pressed into a position where they have to stand together. And since I think it is correct I feel we have got to carry forward certain programs in addition to our own defense build-up even though this complicates our financial situation.

The CHAIRMAN. Are there any other questions? If not, we will proceed. Mr. Blough.

STATEMENT OF ROY BLOUGH, MEMBER, COUNCIL OF ECONOMIC ADVISERS, EXECUTIVE OFFICE OF THE PRESIDENT

Mr. BLOUGH. Mr. Chairman and gentlemen, I consider it a real privilege to talk with this committee on the subject of fiscal policy, because the committee has taken what I consider to be very sound positions on that subject ever since its organization. Particularly, I feel that the position it took in the summer of 1950 in urging strong tax legislation and a pay-as-we-go policy for financing the defense mobilization program was constructive, and influential in achieving that policy.

It is for this reason that I felt a little, shall I say, dispirited that the chairman takes a somewhat pessimistic view that this committee, perhaps, could not again move the sentiment of Congress in the direction of additional taxes.

The CHAIRMAN. I have been around here 18 years, Mr. Blough, and I think I have some feel for the sentiment of Congress. And it has been my judgment for a long time that progress is made by doing what you can do rather than by crusading for the impossible.

Mr. BLOUGH. I quite agree with that as a general philosophy, Mr. Chairman. And I would like to move immediately to the question you asked near the end of Mr. Keyserling's discussion, that is, whether the economy can bear this load without the additional revenue which the President asks.

It seems to me it is not so much a question of whether the economy can bear it without the additional revenue or with the additional revenue. The problem is one of how resources are to be diverted from private use to public use.

The usual method of diverting resources from private use to public use is through Government expenditure, accompanied by taxation. The taxation pays the bill on the one hand and cuts down the ability of the individuals and businesses to spend privately on the other hand.

The resources can be diverted to Government use by other methods than taxation. You can divert the resources away from individuals by such methods as allocations, aided by price controls and wage controls. And while we have not seen any necessity for consumer rationing, that of course is a method. By these direct measures it is possible to take away from individuals and businesses and turn over to the Government the resources which the Government desires to use in connection with its expenditure programs, in this case the military rearmament program.

Expenditures plus taxation is a better method from the viewpoint of a free economy. Using that method makes it less necessary to subject the markets to Government controls.

So that I would say the economy can bear this either way, but if you are not prepared to divert the resources through taxation, then you must be prepared to divert them through rigid controls, or be prepared to see the resources diverted through inflation, which of course none of us wants.

The CHAIRMAN. That, of course, I think is quite true. We are confronted with a realistic problem.

However, two governments have already fallen in Western Europe over this issue which is simplified in the phrase, "guns or butter."

The French Government fell because the people wanted more butter than guns.

And the Belgium Government fell, if I am correctly advised, for the same reason.

In Great Britain the Churchill government faces exactly the same problem. That was made clear in what was said on his visit over here. And was made clear, particularly, in the split in the Labor Party in Great Britain. It went off wholly upon the theory that military expenditures should be cut down in order that normal living could be advanced. That is, the greater proportion of the economy should be diverted to that purpose.

It is useless to deny that we have the same issue, not to the same extent, but the same issue here.

Mr. BLOUGH. I would like to point out three questions that are involved.

First, there is the question of whether the economy can do the job. And I think Mr. Keyserling has pointed out the best evidence that we have on the ability of the economy to do the job so far as production is concerned.

You have, second, the problem of diverting the necessary resources from private and civilian use to this program. And that is a different thing from being able to do the job. That is where the point you have just mentioned comes in. Will the public support the diversion of the resources to the military program?

The figures on the charts indicate the high standard of living which our people have, even with the prospective program, but I am not in a position to say that they will or will not be willing to have these resources diverted to the military program. It is that diversion which constitutes the economic burden of this program.

Then there is the third question, how do we go about doing the diverting. And that is where taxes come in.

The taxes do not set the burden. They distribute the burden, but they do not determine the burden.

The decision that determines the burden is whether you are going to have this program and are going to support it.

The CHAIRMAN. As I see it, the Communist program is all based upon a conviction that the people in a free economy and a free nation will not be willing to make the sacrifices upon the home front that are necessary to support the diversion to military preparedness required in modern warfare.

Senator FLANDERS. There is also I think the conviction that if we do make the sacrifices that it will mean the end of our particular type of economy and reduce us to political, social and economic confusion.

The CHAIRMAN. I quite agree with you.

Senator FLANDERS. It works two ways. That is their conviction.

The CHAIRMAN. Yes, I think that Russia is unquestionably carrying on an economic war against us in the full conviction that it can destroy our economy and as a result communize the world.

Senator FLANDERS. I think you have given good evidence, Dr. Keyserling, that speaking strictly from the economic standpoint, we can stand this and more, but I wonder if we are not going to fall short other than in the question of facts and figures.

Mr. KEYSERLING. I think you are right on that. We could fail through lack of will to do what we are able to do. And, therefore, I think that the main significance of the facts and figures is that they provide a basis for popular education of the ability of this country to go ahead with this, if they properly understand it.

Senator FLANDERS. Let me first say that I am less convinced of taxation as a restraint of inflation than I was a year or two ago, except from the one angle of making it unnecessary for the Government to go to the banks for financing. I think that is direct, immediate and indisputable. To the extent that you can raise it from people and business, to that extent you do not have to expand credit and it has a favorable effect. I am not so sure that taxation under present conditions has anti-inflationary effects to a strong enough degree on personal and corporate spending.

The excise tax, certainly, increases prices. You see it on the gasoline pump at the service station. If you are skeptical about that, why, just buy a little gasoline and you will see to what extent the price of that gasoline has been increased by an excise tax. And the lady who is buying a fur coat knows it. To the extent that it restrains purchases, to that extent it works, perhaps.

We have not yet been able, at least, I have not been able to see that personal taxation has restrained inflation, because the increases of taxes are the firm basis for increases in wages which, in turn, are supposed to be taken out of profits, thereby reducing the corporate taxes to Government and making the burden on the personal income still heavier, if the theory that they all can be taken out of profits is followed.

As a matter of fact, it would seem that personal taxes are acting as part of the inflationary spiral.

I would raise the question as to whether increased personal taxes can result in decreased consumption, so that you get diversion into the defense effort in that direction, can be accomplished in the absence of rationing.

So it seems to me questionable as to the anti-inflationary effects of taxation. The unquestionable effect to my mind is that it decreases the necessity for credit expansion.

Did I ask a question?

The CHAIRMAN. You made a statement, sir.

Senator FLANDERS. I made a statement, yes; but there are questions involved in the statement, I think.

Mr. BLOUGH. Might I comment on your statement?

Senator FLANDERS. Yes.

Mr. BLOUGH. Let us take, first, personal taxes. Would increases in personal taxes be anti-inflationary. It seems to me they clearly would be.

To begin with, there are a great many people whose incomes are not subject to any escalation clause and whose increase in taxes in no way would affect the incomes which they receive. Certainly, the increase in personal taxes would be effective with respect to them.

And with respect to the escalation clauses, wage escalation, personal income taxes are not included, as you know, in the formula for measuring cost-of-living increases.

Senator FLANDERS. I know that. They are not included formally, spelling it f-o-r-m-a-l-l-y? A New Englander pronounces them the same, however it is spelled.

Mr. BLOUGH. You are suggesting that perhaps it is the same however you pronounce it, too.

Senator FLANDERS. Yes; but there is a more or less accepted principle by everyone to keep the same take-home pay under present conditions. I think that is incontestable. And some who belong to the more highly organized, more powerfully organized groups of wage earners, have an advantage in that, which others do not have. So that we get another aspect of taxation which is distortion among income groups and distortion in the economy.

I did not mean to get off on that so soon, but I do not doubt you are approaching that one, too.

Mr. BLOUGH. I think that taxation prevents distortion in the economy, that it is about the only way of preventing distortion.

Senator FLANDERS. You talk to any old person with a fixed income and see what they think about the distortion of the economy.

Mr. BLOUGH. It seems to me that a person with a fixed income gets even more distortion from inflation than he does from taxes, and if there is a connection between taxes and inflation, of course——

Senator FLANDERS. The point is, what is the connection between taxes and inflation?

Mr. BLOUGH. It seems to me that the connection is incontestable, although the effects of more taxes can, certainly, vary from time to time, depending on circumstances.

We have a situation where the Government is adding tremendous amounts of expenditure to total demand. To avoid inflation private demand must be held down. How is this to be done? Our traditional method, the way we have normally used—and the only real justification or, at least, the most basic justification for the balanced budget—is to impose taxes to get private demand down. The anti-inflationary effects of taxes are the basic justification for taxes.

Senator FLANDERS. You are talking plain common sense, but the point I am raising is that plain common sense is not determinative.

Mr. BLOUGH. If you assume that everybody has the power to get all of the income he wants out of the economy, or all that he feels that he should have, why then I suppose we are completely sunk, anyway, because then it is just a matter of how fast the escalation takes place.

Maybe you can slow it down, and maybe you cannot. But I do not believe that people really have that power.

Senator FLANDERS. Is that not what is happening?

Mr. BLOUGH. Well, wages for example have not gone up as they would if labor had that much power and could apply it. They have gone up just about as much as consumer prices have gone up, on the average. Some wages have gone up more and some have gone up less. We have not had an escalation of wages to offset personal tax increases, as far as I know. At any rate, I do not see any other way to divert purchasing power from the private sector of the economy except through taxation, unless you are going to put up barriers against people spending.

You have to suppress your inflation by direct controls of one kind or another if you are going to have the spending and are not going to have the taxes.

It is quite true that people save, and if they save enough, that saving can replace the taxes, so far as the time being is concerned.

We had a period in 1950 when people saved a lot less than usual and spent a lot more than usual. And the fact that we had a budget cash surplus did not save us from a substantial inflation.

In 1951 people saved more than usual, a great deal more than they did in 1950. The fact that during the last half of 1951 we had a substantial Federal deficit, even on a cash basis, did not give us an inflation.

So certainly, you have periods when there is no close correspondence between the surplus deficit and inflation, but I think it is perfectly clear that the deficits of World War II were primarily responsible for the price rises after World War II. And that it does, as you suggest, make common sense to say that it is better to pay for expenditures through taxes than not to pay for them through taxes. If you do not pay for them through taxes, you clearly are going to have an inflationary impact.

It must be recognized that when they are paid through taxes some portions, as you mentioned, will be offset by increases in income; at some tax level, perhaps, the increases in incomes would equal the anti-inflationary effect. Personally, I do not think we have come to that point.

You mentioned excise taxes. I would point out that the increases in prices from excise taxes ought not in themselves be called part of inflation. That is really part of taxation. It may enter into the inflationary picture, because, as a result of those increases in prices resulting from the tax, there may be escalation in wages or other incomes. In that case you would have an inflationary spiral growing out of the increase in excise taxes.

Senator FLANDERS. Is there any other way of measuring inflation than on some price index?

Mr. BLOUGH. I do not know of any way of measuring it, but I would exclude from the price index in measuring inflation those price increases which are directly attributable to taxes, because in those cases the money goes, not into private hands, but into public hands.

Senator FLANDERS. It does not enter into the private income stream, but it comes out of the private income stream and raises the expenditures to the people. It seems to me that should go into the inflationary thing.

Mr. BLOUGH. If it actually raises the expenditures of the people in toto beyond what they would have been before, then to the extent that the amount which did not go into taxes is greater than the amount before, you have an inflationary pressure.

The CHAIRMAN. I should like to interrupt to ask if you meant to say that you know of no ways to measure inflation?

Mr. BLOUGH. No, I did not mean to say that. No other way except the one Senator Flanders mentioned, that is, the general increase in prices. I was trying to suggest that I would not count the increases in prices due directly to taxes, because where the money goes to the Government and not back into private hands you simply have a method of taxing. Of course, if that in turn gives rise to larger expenditures elsewhere in the economy, or expands private incomes, then you are back into your inflationary spiral.

Senator FLANDERS. Have you not an economist's index for inflation instead of a consumer's index for inflation if you do that? The consumer is concerned in inflation to him. It means what he has to pay.

Mr. BLOUGH. The consumer is concerned with both prices and taxes. And if he has to pay his tax through a higher price for the commodity or through a direct personal tax, he is taxed either way. If the price increase does not result in further spiraling, if no other private individual gets any additional income, then if the distribution of the tax load is equally acceptable in the two cases, it is six of one and half a dozen of the other which taxing method is used. The excise tax does not lead to higher incomes except through these escalation methods which you previously mentioned where private incomes are expanded and private costs are expanded. Excluding that, an excise tax does not lead to an inflationary spiral, while an ordinary increase in prices results in more income going into private hands enlarging the income stream out of which additional spending can and will take place. And you then have inflation going on up in a spiral.

Senator FLANDERS. Yes, of course; you are defining very properly inflation as the impact of incomes unsupplied.

Mr. BLOUGH. Yes. I like rather the homely expression that somebody has used—I forget who—too many dollars chasing too few goods.

Senator FLANDERS. Yes; that is it. And that is what causes inflation. Inflation itself I had interpreted more or less as I did, but I do not think we need to quarrel with that. Of course, we are not quarreling, anyway.

I had thought of inflation itself from the consumer's standpoint. The causes of it are the money supply and supply of goods and services. That makes the price rise.

Mr. BLOUGH. I think even from the consumer's point of view, we probably ought to distinguish those increases in prices which he has to pay which help to bring equality between supply and demand, and those increases in prices which he has to pay which contribute to widening or, at least, continuing the gap between supply and demand. And the taxes, even if they cause an increase in price directly, help to close the gap between supply and demand by making the goods more costly to the buyer, but do not raise anybody else's income, while when prices rise for other reasons, some private individual receives more income.

If he receives it, he is likely to spend it or invest it. And thus you get more and more spending, leading to the spiral. But the tax, unless escalation results, would not lead to the spiral.

Senator FLANDERS. I would like, for reasons which I will not detail too greatly, to pass on to this escalation basis and the personal-income tax.

It seems quite clear to me that everyone is trying to keep the same take-home pay.

Mr. BLOUGH. I have observed that the people are even trying to increase their take-home pay.

Senator FLANDERS. Yes; they are even trying to increase their take-home pay, and there seems to be nothing in our present handling of the situation which makes it evident to people they are not going to have the same take-home pay. And that is a political and social question rather than pure economics, except as economics is an investigation of human behavior.

Mr. BLOUGH. It affects economics very intimately, of course.

If I may comment briefly, it seems to me that there is nothing in the anti-inflationary program that we have set up which leads to escalation arising from the personal-income tax.

Our farm price supports and the whole mechanism of farm pricing do not include the income tax as an element in determining the prices.

Senator FLANDERS. That gets into the wage and salary entrance and has a second-degree effect on farm parity prices.

Mr. BLOUGH. Our wage and salary policy does not recognize the personal-income tax as a basis for escalation.

Senator FLANDERS. No; it does not.

Mr. BLOUGH. Our price policy does not recognize profit tax increases as a justification for price increases under price control. It is only as the forces of human nature, if you want to call them that——

Senator FLANDERS. That is it.

Mr. BLOUGH. Get outside of all of the rules——

Senator FLANDERS. That is right.

Mr. BLOUGH. That escalation of the income tax happens.

Senator FLANDERS. I am speaking from what I observe, not from any mechanism at all except the human nature that seems to be working that way. In order to be effective does not any policy directed toward reducing consumer demand have to take rationing into account, rather than working through taxation alone or price-fixing alone?

Mr. BLOUGH. The only time you have to take rationing into account is when, after taxes and savings and credit controls and other general measures are taken, there still remains a substantial excess of market demand over supply which threaten not only to empty shelves, but to leave substantial parts of the population unsupplied with those things that are of major importance. When that happens, then rationing is necessary.

There has been no need for rationing up to now in the present situation.

The CHAIRMAN. Does that mean that you feel the need for rationing is beginning to appear?

Mr. BLOUGH. No; I do not. I do not like to forecast these things, but I would not think that rationing for example, of automobiles would be useful even though the supply is cut, because there will still be enough automobiles for necessary purposes.

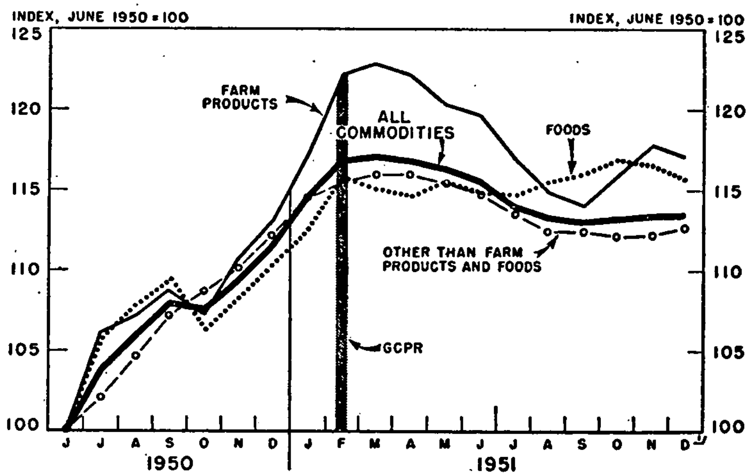
Senator FLANDERS. What page is your price diagram on? It is not a bad-looking diagram, I can say that.

Mr. BLOUGH. Charts 9, 10, and 11, pages 56, 58, and 61.

(The charts referred to follow:)

WHOLESALE PRICES

Average wholesale prices declined during the spring and summer of 1951 and at the end of the year were moderately lower than at the time of the general price freeze.

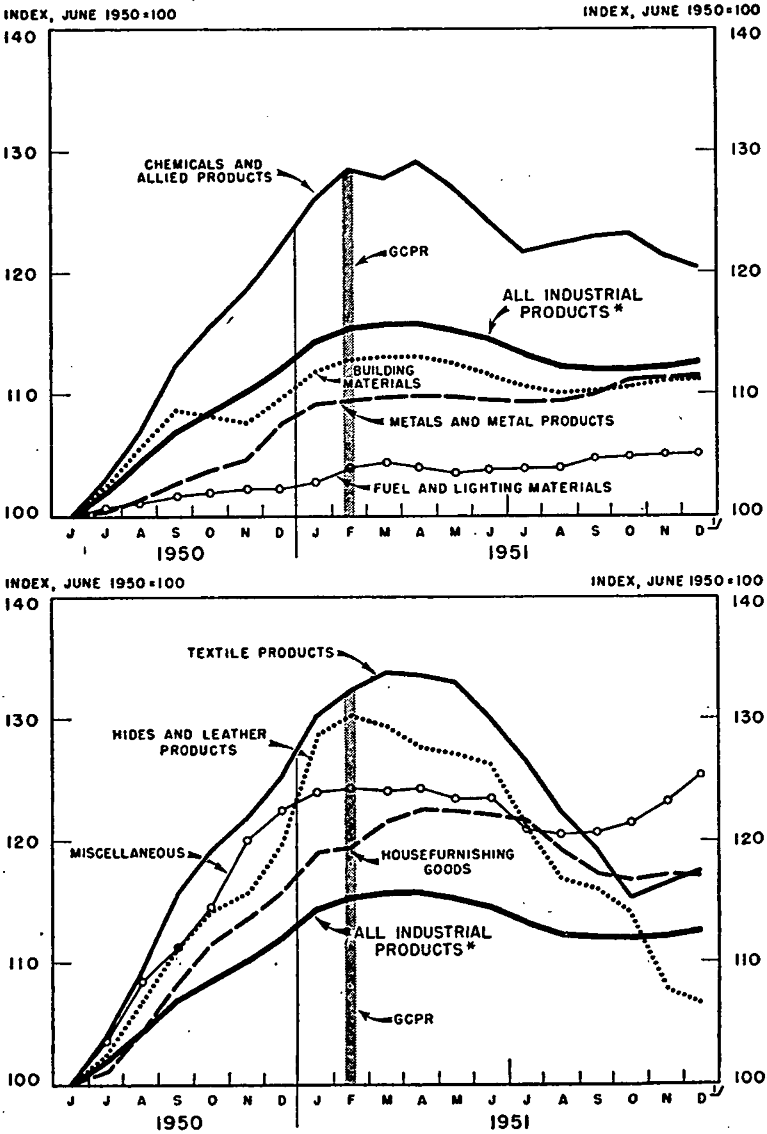


[1] PRELIMINARY ESTIMATES BY COUNCIL OF ECONOMIC ADVISERS.

SOURCE: DEPARTMENT OF LABOR (EXCEPT AS NOTED).

WHOLESALE PRICES OF INDUSTRIAL PRODUCTS

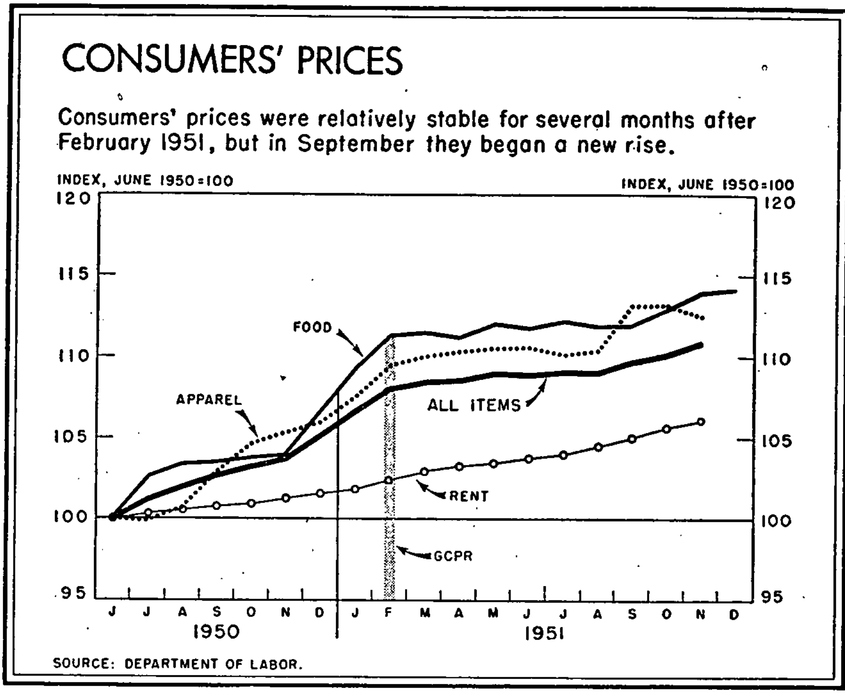
Industrial prices showed mixed trends in 1951. Metals and metal products were strong because of the impact of the growing security program. Sagging consumer demand and excessive inventories caused declines, particularly in soft goods.



* ALL COMMODITIES OTHER THAN FARM PRODUCTS AND FOODS.

1/ PRELIMINARY ESTIMATES BY COUNCIL OF ECONOMIC ADVISERS.

SOURCE: DEPARTMENT OF LABOR (EXCEPT AS NOTED).



CONSUMERS' PRICES

Consumers' prices were relatively stable for several months after February 1951, but in September they began a new rise.

SOURCE: DEPARTMENT OF LABOR.

Senator FLANDERS. That is not a bad-looking chart. That is, prices on the whole would appear to be under control.

Mr. KEYSERLING. Here is your chart, Senator.

Senator FLANDERS. Yes. We do not know to what extent those little upward tendencies and the downward tendencies are going to balance out, but it is not a bad-looking chart. I think your best argument is to ask me to look at that chart.

Mr. BLOUGH. But it is a question whether those prices are going to remain stable without any further action on the side of taxes.

The CHAIRMAN. This chart shows that prices for all commodities had been declining from the middle of 1948 until the early part of 1950, and that after June 1950 there was a very rapid increase which reached its peak in February or March of 1951, and that thereafter prices were reduced, until, perhaps, September of 1951, after which they were more or less stable.

Senator FLANDERS. Have you any comment as to the ultimate effect on the price curves—have you any indication that taxation is actually at work in reducing demand? You say it must be, judging from those curves, but have you any other indication that it is actually working?

Mr. BLOUGH. Only in my private life.

Senator FLANDERS. I am with you there. Will you shake hands with me. I just have a notion that with the great body of consumers who are not in the brackets which you and I enjoy that there has not been any desire, at least, to reduce purchasing, and I do not know there has been any effective reduction, although the increase in savings indicates something.

Mr. BLOUGH. In those commodities such as textiles, where more could have been bought, there is evidence of the effects of taxes on demand. In other areas where all was being bought that could be produced there would have been no larger purchases in real terms, without the taxes, but prices would have been higher. The fact that prices have been stable can certainly be attributed to something. It is logical to attribute a considerable part of that stability to the tax increases, which have undoubtedly cut spending below levels which it otherwise would have reached. That is true, certainly, in families with which I am acquainted. Why do people object to the taxes? Because they believe the taxes are cutting into the amounts of goods they can buy. That may be true regarding the amounts some individual could buy, but not the amounts the nation could buy, at least of many goods, because the nation will buy all there is available, with or without the taxes.

The CHAIRMAN. That is not true with respect to textiles?

Mr. BLOUGH. It is not true with respect to some of the soft goods, that is correct. What the desires of the public are with respect to those is, of course, somewhat hard to judge.

Senator FLANDERS. I want to ask one or two other groups of questions, although I think Mr. Blough may come to them. I want to ask some questions about the limits of taxation. Does that come within your category?

Mr. BLOUGH. I had not planned to raise it, but I rather expected that you might raise it.

Senator FLANDERS. Yes. Thank you. I feel complimented. The economy, as an economy, as a producing machine, can stand what we are giving.

Mr. BLOUGH. That is my feeling.

Senator FLANDERS. What it does, however, to our institutions, in my mind, is another matter. And I am thinking particularly of private investment.

I have had the feeling that the enormous taxation that Great Britain has had to undergo has almost inevitably driven it into national socialism by drying up the sources of capital.

The CHAIRMAN. Yet the testimony of Mr. Keyserling just now has been that, even in the fact of this taxation, the increased taxation of recent years, there has been a much larger and extraordinarily larger amount of private investment.

Senator FLANDERS. That is right.

The CHAIRMAN. More than before.

Senator FLANDERS. And Congressman Patman's inquiries as to that are pertinent.

I figured out something that raises questions that I cannot answer. I figured out that a man in the $50,000 bracket who wishes to invest $10,000 in a new undertaking can only gain from that investment something around six-tenths of 1 percent. And why should he?

Mr. BLOUGH. If it is invested in corporate enterprise?

Senator FLANDERS. Yes, invested in corporate enterprise. And I am assuming that it is a new undertaking, because that is part of the investment field that I think we should have the most interest in.

Maybe the new company in the course of 2 or 3 years makes 10 percent, which when I was young used to be considered as necessary before anyone would consider a risk investment.

The Government will take one-half of that, leaving 5 percent, if it is over a certain size.

The company should not pay all that out to Mr. Investor. It ought to keep at least one-half of it. 2½ percent. And then in his bracket he will only get a quarter of that. He will get $62.50 on a $10,000 investment. Why should he invest? Why should he not buy tax-free State and municipal bonds?

Why should be invest at all?

That thing troubles me. I am surprised to find that some men still do invest, but I cannot see any earthly reason for their doing it.

I think probably those considerations account in fact for the growth of the investment trusts and the insurance company investments which can draw the funds of the little investors who do not have to go through this terrific press, squeezing all of the juice out of what they invest. And it seems as though, perhaps, the investment trusts and the insurance companies are the only honorable ways out, but I do not see why my $50,000 man puts any money into anything new. Do you? He is either a fool or a patriot, or both.

Mr. Blough. If he put it in as a loan he is somewhat better off.

Senator Flanders. Yes.

Mr. Blough. The income which he gets in interest does not pay corporate tax.

Senator Flanders. That is right.

Mr. Blough. It is subject only to his personal tax.

Senator Flanders. That is right.

Mr. Blough. It is quite true that if he puts his funds in the form of an investment in stock, unless he is going to be an officer in the company and get a substantial amount of salary, or unless the investment is going to rise in value so that he can sell out——

Senator Flanders. We are trying to close up that loophole, so-called, capital gains—we are going to make it difficult for him to find that excuse for new investment.

Mr. Blough. I am just heretic enough to feel that if we would proceed with great vigor to close up the loopholes and at the same time perhaps reduce the impact of the over-all rates, we might be better off in the long run.

Senator Flanders. I am trying to find a loophole for investment in the country's future by someone else than the big companies with their riskless capital that Mr. Patman spoke about.

Representative Patman. Costless capital.

Senator Flanders. Costless capital and not riskless. As I see it, the present state of our personal and corporate income tax is going to make it a very difficult thing, to invest in the future of the country, in the expansion of production, new products, new machines, new undertakings, except by the old established corporations. And that is the point at which I begin to question the present size of our tax burden.

The Chairman. Senator Flanders, would the reduction of the tax rate on the big companies which have these retained earnings and great profits be of any benefit at all to the small investor whom you, apparently, desire to bring into the ownership picture?

Senator Flanders. The small investor has a way out. That is through investment trusts, like insurance companies, and so on.

The CHAIRMAN. Even that contributes to the strength of the big company.

Senator FLANDERS. It contributes to the strength of the big companies, but what I am disturbed about is the drying up of the old sources of risk capital. And the old sources came from people not necessarily in the million-dollar income bracket, but from the group, say, from $15,000 up to $50,000 or $75,000. That is where our new and risk investment used to come from.

My arithmetic, as I say, makes it seem to me that they must be either fools or patriots or both to continue to do that, because they get caught twice, both corporate and personal. It reduces their return to an inconsiderable figure. That is the point at which I begin to worry about our tax burden.

Representative McKINNON. Dr. Keyserling showed us this chart that indicated a high private investment ratio for 1951. I wonder what proportion of our tax-amortization program played in that high investment program. Something like $22 billion for 1951 and about $11 billion on tax-amortization certificates. That would indicate that it is dropping more rapidly than the chart seems to indicate.

Senator FLANDERS. Corporate profits were retained and reinvested so as to escape the Government take which it would have had to be paid if it had been distributed and then reinvested by stockholders. And the other large element, as I remember, would be borrowed capital, and that escapes one of the two Government takes out of profits.

Mr. BLOUGH. One escapes the corporate tax, and the other escapes the personal tax.

Senator FLANDERS. Yes.

Mr. BLOUGH. It is only fair to say that the tax system, while it does have a strongly discouraging effect on a person making an equity investment in a corporate enterprise, has, as you pointed out, a strongly encouraging effect for the retention and reinvestment of earnings on the part of a corporation. And the provisions of the penalty surtax section 102 are such that the corporation feels the necessity for getting those earnings into real assets instead of keeping them around in the form of cash or securities. So that the tax system does have a strongly stimulating effect on investment, but not necessarily the kind of investment nor the kind of business structure that we would like to have.

Senator FLANDERS. It does alter the structure to the extent of entrenching the successful corporation in their position.

The CHAIRMAN. Does not this discussion rather overlook the basic character of the problem that faces us? We increase the taxes only because the world is in such position as to require a greater outlay by this Government for defense purposes. And we are urged to increase taxes, also, in order to prevent the inflationary effects of the spending for war and preparation for war.

If we were dealing solely with a normal peace economy, then a discussion of the effect of taxes upon the investment of individuals would be pertinent and relevant, but it seems to me in the present circumstances, with the questions before us and before the Congress that are before us, the matter is just a little bit theoretical.

Senator FLANDERS. What you are doing is throwing this back to the question of the budget now.

The CHAIRMAN. That is right.

Senator FLANDERS. And these gentlemen have very properly dis-associated themselves from any responsibility for the budget.

The CHAIRMAN. But we cannot.

Mr. BLOUGH. It seems to me that the situation during the next couple of years, with the great pressure of this military program on our raw materials and other resources, is such that we are going to get all of the investment that the economy is able to support and that while taxation will have some effect possibly in the distribution of that investment or the structure of its ownership, there will be plenty of pressure for investment. The earlier comments about the attractiveness and unattractiveness of the investment have more pertinence, perhaps far later years. The Congress, if it saw fit, could then change the tax laws and restore the incentives.

Senator FLANDERS. I must confess personally to a pessimism about this being a peak load. I think we are being introduced into a new way of life. That is my pessimistic approach to this thing.

The CHAIRMAN. May I make this comment, Senator? I think that one who travels around the country nowadays will note that there has been a very substantial increase of private investment in the areas in which the investor can himself control the property and the business in which the investment is made; that the investment which is handled by investment trusts and insurance companies is channeled not to small enterprise but to these huge aggregations which dominate the economy in large-scale industrial production in which the little fellow cannot possibly engage because of the tremendous amount of capital that must be put up.

Senator FLANDERS. I am not disagreeing with that, Mr. Chairman; there might be more things to say about it. But what does one do when one's guests are assembled and the host is not there?

The CHAIRMAN. One abandons the argument and retires.

Senator FLANDERS. I will be back. As General MacArthur said, I shall return.

Representative PATMAN. I should like to bring out one point, if I may. It is on the uses of taxes to prevent inflation. I thoroughly agree with you that I think that is the best way to retard inflation; that is, through taxes.

Most of our money is based upon debt, is it not—practically all of it?

Mr. BLOUGH. Yes.

Representative PATMAN. In other words, under our system we have to go into debt to have enough money to do business on?

Mr. BLOUGH. Yes.

Representative PATMAN. If the Government collects $100 in taxes and pays that on a hundred-dollar Government bond owned by a bank, that cancels out $100, does it not?

Mr. BLOUGH. Yes.

Representative PATMAN. Or if a person who holds the bond borrowed the money to buy the bond, he canceled a hundred dollars?

Mr. BLOUGH. Yes.

Representative PATMAN. To that extent there are fewer dollars chasing fewer goods, as you brought out a while ago.

Mr. BLOUGH. Yes.

Representative PATMAN. So that to that extent it is a good cure for inflation; at least it has a greatly retarding effect on inflation through personal income taxes.

Mr. BLOUGH. It has its maximum effect when the money is used in the way you mentioned.

Representative PATMAN. If that money were paid, say, to an individual who did not owe for it, why, he would just seek another avenue of investment for it if the Government paid it to him after it had been collected in taxes, and it would not be as retarding as if it was paid on a bank loan?

Mr. BLOUGH. That is right.

Representative PATMAN. How much in bonds do the banks hold now, approximately, just in round figures?

Mr. BLOUGH. Securities of the United States Government held by all commercial banks were estimated at about $62 billion at the end of 1951.

Representative PATMAN. I am looking at it strictly from the standpoint of the Government and the consumers now. I am not thinking about the repercussions on the banks or anything else. I am just considering strictly this from the standpoint of the Government and the consumer.

Suppose the Government in collecting this money adopted the policy of just paying off this $62 billion as rapidly as possible. Would that have the greatest effect in retarding inflation, rather than paying it to people who would seek other avenues of investment?

Mr. BLOUGH. You would have to have a surplus to pay off any debt at all.

Representative PATMAN. I am talking about this. If you collect the taxes, if we collect money enough to pay the going expenses of the Government, and we have a surplus, say, of a billion dollars, to get the maximum good out of the use of that billion dollars, you would pay it on a bank-held debt?

Mr. BLOUGH. I think so.

Representative PATMAN. Where the banks had created the money on the books of the banks to buy the bonds.

Mr. BLOUGH. Or even more on a Federal Reserve bank-held debt.

Representative PATMAN. On a Federal Reserve bank-held debt?

Mr. BLOUGH. That would give you the maximum.

Representative PATMAN. Well, if you pay it on a Federal Reserve bank-held debt, how would that so greatly increase the retarding effect?

Mr. BLOUGH. Because when the check was cleared through banking channels you would have reduced bank reserves by the amount of the repayment, and that reduction of bank reserve might have and would normally have a multiplier effect.

Representative PATMAN. That is right.

Mr. BLOUGH. And force the reduction of private loans and deposits, thereby, I believe, having the maximum effect.

Next to that, paying off the loan in the hands of the commercial banks would have the most anti-inflationary effect.

Representative PATMAN. Would it not be about the same?

Mr. BLOUGH. It would be about the same if the banks have a ready opportunity for changing some of the other securities they own into reserves; yes.

Representative PATMAN. Normally they can.

Mr. BLOUGH. Under those circumstances it would be more or less the same.

Representative PATMAN. It would be exactly the same?

Mr. BLOUGH. The same; yes.

Representative PATMAN. So if we could arrange some way to pay that money that we get to payments of the debt—if and when we get some, if we paid it there—we would get the maximum benefits from it.

Mr. BLOUGH. Yes. I understand that was the policy of the Treasury during those postwar years when we did have a surplus. To the best of its ability it did use the funds to retire bank-held debt.

Representative PATMAN. I do not believe I will pursue this question any further, Mr. Chairman.

The CHAIRMAN. Mr. McKinnon?

Representative McKINNON. I have no further questions.

The CHAIRMAN. Mr. Blough, had you intended to add anything more?

Mr. BLOUGH. There are a few lines of that in which I assumed the committee would be interested; for example, why not enough taxes are proposed to achieve a fully balanced budget. There is also a point we did not get to talk about that Senator Flanders raised; that is, the importance of trying to get enough revenue during this period so that it will not be necessary to borrow from the banks and thus reverse the process which Mr. Patman was just talking about. The revenue asked for by the President would go a long way toward eliminating the necessity for bank borrowing. I had planned to go into that briefly.

Those were the major points, in addition to the tax limit question, which Senator Flanders indicated an interest in.

The CHAIRMAN. Perhaps you might give us a word or two on the first question that you mentioned, which we had overlooked, as to why the President had not recommended a fully balanced budget. You asked for it. Let us have it.

Mr. BLOUGH. I believe we can feel that under present circumstances there has not been an abandonment of the principle of a balanced budget for the defense program.

The CHAIRMAN. I am very much interested in your explanation because of your opening remark, which was addressed to the chairman, the expression of sorrow that the chairman did not seem to be advocating increased taxes at this moment.

Now we get the picture, the answer to that very question from your mouth.

Mr. BLOUGH. Under the circumstances it seems to me to be a justifiable position to ask for additional taxes, although the amounts requested are not enough to balance the budget. There are two sides of it. Why ask for any more? On the other hand, why not ask for enough to cover the expenditures in full?

Perhaps your earlier remark that one should not be completely unrealistic has a bearing on the present circumstance in view of the prospective $14½ billion of deficit for the fiscal year 1953, the delays that take place in tax legislation and in taxes going into effect, and the fact that large amounts of additional taxes have been imposed since the Korean outbreak. In approaching an increase of the magnitude required to balance the budget, we must consider not only whether the country can stand it in the long run—and I think the country could stand it in the long run—but also the impact of doing it all at once on the heels of the previous increases. We have a timing problem of how fast we can build up the tax system, considering the effects on business and on consumers and on public support. The problem is made more difficult by the fact that last year the Congress did not respond fully to the President's request for taxes and left between 4½ and 5 billion dollars unprovided for. We have lost ground. In addition to making up for the lost ground, we have this future big increase.

The problem is one of the speed at which taxes should be increased when they already are at very high levels.

In the second place, the program contemplates building up to a peak of expenditures, followed by a decline in expenditures to a maintenance level later on. It appears that there will be perhaps 2 years or so of peak expenditures which may then be expected to be followed by a lower figure. I certainly hope so from the fiscal point of view and the economic point of view.

It would hardly seem desirable, if the problem can be met in any other way, to try to follow that peak up with current taxes—in view of the delays in the passage of legislation and in view of the height of the rates and in view of the difficulties of finding sources of that much revenue—only then to be faced with reducing them. This kind of action would not seem to make much sense either from the viewpoint of fiscal procedures or from the economic point of view, assuming that the problems can be met in other ways.

I think that the prospects of being able to deal with a temporary moderate deficit without inflation are reasonably good if the controls can be kept and preferably made more effective and if the savings of the community can be held high, as they probably can in view of the shortages of producer and consumer durable goods that are likely to come—you do have a force encouraging the development of saving in the hands of the consumers.

The CHAIRMAN. Here is to me a very important fact that must be faced. It has a bearing, I think, upon taxes and upon the deficit.

There can be no doubt that a pay-as-you-go system is the desirable system, but an examination of the budget shows that the estimate for interest upon the national debt is, I think, six billion three. The estimate for veteran payments and benefits is something over four billion.

Veteran benefits and payments are governed not by each succeeding Congress deciding what should be appropriated for that purpose, but by the rates of payment fixed in the basic veterans law and the incidence of the factors for which the benefits and payments are made as they come through the years.

Also, there is to be taken into consideration the fact that this Congress will, undoubtedly, extend those benefits and payments to veterans of the Korean war. But this total of in excess of ten billion three is more than the budget estimate for the normal functions of government which I recall to be ten billion two.

That is what confronts us.

Can we, in the face of those figures, continue to increase the deficit and thereby increase the annual obligation of interest on the national debt, particularly when we see constant demand for a higher interest rate upon Government bonds?

Mr. BLOUGH. We have a basic pay-as-we-go position, which is that during the defense build-up, taken as a whole we should be on a pay-as-we-go basis. Thus far the Government has taken in about $2 billion more cash than it has paid out since the Korean outbreak, despite the fact that during the last half of 1951 there was a substantial deficit, even on a cash basis. Certainly we do not want a continuing deficit—or a net deficit in the financing of the whole defense program. If the revenue system is strengthened, as the President has recommended, and if military expenditures taper off to a substantially lower level, for a limited period moderate deficits could be handled, to be followed then by surpluses, bringing the program as a whole to a pay-as-you-go basis——

The CHAIRMAN. To be followed by surpluses?

Mr. BLOUGH. I see no reason why not.

The CHAIRMAN. Well, that would all depend upon the outcome of the world problem, would it not?

Mr. BLOUGH. I am assuming that we do not get into a large-scale war; and that the military program does come down after it has gone up in a substantial degree. On those assumptions, strengthening the tax structure by the amount asked for by the President, certainly does pave the way for surpluses after the peak load has passed.

The CHAIRMAN. The dilemma that faces us, I think, is clearly illustrated by the fact that these bills of limitation of which I have spoken earlier, introduced both in the House and in the Senate, would provide that not to exceed $71 billion should be expended during the next fiscal year. If, therefore, you take into consideration the interest on the national debt which I have mentioned and veterans' benefits and payments amounting to, approximately, ten billion, three, and then the estimate for the normal functioning of Government, which is ten billion, two, it will be necessary to deduct twenty billion, five, from the seventy-one billion, which means that the security program which the budget estimates at about sixty-five billion, would be reduced under that level to $50.5 billion.

So that the question arises, what do you want for your money? Do you want to save your taxes, keep more money in your pocket, or do you want to defend the country against the communist danger.

Mr. BLOUGH. I think you have defined the problem very well.

The CHAIRMAN. Then so far as this discussion is concerned, the question is, which is easier to bear from the practical point of view to gain the objective of defense, to do it by way of deficit or by way of taxes?

Mr. BLOUGH. Under the circumstances, I think a combination.

The CHAIRMAN. I said easier; I meant more practical, in view of the points of view with which you have to contend.

Mr. KEYSERLING. The Senator has answered the question.

Mr. BLOUGH. You know much more about the political limit than I do.

From the point of view which I was expressing, it would seem that we would get your minimum undesirable impact if taxes were high enough to avoid more than a moderate deficit for a couple of years, with at least enough taxes so that there would be practically no bank borrowing. That seems to me quite an important thing.

The CHAIRMAN. In view of the fact of the trend of the discussion, I think that I will put in the record at this point the information contained in the analysis of new obligational authority and budget expenditures which accompanied the submission of the President's budget. This shows that after deducting from the budget the total major national security programs, which called for an expenditure of $65,097,000,000, there remained $20,347,000,000 of which $14,005,000,000 are major fixed charges of one kind or another, like this veteran service, transfer of payroll taxes to the railroad retirement account, permanent appropriations, the postal deficit, public roads, public-assistance grants and other items, for which provision is made by law, the expenditure of which cannot be reduced unless Congress either repeals the law requiring those expenditures or denies the appropriation and lets the debt accumulate to be paid later on, but after deducting this $14,005,000,000 of expenditure there remained for all other expenditures of Government only $6,342,000,000.

So that the fiscal policy is an extraordinarily complex matter which is, unfortunately, not widely understood. So many people think that economies can be effected in the normal functioning of the Government, but they give no consideration to the fact that that represents only a very small percentage of the total outlay.

(The tabulation entitled "Analysis of New Obligational Authority and Budget Expenditures" is as follows:)

Analysis of new obligational authority and budget expenditures for fiscal years 1952 and 1953

[In millions]

	New obligational authority		Expenditures	
	1952	1953	1952	1953
Budget totals:				
Table 1, 1953 Budget			$70,881	$85,444
Table 2, 1953 Budget	$93,431	$84,260		
Deduct:				
Major national security programs:				
Military services	61,655	52,359	39,753	51,163
International security	9,397	8,238	7,196	10,845
Development of atomic energy	1,357	1,255	1,725	1,775
Defense production and economic stabilization	702	1,145	678	811
Civil defense	75	600	44	339
Promotion of the merchant marine	105	73	288	164
Total, major national security programs	73,291	63,670	49,684	65,097
Remainder	20,140	20,590	21,197	20,347
Deduct:				
Major fixed and continuing charges:				
Veterans' services and benefits [1]	4,364	4,006	5,166	4,022
Interest	5,955	6,255	5,955	6,255
Transfer of payroll taxes to railroad retirement account	773	723	773	723
Permanent appropriations	284	305	133	133
Postal deficit [1]	814	669	814	669
Reconstruction Finance Corporation	100		−50	−51
Federal National Mortgage Association			543	65
Commodity Credit Corporation	454	131	206	253
Public assistance grants [1]	1,150	1,140	1,180	1,140
Public roads	557	430	457	464
International Wheat Agreement	77	182	77	182
Payment of claims and reserve for contingencies	41	125	92	150
Total, major fixed and continuing charges	14,569	13,966	15,346	14,005
Equals: Budget totals, excluding major national security, fixed, and continuing charges	5,571	6,624	5,851	6,342
Existing legislation	(5,571)	(5,746)	(5,851)	(5,697)
Proposed legislation		(878)		(645)

[1] Excludes proposed legislation.

The preceding table deducts from the totals of new obligational authority and expenditures for the fiscal years 1952 and 1953 first the amounts for major national security programs and secondly the amounts for the major fixed and continuing charges.

The national security category includes all of the items classified functionally in the 1953 budget as "military services" and "international security and foreign relations," plus atomic energy and some programs initiated or expanded during the present emergency.

The second category "major fixed and continuing charges" includes items not subject to annual budgetary control, such as permanent appropriations, public assistance grants, interest on the public debt, and payment of claims against the Government. It also includes programs sometimes referred to as "open-end." They are programs the requirements for which are largely governed by the exercise by individuals of privileges granted by basic law but still influenced to varying degrees by administrative action. For example, the size of veterans' programs depends largely on the number of veterans availing themselves of hospitalization, readjustment benefits, pensions, insurance, etc. On the other hand, the mortgage purchase program of the Federal National Mortgage Association is influenced by restrictions on credit and home building.

The tabulation does not purport to make a segregation of defense and nondefense expenditures. The residual total at the foot of the table includes amounts for some programs which have been initiated or expanded during the present emergency. Examples are defense housing, aid for schools in defense areas, projects for expansion of electric power generation required by the defense effort, and the port security program of the Coast Guard..

The CHAIRMAN. You have not answered my question as to the choice between taxes and deficit. I wanted your point of view, and Mr. Keyserling said that I had answered it myself.

Mr. KEYSERLING. I thought I had answered it, too.

Mr. BLOUGH. I think the point of view that I was trying to express, which I think is the point of view of the Council, is that we would like to see this paid to the largest extent possible currently through taxes; that under the circumstances covering expenses completely by taxes each year does not seem to be a feasible thing to do because of the speed of increases and the magnitude of increases that would be necessary, and the fact that the increases would be followed by decreases as we come down from the peak of expenditure; that we think the tax program which was asked for last year, or the amounts asked for, at any rate ought to be provided, and we believe would largely save the Government from the necessitv of borrowing additional sums from the banks; and that this program would have the highly desirable result of strengthening the tax system to the point that it could carry the longer load with a balanced budget, and possibly with a surplus.

So we feel that it is highly desirable to have some increases in taxes at this time, but that, for the reasons mentioned, it is not either necessary or desirable to try to cover the whole increase in expenditures that is scheduled to take place, if the President's budget becomes effective.

Is that not roughly our position?

Mr. KEYSERLING. Yes, plus the fact that, if taxes are inadequate, it is better to run a Federal deficit than seriously to weaken the defense program. The economy, if necessary, can carry both the defense program and some deficit, and still be strong and get stronger.

The CHAIRMAN. Are there any other questions?

Representative MCKINNON. Your feeling is that you would look at it from a series of years, rather than any individual year in balancing the income and outgo?

Mr. BLOUGH. If it were feasible to do it in each year, that would normally be the best way to do it, but when you have the prospect of a very big increase followed by, we hope, substantial decreases shortly thereafter——

Representative MCKINNON. You draw your line through there?

Mr. BLOUGH. There are reasons to try to look at the whole picture together. So long as the tax yield is large enough and your other methods of controlling the situation are strong enough that you do not get substantial inflationary pressures out of it during these years of moderate deficit—that, I would say, is the combination of principles which it seems to me it would be wise to follow.

The CHAIRMAN. The committee will recess now until 2:30 o'clock, and at that time Dr. Clark will discuss the long-range problem as indicated by Mr. Keyserling, and other stabilization policies, in the light of the growth of the inflationary pressures.

The meeting will be in this room at 2:30 o'clock.

(Whereupon, at 1:30 p. m., the committee recessed, to reconvene at 2:30 p. m., the same day.)

AFTERNOON SESSION

The CHAIRMAN. The committee will come to order, please.

Dr. Clark, when we adjourned at noon, you were the only member of the committee who hadn't spoken. It is now your turn, Dr. Clark.

STATEMENT OF JOHN D. CLARK, MEMBER OF THE COUNCIL OF ECONOMIC ADVISERS, EXECUTIVE OFFICE OF THE PRESIDENT

Mr. CLARK. Mr. Chairman, I want to take up a particular subject at the outset because I am sure it will be of considerable interest to the committee, although it requires that I set aside for a time the consideration of the inflationary prospect and the consideration of the several recommendations of the President with respect to national economic policy in the coming year.

The specific point of national trouble which was in mind when the Employment Act of 1946 was passed was the problem of depression and of economic policies which would prevent depression, if possible, or depression having come, would modify its effects and cause an earlier return to more active business conditions. Unemployment stood out as the one great danger resulting from depression, to which society could not be blind and about which Congress must have concern. The name of the act itself indicates the dominant position of the question of maintaining employment. In the first section of the act the national policy for which it is devised is described as one for the use of the resources and programs of the Government to maintain maximum production, employment, and purchasing power.

When the act became effective through the appointment of the Council of Economic Advisers and the appointment of this joint committee, the situation had already developed as one not of threats to employment, but one of inflationary danger, which threatened the stability of the economy. By common consent, both the joint committee and the Council of Economic Advisers and the President, in his economic reports, acted upon the assumption that their duty under the statute, although it was specifically directed to problems of maintaining maximum employment and production, included a responsibility for proposing national economic policies to preserve a stable economy against the threat coming to it in a period of inflation. That has been the economic situation from that time.

In 1949 there was a brief interlude in which a large part of the business world feared that we were entering a period of serious recession, which would cause us to turn our attention to the specific functions that are set out in the act. That period passed very quickly and was succeeded by rapid growth in economic activity, which I would characterize more as one of entering a real boom period rather than, as Senator Flanders characterized it this morning, as one in which we had just about pulled out of a recession.

June 1950 we had attained a level of industrial production, a level of employment high enough to cause a good many business analysts to forecast a down-turn later in that year, a view in which the Council did not concur, but which was held by a great many people. We were in a real boom by the middle of 1950.

At this time there are a great many people——

Senator BENTON. Do you attribute that to the outbreak of the Korean war?

Mr. CLARK. We were in a boom by the time the Korean war broke out.

Senator BENTON. Even before?

Senator FLANDERS. The Korean war didn't make the boom. That is the point.

Senator BENTON. Most people think the Korean war did make the boom.

Mr. CLARK. There are now many people who wisely worry—if they are the worrying type, it is wise for them to worry about it—about the situation we will be running into when the mobilization effort has passed its peak. We can describe the peak, I think, as one involving expenditures for the security programs, as they were defined this morning, at an annual rate of $65 billion. The expenditures might be somewhat higher by the second half of 1953. It all depends upon the judgment of the Congress and of the executive officers of the Government as to the speed with which a program of build-up, particularly for the Air Force, should move forward.

But the $65 billion rate, I am now assuming, will be just about the peak of expenditures on the security programs and will continue—we will attain it, according to the present schedule, by the end of this year.

The CHAIRMAN. Calendar year?

Mr. CLARK. Calendar year.

We will maintain it through 1953, calendar year, through the first half of 1954. When it begins to—not level off, but to move downward, is a speculative matter, but certainly not before the middle of 1954.

The CHAIRMAN. Isn't that wishful thinking?

Mr. CLARK. That it can begin to move down?

The CHAIRMAN. That it will begin to move down then. We have no evidence, it seems to me, that the policy of the Kremlin will be altered in any respect by 1953 or 1954, and every evidence to the contrary, that the Russians are pursuing a deliberate policy of provoking as much economic distress for the United States as possible.

Mr. CLARK. Senator, the program has one element that is not taken into account. It includes very heavy expenditures to prepare a production base which, having been prepared, does not have to be expanded further, and that expenditure will drop out.

Senator BENTON. Stockpiling plants and things of that kind.

Mr. CLARK. By the middle of 1954 we will have a productive machine for military purposes under way which will be able to turn out goods so much faster than we can possibly use them for military purposes in the absence of a real shooting war, that I do not think there will be anyone proposing that we expand them still further.

The threat from Russia will require the continuance of a high level of military expenditure on a preparedness basis, maintenance basis. I think that is the term we use in the report. That period may come, if not the middle of 1954, say, at the end of 1954. But it is 2 or 3 years off.

The CHAIRMAN. The point you are making is that the mass-production machine for turning out implements of war will have been completed at least by 1954 and thereafter, in the absence of a war, the demand for military spending will be for the product from this machine.

Mr. CLARK. That is right, and for much less product than the machine is able to produce.

The CHAIRMAN. Unless we get into war.

Mr. CLARK. Because that is the plan.

Senator BENTON. Even on the second point, Charlie Wilson testified before the Banking and Currency Committee that there will be a decline because you will have inventories that will make a drop in both categories—on the capital side and on the material side.

Mr. CLARK. The combination of those factors will mean a substantial drop in the expenditures on the security program.

Senator FLANDERS. There is an element of judgment, is there not, in the number of years in which this build-up should be distributed? If there is such an element, it is based on judgment as to when and whether the Soviet Government will make a military, a large-scale military attack. It seems to me that our problems of adjustment are going to be more difficult the more our preparation is contracted and less difficult the more it is spread out. That, however, is not a question of economics, except as to results one way or the other. It affects the economic situation, but the judgment is primarily political and military.

Mr. CLARK. And it is those effects that I want to discuss.

Senator FLANDERS. Yes.

Mr. CLARK. If the peak of expenditure reached at the end of this year runs through calendar 1953 and most of calendar 1954, and is $65 billion, and we find one stage of our work completed and we drop back to a maintenance basis, if it is $20 billion less, that still leaves $45 billion a year that we are spending on the military machine and on the related security programs. If total expenditures shall have risen to $95 billion—by another $10 billion, which would be $75 billion for the security program—and then defense outlay drops back to $45 billion, the drop is $30 billion. I do not think we need spend time figuring just which of those is the most likely because the problem is created by either. It is created by a drop of $20 billion in Government spending or in a more aggravated form, of course, by a drop of $30 billion.

The fear that is expressed today is that that kind of a drop in Government expenditures, which means a discontinuance of much of the Government demand for goods and for labor, will precipitate a serious depression. Not only are people in the United States worrying about it, but people abroad are worrying about it because they know that a depression in the United States would have an immediate effect on the attitude of the United States with respect to foreign aid of all kinds.

During the recess I read a brief item, telegraphic report, of the views expressed in the current issue of the London Economist on that very point. They have the fear that in 1954 this country will be entering upon a serious depression as the result of the dropping-off of the security program.

Senator FLANDERS. Mr. Clark, would you mind making some comparison between what may presumably happen at the end of our peak defense program and what happened at the end of our war effort? There is something to be learned in a comparison of that sort, I am sure.

Mr. CLARK. I couldn't avoid that, Senator, because that is about the only thing that you can get your teeth into for the purposes of coming out with some kind of an assurance about what we will experience.

Senator BENTON. Your point is right. Europe is terribly worried about this. I heard Ray Willis says a few months ago, "When America coughs, Europe thinks it has pneumonia." That puts its very graphically. That is an important problem for Europe, that problem that Dr. Clark is discussing.

Mr. CLARK. Several groups have spoken to us in our meetings with them about their feeling that the Council of Economic Advisers should be giving attention now to the economic programs that will be necessary to protect us from serious depression when this change occurs. We also have been somewhat belabored by individuals outside the groups because we have not come forward with our views about the program which will then save the country, or save its prosperity. I suspect that most of these individuals have been eager to have us express views so they then could have a whipping boy for their editorial comments.

In the annual review, in the final pages, we do comment briefly upon this coming problem. Mr. Chairman, I would like to put that out on the table as we see it and discuss the things that then might be done to meet the problem in the size that we now view it.

That brings me to the point, Senator Flanders, which you commented upon: What can we learn from our experience after World War II?

They have been good enough to put on the board the chart Mr. Keyserling used this morning, which showed what took place between 1944, which is the middle bar standing by itself, and what took place in the postwar years, the black portion of each bar representing Government purchases of goods and services. In the upper panel you get it expressed in dollar figures on a common basis of the 1951 price level.

Comparing the large black area in 1944 with the corresponding area in the next bar, which is 1947, you will see the great drop in dollar amount on a common price basis in expenditures, Government expenditures, between the two periods.

In the lower panel, the percentage of the total national product devoted to several major purposes is given and again the black bar indicates the percentage of the national product going into Government purchases of goods and services in 1944, and in each of the succeeding years, beginning with 1947.

But I would like to ask you to turn to a table which gives figures that are not difficult to grasp. It is on page 169 of the annual report. There is a table of gross national product, divided into the major categories, on a common price basis. They use 1951 prices for the purpose of bringing all these figures into harmony.

On the preceding page there is the same kind of table, using 1939 prices as the common base. But I will use the 1951 one.

In the first column, the gross national product in 1945 is shown at $330 billion. That is on the basis of 1951 prices.

In the fourth column from the end of the line, under Government purchases of goods and services, the total Federal, State, and local, as given, is $159.5 billion. Federal expenditures for national security purposes given is 144.2.

Moving down 3 years to 1947, you find the gross national product was 271.5 billion and Federal expenditures for national security purposes was 14.5 billion, a drop from the enormous expenditures of 1944 of $130 billion.

Compare that with the prospective drop that I have already speculated about, that perhaps in 1955 expenditures for national security programs will drop from an annual rate of $65 billion to an annual rate of $45 billion, a drop of $20 billion.

Obviously, we are not going to meet a problem anything like as serious as that which we had to meet and which we successfully overcame after the Second World War.

Senator BENTON. Did we produce more in 1932 than we did in 1929?

Mr. CLARK. One hundred and eighteen billion in 1932, and what was the other? In 1929, 167.

Senator BENTON. I read the chart as 117.

The CHAIRMAN. Referring to your point as illustrated on page 169, is it not emphasized by glancing at the total of personal consumption expenditures for 1944 as compared with 1947, the same 2 years in which you pointed out there was a drop of 130 billion in national security expenditures, in those years the total personal consumption expenditures jumped from 155.3 to 188.6. There was a jump in gross private domestic investment from 13.3 in 1944 to 40.2 in 1947, indicating that, while there was a heavy curtailment of Government expenditures for war, after the shooting stopped, private expenditures gained and Government expenditures for normal purposes also gained, thereby having the sum total of Government normal expenditures and private expenditures raising the level of money flow into the economy which brought about the result you are talking about.

Mr. CLARK. A high level, but still a level far below 1944.

The CHAIRMAN. Oh, yes.

Mr. CLARK. In other words, we did not make up the whole gap. We didn't come anywhere near making up the whole gap. We were $50 billion short of making up the full gap and yet we had a booming economy.

The CHAIRMAN. The prediction of which you speak was made when the shooting stopped. It was currently stated in the press that it would be necessary to keep men in the Army in order to prevent a terrific unemployment problem.

Senator FLANDERS. I want to pull the CED out from under that prediction.

The CHAIRMAN. CED didn't make it.

The men were discharged, the Army was demobilized. Many of us now think it was demobilized too fast in Europe and that the iron curtain would not have advanced as fast and as far as it did advance had we kept our troops there. But they were discharged, and the recovering normal economy took up the slack and we did not have the unemployment that had been predicted, nor the depression.

Senator FLANDERS. Dr. Clark, have you thought as to the comparative effect of unsatisfied demands and savings which go together to maintain the private economy, after World War II, as compared with what might be expected after the recession in our defense expenditures?

Mr. CLARK. Yes, we have a view of that, Senator, that probably is not quite the ordinary view, but we think it is very important. We think that too much emphasis has always been placed upon what we call the backlog of demand. It now would be an error, we feel, to assume that there is a pregnant difference between the conditions after World War II and the conditions that will follow the mobilization peak, the present peak, from the standpoint that then there was a very large backlog of demand for many kinds of goods which had been unavailable during the war.

Senator FLANDERS. You have allocations to reckon with.

Mr. CLARK. There were no new houses or automobiles during that period. There was a shortage in ordinary consumer goods as compared to normal demand. All of that, we are supposed to look on, as having furnished the foundation from which a rapidly expanding new economy would be growing and that was why we had such good luck in avoiding the disaster of a desperate depression.

Senator BENTON. Do you question that thesis?

Mr. CLARK. We do. We know there were backlogs, yes. We know that people were eager to buy all of these things, but if you look at the amount of buying of those very things which took place in 1946 and 1947 and, if you want to think of this backlog as still having an influence 3 years after the end of the war, in 1948, if you look at how much of all of these goods were produced and did go to the consumers in those 3 years, you will find that the volume wasn't anything like enough to account for the booming economy that took place. It was the whole range of goods and services which expanded.

Senator BENTON. But lots of those goods—particularly the selling and promotion of those goods—didn't come into it until the fall of 1947.

Mr. CLARK. That is the point I am making, Senator.

Senator BENTON. So it went all over into 1948 and 1949.

Mr. CLARK. As I say, I don't know how far you want to extend this theory of backlog. I think by 1948 the backlog idea ought to be shelved.

Senator BENTON. I can give you evidence of the other.

Senator FLANDERS. Then there was a reluctant backlog that was developed by advertising.

Senator BENTON. The queue-line backlog was exhausted. That is the important distinction. In the fall of 1947 they reemployed their sales organizations and began to bring out the undeveloped backlog.

Mr. CLARK. The theory of a backlog being responsible for our good fortune in avoiding a depression after 1945 is that the demands of consumers for the goods they had not been able to get and which they were quite able to buy brought about an enormous expansion of employment in the production of those goods

Senator FLANDERS. I traded in a new automobile the first chance I had.

Mr. CLARK. Of course you did.

Senator BENTON. In fact, we had to use pull to get one.

Mr. CLARK. As Senator Benton said, it was not until the end of 1947 that production of those things began to hit a high peak. There wasn't that big employment in automobile manufacturing or in housing in the latter part of 1945 or 1946 or the first part of 1947.

Senator BENTON. That is right.

Representative MCKINNON. They were tooling up.

Mr. CLARK. Yet we had a booming economy during that period. Where did it come from?

Senator BENTON. A lot was anticipation.

Mr. CLARK. It came from the expansion of the entire process of production. Goods and services in every line were being produced.

Senator FLANDERS. What element did savings made during the war play in that?

Mr. CLARK. It furnished an opportunity for abundant buying power to consumers, which, added to current income, which was beginning to increase, furnished the active demand for goods as fast as goods would be produced.

Representative MCKINNON. What were the accumulated personal savings in 1946 and 1947?

Mr. CLARK. We don't run a table like that.

Senator BENTON. It was over a hundred billion dollars.

The CHAIRMAN. I take it you have defined "backlog" as meaning a demand by persons with purchasing power for things that they would have ordinarily purchased had they been manufactured.

Mr. CLARK. Yes, sir.

The CHAIRMAN. In other words, a stable purchasing power for goods they were accustomed to buy. What actually happened was that by reason of the increased purchasing power of people who had never purchased such things in the past, there was a bigger demand by far than the backlog for production.

Mr. CLARK. Yes.

Senator BENTON. I think that puts it very well. I think the backlog played a bigger part in businessmen's enthusiasm to go out and develop that second kind of purchasing power than is generally realized. It was the bait in front that put a lot of the steam into the activities of our business economy.

Mr. CLARK. Senator, you are right. That anticipates what I would have said later. One of the reasons we had such good fortune after the war was because the business world had been persuaded that they should not make their plans for the postwar period upon the basis of a sure depression, of a sure drop in employment.

Senator BENTON. That is no doubt correct.

Mr. CLARK. And a loss in consumer's markets. They were conditioned to that more optimistic view of the prospects.

Senator BENTON. And they knew the backlog was there—those two things.

Mr. CLARK. By the fine work that the CED did, they were conditioned to a more optimistic view of the prospects. I have often said this, so I am not saying it merely because you are here.

Senator FLANDERS. Senator Benton and I are both listening.

Mr. CLARK. Also there was similar work done by the United States Chamber of Commerce during that period, which I ran into. It was necessary to sell the American businessman, then, upon the idea that he didn't have to get a storm shelter ready to dive into as soon as the enormous prosperity and activities of the war had been cut off by peace. He was being told by the "croakers" everywhere that he must get himself in shape to cut down, and he had to be persuaded that what he should do was not plan to cut down, but plan for a bigger market than the country had ever before furnished the American businessman.

The CHAIRMAN. To put it in another way, I take it it would be appropriate to say that a modern businessman does not have to depend upon what, in our youth, they used to call the carriage trade. It is on the trade of the masses of the people that modern business depends.

Mr. CLARK. That is what they did rely upon and they made it quite clear that their rosy expectations of future business opportunities arose out of their analysis of the ordinary American family and its future demand backed by its future buying power. That is very definitely not the carriage trade.

Senator BENTON. These people you call the croakers, came out of Washington—very famous ones. They showed us charts beautifully drawn, like this, that there would be 15 million unemployed within 6 months after the end of the war—15 million—that had to be offset.

Mr. CLARK. You had quite a refractory field to work in when you tried to persuade American businessmen to have the courage to make ready for expansion. Compare that with the present situation. There is no such feeling today among American businessmen. They have worries a little bit about just what will happen shortly after a cutback, after Government expenditures are cut, but they are showing, in every possible way, their confidence that the progress of American business is bound to be upward. In the last few weeks there have been some amazing announcements of financing arranged by some of our largest American corporations for enlargement plans, enlargement of a productive plant that is already very large, to take place well beyond the period of this emergency boom. They are showing their faith in the progress of America from normal expansion of a people whose wants are the final determination of the size of the business world.

And our approach to this whole program, gentlemen, is based upon that principle, that we should discard absolutely the idea that any problem is going to arise when this mobilization peak is passed, which will require that the Government step in to fill a gap in buying or in the demand for goods and services.

On the contrary, we assert the principle that we must reply upon the general economy, that the general economy can be relied upon, because a growing population of Americans, with increasing incomes, will assuredly furnish a demand which will enable business to move forward upon a progressing base and will avoid any recession of business levels.

There will be problems, however, that will have to be met in order to attain that progress. I think that one of the most serious problems that we will face then is the problem of competition. American business will have the markets available. The people will have the resources to enter the markets and to buy goods in a volume sufficient to maintain maximum employment. But the prices will have to represent the influence of real competition. If business endeavors to maintain prices at the level that we will have when this shift in conditions arises, they will kill their own fine opportunity.

The CHAIRMAN. That is actually in the future, isn't it?

Mr. CLARK. No; we are talking about a period 2 or 3 years from now.

Senator BENTON. He is talking about 1954.

The CHAIRMAN. That is very encouraging. Do you think within 2 or 3 years the peak will have passed, the peak of military spending?

Mr. CLARK. Oh, yes; 3 years.

The CHAIRMAN. And that is on the basis that the machinery for military production having been fully created by that time, military spending then would be only for the product of the machine?

Mr. CLARK. Yes, sir; that is right.

The CHAIRMAN. And that assumes again that we do not go into an all-out war?

Mr. CLARK. Oh, yes. None of this would apply, of course, in case of a shooting war.

The CHAIRMAN. And, then, of course, there is also the other danger which is implied by some of the reports we get from abroad, the message that Mr. Churchill brought to us, asking that there should be at least a token force at Suez to maintain the Suez Canal for the world rather than for the British and the French, and the message we get from France that the French economy can no longer maintain the fighting at Indochina, that perhaps the tin in Malaya may need protection from the Red Chinese, and the United States may have to engage in military spending for those purposes. All that is not taken into consideration.

Mr. CLARK. We don't take that into account. We base this discussion upon the budget that the President has presented and take the size of expenditures for the security program out of that budget.

The CHAIRMAN. Of course, there are many Members of Congress who think in terms of the length of the period during which military expenditures will be necessary and what the annual amount of those expenditures will have to be. Then, of course, there is its impact upon the normal economy and the capacity of the economy to sustain that. The President's economic report and your supporting view gives the answer that these expenditures can be sustained because we have a general economy which has expanded far beyond anything we had before.

Mr. CLARK. That was what Mr. Keyserling was covering this morning. He was covering the ability of the economy to sustain these expenditures during this period of high mobilization expenditures. I am moving beyond that to the period where the expenditures are off $20 billion a year.

The CHAIRMAN. Off $20 billion. Expenditures for fiscal 1953 are estimated at 85.4.

Mr. CLARK. Sixty-five of that is for security.

The CHAIRMAN. Sixty-five is for national security. Your discussion is based upon the thought that that 65 will be reduced to perhaps 45 and then we will run along at 45 as long as this condition exists.

Mr. CLARK. That is right. That is what I am assuming.

Senator BENTON. That is Charlie Wilson's testimony. That is what he says the program is.

Senator FLANDERS. That was brought to my mind by what Senator O'Mahoney said earlier—what substantiating information have you to indicate that our present effort is primarily directed toward the means of production rather than the stockpiling.

The CHAIRMAN. That was the testimony before the Appropriations Committee last year consistently. That is the program that has been outlined by Wilson and carried out by Lovett in the Department of Defense.

Senator FLANDERS. I just wanted to feel some confidence that that is the way it is going.

Mr. CLARK. I think you have Mr. Wilson before you later this week.

The CHAIRMAN. Yes.

Senator FLANDERS. We can discuss that question with him.

The CHAIRMAN. Last year various branches of the Department of Defense made requests of the Department of Defense in preparation of the budget for a total of something like $104 billion. It was cut down to something over 60 before it was presented. This budget has been cut down below not only what the various elements in the Department of Defense wanted, but what the Department of Defense itself asked of the Bureau of the Budget and the President. This is substantially lower than that.

Mr. KEYSERLING. May I make just one comment, Senator, tieing in what Dr. Clark said with one point that was raised, to show the connection between the two periods?

There are two basic arguments advanced from the economic point of view, as distinguished from what Senator Flanders calls the political point of view, about the size of the security program. The first is that the economy hasn't the strength to stand the strain, and still get a high enough level of industrial strength and civilian strength. We tried to cover that this morning.

The other argument, which is sometimes heard, is this: If the military program gets too big, although the economy can stand that strain, the size of the decline in defense outlays later on would strike the economy a staggering blow. This argument is sometimes addressed to the size of the now proposed program, as a basis for reducing it substantially. It is to this argument that Dr. Clark's remarks were addressed.

Senator FLANDERS. With my pessimism as to whether there is a peak or not, I still feel that we should be at this moment digging in for the long pull on some basis which, if necessary, we can continue for many years. That expresses my point of view at the present time, which may be subject to correction after I have listened to more testimony.

The CHAIRMAN. The question you will want answered on the basis of the testimony and views we have received today is whether or not a $45 billion expenditure for national security can be maintained under our economy and with a pay-as-you-go tax program.

Senator FLANDERS. Yes; that is the general idea.

Senator BENTON. And is it big enough.

Senator FLANDERS. Is it big enough or is it too big.

Mr. BLOUGH. It is not my understanding that anybody in the administration is saying that the size of the Armed Forces or its preparation for action will go up to a peak and then decline, but that in setting a certain standard for our Armed Forces, it will cost a lot more in the build-up stage than it will in the later stage, so that this reduction and leveling off doesn't mean that the reduction of the forces themselves will take place, but only of the annual cost in maintaining them.

The CHAIRMAN. Dr. Clark, a year ago Wilson's program was based upon the assumption that 20 percent of the national output could be safely devoted to national security without any difficulty at all. That would be sufficient to build the mass production military machine. Is that still the view?

Mr. CLARK. I don't think that is just the way it was phrased, Senator. I think it was said that a burden up to 20 percent was not so serious that we should shy away from the security programs because it involved that much. It was not set as the limit to which you could go.

The CHAIRMAN. No; it wasn't set as the limit, but that was the plan.

Mr. CLARK. Yes.

The CHAIRMAN. Are you talking in terms of the 20 percent military security program for a period of years?

Mr. CLARK. Sixty-five billion would be 20 percent of the present gross national product.

Forty-five would be that much less.

The CHAIRMAN. If it could be dropped off to 45, it would considerably lessen the goal.

Senator BENTON. Fifteen percent.

What has happened to the year we lost here? Mr. Wilson last year before the Banking and Currency Committee said this point would be the middle of 1953 or the fall of 1953. Now you are testifying today, after we have spent a year, that we are right where we were. It is still as far off as we were a year ago. It is now the middle of 1954. A year has gone by and we are exactly where we were before on the treadmill.

Mr. CLARK. I have heard several explanations, but I am going to leave that to Mr. Lawton tomorrow and to Mr. Wilson, when you have him here on the following day.

I believe he will have something to say about the enlargement of the Air Force program. That is the principal factor involved, that they are absorbing that enlargement not by accelerating the immediate expenditures, but by spreading it over a longer period—the total program over a longer period.

There are some specific places in this future which I am discussing where we can see that there will be compensating expenditures that will take up some of the gap left by the decrease in the military expenditures. I think by this time that all skepticism about the estimate the Council of Economic Advisers made in the past years about the demand for housing must be pretty well dissipated. Today no one can doubt but that the annual demand for new houses in this country is way above the 800,000 which we are proposing for this year and which is arousing a storm of protest. That is the largest single source of additional demand for labor and materials which we will have come into the market once we are prepared to meet those requirements.

The CHAIRMAN. The storm of protest, I take it, is because it is too low.

Mr. CLARK. Yes. Everybody talks of 800,000——

Senator BENTON. Who is protesting?

Mr. CLARK. As being a terribly inadequate figure.

Senator BENTON. The building industry?

Mr. CLARK. Oh, yes—and communities.

Senator FLANDERS. Have you figured out on some basis what would be a normal demand for new housing? It would be a function of obsolescence, deterioration, population size growth and all the rest of it. Have you ever tried to figure out from that what would be a normal demand?

Mr. CLARK. I should refer that to Mr. Keyserling, except he is embarrassed——

Senator FLANDERS. He doesn't look so.

Mr. CLARK. He made an extravagant estimate about 7 or 8 years ago of the need for housing which now turns out to be so low that I don't know whether he will want to offer it.

Mr. KEYSERLING. I think housing, Senator Flanders, is a good indication of the question you asked before, as to what the real sources of demand are. For that purpose, the middle of 1950, before Korea, is an even better example than 1947 because, while you might argue that we were still traveling along on backlog in 1947, it is a little harder to argue that we were still traveling along on backlog in 1950. It is our feeling in the Council that, while, of course, the backlog argument has considerable merit, to a large degree demand is really a function not of backlog nor of savings but of standard of living as a function of current production and current income. Consequently, our estimates of housing demand, and automobile demand for that matter, in most of the years between 1947 and 1950 were higher than the estimates of the industries, because the industry's computations were made mostly upon two things—backlog demand and prewar norms. Our estimates placed more stress upon the current productive power of the economy, the reasonably good distribution of income, and demand as a reflection of the people's standards of living at that level of production and income.

In 1947, when we first projected our housing estimates—and they envisaged 1 million to a million and a half new nonfarm units per year for a decade—a tremendous dissent went up. Strangely enough, it went up from the building industry, which said that this would satiate the market, and that any figure over a million was out of this world.

Now, after having built as high as a million and a quarter houses in 1 year, when housing was cut back to 850,000, which was higher than the highest level ever made before World War II, they regarded that as phenomenally low.

That is the best illustration of the thesis Mr. Clark is advancing, that it is largely a matter of production, assuming you have the proper price adjustments and the incomes which permit and entice buyers to take the goods off the market.

Senator BENTON. Is your estimate now one million and a quarter?

Mr. KEYSERLING. I would say a million and a half farm and non-farm units for 10 years, assuming a high-level economy—a million and a half units for 10 years would cover population growth and would liquidate, over a 10-year period, about half of the truly obsolescent housing. That would be the outlook if not for the defense emergency.

Senator BENTON. What is that in money?

Mr. KEYSERLING. If you took an average cost of $7,000, that would be a million and a half times 7,000, an annual investment of 10½ billion for the housing alone, and more for facilities, and so forth.

Representative McKINNON. Seven thousand is way low, isn't it, as a figure?

Mr. KEYSERLING. Yes; it is a little low.

The CHAIRMAN. Getting back to your statement, Mr. Clark, are we to assume that on these factors that you have outlined, inflationary pressures might be expected to recede somewhat?

Mr. CLARK. I was giving my attention to the question of whether it would be able to maintain a high degree of employment and, of course, as was said, high production would have to go with it. I wasn't looking to that period for the opposite dangers.

The CHAIRMAN. I didn't mean to bring up anything about the period following the occurrence, but whether or not, in your judgment, having passed the peak of 65 billion, or whatever it may be, for military expenditures and having dropped back to a base of 45 annually, the effect would not be to reduce inflationary pressures during that time.

Mr. CLARK. Oh, yes. We expect that with the leveling off or the dropping off of the securities programs, the inflationary pressures will be reduced enough to make it possible to eliminate a good many controls.

The CHAIRMAN. That would mean, then, that the allocation of materials so as to prevent the construction of more than the given number of automobiles or more than the given number of houses and such products, the other controls might be dropped.

Mr. CLARK. Yes. We think that you could certainly have a free market in building materials which would enable more than a million and a quarter houses to be built without any Government orders needed to authorize it. We think the automobile production would be able to step up again.

The shortages in copper will be the more disturbing problem for that long a period. The steel situation ought to be remedied by the end of 1954 certainly and perhaps much earlier. The aluminum situation will be very much improved by 1954. Copper is the one that they worry most about.

Let me mention a couple of other needs which we will be wanting to fill as soon as the opportunity arises. These are on the Government side. Our highway system is deteriorating rapidly. We are not nearly keeping even with it. With its decline, we ought to be expanding instead of which we are dropping further back. This committee has already made one special report on prospective highway construction requirements which had some amazingly high figures on what that would be. Here is a place where one kind of Government expenditure would step in to make up some of the gap caused by a decline in another.

Equally important and praiseworthy would be our attention to public school buildings. There is certainly going to be continued pressure for school construction throughout this entire period. The pressure will be so great that the control authorities will often have to yield a point at times in order to meet some of the requirements. As soon as the pressure is off so we can resort to that kind of construction, it will be under way. Hospitals are also going to present somewhat the same kind of problem.

Mr. Chairman, I want to return briefly to the other aspect of the subject I was to discuss, and I think it can be a very brief discussion.

Senator FLANDERS. If you are not interrupted.

Mr. CLARK. If there are points that cause interruption, I will be very glad to have them come up, because I feel just a little despondent over the fact that we are not able to interest the reading public by coming up with new gadgets every time we write a report. We have to come up with pretty much the same act.

Senator FLANDERS. You have to defend your old ones.

Mr. CLARK. The same old ones.

The CHAIRMAN. You are still having toast and eggs for breakfast.

Mr. CLARK. The same diet continually. We haven't been able to invent any new ideas of how to endeavor to stabilize the economic situation during this period of very heavy Government expenditures. We have nothing now that we didn't propose immediately after the Korean outbreak and repeated at the beginning of the following year and then for the third time set out 6 months ago, and here we are up for the fourth edition.

The anti-inflationary measures available in a democratic society are thoroughly standardized. We do not feel that there is any call upon us to be inventing new ones. The old ones are, in our opinion, well buttressed by experience, and we come forward with them once more.

This morning you discussed taxation as one of the principal elements in an anti-inflationary program. We have direct control of prices and wages. They are far more successful than is generally credited. I am very anxious to give you a little information on that which shows how wrong is the popular impression of just exactly what was done by price control.

Price control was imposed on January 26, 1951. The wholesale price index of a great range of goods other than food and farm products stood at 164.2 on November 28, 1950. That was almost the moment that the Chinese attacked us and threw us into our second wave of agitated buying by consumers.

On December 26, it had risen 3.6, to 167.8 on the index.

On January 30, it had risen to 171.7, a rise of 3.9 points.

Those are very rapid price rises.

On February 27, 1 month after the price freeze, that index stood at 172, three-tenths of 1 point increase since the price freeze.

Senator BENTON. What date?

Mr. CLARK. February 27, 1951.

Nothing else had happened. February was not a month of large drain of funds from consumers and from business to pay taxes. That began a few days later. There were no other economic circumstances to stop the increase in price rises. There was no decline in buying. The index of retail sales in February was at just about the same very high level as in January, which was above December. Consumer buying was still putting all of the pressure on the market. No offsetting pressure had developed except price control.

If you want to take the total index, which includes prices of farm products and foods, which are very volatile, you get a similar change, atlhough it did have some slight increase in February. Let me give them to you.

Senator FLANDERS. Which index is it?

Mr. CLARK. You have it in the indicators. I am talking about total index on all commodities, manufactured goods as well as farm products.

The first figure I gave you did not include the farm and food products.

Senator FLANDERS. Are these wholesale or retail?

Mr. CLARK. These are wholesale.

On November 28 the total index was 172.6. On December 26 it was 177, a very very wide jump. On January 30 it was 182.1. That was another big jump. On February 27 it was 183.4, an increase of 1.3 points.

Compared with the preceding increase, the effect of the price freeze was very impressive even on farm and food products, some of which could not be reached at all by price control.

If you take the so-called sensitive commodities, the index of prices of basic raw commodities, of which there are three—one by Dun & Bradstreet, one by the New York Times, and one by BLS—and I don't remember which one I looked at—the one I looked at reached its peak 2 weeks after the price freeze and then began to go off.

I think that we have to give price control far more credit than is usually attributed to it for the stabilization of prices which took place in February and March 1951.

Then the consumer became the——

Senator BENTON. Do these include rents?

Mr. CLARK. These are wholesale prices. Shall I give you the consumer-price index?

Senator BENTON. I have the charts.

Mr. CLARK. That index is by months, so I cannot get a very close comparison with the impact of the price freeze on a certain date. The consumers' price index went up very rapidly until February and then flattened until later in the year, when it began to move up a little bit. Through most of the year it was the consumer who was the key factor in the situation. His quiet buying mood, which resulted in an amazing situation, showed that unit sales, as distinguished from dollar sales, during the middle months of 1951, were not as large as they were in the period before Korea. The consumer held the key to the economic situation then during most of the year.

While his income was rising, he chose not to buy. In many lines of goods nearly every line except the hard goods, the durables, there was unused productive capacity which would have been at work turning out goods if consumer demand had been large enough, but consumers, having funds, chose not to buy. The textile industries suffered quite a slump during the year for that reason.

That is a phenomenon that the economist despairs of explaining. Why were the consumers not buying in line with their increase in income? The result was a saving at a rate which, you will remember, your staff advised you 6 months ago shouldn't be looked upon as something that you could anticipate would continue; that it was quite abnormal and we should not make any economic plans on any assumption that that high rate—10 percent of personal income—going into savings could continue. It has continued. It has been running in the most recent period at the rate of more than $22 billion a year. Perhaps you will remember that at your round table a year ago Donald Woodward, of the Mutual Life Insurance Co., gave you a prospective lay-out of the various factors in the economy and forecast that at the end of 1951 personal savings would be running at the rate of $26 billion a year, and everybody in the outfit hooted the idea that it could happen. He was very near right.

That situation is still continuing. There has been no expansion of consumer buying. January has been a very quiet month. So long as that continues, we are apt to be deceived into believing that we do not require these controls. The inflationary pressure is not active. Therefore we may think that it is permissible to drop some of the controls and look to the economy to move along without the annoyance of that kind of Government action.

There couldn't be a greater mistake made, gentlemen, than to act upon that assumption today. All you have to do to realize the danger in it is to look back to the situation in December 1950. We did not move then to impose price control promptly. We had to wait. The experts said we had to wait until they were prepared to make it effective. In the 2 months between the outbreak of the Chinese attack and the time the price controls finally were imposed, the whole price situation became thoroughly distorted. Many prices rose very rapidly. Others couldn't go as fast. The whole price level, of course, advanced in line with the figures I have just given to you. When we finally did impose price control, we had to deal with a situation that had almost gotten out of hand.

If we drop controls today, we are putting ourselves in a position where, if the consumer attitude changes, if consumers, having increasing income, as they are bound to have as Government expenditures expand, decide that they are going to begin to buy goods rather than hold funds, you are going to have an immediate impact of vigorous inflationary pressure upon the markets that will cause those prices to spurt forward, and you will come along weeks later trying to catch up with that. Perhaps once again we will be under the delusion that we can get some roll-backs when we do get under way, although I do not know how anybody now thinks a roll-back is possible. The only safety in a situation where we know that many of the most important consumer durable goods are going to be restricted in output is to maintain the series of controls which we now have. If the markets are permitting prices to drop away from under them, be happy about it, but do not use that as an excuse for discontinuing the system and leaving us helpless if there should be another sudden resumption of what you call just normal buying by our consumers.

Senator BENTON. Don't we need a psychologist on our Council to explain to us what might cause the consumers to do this, because, if we knew better what might cause it——

Mr. KEYSERLING. One thing that causes it is, when prices start to move upward—you may say, How do prices start to move upward first? If you drop the controls, you get some random upward rise of prices and that, with the controls off, will start the buying. What started it after Korea? There wasn't any great expansion of Government buying. The defense program hadn't started to grow. It was the interaction of expectancy of rising prices and the fear of scarcity.

Senator BENTON. Fear of scarcity.

Senator FLANDERS. You would be concerned, would you not, with the effectiveness of our present controls in the face of our present psychology of the American people as a whole—of whom, let us say, you and I are units—you would be concerned with the effectiveness in the same way that we are concerned in retrospect with the effectiveness of the eighteenth amendment. It seems to me that there is—I am not looking for trouble, but just suggesting some things—it seems to me that we are in a condition which is quite different from the time when we were engaged in World War II, all out. At that time we were looking forward to a conflict which would have an end in victory. In this case we see no end. We do not have that stimulus of everybody buckling down, working together, to accomplish a definite end. There is no end in sight. I am just wondering whether, when our price control is put to the test, we may not find it more difficult to operate successfully than we did in the midst of World War II. I think it is worth while doing a little worrying about that if worry is ever advisable, because we do not have a clear-cut crisis.

The CHAIRMAN. And we do not have the realization of a clear-cut crisis.

Senator FLANDERS. It isn't a clear-cut crisis. It is a chronic disease instead of a bout of pneumonia.

The CHAIRMAN. Chronic tuberculosis is a very deadly thing to become afflicted with.

Senator FLANDERS. You are right.

Senator BENTON. There will be a very heavy drive this year to further weaken the legislation we now have for controls, and it is going to be one of the major issues before us as we go through the year.

The CHAIRMAN. The President's report says specifically that this is no time to weaken controls. We have had a peculiar experience during the year of having OPS order increased prices on some commodities and roll-backs on others.

Senator FLANDERS. Related to that, I was rather intrigued by the CED proposal which I think has a little broader application. They propose having a waiting period in the Capehart scheme, a waiting period in the Capehart amendment, a waiting period likewise with respect to wage acceleration, so that the inflationary effect is not immediate and is proportional.

Senator BENTON. I don't understand that. A waiting period?

Senator FLANDERS. A waiting period on wages. The consumer index rises so many points, which requires a wage rise. Wait 3 months before it is granted. On the Capehart amendment, the costs have increased to a certain point. Wait 3 months, or whatever the period is, before the price rise is granted.

The CHAIRMAN. The members of the staff are hunting around here trying to find the expressed reference to this in our report of a year ago. It appeared on page 9 of the report.

Senator FLANDERS. May I look at it?

The CHAIRMAN. Yes, indeed.

A minimum waiting period of 3 or 6 months might be established before automatic adjustments are allowed to take place, such as that between increases in the cost of living and wage rates, thereby bringing some stability and less frequency of change into the price-wage-cost picture.

Senator FLANDERS. Did I sign that report?

The CHAIRMAN. You did.

Senator BENTON. Ralph, when we were in the CED, we used to teach the Government. Now it is the other way around.

Senator FLANDERS. That is right.

Senator BENTON. It is reversed.

The CHAIRMAN. Well, Dr. Clark, do you care to add any more observations?

Mr. CLARK. No.

The CHAIRMAN. Perhaps some questions ought to be addressed to you and your two colleagues.

The President's Economic Report discusses, in general, the effect on the economy of defense expenditures and of military and economic aid on foreign nations. The recommendation is for expanding the productive capacity in the United States, a support of civilian strength, inflation control, increased taxes, encouragement of savings, and the maintenance of price control, rent control, and wage stabilization. Those will be the general subjects which will form the basis for legislative recommendations to be made.

I think I remarked this morning that there is evidence that military expenditures in Western Europe and inflation are going hand in hand there. There was a great breadth of opinion in the Congress last year that economic aid to Western Europe should be sacrified in favor of military aid. The President's budget this year gives estimates for about $600 million more this year for assistance than was appropriated last year. But it does not break down that recommendation into military and economic aid.

As I recall it, last year the economic aid was reduced to about a billion and a half or somewhere in that neighborhood. The rest was military aid.

Have the members of the Council expressed any views about the inflationary aspects of this military expenditure in Europe? Have you reviewed the value of the economic aid?

I don't find it in the review.

Mr. KEYSERLING. There is discussion of that at various places, Senator.

I believe the position the Council takes is this: The distinction between military and economic aid at any given level of total aid is hard to draw and may be fallacious because, for the same reasons that in our own economy the strength of the Nation depends upon the three sides of the triangle, particularly the industrial and military sides, it is even more acutely true in countries like France, Italy, and England. Whether they get steel to expand their facilities so they can produce guns, or whether they get steel to make guns, or whether they get guns, it adds to their strength. The form of aid should be based on considerations of efficiency of expenditure.

Senator BENTON. You would not call economic aid inflationary in the same sense as the military aid is to them, would you?

Mr. KEYSERLING. To them or to us?

Senator BENTON. To them.

The CHAIRMAN. To them.

Senator BENTON. What the people in Europe think is more responsible for their inflation is our domestic program of procurement which has driven up the prices of so many things they have to buy to maintain their own economies.

The CHAIRMAN. International commodities had been driven up in price by our defense programs and our stimulation of theirs.

Senator BENTON. That is what has hit them very hard and contrasted with that our military program within Europe hasn't yet come in with any major inflationary force. The military program hasn't yet hit them to a comparable extent.

Mr. KEYSERLING. There were two discussions of it in the council's review and in the President's Economic Report. There is the stark fact that their effort to build up their military-defense programs is having a very large inflationary effect upon their economy.

Senator BENTON. Yes, it is.

Mr. KEYSERLING. The reasons for that are clear.

Senator BENTON. Pyramided on top of our procurement program.

Mr. KEYSERLING. I mentioned some of that this morning. Take England as an example. The austerity program under Cripps was a sacrifice of consumption to build up productive equipment. They were putting about 25 percent of their total national product into capital formation. Even at the height of our capital formation boom, we were much below that. They were sacrificing standards of living for a while, to gain the productive strength to lift standards of living later and to have the productive strength also to make goods for export in exchange for the materials they have to import.

When they had begun to see clear on that, in the middle of 1950, as reflected by the drop in our own export surplus and in their improved dollar balance and trade position, superimposed upon that came the new defense program, which tends to push them under again.

So there is a tremendous problem in those countries, both in respect to economic and political problems, larger than ours, to be frank about it, as to how they will carry this military program.

When you come to the second side of the argument, which has been made, our own defense program is straining their economy in two ways:

First, because there is a certain relationship established between their program and ours—if ours is bigger—theirs must be bigger.

Secondly, our defense program is straining them because it is demanding or taking into the ambit of the United States economy, along with our high level of civilian production, an amount of raw materials which is having a great effect upon international prices. That, in turn, is having an effect upon their ability to obtain raw materials.

Senator BENTON. There is no question about that. That is an economic fact, not just a contention.

Mr. KEYSERLING. That is true.

This raises the next question as to how we meet this problem. One way would be to reduce our own security program, reduce the size of our program. The difficulty we find with this is, if you start with the assumption that the danger is real and you set an optimum minimum level of what is needed over all for security, then it seems dangerous to reduce our own security program because others cannot carry quite so much as had been intended.

A better approach would be, at least in part, not to reduce our own security program, but to reduce within various other areas of the economy the enormous drain upon raw materials and upon the price structure that was involved last year in one and a quarter million units of housing, so many million radio and television sets, five and a half million automobiles, and so forth. There are, from the economic point of view, other ways of relieving the pressure without cutting the security program.

Senator BENTON. Or we could have been smarter in buying for our stockpiling program.

Mr. KEYSERLING. There is no doubt about it that this Nation has the economic strength and resources to carry this job, but will we, in recognition of the danger or in the making of choices, be willing to give up some of the things we like to have? Of course, you have to give up some things to build security.

The CHAIRMAN. Among the President's recommendations, of course, is the initiation of the St. Lawrence Canal. That is a subject which will come into immediate collision with the drive for avoiding expenditures or increased expenditures, new expenditures. People who ask for curtailment of outlay are also overlooking the dynamic conditions under which Congress operates, bringing up constantly new problems for expenditures.

Last year, after the Kansas floods, Congress enacted four or maybe five laws that had not been in anybody's mind except perhaps an engineer or two, before the floods took place, and which caused very large expenditures, authorized new outlays of money above and beyond the President's budget.

The House has passed the military pay increase bill. The universal military training bill has been introduced in both Houses. The commission specially appointed to consider that subject has recommended very vigorously the establishment of universal military training, which, of course, will, in turn, call for additional expenditures.

But all of these subjects as recommended in this report will be under consideration by this committee. I don't know whether it is proper for us, for the chairman, to cross-examine you gentlemen on that. You are here supporting the President's recommendations. But the Congress will go much further and this committee will go much further in analyzing these various recommendations.

That St. Lawrence seaway and power project, of course, will require a large expenditure.

Are there any other questions to be asked?

Representative McKINNON. Mr. Chairman, I don't want to prolong the meeting, but I would like to know briefly what is your attitude on credit policy and interest rates as other measures than price control?

Mr. CLARK. The President has recommended, as he has done before and we have joined in it, that selective price controls are very important in this situation, that it was a mistake to limit the breadth of consumer credit control in regulation W and that the authority to regulate terms of credit on new housing under regulation X, which also was limited by congressional action, should be broader than it is now.

Representative McKINNON. What about Federal Reserve Board policy on general commercial credit, bank credit?

Mr. CLARK. The President makes no recommendation with respect to that policy, except to propose wider authority for the Federal Reserve Board over bank reserve requirements.

Representative McKINNON. Don't you think that availability of credit to a lot of retail and wholesale merchants had a lot to do with pushing up this price structure in the latter part of 1950 and the early part of 1951 by speculative buying?

Mr. CLARK. Credit has been a very important part of our business operation always. In the absence of credit, no doubt there would have been lessened opportunity for businessmen to carry on operations.

Representative McKINNON. That being true, don't you think some steps should be taken in that direction as an assist to price control rather than just a direct control?

A very definite policy should be established as far as commercial bank credit goes and as far as your Federal Reserve Board operations go.

Mr. CLARK. In past reports the Council has shown little enthusiasm for general credit control. We have always taken a very emphatic position in favor of the selective controls which hit just the points that you want to hit. I call attention to the fact that the general credit controls being general, hit everything, including the places where you would not want to limit credit.

Representative McKINNON. It seems to me that a lot of our wholesale rises in prices were due to the fact that many merchants rushed into the market and bought, who would not have bought had interest rates been higher and credit been tougher to get. That had a definite influence on the wholesaler and in a longer length of time affected the retail buying.

Mr. CLARK. Tighter credit might have some effect, but higher interest rates probably would not. The general view is that, at anywhere near the present level of interest, small changes in interest rates have no noticeable effect at all upon the demand for credit.

The CHAIRMAN. I might say for the record, Congressman McKinnon, that the Subcommittee on General Credit Control and Debt Management, of which Congressman Patman is chairman, has now completed a compendium of information which was developed by questionnaires which were very broadly circulated to appropriate experts. That ought to be ready in about 2 weeks. Our general feeling was that the subject of credit and monetary policy might well await the publication of that and the presence of the members of that subcommittee. So, I made no effort to bring that particular phase of the report out.

I didn't know whether you were aware of that.

Representative McKINNON. I did know Patman had a subcommittee on that, but I was wondering what Mr. Clark's attitude on it was, too.

The CHAIRMAN. Are there any other questions?

We thank you, Mr. Keyserling, Mr. Clark, and Mr. Blough, for your presentation.

Mr. ENSLEY. I wonder if the chairman or the other members of the Council would indicate for the record just how they handled their annual report this year, which the statute calls for transmission to the President in December. In previous years they published such a report, and this year it was given to the President on a confidential basis. We have had a number of requests to us for that report from outsiders, and I thought it would be well to show in the record the way it was handled this year.

Mr. KEYSERLING. In December 1951, the Council prepared and submitted to the President an annual report. However, since this report dealt exclusively with some administrative problems of the Council not of general public interest, we did not deem it desirable to entail the expense of publishing and distributing this report. The statute does not require that this annual report to the President be published.

The CHAIRMAN. The committee will stand in recess until tomorrow morning at 10 o'clock, when Mr. Lawton will appear.

The meeting will be in this room and in executive session.

(Whereupon, at 5:45 p. m., the committee adjourned to reconvene Thursday, January 24, 1952, at 10 a. m.)

JANUARY 1952 ECONOMIC REPORT OF THE PRESIDENT

THURSDAY, JANUARY 24, 1952

(This hearing was held in executive session of the committee, but is made part of the printed record by mutual consent.)

CONGRESS OF THE UNITED STATES,
JOINT COMMITTEE OF THE ECONOMIC REPORT,
Washington, D. C.

The joint committee met, pursuant to adjournment, at 10:25 a. m., in room 224, Senate Office Building, Senator Joseph C. O'Mahoney (chairman) presiding.

Present: Senators O'Mahoney (chairman), Sparkman, Benton, Taft, and Flanders; Representatives Patman, McKinnon, and Herter.

Also present: Grover W. Ensley, staff director, John W. Lehman, clerk, and staff members of the Joint Committee and the Bureau of the Budget.

The CHAIRMAN. The committee will please come to order.

The committee has assembled this morning to hear a discussion of the budget by the Director of the Budget, Mr. Frederick J. Lawton, and his staff.

I invite you, Mr. Lawton, to reveal to us all the mysteries of this document.

STATEMENT OF FREDERICK J. LAWTON, DIRECTOR; ACCOMPANIED BY ELMER B. STAATS, ASSISTANT DIRECTOR, AND JOSEPH E. REEVE, FISCAL ANALYST, BUREAU OF THE BUDGET

Mr. LAWTON. Mr. Chairman and members of the committee, I start with the assumption that you are generally familiar with the budget message that the President transmitted last Monday, and in this statement I am going to try to highlight a few of the points that I think may be particularly useful to your committee.

For the fiscal year 1953, budget expenditures are estimated at $85.4 billion and receipts at $71 billion, leaving a deficit of $14.4 billion under present tax legislation.

The expenditure totals do not include the new expansion of atomic-energy facilities which the President announced last week end. It is unlikely, however, that this program will involve any substantial changes in expenditures in the fiscal year 1953.

The CHAIRMAN. May I interrupt you Mr. Lawton? Over a period of years I find that it is a common assumption for witnesses from the various branches of the Government, coming before a committee, that not only the members of the committee but also the general public understand the fundamentals, the very basic facts, of whatever problem they are testifying about. The consequence is that the record that is made is usually rather mystifying to the general public, and I might even say to Members of Congress who are not members of the committee which is hearing the testimony.

I think, in outlining the budget that you have brought to this committee now, since this testimony is going to be printed, you ought to begin with the very basic fundamentals of the budget, showing the difference between appropriations and expenditures, how expenditures accumulate from prior appropriations, how the annual appropriations are one thing and the permanent appropriations are another thing.

So many people have the impression that any Congress at any session may make wide changes in the amount of money to be expended, but I think that ought to be made clear, first of all.

We pointed out yesterday that resolutions have been introduced in both Houses of Congress to limit the amount of expenditures, and $71 billion, I think, is the limitation named in the resolution introduced by Senator Johnson in the Senate, and by Congressman Coudert in the House.

I think, therefore, if you would make that basic analysis of the budget first, it would be most helpful to those who read the record.

Mr. LAWTON. Mr. Chairman, the basis for the initiation of Federal spending comes from budget authorizations provided by the Congress.

Those authorizations take various forms as set forth, however, in a summary prepared by Bureau staff. They are generally authorizations made annually by each session of Congress and authorizations to spend funds that are provided by basic legislation, and continue to be effective each year without subsequent annual enactment by the Congress. Examples of the latter are permanent appropriations, and borrowing authority of Government corporations.

The CHAIRMAN. There are more than that. There is interest on the national debt.

Mr. LAWTON. That is a permanent appropriation.

Senator FLANDERS. What else is there?

Mr. LAWTON. There is the 30 percent of customs revenue that goes to the Agriculture Department for removal of surplus crops. That is dependent upon the customs revenue for the year preceding. And 30 percent of that is annually appropriated without specific action by the Congress.

The CHAIRMAN. In our report last year, it may be proper to state here, we published in the appendix, as I recall it, a list of basic legislation which requires expenditure, for which the Bureau of the Budget and the President must make allowance, unless the Congress changes that basic law. The committee staff assembled for us, and we printed, a list of the fundamental changes of law which would have to be made to reduce in part some of these expenditures.

Mr. LAWTON. That list is still primarily a good list. There has been no major change.

The CHAIRMAN. We will make reference to that at this point in the record.

(The material referred to appears at pp. 86–95 of the Joint Economic Report, 82d Cong., 1st sess., S. Rept. No. 210.)

Mr. LAWTON. Another type of permanent appropriation is one that is in specific amount. For example, the appropriation for aid to colleges for the agricultural and mechanic arts, which requires a payment of $50,000 to each State and Territory each year.

There is, in addition, the borrowing authority granted to corporations, which is utilized for expenditures of those corporations that may be granted in basic legislation and not renewed again until some change in the program of the corporation is directed by the Congress, at which time they may either increase or decrease the borrowing authority of the corporation, but up to that point it remains available for the expenditures of the corporation.

(The summary referred to by Mr. Lawton is inserted at this point:)

Types of Budget Authorizations

Budget authorizations provide authority to incur obligations or to make expenditures of Federal funds, or both. All the budget authorizations of a given year which provide authority to incur obligations, of whatever type, when added together, equal new obligational authority. The budget authorizations of a given year of all types which provide authority to make expenditures, when added together, equal new authorizations for expenditure.

Obligations represent purchase orders placed, contracts awarded, salaries and wages earned, contractual services received, and similar transactions requiring the payment of money. The term "expenditures" as used here represents payments made by the issuance of checks or payment of cash (or in a few cases by an increase in a public-debt liability, as in the case of the accrual of interest on savings bonds).

Budget authorizations are to be distinguished from legislative authorizations which provide authority to carry on certain specified programs of work. In a few cases the two authorizations are combined (such as in the Federal-Aid Highway Act of 1950). Generally, however, legislative authorizations merely make it in order, under the rules of Congress, for budget authorizations to be reported favorably in appropriation acts. Budget authorizations and legislative authorizations are both enacted only by Congress.

INDIVIDUAL TYPES OF BUDGET AUTHORIZATIONS

Budget authorizations are of the following types:

1. Ordinary current appropriations

Ordinary appropriations are authorizations granted currently by Congress, both to incur obligations and make expenditures in a definite, specified amount. Ordinary current appropriations may be subdivided into three classes, as follows:

One-year appropriations—appropriations which are available for the incurring of obligations within only one fiscal year and which expire for this purpose at the end of that time. Such appropriations remain available for the making of expenditures in payment of such obligations for two additional years. This is the commonest form of budget authorization. (Examples: Salaries and expenses, Federal Bureau of Investigation, 1952.)

Multiple-year appropriations—appropriations which are available for obligation for a specified period of time in excess of 1 year and which expire for this purpose at the end of that time. Such appropriations remain available for the making of expenditures in payment of such obligations for two additional years. This type of appropriation is used occasionally for programs of an unusual seasonal nature or programs of a nonrecurring type which do not fit precisely within the fiscal year. (Example: Sugar Act program, Agriculture, 1952 and 1953.)

No-year appropriations—appropriations which are available for obligation and expenditure until the purpose is accomplished and which do not expire at any fixed time. This type of appropriation is used primarily for certain types of benefit payments and for construction projects where a time limit would not add appreciably to the system of expenditure control. (Example: Maintenance and improvement of existing river and harbor works, Army.)

2. Annual indefinite appropriations

Annual indefinite appropriations are authorizations granted currently by Congress, both to incur obligations and make expenditures in an indefinite amount.

Although such appropriations are found in appropriation acts, the amount of each is not specified in the act but is determined otherwise. Often the amount of the appropriation is equal to the amount of receipts (or a percentage thereof) from a specified source. (Example: Payments to Oklahoma (royalties), Interior, which appropriates 37½ percent of certain royalties for payment to the State of Oklahoma in lieu of taxes on tribal lands.) In some cases the amount of the appropriation is determined by financial needs. (Example: The appropriation from the general fund for contribution to the postal revenue.) These appropriations may have varying periods of availability, just as do ordinary current appropriations.

3. Permanent appropriations

Permanent appropriations are those in which additional amounts become available from year to year under standing law without new action by Congress. The law may provide for such appropriations to operate for a specified number of years and then stop, but in most cases the law provides for them to operate indefinitely until it is amended or repealed. Some permanent appropriations are found in ordinary legislation: others were enacted originally in appropriation acts which provided not only for the amount to become available in the year of the act but also for additional amounts to become available in succeeding years.

Permanent appropriations are customarily subdivided into two principal groups:

Permanent definite appropriations—those where the amount becoming available for obligations and for expenditure each year is specified in the law. (Example: The appropriation "Colleges for agriculture and mechanic arts, Federal Security Agency," provides for the payment of $50,000 to each State and Territory each year (7 U. S. C. 301–308; 321–328).)

Permanent indefinite appropriations—those where the amount becoming available for obligation and for expenditure is not specified in the law, but is determined by the amount of receipts from a specified source, by the amount of financial requirements, or by other means. (Example: An amount equal to 30 percent of the customs receipts each year is appropriated for removal of surplus agricultural commodities, Agriculture (7 U. S. C. 612c).)

The permanent appropriations becoming available in any year may have varying periods of availability, just as do ordinary current appropriations.

4. Contract authorizations

Contract authorizations confer authority to enter into contracts and incur other obligations in advance of an appropriation. The general rule is that the Government cannot incur obligations for the future payment of money in excess of the amount available in an appropriation or the amount becoming available in a revolving fund, except where Congress has granted permission to do so. Such permission normally takes the form of a contract authorization. (In a few cases such permission has taken some other form, such as authority to enter into long-term leases. Such authority cannot be firmly stated in dollar terms and hence is not included in the totals of budget authorizations.)

Contract authorizations do not provide the authority to make expenditures; hence, they must be followed by an appropriation to liquidate obligations incurred pursuant to them. Most contract authorizations appear in annual appropriation acts; a few are made by substantive legislation, being combined there with the legislative authorization. Contract authorizations are used chiefly where more than a year is expected to elapse between the time the obligation is placed and the time expenditures will become necessary in payment thereof.

For a time, contract authorizations for Navy ship building were indefinite in amount, the authorization being stated in terms of tonnage, number of ships of a given type, or some other factor. However, no new contract authorizations for shipbuilding have been stated in such terms in recent years.

Contract authorizations may be subdivided as follows:

(*a*) Current contract authorizations, enacted currently by Congress, usually in appropriation acts.—These are usually definite in amount. (Example: Establishment of air navigation facilities, Civil Aeronautics Administration, Commerce, 1951.) However, at times recently the contract authorizations for certain construction purposes have contained an escalator provision providing that the basic authorization may be increased in an indefinite amount equal to the rise in construction prices after the authorization is enacted. (Example: Construction and equipment, storeroom, etc., St. Elizabeths Hospital, 1949.)

(*b*) Permanent contract authorizations found in substantive law. Some provide for specified amounts to become available for obligation purposes for a limited number of years. (Examples: Federal aid, postwar highways, Commerce, and slum clearance and urban redevelopment, Housing and Home Finance Agency.) Others provide for renewal each year with no time limit. (Example: The contract authorization for beginning certain work in Alaska prior to July 1 each year under the appropriation for health, education, and welfare services, Bureau of Indian Affairs (Interior).)

5. Appropriations to liquidate contract authorizations

Appropriations to permit the payment of obligations incurred under previously granted contract authorizations are called appropriations to liquidate contract authorizations. Such appropriations appear in appropriation acts and are often included in the same paragraph as an ordinary current appropriation. They are authorizations to make expenditures only and are not authority to incur additional obligations. (Example: Establishment of air navigation facilities, Civil Aeronautics Administration, Commerce, 1952.)

6. Authorizations to expend from debt receipts

In lieu of appropriations, the law in some cases authorizes obligations and expenditures to be made specifically from money which the Treasury is directed to borrow. Sometimes a Government-owned corporation is authorized to borrow directly from the public. Both of these authorizations are called authorizations to expend from debt receipts. Spending under such authorizations has the same effect on budget totals and on the deficit as does the spending of money which has been directly appropriated. These authorizations may be found both in appropriation acts and in other laws. They have been used particularly where the money is used for loans or recoverable expenditures usually through a business enterprise of the Government (such as a Government corporation). (Example: Loans, etc., Defense Production Act.)

In the case of Government-owned corporations the budget programs are reviewed annually by Congress, and provision is customarily made in the appropriation act for the corporations to carry out their programs in the ensuing year. This is true of corporations which use authorizations to expend debt receipts as well as other Government-owned corporations.

Sometimes an act of Congress directs the cancellation of notes of a Government enterprise to the Treasury. If the cancellation restores a given amount to the enterprise's borrowing authority, it is in effect a variety of this type of authorization, since it makes it possible for new obligations and expenditures to be made in that amount from public debt receipts. (Example: Restoration of capital of the Commodity Credit Corporation by cancellation of notes.)

7. Reappropriations

In some cases part or all of the unobligated balance of a prior 1-year or multiple-year appropriation is continued available for obligation and expenditure after it would otherwise expire. Such actions are called "Reappropriations." They are usually enacted in appropriation acts, but sometimes occur in other laws. They may be definite or indefinite in amount. (Example: Expenses, Commission on Renovation of Executive Mansion, 1951.)

8. Reauthorizations of contract authority

The contract authority described in item 4 above, like appropriations, may be 1 year, multiple year, or no year. Occasionally part of a 1 year or multiple year contract authorization is continued available by act of Congress after it would otherwise expire for obligation purposes. Such cases are called "Reauthorizations of contract authority." They may be definite or indefinite in amount. (Example: Ship construction, maritime activities, commerce, 1951.)

9. Reauthorizations to expend from debt receipts

Authorizations to expend from debt receipts, like appropriations, may be 1 year, multiple year, or no year. Occasionally part of a 1-year or multiple-year reauthorization to expend from debt receipts is continued available by act of Congress after it would otherwise expire for obligation purposes. Such cases are called "Reauthorizations to expend from debt receipts." They may be definite or indefinite in amount. (Example: Economic cooperation, foreign assistance, 1951.)

COMPUTING THE TOTAL BUDGET AUTHORIZATIONS

New obligational authority

New obligational authority represents the sum total of all authority becoming available during a given fiscal year to incur financial obligations on behalf of the Government. This consists of the various types of authorizations named above, with the exception of appropriations to liquidate contract authorizations (such appropriations do not confer any obligational authority).

Thus the total obligational authority becoming available for the fiscal year 1952, under enactments in effect at the time the 1953 budget was printed, consisted of the following (numbers refer to the types of authorizations listed above):

[In millions of dollars]

	Current	Permanent
1. Ordinary appropriations	$79,106	
2. Annual indefinite appropriations	1,387	
3. Permanent appropriations		$6,272
4. Contract authorizations	1	648
6. Authorizations to expend from debt receipts:		
(a) Public debt	2,361	250
(b) Corporate debt		71
7. Reappropriations	856	
8. Reauthorizations of contract authority	95	
9. Reauthorizations to expend from public debt receipts	43	
Total	83,849	7,241

New authorizations for expenditure

New authorizations for expenditure represent the sum total of new authorizations to make payments, becoming available during a given fiscal year. This excludes two types of items (contract authorizations and reauthorizations thereof included in the total of new obligational authority, while it includes one other item (appropriations to liquidate contract authorizations) not included in new obligational authority.

Thus, the total new authorizations for expenditure becoming available for the fiscal year 1952, under enactments made at the time the 1953 Budget was printed, were as follows (numbers refer to the types of authorizations listed above):

[In millions of dollars]

	Current	Permanent
1. Ordinary appropriations	$79,106	
2. Annual indefinite appropriations	1,387	
3. Permanent appropriations		$6,272
5. Appropriations to liquidate contract authorizations	2,791	
6. Authorizations to expend from debt receipts:		
(a) Public debt	2,361	250
(b) Corporate debt		71
7. Reappropriations	856	
9. Reauthorizations to expend from public debt receipts	43	
Total	86,544	6,593

NOTES

I. Use of collections

In some cases collections are made available for obligation and expenditure by provisions, either of permanent law or of appropriation acts, that they shall be credited to revolving and business enterprise funds or treated as reimbursements to general fund appropriations. In such cases the collections are treated as credits to expenditures, so that expenditures are stated in the budget net of the collections received. Where expenditures are thus netted, the collections are not treated as budget authorizations.

Net expenditures of a business enterprise or revolving fund in any year come either from one of the types of budget authorizations named above, or from balances of collections credited to the fund in prior years.

II. "Federal funds" as distinguished from "Trust and deposit funds"

The Budget distinguishes two main groups of funds:

"Federal funds," which are those owned by the Government. They may be subdivided into the general fund, special funds, and revolving and business enterprise funds. (The types of authorizations described above could also be reclassified by types of funds.)

"Trust and deposit funds," which are those held by the Government as trustee or banker.

The discussion of "budget authorizations" and the figures used above refer to authorizations for the use of Federal funds, including contributions from Federal funds to the trust funds. The dicussion and figures above exclude authorizations to use the regular receipts of the trust funds and deposit funds. Although trust and deposit funds are printed in the Budget Document, they are not included in the conventional "budget" totals.

III. Balances of prior authorizations

In addition to the authorizations becoming available in any given year, balances of prior year authorizations are brought forward into the year. As explained in item one above and mentioned under some of the other items, appropriations and most other authorizations can have varying periods of availability for obligation, and virtually all budget authorizations are available for expenditure beyond the end of the year in which they first become available.

Therefore, there may be balances at the beginning of each year of the various types of authorizations named above. These balances may be redivided in turn into three principal groups:

Obligated balances—the portion of authorizations previously made which have been obligated, but not yet expended. Except for obligated balances of contract authorizations (which must later be appropriated for), the obligated balances at the beginning of a year are sources of potential expenditures in addition to the new authorizations for expenditure for that year.

Unobligated balances of expired accounts—these are balances of 1-year or multiple-year authorizations which have expired, and which are not obligated. They remain available ordinarily for 2 years after the time that the account expires, but can be used solely for adjustments in obligations which may become necessary at the time payments are made. (Such adjustments are required at times because it is impossible to estimate to the exact cent at the time the obligation is incurred the amount that will ultimately be required to pay for what is received and billed.)

Unobligated balances of unexpired accounts—these are the balances in no-year authorizations and in multiple-year authorizations which not yet expired, available for the incurring of further ogligations. These balances provide obligational authority in addition to the new obligational authority described earlier in this memorandum.

The CHAIRMAN. One of the largest of the expenditures in the budget depending upon basic law rather than upon annual appropriations is the public assistance grants to the various States, is it not?

Mr. LAWTON. The public assistance grants are annual appropriations, but they depend upon the basic law which has, in a sense, committed the Government to match the States on a formula basis for the payments made by the States to the recipients of public assistance.

The CHAIRMAN. So when the Bureau of the Budget undertakes to prepare the estimate for public assistance grants, how does it go about that?

Mr. LAWTON. It is largely a matter of multiplying the rates currently being paid by the States by the number of persons estimated to qualify under those rates in the given fiscal year.

The CHAIRMAN. That expenditure, then, is measured, first, by the rate fixed by Congress in the basic legislation, and then the estimate as to the number of persons who will meet the qualifications set in that basic law?

Mr. LAWTON. Yes. The rate fixed by Congress, however, is in part a flexible rate, since it depends upon the amount that the State will pay. It matches on a formula basis what the State fixes as its payment to recipients of public assistance.

The CHAIRMAN. And if the States then were to reduce or to increase their rate of payment, the Federal rate of payment would thereby be increased, would it not?

Mr. LAWTON. It would vary under the formula. It is a percentage formula that applies at different levels.

The CHAIRMAN. How about veterans' benefits and payments?

Mr. LAWTON. Veteran payments are a pure estimate, a mathematical estimate again of the number of persons who are expected to qualify and apply for pensions, times the rates fixed by the Congress for pensions for various causes, various degrees of disability, and in some cases age limits—Spanish War veterans become eligible at the age of 65, for example.

And in the case of veteran benefits, such as the GI bill benefits, it depends upon the rates fixed by the Congress in the basic law, times the number of people who will qualify or take advantage of the benefits granted under that bill—for example, the number of veterans who will go to school with the aid of educational benefits under the GI bill.

The CHAIRMAN. Does this budget take any cognizance of the expense to which the Federal Government will be put in the event a bill is passed, as seems likely, extending to veterans of the Korean war, the benefits now allowed to veterans of World War II?

Mr. LAWTON. We have an item, under proposed legislation, an expenditure estimate of $75 million for the fiscal year 1953 for an extension of the GI bill to Korean veterans on a modified basis; in other words, that estimate does not assume that the 52–20 Club, for example, will be renewed. It assumes that many of the problem areas, the abuses, if you will, that were possible under the earlier bill will be corrected. That is, the reentry provisions will be drastically limited, students will not be permited to shift from course to course as they see fit, and there will be a limitation on the amount of tuition, rather than whatever the school may charge. In a sense, I think it is the Kerr bill.

The CHAIRMAN. Is there anything in this budget that reflects the probable cost of the recent increased pay bill for the Military Establishment that passed the House?

Mr. LAWTON. Again, we have made provision under proposed supplemental for 1952, and again for 1953, for military pay increase.

The CHAIRMAN. Is it in this budget?

Mr. LAWTON. There is about $900 million in this budget document for that purpose in 1953, and about $400 million for 1952.

The CHAIRMAN. Are there any other forecasts of probable legislative increase of expenditures?

Mr. LAWTON. I can read them off to you. There is a list of about a dozen items.

We are estimating for the extension of existing legislation, such as the Mutual Security Act, appropriations of $7.9 billion, and expenditures of $3.339 millions in 1953 out of that authority.

The remainder of the expenditures will come out of prior appropriations.

Representative HERTER. You expect to get all of the prior appropriations expended, do you?

Mr. LAWTON. Largely; yes. This is the current year's appropriation.

Representative HERTER. There is at least $9 billion still in arrears of the appropriations made, and only about $2 billion has been spent for that purpose out of the $10 billion appropriated?

Mr. LAWTON. The estimate in this year for end-item aid is $4 billion, and in 1953 $8 billion for end-item aid, based on the fact that there has been a new allocation policy directed by the President on the transfer of materials to NATO and other countries which in the event of war would be most likely to be first attacked.

Representative HERTER. At that point, may I ask one question? I do not want to digress from the rest of this.

Is there any reason in the world why end items which are nothing but an allocation from a machine that are identical in every way, whether they be tanks, whether they be guns or ammunition, the other hardware—is there any reason why they should not come under the regular military appropriation and then be allocated from that?

Mr. LAWTON. This method gives Congress the opportunity to judge just how much it wants to appropriate specifically for the military and economic aid to foreign countries.

Representatives HERTER. Can it not do exactly the same thing by allocating from the military appropriation so many billions without specifying the kind of thing, but allocating so much that can be transferred for foreign aid by the military?

Mr. LAWTON. It is possible that you could arrive at the same end result.

Representative HERTER. Would you not get much better flexibility than having to have an entirely separate appropriation and a separate bill?

Mr. LAWTON. You would not get any greater flexibility.

This money is allocated to the military. It is scheduled in their production schedules along with the other equipment that they are buying for themselves, and it is simply allocated and charged to this appropriation.

Mr. STAATS. It is allocated at the beginning of the fiscal year or as soon as the money is available, so that it is available at the same time and for the same period of time.

Representative HERTER. But it makes not the slightest difference how much new money we put in the foreign-aid program, the military determines its priorities, dependent on military needs—it makes no difference what money we put in, the money does not guarantee the delivery of a single piece of hardware in a separate appropriation—not a piece.

Mr. LAWTON. That is correct.

Representative HERTER. It seems to me perfectly ridiculous to separate the two things, as though they are entirely different. They are an integral part of the national defense or else there is no excuse for them. And why they are separated into two, one foreign-aid package, and one domestic defense, I do not see, and a large part of the domestic program goes into foreign aid of a slightly different kind.

The CHAIRMAN. I wonder if I understand the point that you are making.

Last year with respect to this mutual security appropriation and with respect to the reorganization, too, it was broken down into two categories—military aid and economic aid.

Representative HERTER. I am speaking only of military aid.

The CHAIRMAN. This year the budget has come up recommending an appropriation of $7.9 billion, but there is no allocation between military and economic aid, as I understand it.

Mr. LAWTON. That will be made, of course, when the legislation is submitted.

Representative HERTER. There will be a breakdown of that?

Mr. LAWTON. There certainly will be a breakdown.

The CHAIRMAN. But in your budget estimate you have not undertaken to segregate the two now?

Mr. LAWTON. That is correct.

The CHAIRMAN. Then your point has to do not with that segregation, but merely with the segregation of the foreign military appropriation from the domestic?

Representative HERTER. That is right, because we found this: It made no difference how much money we appropriated for foreign aid, you did not get any if the military did not want it to go there. It makes no difference what money was in the budget. The allocations just put that material at the tail end somewhere which would be delivered some day when other priorities had been met, and it makes no difference what we say about it. The military makes the determination of priority.

When a tank comes off the assembly line they decide where it will go, no matter what appropriation has been made.

The CHAIRMAN. I think that was the general feeling last year as to the proper course of procedure.

Representative HERTER. I do not see why there should be a separation of the appropriations. It seems to me it ought to be one for end items which are the hardware which come off the production line. And when they are exactly alike as two peas in a pod, or go to foreign aid or to domestic training camps or go into Indochina or to Korea, it is all part and parcel of one defense effort, and why it should be split up into these separate things and just make the problem a little more difficult, I think, from the point of view of seeing the over-all picture than it would otherwise, I have not been able to understand.

Mr. STAATS. If I might add some more on that.

The CHAIRMAN. Yes, Mr. Staats.

Mr. STAATS. I think as you probably know better than I do, it has been a matter of the way the legislation actually developed.

Representative HERTER. You are quite right. The original legislation.

Mr. STAATS. With respect to the Economic Cooperation Act and the shifting of emphasis over to the military side, I think there are a couple of practical considerations.

One is the shift between economic aid and military end items which is provided in the statute. This is a matter of administration during the course of the year.

And the second is the policy issues that evolve in the actual administration of the program, such matters as offshore procurement, so-

-called infrastructure, and common supplies, and so forth, and so on, overseas.

The Congress last year placed the responsibility in the Director for Mutual Security for those policies.

I think those two practical problems have been fairly important in the decision to propose a separate appropriation for end items.

Representative HERTER. I still think it ought to be a single appropriation. I think we are at fault. I am not thinking that you are at fault.

Mr. STAATS. You are entirely correct in stating that the actual deliveries and scheduled deliveries are a matter of allocation policy. The estimate in this budget reflects a new policy directive from the President to the Secretary of Defense, just prior to the sending up of the budget, which indicates a larger percentage of deliveries of end items for NATO programs.

The CHAIRMAN. After all, that, of course, is a matter of policy with respect to the amount of money to be appropriated and authorized to be expended which is separate and apart from consideration we are giving here to the total amount and breakdown of the budget.

May I say, Congressman Herter, that at the outset this morning I interrupted Mr. Lawton in the presentation that he had prepared in order to ask him to put in the record a list of those expenditures which are the result of permanent appropriations, or the result of basic laws which measure the expenditure by some rule a little bit outside of the annual operation, and he has been doing that.

Representative HERTER. I am sorry if I got off the track at that point.

The CHAIRMAN. I just wanted to bring you up to the minute.

Representative HERTER. Thank you.

The CHAIRMAN. The first of these was the extension of mutual security.

Mr. LAWTON. That is right.

The second is an extension of the Federal-aid highway program, the 2-year authorization having expired, and for that we have new obligational authority of $400 million for the Federal-aid highway program and $17.5 million for the forest highway program, with no expenditures anticipated in 1953 from those funds. The expenditures will come from the prior years' appropriations.

The expenditures are 1 to 2 years behind the authorization.

The CHAIRMAN. That is, of course, a basic fact which is not generally understood, that the expenditure for the construction of Federal-aid highways is a result of a process that goes on over a number of years. I think as much as five. It includes, as we set forth in one of our reports, Report No. 210 of the Eighty-second Congress, first session, that highway expenditures go along by steps.

First, there is the planning, at the local levels?

Mr. LAWTON. The first step is the apportionment, by the Secretary of Commerce to the States, under the formula that Congress fixes.

After that apportionment is made the States submit first their general programs, and subsequently their definite project plans. When those plans are approved they become contractual obligations on the part of the United States.

The State then proceeds to let contracts for the construction of highways. As those contracts are completed, the State pays the bills and submits vouchers to the Government for reimbursement.

So that the Government's expenditure is after completion of the construction or various parts thereof.

The CHAIRMAN. But there are salary appropriations to compensate the employees, both Federal and State, who do this preliminary work.

Mr. LAWTON. That is right. There is a percentage allowed for Federal administrative expenses in each highway authorization.

The next item is the extension of the Defense Production Act with a proposed $900 million increase in the borrowing authority and appropriations of $256 million for the administrative expenses of the various segments of the Defense Production Act, Price Stabilization, Wage Stabilization, NPA and DPA, and so forth.

The CHAIRMAN. That borrowing authority, as I recall it, is the authority contained in the Defense Production Act to authorize the acquisition of these funds for the purpose of stimulating production of essential and critical materials.

Mr. LAWTON. And for loans and purchase of industrial equipment and of strategic and critical materials from foreign sources as well as our own.

Out of the $900 million borrowing authority, we anticipate an expenditure of about $285 million in the fiscal year 1953. And out of the $256 million in appropriations, we anticipate expenditures of $213 million. The remainder will be carried over into 1954 for expenditure.

The CHAIRMAN. You have prepared a list of all of these, have you not?

Mr. LAWTON. We have a list which we have supplied to the committee.

The CHAIRMAN. I think it may be appropriately inserted in the record at this point.

(The document entitled "Proposed Legislation Affecting Budget Expenditures" is as follows:)

Proposed legislation affecting budget expenditures (summary of amounts included in the 1953 budget)

[Fiscal years, in millions]

Function and program	Anticipated supplemental appropriations and other authorizations		Estimated expenditures	
	1952	1953	1952	1953
Extension of existing legislation:				
International security and foreign relations: Extension of Mutual Security Program		$7,900		$3,339
Transportation and communication:				
Extension of Federal-aid highway program		400		
Extension of forest highway program		17		
Extension of Defense Production Act:[1]				
Borrowing authority		900		285
Other expenses		256		213
Total, extension of existing legislation		9,473		3,837
Military services:				
Military services: Department of Defense, military functions [2]	$500	3,500	$400	1,100
Total, military services	500	3,500	400	1,100
New legislation:				
Transportation and communication: Postal rate increase (increased revenue)		−225		−225
Natural resources:				
Hells Canyon power project		8		6
St. Lawrence Seaway and power project		20		15
Housing and community development:				
Expansion of programs for defense housing, community facilities and services		325		213
Flood insurance		50		1
Education and general research:				
General aid for operating expenses, elementary and secondary schools		300		290
Expansion of programs for education of children on Federal property and in emergency and critical defense housing areas		80		35
General assistance to college students		30		30
Social security, welfare, and health: Additional grants to States to increase public-assistance benefits		100		100
Veterans' services and benefits:				
Education and training benefits, Korean veterans		75		75
Increases in disability and death compensation rates		100		100
General government: Dispersal of Government activities		15		5
Total, new legislation		878		645
Total, proposed legislation	500	13,851	400	5,582

[1] Funds for the Defense Production Act are included mainly under Finance, Commerce, and Industry, but are also in several other functions.
[2] Includes military pay increase and military construction.

NOTE.—The 1953 budget also includes estimates for legislation to increase old-age and survivors insurance benefits involving added trust fund expenditures of $225 million in 1953, and legislation increasing miscellaneous budget receipts by $15 million in 1953 by raising fees charged by Government.

The CHAIRMAN. Yesterday I put in the record while the Council of Economic Advisers was here, the analysis of new obligational authority and budget expenditures which was issued at the same time that the budget was sent to the Congress by the President.

This table shows that the expenditures for 1953 for major national security programs, which include international security and development of atomic energy, amount to $65,097 million which, when deducted from the total budget expenditures as estimated at $85,444 million, leaves a balance of $20,347 million, and of that $20,347 million you total $14,000 million for these continuing items such as we have now been discussing. The permanent appropriations like the interest on the national debt, amounting to $6,255 million, the other permanent appropriations amounting to $133 million, the veterans' services and benefits which depend upon the rate fixed in the GI bill of rights and the incidence of obligation as may develop among the veterans, and that you figure at $4,022 million, and the third largest was the public assistance grants which you estimated at $1,140 million, so that any great saving to be made out of the $20,347 million must of necessity come out of modifications of these prior congressional grants of authority, is that right?

Mr. LAWTON. For fourteen-twentieths of them or 70 percent, the Congress would have to deal with these prior grants of authority.

Representative HERTER. May I ask one question at that point, Mr. Chairman?

The CHAIRMAN. You may.

Representative HERTER. When you speak of a grant of authority, as I understand it 2 years ago the Appropriations Committee began objecting to future contract authorization and insisted on appropriation instead.

Mr. LAWTON. That is correct.

Representative HERTER. So that appropriations were made by the Congress which are a legal green light to a given Department to spend, are they not, an appropriation?

Mr. LAWTON. Just the same as a contract authorization.

Representative HERTER. Just the same as the contract authorization, except that in the contract authorization they cannot pay the bill until money has been provided for.

Mr. LAWTON. That is right.

Representative HERTER. There are now accumulated quite a large backlog, so to speak, of appropriations in the Defense Department. It is estimated that when the fiscal year 1953 is finished, there will still be over $70 billion that has not been expended, but that has been authorized in the form of appropriations and carried over into the next fiscal year. That includes Mutual Assistance Act for military expenditures.

Mr. LAWTON. The carry-over into 1953 for military expenditures is $60 billion. Mutual Security Act $8.8 billion.

Representative HERTER. Nearly $70 billion.

Mr. LAWTON. The total for all other agencies is $4 billion in other appropriations or a total carry-over into 1953 or 72.8 for the whole appropriation structure.

Representative HERTER. May I just continue this, because I am a little confused on the controls that are involved here. $72 billion are carried over. That is in the Department of Defense, except the Atomic Energy Commission—everything rests in there, they are authorized to spend that at whatever rate they see fit from the point of view of the legislation.

What controls are there?

You say that only $65 billion are going to be spent in the new appropriations, and a lot of the new appropriations have got to be for pay items, for food, for the current maintenance of the armed services, so that only a part of the new appropriations will be for these end items, just as they were in the past appropriation.

How do you control the rate of expenditure in this year?

Have you any authority over the Defense Department, or can it spend whatever it sees fit anywhere between $40 billion and $70 billion, let us say, during the current year?

Mr. LAWTON. We have no control directly over expenditures. Our controls are over obligational authority, and over the entering into of contracts under the apportionment system for most agencies.

The problem is in the larger or long-lead-time items. For example, in the case of aircraft the average lead time, based on a recent study that the Defense Department has made, is 24 months. That means that to get deliveries by a date in the future you have to provide the obligational authority in the form of an appropriation now in order that you may let your contracts, so that the suppliers can begin work and, ultimately, deliver that 2 or 3 years from now.

Senator FLANDERS. Is that for an already completed design, or is that for a future development not yet established on the board or in trial?

Mr. LAWTON. Largely, it is for such things on which the initial research and development has been completed. The problems are tooling, getting production lines in being, making necessary modifications.

Senator FLANDERS. A model has been accepted?

Mr. LAWTON. I would say in substantially most cases that is true. For example, the B-47 takes quite a while to produce. They have to go through a modification center now before they are finally accepted.

The CHAIRMAN. Let me say, Mr. Lawton, incidentally I wear two hats on this problem: One is chairman of this committee and one is chairman of the Senate Defense Appropriations Subcommittee.

At the conclusion of the action on the defense appropriations bill last year I asked the Department of Defense to be prepared this year to submit to our committee a complete statement of all unexpended appropriations, appropriations made in the past, all appropriations and authorizations, accompanied by a statement of the amount out of each such appropriation which has been obligated, and then a statement of the amount which has been programed, with a view of determining the area in which it might be possible to reduce the former appropriation.

That may be illustrated by a simple incident that arose during the consideration of the budget last year: The Army Ordnance had planned a new sort of manpower-carrying tank which was designed for land warfare. Well, the committee looking into that matter with the aid and assistance of the witnesses from the Army, raised a question as to whether or not such an implement would be a desirable and necessary one. And, finally, the Army agreed that it could be abandoned.

So the money which was being asked for the construction of that particular vehicle was taken out of the appropriation.

And our feeling was that there might be others of that kind, and that upon scrutiny of the unobligated balance of moneys already appropriated and authorized, we might find a means of making a saving.

The Budget Bureau, which has also been working on this matter, has brought to the committee this morning a statement which will be discussed at an appropriate time.

Representative HERTER. There is one more question I should like to ask.

The CHAIRMAN. Let me say just before you do that, that this table which was placed in my hands this morning shows that the estimated obligations for fiscal 1952, out of these previous appropriations and authorizations, amounts to $25,974 millions and that there is an unobligated balance of $39,179 million.

So that my feeling is that the Defense Appropriations Committee, by scrutinizing those former authorizations and appropriations, may find the way of making a considerable saving. Personally, I have no doubt that there may be in unobligated balances, plans to construct conventional weapons or conventional implements which may not be needed in the modern situation.

Representative HERTER. Again, only one more question, if I may, that I think perhaps you could answer just as well as Mr. Lawton.

Take the question of tanks that has been discussed a good deal.

There has been a good deal of trouble with the new design tank. The production of the finished tank has been tremendously delayed over the original lead time of 10 months. That is the standard time that the military people estimate for that. A large part of the appropriations, both for overseas use and for domestic use, was for tanks. And when I say "large," I mean very large figures.

Those tanks were just not delivered. They could not be because they were imperfect. They are still monkeying with them.

The new tanks that are serviceable are coming off very slowly.

What happens from a budgetary point of view?

The money is still available for tanks. Further, there is further obligational money for tanks that we were told last year that would be running into 1953 and 1954, at the tail end of the same contract.

Does the Military Defense Department, because they get behind, or did in this last year, in tanks—do they pile it all into this coming fiscal year with an additional strain on steel and additional strain on manpower, because they can step that tank program up tremendously from the point of view of shifts of labor, and so forth, if they want to? What happened to them? Are the tanks that are not delivered in the program in 1952 tacked on to the program in 1954 or 1955, or are they all jammed into the fiscal year 1953, so that you have an additional expenditure and an additional use of the steel because of the delay in the program in 1952?

The CHAIRMAN. Well, if I may answer that, I would say "No."

What happens is that there is rather an accumulation of dollar appropriations and authorizations, than there is of delivery of tanks or implements of any kind.

Representative HERTER. The money is there to speed up the program if they want to speed it up, to catch up with their requirements in tanks?

The CHAIRMAN. Of course. I have not examined the military budget as yet, but as far as I have examined it, and it is some $9 billion below the appropriation of last year—am I not correct in that figure, Mr. Lawton?

Mr. LAWTON. The obligational authority for the military is $9.3 billion below last year.

The CHAIRMAN. Yes. The 1953 obligational authority is estimated at $52.4 billion as compared with $61.7 billion last year.

Representative HERTER. That means appropriations, really not obligational authority.

Mr. LAWTON. It is appropriations. That is obligational authority.

Senator FLANDERS. This is the cash basis, referring to the chart?

Mr. LAWTON. No, sir. It is an expenditure basis, but if you want to distinguish between what is sometimes called the cash budget, it does not include trust-fund transactions. It is a cash-expenditure basis, checks paid.

Senator FLANDERS. A cash-expenditures basis?

Mr. LAWTON. For the items in the budget.

The CHAIRMAN. That is why I asked at the outset, to have him put in the record an explanation of the difference between expenditures in any fiscal year and appropriations.

Expenditures are the accumulation of past authorizations for long-lead-time items and current expenditures, like food and clothing and pay to the men in service, whereas the appropriations are for those current expenditures which must be made during the current fiscal year and the authorizations for long-lead-time items which develop in some future year into expenditures.

Senator FLANDERS. I think I understand, but when we say that the new obligational authority is $9 billion less this year than last, this column here includes expenditures which will be required by the heavier obligations incurred last year.

Mr. LAWTON. That is correct; it is about a 50–50 proposition.

Representative HERTER. That is reappropriations, really, is it not?

Mr. LAWTON. The authorization is available for expenditure for two fiscal years after the one in which it was made.

Representative HERTER. If it comes out of 1951, as some of it has, it has to be reappropriated.

Mr. LAWTON. No, sir.

Representative HERTER. It does in the foreign aid program.

Mr. LAWTON. In the foreign aid program you are making expenditures out of money that was appropriated in 1951. You are making those in 1953.

The CHAIRMAN. I think the issue can be made more clear by pointing out that while the new obligational authority for 1953 is less than that for 1952, by the difference between $61.7 billion, which was appropriated in 1952, to $52.4 billion, as estimated for this year, the expenditures for 1953 are greatly in excess of the expenditures in 1952.

The expenditures in 1952, as set forth in this budget, amounted to $39.8 billion; in other words, they were considerably less in the appropriations. But the expenditures estimated for 1953 amount to $51.2 billion.

They are still less than the new obligational authority for 1953, but as I said, they are greatly in excess of the expenditures of 1952.

So that expenditures in any fiscal year are the sum of the prior appropriations and obligational authority which mature in the year and the current expenditures.

Representative HERTER. I fully understand that.

The one point that I am still concerned about is one that is this committee's primary interest, namely the expenditure item from the inflationary point of view, the impact on the economy.

The CHAIRMAN. Right.

Representative HERTER. What control have we over the rate of expenditures, not over appropriations but expenditures? What control?

Mr. Lawton says he has no control over the Military Department from the point of view of rate of expenditures, once the appropriation has been made.

What control have we over rate of expenditures? What can de do, once the appropriation has been made?

Here you have seventy-odd billions of former appropriations hanging over, coming into the fiscal year. Some of them have already been obligated for long-lead items, so you can write them off. Some have not been obligated at all.

Congress has completely lost control of the rate of expenditures that we are particularly interested in, because of the tremendous unexpended, unobligated appropriations or prior authorizations that had been made.

The CHAIRMAN. Not necessarily. Take, for example, an airplane carrier for the Navy. Such a vessel is one of the longest of all of the long-lead-time implements of war.

The Congress passes a bill authorizing the construction of such an implement.

I understand that the chairman of the Armed Services Committee of the House has already announced that he plans to introduce legislation of that kind with respect to aircraft carriers.

If Congress should pass that and the Navy would then be authorized to proceed with the expenditure of current funds for the planning of that aircraft carrier, nevertheless Congress at any time during the period of construction could step in and say, "No, we have changed our mind, we will not build that."

But the question which would arise, naturally would be, should we stop this construction and waste the money that has been spent?

Representative HERTER. How do you hold up the appropriations already made? You either rescind the appropriation or change the appropriation, do you not?

The CHAIRMAN. One way or the other, yes, sir.

Representative HERTER. Changing an authorization in the middle of construction might not change the rate of operations on that aircraft carrier. You might feel from the standpoint of economy it would be a good idea to slow down the work on it, to take another year in getting it done.

The CHAIRMAN. Congress could do that.

Representative HERTER. By what process do we do it? That is what I am interested in.

The CHAIRMAN. It would have to be done by legislation.

Senator FLANDERS. Have you not a better case in connection with such things as the authorization of the new quantity of planes or tanks which you could stop delivery of at any point?

The CHAIRMAN. That is right, yes.

Senator FLANDERS. Whereas, in aircraft carriers you have nothing if you stop construction. The rest is all waste. So that your Appropriations Committee can recommend the stopping of construction of a line of tanks.

Representative HERTER. They cannot cancel contracts without loss, can they?

Mr. LAWTON. They will have to pay damages. It may not be the full amount.

The CHAIRMAN. This is illustrated, for example, by the item for Air Force defense. Congress appropriated for 1952 $20,600,000,000. The estimate in the budget is $14,002,000,000. That may represent a cut-back in the program for air power for which the Department of Defense made an original request.

Congress could make a further reduction in that, and that reduction could be made to affect not only the current rate of delivery, or the projected rate of delivery, but the delivery that had been planned.

Mr. LAWTON. Mr. Chairman, that is not a cut-back in the goal that was established.

The CHAIRMAN. It is a postponement.

Mr. LAWTON. As a matter of fact, one of the things involved in that figure is a change in lead time. There is $3½ billion in there, because of the fact that they found that they would have to extend their lead time for aircraft from an average of 18 to 24 months.

The CHAIRMAN. I was not going into the reasons for it, I was just citing it as an illustration of the point that Congressman Herter had raised.

Mr. LAWTON. Actually, the major determinant on this rate of expenditure, the major question in connection with the hard goods procurement, which is a substantial part of the military, is the materials allocations. That will have more effect on it than any other single factor.

Mr. STAATS. If I might add this: The actual procurement schedules have to be approved by Mr. Wilson. That is the real legal control that you have as to the spread which will be made of this available obligational authority in terms of expenditures.

Representative HERTER. Generally speaking, has not Mr. Wilson's philosophy been to expend faster over a shorter period of time, with the Defense Department feeling that they should spend less over a longer period of time?

Mr. STAATS. That is not my understanding, sir.

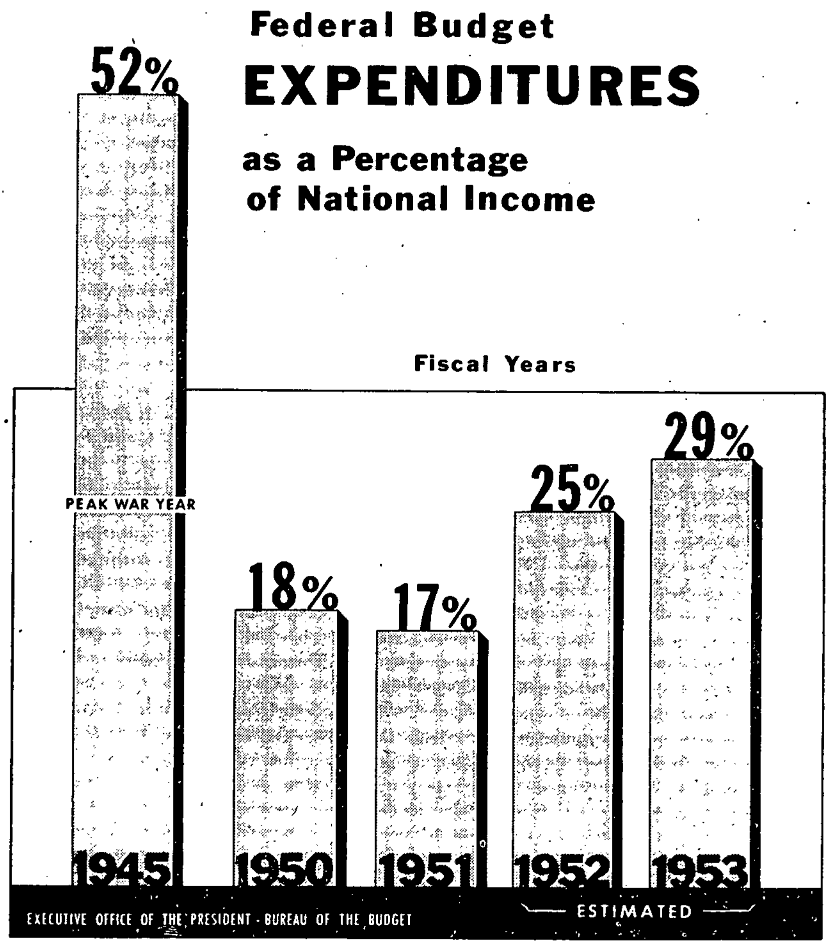
Mr. LAWTON. No, the concept that the last budget and this budget are based on is to maintain a mobilization base in being without undue peaking in any particular part of that curve of the production rate. Instead of going up sharply and cutting right back, that production goes up on a more gradual basis extended over a somewhat longer period, but production lines are running that are capable of expansion to meet any sudden greater need. In other words, from a production line, going at a slightly increasing rate we can move upward much more rapidly than from one that has been cut back or curtailed.

The CHAIRMAN. Well, now, Mr. Lawton, I am sorry to have interrupted the orderly presentation of your testimony in the manner in which you planned it, but I think that this preliminary discussion has served to illuminate the subject, and we will be glad to have you proceed as you had planned.

Mr. LAWTON. Well, actually, Mr. Chairman, we have covered a great many of the things that I had in here.

The Government program, as reflected in the 1953 budget, is probably the largest single factor affecting economic activity currently and for the next few years. This chart (Federal Budget Expenditures as a Percentage of National Income) gives a very rough measure of the relative importance of the Government program in the national economy. For the fiscal year 1953, budget expenditures are estimated at about 29 percent of the national income. This compares with about 18 percent in 1950, the fiscal year which ended a few days after the attack on Korea. It is much lower in comparison to national income than in 1945, when Federal spending was equal to 52 percent of the national income.

(The chart entitled "Federal Budget Expenditures as a Percentage of National Income" is as follows:)



The change in the deficit or the surplus ordinarily means corresponding changes in the inflationary or deflationary impact of the program. What we do to close this $14 billion gap between receipts and expenditures in the fiscal year 1953 will be very important for our economic stability. About $4 billion of this budget deficit can be financed by selling bonds to the trust funds.

The President has recommended that Congress enact additional taxes equal to the amount by which last year's legislation fell short of his recommendations.

Unless taxes of this amount are enacted a substantial part of the borrowing required will have to come from the commercial banking system. This means additional credit creation.

With increased taxes and a smaller deficit, however, it would be possible to absorb enough purchasing power through the sale of bonds to individuals and savings institutions to avoid serious inflationary pressures.

Representative HERTER. May I interrupt there? You imply if there were $5 billion less in the deficit taken up by new taxes there could be an absorption of the rest, so there would not be inflationary pressures?

Mr. LAWTON. Enough of it; not all of it.

Representative HERTER. But in effect that is what you are saying. But if we put $5 billion more in taxes we need not worry too much, because you think that you can absorb the rest of the inflationary pressure.

Would not exactly the same result be achieved if you took $5 billion off of expenditures?

Mr. LAWTON. Sure.

Senator TAFT. Mr. Lawton, going back for a moment to that chart, you had 29 percent. Do you figure State and local around 7 percent, that is, of national income—and is the total then 36 percent?

Mr. LAWTON. I do not have the State and local figures here.

Senator TAFT. I use the figure 7 or 8 percent. Those expenses are also steadily going up. Probably, in proportion to the increase in national income.

Mr. STAATS. It was running above $20 billion last year.

Senator TAFT. Yes; I think that is it.

Mr. LAWTON. That would be about right.

Senator TAFT. That would make it about 7 percent, making total Government expenditures above 36 percent, then, of the national income?

Mr. LAWTON. That is right.

Senator TAFT. This $85 billion is very close to what the Budget Bureau informally estimated for us about 6 months ago, although probably there have been changes.

Have you a guess on 1954? Have we now postponed the peak, so that 1954 will still be 85?

Mr. LAWTON. It will be at least as high as this year.

Senator TAFT. Mr. Wilson testified before the Finance Committee last year, and he had a peak in 1953, beginning to fall off in 1954. Now, the whole thing has been shoved back a bit, I would judge.

Do you think that 1954 will be at least 85 again; is that right?

Mr. LAWTON. That is right.

Senator TAFT. Under the present program?

Mr. LAWTON. Yes.

Senator TAFT. Would it then begin to come off or not?

Mr. LAWTON. Presently we think it will begin to tail off toward the end of 1954.

Senator TAFT. It will be less in the next year?

Mr. STAATS. If you do not get any serious slippage in schedules, the present plan starts tailing off then.

Senator TAFT. There is one other estimate I have seen. I do not have it available here.

Savings this year, since February, have been at the rate of $20 billion a year. I do not know just what savings those are, whether that is individual or corporate savings, and everything else. The estimate is about $20 billion.

How do you happen to put this $5 billion of taxes in the peculiar situation where you cannot reach real savings for $14 billion, and you can reach real savings for $10 billion deficit? How do you reach that conclusion?

Mr. LAWTON. The first thing, of course, is that bonds sold to trust funds come out when we are talking about $10 billion.

The assumption we have made is based on the savings estimates that we have seen. New purchases have been less than redemption of savings bonds. Sales of types of bonds usually held by individual investors are not moving very rapidly upward. We feel that there is not much greater margin to increase those. We think that when we get much above $5 billion commercial bank borrowing will be necessary.

Senator TAFT. That is a guess, an estimate.

Mr. LAWTON. An estimate.

Senator TAFT. Yes.

There is one other thing. Why do you think $5 billion more taxes will not be inflationary?

Senator FLANDERS. We had a long discussion of that yesterday.

Senator TAFT. I was not here.

Senator FLANDERS. The Council of Economic Advisers made a pretty good case for most taxes not being inflationary. Of course, the fact to the extent they are in lieu of bank borrowing, they are anti-inflationary. That is the real thing.

Senator TAFT. But the real question is that they come out of the standard of living of the people, and the moment you decrease the standard the demand for increased wages is more than sufficient to take it up at the present time.

Senator FLANDERS. We pressed that point yesterday.

Senator TAFT. I do not see any reason to think that is not as inflationary as anything else.

Representative MCKINNON. There were no changes in conviction.

Senator TAFT. I have had four cases of manufacturers, at least, where the labor people have already demanded increases to take care of the taxes that we levied, that is, the additional taxes that we levied on income last year.

If we levy them on excises or in any other way, they increase prices, and that is going to be met. In fact, the theory of the Stabilization Board is apparently that it shall be met—I do not suppose, perhaps, that they are going to meet direct income-tax increases that way, they are not proposing that—but apparently the theory is that the increase in cost of living resulting from increased excises is to be reflected in increased wages. That is the present thought.

Other taxes of that kind are certainly inflationary.

I do not quite see why borrowing money up to a point—there is a point there, I agree, where borrowing the money from real savings is not less inflationary than increased taxes.

Mr. LAWTON. It is a question of judgment.

We have followed the advice generally of the Council of Economic Advisers and the Treasury Department for the tax program in the budget. As you know, the taxation estimates are made by the Treasury.

Senator TAFT. As to these estimates of taxes, $71 billion in the budget, which is very much higher than the Treasury estimated when we passed this bill, 5 or 6 billion—is that due to an increase in national income—on what basis is this $71 billion calculated—on what basis of national income is it calculated?

Mr. LAWTON. It is based on calendar year 1952 personal income of $265 billion and corporation profits before taxes of $46 billion. That represents national income for the fiscal year 1952 between $280 and $285 billion, and in the fiscal year 1953 between $295 and $300 billion.

Senator BENTON. If I may suggest, I don't understand what you said in answer to Senator Taft's question.

Mr. LAWTON. The Senator asked me on what basis of national income was this estimated.

Senator TAFT. $71 billion taxes, which is $5 or $6 billion more than the Treasury told us we would get.

Senator BENTON. Is it the higher national income?

Mr. LAWTON. Yes.

Senator BENTON. The whole thing is on the higher income, the whole $6 billion difference?

Mr. LAWTON. I think it is largely on income.

Senator SPARKMAN. May I ask a question there?

Senator TAFT. I realize Mr. Lawton is not the expert on taxes. I was trying to get a picture in my mind.

Senator SPARKMAN. Do you say that is between $295 and $300 billion.

Mr. LAWTON. That is right.

Senator SPARKMAN. Twenty-nine percent of $300 billion would be $87 billion. I am just going by this chart you show for 1953. It is estimated that 29 percent—that is expenditures rather than revenue. I am sorry.

Mr. LAWTON. Of the $85.4 billion of total budget expenditures——

The CHAIRMAN. Before you go to that, what assumption of price levels did you make?

Mr. LAWTON. July 1951 prices were the basis on which we estimated—a continuation of July 1951 price level.

The CHAIRMAN. How was this estimate reached? Was it in conjunction with the Council of Economic Advisers and the Treasury or was it a Bureau of the Budget estimate?

Mr. LAWTON. The taxation estimate was a Treasury estimate.

The CHAIRMAN. The receipts, therefore, were also Treasury estimates?

Mr. LAWTON. That is right.

The CHAIRMAN. That was the basis of the chart which shows Federal budget receipts and expenditures?

Mr. LAWTON. That is correct.

Mr. ENSLEY. Does that mean the Treasury in estimating receipts used the same assumption with respect to national income, personal income, and corporate profits and price levels and wage assumptions as you people in the Bureau of the Budget did with respect to the expenditures side of the budget?

Mr. LAWTON. On the expenditures side of the budget the primary problem we had was with the price levels. The others relatively don't affect the expenditure side nearly as much as they do the receipts side, of course. The estimates were prepared by the agencies in July, August, and September; they were worked on and submitted to us in September or later. July 1951 price levels were used as the assumption for the estimates for 1953.

Senator TAFT. There is some question when people say these expenditures, et cetera—they say that doesn't include the Korean war. The Korean war is to be treated specially. We are to have presentation of estimates the latter part of this year. Do these expenditures, these estimates, include the Korean war?

Mr. LAWTON. In 1952 they do. In 1953 it assures the peacetime attrition rates for the forces in Korea and not wartime attrition rates.

Senator TAFT. For the purpose you are assuming the Korean war will be over for fiscal 1953?

Mr. LAWTON. Yes, in effect.

Senator TAFT. And that there won't be any other?

Mr. LAWTON. That is correct.

Senator BENTON. There was a previous question about the tapering off in late 1954, to which you replied. We asked a question yesterday which I understood you would answer today, and that as to what happened to this missing year in view of Mr. Wilson's testimony last year that this tapering-off process would come in late 1953.

It is increased Air Force expenditures primarily, is it, or what has come in on the expenditure side to have us go by a year and still be about the same distance removed, as estimated last May by Mr. Wilson?

Mr. LAWTON. I think Mr. Wilson's estimate was probably based on somewhat different Air Force programs.

Senator BENTON. It is the Air Force?

Mr. LAWTON. And also, on anticipated rates of deliveries that perhaps were a bit higher than was the actual reality, the program has moved back somewhat.

Senator BENTON. Has there been a deliberate intent to spread the program out over a longer period? Is that partly it and partly a stepped-up program?

Mr. LAWTON. I think not so much deliberate intent in the current year's picture.

Senator BENTON. You mean overestimate of how fast we would go?

Mr. LAWTON. Some of the original schedules were just too high, couldn't be realized, because they hadn't been geared one to another with a sufficient degree of interrelationship.

In other words, the various assumptions made by the people that were making each particular schedule——

Senator BENTON. You couldn't get tanks until you had the steel, that kind of thing.

Mr. LAWTON. They didn't take into full account the competing demands for tools and steel, et cetera. They have been reviewing and revising these constantly.

Senator BENTON. How much of these expenditures would you guess, in line with our discussion of yesterday, could be called capital expenditures in the sense that they are plants to put into stockpile and moth balls, and so forth, as against how much of the expenditures are what might be called operational expenditures or for material that is consumable, such even as airplanes and tanks?

Mr. LAWTON. I haven't got the total figures, but, for example, in 1953 in the Department of Defense 49 percent of the $50 billion direct military total is for major procurement and construction.

Senator BENTON. Fifty percent?

Mr. LAWTON. Forty-nine percent, plus nearly all of the end-use items or military end items in the foreign-aid program, nearly all of the $8 billion is also hard goods.

Senator BENTON. So about $33 billion is the figure for last year?

Mr. LAWTON. In 1953.

Senator BENTON. In 1953?

Mr. LAWTON. That is the projection.

Senator BENTON. And the theory is that in 1955 at least, if things go according to our hopes, that particular $33 billion won't be repeated in the budget. I know we can't look ahead in the world crisis to 1955, but that is the general hope and assumption.

If you talk about tapering off, it means we get rid of the $33 billion.

Mr. LAWTON. Not all of it. You always have replacements. It depends entirely on quite a few factors: Your rate of modernization, if you follow a definite rate of modernization——

Senator BENTON. Such savings as you achieve come out of the $33 billion.

Mr. LAWTON. That is the area in which the drop-off occurs.

Senator BENTON. You haven't made an estimate of whether you are talking about half of it. I think the chairman or somebody roughly took $20 billion as an illustration.

The CHAIRMAN. The Council of Economic Advisers made that rough estimate, that after the production plant had been constructed, at the rate of military expenditure amounting to $65 billion, it might be expected to drop off to $45 billion, assuming that the international situation remains the same.

Senator TAFT. There was an estimate of $40 billion to maintain a current army at the new rate of 3,700,000 men, I think, as a permanent figure, $40 billion instead of what would this be—this is 52—total Armed Forces.

Mr. LAWTON. The Armed Forces estimate of expenditures in here is $50 billion for fiscal year 1953.

Senator TAFT. The estimate I saw was, if you got back to three million eight, you would have $40 billion, so that would be a saving of $10 billion.

The CHAIRMAN. It depends on what you are talking about again. The estimate in this budget for appropriation or total military service is 52.4. The estimate for expenditures is 51.2 for 1953.

Senator TAFT. Isn't it true, roughly speaking, that the total program in all its aspects probably takes all that $20 billion of the general budget?

Mr. LAWTON. Of the expenditures?

Senator TAFT. Of the expenditures.

Mr. LAWTON. That is right.

Senator TAFT. I mean you take 51 for the Armed Forces, 8 or 9 for foreign aid, 2 billion nearly for the Atomic Energy Commission. I just meant for a rule of thumb it is fair enough to say that outside of the whole program there is about $20 billion for domestic expenditures. Is that roughly correct?

Mr. LAWTON. That is correct; $65.1 billion for the major national security programs and $20.3 billion for the remainder.

Representative PATMAN. You mean domestic expenditures, Senator Taft, for veterans and things like that?

Senator TAFT. That is right; all the departments.

Representative PATMAN. By the chart here I see military services will get 60 cents out of every dollar in this new budget; international, 13—that is 73; veterans, 5—that is 78; and interest, 7. That is 85. Eighty-five cents out of that dollar will go for military preparedness and cost of the past wars; will it not?

Senator TAFT. Yes. This chart exactly expresses what I had in mind, the major security programs and twenty billion three for everything else.

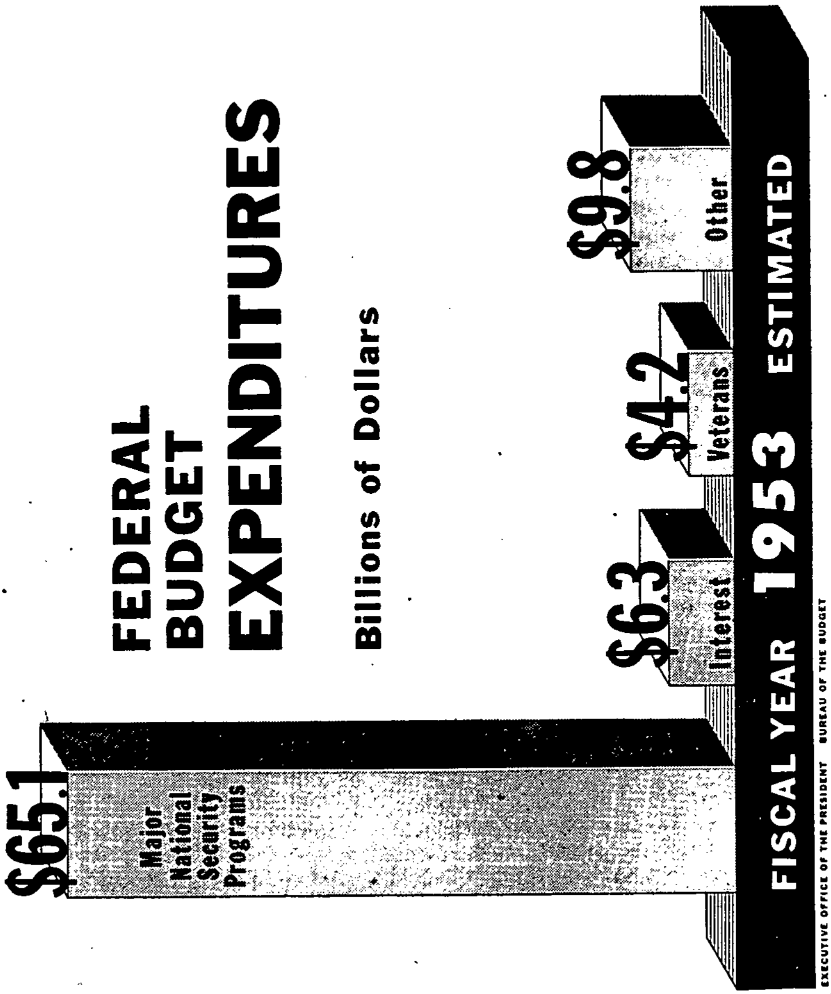
Of the $85.4 billion of total budget expenditures, as this chart shows, $65.1 billion will be for six major national security programs. These include military services, international security and foreign relations, atomic energy, defense production and economic stabilization, civil defense, and maritime activities. Since 1950 this portion of the budget has increased 266 percent.

Of the $20.3 billion in all other programs, $6.3 billion will be for interest and $4.2 billion for veterans' services and benefits. This leaves $9.8 billion for all other activities of the Government. Included in this amount are expenditures for programs which will directly contribute to our national security, although they were not classified with the six major-security programs; for example, expansion of electric power and provision of housing and community facilities for defense workers. It also includes many programs which are essential to the operation of the Government and to the continued growth and strength of the economy, although they cannot be classified as security programs. For example, these programs include costs of enforcing our laws, collecting our taxes, conserving our natural resources, and carrying the mail.

Senator FLANDERS. Mr. Lawton, I would like to inquire about some of the things in the background of the $65.1 billion. Do you feel—well, in the first place, you approached it on the basis of adding up what the separate services asked for—that, having been screened through the Secretary of Defense, it is built up that way or do you feel that there is in the background a logical—I don't know just what the adjective is—a logical strategic structure which assigns to each of the services its place in the whole problem of defense?

Is it a total of aggregates as it finally comes to you, or is it the cost of an integrated program?

Mr. LAWTON. I think, if I might run down through the process, it might establish it a little more clearly on that particular point.



Actually, the initial step is the assessment by the Joint Chiefs of Staff of what the military security demands of the country are, what the problems are that face us, what we need to do to meet them.

Based on that judgment or assay of the situation, they make the assignment of roles and missions to the various services. They also make recommendations as to the number of personnel, number of soldiers, sailors, marines, and airmen necessary to carry out those roles and missions, and assign strengths to each of the services.

Those strengths are submitted to the President for approval. It is from that point that we take off on the development of a budget, the first step being the services' estimates of the material requirements to fit the strength and structure that the Joint Chiefs establish.

Senator FLANDERS. You haven't any way of knowing whether that decision and assignment of functions to the Joint Chiefs is done on a political basis or on an integrated, strategic basis? When I say "political basis," I don't mean Democratic or Republican; I mean the internal politics of the Defense Department, the relationships between the three subdivisions.

Mr. LAWTON. I think, since there is Joint Chiefs of Staff, different viewpoints are brought to bear, since each of the members of that group is the Chief of Staff for the respective service. I wouldn't say that any one of them individually would make exactly the same assignment of structure and role, et cetera. The decision may not reflect the complete opinion of any one of the three, but it represents a composite judgment of the three as to the best assignment of missions among the three services to get the most security for the United States.

Now, it is following up on those, as I say, that the services proceed, the technical services within each of the departments proceed to make the estimates of the costs of maintaining and operating and equipping forces of that kind and of those dimensions.

Those estimates come in to the Secretary of Defense, and in this current year, because of the necessity for compressing the time very greatly between the enactment of this 1952 appropriations and the time that we had to submit the 1953 budget, our staff and the Secretary of Defense's budget staff together conducted a joint review of those programs.

We brought into it Mr. Wilson and his organization, Mr. Fleischmann's organization, particularly the DPA, on the availability of material, the productive capacity, and so forth; and the final results represented a composite judgment of, you might say, the Department of Defense, Bureau of the Budget, and the Office of Defense Mobilization.

Senator FLANDERS. I think the Congress and the citizens of the country need to feel assurance that there is in this enormous sum nothing in the way of horse trading between the departments, and I think that puts in blunt language the questions I am asking.

Mr. LAWTON. I don't believe that is true in this particular case, certainly, because this represents, as Mr. Lovett stated yesterday to the Appropriations Committee, a reduction in material degree below the initial separate service estimates. It washed out in the process approximately 18 to 19 billion dollars of obligational authority.

Senator FLANDERS. May I inquire whether in your position you have seen any evidences of readjustment of over-all strategy due to the experiences of the Korean war, allocation of duties, and so on, as between the three services.

Mr. LAWTON. Well, I would like this off the record.

The CHAIRMAN. Off the record.

(Discussion off the record.)

Senator FLANDERS. I want to say it is clearly in my mind that the Congress and the people have an interest in the size and the nature and the planning of the whole defense set-up, purpose, strategy, and all the rest of it. I have this feeling quite strongly: That the military defense cannot be neglected, the military defense must be carried out on an efficient, effective basis; that it must be carried on, as I said yesterday to the Council of Economic Advisers, on the basis of digging in for a long pull, because I have no confidence whatever that the natural professional way of thinking, which is perfectly proper to the military but which has to be balanced by civilian counterbalance, will ever be satisfied with any scale of military development and expenditure.

It is just in the nature of the case that they should not be. I think we have not yet had—perhaps in the nature of the case we can't—but I would hope Secretary Lovett could give us an outline of the over-all defense plan which didn't reveal restricted information but would give some confidence to us so that we are not in deeper than we need to be.

The CHAIRMAN. That, of course, was precisely what the chairman had in mind in his original invitation.

Senator TAFT. My confidence in the Joint Chiefs of Staff is somewhat upset when I read the testimony of the Chairman of the Joint Chiefs 2 years ago in March where he said in his opinion 15 billion was completely adequate for the security of the United States and that if he recommended $30 billion for the Armed Forces, he ought to be dismissed as Chairman of the Joint Chief of Staff. That is just 2 years ago today. It shakes your confidence as to whether he is right now.

The CHAIRMAN. May I say at this point—I notice that several members have left—let me say that in the Senate the calendar is to be called at 12 o'clock. The Chair has to leave because of a luncheon engagement. It might be we could postpone the discussion now until 2:30 this afternoon, or you may proceed for another half hour. I was going to ask Congressman Patman to take over.

Representative PATMAN. Can you finish in a half hour?

Mr. LAWTON. I can finish this in a shorter time than that.

I think this next part you may be interested in, and I think I can cover it rather quickly. It deals with a number of questions you have been raising.

The military functions of the Department of Defense will have expenditures of $50 billion in 1953. About $11 billion or a little more than one-fifth of this will be for military personnel—for pay, clothing, subsistence, and transportation. This will allow for a slight increase in over-all strength—from 3.6 million men at the end of the current fiscal year to 3.7 million men at the end of the fiscal year 1953. Another $14.5 billion will go for such items as operation and maintenance, the National Guard and the reserve forces, research and development, and retired pay. The remaining $24.5 billion—or 49 percent of the total—will be for major procurement and for construction.

We are building toward an Air Force of 143 wings, an Army of 21 divisions, a Navy with 408 major combatant vessels in the active fleet, and a Marine Corps of 3 divisions, with the supporting elements which are essential for all these services.

In addition to the increased expenditures for our own military programs, an even sharper acceleration is necessary in the military assistance provided to our allies under the Mutual Security Program. About 90 percent of these funds will be spent for hard goods of the same types as those purchased for the Defense Department.

Senator FLANDERS. May I interrupt you, sir? I would like to ask whether those for our European allies and for our own use will come out of the same contracts.

Mr. LAWTON. Largely, yes; not entirely.

Senator FLANDERS. There did develop an abuse on that in which they were placed in separate contracts where they could have been made much more efficiently in the same contract.

Mr. LAWTON. There were some planes, for example, that will come out of separate contracts because we are not building that particular model at this time.

Senator FLANDERS. I mean where they are the same they should be under the same contract.

Mr. LAWTON. Well, if it were a single contract with a single plant for it, yes; but these contracts are divided among several plants. One may take a segment of the requirements.

Senator FLANDERS. That is not in question.

Mr. LAWTON. They come off the same schedule.

Senator FLANDERS. All right.

The CHAIRMAN. Mr. Lawton, I am sorry to interrupt you again, but I have got to leave now and I will turn the meeting over to Congressman Patman as chairman.

I want to hand you a copy of a brief analysis of the expenditures, obligational authority, receipts, and the deficits for the fiscal years 1952 and 1953, as prepared by our staff from the budget in order to have you check it.

I think it is accurate, but it ought to be checked so that it represents the figures as you have sent them up, and then I would like to have it made a part of the record.

(The material referred to follows:)

Federal expenditures, new obligational authority, receipts, and deficits, fiscal years 1952 and 1953

[Amounts in billions]

Item	New obligational authority				Expenditures			
	1952		1953		1952		1953	
	Amount	Percent of total	Amount	Percent of total	Amount	Percent of total	Amount	Percent of total
Expenditures and new obligational authority:								
Major national security programs:								
Military services:								
Air Force defense	$22.1		$20.7		$12.5		$18.9	
Army defense	20.8		14.2		15.0		16.8	
Naval defense	(16.0)		(13.2)		(10.0)		(12.3)	
Aircraft program [1]	4.6		4.3		1.8		3.3	
Other	11.4		8.9		8.2		9.0	
Other military services	2.8		4.3		2.3		3.2	
Total military services	61.7	(66.1)	52.4	(62.2)	39.8	(56.1)	51.2	(60.0)
International security and foreign relations [2]	9.4		8.2		7.2		10.8	
Development and control of atomic energy	1.4		1.3		1.7		1.8	
Promotion of merchant marine	.1		.1		.3		.2	
Other	.7		1.7		.7		1.1	
Total major national security programs	73.3	78.5	63.7	75.6	49.7	70.1	65.1	76.2
Major defense-connected programs:								
Interest on the public debt	5.9		6.2		5.9		6.2	
Veterans' services and benefits	4.4		4.2		5.2		4.2	
Total major defense-connected programs	10.3	11.0	10.4	12.3	11.1	15.7	10.4	12.2
Total major national security and major defense-connected programs	83.6	(89.5)	74.1	(87.9)	60.8	(85.8)	75.5	(88.4)
All other	9.8	10.5	10.2	12.1	10.1	14.2	9.9	11.6
Total expenditures and new obligational authority	93.4	100.0	84.3	100.0	70.9	100.0	85.4	100.0
Receipts					62.7		71.0	
Deficit					8.2		14.4	

[1] Includes operations, but excludes aircraft-carrier program.
[2] Detail for Mutual Security Program will be transmitted later. Appropriation for economic assistance for 1952 was $1.5 billion, of which $1.1 billion was aid to Europe, leaving about $400 million for economic and technical assistance to non-European areas (point 4, GARIOA, Palestine refugees, etc.).

Source: President's Budget for the fiscal year ending June 30, 1953.

I can announce now that Mr. Wilson has agreed to come Saturday morning and we will hold the meeting in the House Caucus Room at 10 o'clock.

Representative PATMAN (presiding). You may proceed, Mr. Lawton.

Mr. LAWTON. For the military and military assistance programs together, expenditures in the fiscal year 1953 are estimated at $58 billion. Of this total, slightly more than half will be spent from funds authorized in 1952 and earlier years.

One significant aspect of the budget this year is that while expenditures for these two programs will rise by about $15 billion over the 1952 level, new obligational authority will decline by about $9 billion. This reflects the fact that with funds already appropriated we expect to reach peak production rates for most major military items by the end of the fiscal year 1953. The exceptions are some of the newer model aircraft and other weapons not yet in production. As I pointed out to you last year, the lead time on much of the military equipment is so long that expenditures may not take place until a year or two after the obligational authority has been granted by the Congress.

You will probably be especially interested in this chart—chart on cash expenditures and deliveries—showing the trend of deliveries and expenditures for military personnel and services and soft goods on the one hand and hard goods and construction on the other hand, for the fiscal years 1951 through 1954. These figures again include not only the expenditures for our own military forces, but also the military assistance portion of the Mutual Security Program.

I should like to call your attention to two features of this chart. First, the relatively small future increases estimated in expenditures for military personnel and services and so-called soft goods. That is beyond the rate we are achieving in 1952. The big increase in these programs came during the past fiscal year as we built up our personnel strength. That is the increase from this point on the chart as we went up to the present military strengths.

Second, the very sharp rise in deliveries and expenditures for hard goods and construction, especially during the current fiscal year, with a continuing rise at a slower rate in 1953 and a slight decline indicated late in 1954. In a program of this size, it should be recognized that a lag or speed-up in anticipated deliveries of hard goods might cause a shift of several billion dollars of expenditures from one year to another. The timing of the increase and of the later possible decrease are, therefore, peculiarly difficult to forecast, but the peak level shown represents our best current judgment.

As soon as mention is made of a peak military production, the question arises as to the long-range cost of our military program on a maintenance and replacement basis. You recognize, of course, that we will not be operating on such a basis as soon as we pass the peak, because procurement of some hard goods, such as aircraft, will still be rising as we build toward 143 wings. The other will be offset by a greater decline in hard-goods expenditures. Even after we complete our build-up, the size of the military budget is almost impossible to predict at this time, because it involves so many military and strategic decisions which cannot now be evaluated.

The level of active military strength will depend on two things: (1) The international situation at the time with the resulting necessity of deploying men in various spots around the world; (2) the possibility of decreasing the number of active forces because of a well-trained Reserve resulting from universal military training and the present rotation policy.

Given an assumption on the level of military strength, personnel costs might be estimated fairly closely. Procurement costs for this strength, however, cannot be estimated as closely for two reasons: (1) The expenditures for fuel, lubricants, spare parts, et cetera, will depend on the extent of use of military equipment, which can vary considerably depending on the duration and type of military training for both active members of the Armed Forces and reservists; (2) the variation of possible costs for modernization and replacement of equipment can be very large. For example, how much shall we spend for modification of ships, planes, and tanks to keep them up to date with the newest technical development, both offensive and defensive, or if we are unable to modify existing equipment, how often will we have to replace it? Obviously expenditures can differ greatly if we replace every 2 years or every 10 years or if new weapons permit economies.

I have emphasized in this statement the military and foreign aid programs and the other major national security programs which account for $65,000,000,000 in expenditures. With respect to the remaining $20,000,000,000 in Government expenditures—or perhaps I should say the remaining $14,000,000,000 after deducting interest payments—we have carefully reviewed these programs not only from the standpoint of the dollar expenditures which they involve but also in terms of the demands they place on the economy for materials.

(The following table gives the data for the unclassified portion of the chart:)

Deliveries and expenditures for the Department of Defense and the Mutual Defense Assistance Program (allocations to Department of Defense)

[In billions]

Item	Fiscal year 1951				Fiscal year 1952	
	First quarter	Second quarter	Third quarter	Fourth quarter	First quarter	Second quarter
Military personnel and services	$1.4	$1.8	$1.7	$2.6	$3.1	$2.9
Soft goods deliveries	.2	.4	.7	1.2	1.2	1.3
Total military personnel and services and soft goods	1.6	2.2	2.4	3.8	4.3	4.2
Total hard goods and construction	.9	1.3	1.6	2.5	3.3	4.4
Total delivery basis	2.5	3.5	4.0	6.3	7.6	8.6
Total expenditure basis (daily Treasury statement)	3.1	4.3	5.4	7.3	8.7	9.6

Mr. LAWTON. At the various stages in the preparation of the 1953 budget, we have reviewed the outlook for the supply of critical materials with the Office of Defense Mobilization and other responsible agencies in all cases where this outlook might materially influence the rate of progress on Federal programs. The expenditure estimates for all such programs—for example, those for Federal power projects, Federal aid to highways, school and hospital construction, housing construction and credit, and maritime ship construction—have been held to levels consistent with the best available guidance we have been able to obtain on the materials outlook.

As I have already indicated, the bulk of the $20 billion in expenditures outside major national security programs represents expenditures for major fixed and continuing charges. The largest of these are interest payments, which are increasing because of the larger debt and higher rates of interest, and veterans' services and benefits, which are decreasing as education and training for World War II veterans under the GI bill rapidly nears completion. Other sizable items, of which public assistance grants are the largest, are not subject to annual budgetary control.

On all going programs which are subject to budgetary control, two primary tests have been applied: (1) Contribution to the defense effort and (2) adequacy of present staff to handle the minimum prospective workload. Increases have been allowed for certain programs contributing directly to the defense effort, although they are not major programs.

In addition to the electric power and the defense housing programs which I already mentioned, these include aid for schools in defense areas, the port security program of the Coast Guard, the internal security program of the FBI, and several smaller programs. In some other cases where the Congress had made arbitrary percentage reductions in the 1952 appropriations, the demonstrated workload made it necessary to recommend at least a partial restoration of the previous cut in order to furnish the minimum level of services required for orderly government. There has also been new legislation—the gambling tax, for example—which will cost the Internal Revenue Bureau a certain number of personnel to enforce.

As the President indicated in the budget message, reductions have been made in programs which could be deferred—for example, in flood control, reclamation, and river and harbor works not involving urgently needed power facilities. Expenditures for rural electrification and rural telephones have been further reduced. All major housing and community development programs, except those in critical defense housing areas, have been held far below the annual levels authorized by the basic legislation. Expenditures for these and many other programs will be considerably less than those which would be clearly justifiable in more normal times.

Senator FLANDERS. I would like to ask one or two more questions, Mr. Chairman.

Representative PATMAN. You may proceed.

Senator FLANDERS. One question I would like to ask is: Do you feel satisfied that the integration of the three services has resulted in any actual economies in administration?

Mr. LAWTON. I think it has in several respects. I think perhaps one of the major economies has been in the consolidation of ocean transport services.

Senator FLANDERS. And air transport also?

Mr. LAWTON. And air transport. In the case of ocean transportation service they are operating under an industrial fund or revolving fund type of operation, and each agency has to pay its own bills to the central operating agency for services rendered.

In other words, where they have to make a direct cash contribution, they are pretty careful about orders for shipments.

Senator FLANDERS. I have heard a criticism to the effect that when we set up the Air Force as a third force instead of having it a part of the Army, we thereupon began to have many different services for the forces in triplicate instead of duplicate, that that actually increased our overhead. Have you any thoughts on that?

Mr. LAWTON. In some cases that is true. We have been working on the consolidation, for example, of medical supply depots. We think there are economies possible in that sort of an operation. Also in joint use of facilities, in certain common use of warehousing.

But, of course, there are certain aspects where it is necessary to have the service and supply facilities available where the deployment is different.

In other words, where you have bases for one force that are nowhere near those of another force, you have got to have the service facilities there.

Senator FLANDERS. And ought not to be those of other forces.

Mr. LAWTON. That is right.

SENATOR FLANDERS. Another criticism that has come to me from contacts of many years' standing with scientists and engineers is the criticism of the expensiveness and disorderliness of research programs. Do you ever hear anything with regard to that?

Mr. LAWTON. Yes, we have. We have attempted and raised the same sort of issue with the Defense Department, and I think they are taking steps to strengthen the hand of the Research and Development Board as an agency of the Secretary of Defense to review the programs of the three services to eliminate any unnecessary duplications between them, to evaluate proposals and projects as to their opportunity for success or for contribution to the defense effort.

I think Mr. Foster, the new Under Secretary of Defense, is going to take a pretty direct interest in the work of the Research and Development Board and make some changes over there, and I believe that there will be an increasing effort to supervise and regulate the expenditure of research funds, which are of considerable volume, over a billion and a half dollars that it is appropriated directly under those heads.

Senator FLANDERS. One other question, and then I am through. Did I hear some remark or have I seen a paragraph somewhere in this material to the effect that there were Atomic Energy appropriations coming in on top of anything here.

Mr. LAWTON. Yes. Last week the President approved the program of the Department of Defense and the Atomic Energy Commission for an expansion of AEC facilities. The initial appropriation will be large. It is being worked out in detail now, but the expenditures will be practically negligible in 1952, and in 1953 they will not affect the expenditure totals that we have estimated here to any appreciable extent certainly, because a great many of the materials and equipment that will be needed in the construction of those will have to come out of other programs.

If they receive the priorities, and we are going to move ahead with them, they will be competitive with programs that are in this budget for materials, particularly those that are extremely scarce. It would be competitive for nickel, copper, stainless steel, and in that competition something else in here is going to have to give. For that reason we don't anticipate there will be a change in the over-all total.

Senator FLANDERS. That is good news.

Mr. Chairman, I said I was through. I find I am not.

Representative PATMAN. Go right ahead.

Senator FLANDERS. I want to make one more suggestion, and that is that the Congress tell the administration through the Bureau of the Budget how much money we are going to raise and ask you to keep within it. Do you have any comments on that proposal?

Mr. LAWTON. Well, are you referring to the Coudert resolution?

Senator FLANDERS. I am referring to the Coudert resolution, but it is a matter on which I have corresponded with some of my associates before Mr. Coudert put it in; so that it was not a new idea to me. It ties in in my mind with a conviction that on the broad scale of our total effort we are putting too much into the military end of it. We have military containment, economic containment, and then my own specialty is moral containment, which doesn't cost much, but which counterbalances the psychological effort of the Russians where they have had their greatest success.

I think we had better use some brains in place of a few billions of the money that we are spending. Maybe brains are the equivalent of money. I am not sure, but it sometimes happens that way.

In pursuing those thoughts—and I have expressed them often on the floor of the Senate—in pursuing those thoughts the question was how to get the military people to reduce their expenditures and the straight way seemed to be the Coudert way. That goes right to the point; it is unequivocal, it is direct, it is not devious, and what would happen to your shop if those proposals were put into legislation?

Mr. LAWTON. I will be more unpopular than I am now. Actually, that is a very broad delegation of authority that is in that Coudert resolution, and it is so broad that it reminds me somewhat of Justice Cardozo's remark in the Schechter case when the NRA was wiped off the books—that it was a delegation running riot.

In this case the bill provides for a maximum of $54 billion of new obligational outlay. If Congress provides more than that, the Congress ought to cut some place else. But if it doesn't, the President should trim it.

Now, that seems to me a complete delegation of appropriating power without any standard to guide it except one total.

Senator FLANDERS. Historically, however, it follows the pattern by which parliaments and legislative bodies have been developed. The power of the purse strengthened the Parliaments throughout the whole course of English history. That was its weapon. You, sir, are a valuable adjunct to the administrative set-up as a whole. The establishment of your body represents an advance in fiscal policy and fiscal management, but I don't think that the legislative body is to be—it must be expected that we shall be interested in totals.

Mr. LAWTON. I think, Senator, my real point is this: Unless you wipe out the rest of the Government completely, if you are talking of removing the $14 billion difference between the $85.4 billion of expenditures and the $71.0 billion of receipts, the bulk of any reduction in expenditures will have to come out of the military or the security programs.

I think that is a responsibility that must be shared by the elected representatives of the people, because you are dealing with the question of national security. I think to say, "Produce something that you may not believe in and give it to us and let us enact that" is, if you will, an avoidance of responsibility that Congress must assume.

Senator FLANDERS. That goes directly to my primary concern, which is that of whether we cannot get the maximum degree of safety vis-à-vis the Soviet power by depending more heavily on certain other things for which I think we have blind spots.

But that is nothing with which I want to take up your time or our time this morning.

Mr. LAWTON. I think in this particular area it is more peculiarly a constitutional responsibility of Congress—the power to raise armies, and so forth, common defense; it is directly in the Constitution as a responsibility of Congress.

Last year, if you remember, the attempt was not to cut down the military but there was some attempt made to up it $5 billion.

Senator FLANDERS. The thing that I think we need is what I hoped to have had from Secretary Lovett, testimony which I possibly may be able to hear, and it is to get some notion of the over-all plan or strategy as it fits into—well, there is the military, the economic, and the moral containment of Russia, and some satisfaction that the military effort is not disproportionate to the possibilities of the others. That is the thing, in brief.

Mr. Chairman, I am going to quit.

Representative PATMAN. That is all right, Senator. You always ask good, thought-provoking questions, the answers to which are constructive.

Mr. Lawton, I want to commend you for making a very courageous answer. He crowded you into an answer, and you gave him one, to the effect that you felt as though it would be an avoidance by Congress of their responsibility to give you such authority as proposed in this resolution.

I thoroughly agree with the Senator that something should be done in that direction, and I just wonder if it wouldn't be better to have Congress accept the responsibility that it has and just refuse to adjourn Congress until we had a balanced budget. Then Congress itself could pass on the question.

Senator FLANDERS. That is what we do up in the State of Vermont. The Legislature of the State of Vermont does not adjourn until it has provided the funds for the appropriations it has made.

Representative HERTER. We do the same thing in Massachusetts.

Senator FLANDERS. It is preferable provided you keep the appropriations down.

Representative PATMAN. Wouldn't you much prefer that to giving some person the power to change the appropriations after Congress left?

Senator FLANDERS. Can you change these after Congress leaves?

Representative PATMAN. If I understand it right, the Bureau would be required, in order to balance the budget, to take off one place, or off some place else, and not spend as much money as Congress provided. Am I correct about that? I haven't read the Coudert resolution.

Representative HERTER. You would have to rescind——

Mr. LAWTON. Put in reserve or rescind.

Representative HERTER. Suppose Congress itself ordered the cut-down.

Mr. LAWTON. I went through that once on a much smaller scale 2 years ago, and I had to take $550 million out of the budget.

Representative HERTER. I remember that.

Mr. LAWTON. I found out that in practically every instance in somebody's opinion I was wrong.

Representative PATMAN. Would you like to ask any questions, Mr. Herter?

Representative HERTER. I am still awfully puzzled as to the procedure Congress itself would adopt if it tried to cut $5 billion out of the expenditures provided this year. Let's say it comes out of the military and foreign aid. You would have to go through item by item. You probably would make new appropritaions for certain things, while at the same time you would say on such-and-such appropriation you have to slow down on your rate of delivery—string this thing out, cut down one assembly line in those cases where you have four assembly lines operating on a certain product, cut out one—make sure the bills for this don't come in to us until the next fiscal year.

How you would begin to operate on that from a legislative point of view without getting into infinitely greater detail than you got into in the original appropriation, I don't know.

Senator FLANDERS. Still would you not agree that it is within the function of Congress to decide what appropriations the country can safely stand on the long pull?

Representative HERTER. It has nothing to do with the appropriations. They have already been made.

Senator FLANDERS. Wait a minute, let's come back to this nevertheless. The Congress says that we can't raise more than this amount of money safely for the economy and the well-being of the people of the country. It is our judgment that not more than this amount of money annually should be raised. It says that.

Now, how is the Congress going to implement that if it believes that and says it?

Representative HERTER. That is my point. It is a very complicated procedure.

Senator FLANDERS. Supposing that the Congress should decide that that was the case; it is the duty of the Congress in some way to implement its decision.

Representative HERTER. That is right.

Representative PATMAN. Either reduce the appropriations or increase the revenue.

Senator FLANDERS. Yes.

Representative PATMAN. How do you do it in Vermont?

Senator FLANDERS. Out of the appropriations made in this budget, the new obligational authority in the budget for the Department of Defense, about $20 billion will be spent out of that new authority and about $30 billion out of prior years' authorities. So it is 40 percent of the defense spending in 1953 that will be out of appropriations made for 1953.

Representative HERTER. You have an extraordinary—you say you have $74 billion carry-over?

Mr. LAWTON. $72 billion for all agencies.

Representative HERTER. Only 30 of that will be expended in 1953. What was appropriated last year will carry on and on?

Mr. LAWTON. I say that out of the new authorizations you will spend for the Defense Department about $20 billion plus $30 billion out of the carry-over—that comes out of the $60 billion carry-over for the Defense Department.

Representative HERTER. That is a carry-over of $74 billion.

Mr. STAATS. If the Congress appropriated the entire amount requested by the President for the Defense Department for fiscal 1953, that amount plus the carry-over from prior years' appropriations would be $112.1 billion. In that year we estimate roughly $50 billion expenditures.

Your point, as I understand it, is: How do you control that $50 billion?

Representative HERTER. Yes. Congress has nothing to say about it.

Mr. STAATS. I don't know whether this is what you have in mind.

Representative HERTER. If we give you the new appropriations——

Mr. STAATS. Pardon me. I don't know whether this is exactly the idea you had in mind, but Congress did, I think, 2 years ago put into legislation an expenditure control on the Atomic Energy Commission. There are problems involved in that, but that is a possibility of expenditure limitations or expenditure rate limitations authorized by law.

Representative HERTER. They ought to be put in at the time the appropriation is made, because how do the armed services know, how does anybody know what limitation is going to be put on? They go ahead in good faith and let a contract, and presumably here is the money to spend as fast as they want to.

Mr. LAWTON. I think you have a law on the books that provides for that; the Legislative Reorganization Act has something of that nature in it.

Representative HERTER. The moment an appropriation is made to a Government department, the Government department is at liberty to spend it as fast as it knows how. There has been an element of haste in this whole thing. Presumably they know at the time they ask for that money that they can't spend it all at once.

Mr. LAWTON. I think it has been made perfectly clear in requesting those funds that they were not for expenditure in the current year.

Representative HERTER. When you say that the only limiting factor in this is the allocation of materials, the allocation of materials is an absolutely arbitrary factor in which you can cut down civilian production of automobiles, for example, and increase the allocation to these other things.

That is a human factor, somebody makes up their minds on that. We have nothing to say about the division of raw materials between the civilian economy and the military economy.

Mr. LAWTON. That depends entirely on whether you can place new contracts for particular types of goods you want in existing plants without retooling, without redoing the production line, et cetera, which are all delays.

One of our problems is shortage of machine tools. That has held this program back from some of the original schedules. Now, regardless of what you do with the allocation of materials, unless the man has tools to fabricate those materials, he has to wait, and you won't get the expenditure until he has the tools.

Representative HERTER. We could have gone much faster than we had if we had been in total war; isn't that right?

Mr. LAWTON. Yes.

Representative PATMAN. Excuse me a moment, please. Senator Flanders must leave, and I would like to suggest that our committee consider making recommendations to Congress as to how we should proceed as a Congress in the event we appropriate more money than we have money to pay out.

Representative HERTER. Not appropriate more money unless we are faced with expenditures which the administrative side of the Government says they are going to make.

Representative PATMAN. Our committee possibly has a responsibility there to recommend how Congress should proceed in order to have a balanced budget. In other words, should we have a joint committee get together with the Budget and make recommendations to cut down here and there. If the two Houses approve it, it is adopted, and if they don't approve it the committee would have to go back and start anew.

That is just thinking out loud, giving an example of what might be done to recommend to Congress. What do you suggest about that, Senator Flanders?

Senator FLANDERS. I think we have a responsibility for the general economic condition of the country. That affects the specific considerations we are charged with: that of employment and production and general well-being.

How that should be implemented, I am not sure, but I am quite sure we should have a meeting in which we can consider how we should get at this question of balancing expenditures and of the relations between authorization and expenditure and income and all of the rest of it.

In other words, I think it is within our field.

Representative PATMAN. And we should give consideration to it.

Senator FLANDERS. Yes. How far we would get with the committees specifically charged with the elements of that thing, I don't know.

Representative PATMAN. I am not bringing this up to try to establish a policy now; certainly I would not in view of the absence of the chairman, but I am bringing it up so that when we have a full committee meeting we can take it up and see if there is enough support to give it further consideration.

Representative HERTER. I fully concur with Mr. Lawton's statement that we ought not to dump the baby in the Bureau of the Budget's lap.

Representative PATMAN. That is right. I wonder, Mr. Lawton, if you would be kind enough to furnish the committee with detailed information on budget expenditures which are uncontrollable in any one year.

(The material referred to appears at the end of the hearings, p. 467.)

Are there any further questions, gentlemen?

Thank you very kindly, Mr. Lawton.

The committee will stand adjourned until 10 o'clock tomorrow morning, in room 362, the caucus room of the House of Representatives.

(Whereupon, at 12:35 p. m., the joint committee recessed to reconvene at 10 a. m. Friday, January 25, 1952, in room 362, the caucus room of the House of Representatives.)

JANUARY 1952 ECONOMIC REPORT OF THE PRESIDENT

FRIDAY, JANUARY 25, 1952

CONGRESS OF THE UNITED STATES,
JOINT COMMITTEE ON THE ECONOMIC REPORT,
Washington, D. C.

The joint committee met, pursuant to call, at 10:25 a. m., in room 362, Old House Office Building, Senator Joseph C. O'Mahoney (chairman) presiding.

Present: Senators O'Mahoney (chairman), Benton; Representatives Patman, McKinnon, Herter, and Boggs.

Also present: Grover W. Ensley, staff director, and John W. Lehman, clerk.

The CHAIRMAN. The committee will come to order.

STATEMENT OF ROGER L. PUTNAM, ADMINISTRATOR, ECONOMIC STABILIZATION AGENCY; ACCOMPANIED BY JAMES McI. HENDERSON, GENERAL COUNSEL

The CHAIRMAN. Mr. Putnam, you are the Administrator of the Economic Stabilization Agency?

Mr. PUTNAM. Yes.

The CHAIRMAN. Would you be good enough to tell the committee, since you have been the successor of Eric Johnston, originally appointed to that position, what you have found the functions of that position to be?

Mr. PUTNAM. The function of the Economic Stabilization Agency, as I see it, is to keep our economy on an even keel while we are going through some very stormy waters as evidenced by the budget you have been discussing.

We have a tremendous amount of additional military spending to do in the next few years. That additional money thrown into our economy, without stabilization controls of all types, could wreck our economy inside, and if we do not keep strong inside there is no use in trying to be strong outside because we couldn't be strong. I think it is a combination approach that we have to take if we are going to keep this world free.

The CHAIRMAN. What is the relation of your agency to the other agencies which have been established under the Defense Production Act?

Mr. PUTNAM. The other control agencies are the Office of Price Stabilization, the Wage Stabilization Board, the Office of Rent Stabilization, the Salary Stabilization Board, and the Railroad and Airline Wage Board. They are all part of the Economic Stabilization Agency.

The CHAIRMAN. And each one of those, however, has an administrator?

Mr. PUTNAM. Has a director or a chairman of its own. My job is to coordinate their efforts so that we make a concerted attack on inflation from all sides.

I have a further job which is to consult with the other departments of the Government, and put the needs of stabilization before them in making their own decisions.

Fiscal policy, credit policy, things of that sort have a great deal of influence on inflation. I have an indirect mandate to use my influence in those areas, as well as in the direct work that is under my responsibility.

Representative PATMAN. In other words, you hold the same position that Chief Justice Vinson held at the beginning of World War II?

Mr. PUTNAM. That is correct.

Representative PATMAN. A comparable position?

Mr. PUTNAM. That is correct; yes.

Justice Byrnes held it even before that, before he moved on up.

The CHAIRMAN. Are there appeals to you from the decisions of the other agencies, for example, from the Office of Price Stabilization?

Mr. PUTNAM. There are not direct appeals as such; that is, there is no legal appeal from a ruling of theirs to me. People do come to me to protest some of the rulings on regulations and I could, of course, overturn them if the situation required it. But, since we work out our policies together, I would not be inclined to overturn their rulings as a normal thing.

There are many indirect appeals, of course. In important decisions, however, the constituent units consult with me first so as to be sure that we are in agreement on economic policy.

That is part of my responsibility, to make sure that we do have a concerted, unified program to combat this very strong pressure that is still to come. We have not hit the worst of the pressures yet.

The CHAIRMAN. Is there any duplication of effort?

Mr. PUTNAM. No, I think not. My own staff is small. That is what I am here for—one of the things is to coordinate the whole agency program and make sure there is not duplication of effort.

The CHAIRMAN. How large a staff do you have?

Mr. PUTNAM. Sixty-nine people, I think, right now.

The CHAIRMAN. What is your relationship with Mr. Wilson?

Mr. PUTNAM. I am under him. I am parallel with Manly Fleischmann, who is the Defense Production Administrator. We administer separate programs under Mr. Wilson. Mr. Fleischmann has the production problems and I have stabilization.

I keep in touch with Mr. Wilson by practically daily conferences of one-half hour, early in the morning usually.

The CHAIRMAN. Then, it is part of your obligation to keep in touch not only with Mr. Wilson but with Mr. Fleischmann; is it?

Mr. PUTNAM. Not as directly as I keep in touch with Mr. Wilson and with my "children"—the five units under me. I do keep in touch with Mr. Fleischmann, too, but less directly.

The CHAIRMAN. From your statement, then, I take it that your chief function is to coordinate the stabilization activities of the Government under the Defense Production Act?

Mr. PUTNAM. That is correct.

The CHAIRMAN. And to do that you keep in touch not only with the subordinate agencies, so to speak, and with Mr. Wilson, the general administrator, but also with other agencies of Government which have some influence upon these activities?

Mr. PUTNAM. That is right. It is somewhat nebulous. It requires a good deal of personal contact to do those things because although we are supposed to try to influence the decisions of other agencies we can not in any way command.

The CHAIRMAN. Our function in this committee, of course, is to report upon the Economic Report of the President. So, we would be very glad to have you now state to the committee your views of the situation as it exists, the strain upon the economy of the expenditures which are proposed to be made for the defense effort and for the general activities of the Government, the capacity of the economy to bear this strain, and what you are doing about it.

Mr. PUTNAM. Of course, as you know, I have only been on the job probably a little less than 60 days; so that I probably qualify as an expert. I probably know more about it now than I will as time goes on, but I have been making just as much study as I can in that time.

I think that, so far, the direct controls have worked very well. They were put on just almost exactly a year ago, and since that time the cost of living and the straight-time hourly wage rates, both of them——

The CHAIRMAN. May I interrupt you to say, Mr. Putnam, that I am not willing to allow your expert status to depend solely upon the 60 days of service. So, I am going to ask you to state for the record what your previous experience was.

Mr. PUTNAM. Well, my experience has been in various directions.

I have been a businessman all of my life. My primary experience has been manufacturing machinery—packaging machinery. I have had some governmental experience, too.

I was mayor of the city of Springfield, Mass., for three terms.

Then, after I got out of the Navy, in the summer of 1944, I joined with Bob Hinckley, and we organized the Office of Contract Settlement, which made the rules for settling contracts.

I was there—or rather, here in Washington—for a year and a half then, and then I went back to Package Machinery Co. and was drafted into this job 2 months ago. So that I have had some experience with Government but not any before this in the field of controlling inflation.

That is a short résumé of what I have done.

Now, going on from there, if I may, to what I think the prospects are, I think inflation is like a balloon. Many cartoons show it that way. When you are pumping pressure into a balloon you have to hold it in all directions. If one side of it is weak, it can blow out on that side.

My responsibility is to administer the so-called direct controls.

The indirect controls are equally important. However, neither kind can do the job alone, in my estimation.

We need a rounded program of both direct and indirect controls to hold this balloon in place. As far as the direct controls are concerned, I think that the record of my predecessor while he was in office shows that they have done very well.

Prices and wages have gone up no more in percentages in the 10 months that we have the figures for so far since controls went into effect than they did during the tight controls of the war. People have sometimes gotten a wrong impression about the effectiveness of the controls, believing perhaps that things are slipping away from us. Actually, they have been operated just as tightly as the tight controls of the war.

Some of that has been, I hope and believe, because of the very great cooperation of the American people. The people have been saving their money instead of rushing in to spend.

I think the controls gave a feeling of confidence—assured the people that they did not have to rush in and buy something before it went any higher.

We know that many items now are in long supply, because people are not buying them as fast as they did before the controls went on.

The CHAIRMAN. How do you know that some items are in long supply?

Mr. PUTNAM. Because they are selling below their ceiling prices, even below pre-Korea prices in some cases—although not much below.

I have checked into the so-called soft areas that we hear so much complaining about, and find very few of them are more than 2 or 3 percent below the pre-Korea prices. But there are some items that are in apparently ample supply at this moment.

The CHAIRMAN. Do you have any statistical inventory information which your organization or any of the subordinate organizations have gathered especially for this point?

Mr. PUTNAM. There is quite a little. I think you could get more of that from Mr. DiSalle, who is coming up here Monday. His organization is the biggest one of my subordinate ones and has the best price statistics. I think he will have quite a little on that. I can get them for you if you want them.

The CHAIRMAN. My question was: Do you have that material available to you?

Mr. PUTNAM. I do have it available to me. I have some of it in here [indicating]. I get his statistical material, but I think he would make a better witness on that than I would. I do not have it in my head. I have it available.

The CHAIRMAN. I have been asking you a lot of questions and preventing you from making a statement which I think you came prepared to discuss. So, suppose we give you the rein and let you tell us what you have in mind, Mr. Putnam.

Mr. PUTNAM. Thank you very much, Senator.

I did not come here with a prepared speech to hand in. I came here to give you what information I had. Answering your questions may be the best way.

I have some things I want to be sure to bring out. I will go ahead and I will be glad to be interrupted.

I have referred to what has happened this past year with the controls and the way things have been held in check. I can go on now to what I think is going to happen, which is, I believe, the most important part of what we are all here to discuss.

This coming year is going to be difficult. It is going to be a very difficult one for inflation controls, because we are going to be pumping into this economy billions upon billions of dollars more for defense purposes than was spent last year. The annual rate of defense spending a year from now will be almost $30 billion more than the rate in the last half of 1950. Let's look at what $30 billion represents—it's more than this country spent in 1950 or 1951 for all consumer durable goods, including automobiles.

The increase in actual defense expenditures in 1952 over 1951 will be somewhere in the neighborhood of $20 billions, and we are adding that whole thing extra into the economy this year. That is a great deal, and that is why I don't think we have seen the full pressure of inflation.

This coming year there are a number of factors at work, some that will be inflationary, some that will not be inflationary, but the biggest thing is the great increase in defense spending. I am not speaking of appropriations. I am speaking of actual money going out into payrolls and into goods and services.

The thing that will help, of course, is that we are also building up our productive capacity. The gross national product is increasing. It is not going to increase by anything like the amount of increased defense expenditures but any increase in supplies removes some of the inflationary pressure. On the other hand, that great spending for defense goes eventually into higher personal incomes which can then be spent for the civilian goods available.

That is why I believe that it is very important still to keep this balloon surrounded by its casing of all sort of controls, including taxation, until this inflationary pressure that we are pumping into it gets up to its peak.

I think it will level off—I believe it will level off within a year to a year and a half. I think then it will be at the maximum pressure. At that time I believe we should very seriously consider—and we should be planning ahead for that time—how best to start decontrolling. I am one of these people who believes that direct—or any—controls on the American economy should be at a very minimum. We shouldn't keep them longer than necessary.

Our economy is a very dynamic one, and you start controlling in one spot, you never know where it will break out in some other spots. At the same time, however, we mustn't throw our guns away at the first lull in the fighting.

The CHAIRMAN. When you speak of decontrols, it is necessary to know within what framework you are thinking of decontrols.

Do you believe that within any foreseeable time the spending for military purposes, for defense and international aid, will fall off to such levels as to make controls unnecessary, and as a corollary, do you think the productive capacity of the United States is going to increase sufficiently to enable it to continue to turn out the things that people want to buy in such quantities as to make controls unnecessary?

Mr. PUTNAM. It is the second part of your question that I believe in wholeheartedly. As to the first part, I am not any authority on international affairs. And I think somewhat that may depend upon what is done behind the iron curtain. I presume we are going to continue with substantial military expenses for a long while. I think that is the assumption that my office has to go on. But we are also building up our production capacity all the time, and I think that the time is coming, and I believe it is in the foreseeable future, when our productive capacity will be built up sufficiently so that we can do both without having to have controls.

And the foreseeable future may be 3 years, or something of that sort. I believe we can begin decontrolling well ahead of that time. I do not think we can begin until we can see the time down the road when one will catch up with the other.

The CHAIRMAN. Do you have any responsibility for the allocation of materials?

Mr. PUTNAM. No, I do not, only in consultation. That power is in the Defense Production Administration.

The CHAIRMAN. Yes, that is right.

Mr. PUTNAM. I can consult with them and hope that we can have allocations of materials in a manner which might be of greater aid to stabilization but that is their primary responsibility.

The CHAIRMAN. And you are speaking primarily of wage and price controls?

Mr. PUTNAM. I am speaking not only of wage and price controls, which are my province, but also of credit controls and other forms of handling the money supply. These are in my province only to the extent that I am authorized to consult and advise on them. The operations of the indirect controls are of course very important to our direct controls programs.

The CHAIRMAN. I interrupted you while you were discussing the increase of the American productive capacity. Will you proceed.

Mr. PUTNAM. That, of course, is not my job directly, but I can watch it happening. It is happening and it is going to continue to happen. I think when our military spending reaches a plateau, as I presume it is going to—perhaps a year to a year and a half from now—that then we will no longer be increasing the inflationary pressure, we will no longer be pumping more air into this balloon. It will be at a static pressure. When that occurs I believe we can then test controls on the outside of the balloon to see what happens, if we relax them here and there. If all goes well we can then head toward a general and complete relaxation.

The thing I do not want to do is to start monkeying with the casing of this balloon while I know we are still pumping more air into it. The pumps will be going for the next year, or year and a half. It is a lot of pressure.

As I said, we are pumping in an additional $20 billion this year. That is twice as much as we spent in 1951 for automobiles, trucks, and parts. We are adding that much pressure into the balloon in this coming year.

That is why I think we must still keep the casing of this stabilization balloon strong and tight to hold it in. That is what I have learned in this relatively short time that I have been here.

We are always looking at our controls, not as fixed and rigid things, however. A balloon is something flexible. All of my associate agencies are, at my suggestion and probably on their own also, feeling that they must constantly test and look at their rules to see if they are still right.

We are not going to be frozen to a rigid concept of any part of our rules. We are trying to make sure that they give the American people what the President says rightly is equality of sacrifice, but what somebody else has characterized as equality of injustice.

As long as the different segments of the economy are treated relatively equally and make relatively equal sacrifices, I think we can do a good job in holding the economy in check.

It is the equality that we must keep looking at all the time.

The CHAIRMAN. Assuming that the international situation continues to demand military expenditures of the kind which has been suggested here at our previous hearings, and it may be appropriate for me to say now that the assumption which has been discussed is to the effect that the mass production machine for military goods will have been completed by the end of 1954 or thereabouts, and that that will mean the peak of military expenditures. Thereafter military spending will be needed solely for the purpose of purchasing the output of this mass production machine, which will mean a reduction of spending since it will no longer require the construction of plant. It was also testified to this committee that an extraordinary amount of the capital which has gone into the expansion of our military productive machine, the plant capacity, has been contributed by private capital under the stimulus of the accelerated depreciation plan and that, therefore, while the peak of military spending may be expected to reach the point of $65 billion plus in 1953 and probably in 1954, if there is no war—it might drop off to $45 billion in succeeding years.

Do you share that point of view?

Mr. PUTNAM. I do. I am not a military expert. I am not a military expert. That is their job.

I think we can start considering and probably actively decontrolling things before we reach that time.

It is not exactly a peak, as I understand it. It is a plateau extending over another year or two. We will get to the top of the plateau in, perhaps, a year to a year and a half from now, and we will stay on that plateau for another year or year and a half, to get to 1954.

I think we may very well be able to start decontrolling when we get up to the plateau and can look at level ground ahead of us, but not now while we still have more climbing to do—if that is a proper simile for our expenditures.

The CHAIRMAN. Is it realistic to talk of decontrols while we see what is going on in the world front, constant pressure of communistic policy to stir up and agitate turbulence in various parts of the world, constant pressure, constant suggestion of aid to Communists in various countries and distant parts of the world, to initiate uprisings and revolutions—is it realistic to assume that within 2 years this thing will pass away and we can go back to an era of normalcy in which we shall have no Government controls and everybody can buy whatever luxuries his heart desires?

Mr. PUTNAM. I do not want to mislead the American public or anyone else, but I am a great optimist.

I have great confidence in the ability of the American people collectively to build up and produce almost anything that is needed.

They cannot do it overnight however. It takes time.

I think we can look forward to the time when people will be able to buy almost anything they want and also have a military defense—that is, if we can keep our economy from toppling over in the interim period. How long that period will be no one can be sure. I should say that a year or a year and a half from now we could begin to consider the decontrols, but I think it would be a great mistake to lead people to feel that it might be done right now.

We have been accused in Washington—I think all of us, in all parts of Washington—of crying "wolf" too soon because the military expenditures did not actually begin chewing up metal and going into wages as quickly as many people thought. We cried "wolf" when the wolf was not actually at the door. But I am sure there are wolves still—plenty of them—running around. We must not throw our guns away until we are out of the woods where the wolves still are. We are not out of those woods yet.

The CHAIRMAN. An increased level of prices has just been announced for lead and zinc, and properly I think, as a stimulus to increased production. And there is pending on the Senate Calendar a measure designed to remove the tariff barrier on lead and zinc, so that supplies from foreign countries may be brought in.

The reason for this action is, of course, that greater quantities of lead and zinc than we are now producing are required in the preparedness campaign. They will continue to be required after the military plant has been completed and we are only purchasing for the production of the implements of war.

The demand, therefore, will continue upon foreign sources of supply as well as for the stimulation of domestic sources of supply.

Abroad we are told the foreign governments complain that our competing with them for these essential materials reacts to drive up the price of such commodities on the world market.

Do you see any end of that in sight?

Mr. PUTNAM. I see no immediate end to a big demand for lead and zinc. Probably the best solution to the competition among the free nations is international agreement on allocations.

The CHAIRMAN. I use those only as examples. There are others.

Mr. PUTNAM. Copper is another one. And, of course, tin. We do not produce tin at all. It is perhaps an even better example of what you referred to. But I have such faith in the inventive ingenuity of the American people that I think we will either find some way to make the existing supply of these metals stretch further to cover our needs, find substitutes, or find some new sources. All of those things are possibilities. We Americans rise to occasions. But there is always a lag and it is during that lag that we have to control things.

I believe completely that in the future we will find ways out of these shortages. We always have. We are a very resourceful and wonderful people.

The CHAIRMAN. Congressman Herter, I believe you desire to ask some questions.

Representative HERTER. I would like to ask a question rather similar to the one that the Chairman asked, but with a rather different twist to it.

When you speak about decontrols you have to accept a certain number of premises that are given to you by other persons of the administration, particularly the military, from the point of view of the sum total of military spending. You have to calculate, as I understand it, the impact of that on our economy and adjust your controls accordingly.

Assuming the plateau, the very picture that you have spoken about which would allow you to decontrol—assuming that that plateau is brought down to a considerably lower level, let us say a level of 5 or 6 or 7 billions below what is now contemplated—a level where your internal and external pressures in Government from a monetary point of view were in balance—would you then feel that you could advocate decontrols and that the remaining controls which are a permanent part of our economy, the indirect controls, fiscal controls, credit controls, et cetera, would be sufficient to take care of the situation?

Mr. PUTNAM. I think that depends on what parts of the economy our plateau comes down on. I mean, controls are in a sense for two reasons. There is the all over reason, which I was speaking of earlier, like a balloon with pressures going into it. In that case you take the total spending. Now the other reason—there are going to be special areas in which certain items may be very scarce and may be bid up. There may be areas in which certain industries are bidding and competing for labor. The economy would still be thrown out of gear if wage rates in those industries went way up and other industries were starved for labor. One would have to look at the picture as it was at that time and not answer completely just by taking total spending.

Totals have a great bearing on inflation, but particular industries and their troubles also have a bearing on the question.

I have not meant to emphasize decontrols as much as I seem to have done, because I do not think we should talk about decontrol for another year or year and a half. Right now we have got to think of how to hold this additional pressure that we all know is coming.

It is not 5 or 6 billion, it is 20 billion more than last year.

Representative HERTER. I understand that. On the other hand, the revenues are going to be very considerably more than that.

Mr. PUTNAM. That is true.

Representative HERTER. As I understand it, the actual imbalance from the point of view of cash intake and outgo is in the nature of 5 to 7 billion, when you include the intake of the trust funds.

Mr. PUTNAM. Certainly, the less that is spent the less the pressures are. There is no question about that, of course. But I would not like to make any categorical answer about how much quicker it would bring the question of decontrols. I think that would depend on where the spending was cut.

Some things would still be very scarce and would perhaps require to be controlled, both pricewise and wagewise. And if you control wages in any area it is pretty hard not to control wages in other areas. You have questions of equity there. When you start decontrolling prices you may quickly run into difficulties with wage controls.

Prices can be decontrolled more selectively and easier, I think, than wages can be decontrolled.

Representative HERTER. That is a very interesting statement, that last one.

Representative PATMAN. Mr. Chairman, I would like to ask the witness something about the price of lead and zinc.

You are not permitted under existing law to use subsidies, are you?

Mr. PUTNAM. Yes, we are permitted to use subsidies. That, again, does not come under me. That comes under Mr. Wilson and Mr. Fleischmann. Subsidies are permitted.

Representative PATMAN. In connection with the price of lead and zinc, are you?

Mr. PUTNAM. No, not yet.

Representative PATMAN. What is the price of lead?

Mr. PUTNAM. One is 17 and the other is 17½, as I remember it, cents a pound.

Representative PATMAN. You mean since the increase or before?

Mr. PUTNAM. I had better consult one of my people and make sure that I am right on that, because I do not want to give you a wrong figure.

It was 17 and 17½ cents before the increase and is 19 and 19½ cents now.

Representative PATMAN. You made an across-the-board increase?

Mr. PUTNAM. An across-the-board increase, yes.

Representative PATMAN. Do you not have a lot of what you might call marginal high-cost producers?

Mr. PUTNAM. There are such.

Representative PATMAN. Do you not have some low-cost producers?

Mr. PUTNAM. Most of the problem with lead and zinc, however, was the foreign supply rather than domestic.

Representative PATMAN. I am talking about the domestic supply. It occurs to me that that is one place where subsidies are thoroughly justified from the standpoint of national defense and the economy of the Nation. I know that during World War II subsidies were used particularly on copper. I am just giving this for the purpose of illustration and not trying to be accurate. Instead of increasing all copper producers, that is, their price from 12 to 24 cents a pound, the Government gave the high-cost producers a 12-cent subsidy and in that way got the benefit of maximum production from the high-cost producers without increasing the price to the low-cost producers. And in that way on copper and other metals, considering the increase, I suspect that the Government saved billions of dollars in the national defense program.

I wonder if you have given consideration to the use of subsidies to high-cost producers in the case of lead and zinc?

Mr. PUTNAM. That increase of 2 cents took place before I took office, but I know that the question of subsidies is very much under consideration.

Representative PATMAN. I mean, was it considered before the increase? You see, the point I am trying to make is that instead of making an across-the-board increase of 2 cents a pound on lead and zinc, why give it to the companies that did not need it who were already making a good profit; why not increase through subsidies the price to high-cost producers?

I just wondered if your organization considered that before authorizing an across-the-board increase of 2 cents a pound.

Mr. PUTNAM. Let me explain this a little. That is really the Defense Production Administration's primary function. It is their function to get the metal.

Representative PATMAN. But the price is under you.

Mr. PUTNAM. The price is under me.

There is always in any case like this perhaps a compromise between agencies. My agency agrees generally with you on the value of using subsidies in appropriate cases.

Representative PATMAN. Wait just a minute. The price—you have complete control of that, do you not?

Mr. PUTNAM. Not completely. If Mr. Wilson feels that production incentive is more important than price considerations, why, he can overrule me.

Representative PATMAN. The information I am trying to get is, Was that question actually considered?

Mr. PUTNAM. It was considered, sir, I know. It was before I came. That price was decided before I took office. So I was not myself in on the consideration of it.

Representative PATMAN. Now, then, since you have just entered the picture, are you going to make sure in the future that in the consideration of the price increase on metals consideration is given of using subsidies instead of an arbitrary across-the-board increase?

Mr. PUTNAM. I can assure you that it will. I feel that in most cases that will save the American economy a great deal, just as you pointed out. I will make sure that it is considered in any case of the sort.

The CHAIRMAN. This recent increase of price for lead and zinc which I mentioned a few moments ago was announced within the last 2 or 3 days, was it not?

Mr. PUTNAM. The one just this moment is, I believe, a Capehart increase reflecting additional costs. I am not up to date on that.

Representative PATMAN. I did not get that answer.

Mr. PUTNAM. I called it a Capehart increase. It was, I believe, an increase to cover higher costs of production up to last July 26.

The CHAIRMAN. The witness means that it was an increase that was required by reason of the provision of law written into the Defense Production Act at the last session.

Mr. PUTNAM. Thank you for explaining that. That is a word of art in our Administration. We speak of a Capehart increase, meaning an increase required by the so-called Capehart amendment to the Defense Production Act of last year.

However, my counsel advises me that I am not completely accurate on that. It was not strictly a Capehart increase. The 2-cents-a-pound increase was to get out more production. Then we had to allow some increases to manufacturers to overcome increases in costs and from that standpoint it was similar to the Capehart principle. I do not want to malign the Senator from Indiana by getting that wrong on the record. It was not strictly a Capehart increase in this case.

The CHAIRMAN. Well, now, if it were based upon increases of cost the question still remains, as asked by Congressman Patman. Was it made straight across the board, regardless of the differences in cost of the various producers of these commodities?

Mr. PUTNAM. I better check on that. In the future I am going to see to it that the suggestion Congressman Patman spoke of is considered. I have already started on this with copper at this moment. I agree it is often a much cheaper way to keep the economy in balance—to use subsidies for a small amount than an over-all increase for the whole amount. It depends on the amounts involved. Those questions will be very much considered by me and my office in this metal situation.

The CHAIRMAN. Has any decision been reached yet with respect to them?

Mr. PUTNAM. The copper situation is very much in front of us now. Mr. Wilson has just announced that no increase in copper prices is necessary and none is contemplated. Some marginal high-cost copper mines are now being kept in operation through a form of subsidies rather than by an over-all increase.

Representative PATMAN. I do not want the word "subsidy" used loosely in connection with my remarks. I had reference to the use of a subsidy to increase production of critical metals.

Mr. PUTNAM. Yes, I had that, too. That is what I understood you to mean—that is, critical metals and the extra production from marginal producers. My remarks were directed to the same thing.

(The following letter was received by the chairman for inclusion in the record at this point:)

ECONOMIC STABILIZATION AGENCY,
Washington 25, D. C.

Hon. JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
United States Senate, Washington, D. C.

DEAR SENATOR O'MAHONEY: When I appeared before your committee on January 25 I said I would want to check further into OPS price actions on lead and zinc to make sure I had given you proper information. I find now that whereas I was discussing two previous price actions on lead and zinc, the members of the committee apparently were referring to a third one which had just been announced in that morning's newspapers.

This is the chronology of the price actions in lead and zinc:

1. On October 2, 1951, OPS issued a price regulation (GCPR, SR 70) raising the domestic price ceiling for refined pig lead and slab zinc 2 cents a pound—from 17 and 17½ cents, respectively, to 19 and 19½ cents. These increases were put into effect at the request of the Office of Defense Mobilization.

2. As a result of these increases in the primary metals, OPS subsequently found it necessary to raise the ceiling price for some products which have lead and zinc as their primary raw materials. These actions were taken in order to assure fair and equitable ceilings to manufacturers whose raw material costs had risen substantially. They were not done under the Capehart amendment but rather under other provisions of the law requiring fair and equitable price ceilings.

3. On January 25, 1952—on the morning I appeared before your committee—OPS made public a revision of the October 2 regulation extending to lead and zinc ores and concentrates the increases previously allowed for the refined metals. This action in no way affects the prices of the refined metals but merely makes sure that the increased prices already allowed for the refined metals were reflected in higher prices at the mine level. As you know, most refiners mine their own ores. The January 25 order was designed to make sure all lead and zinc mined in this country was covered by the October 2 order.

From this chronology it can be seen that the basic decision to increase refined lead and zinc prices across the board was made some time ago, and that this in turn required a partial pass-through of the higher costs in the prices of manufacturers using lead and zinc as their primary raw materials.

For the reasoning behind the decision to grant an across-the-board increase in domestic lead and zinc price ceilings, I enclose a copy of a statement issued on September 30 by Mr. Charles E. Wilson, Director of the Office of Defense Mobilization.

Sincerely yours,

ROGER L. PUTNAM, *Administrator.*

[Press release, September 30, 1951]

EXECUTIVE OFFICE OF THE PRESIDENT

OFFICE OF DEFENSE MOBILIZATION

Washington 25, D. C.

Charles E. Wilson, Director of the Office of Defense Mobilization, announced today a broad program designed to assure essential supplies of lead and zinc at stable and reasonable prices. This program will involve immediate action by the Government agencies responsible for price control, production, and procurement.

As an immediate and first step in the broader program, the Office of Price Stabilization is issuing a control order setting ceiling prices on domestic and imported lead and zinc. The order sets a ceiling at 19½ cents per pound for imported zinc and 19 cents for imported lead. The order also provides for an increase of 2 cents per pound over the existing domestic ceilings, and this, with the exception of a small portion of the domestic production, will result in domestic ceilings identical with import ceilings. (On imports the ceiling will be applied on the basis of delivered price before duty.) The new prices are substantially lower than current world market prices, including prices currently being paid by consumers of the United States for much of their imports.

International allocations have already been accepted for zinc. If limiting the requirements of the nations participating in the International Materials Conference to an agreed figure, in line with available world supplies, can be accompanied by price action, a substantial arrest of the inflationary trends in the nonferrous metals may be achieved.

In developing the program, Mr. Wilson emphasized that conversations will be held with other interested countries and that the import prices had been set after an expert assessment of the prices at which foreign lead and zinc would be forthcoming in order to meet essential United States requirements. The domestic prices of lead and zinc have had to be adjusted in the light of increased costs which have limited the possibility of developing some mines and which have retarded production of domestic supplies at existing ceiling prices. It is possible, however, in the judgment of the agencies concerned, to develop an increased volume of lead and zinc through this joint action.

This program has been adopted on the recommendation of the various agencies concerned. The establishment of a ceiling which is somewhat below current world prices involves the calculated risk of some decrease in imports, but, since the ceiling is above present domestic price ceilings, should result in increased domestic production. This action will thus tend to reduce the pressure of United States demand on free world supplies, ease the problems of friendly consuming countries, and make any international allocation arrangement more effective.

It is contemplated that accelerated action will be taken by the Defense Materials Procurement Agency to develop marginal supplies, both at home and abroad, through the necessary contracts where supplies cannot be developed under existing ceilings.

The United States is in an especially favorable position to initiate such action since it is both one of the largest producers and the largest consumer of these materials. Its leadership in cooperation with other nations similarly circumstanced as producers or consumers may prove to be the anchor point for a program of international allocation and stabilization.

It is important to the success of this operation that Congress proceed with a removal of the duties on lead and zinc in legislation presently pending before the appropriate committees.

The CHAIRMAN. Getting back, Mr. Putnam, to this suggestion of decontrols somewhere in the future which, frankly, I regard to be an unrealistic thing——

Mr. PUTMAN. I want the future very clearly kept in mind in that as I talk. I did not want to give anybody a wrong impression that way.

The CHAIRMAN. That is why I am raising the question here. Have you in your shop or in any of these other agencies given any consideration as yet to the criteria which would be set down under which to determine which commodities and what industries would be eligible for decontrol?

Mr. PUTNAM. We have started to do that. We are getting prepared as one should, I think, for any contingency. We have not got any published regulations ready, but we are definitely thinking—trying to think that far in the future. But I do not think it would be well to publish anything of the sort—even if we had it ready—for just the reasons that you and I have both cited. It is well into the future and I do not want to raise people's expectations at this time.

The CHAIRMAN. The President, in his economic report, recommended the continuance of the Defense Production Act for a period of 2 years. I take it, therefore, that in your opinion there is no prospect of decontrol within 2 years?

Mr. PUTNAM. I would hope that within 2 years we could begin to decontrol some areas, but the control powers—many of them—would definitely be needed all during the 2 years, in my opinion.

I hope that before that time comes some decontrol could have been started.

The CHAIRMAN. Have you reached any conclusion as to what areas might be subject to decontrol, or do you think that is something that should not be announced?

Mr. PUTNAM. I think it is not only something that should not be announced, it is something that I do not think I am able to see that far ahead.

Certain areas of the economy are referred to as soft at this moment, but they may not be soft a year from now.

When the pressures have reached the maximum, any areas that are still soft are the ones you would then begin to decontrol. What those would be a year or a year and a half from now, I would hesitate to even try to guess.

And, as you say, even if I thought I was sure, it might not be wise to say so. But I have not myself any definite conclusions.

The CHAIRMAN. Have you personally gone into the establishment of ceilings in depressed industries where a ceiling established is far above the actual market level?

Mr. PUTNAM. I have discussed that problem very much with Mr. DiSalle. I think when he comes here Monday he can talk about it much better. He has been in this from the beginning. I have only come in recently, as you know. I have discussed it with him because I know there is much interest in this matter.

The CHAIRMAN. Have you yourself formed any opinion about that policy?

Mr. PUTNAM. Yes; I have. I have an opinion that it is not wise, even in cases where things are selling way below their ceiling prices, to decontrol the industry. Is anyone yet able to say that there will not be pressures in that section of the economy before this defense spending is over? When anybody can be really sure that there will not be pressure or a wave of fear buying in those areas before the accelerating increase in defense spending is over, then I think it is time to talk about decontrolling them, but not until we can be sure.

I personally do not think we are far enough up that road to look over the plateau yet.

The CHAIRMAN. Has any argument been presented to you from any industry that if controls were lifted in that particular industry prices would go down; have you heard such an argument?

Mr. PUTNAM. No. I have heard the other argument from the depressed industries that if controls were lifted depressed prices might go up. It has been very hard for me to take that argument very realistically because the prices of a depressed industry are governed by what people are willing to pay, and I am not sure that the simple step of removing the controls would make them willing to pay any more. I found it hard to follow that argument. The argument that if controls were removed prices would go down is even harder to follow. That is new to me.

The CHAIRMAN. Well, if there be a depressed industry and——

Mr. PUTNAM. I feel sure there are. I believe the people who come to me would say so.

The CHAIRMAN. Would it not be part of the function of the Economic Stabilization Agency to adopt policies specifically designed to help that industry? Stabilization means balance.

Mr. PUTNAM. Fair and equitable treatment to all.

The CHAIRMAN. Now here you say that you know of depressed industries, and yet you argue for controls and ceilings on such a depressed industry even though such ceilings may be above the market price.

Is there not something to the argument to establish a roll-back or ceiling upon a depressed industry is to introduce psychological factors that will keep the industry depressed and not stabilize it?

Mr. PUTNAM. There are arguments both ways on that. It is very hard for me to see how the removal of a ceiling that happens to be well above the demand price would increase the demand. I have no feeling that ceilings should be pushed down to a depressed level. They should be at a fair and equitable level. But my reason is not compelled to follow the thought that removing the ceiling will help the industry, although I know many industry people often feel that. But I think that is often the result of a desire to blame something somewhere that they cannot control at all. If they could feel that it is a ceiling that keeps their market low they would much rather talk about that, rather than about a lack of demand.

Representative HERTER. I do not want to put you on the spot in connection with any industry.

As New Englanders you and I know that the textile industry has been operating below ceiling for some time. Has there been any general demand on you by the textile industry to remove controls from a psychological point of view? From a practical point of view they do not mean anything, but from a psychological point of view has there been any pressure?

Mr. PUTNAM. Very little. I have talked to some of my textile friends. They have been in Washington and have seen me. I find them on the whole very, very reasonable about it. They feel that it is not affecting them.

My desire, of course, is to make sure that in the process of maintaining the ceiling they are not subjected to a great many unnecessary calculations and reports and anything of that sort. But I have not found anyone objecting to the principle of ceilings, even though their prices are depressed. They have not come to me with any concerted demand at all.

Representative McKINNON. I think you are familiar, of course, with the fact that if you start edging ceilings up on a rising market you have this entire avalanche of personal savings that we have been accumulating with a good deflationary effect coming in to very great effect upon our market.

Mr. PUTNAM. You have there a point that is very close to my own personal thinking on that. One of the objects of ceilings is to encourage people to continue to save as they have. If the public will cooperate with this whole program as they have in this last year, it will make it possible to hold the pressures down. But, if they get the idea that things are going to start going up again, they may rush in with panic buying, just as they did in the first 7 months after Korea.

That is why I think it is important to keep fair ceilings, not depressed ceilings.

Representative MCKINNON. You mentioned a minute ago your interest and your responsibility in fiscal matters where they affect the stabilization program. This committee during the past couple of days has been discussing the matter of increased taxes, as to whether they would be deflationary or inflationary. It is felt by many that if the tax rate was increased that would have the effect of making the working people come in and demand more money to offset their depleted buying power by increased taxes. I think you as a practical businessman know about that.

What would be your idea in that regard?

Mr. PUTNAM. I start off by saying nobody likes taxes. But I go on from that and say, of course, there is a point of diminishing returns in taxes. I am not expert enough to know where that is. But I think within reason that taxes, properly levied, are deflationary rather than inflationary.

Everybody will want somehow or other to get their taxes back if they are raised, but then, if they are properly apportioned, why, it is still equality of sacrifice. I think up to a point additional taxes are definitely deflationary, not inflationary, in spite of the demand that everybody will have to try to get their taxes paid by somebody else.

Representative MCKINNON. Suppose taxes were raised on the workingman tomorrow and the individual workingman's check was reduced by 2 or 3 dollars a week in take-home pay, would he not be coming back to your Stabilization Agency, through his organizations, would he not be going to the employer and demanding an increase in the pay scale to back up the difference that he felt by the increased tax load?

Mr. PUTNAM. Of course he would. Already they are talking about that now. Corporations are feeling the same way. You hear many of the corporations talk about income being less after taxes. Corporations never like to talk about income before taxes. They always talk about income after taxes.

Everybody tries somehow or other to get somebody else to pay their taxes. They will try. But I think that is where controls come in, too.

Representative MCKINNON. You think your Stabilization Agency would be able to hold the line on wages if they had those pressures put upon them?

Mr. PUTNAM. It depends on how much. Everything depends on degree. If additional taxes should be spread equitably through the whole population and if you can get people to believing that they are getting fair and equal treatment with everyone else, the American people are pretty willing to go along when they think they are treated fairly.

Representative McKINNON. Do you feel that the proposed $5 billion tax increase would be reasonable? Do you think it would be of a degree so that you could hold the line?

Mr. PUTNAM. If spread fairly throughout the various segments of the economy, I believe it would help us to hold the line.

Representative McKINNON. After you have been here 6 months or a year, you will find that nobody believes that any tax bill is fair. They always feel that the other fellow should pay it.

Mr. PUTNAM. Equality of injustice, as somebody said. Everybody feels that way. There is no question about that. Everybody wants to pass their taxes on to somebody else. That is natural. In other words, everybody is human. But I believe that a reasonable increase in taxes of that magnitude fairly spread would be deflationary, on the whole, rather than inflationary. I think it would help us to hold the line rather than hurt.

It would have its difficulties. Any tax bill has its difficulties, but I think it would help.

Representative McKINNON. You believe that $5 billion tax bill passed along to the working people would not increase pressures to such a degree that you could not hold the line on the present wage?

Mr. PUTNAM. Spread fairly throughout the economy. I would not attempt to say where it ought to be put, because I certainly have not made a study of taxation. But spread fairly throughout the economy I think that $5 billion tax raise would be deflationary and, therefore, help my Agency to hold the economy in line.

Representative McKINNON. Getting to another point, in this decentralization movement of mobilization and trying to spread industries throughout the United States, both as a matter of security and a matter of employment, is your Agency consulted in that regard as to how it affects the stabilization of employment?

Mr. PUTNAM. That is not primarily up to my Agency. Mr. Fleischmann and Mr. Wilson primarily watch the unemployment aspects.

Representative McKINNON. Unemployment would have an effect upon stabilization, too, would it not?

Mr. PUTNAM. It has some effect, but basically as applied not to the individual but to the over-all economy. It is in the direction of deflation rather than inflation. It is only in a very indirect way brought to my office. It is primarily a production problem—a problem of using resources properly and making sure that production policies do not unnecessarily cause unemployment when there is need of skilled people. They are trying to move the work to where the people are. That is primarily a Defense Production job rather than an Economic Stabilization job. That is primarily in the hands of Manly Fleischmann.

Representative McKINNON. But the allocation of orders does have a very definite effect upon stabilization.

Mr. PUTNAM. It does have, particularly the allocation of orders to areas where there is too much already. That, again, however, is primarily the Production Agency's job rather than mine. I am, however, interested in this problem, and I am very much interested in using what influence I have to make sure the defense work is spread to the places where it will help relieve unemployment the most rather than to areas where it will increase inflationary pressures unnecessarily. My influence is all in that direction. But the decisions are not my primary responsibility. It is one of the fields where I have influence rather than control.

Representative McKINNON. It is primarily in the hands of Mr. Wilson and Mr. Fleischmann?

Mr. PUTNAM. Mr. Fleischmann primarily. We are all in the hands of Mr. Wilson; Mr. Fleischmann and I are both under him.

Representative PATMAN. Any questions?

Senator BENTON. I would like to comment, Mr. Chairman. I am Senator Benton, Mr. Putnam, a neighbor of yours from New England.

Mr. PUTNAM. I recognize you, Senator.

Senator BENTON. I had the pleasure of recommending you for a previous job before you came down on this one, so, though I have never seen you before, I am sorry I was late this morning and missed the material part of your statement.

I congratulate you on accepting as dirty, onerous, and as tough a job as there is in this town. I am very glad to see you here, and I apologize for missing so much of your statement, which I shall read with interest.

Mr. PUTNAM. I did not bring a written statement, so that, Senator, you haven't missed a great deal.

Senator BENTON. Don't worry; you are embalmed in the type just the same.

Mr. PUTNAM. Thank you very much. I have learned this, Senator, about my job already, and I think it is an important thing for us all to think about. To most of us, what happens to our incomes just now is not inflation. It is a merited increase that we really ought to have gotten 2 years ago, or it is a little extra profit that we got because we were unusually smart. It is only inflation when it happens to the other fellow.

Senator BENTON. Inflation is for the other fellow.

Mr. PUTNAM. Definitely.

Senator BENTON. With all respect to you, the men don't live who are big enough to hold these jobs.

Mr. PUTNAM. I have found that already, so I am the boy that has to prevent people from getting what they think they have deserved for a long time.

Senator BENTON. That's right. That puts it very well.

Representative PATMAN. Have you finished?

Senator BENTON. Yes. I have no questions.

Representative PATMAN. Now, in keeping down inflation, I guess the money supply is the greatest contributing factor toward inflation?

Mr. PUTNAM. It is a very important one, certainly.

Representative PATMAN. What I mean is, too much money——

Mr. PUTNAM. Too much money and too few goods is one way of spelling inflation; yes.

Representative PATMAN. That's right; I agree with you. Do you have any control at all over the supply of money and credit?

Mr. PUTNAM. No. I have some influence, I hope, but no control.

Representative PATMAN. Are you on any of the boards that consider the availability of credit in money?

Mr. PUTNAM. There is an unofficial committee that one of my people has been on. It is pretty nebulous. I am starting to work to see if I can organize something of that sort right now.

I talked to Mr. Martin yesterday, of the Federal Reserve, and suggested that we get together and see if we can't get a committee that may function better, one on which the antiinflation voice can be heard in some of those policies. I am in the process of trying to see if such a committee cannot be organized right now.

Representative PATMAN. Do you have any voice on the voluntary credit committee?

Mr. PUTNAM. No.

Representative PATMAN. You are not consulted about that?

Mr. PUTNAM. No.

Representative PATMAN. But you are trying to arrange some coordination?

Mr. PUTNAM. Yes.

Representative PATMAN. Between your office?

Mr. PUTNAM. I don't mean I am getting resistance. When I said trying to arrange, I did not mean that I was having difficulty in it. I had been doing some other things first, and that is one I just started to work on yesterday. I am working in that direction now to try and have a stabilization given a voice in those fiscal policies.

The CHAIRMAN. How would you like to discuss the general question of the interrelation of wages and prices and the capacity of industry to absorb wage increases and the criteria by which these problems are decided in your shop?

Mr. PUTNAM. Is this an asbestos seat I am sitting on, sir?

Senator O'MAHONEY. It is the seat on which every Member of Congress is sitting all the time.

Mr. PUTNAM. Quite right. That is the most difficult thing there is. There is no question that there is, of course, a close relationship between wages and prices. There has to be a close relationship between wages and prices.

I believe the American economy on the whole has shown that it can absorb, and has over a long period steadily absorbed, a certain amount of wage increases. That is why the standard of living of the ordinary workingman has gone up steadily over the centuries and also over the last 10 years.

His real income measured in goods is continuing to go up, which is proof that industry can absorb a certain amount of wage increases. How much it can absorb depends on the industry. Some industries can absorb quite a lot, some, which are just on a marginal basis, can perhaps absorb none at all.

The standard under which my agency or Mr. DiSalle should force an industry to absorb wage increases is a matter of very close discussion at this moment. My predecessor put out a policy last year called the earning standard which has many things to recommend it. He based it primarily on the criteria of excess profits taxes. If an industry was in line to pay excess profits taxes, it was not in line to get price relief. That is a simplification of his earning standard. It applies not to a company but to an industry, leaving each company within the industry to better itself if it possibly could.

I think there are some faults with that. I have not yet, however, come up with anything that I am convinced is better. Our economists are thinking of it right this minute. That is what I meant earlier when I said I did not want us to freeze any policies into our thinking.

That standard has a connotation of profit control which is, I think, foreign to the American economy. Although it is industry-wide in application and is not an individual company control, I am not completely happy with it. But I haven't found a better one yet.

Now there are particular industries that very definitely have power to absorb certain wage increases. We might just as well name names because I think everybody is thinking of the steel situation at this moment.

I have no idea what recommendations the Wage Board will come up with. It is acting independently of me in this case—they are a fact-finding board for the President. They are not working under me directly in their disputes-settling function, so I have no idea what recommendations they will come up with. But both Mr. DiSalle and I are convinced that the steel industry can absorb a certain amount of any wage increase without coming anywhere near any standard you could give that would entitle them to price relief. They are certainly making a great deal more money than they were pre-Korea, so there is room there for what we call absorptive capacity.

The CHAIRMAN. But you haven't reached the point of having to make a decision upon that question yet?

Mr. PUTNAM. We should not until we have heard all sides on both the price and wage cases. It is a quasi-judicial position that we occupy there, both as to the wage case and the price case. The wage issue is before the Wage Board and the price will come before Mr. DiSalle. I know he will talk with me when they come to bring it up, and I think I should not come to a definite conclusion until I have heard all sides of it. The case should not be prejudged. They should have their day in court. But I will say that the published figures I have seen lead me to believe there is considerable absorptive capacity in that industry.

Representative HERTER. Mr. Chairman, may I ask a question there? I am very much confused as to your legal function in connection with wages. I read this morning, for instance, of the fine that was assessed on a contractor who had paid $3 an hour to bricklayers when $2.75 was the approved wage.

What happens if those same bricklayers go on strike and strike for $3? The man can't go ahead with his work. Finally he gives in to the strike and agrees to pay $3. Who do you fine at that point?

Do you fine the employer? Do you fine the labor union? Do you say, "In our opinion that is an improper thing to have struck for"? Who is held responsible legally and what enforcing powers have you got?

Mr. PUTNAM. There is no law preventing strikes. I think we can start off with that. I think I need my counsel with me to help me a little on this, if you don't mind.

I saw the story you referred to. I know what happened. To begin with, there is, as I say, no law preventing strikes. There is a law giving my agency and delegated by me to the Wage Stabilization Board the right to set standards for wages. They have set a standard and this employer broke the standard by paying more.

What would have happened if they had struck, that is another question. They would have gone on as an ordinary strike, and it might have been certified to this Board as a dispute, the same Board, but the rules of the Board are very definite that $2.75 is the maximum for bricklayers in that area. I don't know whether the man knew the rules or not, but I presume he did. He paid $3 when the ceiling was $2.75.

That is definitely breaking the regulations of the Wage Board. The Wage Board has the right, under the act, you know, to certify the whole wage payment to those people—not just the excess payment—as something that they cannot collect on a Government contract and they could have certified the whole amount to the Internal Revenue Bureau to be disallowed as a business expense. Instead, they certified only the amount of the excess-wage payment to be held back from the contractor and also to be disallowed for tax purposes.

Representative HERTER. You can control only on Government contracts?

Mr. PUTNAM. We can control the payment only on Government contracts. But the tax disallowance can be imposed on any violations. We can certify to the Internal Revenue that they should not be allowed as a deductible expense not only the actual illegal part of the wage payment but the whole payment to these people. They did not do that. They only certified the excess payment, not the total. They could have certified the total wage bill as being not collectible and also not deductible.

Representative HERTER. I understand that, but assuming that a strike takes place for a wage which is in excess of a Wage Board's ruling as being a proper wage, and that is given into by the employer, is the employer the only one who is held responsible?

Mr. PUTNAM. The employer is the one who is making the payment.

Representative HERTER. If he can't get workers otherwise because they are striking, and he can't go ahead with this contract, he is perfectly willing to pay even within the terms of the contract just to get his work done. He does that. Then he is fined, but he has been absolutely helpless because he could not get workmen to operate except at a rate higher than the one that has been approved by the Wage Stabilization Board, then what does the Wage Stabilization Board do?

Mr. PUTNAM. I think that the employer should not have agreed to pay this. He should have said, "We will pay it subject to Wage Stabilization Board approval." That is the only way he should have done it. He could have done that and put the case before the Wage Stabilization Board and then let them judge it on its merits at that time.

Representative HERTER. It is not a question of the union first going to the Wage Stabilization Board and saying, "Are we justified in asking this?"

Mr. PUTNAM. That isn't usual, but if he said, "We will pay it if it is allowed, we will even pay it retroactive if it is allowed," he would have been perfectly all right. He could have even petitioned the Board along with the union.

In most cases that we hear complaints about piercing wage ceilings and pushing wages up, the employer has joined with the union in requesting the Board's approval. Except in the case of disputes submitted to the Board by the parties themselves or by the President, it is seldom that a request comes to the Wage Board to allow a wage increase that both sides haven't agreed to voluntarily. But here he did not even put it up to the Board. He paid it without asking anybody.

Senator BENTON. Can he deduct the $40,000?

Mr. PUTNAM. No. That is the part that we are certifying to the Internal Revenue Bureau. We could have certified that he could not deduct the whole $116,000, I think it was, which was his total wage for bricklayers. We only certified the excess or illegal amount of the payment. That seemed to us the least we could do. This contract was a voluntary agreement, but it wasn't put in for ratification. There was no proviso in there, "We will do this if they allow it." They just did it presumably knowing what the regulations were. It is a fairly big outfit that knows what is going on.

Representative HERTER. One other question. If you allow an increase, let us assume that in a given industry, call it the steel industry or whatever industry you want, there is a dispute that leads to a strike or a threatened strike. The employer agrees finally, whether under duress or not.

Then under the Capehart amendment you are required to give him an increase in price because of an increase in expenses, are you not?

Mr. PUTNAM. The Capehart amendment only gives increases in costs that occurred before July 26, 1951.

Representative HERTER. It does not take in any further increases?

Mr. PUTNAM. Not past July 26.

Representative HERTER. I thought you had to take those into consideration.

Mr. PUTNAM. Nothing past July 26. But the law says elsewhere we have to be fair and equitable. That is the reason we need a standard such as we were talking of earlier—an earning standard or some other standard to insure that price ceilings are fair and equitable when circumstances change.

That is a matter that is under very definite consideration by us right now. Whether there is any better way of applying a fair and equitable standard. If somebody has a really good idea in that direction that is better than the present standard, I would love to have it and consider it.

It is difficult, but we must be fair and equitable, not only because legally we must be but also because we should be. We are serving the American public and we have got to serve them as fairly as possible.

Representative PATMAN. That was one of the compromises in the conference, that July 26, 1951, regulation. At some stage of the proceedings the amendment had no cut-off period, but before it was finally agreed upon, that cut-off date, July 26, 1951, was inserted. That was one of what you might call the major compromises of the conferences between the two Houses.

Mr. PUTNAM. Of course I was not down here and in the thick of that at all, but I had always assumed there was a very good reason for that, aside from the good reason of a compromise, and that was that the original cut-off date used by the OPS in the manufacturers regulation was the month before controls went into effect. That was a month of turmoil economically.

Prices were going this way and that way and some things might have been frozen after they got up and some might have been frozen before they got up. I had always assumed that by July 26 the economy had gotten back pretty much on to an even keel and that was a pretty good cut-off date to make.

I don't know whether that was the fact or not, but, I had assumed that they felt that as of the earlier date things were still in a turmoil, whereas by July 26 things had smoothed down and it was perhaps a fairer place to start from.

Representative PATMAN. I will say this, too! That the conferees were rather groggy about that time. At adjournment, as we walked out of the east side of the Capitol, the sun was rising.

The CHAIRMAN. And the law was expiring.

Representative PATMAN. The law was expiring.

Representative MCKINNON. Mr. Putnam, just so you don't get interpreted wrongly, do I understand you to say that you are endorsing the Capehart amendment as a leveling influence?

Mr. PUTNAM. I did not say that; no. I am glad you gave me a chance to say that.

I said I presume that is why that was done and why that date was arrived at, but I see that 4 o'clock in the morning may have had something else to do with it. No, I do not endorse it. I believe that it has prevented some of the controls from acting as well as they might very well have done. It has caused us a lot of trouble.

The CHAIRMAN. The law will expire again. The President has recommended its continuance. Has your experience in office been sufficient as yet to enable you to formulate your judgment as to what should be in that law to enable the Stablization Agency and the Office of Price Stabilization to control inflation?

Mr. PUTNAM. Yes. I feel first and foremost it should be extended, definitely, and for 2 years, because I think that is as quickly as we can—any of us—envision getting out of these woods.

I think it should be strengthened in about four places very definitely, too. First and foremost I think the credit control authority should be restored—the so-called regulations X and W—the authority to impose selective credit control should be restored. I think that is one of the most important possible amendments. That is one of these so-called indirect anti-inflation controls.

I also think that both the Capehart and the Herlong amendments should be nullified in some way or other if possible. Changing Herlong won't have tremendous effect, since the basic controls over wholesalers and retailers will be under regulations envisioned by the Herlong type of amendment anyway. But I hate putting into the law an absolute freeze and allowing no administrative leeway. I think there are cases where there should be administrative leeway. Then I think that in order to control meat prices and to protect the legitimate producers and packers, we should be restoring some form of slaughter-quota authority. With the demand for beef so high, there is a tremendous black-market tendency. The quota controls were intended to make sure that the legitimate people got the beef, and it wasn't channeled off into the black market. I think Mr. DiSalle can talk much better on that than I, because he has had longer experience.

Senator O'MAHONEY. Perhaps the Secretary of Agriculture might talk better than either of you.

Mr. PUTNAM. Very likely he might, sir. I am not an expert on any of the agricultural matters at all. I know something about industry, but I am learning about agriculture. I have learned a lot, but I haven't learned enough to call myself an expert on that.

The CHAIRMAN. I can speak from experienced observation at least with respect to the meat problem. The factor which to my mind is most possible but to which the least attention is given and has been given in the past by price-control agencies is that cattle are produced by thousands of producers. The production of cattle is utterly different from the production of automobiles. Automobiles are standard production. They are the same in whatever factory they are turned out, if the same model.

The purchaser in California gets the same model as the purchaser in New York or even in New England, but nobody can set a standard for the cattle of California and the cattle of New England or the cattle of even Wyoming. They are all different; so that it is utterly beyond the capacity of a stabilization agency to enforce price control among so many producers when the product is so easy to raise and so easy to dispose of.

You are dealing with human nature in its individual capacity. You would not be able to hire enough people, just as OPA was not able to hire enough people, to prevent the butcher shops of the East becoming empty of meat while the ranches were filled with fat cattle.

Mr. PUTNAM. How do we accomplish what I said earlier was called by some people equality of sacrifice and by some equality of injustice in a case like that?

I agree that the agricultural problem, all of it, seems to me very difficult because you have got so many different producers each deciding individually himself how much he will grow or raise in cattle. The same is true with crops. To me it is very difficult to know the right answers.

The CHAIRMAN. We all must acknowledge it is a very difficult problem.

Mr. PUTNAM. I feel very strongly it is very difficult, and I don't feel that I am sure of the right answers this minute. I would like to see in the law, however, enough tools to cope with the situation adequately, but not tools to be abused.

The CHAIRMAN. Now, it is your judgment that the economy is strong enough to bear the burden of expenditures required by defense, but that it is essential to have the legal authority contained in an improved and amended Defense Production Act to maintain effective controls and stabilization policies in order to prevent inflation?

Mr. PUTNAM. That is my considered judgment, sir; yes. I would add to that one other requirement which you could only help us to have, and that is public cooperation in this whole inflation control.

I think the ordinary housewife can help a great deal if she will not buy things that are expensive and will buy things that are cheap and will not buy anything she does not have to buy. That is even better control than anything else. One of the reasons the law is required is to give her confidence in stable prices so she will not feel she has to rush in and buy unnecessarily.

The CHAIRMAN. One of the important things to accomplish public confidence, it seems to me, is to revise this law if necessary or to revise its administration if necessary, so that we shall not be raising prices by the order of OPS upon the one hand and reducing prices by the order of the same agency upon the other.

Prices are raised for automobiles. Ceilings are lowered for agricultural commodities. Now, it is difficult for the public to understand that contrary movement. I am not talking about the justification that you may have at all. I understand perfectly well the explanation of why the increases have to be made, but the fact seems to be, according to the testimony from your agency and from OPS, that the so-called Capehart amendment is responsible for driving certain prices up, and that in the other area of agricultural prices, where you lower the ceilings, you are acting in the manner in which you would like to act with respect to all production. Am I right?

Mr. PUTNAM. I think you are right in that we would like to keep them at least fair and equitable. The automobile increases, as you know, were in accordance with the law that Congress in its wisdom passed, and we had no choice.

The CHAIRMAN. Or lack of wisdom. I just supplied that.

Mr. PUTNAM. I did not.

The CHAIRMAN. Are there any other questions? Mr. Putnam, are there any other statements that you would like to make?

Mr. PUTNAM. I think you have in your judicious questioning taken from me most of the information that I have. I have no other statements I want to make except to thank all the members of the Committee for your very great courtesy in listening to me and to urge your help in enacting a new law that we can carry on with.

The CHAIRMAN. Mr. Putnam, it occurs to me to raise this question. As I recall it, shortly before he retired as Administrator of the Economic Stabilization Agency, Eric Johnston made an extended trip through Europe for the purpose of getting information with respect to the effect on prices of the economic program, the military expenditure, and the like. Has that information been available to you?

Mr. PUTNAM. That has been available, and a great piece of it was in his final report that he put out just before he left office. It is pretty well covered in that, but all the things he had have been available in my office.

The CHAIRMAN. You had an opportunity to review it?

Mr. PUTNAM. I have gone over it; yes, sir. I have not got it all at my finger tips at this moment.

The CHAIRMAN. Have you formed any personal opinion with respect to the inflationary effect of our military aid abroad?

Mr. PUTNAM. Yes; I have in this way. I think that our military aid abroad is helping. The attempts of our allies to impose their own military spending on their own strained economies—strained much more than ours—that is causing them more inflationary pressures than we have.

Every bit of aid that we can give them—I get this impression from his report and from some other things, too—helps them to manage their own inflationary problems and thus to get along on this common program of defense. Their inflationary problems, particularly in France, are much worse than ours because their economies were more strained to begin with. Trying to add on military preparedness made the pressure worse. Anything we can give to them is a help to them to rearm. I get that impression very definitely.

The CHAIRMAN. I say to you that the primary question to which I am seeking to get a personal answer and to which I know many other Members of Congress are trying to get a satisfactory answer is this: That knowing as we do what the policy of the Kremlin is—namely, to carry on an economic war against the free nations, to create as much turbulence and agitation around the world as possible, to start small wars wherever they can and in the meantime to promote economic distress within the free nations—are we doing the right thing to maintain a strong and sound American economy, since without such a sound economy the free world will have lost its most essential prop?

Mr. PUTNAM. Senator, you are making for me the best speech I have made yet. I have talked in just that sort of language, but you have put it in better words than I have. I feel completely that the job of my agency and my associates is a fundamental part of this war that we are actually engaged in.

We can call it by any name we want, but it is an all-over struggle in which the economic part is as important as the military part. First and foremost, we must maintain a strong economy in this country as the bulwark of the free world. But we must not do it at the expense of ruining our allies, because they are part also of the free world.

We have got to strengthen the whole free world, and we have got to strengthen them economically, which is just as important as strengthening them militarily. If our economy goes to pieces, the Kremlin gets what it wants without having to do anything else.

The CHAIRMAN. History teaches us that military expenditures have always been inflationary, and in the midst of the Second World War, because we recognized that, Congress passed a law granting much more rigid controls than have been extended under the Defense production Act.

We have not attempted rationing, for example, in this preparedness program because we have not planned as yet to devote more than 19 or 20 percent of our gross product to military expenditures. The budget for 1953 raises that percentage from something like 15 or 16 percent, as I recall it, to nearly 20 percent; but, if military expenditures are inflationary here and are inflationary in Europe, is the economic crash which the Kremlin hopes for likely to come from any failure on our part to take the proper steps to maintain our economy?

Mr. PUTNAM. It could. That is why this work, I believe, is so fundamentally important. It is repugnant to me; it is repugnant to control the American economy.

It is not the way I think America wants to live and should live ordinarily. Perhaps one of the reasons we have not done it perfectly and have had confusion is that we are not used to this sort of thing. I hope we never will get used to it. But for a temporary time, while this extra pressure is on us—until we can build up our economy to carry the extra load—we have to have these controls or we could very easily inflate ourselves into bankruptcy here.

I think it is fundamental that we control our economy during this period. To my mind, that is very definitely part—and an essential part—of the whole structure of our security.

Representative PATMAN. May I comment on your statement a few minutes ago as to what we are doing in the way of furnishing machinery and supplies to France which is helping France. I believe you mentioned the country France.

Mr. PUTNAM. I mentioned France particularly.

Representative PATMAN. I personally do not have a very pleasant memory of France in that connection. Our committee was over there recently, and we were told by the highest officials in France, I thought rather boastfully, that they had substantially wiped out the burden of their national debt by inflation.

I don't think I would be very proud of that myself. I know that I would not be proud of our country if we were to issue $260 billion in greenbacks and pay off all of our bondholders. I don't think anybody could very proudly say that we have no national debt if we had wiped it out by inflation. So, I don't think France has been helping herself very much in that respect by paying off her national debt by inflation.

Mr. PUTNAM. I would rather not comment on that. I am not sure whether that is a question to me.

Representative PATMAN. I am just making a comment on it in view of what you said of our help to France.

Mr. PUTNAM. I want to go from there back to this country if I might, and say this: That I regard it as my agency's function—one of its function—to protect the integrity of our national debt.

Representative PATMAN. Certainly.

Mr. PUTNAM. To protect the integrity of the dollar.

Representative PATMAN. We must pay it with honest dollars and not do it like France did.

Mr. PUTNAM. Part of my job is to see that with your help the dollar stays honest.

The CHAIRMAN. I was about to add, Mr. Putnam, that within the period of your tenure of office, two Western European governments have failed, the French and the Belgian. In both cases the failure was attributable, according to the information that came here, to the fact that the legislatures in the two countries were unwilling to support the rigorous military program that was being imposed or being asked as a result of NATO.

In other words, it was the old question of butter versus guns. The same issue confronts Churchill in Great Britain. The Labor government split because the wing led by Bevan was against military spending, primarily I think because of its desire to raise the standard of living of the people of Great Britain, which is admittedly low. They are going through a very strenuous period of self-denial.

Now, if military spending in Europe causes the lowering of the living standards of the people of Western Europe, isn't that likely to produce the conditions upon which the Kremlin is depending to undermine the economy and to promote the disturbances there which are expected to advance the cause of the world revolution that Lenin and Stalin have been preaching in their books?

Mr. PUTNAM. It can. It could be anywhere. It is a question of degree. You must have some butter to live. It is a question of willingness of people—not of governments, but of individuals. It depends partly on how well it is explained to them how much butter they will have to do without in order to get guns. But you must have some butter to live, and obviously you must have some guns to defend yourself in a period like this. It is a question of degree for the European countries. It is also a question of degree for us.

I myself feel that we have—continuing the simile—an ample supply of butter. We have a much bigger supply than the others do. We probably have, therefore, got to make the greater proportionate sacrifice in order to build up our defenses. But we can only do it if we use our self-control and our other controls to keep our economy strong. It is a question of degree all the way through.

Representative McKINNON. Mr. Putnam, we are sort of on the eve now in Congress of facing perhaps three policy alternatives in matching up to our responsibilities in this world. One seems to be pretty much the President's program which calls for an $85 billion budget, which calls for a $5 billion increased tax program, and which calls for the continuation of the Defense Production Act pretty much the way it is now. That is putting the emphasis pretty much on guns.

Then we have certain other resolutions that have now been introduced in the Congress which call for a reduction in the budget to about $71 billion, no increase in taxes, and I presume a lessening of our Defense Production Act, a lessening of the effectiveness of it, which is putting more or less the emphasis upon butter instead of guns.

Then we have the third alternative which I imagine Congress is pretty likely to adopt in one way or another, which means an $85 billion budget, which means no increase in taxes, and which would be a continuation of the Defense Production Act pretty much in its present form.

Now, if we adopt that third alternative as more or less a compromise between the two extremes, and with the Defense Production Act the way it is, do you think you can hold the line on the stabilization front with the $85 billion, with no increase in taxes, and with a continuation of the Defense Production Act as it is now?

Mr. PUTNAM. Congressman McKinnon, if I was sure of the answer to that, it would be wonderful. I am not sure of the answer to that.

I can say this: That with that third alternative—with the full budget but without the additional taxes—the job of controlling the economy would be more difficult. We would need, if anything, a tighter law, not a looser law. I would hope that, if the third alternative was adopted, you would strengthen our act rather than weaken it.

I believe that if that is done we can do a pretty good job. We will do the best we can. It will be harder. It will depend again on how much the public cooperates with us. If they will save the equivalent of what otherwise might be taxed, why that would help it a great deal. But the harder you make our job, the stronger rope we will need to hold inflation in check.

Representative McKINNON. You feel then that for national security and stabilization in our country, if we take that third alternative without a stronger Defense Production Act, we are taking an undue and unnecessary chance with our whole structure?

Mr. PUTNAM. It will be a harder job to hold the pressures. We will need a stronger rope. We want to be sure that it is at least not weakened, and preferably is strengthened. The harder you make our job, the heavier rope we have to have to hold a line.

Representative McKINNON. And, if the Defense Production Act was strengthened, would you go so far as to say that it would not disturb the incentive for more production?

Mr. PUTNAM. I think we can avoid discouraging increased production. One of our jobs is to encourage production.

Representative McKINNON. Do you feel you could administer a tighter Defense Production Act so that we can stabilize our price front and at the same time administer it so as to encourage more production?

Mr. PUTNAM. I use the word "stabilize"; I don't use the word "freeze." I think there has been for centuries a creeping increase in prices and in wages, and there will continue to be certain areas where there will have to be creeping advances.

I think that is true anyway, but I think the stronger you can make our rope, why, the more we can hold with it. The tougher you make our problem, the stronger it has got to be for us to hold the line. The more money you take out of circulation, the easier our job is. The more you leave in, the harder it is.

The CHAIRMAN. Congressman Boggs?

Representative BOGGS. Mr. Putnam, do you meet many businessmen who express the opinion that direct controls are not essential at this time?

Mr. PUTNAM. I meet some. I am going from here to a luncheon date—not until 1 o'clock, but I have a luncheon date—with the directors of the national chamber of commerce, the United States Chamber of Commerce, and if you would ask me that question this afternoon, I can tell you better.

I meet some, but I don't meet many. Most businessmen I meet separately feel that controls are necessary. When they get together and pass resolutions, they want them removed. That has been my experience so far.

Representative BOGGS. I understand that. I was speaking of direct controls primarily.

Mr. PUTNAM. Yes. When I get with people who say they want to remove the direct controls, I ask them how hard have they been crusading for the indirect controls. Are they fighting to get taxes increased? I do not find them ever doing it. They would like to remove the direct controls but they do not want to impose the indirect controls either.

Representative BOGGS. But you will admit that through resolutions——

The CHAIRMAN. You mean they do not want to impose the indirect controls?

Mr. PUTNAM. Yes.

Representative BOGGS. But you do admit that at least through resolutions and their organizations, many businessmen and agricultural people do express opposition to direct controls?

Mr. PUTNAM. Yes. I have seen those resolutions, certainly.

Representative BOGGS. Would you think for a minute that the President would have selected a person to fill your important position who had expressed or had a feeling that direct controls were not needed?

Mr. PUTNAM. I don't know, because nobody asked me my views before I was asked to come down here and do this job. I refused it the first time I was asked. Nobody canvassed my opinions, and I do not think I had made many public statements on this subject. I do not think I made any.

Representative BOGGS. Well, that is fine. I certainly recognize your ability and your outstanding accomplishments with this very difficult job.

Mr. PUTNAM. I am anxious to find out who did put my name in so I can get even with him some time or other. I don't know how it was done.

Representative BOGGS. Of course, as you well recognize, in every community, in every phase of life, our people are vitally concerned about these direct controls, and I daresay you cannot go anywhere without questions coming up concerning them and what the future holds in the next year, the next 2 years and so forth beyond that. I am convinced that you believe this whole structure should be reenacted for a period of 2 years, with a tightening up of controls.

Mr. PUTNAM. I do not say necessarily with tightening up of controls, but with the power given to us to tighten them if we feel they are needed.

I want you to realize, as I said earlier, controls are abhorrent to me. I don't like them. But I feel at this moment that they are necessary.

Representative BOGGS. Now, of course, we do not know what the Congress is going to do about it at this time. There is a possibility that the Congress will not continue the authority on direct controls.

Now in the beginning of your statement you referred several times to this economic balloon we have here in the country. Do you think that this balloon could be kept up in the air, that we could keep it going for a while longer without direct controls? Suppose the Congress would fail to go along and we enact direct controls for another 2-year period, what in your opinion would happen on that point?

Mr. PUTNAM. I hate to think of it. I hate to think of something like that happening. What I believe would happen if the public was told all the facts—that is, all the military spending that is going to happen that you all know so much about—if they realized that, and if they realized there were going to be no price controls we might very well get into another period like the 6 months after Korea when they jumped in to buy supplies "before the hoarders did." If you will remember what happened to the economy then, you will recall that the whole price structure went up nearly 10 percent in 6 or 7 months.

I would be very fearful of something of that sort happening, again. That, of course, would be exactly what the Kremlin would love more than anything else to have happen.

Of course, selfishly for my own family and myself, it would be nice if I could go home. I consider that I am in uniform now. I could resign this task which I think is so important. I would gladly push off the responsibility, but I would hate to see it for the country. I would be frightened.

The CHAIRMAN. If there are no other questions, the Chair will express the appreciation of the committee, Mr. Putnam, for your appearance here, for your ready and responsive answers to the various questions which have been asked. We are very much obliged to you.

Mr. PUTNAM. May I thank you and the other members of the committee for your very extreme courtesy to me and the wisdom and incisiveness of all these questions.

The CHAIRMAN. Now we are complimented.

The committee will meet tomorrow morning at 10 o'clock in this room for the purpose of hearing Mr. C. E. Wilson. It had been planned for Mr. Wilson to appear this afternoon, but the funeral of the late Secretary Robert Patterson is taking place at 3 o'clock, and the meeting therefore has been canceled.

If it is convenient for Secretary Lovett to appear on short notice, the Chair will also invite him to sit in on the hearing tomorrow. The committee is now in recess until tomorrow morning at 10 o'clock.

(Whereupon, at 12:10 p. m., the joint committee adjourned, to reconvene at 10 a. m., Saturday, January 26, 1952.)

JANUARY 1952 ECONOMIC REPORT OF THE PRESIDENT

SATURDAY, JANUARY 26, 1952

CONGRESS OF THE UNITED STATES,
JOINT COMMITTEE ON THE ECONOMIC REPORT,
Washington, D. C.

The joint committee met, pursuant to adjournment, at 10:20 a. m., in the caucus room, Old House Office Building, Senator Joseph C. O'Mahoney (chairman) presiding.

Present: Senator O'Mahoney (chairman); Representatives Patman, McKinnon, and Herter.

Also present: Grover W. Ensley, staff director; and John W. Lehman, clerk.

The CHAIRMAN. The committee will come to order.

Mr. Wilson, if you will be good enough to come forward, please. The committee regrets very much, sir, that it was necessary to postpone your appearance from yesterday afternoon until this morning. I had hoped to be able to have Secretary Lovett at the same time that you were here so that we could have the benefit of the advice of both you and the Secretary of Defense with respect to the standards by which the judgment has been made as to the military program, and the expenditures that naturally result from it. Perhaps we will be able to develop that in any event.

Your report of January 1 on the battle of production has been available to all the members of the committee, and I observe that you have come with a prepared statement this morning.

Would it be your preference to present that statement as a whole, without interruption, or do you mind if interruptions come as we go along?

Mr. WILSON. I do not mind at all, Senator.

The CHAIRMAN. Very well, then, we will proceed in the usual catch-as-catch-can method.

Mr. WILSON. All right.

The CHAIRMAN. Perhaps I ought to say at the outset that it seems to the chairman—I am speaking only for myself—that the basic issue is whether or not the Government of the United States is actually facing the facts of the international crisis.

The Russians, through their spokesmen, Lenin and Stalin, have repeatedly stated that they are engaged in world conquest; they have stated in their published works that it is their plan to work through the so-called bourgeois states. They have been working through their satellite states.

Stalin himself declared that Russian manpower would be held in reserve until the last, when it was hoped it would be possible to march, as it were, into a vacuum, and just take over.

In the meantime, according to the program which they outlined, just as Hitler outlined his program in Mein Kampf, the program to which nobody paid any attention, least of all the United States, they have outlined their intention of taking advantage of the internal difficulties that naturally occur in free states.

They have announced over and over again that in their belief capitalism is outmoded, that international debt cannot and will not be paid, that we move in a capitalistic system from imperialism into war, and they represent us to all the people of the world as ambitious to step into the shoes of the dying empires of France and Great Britain. That is our picture.

We are apparently proceeding upon the theory that war is not just around the corner; that the Russians do not want to start a war with us, and so we are devoting only a fraction of our output to military purposes. We are not engaged in an all-out mobilization.

There are some who say that our production lines themselves have not been satisfactorily completed. There are some who say that we are not producing enough implements of war; and then there are some who say we are spending too much, and that we ought to next year or the year thereafter get to some basis of normalcy where everybody can have all the luxuries that they wanted and used to have and enjoy. In effect they say, "let George solve the international problem."

Do you agree with that summary of the situation?

Mr. WILSON. I certainly do. I agree with it wholeheartedly.

The CHAIRMAN. Now, the question, therefore, is Are we preparing at a sufficiently rapid rate? Can we look forward to any degree of normalcy in a couple of years?

The testimony presented before this committee to date has been to the effect that when we have completed the mass production machine for turning out implements of war, it will then be possible to step down our expenditures, and that in the meantime the national economy can be kept running at a sufficiently productive pace, profitwise and outputwise, to enable us to carry this burden of military expenditures.

Those, I think, are some of the questions which you are being called upon to answer.

Mr. WILSON. Mr. Chairman, I tried to answer some of them in this prepared statement, and I would be glad to try to enlarge on them afterward, or if you would rather just put the statement in the record, and go ahead——

The CHAIRMAN. Suppose you begin with your statement.

STATEMENT OF CHARLES E. WILSON, DIRECTOR OF DEFENSE MOBILIZATION

Mr. WILSON. All right, sir. I should say that I appreciate the opportunity to appear before you to comment briefly on the Nation's mobilization program, on its objectives, on how we are moving toward them, and on the developments I think we can reasonably expect.

At the beginning of our mobilization for defense, it was decided that the effort to restore America's military strength had four main goals. I would like to restate them as they are the basic policy determinations governing the mobilization program.

As you know, the first of these goals is to turn out guns, tanks, planes, and other arms for our forces in Korea and elsewhere overseas and in this country, and for our allies, and for our reserve arsenal.

Secondly, to make ready added production lines, beyond current armament needs, as a protection in case of full-scale war.

Third, to develop our basic resources and expand our industrial potential until they are able to sustain the necessary military program and at the same time maintain our standard of living—or, if all-out war comes, able to furnish a broad and powerful industrial base.

Fourth, to maintain the healthiest and most productive civilian economy we can, while achieving these first three goals.

The next task which faced us was to settle upon the type of program to be employed to achieve these goals. Should we build up strictly military strength as fast as possible, freezing our models and techniques and pouring out today's arms, that is, pouring them out today? Or should we use a broader and more sustained buildup, developing our resources, our techniques, and our production lines for the newer weapons of the future, and keeping our civilian economy as strong as possible for the long pull? In other words, should we assume that the maximum need for strength was immediate, or that our greatest need might come at any time over a longer period?

We did know one very important thing. We knew that we and other freemen were girding to defend ourselves, not to attack others. We could not choose the day on which our armor would be put to the test—nor can we now. Therefore, we must be strong against an attack which may come at any time over an indefinite future. Over that future, our best defense is not in the guns which come off the assembly line this morning, or next week. Over that future, our best defense is in the newer and better weapons, the greater resources, and the more effective production lines, which a healthy civilian economy can build and maintain under a longer range program.

The CHAIRMAN. Does that mean, Mr. Wilson, that the defense mobilization program is directed toward the manufacture of modern weapons primarily?

Mr. WILSON. That is right, sir.

The CHAIRMAN. Are we actually developing the modern weapons instead of turning out old style weapons?

Mr. WILSON. I think that question can certainly be answered in the affirmative, Mr. Senator. If a year ago we had simply steamed up our whole economy for the production of the then available weapon designs, war matériel would be pouring off those lines today a great deal faster than it is. But the truth is that the first step in the use of the vast amounts of money which you legislators gave the Defense Department about a year ago was to design these new weapons; next, to do the production engineering necessary after design; then as a third step, to produce the rather difficult-to-produce machine tools that were found to be necessary once the new designs had been frozen, and then to get the production lines themselves tuned up.

Now, it is a sad fact, but it may as well be acknowledged, that even those charged with the responsibility for producing the military end items just as fast as it is humanly possible to do it have to admit that after the appropriations are received, and if they are going to be turned into these, well, to quote the popular term now, these new fantastic weapons, that you cannot get them rolling in production the way you would take the money and send it to Sears, Roebuck, and get them back by return mail.

The CHAIRMAN. In other words, there is no inventory of the new weapons which you are seeking to build.

Mr. WILSON. In many, many cases, sir, they were not much more than a gleam in the eye of some of the designers and inventors, and it takes a little time to get them out.

The CHAIRMAN. You said a moment ago, in response to one of these questions, that had we been building the old-time weapons they would have been pouring off the production lines now in great volume.

Mr. WILSON. That is right.

The CHAIRMAN. But would they have been suitable for the type of conflict which is likely to occur?

Mr. WILSON. In the case of aircraft, for instance, I think they would have been worth about a dime a dozen for the kind of warfare we are obviously going to have to pursue.

The CHAIRMAN. In other words, the airplanes of World War II were not at all suited even to the conflict that is now going on in Korea.

Mr. WILSON. Quite right.

The CHAIRMAN. To say nothing of the possibility of an international warfare.

Mr. WILSON. I think we are finding that out just by the loss of our piston engine type planes in Korea. They are just knocked down by modern radar-equipped gunfire, and they just do not get high enough, fast enough to be safe.

The CHAIRMAN. They are being knocked down from the ground?

Mr. WILSON. Yes. It is ground action that has destroyed the majority of the planes we have lost in Korea, not air action.

The CHAIRMAN. Does not that mean that from some source the Chinese Communists and the North Koreans have been armed with the most modern of weapons?

Mr. WILSON. I think there is every evidence of that, Senator.

The CHAIRMAN. If there be every evidence of that, then from what is going on in Korea, how realistic is this program which calls for not to exceed 29 percent of the gross national income for military expenditure in 1953?

Mr. WILSON. Well, I think it is realistic, Senator, maybe for a reason that you will find disagreement with.

In the first place, I still believe that approximately $50 billion worth of war matériel is a lot—that is a lot of matériel to get ready; and roughly 15, 16 percent of the total national production to be turned out in that kind of matériel is a considerable portion. I may be too mindful of the fact that Mr. Stalin—well, Lenin before him, but Stalin—repeatedly since has reminded us that the way to knock the democracies out is not to plan on doing that physically, but to do it to things that their economy depends on—or to permit them to force them to liquidate their economies, and I think there is a danger of that when—you, after all, know we have already planned on expenditures of, well, a $150 billion, and there is more to come, and I believe myself that is about all that a safe, strong economy can withstand for the security of the Nation.

But there is another reason. I think it is a much more potent one, and on this one I am sure there would be a wide difference of opinion. I just do not believe you can effectively spend more money on modern weapons unless you plan for it for a considerably longer period of time than this Nation has planned for it.

You know, we did not do very much from 1945 until Korea to really plan for and develop modern weapons, and that is why I keep reiterating now that you just cannot turn on the spigot, and turn out these fantastic new weapons after you legislators finally gave the money or after they asked for the money—I do not know which it is—but in any event, after they had the ability to go ahead—the first job they had to go ahead with is a terribly slow one, and that is to design the stuff.

Representative HERTER. Mr. Chairman?

The CHAIRMAN. Congressman Herter.

Representative HERTER. Mr. Wilson, in connection with the disappointing, if one may call it that, slowness with which these modern weapons have been turned out, there has been a good deal of difference of opinion as to whether it was due entirely to new designs having to be approved, new tooling done, and so on, or whether some of the slow-down was due to lack of raw materials or the lack of allocation from the civilian economy of certain types of goods to the others.

Mr. WILSON. You can write that last statement off; you can write it off. I defy anybody to produce a single shred of evidence that will prove that last statement.

Representative HERTER. That is just what I wanted brought out at this time, because I have heard——

Mr. WILSON. I hear a lot of talk about it, but I have not heard anybody prove it.

Representative HERTER. I have heard that a number of times, and it looked to me like it was an effort to pass the buck from the military designers to you, and I think it is something that ought to be cleared up.

Mr. WILSON. The military designers and the military people have never made that claim to me in a single instance.

Representative HERTER. They have not; but other people on the outside have.

Mr. WILSON. Yes; I know that.

Representative HERTER. I wanted to get that cleared away.

Mr. WILSON. But the military know better.

Representative HERTER. In other words, there has never been a delay in production because of inability to get raw materials or strategic materials?

Mr. WILSON. Oh, no; I will not go that far. They probably will charge—some people would charge—a delay, not because we allocated the material to nonmilitary purposes that we had, but because the military, after they froze a design, suddenly found that they needed, let us say, certain kinds of alloying materials in quantities greater than all the nations of the world, to the best of our knowledge, can produce.

Well, now, we could not give them that. The reason we could not give it, in the quantites they wanted and when they wanted it, was not because we were allocating it to civilian production, but because there just is not that much, to the best of our knowledge, alloying material in the world; and, therefore, we had to wait until they could introduce and agree upon new types of alloying metals, and—well, the classic case, if you please, of eliminating or almost eliminating columbium and using other alloying agents that you can get, that maybe the world could produce, things like that.

The CHAIRMAN. From page 2 of your production report of January 1, 1952, one finds the information contained in a chart labeled "Machine Tool Shipments," that in January of 1951 machine tool shipments were being made at a very slight level above the average for 1945 to 1947. The shipments of 1945 to 1947 are set down in this chart as 100.

The shipments of machine tools fell off in June and July after having gained almost to the 200 index point; but in October and November shipments were running, according to this chart, at above the 200 index point, probably about 225.

Mr. WILSON. That is about right, Senator.

The CHAIRMAN. Are those shipments still gaining?

Mr. WILSON. They are still gaining, and unless we cut them back, and we are in the process of cutting some of them back because of the finding in some few instances that they do not need some of the tools after all, but barring those cutbacks, unless they cut too deeply, why, I think, you can be pretty reasonably assured that machine tool production through the current year will double again over the gain that it made in 1951.

In other words, I think you can be quite well assured that the industry will produce about $1,400,000,000 in machine tools, which is a lot of machine tools.

The CHAIRMAN. The reason I asked the question is because the lag, the alleged lag, in the delivery of new types of weapons was ascribed to the failure to get machine tools moving fast enough.

Mr. WILSON. That is right.

The CHAIRMAN. Has that problem been licked?

Mr. WILSON. I think it has been licked to the extent that it can be licked. You never can make up fully the lost time, Senator. I think there were delays in getting some of the new type machine tools under way for a great variety of reasons, and, well, maybe some of it was just stupidity, some of it was bad. I think we have a certain amount of responsibility for it, but among the reasons, there were also the difficulties of getting the contractors of some of these new weapons to decide what machine tools, what types of machine tools, they really ought to have, and then to get the military to give them the go ahead on buying the machine tools; and then, after that—and this was not done overnight, either—after we really discovered what a tremendous problem we really had on our hands with machine tools, which seemed to be just about a year ago now or a little later than that—a worse problem than we even had in World War II—then we woke up to the fact that the machine tool builders were not going to go ahead on the basis of the vastly increased production that we were demanding, because they did not like the price situation, and we had to get into that and fix a lot of them up with prices that were, well, as much as 30, 40 percent higher, I think.

Representative MCKINNON. You mean the manufacturers also were on strike, the same as labor sometimes goes on strike?

Mr. WILSON. Well, to that extent, that is right. They wanted to be recompensed for some reason or other—for the higher labor rates they were going to have to pay, and the costs, and so on.

Representative McKINNON. And assurance of higher profits? So often we read in the papers where labor is always to blame for the slow-up of our rearmament program, and I just could not let that go by, Mr. Wilson, by stating that labor is not the only one that sometimes wants more money.

Mr. WILSON. I think anybody who thinks they are the only ones is not very factual.

The CHAIRMAN. I think that brings us face to face with the fundamental conflict in ideology between our economy and the Russian economy, and reveals the conviction of the Russians that the free economy is bound to break down. The Russians have said over and over again—I mean the Communist Russians—the dictators of the Kremlin, that our people are constantly looking for profits out of war, and because we look for profit out of war we are going to wreck ourselves, because we will be constantly pushing the price line upward by pushing profits upward, by pushing wages upward, by trying to gain instead of trying to contribute.

Now, the Russians solved that problem of contribution by force. They just make the individual contribute, and he has nothing to say about it. He either does what he is told or he goes to a concentration camp.

Mr. WILSON. Or stood up against a stone wall, one or the other.

The CHAIRMAN. Sure. Our problem is getting voluntary contributions from freemen to meet the issue of our time.

Mr. WILSON. If they want to keep their freedom.

The CHAIRMAN. That is right.

Well, let me go back to this machine tool business. You say that that is pretty well licked?

Mr. WILSON. That is right.

The CHAIRMAN. You are getting the machine tools now to build the modern weapons?

Mr. WILSON. That is right. They are beginning to come much faster, Senator.

The CHAIRMAN. All right. Now, to what extent have you got the plants finished to manufacture the modern weapons, the mass production plants?

Mr. WILSON. They are being finished up, many have been finished, others are being finished up, and I think by the end of this year the most important to the security of the country will be pretty well in place.

The CHAIRMAN. Are you speaking of the calendar or fiscal year?

Mr. WILSON. Calendar year; I meant the calendar year.

The CHAIRMAN. You mean by the end of 1952?

Mr. WILSON. Yes, by the end of 1952, the most important plants, in the majority of the cases, will be finished.

That does not apply to all our raw material expansion, Senator. Some of the raw material, or rather some of the metallics, those shortages will not be overcome until late 1953 in the case of aluminum; some of them will not come in until then; 1954 in the case of copper expansions; but for the building of some of the new equipment, many of the plants are beginning to come and will continue to come in this year.

The CHAIRMAN. May I put it this way: Are you willing to hazard a guess or a statement as to whether or not by the end of fiscal 1953, which is the year for which the Congress is now considering the budget, we will have reasonably completed the production machine, the production plant, capable of turning out the type of modern weapons which would enable us to meet the Russian threat?

Mr. WILSON. Yes; I think we will have reasonably completed it to use our own materials, yes. I do not mean that we will have completed it, entirely, but I think to a reasonable degree, yes.

The CHAIRMAN. Well, of course, there are changes all the time, and nobody can predict what those changes will be.

Mr. WILSON. That is an understatement, Senator.

The CHAIRMAN. That is why I used the word "reasonable."

Mr. WILSON. Yes, I know. That is an understatement when you say there are changes all the time.

The CHAIRMAN. You may proceed, sir.

Mr. WILSON. We chose the long-range strength. It was a calculated risk. I believe the events of the past year have proved that the choice was a good choice.

If we had chosen a course directed only at immediate strength, we could have built up faster the number of planes, tanks, and guns on hand and increased the number of soldiers on active duty. But this would have meant freezing our weapon models. Many of those planes, tanks and guns would have been out of date by now. In addition, a sudden change-over to all-out military production would have resulted in violent dislocations in our economy. The shortages of manpower and raw materials for civilian goods might have greatly lowered our standard of living and caused a substantial amount of business failure and unemployment. We would have been in much worse shape to stand the long pull of partial mobilization. We might even have disrupted our economy so much as to fall an easy victim to later aggression.

Having taken the longer range course, there is the question of how long it shall last. The program we have adopted, as reflected in the proposed 1953 budget, calls for $65.1 billion for major national security programs, of which $51.2 billion is for the military. By projecting production schedules on this basis, I believe that by the end of calendar 1954 we will have passed the peak of expenditures needed for the program. At the same time we will have obtained very substantial increments of military strength. Unless the situation of the world with respect to possible aggression changes considerably, we should be able to cut back the programs substantially from that time forward because we will have a good position of defense.

The CHAIRMAN. When you say "production schedules," you are referring to actually the production of the end item, are you not?

Mr. WILSON. That is right. That is right, sir.

The CHAIRMAN. So that, if you have the peak of your production schedules by the end of calendar year 1954, you will necessarily have passed long before that the peak of building the plant necessary to make the production?

Mr. WILSON. Oh, yes; that is right, sir, by the end of calendar 1954, by all means—by all means.

The CHAIRMAN. Will these production schedules, in your judgment, cover items that are equal to if not superior to the weapons that the Russians are developing? I ask that question because there seems to be no doubt that the MIG, which is in use in Korea, is a plane which climbs much faster than any plane we have heretofore sent against them; and our success in knocking the MIG's down is due rather to personnel superiority and our trained pilots than it is to the superiority of the instrument we are sending in.

Mr. WILSON. You make that as a statement?

The CHAIRMAN. I do. I make that on the basis of the information which comes through the public press and over the radio daily.

Mr. WILSON. Yes. Well, it could well be, Senator. Maybe the best way to put it, because this is a pretty broad subject, is that my belief is—from some check of the plans, the types of planes, and the new weapons that are in sight—is that in every department the outlook is for good weapons, certainly as good or better than the enemy's, from what we know of the enemy's—that we can be assured of that. I believe that sincerely.

The CHAIRMAN. This whole plan of defense mobilization is based upon the assumption that we are not entering an all-out war.

Mr. WILSON. That is right. It is, as far as my own understanding goes, to get so strong that we will not have an all-out war.

The CHAIRMAN. Let me make this observation, sir, that the history of two world wars shows that little wars grow into big wars.

Mr. WILSON. That is right.

The CHAIRMAN. When the Austrians moved into Serbia after the assassination of the grand duke, there were very few people, even among the leaders of the nations of the world, who thought that was going to be more than a local action. It turned out to be an all-enveloping world conflict.

Mr. WILSON. That is right.

The CHAIRMAN. There is nobody in this room who does not remember all the talk we had about "the phony war" when the French and the Hitlerites were facing one another across the Maginot line. Nobody at that time envisaged what World War II turned out to be.

Mr. WILSON. That is right, Senator.

The CHAIRMAN. Now we have not only Korea, we have not only Indochina, but we have also the growing bloodshed in Egypt; we have the turbulence in Iran; we have trouble all around the boundary of the Soviet Empire; and we are planning as though those things did not exist; and that is what prompted me to ask you the question at the outset, Are we really facing the problem that confronts us?

Mr. WILSON. Well, it is my belief that this is a good way to face it. I would just like to go back to one point you made, Senator, whether this program is really a futile one as far as preventing the possibility of world war III or providing reasonable hope that you would prevent world war III, and I would just like to use your own analogy of the time, the period when the French and the Hitlerites were facing each other, and so forth.

Just remember, sir—let us take the case of the British in that situation. The symbol of their strength at the time was an umbrella. Do you remember that?

The CHAIRMAN. Yes.

Mr. WILSON. It was an umbrella. Well, the symbol of our strength, if I understand this program, is going to be about a hundred and fifty billion dollars—given reasonable time to pursue it, is going to be about a hundred and fifty billion dollars' worth of war matériel—a little bit better than an umbrella.

The CHAIRMAN. Well, of course, we cannot exactly measure it in dollars, because if we do not lick inflation the dollar will constantly be buying a smaller quantity of airplanes even to make an umbrella.

Mr. WILSON. That is one of the greatest dangers. You certainly would not get any argument from me on that.

I am more worried about that than I am of the question of whether we are going to be able to produce fast enough or in volume enough, and so on.

The CHAIRMAN. I want the record to be clear that I am not asking these questions in an argumentative way or as necessarily revealing the opinions of the chairman, but merely to help illustrate the problem that we have to solve.

Mr. WILSON. Yes; I think it is a real problem, sir.

Representative HERTER. Mr. Wilson, in the paragraph that you have just read, you have used certain figures, and I just wanted to get straight on those figures because I was coming back to them after you got through with your statement.

You say that the program calls for $65 billion for major national security programs, of which $51.2 billion are for the military.

Actually for the military there are an additional $8 billion or so, although it has not been segregated, in the foreign-aid program, which is identical in end items, and so on, which ought to be added into the military figure here.

Mr. WILSON. Yes, sir. Well, I meant domestic military. In thinking about it, we do differentiate to that extent. As a matter of fact, if you want to take that view, then, why don't you include the atomic-energy program?

Representative HERTER. Exactly.

Mr. WILSON. I do not quite see the difference myself.

Representative HERTER. Except that the atomic energy is not distributed overseas, necessarily, whereas that is retained here.

Mr. WILSON. I hope it is going to be well distributed overseas.

Representative HERTER. In our own hands.

The CHAIRMAN. May I interrupt, Congressman? The figures in the budget indicate that this 65.1 for expenditures in 1953 includes the total for the three military services.

Representative HERTER. That is right.

The CHAIRMAN. The international security and foreign relations program of $10.8 billion, the development and control of atomic energy of $1.2 billion, the promotion of the merchant marine of $200 million, and other items of a similar character, which are set down as $1.1 billion, making a total of $51.2 billion for the three defense departments, and a total of $65.1 billion for those other services, when added to the Department of Defense services.

Representative HERTER. I am not questioning that for a moment.

The CHAIRMAN. But it doesn't include the additional expenditure that is projected for atomic energy.

Representative HERTER. I merely am saying that this $51.2 billion is for the military. The way it is stated here makes it look as though some of the other was not for the military, when actually a large quantity of it is.

Mr. WILSON. Shall I go ahead, Senator?

The CHAIRMAN. Yes.

Mr. WILSON. Nevertheless, for the time being, and you will pardon me, I repeat for the time being, we cannot have all the guns we need and all the butter we want, even with our vast wealth.

Over the long haul our men and women and our natural resources can make and obtain everything we need for war or peace or for any mixture of the two. But the program must be dovetailed into our economy. We must make some temporary adjustments while we work through to our goal.

Before Korea our economy was already running all-out. It was using all its facilities, manpower, and raw materials to fill orders for the good things we enjoy in peacetime. That demand still exists. On top of that demand—or ahead of it, rather—we have now added a great pile of orders for armament. That alone would have caused some shortages. To turn those shortages into mere temporary deferments—to make sure they would not go on and on, and more important, as insurance against full-scale war—we have added a great pile of orders for industrial expansion. Congress recognized the need for this expansion in title III of the Defense Production Act and in the accelerated tax-amortization provision of the Internal Revenue Code.

This tremendous demand for metals, minerals, and other materials, and the limited supply, required adjustments in the economy. It meant allocation of scarce materials and control of prices, wages, and credit to tide us over the period when there is not enough to go around—to turn out the military goods and at the same time check inflation. Congress provided for those adjustments in the Defense Production Act.

We are confident that those adjustments will be only temporary. As I indicated, Congress provided authority for a program of expansion of productive capacity. We have developed such a program and are carrying it out. When it is completed, it will largely take care of the problem of shortages and adjustments in the economy which make controls necessary now. The completion of this program will increase the annual output of steel by an additional 12 million tons; of aluminum by an additional 700,000 tons; of power capacity by an additional 30 million kilowatts, with corresponding increases in production of other materials.

The CHAIRMAN. When will that have been accomplished?

Mr. WILSON. Well, most of it by the end of calendar year 1953; not all the power by that time, but all the aluminum should be in by the end of calendar 1953; all the steel, I think, will be in, the increase to 120 million tons capacity, that will all be in, I believe, by calendar 1953; and, I believe, all the additional electric power we need for the program, as I can see it, at the end of 1953.

The CHAIRMAN. Do you regard all of these objectives as essential objectives?

Mr. WILSON. Yes; I think so.

The CHAIRMAN. The production of power is essential?

Mr. WILSON. Oh, by all means.

The CHAIRMAN. Does that goal include the St. Lawrence seaway?

Mr. WILSON. It does not, Senator.

The CHAIRMAN. Have you any opinion with respect to that power development?

Mr. WILSON. As a power development, no; I do not think the essentiality of the use of the hydro power from that part of the country is nearly as important as the use of the seaway for bringing in iron ore.

The CHAIRMAN. Do you think it is important as a means of transportation for iron ore?

Mr. WILSON. Oh, yes. Not that it makes any difference, but my own standpoint, sir, has changed completely. From an economic standpoint I opposed going ahead, insofar as I had any right to oppose it in the old days; I did not believe in it as a power development. But I certainly believe in it as transportation, as a waterway transportation, that we are going to need in the future to get that iron ore economically.

Representative PATMAN. Mr. Chairman, may I ask a question?

The CHAIRMAN. Certainly.

Representative PATMAN. Although you do not approve of that particular project, you are not against the development of these hydroelectric power projects generally where they are feasible and practicable?

Mr. WILSON. No; I am not against them. I am against them as public projects, yes; because I still believe in the free-enterprise system. I think it is what made us what we are today, and I think that is pretty good, and I hate to see us weaken it by trying to be half Socialist and half free enterprise.

Representative PATMAN. You will not get any argument out of me on that.

Mr. WILSON. Good.

Representative PATMAN. I think that is what is retarding Western Europe now, the cartel system and the monopolies, this lack of private enterprise that we have here. I think that is retarding Western Europe.

In your search for resources would you find generally a shortage of water in the Nation?

In other words, where you desire to locate a facility—do you not have two things that you first inquire about, the availability of electric power and, next, of water?

Mr. WILSON. I am trying to remember where we have been confronted with that as a problem. I can only think of one, and that was in the case of a plant for the production of fissionable material, which takes just a terrific amount of water. I remember that, but I cannot remember another project that ran into serious water conditions, Mr. Patman. Power, yes.

Representative PATMAN. The information we get in our section of the country, where we have always had plenty of water, is that the water level is going down——

Mr. WILSON. Oh, seriously.

Representatve PATMAN. And it is becoming serious not only there but elsewhere, even in New York State, all over the country.

Mr. WILSON. That is right.

Representative PATMAN. It occurs to me that we can very well give thought and consideration in selecting, out of all the projects in the Nation, those where you can have flood control and water conservation, which goes along with soil conservation, together with the development of hydroelectric power projects, without getting into the question of who distributes the power. That is not important at this stage of the proceeding. But do you not think that, in order to have maximum strength for the future, we should as quickly as possible try to develop all those projects in our country?

Mr. WILSON. I think we ought to develop any projects that are a combination of flood control, and save the water against the day you want to use it for the benefit of the Nation, yes. Power, yes, if it is really economical and if it is in locations where we really need it. But I think we fool ourselves a great deal, you know, by spending vast sums of the taxpayers' money to build a lot of power dams in one particular section of the country, and then because we have it, stick a lot of production up there that certainly does not belong in that part of the country, just because you can get 2-mill power, which the taxpayer is really paying for, you know, but you can get 2-mill power to make, let us say, aluminum.

I personally think that is the bunk. I think we are just fooling ourselves.

Representative PATMAN. Do you mean to say there is 2-mill power in the country?

Mr. WILSON. Sure.

Representative PATMAN. I did not know that power was that low.

Mr. WILSON. You have got—you are selling 2-mill power or else I am greatly mistaken, and I do not think I am—you are selling 2-mill power for the production of aluminum in the Northwest.

Representative PATMAN. That is not retail distribution; it is wholesale.

Mr. WILSON. This is the wholesale rate to an aluminum company.

Representative PATMAN. That is what I meant. I thought you meant the consumer rate on some project.

Mr. WILSON. No.

Representative PATMAN. As to consumers, I never heard of them receiving it at less than 5 mills.

Mr. WILSON. A half cent.

Representative PATMAN. A half cent.

Mr. WILSON. That is pretty cheap, too.

Representative PATMAN. That is about the lowest I have heard of.

Mr. WILSON. That is the best half-cent's worth that a man can buy in the United States, in my opinion.

Representative PATMAN. We know of a lot of rates of 5.6 mills, but it is very seldom——

Mr. WILSON. I wish I had it. You ought to see what I have to pay where I live.

Representative PATMAN. I want to ask you just a little bit about procurement.

The CHAIRMAN. Before you leave the question of power, may I ask a question?

Representative PATMAN. Certainly.

The CHAIRMAN. Your statement, Mr. Wilson, announces that the completion of the program, among other things, will increase our power capacity by an additional 30 million kilowatts.

Is that public or private power?

Mr. WILSON. It is both.

The CHAIRMAN. Do you think it more important to get the power than it is to determine whether it shall be produced by public or private agencies?

Mr. WILSON. Of course. You get the power, and fuss the other question out afterward.

Representative PATMAN. That is right; I thoroughly agree with you.

The CHAIRMAN. Get the power first.

Mr. WILSON. Yes. You would just be ages threshing out all the social questions about which comes first, the chicken or the egg, or the means to pay for it, or what have you. I agree that we ought to go ahead and do it, Senator.

The CHAIRMAN. Regardless of this question of socialism?

Mr. WILSON. Then, I hope we take it away from adherents of that system some day, but that is another question.

The CHAIRMAN. Here is the question of the aluminum project in Montana where the Anaconda Copper Co. wants to turn over to the manufacturer of aluminum and is using or plans to use the power developed at the publicly owned Government project at Hungry Horse.

Mr. WILSON. Hungry Horse, is it?

The CHAIRMAN. That is perfectly O. K. in the present emergency, according to your opinion?

Mr. WILSON. I think so, as long as we have——

The CHAIRMAN. I just wanted to clear the record. I knew that would be your answer, but I wanted to clear the record.

Mr. WILSON. Sure, I think it is all right. I think that is a silly place to make aluminum. I think it is silly, but who am I to judge, as long as you have got——

The CHAIRMAN. The judge is the Anaconda Copper Co.

Mr. WILSON. As long as you have somebody who is sucker enough to do it, and the country is for it, that is all right—not with my money, if I had enough to do that.

The CHAIRMAN. Well, I suppose you would not have enough money to do it.

Mr. WILSON. You bet I would not. That is one of the jokes, the standing jokes of ODM, you know, Senator. We had to try to find small business that would go in and make increments of a hundred thousand tons of aluminum, and one of the first things we all discovered, and I guess small business did, too, was that it takes a hundred million dollars to produce an increment of a hundred thousand tons of aluminum a year. So I got a new definition for small business. The first thing you had to have was $100 million.

The CHAIRMAN. Well, that raises, of course, another aspect of this terrible dilemma in which we find ourselves, a dilemma in which we can altogether go off the beam by a discussion of ideological questions.

Mr. WILSON. Yes; that is right.

The CHAIRMAN. I remember so well when the testimony was being presented to the Appropriations Committee last year for the Department of Defense the illustration which Secretary Lovett brought up to the committee of a wonderful plane with which we demolished the industrial plant of Germany during World War II. These planes cost per unit about $417,000; and the plane with which we are replacing that nowadays costs about $3,250,000.

Mr. WILSON. That is right. The electronics in it costs twice as much as two of the planes, two of those other World War II planes.

The CHAIRMAN. So when we talk about these fantastic new weapons we are talking about weapons which are incomparably more costly in materials and in labor than the implements that were used in any previous conflict?

Mr. WILSON. That is right.

The CHAIRMAN. And more costly in the time it takes to turn them out?

Mr. WILSON. That is right.

The CHAIRMAN. All of which has its bearing upon the Soviet belief that we can wreck ourselves in producing for war?

Mr. WILSON. That is right. Of course, if we produce good enough weapons, Senator, and if they are as effective as those who are producing these fantastic new weapons believe they are, and if we keep a reasonably strong economy for the necessary length of time so that we will not go bankrupt or will not bring down the value of the dollar too much in the 3- or 4-year period, then I would think that the people behind the iron curtain, the slave drivers of the Kremlin, are going to get a shock, because I believe we can ride out of this thing, from an economic standpoint, if we have the restraint—if the various segments of the economy who might otherwise go off the deep end in their own demands—if they can all exercise restraint and we can keep a reasonably sound economy. After all, it is only two or three more years in the life of a nation, and that is just a second as history goes.

The CHAIRMAN. I am very glad personally to hear you say that.

Mr. WILSON. I believe that.

The CHAIRMAN. Because I have myself felt for a long time that the cold war is an economic war and it must be fought on an economic base. You may proceed.

Representative PATMAN. On the question of procurement, Mr. Wilson, I am not going to bring up the question of small or large business, I am talking about the question of procurement for the military.

Mr. WILSON. Yes, sir.

Representative PATMAN. You have mentioned the $100,000,000 concern possibly still being a "small concern." I can conceive of that being true and still being small business, since it is a relative term the way I consider it; I can see in certain cases a hundred-million-dollar concern would still be a small business. That is true in several lines of business, like the automobile industry, as you know. Several companies are worth a lot of money, hundreds of millions of dollars, yet they are small compared to the Big Three—General Motors, Ford. and Chrysler.

Mr. WILSON. Yes.

Representative PATMAN. Our procurement, it has been brought to my attention through another committee of which I am a member that there is a lot of objection to the military having the power to procure anything in substantial quantity, especially for defense purposes. The argument is that it is all right for the military to make recommendations that they want certain type guns and certain fire power and anything else they want to specify, but after they have done that they should turn it over to a civilian production man to actually get the production and make the contracts with the different people to produce it. The position is that the military does not fit into the procurement of supplies and equipment for the reason they are not schooled and trained in that line of business.

In your particular case, you are a production man. You are a manufacturer. You have had long years of experience in one of the most successful concerns in the world, and you know all about it. But, you take a lieutenant or some officer of any rank in the service, he has not had any training like that. He does not know anything about the procurement of materials; does not know anything about contracts.

Do you not think there is possibly something to that argument that the military should turn all procurement over to the civilian; that is, to a civilian agency?

Mr. WILSON. You mean a civilian agency?

Representative PATMAN. That is right.

Mr. WILSON. Outside of military control?

Representative PATMAN. That is right. With very good coordination, of course. Let the military say that they want so-and-so—they want a certain kind of tank or a certain kind of ship—that is where their authority will end. They will not have the power to go out and make contracts for any part of it.

I know of cases where an officer will be passing on important contracts one week, and the next week he is moved 5,000 miles away, clear out of the picture entirely.

I am impressed with the fact that many of the officers, having a lot of authority along that line—not assuming it, they are merely acting upon the authority that has been granted to them—are not particularly well qualified to do that line of work. They are, moreover, not charged with the responsibility personally if they do a bad job, and they are not given credit if they do a good job. Unless a person is in a position where he can be blamed or given credit, it occurs to me he would not take as much interest as one who is in that position.

Do you agree with that or not?

Mr. WILSON. You are on a subject, sir, that would be wonderful to talk out. Did you ever read my book? Did you ever hear that crack before?

Well, you know, I have made speeches on this subject for years, and usually before the American Ordnance Association. I just mention that because this is a long, continuing subject.

I do not think I could give you a satisfactory answer to it. Maybe I could say this: for this war that we are facing or getting ready to prevent, world war III, I think that this subject you are on is one that is just academic. There is not anything you can do about it.

After all, the military, whether they are efficient or not, or whether they have these draw-backs that you mention, after all you have got it, and you could not turn that over to a civilian organization in the next

2 or 3 years. It would take a long, long time to train the kind of an organization that you are talking about.

Some of us have recommended that there be in being at all times the kind of an organization that could relieve the military of this deadly purchase job, procurement job, production job. But you are not talking about world war III really. You are talking about some future time. Maybe it would be good then.

Representative PATMAN. Your agency was set up rather quickly and hurriedly, and I think you are doing a mighty good job.

Mr. WILSON. Well, I know, but we are not——

Representative PATMAN. I see no reason why the military could not be required to turn the procurement over to you and have you procure all of this stuff, to make all of the contracts.

Mr. WILSON And make all of the contracts? So they have 100,000 people over there, and heaven only knows how many more around the country.

Representative PATMAN. That is incidental. That does not enter into the picture.

Mr. WILSON. No? What do you mean?

Representative PATMAN. Finding jobs for those people?

Mr. WILSON. I am not finding jobs. They will make jobs for them. You want me to duplicate?

Representative PATMAN. No.

Mr. WILSON. And put in about 25,000?

Representative PATMAN. You could even take some of those people where they are qualified, but the point is to put the procurement in the hands of the civilian who know something about production and procurement, and who are concerned about the payment of taxes and national budget, things like that.

Mr. WILSON. Have you not got it? What did you institute the Munitions Board for? Was not the Munitions Board set up to do this very thing?

Representative PATMAN. Their power is rather limited and restricted, is it not? It does not go as far as I have suggested that maybe a procurement board should go.

Mr. WILSON. Why not fix that without creating a third body?

Representative PATMAN. Of course, I would be in favor of having an existing agency like your own or the Munitions Board or some agency that would not be a different agency. I am not advocating the creation of a separate agency, but over the long pull you think for the future and for 25 years from now that would be a pretty good thing?

Mr. WILSON. I think there are a number of changes in the fundamental approach to it, both on research, developments, production, procurement—I mean, first procurement and then production—I think the whole thing ought to be looked into.

Representative PATMAN. What about substitution of materials?

Mr. WILSON. That would come in your research and engineering phase; yes.

Representative PATMAN. I have been told that copper and brass have been required, specified in contracts, where steel, which is now used, would do just as well.

Mr. WILSON. Why do you not get somebody to run down that statement? I hear that every day, but when I run it down I do not find it. I think it is true to this extent, really, Mr. Patman——

Representative PATMAN. I do not say in all cases.

Mr. WILSON. But there are people who look, for example, at a 50-millimeter shell and say that should not be made of brass. Well, maybe it should not. Personally I think it ought to be made of plastic. That is how far I go, you see.

The truth of the matter is they have not found out how to do it yet, and they have not found out how to do it effectively out of steel yet, either.

Representative PATMAN. What about plastics? Can they make it out of that?

Mr. WILSON. They can make it, but you cannot find anybody that wants to shoot it after they make it.

Representative PATMAN. But, anyway, the substitution of materials is a question that should receive a lot of consideration?

Mr. WILSON. It is. That we have got over in ODM, and we are going to try to gradually get up to do a decent job. Of course, you know we are just a new organization, just a year and a month old, limping along and trying to see the opportunities for saving the taxpayers some money, and a few other things.

Give us time, you know, and after 10 or 20 years we will get as efficient as these big corporations and we will really do a job of making substitutions and making shells out of plastics, and all of that, but you cannot do it as quickly as this.

I think there ought to be a permanent organization working on it. I have recommended it now for about 10 years, that it ought to have liaison groups with industry and with the educational institutions, especially the technical ones, and it ought to use all of the forces that are available in America to keep us up to date in the perfection of weapons, and so on. But that is a long story, and you cannot do much with it when you have got boys with the hammer and sickle breathing down the back of your neck, can you?

Representative PATMAN. Does not the President have a committee now that is to report pretty soon on what would be provided in another country 5 years from now, something along that line?

Mr. WILSON. He has a Natural Resources Committee. You mean metals and all. I think the Paley committee.

Representative PATMAN. I did not even know the name of it.

Mr. WILSON. The Paley committee is looking to see where in world war IV, if it starts, we are going to get the copper and the zinc and the lead, and so on.

Representative PATMAN. They are studying the substitution of materials, too, I understand?

Mr. WILSON. Yes.

The CHAIRMAN. I suggest if we ever get to world war IV we will be using stones, and we will not be needing copper and lead and zinc and other things.

Mr. WILSON. I hope you and I will not be around, do you not?

Representative PATMAN. We will go back to primitive methods.

The CHAIRMAN. You may proceed.

Mr. WILSON. Thank you, sir.

It will be also free for other uses that part of the supply of steel, aluminum, copper, and other scarce materials which is now being allocated to the expansion program.

As you would expect, all of the expansion program will not be finished at the same time. Although some projects in the program have already been finished, many of the larger projects, and some which have had to be deferred because there were not enough materials for them, will not be finished and in production until 1953 and even 1954.

That is the point I made to you before, Mr. Chairman.

As times goes on, more and more of these projects will be finished, and will no longer be a drain on scarce construction materials and equipment. Instead they will be adding to our supplies for military production and for deferred civilian needs.

Over the past year, we have made progress on the four objectives of the mobilization program. The details are given in my fourth quarterly report, but I should like to point out a few high lights now.

The rate of delivery to the military, including construction, has tripled since Korea to a figure of about $2 billion a month. That rate will have to be doubled over the next year to close to $4 billion a month. It will not be easy, nor can it be done without consuming vast amounts of materials, most of them scarce at the present time.

Representative PATMAN. That will be about 50 percent of the amount of production of World War II, at the maximum, would it not?

Mr. WILSON. You figure we are up to $100 billion?

Representative PATMAN. You state that it will be double next year, which will be close to $4 billion. I think we got up to about $8 billion a month in World War II, did we not?

Mr. WILSON. Well, now, we may have. Of course, we were all-out then; yes.

Representative PATMAN. So this would be about 50 percent of what we did in World War II?

Mr. WILSON. Yes; that it right, if we got to $8 billion. I did not remember that we had achieved a total of $8 billion a month.

Representative PATMAN. Mr. Ensley calls my attention to the fact that the price level has changed considerably, which would make a difference in the actual commodities delivered.

Mr. WILSON. Yes.

Representative PATMAN. There may not be so much difference.

The CHAIRMAN. I note you say "including construction."

Mr. WILSON. That is right.

The CHAIRMAN. That, I take it, means plant construction?

Mr. WILSON. Yes; and the equipment thereof, machine tools, and so on, Senator, but that is only military—only for the military.

The CHAIRMAN. I understand.

Mr. WILSON. I have to keep being reminded of that.

The CHAIRMAN. I meant military.

Mr. WILSON. That is right; I thought you did, sir.

The industrial expansion program has also gone ahead rapidly, though a lot remains to be done. Steel production is now up to 108 million tons a year, compared with less than 100 million tons before Korea. Aluminum production has increased by more than 100,000 tons a year. Seven million kilowatts have been added to our electric power capacity.

We have made increases in the strength of our Armed Forces—increases which make us far stronger than we were when the aggressors stepped over the line in Korea. More than 1,000,000 additional men and women have joined our Armed Forces. Our Air Force has 28 new wings. Over 270 ships have come from "moth balls" to active duty in the Navy.

The CHAIRMAN. Does the program that you are now working on envisage a sufficiently rapid expansion of air power to meet the threat?

Mr. WILSON. As one man's belief, I believe it does, Senator; yes. I believe it does. If we ever get the program off the ground as far as designs are concerned, I think they will come out fast enough to take care of our security in the end.

The CHAIRMAN. Well, now, that statement carries implications which I think call for further amplification. You say if we get the program off the ground.

Mr. WILSON. Yes; that is right.

The CHAIRMAN. It means that it is not off the ground?

Mr. WILSON. Well, some parts of it. Some parts are still undergoing changes, Senator, and some of the most important changes we have. Take some of the very large bombers, they are finding in the good old American way means of improving them right along. And my own guess is that for the security of the country some day, regardless of the obsolescence that would be brought about by going ahead, freezing designs and going ahead, regardless of that—I think some day we have got to just say, "This is it," and the planes we make, sure, they may be obsolescent rather than obsolete 5 years from now, but we better have that umbrella over us and be sure.

The CHAIRMAN. Of course; everybody knows that you cannot expect to reach perfection at any moment along the line. There is constant improvement.

Mr. WILSON. That is right.

The CHAIRMAN. So my question was not designed to elicit an answer on that point, but as to whether or not we are making sufficient progress in the construction of air power and in the delivery of airplanes to keep pace with what we are told is the Russian head start.

Mr. WILSON. I believe the situation is improving substantially in that respect. I believe that the volume of planes and the character of the planes that will come out month by month this year gives us very good striking power.

The CHAIRMAN. I am frank to say to you, sir, that the thing that appalls me about this whole matter is this: First, we know if we have a third world war, the atom bomb in a far more deadly form than that which we used against Japan will be available to us and to the Russians, and it may mean the destruction of the civilization that we know.

Secondly, the preparation for war, the construction of these new implements is far more costly in every possible way in time, in manpower, in materials, in money, than anybody ever dreamed of even a year ago or 2 years ago.

Mr. WILSON. That is right.

The CHAIRMAN. And, finally, that the construction of these implements, the building of the plant to turn them out causes such a divergence from the normal uses of the time of a human being and the natural resources of the world that we may, indeed, lose the very system which we are defending in our effort to defend it.

Mr. WILSON. That is right. That is the real danger.

The CHAIRMAN. Well, now, give us your answer. This is it, I take it, so far as you can see?

Mr. WILSON. In my belief, Senator. I believe that with the scheduling out or the phasing out—if I can use this juicy word of the bureaucrats—phasing it out at the rate of approximately 50 billions a year for 2 or 3 years, and trying to maintain a strong economy with all that that means, exerting effort to have people be willing to restrain themselves with respect to the things that otherwise their segment of the population might demand in the normal course of events, and so on—I believe that we can build our strength in time and physically take care of the security of the Nation. And if we can obtain these restraints on the part of all segments of the economy, I think we can have a sound economy and the dollar will still be worth something at the end of the period.

Representative HERTER. Might I ask one question that I was going to reserve for the end? It is rather a detailed question.

In the hearings that we have had up to date, from the Bureau of the Budget and others, it is clear that Congress has itself lost the power to adjust at the rate of expenditure we appropriated for the military departments for all of the things you have been talking about.

Mr. WILSON. Yes.

Representative HERTER. A great deal more money than was expendable in the immediate calendar year for which the appropriation was made.

Mr. WILSON. They have been obligated, but not expended.

Representative HERTER. That is right. So it has been carried over.

The actual rate of expenditure for this year was not determined by the Congress in any way whatsoever. It was determined by the executive department. And when we asked the head of the Bureau of the Budget whether he had any control over that, he said "None whatsoever." The appropriations had been made to the Government departments and they determined the rate of expenditure, that is, the military themselves.

The Director of the Budget was then asked, "Is there no control at all?" To this question he said, "Yes; the only control there is is Mr. Wilson's control over the rate at which they can actually produce things, because he controls the allocation of materials."

Mr. WILSON. Well, that is only partly so. The rate of expenditure to a very considerable degree may be determined by what Mr. Lawton hinted at, that is, the rate at which we get them the materials and resources with which to go ahead, but to date—and I hope you will note this, because it is absolutely correct—is determined by the time requirement of designing and preparing to turn the stuff out.

Representative HERTER. Then may I ask you this question: We are studying the economic aspects of this thing.

The gap, apparently, between the expected rate of expenditure and income is, roughly, $15 billion. That gap is reduced roughly by $5 billion, a little less than that, by surplus cash in the trust funds that is collected as a form of taxation. That leaves the gap of roughly $10 billion that you might call the inflationary gap.

Mr. WILSON. Yes.

Representative HERTER. The President has recommended that one-half of that gap be filled by additional taxation. The leaders of the Congress have said there will be no additional taxation. And the economic experts who come before us say that without that one-half gap being filled there will be unnecessary inflation.

This then is the question, and it is a mean one: If the economists are right that the question of $5 billion one way or the other is going to determine whether there is unnecessary, excessive inflation in our economic system, would it be better from your point of view to slow down our expenditures by $5 billion, rather than do nothing, if we cannot get additional taxes?

Mr. WILSON. I do not think I would slow down. Having in mind first and foremost the security of the country, I do not think I would slow down.

Representative HERTER. That brings the whole question of the pressures, the degree of urgency, the sense of urgency in this whole program.

Mr. WILSON. That is right.

Representative HERTER. What consideration have you given in making your answer to the possibility of extending the build-up over a longer period of time as against running the inflationary risk of pushing it very fast in a given year—what did you take into account?

Mr. WILSON. Of course, you know that we already have two vast bodies of people, some of them in the Legislature, 180 degrees apart in their opinion of this subject already. Some say that we ought to go pell-mell down the road in preparation and never mind the civilian economy, never mind the cost, the ultimate cost—get it done.

From the standpoint of the security of the country it sounds good, and in one sense I would be for it, except that I do not believe it would add to the security of the country one bit, because I just do not think you can economically produce the goods any faster.

The other group says that we ought to slow down even more than we are slowing down.

I think we have taken a pretty much middle-of-the-road course, and that it is a road that we can go down and still have a sound economy, if we watch our step. I believe that.

I do not believe if you go any faster, much faster, you can have that. I do not believe if you go much slower you can have the security that the people have a right to expect. So I think this is a middle-of-the-road course.

Representative MCKINNON. Would you yield?

Representative HERTER. Yes.

Representative MCKINNON. A year ago we anticipated we would be spending our money faster for national defense; did we not?

Mr. WILSON. Yes, we did, because I think we all were lulled to sleep by a lot of so-called dreams that had been set down on paper and called schedules, and we thought that they were going to turn into expenditures much earlier than they are.

Representative MCKINNON. Irrespective of the reason why we did not do it, I wonder if our national security has been threatened by our lack of being able to convert into a faster defense system—do you think we are any worse off as a result of our slow-downs or lack of reaching objectives?

Mr. WILSON. Sure; of course, if we could have produced the whole 50 billion or 100 billion in 1 year we would be that much stronger.

Representative McKINNON. And 2 years from now would there not be that much more obsolescence?

Mr. WILSON. Yes, sure. I think it is all a matter of comparison. The Nation today is infinitely stronger than it was a year ago.

Representative McKINNON. Yes, that is true.

Mr. WILSON. Even with the $2 billion a month coming out.

Representative McKINNON. The question that I simply wanted to raise was, if we are going to be $14 billion in the red in the next fiscal year—and I think that is Mr. Herter's point, too—would we be better off to still slow down our objectives and retain a stronger economy, or would we be better to go ahead and spend this money. even if we incurred a deficit, for security reasons? Is that balance being struck more or less by hit and miss and guess, or is it being pretty carefully calculated?

Mr. WILSON. No; it has been calculated. I am frank to say to you I do not know how to answer the question as to just this $5 billion that is left.

Representative HERTER. It is less than 10 percent of defense expenditures that is involved, but that 10 percent, we are told, will make the difference between dangerous and nondangerous inflation in the rest of the economy.

Mr. WILSON. I do not believe I am capable of adding much to that question. I believe that the program you now have before you is one that gives you the military strength you need over this period, and that is necessary. I believe sincerely that is necessary for the security of this Nation.

The CHAIRMAN. If I understand your answer to Congressman Herter's question, which was a very searching question and one for which we must find the answer, it is that you would rather have this production, and lacking the taxes to pay for it you would choose a deficit rather than not get the production which we hope can be purchased by the $5 billion of which the Congressman spoke?

Mr. WILSON. As usual, Mr. Chairman, you stated it most succinctly and exactly, as I wish I had been able to answer it.

The CHAIRMAN. You silenced me, Mr. Witness. You may proceed.

Mr. WILSON. While achieving this progress we have maintained a healthy civilian economy. During 1951 industrial production as a whole rose 10 percent over 1950; the number of business firms in existence rose slightly; and corporate profits, after taxes, while below the record year of 1950, were twice as high as in 1929 or 1940, and more than three times as high as in 1939. Despite the growth of the Armed Forces, employment rose by 1 million, and unemployment, in the face of the increased population, fell from 2,200,000 to 1,700,000; and disposable personal income rose 9 percent above 1950. Production of consumer goods, including houses, was at extremely high levels, though generally below the record levels of 1950.

There have been weak spots, unemployment in a number of local areas, industries suffering from scarcities of materials or lack of demand, and localities and individuals who have been unable to carry out their plans to build schools, hospitals, stores, theaters, and so on. But I think all of us can agree that on the whole the civilian economy has not been seriously weakened.

As a result of the past year's efforts, I think the country is in much better shape either for an immediate war or for a long period of partial mobilization.

Nevertheless, considered from the viewpoint of the program as a whole, 1951 was largely a year of making ready. We had serious difficulty in the matter of machine tools. A tremendous quantity of them was needed in a relatively short time. Many tools could not be designed until the designs of the items for which they were to be used had been completed. By encouraging large amounts of subcontracting and by other measures, the output of machine tools was doubled in 1951 as compared with 1950. In 1952 it will be doubled again. Even with these difficulties, by the use of substitute tools and methods we have managed to get out the production I have indicated previously.

We must recognize that there will be a period—brief, we hope—when the requirements for the military and for the industrial-expansion program will have increased greatly, but the increases in supply will not yet be realized. We are entering into this period now. Just how long it will last will depend on a multitude of factors, many of which we cannot yet evaluate, but my present judgment is that this period of shortages will last at least through 1952 and to some lesser degree 1953; substantial relief will not be felt until sometime in 1954.

Representative HERTER. From the point of view of having the record very clear, I think we ought to be sure whether we are talking about a fiscal or calendar year when the record is printed. I hope you can make that clear.

Mr. WILSON. I should have said calendar year, and I will try to remember to say that. Calendar year is what we are talking about.

Here again, there will be no single date on which shortages will be ended. In the case of some materials which are now scarce, shortages may well be ended during calendar 1952. In the case of other materials, particularly copper, I do not foresee any substantial alleviation of our problems before calendar 1954, and very likely not fully then. And as new materials and new needs develop, as our military programs change to meet changing international situations, we can expect materials which are now scarce to become plentiful, and perhaps other materials which are now relatively plentiful to become scarce.

During the period of greatest shortages, our civilian economy will suffer to some extent, although it will operate still at a high level by any standard except the years 1950 and 1951. I regret the necessity for this, but none of us would choose the alternative of impairing our military strength or the necessary defense-supporting industrial expansion program.

These shortages will be hard on industries which use the more scarce materials, and cannot convert to defense production; they will be hard on labor in those industries; and they will be hard on the consumers of the products of those industries. We are working to ease the shock of these blows, and we must continue to do so, even though we will not be able to eliminate all of them. But if the mobilization program accomplishes its purpose, if the strengthening of the industrial and military might of this Nation and the free world, on which we have embarked, results in preventing an all-out world war, then I think we can all agree that the temporary hardships will have been amply justified.

The diversion of scarce materials to the military and to industrial expansion has reduced the amounts available for the civilian economy, for consumers' goods, and for housing and commercial construction. The effect of this diversion has varied from one material to another. In the case of the most scarce metals and forms, such as nickel, copper, and structural steel, the reduction has been very sharp. The result has been that many kinds of businesses have been cut drastically where they used these materials and could not find substitutes, while other industries have been able to operate at very high rates, even though somewhat below the record levels of 1950.

As the result of the continued production of most consumer goods, there have been few real shortages of important consumer products. The substantial inventories in the hands of consumers and distributors which were accumulated during 1950 and early 1951 have contributed to the relatively free supply of goods. These factors have added considerably to the stability in consumers' prices since the imposition of general price and wage controls in January 1951.

But with the continued diversion of scarce materials to the military and to the industrial expansion, and with the continued increase in purchasing power and savings in the hands of consumers, there is real danger of serious pressure upon prices. The Consumers' Price Index, which was virtually stable from May to August 1951, resumed its upward trend in September and is still rising. This gives us warning in the light of increasing scarcities and increasing savings that inflationary pressures are still very real and cannot be allowed to get out of hand.

The crucial test of our determination to curb inflation and to carry out our program to the end is just ahead. It will be during the next year that supplies will be shortest. After that we may expect a period of increasing improvement as we get closer and closer to the accomplishment of the objectives of the mobilization program. But we must push forward vigorously with the mobilization program, in order to achieve this security and end the period of shortages. Delays in the program will both impair our security and prolong the period of shortages.

In order to continue the program, we need continued statutory authority. Without the powers contained in the Defense Production Act achievement of our objectives will be impossible.

The CHAIRMAN. Congressman McKinnon, do you have any questions to ask at this point?

Representative MCKINNON. Mr. Chairman, I would like to ask Mr. Wilson in regard to our production facilities. These plants that we are building now are more or less stand-by plants for the future?

Mr. WILSON. Some are and some are not, Mr. Congressman. Some of them are plants which will be used immediately for the production of important items. Others are stand-by.

Representative MCKINNON. In this whole defense program we are creating a military productive facility while at the same time we are trying to maintain and likewise expand our civilian productive capacity?

Mr. WILSON. That is right.

Representative MCKINNON. And we are limiting the amount of hardware for the armed services in the next 2 or 3 years ahead, trying to time that, space that, to suit the needs of the world emergency, so that we do not end up today or 2 years from now with a lot of obsolete weapons, but rather have productive facility to manufacture them as we need them and have their design up to date; is that pretty much the philosophy?

Mr. WILSON. That is it pretty generally.

Representative MCKINNON. On these productive facilities that we are planning for war manufacture that will be stand-by in case we should get into a period of relative peace, but in the event of war, say, in the late fifties, will they be pretty much up to date or will they be obsolete, the same as the World War II weapons are today?

Mr. WILSON. I think they would be perfectly good for the jobs they had ahead of them.

Representative MCKINNON. As we change our designs, we must change our tools and our jigs, too, must we not?

Mr. WILSON. That is right. If the new designs that are concocted, for example, require new types of machine tools, we ought to have the sense to go in and provide the new machine tools.

Representative MCKINNON. In other words, endeavor to keep our plants up to date?

Mr. WILSON. That is right; but remember that in these rather fantastic new machine tools being turned out in 1952 are many categories of extremely modern tools, and I think they will be all right for the kind of weapons we are going to have to make for a considerable period. There may be some deviation.

Representative MCKINNON. But your view is that it would be relatively a minor matter?

Mr. WILSON. I would think so.

Representative MCKINNON. And this investment we are making will be worth while for a long time to come?

Mr. WILSON. Yes; you see, we have really had to make machine tools to take care of practically fundamental basic changes in the weapons.

For example, in the last war we used tools that could bend up and rivet, and what will you, aluminum for airplane wings. That was what, at the most? An eighth of an inch thick.

Now, we have to provide tools for handling the aluminum of, let us say, the wings of a jet fighter of three-quarters of an inch thick.

And we never had a milling job, for example. We never had to mill slots, and what will you, in three-quarters-inch thick aluminum for the wings of fighters. We have to do it now.

So, we had to provide rather difficult tools. We had to design the tools that could do it. But you can hardly conceive that in the next decade we are going to so change those wings that those tools that we are providing, to mill them down to a feather edge, and so on, that these tools that we are providing now will not be all right for that. I believe they will be.

Representative MCKINNON. Suppose in 1955 or 1956 or some period thereafter, after this productive facility is completed, and we had our stand-by war production facility plus our civilian production and we got into an all-out war, would we have the manpower and the resources available to carry on both a full wartime production and continue a pretty substantial level of civilian production?

Mr. WILSON. I think so. I believe so. Every survey indicates we would.

Representative McKINNON. The manpower is sufficient to man both the defense and civilian plants?

Mr. WILSON. That is right.

Representative McKINNON. That is all.

The CHAIRMAN. Congressman Patman?

Representative PATMAN. You have made a very fine statement, Mr. Wilson. I commend you for it. I do not think I will ask any further questions here. You have answered patiently all of the questions which I have asked so far, which I appreciate.

The CHAIRMAN. The impression has been gathered by this committee, Mr. Wilson, that part of the items budgeted for fiscal 1953 have been pushed forward into 1954; that is to say, part of the expenditures for plant and for delivered materials which had originally been planned to be made during fiscal 1952 or in 1953. What are the factors that entered into the judgment which pushed that expenditure on into the future about 12 months?

Mr. WILSON. Well, I think to some degree the design question. I think facing up to the fact that if we could make real improvements in some of these weapons, not only aircraft but some others, by taking time to further improve the designs, and one other factor—and this applies to aircraft as well as some others—since it has taken all of this time to get these designs shaped up the way everybody is satisfied, and we can begin production after we do the production-engineering job, and after we get the very special tools that it has been determined it will take to make these new designs—it has been found, and I think it is an augury of a better day in the spending of the taxpayers' money, that if we phase out the actual production maybe for another year, instead of trying to bring about a great hump of production in, let us say, the calendar year 1953, but phase it out a little bit more that you are going to get a whole lot more for the taxpayer's dollar by phasing it out 1 year more than you would otherwise.

The CHAIRMAN. Does it not involve the danger that by the time you get the mass-production plant finished it will be to some degree, at least, outmoded?

Mr. WILSON. I do not think so for 1 year. You are starting now from a very modern base, with some really fantastic engineering and scientific research having been accomplished. When you start from that base, I think the 1 year is not such a factor of obsolescence as it otherwise would be.

The CHAIRMAN. What they call the lead time on these items is constantly getting greater; is it not?

Mr. WILSON. Yes; it is, even greater than in World War II, in my judgment, although it is amazing how they are breaking down some of it, Senator.

The CHAIRMAN. Is that so? I am interested to hear that.

Mr. WILSON. For example, and I guess we had better not name numbers, but take some of the new things, one of the new fighter planes. Really, it is a pretty big step forward. I believe that plane will be in full production, well, within about 3 years, from what I can see now—it will be about 3 years, and it will hit a good, substantial production. We did not do that in the last war. We really did not fight any planes in the last war that had not been designed before Pearl Harbor that I can remember. But here we are, and we will be turning out a lot of them in 1953, designed just around Korea. I think they are doing a better job.

Representative PATMAN. Can you think of a single weapon that we used in World War II that was not in actual production before Pearl Harbor, except maybe the atomic bomb?

Mr. WILSON. That is about all that I could be sure of, Mr. Patman.

Representative PATMAN. In fact, they were all in production before Pearl Harbor?

Mr. WILSON. That is right.

The CHAIRMAN. Well, your ready response to all of the questions which have been directed to you, Mr. Wilson, and the clearness of your answers, I think, properly lead to the conclusion that you have presented to this committee, at least, a program which represents the very best judgment of patriotic men trying to do the best they can with the terrible dilemma for the defense of the country.

And I want to thank you, sir, for your presentation today.

Mr. WILSON. Thank you, Senator. Thank you all.

The CHAIRMAN. The next meeting of the committee will be on Monday morning in this room, when the Director of the Office of Price Stabilization, Mr. DiSalle, and the Chairman of the Wage Stabilization Board, Mr. Nathan Feinsinger, will be the witness.

The committee stands in recess until Monday morning.

(Whereupon, at 12:10 p. m., the joint committee recessed, to reconvene at 10 a. m. Monday, January 28, 1952.)

JANUARY 1952 ECONOMIC REPORT OF THE PRESIDENT

MONDAY, JANUARY 28, 1952

CONGRESS OF THE UNITED STATES,
JOINT COMMITTEE ON THE ECONOMIC REPORT,
Washington, D. C.

The joint committee met, pursuant to adjournment, at 10:30 a. m., in the caucus room, Old House Office Building, Senator Joseph C. O'Mahoney (chairman) presiding.

Present: Senators O'Mahoney (chairman), Sparkman, and Benton; Representatives Patman and McKinnon.

Also present: Grover W. Ensley, staff director; and John W. Lehman, clerk.

The CHAIRMAN. The committee will please come to order.

This morning we are to hear Mr. Michael V. DiSalle, Director of the Office of Price Stabilization, and Mr. Nathan Feinsinger, Chairman of the Wage Stabilization Board.

The television camera and its operators are in the room; and I think, if both gentlemen will come up and take their seat before the microphones, it will facilitate both the operation of the television mechanism and facilitate the presentation of the issues that are before this committee.

The issue, of course, which the committee desires to look into today through the testimony of both you gentlemen, is the issue of wage and price control, and the interplay of both factors, the effect of one upon the other, the success or lack of success which has been achieved thus far under the Defense Production Act, and the outlook for the future.

Mr. DiSalle, the papers seem to announce that you are planning to leave us shortly so, perhaps, it would be appropriate to begin with you.

STATEMENT OF MICHAEL V. DiSALLE, DIRECTOR, OFFICE OF PRICE STABILIZATION

Mr. DISALLE. Mr. Chairman, in view of my recent announcement, you can rest assured that I listened with rapt attention to your coaching with reference to television performances.

Mr. Chairman and members of the committee, as I approach the completion of my tenure as Director of Price Stabilization, I cannot avoid looking backward to the situation which prevailed when I took office just a little more than a year ago. I find myself contrasting the situation which prevailed then with that which faces us today, with deep gratification for the improvement which has taken place.

We certainly do not claim full credit for the striking contrast. Surely, many factors have contributed to our success, not the least of which has been the splendid cooperation of the American people. Yet I cannot help feeling that the efforts of our organization have played a substantial part in the remarkable reversal of the economic situation which has occurred. This feeling of having shared in a successful fight more than compensates for all the difficulties that are the daily lot of anyone who assumes the job of Price Director.

I am sure that you recall the situation which we faced a year ago. A year ago our economy was in danger—serious danger. Sober businessmen told me that they were deeply afraid—and well they might be. A flight from the dollar was in full swing—a flight whose severity has almost never before been matched in United States history. In just a few months, some prices had doubled—or even tripled—and the rate of increase seemed to be accelerating. Hard-headed business firms were frantically trying to build inventories out of all proportion to reasonable needs. Consumers were throwing caution to the winds and trying to beat the price rises and shortages that their own behavior was helping to create.

Let me emphasize again that the price freeze which we imposed a year and 2 days ago cannot be given all the credit for the sharp check of inflationary pressures we have experienced.

The CHAIRMAN. What was the date of the price freeze?

Mr. DISALLE. January 26—effective January 25.

The higher taxes and credit controls——

The CHAIRMAN. Is that 1951?

Mr. DISALLE. 1951.

The higher taxes and credit controls, the allocations and other measures of the supply agencies must be given an important share of the credit. Perhaps they would have resulted in some reversal, at some time at some level. But without the freeze, the crest of the wave would surely have come later, and risen higher. And the succeeding plateau would have been at a higher level.

Further, the problems of readjustment would have been much more severe. We all know that the backlash of speculation has been as severely felt in textiles as anywhere else. But I was very interested to hear a prominent executive in the textile industry say that, if it had not been for the freeze, his industry would have been faced with even more severe problems in the last 9 months than they have in fact encountered.

The CHAIRMAN. May I interrupt to say at this point, Mr. DiSalle, that the Economic Indicators for January 1952—which is a monthly publication issued for this committee—contains material on all aspects of the economic picture gathered from objective statistical sources.

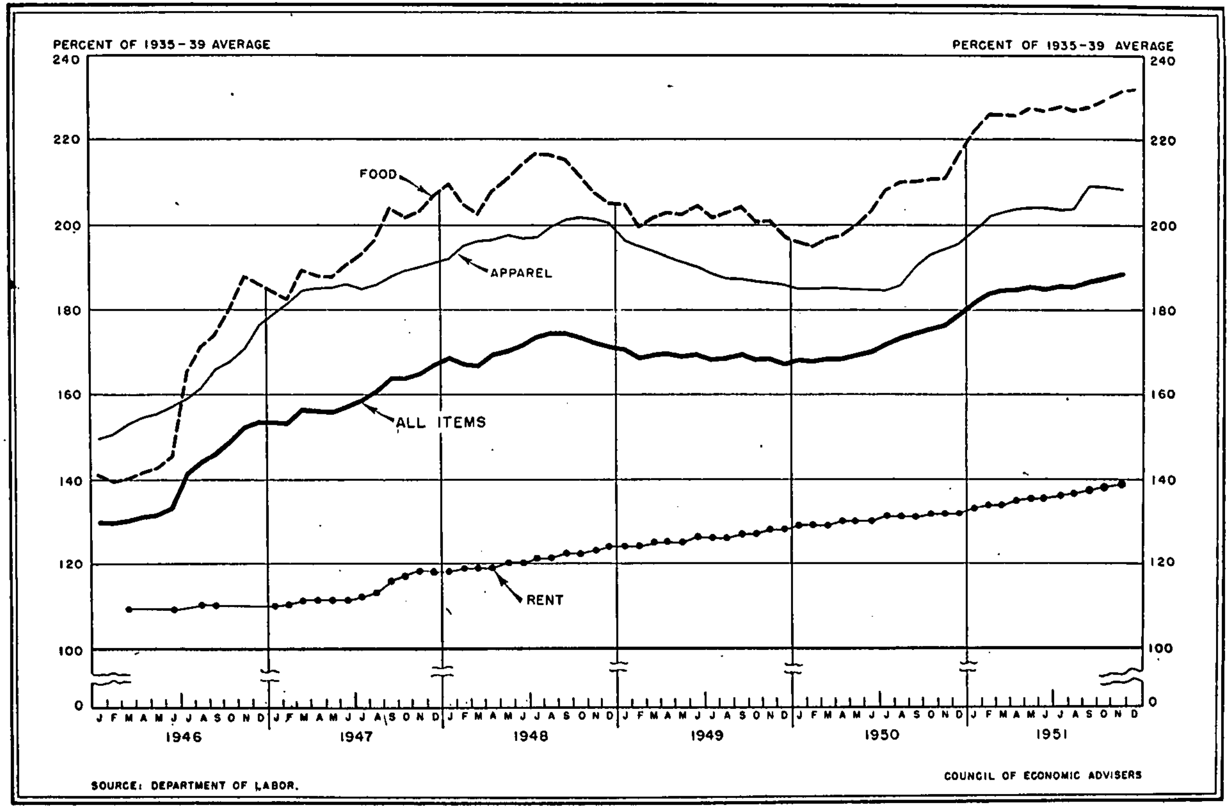
On page 3 of the January issue of Economic Indicators there is a chart showing the range of consumer prices, and a table which gives the index for all items for food, apparel, rent, fuel, electricity and refrigeration, house furnishings, and miscellaneous from 1939 on a monthly average through 1950 on a monthly average; and then for June 1950, November 1950, December 1950, followed by each month in 1951.

I am going to insert this chart and table in the record at this point because it has a bearing on what you are saying.

(The document referred to is as follows:)

CONSUMERS' PRICES

Consumers' prices rose another 0.6 percent between mid-October and mid-November. Apparel prices were the only group to decline. Retail food prices, which increased 1.0 percent, advanced another 0.6 percent by the end of the year.



Consumer prices

[1935-39=100]

Period	All items	Food	Apparel	Rent	Fuel, electricity, and refrigeration	House-furnishings	Miscellaneous
1939 monthly average	99.4	95.2	100.5	104.3	99.0	101.3	100.7
1943 monthly average	123.7	138.0	129.7	108.7	107.7	125.6	115.8
1944 monthly average	125.7	136.1	138.8	109.1	109.8	136.4	121.3
1945 monthly average	128.6	139.1	145.9	109.5	110.3	145.8	124.1
1946 monthly average	139.5	159.6	160.2	110.1	112.4	159.2	128.8
1948 monthly average	171.9	210.2	198.0	121.2	133.9	195.8	149.9
1949 monthly average	170.2	201.9	190.1	126.4	137.5	189.0	154.6
1950 monthly average	171.9	204.5	187.7	131.0	140.6	190.2	156.5
June 15	170.2	203.1	184.6	130.9	139.1	184.8	154.6
Nov. 15	176.4	210.8	194.3	132.5	142.5	201.1	159.2
Dec. 15	178.8	216.3	195.5	132.9	142.8	203.2	160.6
1951—Jan. 15	181.5	221.9	198.5	133.2	143.3	207.4	162.1
Feb. 15	183.8	226.0	202.0	134.0	143.9	209.7	163.2
Mar. 15	184.5	226.2	203.1	134.7	144.2	210.7	164.3
Apr. 15	184.6	225.7	203.6	135.1	144.0	211.8	164.6
May 15	185.4	227.4	204.0	135.4	143.6	212.6	165.0
June 15	185.2	226.9	204.0	135.7	143.6	212.5	164.8
July 15	185.5	227.7	203.3	136.2	144.0	212.4	165.0
Aug. 15	185.5	227.0	203.6	136.8	144.2	210.8	165.4
Sept. 15	186.6	227.3	209.0	137.5	144.4	211.1	166.0
Oct. 15	187.4	229.2	208.9	138.2	144.6	210.4	166.6
Nov. 15	188.6	231.4	207.6	138.9	144.8	210.8	168.4
December	189.1	232.2	206.8	139.2	144.9	210.2	169.1

The index has been revised, beginning with January 1940, to correct the downward bias resulting from the failure to take account of the differentials in rent between newly built housing and comparable existing dwellings. Certain changes, starting with January 1950, in commodity coverage and weighting were linked into the index providing an improved and consistent series.

NOTE.—Prices are for moderate-income families in large cities.

Source: Department of Labor.

The CHAIRMAN. The base of computation is the average price for consumers, of course, for the period 1935–39. That is taken as 100.

In 1939 the monthly average was running at 99.4; in 1944 it had risen to 125.7, and in 1945 the monthly average reached 128.6. That was the highest peak of consumer prices during World War II.

Price controls were abandoned, and in 1946 the monthly average rose to 139.5; 1948 to 171.9; 1949 it dropped back to 170.2, and the monthly average for 1950 was 171.9.

On January 15, 1951, it showed an index of 181.5; February, the month after you imposed your general freeze order, the increase was 2.3 points to 183.8.

There has been a steady but very small increase since that time, as illustrated by the fact that between February at 183.8 and August 15 at 185.5, there was an increase of less than 2 points.

There has been a change, however, recently. In October it jumped up to 187.4, November to 188.6, and the current price index issued by the Bureau of Labor Statistics for all items as of December 15, is 189.1.

Do those figures coincide with the information you have?

Mr. DISALLE. Yes, they do. Mr. Chairman, I was wondering in view of the fact that I have demonstrated that I can read and all the members of the committee do have this statement, in the interest of saving time, whether it would not be just as well to file the statement with the committee, and we will get down to the question at issue.

The CHAIRMAN. Of course, you have this advantage, Mr. DiSalle, you have written this statement, and you have read it before you came up here; but the other members of the committee have not had the opportunity of reading it. Certainly, the chairman has not.

Mr. DiSalle. I will be glad to continue.

The Chairman. If you will just proceed in the regular order.

Mr. DiSalle. It was the freeze that burst the bubble. No such bubble could burst without severe repercussions, many of which we are still paying for. But our situation today is infinitely sounder and more hopeful because of what happened 1 year and 2 days ago.

Last January the causes of inflation were largely psychological. It was impelled by fear. Fear of what? In part, fear of general war. But the basic international situation is today only little more secure than it was then. In larger part, it was fear of the economic effects of an expanded defense program. A year ago, we did not have, except on paper, such a program. We had a budget surplus; practically no increase had yet occurred in the defense take of our material and labor supply. What people then feared was precisely what is today rapidly becoming a fact.

Today the production level is higher and a much larger portion of the total is going to defense; today unemployment is lower; today most raw materials are scarcer; today the Government is operating at a deficit; today our world-wide commitments are greater. Today the economy is rapidly approaching the situation the mere fear of which a year ago caused frantic inflation.

Neither you nor I, however, could say or would want to say, fortunately, that the present situation is remotely as threatening to our domestic stability, or to our ability to defend ourselves, as it was last January. The relative stabilization which has been accomplished has more than all else been created by a return of public confidence that, although the value of the dollar is still seriously threatened, the Government can and will deal with inflation, and no major economic group will be victimized in the process.

From the excessive and highly speculative price levels at the time of the wage-price freeze 1 year ago, sensitime commodities have fallen 17 percent and wholesale prices about 4 percent. Resistance to inflation abroad—in most cases less successful than in the United States—has been strengthened by our success. Prices paid by consumers have not receded—in fact they have crept upward to successive peaks during the last 4 months—but their advance has been substantially slowed. While they are 3 percent above last February, they have risen less than most of us thought possible a year ago. And confidence in continuing stability is such that consumers are ready to save rather than spend their dollars. And here success feeds on itself—the increased savings rate in turn reduces the present pressure on prices.

In fact, the situation is so changed that some people question the need for continuing price controls at all; or, at least, whether a partial decontrol of "soft items" should not be immediately undertaken. Now I have repeatedly said—and I sincerely believe—that direct price controls should be removed as rapidly as we may safely do so. But premature or unwarranted action could do much harm. Controls—once removed—cannot easily, and should not hastily be reimposed.

Contrary to the impression gained from some quarters, OPS is still under plenty of pressure to raise ceilings. Perhaps some of you would like to spend a day in my office to appreciate just how much pressure. More than 1,000 companies have filed reports and applications under the Capehart amendment for ceiling price rises covering more than 5,000 product lines, and many more are coming in every day. I doubt if these applications are being filed as mere insurance, or for the pleasure of filling out our simplified forms.

The CHAIRMAN. Mr. DiSalle, on page 2 of your prepared statement, carrying over to page 3, you point out that last January the causes of inflation were largely psychological, that the rapid rise of prices in 1950, at the time of Korea, was due to the fear of shortages. You then say that while the conditions which were then feared no longer exist, other similar conditions do exist now.

Do you mean that conditions now developing by reason of the defense program are causing the need for controls to be greater and more in the public interest than ever before?

Mr. DISALLE. There is not any question about that, Senator.

The real questions that are being asked today are with reference to materials. I know that Members of Congress are being deluged by manufacturers in their own districts or States with reference to shortages that are beginning to occur in various lines, and so these pressures will continue to build through 1952 and, as Mr. Wilson has said, 1952 may be the most critical year of this whole defense program, as we step up the defense effort without quite catching up with the productive capacity needed to support our civilian effort.

The CHAIRMAN. You were about to discuss the experiences which you have in your office from day to day with respect to price levels.

Mr. DISALLE. The prices of almost all industries directly or indirectly related to defense, are pushing ceilings—the metal-producing and fabricating industries, industrial machinery and equipment, most chemicals and petroleum products. I earnestly wish there were some reasonable way of estimating what we have saved the taxpayers of the United States by holding down the cost of the items going into our defense program. I am sure that it is many times as great as the entire budget of the stabilization agencies. Just by way of indication, however, the "hard goods" purchased for defense are now running at the rate of about $16 billions and scheduled to rise sharply. If this cost has been reduced by only 1 percent, the expenditure on stabilization has far more than paid for itself.

The CHAIRMAN. You mean at the annual rate of $16 billion or the monthly rate?

Mr. DISALLE. The present rate, the current rate.

The CHAIRMAN. Well, what element of time? What time?

Mr. DISALLE. The present annual rates.

Turning now to consumer goods, the most important area is food. Apart from seasonal fluctuations and some soft spots, most food items remain at their high levels, and startling advances have occurred in prices of some foods on which we have so far been legally unable to put ceilings. In the fresh fruits and vegetables group, for example, wholesale cabbage prices are now 289 percent of those of last January and onions 262 percent. Very large price increases have also occurred in lettuce, potatoes, carrots, celery, green beans, and others which have helped push the cost of food to an all-time high.

Dairy products and meat, for the most part, are under heavy pressure. As high as present meat prices are, we are far from certain that they will not go higher where prices are below the minimum ceilings we can set. Prices of feed grains have been continuously moving up. Agricultural labor, rapidly forsaking the farms for more lucrative city employment, will command higher rates to remain on the land. Farm machinery, in competition with defense production, is becoming scarcer. Pressure on fertilizer may develop. Unless we are successful in controlling farmers' costs, food prices could easily rise significantly during the next year—and food prices are key items in maintaining the well-being and morale of our workers.

The CHAIRMAN. What are you doing to control farmers' costs or the sale——

Mr. DISALLE. Wherever we can, we have imposed ceilings on all manufactured products, things that the farmers buy.

The CHAIRMAN. Is it not a fact that most of the machines which the farmers, like the rest of the public, buy have benefited from increased ceilings rather than from lowered ceilings? Automobiles are more expensive now than they were 6 months ago.

Mr. DISALLE. As a result of the last Defense Production Act we have been forced to grant some increases due to the provisions of that act, which caused us to live in a cost-plus economy up to July of 1951. That was something that was created for us and not by us.

The CHAIRMAN. We have had examples of decreased ceilings on farm products and increased ceilings on products that the farmer has to buy which, of course, operates again to shift the so-called parity price.

Mr. DISALLE. But again in no case have the prices of farm products been decreased below the standard established by Congress itself, and that is the parity standard that has been written into the act; and in most cases where ceilings have been imposed, those items were substantially imposed at parity.

The CHAIRMAN. But my point is, Mr. DiSalle, how can you reduce the farmer's costs if you raise the prices of the things that the farmer must buy while decreasing the ceiling even to the level that Congress wrote into the law of the things that the farmer produces? Does that not widen the gap rather than narrow it?

Mr. DISALLE. Let us not forget, Senator, that a substantial part of the parity index of the things that farmers buy is food, and that it is constantly rotating situations that make it very difficult to achieve an absolute level of controls. For, if the price of food which the farmer produces continues to rise and that, in turn, increases the index of the things that he buys, parity continues to escalate, and we have had situations in the past year where although we have had a rise in the actual price of farm commodities those farm commodities have never quite reached parity.

The CHAIRMAN. Our objective is clear to hold costs down for the farmers; am I correct in that understanding?

Mr. DISALLE. There is not any question about that: not just for the farmer but for the Nation generally. Our objective is—we are not picking out any particular segment and saying "We want to hold the costs for you." We are trying to hold the costs of the consumer, the costs of the Nation which, of course, are the largest consumers of most of these items at this time, and keeps the costs down generally. We want to maintain prices so that neither the Nation gets penalized in its defense effort nor the consumer gets penalized as a result of the defense effort.

The CHAIRMAN. The average monthly index in 1950 for food, according to this exhibit which is already in the record, was 204.5. That index, of course, is based upon the average for the years 1935 to 1939, which was set at a hundred.

Now, in January 1951—on January 15—before your price freeze became effective, the food index was 221.9, 5.6 points above the figure for December 1950.

In November of 1951 this figure had risen almost 10 points to 231.4, and the latest figure on food is 232.2.

Have you looked into the question of what portion of this increase is due to processing?

Mr. DISALLE. We have maintained a fairly tight rein on distribution and processing costs, but we have been forced to pass through the increase of farm products toward parity, and a substantial part of the rise in food costs has been as a result of that rise.

Senator BENTON. Could I ask a question, Mr. Chairman?

The CHAIRMAN. Surely.

Senator BENTON. If all commodities continue to go up to parity and reach parity, have you made an estimate of about how much difference that would make in the price level before you would be able to take action?

Mr. DISALLE. Not recently. The last time that I checked that I think there was about a 5 percent spread between the price, the market price, and the parity price of those food items that were below parity.

Senator BENTON. My question was the sum total price level not just the price level applied to those particular products.

Mr. DISALLE. The sum total we estimated would be about a 2-percent increase over all.

Senator BENTON. Two percent.

Well, we are mostly up there by this time, and there is not much further left to go.

Mr. DISALLE. As I said before, parity itself keeps increasing, and so there has not been——

The CHAIRMAN. As the costs of the thing the farmer has to buy increased——

Mr. DISALLE. There has not been too much of that gap closed.

Senator BENTON. So you keep chasing it.

Mr. DISALLE. That is right. For example, in the price of hogs in January——

Senator BENTON. If it stood firm it would go up to 2 percent, your price level would go up 2 percent.

Mr. DISALLE. That is right.

Senator BENTON. But that, in turn, would push it up again.

Mr. DISALLE. That is right. In January 1951, for example, hogs were selling around $20. They got up as high as $23.75 and never quite reached parity. They were just about at parity all the time and we were waiting for them to reach parity so that we might impose ceilings.

Now hogs are back down to around $18.50, and they are substantially below parity, but under the law our ceiling prices of pork products still have to reflect parity.

Senator BENTON. Who worked out this clever formula for fixing parity? Do you know the antecedents?

Mr. DiSalle. I understand there is a man locked up in the Department of Agriculture—they never let him quite get out. But actually, as I have said many times before, if we did not have parity as a standard we would have to have some other standard for food, and some of the men who have had this job during World War II felt that parity was as good a standard as might be used.

The Chairman. I think the record ought to show what the real answer to the Senator's question is.

For more than 20 years, after World War I, there was a farm depression in the United States. Congress attempted on, three occasions I think, to do something about it.

The McNary-Haugen Act was passed on at least two occasions but whenever it passed Congress it was vetoed by the President and the farm prices continued to be very low. Farmers were suffering more than any other segment of the economy. That was, I think, generally recognized.

Then, early in 1933 the Agricultural Adjustment Act was passed. various farm-relief measures were passed, and one of the principles in the relief to the agricultural community, designed to stabilize prices, was this parity formula. The principle was merely that the farmer should get for his crops a price sufficient to enable him to buy things, the things that he had to buy during an arbitrary period of 1910 to 1914, taken as a base period.

Representative Patman. 1909 to 1914.

The Chairman. The theory simply was that farm products should buy just as many industrial products at any time as they were capable of buying during this base period. That is the brief explanation of the parity formula.

Senator Benton. I am very grateful to you, Mr. Chairman, for that explanation.

The Chairman. Of course, it is true, as the witness says, that as the prices of industrial commodities, that is to say, the things that the farmer buys, rise, the parity level rises.

Representative Patman. It did not include a profit to the farmer.

The Chairman. No; it did not.

Senator Benton. Could I ask one more question that goes along this same line, Mr. Chairman?

The Chairman. Surely.

Senator Benton. On your cost-plus, your very neat phrase the cost-plus economy, how much do you think the so-called Capehart amendment, which forced the cost-plus principle on your staff, may have added to the price level-index rise?

Mr. DiSalle. It is very difficult to estimate. As I said earlier, we do have applications from a thousand companies for about 5,000 product lines, and the applications are still coming.

I think the time will come when we will be definitely able to ascertain just what the cost of it is, but right now I would not want to venture a guess. But I would like to point out that when we talk about a thousand companies, with 5,000 product lines, the extent is much greater than is apparent from saying a thousand companies.

Senator Benton. Oh, yes.

Mr. DiSalle. For example, there are 9 or 10 automobile companies, but they are a very important factor in our economy, and when you increase the price of automobiles generally that is a big item.

Senator Benton. Do you not suppose there are some companies making trial runs here, running trial heats for other companies that are yet to come if the first venture is successful?

Mr. DiSalle. Another thing that we cannot estimate at this time is how many of those increases may have to be passed on at subsequent levels.

Senator Benton. Thank you, Mr. Chairman.

Mr. DiSalle. Unless we can maintain reasonable stability of food prices, we cannot expect stability of wages. Some 3 million workers have their wages formally tied to the consumers' price index. As their union leaders have often said, they prefer stable prices to escalated wages. But rising food costs have in recent months led directly to rising wages. Take, for instance, the wage increase of 4 cents an hour for 1,250,000 railroad workers on the basis of the cost of living increase between August 15 and November 15, 1951; price increases for fresh fruits and vegetables alone were responsible for half that increase. This but a small illustration of the way in which the entire stabilization progra mis affected when food prices rise.

Consumer soft goods—textiles, apparel, shoes—represent the one area where some softness is almost universal. Even here there are significant exceptions—but they are truly exceptions. In part this is still a "hangover" from the speculative spree of a year ago. In part it reflects the relatively good cotton crop this year. Continuance of this situation will depend on another good cotton crop—and it is too early to make any forecast on this score. Developments in the highly volatile world wool market could also create new trouble. We can hope for good fortune in both respects, but can we count on it? Even more important, continued stability in this area depends upon the continuance of moderation in consumer buying, and on that we surely cannot count unless public confidence in price stability is maintained.

In the case of consumer durable goods, current buying levels and high recent production have likewise created some price weakness, but far less general and less marked than in soft goods. Here, the outlook is for decreased production because of decreased availability of steel, copper, and aluminum, and the inventory situation is gradually but steadily changing.

One of the things that I am sure you want to know, is precisely how many commodities are selling below ceiling, which ones they are, and how far below ceiling they are. This is a question we have been making strenuous efforts to answer. I wish the answer were ready now, but it is not. It is one of the most baffling questions that statisticians have faced. We are doing our best to get the fullest and most accurate story we can get, and, as soon as it is ready, Congress will receive it.

The Chairman. I can give you one commodity.

Mr. DiSalle. Yes; I understand you are familiar with one commodity.

The CHAIRMAN. Perhaps I might be familiar with some others. I, of course, had in mind the price of wool upon which there was——

Mr. DISALLE. I wondered if that might come up today.

The CHAIRMAN. I might also have in mind the price of potatoes on which I am still working on the OPS, I think, with some success, however.

Mr. DISALLE. I have a distinct feeling, and our study so far supports it, that the extent of price weakness has been greatly exaggerated by some who have only a supervicial knowledge of the situation or by some who use this as a means to attack controls generally. But I want, and Congress deserves, the facts.

The question of soft markets not only raises these statistical questions, but policy problems as well. These problems have been receiving continuous and sincere study in our agency. Up to this point, we have been, and still are, quite convinced that we should not properly take the risk of any major decontrol. It may very well be that this will continue to be the case in the months ahead. But we do not want to incur any risk that this problem, and similar problems, of longer range policy become submerged in our day-to-day activities, or that a purely negative attitude may unconsciously develop. Consequently, I am now preparing to appoint a top-level committee within the agency with the following mandate:

(1) To explore critically and continuously the question of decontrol in specific areas where price pressures, at the moment, are largely absent;

(2) To explore all possible means for reducing or eliminating any burdens of computation, record keeping, or reporting which our regulations impose in areas which remain under ceiling, but where ceilings are, at any particular time not effective; and,

(3) To develop standards under which we can continually test whether decontrol is feasible, and, when it becomes feasible, to provide an orderly and objective procedure for its accomplishment.

Representative PATMAN. Mr. Chairman, I would like to ask Mr. DiSalle a question.

You state that you have selected a committee to pass on these present problems, in particular.

Mr. DISALLE. I said I am about to select.

Representative PATMAN. You are about to select.

My question was going to be: When is the committee going to report?

Mr. DISALLE. It will be a continual——

Representative PATMAN. Continuing committee?

Mr. DISALLE. That is right.

Representative PATMAN. You know the crticism I get is that you just never get around to it; it is too slow operating I know that you cannot satisfy everybody, and whatever you do seems too slow to a lot of people, but it occurse to me that these problems should have immediate consideration.

Mr. DISALLE. That is why we are setting up——

Representative PATMAN. I was encouraged and almost thrilled to think that you would appoint a committee to do this. Now, you tell me that you are thinking about appointing a committee.

Mr. DiSalle. No; we will appoint the committee.

Representative Patman. You will appoint a committee.

Mr. DiSalle. Appoint a committee. We are about to appoint a committee which will be a committee within our office, and a committee which will devote full time, as nearly as possible, to these problems.

(The following letter, naming the committee discussed above, was received after the close of the hearing and is made a part of the record:)

Office of Price Stabilization,
Office of Director,
Washington, D. C., February 11, 1952.

Hon. Joseph C. O'Mahoney,
Joint Committee on the Economic Report,
The Capitol, Washington, D. C.

Dear Senator O'Mahoney: Pursuant to the discussion before the Joint Committee on the Economic Report on January 28, I have named an intra-agency committee to study the question of suspension of ceilings or decontrol composed of the following officials of the Office of Price Stabilization:

Edward F. Phelps, Jr., Assistant Director of OPS for Price, Chairman
Joseph Freehill, Acting Chief Counsel
Gardner Ackley, Assistant Director for Economic Policy
Tom Karsten, Director of the Consumer Goods, Distribution, Textile and Apparel Division
George Mehren, Director of the Food and Restaurant Division
Robert V. Faragher, Associate Chief Counsel for Legal Review
Franz Wolf, Director of the Research and Statistics Division, Office of Economic Policy

The Committee will report its findings to the Director of the Office of Price Stabilization, and he will in turn transmit them to the Economic Stabilization Agency.

Sincerely yours,

Michael V. DiSalle.

Representative Patman. A continuing study, in other words?

Mr. DiSalle. A continuing study.

Representative Patman. I can see the necessity for it.

Mr. DiSalle. Because these problems will arise in one area at one time and another area at other times.

Representative Patman. But in products where it is obvious they should not be controlled, why can't you get around to them right away?

Mr. DiSalle. It is never an obvious thing.

Representative Patman. It is never that obvious? Well, I am not as familiar with it as you are, not by any means—in fact, I am not familiar with a great many of them—but it occurs to me that some, if you were to go over the list, would be obvious.

Mr. DiSalle. We are decontrolling. We do have standards for decontrol, and we are decontrolling items which we feel are insignificant in the cost of living, and where the administrative burden would far exceed the cost of attempting to keep those items under control. There has been a long list of those items decontrolled. But in major segments of the economy we just have not felt that the time has come where we could do that.

Senator Benton. Mr. Chairman, could I ask a question?

The Chairman. Senator Benton.

Senator Benton. If your committee is successful in reducing these burdens of computation, record keeping, and so on, why should there be such pressure for decontrol? What difference does it make to the manufacturers, apart from the problem of the records whether he is controlled or decontrolled, if the competitive conditions in his field bring his prices below the price levels?

Mr. DISALLE. Well, there are a good many reasons. In some of the depressed industries, people in those industries——

Senator BENTON. Why do they want decontrol so badly when they are below the price ceiling, that is what I would like to know.

Mr. DISALLE. Well, they feel controls, regardless of the record-keeping provisions, have some effect.

Senator BENTON. Will depress the prices.

Mr. DISALLE. That is right.

Senator BENTON. The very fact they are not decontrolled depresses the prices?

Mr. DISALLE. That is right.

Senator BENTON. Do you think that is true?

Mr. DISALLE. We have not found it true. We feel in some areas where prices are largely speculative that that is true.

Senator BENTON. It sounds pretty theoretical.

Mr. DISALLE. But when you reduce the area of speculation in those commodities it is bound to keep prices down, but that is the purpose of the program.

Representative MCKINNON. Mr. DiSalle, right there, if we had had that amendment in the Defense Production Act that would eliminate speculation in the market, many of our commodities would be much lower, which indicates that speculation does have a tremendous influence on the price situation.

Mr. DISALLE. Well, we found that it does have an influence on the price situation.

Representative MCKINNON. So when you have your price ceiling you take that speculation out of it.

Senator BENTON. What other reasons are there besides the record keeping and the fear of some people that controls depress prices, what other objections are there?

Mr. DISALLE. I have not run into them or have not heard any reasons why.

Senator BENTON. If you reject as being theoretical or doctrinaire the theory that that decreases prices, you are left mostly with your point 2, which relates to hiring of lawyers and accountants and record keeping and things of that kind?

Mr. DISALLE. That is right.

The CHAIRMAN. Do you control the prices of luxuries?

Mr. DISALLE. Some items. Mink coats are still under control, although they tell me that that market is soft recently.

The CHAIRMAN. I have a clipping from the Wall Street Journal of last Friday which reads as follows:

> The Office of Price Stabilization ruled that six major-league baseball clubs could boost their admission charges. The rule affects the two Philadelphia and Chicago clubs and those in Cleveland and Detroit.

This seems to mean that baseball fans in Philadelphia, Cleveland, and Detroit, under an OPS order, will this year have to pay a higher admission charge. Can you explain the theory upon which OPS goes into that field at all?

Mr. DiSalle. Well, under the law we are charged with the control of the entire economy, services as well as commodities.

In World War II there was an interpretation of the law at that time which said that it did not apply to spectator sports, and baseball was not under control.

This time there is no such ruling, and the law could not be interpreted to exempt them. So we adopted an industry-wide regulation making a study of what clubs seemed to be in need and what clubs were not in need, and established dollars-and-cents ceilings for the season, which can be changed from season to season.

For example, the two Chicago clubs had had no price increase for 33 years, and the increases that were granted were largely to bring them in line with prices that were charged around the league.

The Chairman. Well, frankly speaking, if they had not increased their prices during the period of 33 years, that level had nothing to do with Korea or defense or any of the bitter problems with which we are now struggling. It was a voluntary act upon the part of the club owners.

Mr. DiSalle. But they have also had increases in operation, in operating costs.

Senator Benton. You mean the cost of ballplayers is going up.

Mr. DiSalle. Well, the cost of transportation, which is part of their operating costs, the cost of help around their parks, other items.

Baseball is a very difficult sport to get into at all, because a winning ball club usually attracts crowds, and a losing ball club does not attract crowds, and it varies.

If the Chicago ball club should have a good season next year, maybe the price increase would have been entirely immaterial to them.

The Chairman. There is a committee of the House, the Judiciary Committee, the chairman of which, at least, seems to feel that baseball is quite a monopoly, which controls the lives of the players, the salaries they get, the opportunities they get.

I am wondering quite seriously whether that old rule to which you refer during World War II would not be a good rule.

Is there anything in the law which prohibits you from saying that spectator sports are not subject to control?

Mr. DiSalle. No; there is nothing in the law that would prevent us from decontrolling. But you start off a large chain of decontrol steps that would be necessary. You start decontrolling baseball, and then you have got football, you have got boxing, you have got hockey, and if you decontrol the spectator sports, then you have got the participant sports, people who bowl, and then if you decontrol bowling, it leads on to subsequent steps, and at this particular time you are doing no particular harm in maintaining some sort of level of prices in those industries. If you control an essential defense industry and do not control someone else, you create a feeling of inequity among those people who are engaging in a defense effort that they are being controlled whereas someone else who is not contributing a great deal to the defense effort, is permitted to go on unchecked and just to do practically anything that he pleases.

The Chairman. Is this newspaper account correct in saying that only four cities are affected by the rule?

Mr. DiSalle. That is right. We checked over the 16 clubs that participated and brought these other clubs in line with those prices.

The CHAIRMAN. Mr. McKinnon?

Representative MCKINNON. I was wondering what sports you do not control, Mr. DiSalle.

Mr. DISALLE. The only sports that are not controlled are college and high-school sports where we can draw a line as to operation for profit or not for profit.

I cannot stress strongly enough the dangers of premature decontrol, particularly at this time when pressures are still building up. On the other hand, all of us are united in our abhorrence of controls for controls' sake. Perhaps, somewhat later on, my successor can report to you on the progress of this study.

Meanwhile, as the President's Economic Report so clearly indicates, my successor will have no easy time. The build-up of inflationary forces which the report foreshadows will mean that soft spots will become fewer and upward pressure on prices even more general. I have every confidence that my successor, whoever he may be, will be able to keep prices reasonably stable. He can count on the help of the organization which has been developed, and he can build on the solid foundation which has been laid. But he will also need the wholehearted support of every patriotic American.

Representative PATMAN. Mr. Chairman, I want to ask him about a commodity about which there has been a lot of publicity recently, and I do not know whether it is dog food or human food, and that is horse meat. What is the situation with regard to the sale of horse meat?

Mr. DISALLE. We have uncovered a very distressing situation in Illinois where a ring has been engaged for some time in a very systematic sale of horse meat under the guise of prime beef.

The investigation each day develops more and more. It is a far-flung operation which has many, many ramifications. It is not something that has existed since the imposition of controls, but something which has existed and flourished for many years, and we expect that some of the ramifications of this investigation will make itself felt in many sections of the country.

Last September in San Diego, in speaking on the meat situation at that time and the fact that there was a great deal of pressure for decontrol, we invited the meat industry in to cooperate with us, the legitimate members of that industry, to try to bring an end to these practices which have hounded the meat industry for years and which have made it very difficult for a legitimate operator to operate and continue to exist.

At that time some of the segments of the meat industry said it was the rantings of a frustrated man. But I am sure that when the committee is made aware of the entire investigation in Illinois they will realize that it was not the rantings of a frustrated man but that it was based on very solid evidence. Even the Chicago Tribune in an editorial said it was an ill wind that brought no one no good; that even OPS had rendered some service in uncovering this situation.

I am sure that story, when it is told, will raise the hair on the heads of some of the members of the committee.

Representative PATMAN. You mean just in Illinois or in other States as well?

Mr. DISALLE. It will also go to other States.

Representative PATMAN. How far-flung is it? Has it reached New York and Texas and California?

Mr. DiSalle. We have some evidence in the Northwest and some in the East.

Representative Patman. None in the cattle regions?

Mr. DiSalle. No; none in the cattle regions, except we did run into some evidence of it in New Mexico.

Representative Patman. That is, the sale of horse meat for human consumption is what you are talking about?

Mr. DiSalle. That is right; under the guise of beef.

Representative Patman. Under the guise of beef. How can you tell a horse-meat steak from a beefsteak; do you know about that?

Mr. DiSalle. I know a lot of things, but that is one I do not know.

Representative Patman. I have always been told where you have a fillet that sometimes it is difficult to tell, but if you get a steak with fat on it you know it is beef.

Mr. DiSalle. I just would not know.

The Chairman. You say this report is to be submitted to a committee. I assume you mean to the Committee on Banking and Currency, which has jurisdiction over the legislation?

Mr. DiSalle. Yes, sir; as part of our regular report. It is now in the hands of the Department of Justice, and I understand a grand jury has been called to receive the evidence.

The Chairman. When do you think it will be submitted to the committee?

Mr. DiSalle. I would not be able to tell yet, because——

The Chairman. Have you advised the chairman of either the committee in the House or the Senate——

Mr. DiSalle. Because every day our investigation develops some new leads.

Representative Patman. Will it be within 30 days, 60 days, or 90 days?

Mr. DiSalle. Yes; I am confident that it will be.

Representative Patman. Within 30 days?

Mr. DiSalle. Yes; 30 to 60 days.

Representative Patman. Thirty to sixty days. All right.

The Chairman. Your reference to the appointment of a committee to consider decontrol, where decontrol is possible, is followed by your warning against the premature lifting of beef controls. The huge expenditures which are required to purchase hard goods required by the three Departments of Defense, the weapons of war, are increasing all the time and creating shortages of certain materials, diverting materials, say steel, from the building of schools and hospitals, so desired by so many communities throughout the land, to the building of tanks and other implements of war. These will create the inflationary condition which drives prices upward, both for the cost of living and for the cost of defense.

How do you differentiate, how do you classify, the industries which you now feel can be subject to decontrol?

Mr. DiSalle. Well, that is exactly the point that we make; and, while we caution against premature decontrol, you have some real problems in connection with any major decontrol movement.

For example, even though prices may be soft in an area, if you decontrol that particular area you are faced not with a legal problem but with a real practical problem as to whether or not you decontrol wages in that particular industry. And, should you decontrol wages in that particular industry, do you say to the worker on one side of the street—that is, in that industry—that "Your wages are decontrolled," while the worker who is in an essential defense industry across the street, his wages must be controlled, and where do you draw the line? There are many questions of possible manpower shifts; and so, as long as this Nation is engaged in a defense effort and as long as the control program is not interfering with production, I would say that doubts should be resolved against decontrol. But I do think that it is not too early to start making a study and establishing standards as and if we find that decontrol can be achieved without harming the over-all effort, that we should do it.

The CHAIRMAN. Have you received any evidence from any source, governmental or otherwise, that the pressure for continued manufacture of defense material is likely to fall off in any foreseeable time?

Mr. DISALLE. No. Every evidence goes to the contrary, of course.

The CHAIRMAN. So that it would be a mistake to assume from this discussion of the study of possible decontrol areas that there is any likelihood that in the near future there will be any serious decontrol.

Mr. DISALLE. That is right. We have definitely turned down requests for decontrol in areas where markets are soft at the present time. But I think we ought to try to avoid the mistakes that were made the last time, when we had precipitous decontrol and where prices shot up so quickly because decontrol was achieved before we had sufficient production to take up the slack.

The CHAIRMAN. Are there any other questions?

Senator BENTON. I have two questions.

The CHAIRMAN. Senator Benton.

Senator BENTON. I think this would be of particular interest to Mr. DiSalle in view of his announced intentions.

Last week I was in Connecticut, sitting next to a shrewd lady, formerly our State secretary of state, who lost by only 400 votes in the last election out of a million votes cast.

She said, "Senator Benton, the biggest issue in this coming election is going to be prices. Don't be fooled by Korea or anything else; it is going to be prices. You go down and find out why does butter cost 95 cents a pound. That is the question."

I don't have the retail-price curve before me, but a year ago the wholesale price of butter was 68 cents; today it is 79½ cents, which must indicate a retail jump of close to 20 percent when you add the retail markup in there.

Mr. DISALLE. I think you will find butter is still below parity.

Senator BENTON. You are going to be asked this question rather shortly, and I would be interested in your comment on it this morning. It is just the general subject: Why does butter cost 95 cents a pound?

Mr. DISALLE. There have been increases in production costs that we just can't avoid, and I think, Senator, that Senator O'Mahoney pointed out very well that costs to the farmer have also increased as well as costs to everyone else.

Those increased production costs are reflected in higher prices. Now the fact that we have been able to hold the increase in cost of living through 1951 to 2.9 percent is a lot better than we anticipated we would be able to do, because you find that from Korea to the freeze there had been an increase in wholesale of about 16 percent, which had not yet been reflected at retail; you had a 5-percent spread between the price of raw agricultural commodities and parity, which we thought would be translated into price increases; and you also had some hardship adjustments that would necessarily have to be made because a good many industries were depressed just prior to Korea.

Senator BENTON. This affects the parity price of butter?

Mr. DISALLE. That is right.

Senator BENTON. That is the start of the question?

Mr. DISALLE. That is right.

Senator BENTON. So butter has never been an item that you have exercised any control over at all?

Mr. DISALLE. No; we never have. And fresh fruits and vegetables have increased 23 percent in the past year. It is one of the items we have never been able to impose controls on until we imposed ceilings on potatoes just a few weeks ago. Potato prices reached parity at about January 4. We had the official announcement somewhere around there.

Senator BENTON. How much does butter have to go at 79½ cents?

Mr. DISALLE. I don't have that exact figure, but I think butter is somewhere between 90 and 100 percent of parity now.

Senator BENTON. My second question is: Out of your experience, what authority do you think your successor ought to have which you have lacked in order to do a stronger and better job in this area of price control?

Mr. DISALLE. I would rather wait until the President's message comes up and discuss it before the Senate Banking and Currency Committee.

Senator BENTON. Your answer now is you need more authority?

Mr. DISALLE. Yes; there is no question about that, in view of the amendments like the ones we got last time that weakened our authority.

Senator BENTON. You pointed out the Capehart amendment—or shall I call it the Capehart-Bricker amendment for your benefit?

Mr. DISALLE. I would just as leave you wouldn't mention the name at all.

Senator BENTON. That weakened the act, but what other amendments were the principal ones that weakened the authority you needed?

Mr. DISALLE. The Herlong amendment, of course, was harmful. For example, when you imposed excise taxes during the past year in some cases we were forced to permit the customary percentage markup on top of excise taxes as a result of that amendment. Those were the two principal harmful amendments.

The Butler-Hope amendment, of course, which took away the power to impose slaughter quotas, we felt was harmful; but that in itself has not been felt in the price situation to date.

Senator BENTON. It hasn't had the bad effects that were prophesied by Senator Anderson? He called it the black-market amendment on the floor of the Senate.

Mr. DISALLE. It was very harmful from the standpoint that we had to devote a great deal more of our enforcement organization to that particular field than would have been necessary had we had slaughter quotas.

Senator BENTON. That is all I have, Mr. Chairman.

The CHAIRMAN. I am just tempted to remark that my own feeling is that, with an amendment of that kind in a field where so many individuals are in the production of meat animals, you probably would have needed a much larger enforcement agency with slaughter quotas than without them. But that is just an opinion and doesn't go into the merits of the discussion here, which, of course, after all, is simply whether or not controls have held down the cost of living and cost of defense and whether they can be safely abandoned at any reasonable time in the future, considering what the Government has to do.

Mr. DISALLE. Senator, there is no question in my mind—you take controls off tomorrow and prices would begin to rise. There is no theoretical substitute for saying to an individual, "You can't increase your price." You might say all you want about indirect approaches, but Canada has been operating with the indirect approach, and their cost of living has increased more than three times the increase in this country during the same period of time.

It is just a natural human impulse—if the traffic is going to bear it and you can get an extra nickel for the thing you are selling, you will get that extra nickel.

Senator BENTON. Is that 9 percent for them against our 3 percent in that period?

Mr. DISALLE. Yes. We checked a month ago, and our cost of living had gone up 2.6 percent, while Canada's had gone up 9.1 percent in the same period.

Senator BENTON. If you took the longer period since the outbreak of the Korean war, what would the comparison be? Their method may have worked more successfully earlier. It seems to me you should have both sets of figures.

Mr. DISALLE. Their index was less than ours at that time, and in the meantime they have approached it and passed us.

Senator BENTON. I see.

The CHAIRMAN. Congressman McKinnon?

Representative MCKINNON. What happens when you get wage increases given by industry? Is OPS allowing ceiling increases?

Mr. DISALLE. We are not allowing an automatic pass-through. We are using the earning standards on those cost increases incurred after July 26, 1951. We are requiring that we measure those cost increases against the earning standard and requiring absorption where it is possible.

Representative MCKINNON. What sort of yardstick do you use in that? I think Mr. Johnston said 85 percent.

Mr. DISALLE. That is right. The earning standard given to us by Mr. Johnston in April 1951, said that no price increase may be granted if the earnings were in excess of 85 percent of the best 3 years from 1946 to 1949.

The CHAIRMAN. Senator Sparkman, do you have any questions?

Senator SPARKMAN. I believe not, Mr. Chairman.

The CHAIRMAN. Mr. DiSalle, the committee is very much obliged to you, sir, for your prompt and clear answers to the questions which have been asked of you.

Mr. DISALLE. Shall I stay here and help Mr. Feinsinger now?

Mr. FEINSINGER. I wish you would.

The CHAIRMAN. I think possibly the interplay of wage and price may be a little more active now than it was while you were testifying.

Mr. Feinsinger, will you please state for the committee your name and your function, sir?

STATEMENT OF NATHAN P. FEINSINGER, CHAIRMAN, WAGE STABILIZATION BOARD

Mr. FEINSINGER. My name is Nathan P. Feinsinger, and I appear here as Chairman of the Wage Stabilization Board.

The CHAIRMAN. How long have you occupied that position?

Mr. FEINSINGER. Since around the 1st of September. I had previously been Vice Chairman. I came to Washington on May 8, the date the Board was organized, to help Dr. George W. Taylor organize the Board, for a period of service which I thought would last about 2 months.

The CHAIRMAN. What was your previous background?

Mr. FEINSINGER. My regular job is teaching law at the University of Wisconsin Law School. I served with the War Labor Board in World War II in various capacities, including that of a public member of that Board.

I have also served as special representative of the President and of the Secretary of Labor in various labor disputes involving economic matters and have, of course, taught labor law and collective bargaining as one of my regular subjects.

The CHAIRMAN. You may proceed.

Mr. FEINSINGER. Mr. Chairman, before I proceed with my prepared statement, I would like to say this: It is not customary for officials in charge of wage stabilization to give too much credit to the price-stabilization program, but in this case I want to say that I think Mike DiSalle has done a magnificent job under very difficult circumstances, a job for which the Nation should be grateful. I am sorry to see him go.

Mr. DISALLE. Have you got any relatives in Ohio?

Mr. FEINSINGER. No, but I have a few friends there.

The CHAIRMAN. Proceed.

Mr. FEINSINGER. Mr. Chairman and members of the committee, I appear in response to your invitation to discuss the President's economic program, and in particular the economic report by the President. I might say I am not going to discuss our disputes function which stem directly from the President, although the wage stabilization problems involved in a case like steel, aluminum, et cetera, obviously are related to the over-all stabilization problem.

The portion of the report devoted to wage stabilization, page 24, reads as follows:

WAGE STABILIZATION

Wage stabilization, like price control, cuts the inflationary spiral and limits the rise of prices and costs and should be continued. It also helps to prevent buying power from rising too far above the available supply of civlian goods. The policies of the Wage Stabilizaiton Board are designed to put a brake upon excessive wage adjustments, while at the same time recognizing that some adjustments in a free and dynamic economy are essential from the viewpoint both of equity and incentives.

I would like to stress throughout my discussion from the viewpoint both of equity and of incentives.

Adjustments to take account of increases in the cost of living are a matter of simple equity, because price inflation is not a fair way to impose the burden of national defense. The fair way to impose the burden of national defense is by taxation and other restraints which can be equitably imposed. Wage adjustments to allow for increases in productivity, if carefully limited and firmly administered, can provide incentives which outweight any possible inflationary effect. There are a few other specialized problems with which the Wage Stabilization Board must deal.

To avoid inflation, we must maintain a firm price policy and a firm wage policy throughout the peak of the defense effort, and we must maintain a fair relationship between the two.

That is the end of that portion of the President's Economic Report devoted to wage stabilization.

I would like to discuss the objectives of wage stabilization as I see them, the policies of the Board now in effect, the policies still pending before the Board, and some aspects of the relationship between wage stabilization and the over-all economic stabilization program.

The immediate objective of wage stabilization is to help combat the threat of inflation in a defense economy. Increases in wage rates may add to inflationary pressures in two ways: by adding to purchasing power and by adding to business costs. I refer specifically to wage rates because our primary task is to stabilize rates rather than earnings. Today the Nation is interested in maximum production. This means increased earnings through increased employment, increased hours, increased output through incentive systems, and the like. The advantages derived through such increased earnings obviously outweigh any possible inflationary effects.

Obviously it would be wrong for the Board to stabilize wages without regard to the primary objectives of the Defense Production Act. In title IV, Congress directed that in stabilizing wages regard be had among other things for the "maintenance and furtherance of sound working relations, including collective bargaining"; and the prevention of "economic disturbances, labor disputes, interference with effective mobilization of national resources and impairment of national unity and morale." Congress stressed that the stabilization program must help to achieve "maximum production" and must be administered in a way which is "generally fair and equitable" and which will "prevent or correct hardships and inequities."

I believe that Congress was right in adopting this broad concept of wage stabilization. It was also right in refraining from laying down any specific formula which would hamper the Board in developing a program geared to the dynamic needs of a defense economy.

I might interpolate here to say I hope Congress will keep this authority in mind in its consideration of extending the Defense Production Act.

In keeping with the philosophy of Congress, the Board has rejected a "slide rule" approach to wage stabilization. It has sought instead to develop a fair and flexible program on the basis of experience and the combined wisdom and judgment of its tripartite membership.

A flexible program must not be confused with a program of steady retreat under pressure. On the other hand, "a firm price policy and a firm wage policy," in the words of the President, does not mean a frozen price policy or a frozen wage policy or wage stabilization policy.

My second point deals with a review of wage stabilization policies now in effect.

The Board's regulations are permissive only. They do not require the payment of any particular wage. They establish criteria for voluntary wage adjustments. The boss has to agree to give it before we have anything to do with it in the Board, except where there is a dispute which is referred to us.

Congress has defined "wages, salaries and other compensation" as including "all forms of remuneration to employees by their employers for personal services, including but not limited to, vacation and holiday payments, night shift and other bonuses, incentive payments, year-end bonuses, employer contributions to or payments of insurance or welfare benefits, employer contributions to a pension fund or annuity, payment in kind, and premium overtime payments." The Board must therefore stabilize every such element of compensation. Each separate pay practice or problem requires separate consideration.

The CHAIRMAN. If that is the case and separate consideration has to be given to every separate practice and every separate problem, the question arises—particularly since the regulations are permissive only—to what extent voluntary wage adjustments have been made upon the basis of these findings which you have just summarized.

Mr. FEINSINGER. If I get your question, there has been no voluntary wage payment made as a result of a collective bargaining agreement or otherwise, assuming it is a legal payment, that has not been made within the standards established by the Board or approved in an individual case on the basis of a special showing of hardship and inequity.

The CHAIRMAN. I didn't make myself clear. You said that the regulations are permissive only.

Mr. FEINSINGER. Yes.

The CHAIRMAN. And "they establish criteria for voluntary wage adjustments."

Then you outline the various considerations which must be taken into account. So I am trying to determine to what extent industry has voluntarily followed the suggestions embodied in your regulations.

Mr. FEINSINGER. I think I have some statistics bearing on that point, Mr. Chairman, a page or two later on. I don't know whether your question relates to statistics or whether it relates to something else.

The CHAIRMAN. Have you found that industry voluntarily does or does not follow the lead of the Wage Stabilization Board, in the majority of cases? What is characteristic?

Mr. FEINSINGER. Well, what is characteristic is a wage settlement voluntarily arrived at which embraces some progress on some of these items.

The CHAIRMAN. Now you are making it individual. I am trying to get the picture as a whole. Has industry voluntarily followed the suggestions of the Wage Stabilization Board?

Mr. FEINSINGER. They have made their agreements voluntarily within the regulations, within the criteria that the Board has established. The Board has not suggested a settlement for any industry or any company or any plant except where it has had a dispute case referred to it, Mr. Chairman.

The CHAIRMAN. I understand. The question to me seems perfectly simple. To you it seems to be complex and difficult to understand.

All I am trying to determine is whether or not there has been resistance to the suggestions which you make for voluntary adjustments.

Mr. FEINSINGER. I would answer that——

The CHAIRMAN. Such resistance which has resulted in not getting the adjustments which you recommend—or do you get the adjustments?

Mr. FEINSINGER. There has been substantial resistance in some quarters.

The CHAIRMAN. All right. You are getting now back to individual cases again. On the whole what would you say? Have your suggestions for stabilization of wages been voluntarily followed—on the whole?

Mr. FEINSINGER. Yes.

The CHAIRMAN. All right.

Senator BENTON. Is the nature of the resistance that businessmen go ahead with the increases illegally, without coming to the Board? Is that what you mean by resistance?

Mr. FEINSINGER. There are two areas of resistance.

Senator BENTON Anybody who comes before the Board manifestly is not resisting; he is in agreement and he is coming before the Board to try to get your permission to do what he wants to do.

Mr. FEINSINGER. There are two areas of resistance, Senator, and that is why I hesitated to give a yes or no answer to the question of the chairman, though finally his question penetrated my mind.

Senator BENTON. It hasn't quite penetrated my mind yet.

The CHAIRMAN. You mean the question or the answer?

Senator BENTON. Neither.

Mr. FEINSINGER. One area of resistance is where the employer refuses to grant a demand for a wage adjustment, all of which can be granted within the existing regulations. He says he can't afford to pay them.

Senator BENTON. But he is not resisting the Board, he is resisting the union.

Mr. FEINSINGER. He is not resisting the Board or the regulations—he is resisting the demand.

Senator BENTON. That is normal resistance. You can't call that resistance to the Board.

Mr. FEINSINGER. That is correct, so you may have strife there. You may have a strike and resistance, and we are trying to preserve the right to strike and the right to resist unless it is a case of such importance to the defense effort that the President will refer it to us.

Senator BENTON. But the Board is not in this yet, so there is no element of resistance to the Board.

Mr. FEINSINGER. The other area of resistance is where the employer wants to pay more than our regulations permit in order to keep his labor which somebody else is trying to take away from him or to get more labor.

Senator BENTON. That is what I thought would be the only resistance.

Mr. FEINSINGER. That is resistance to the wage stabilization program itself, sir.

Senator BENTON. Where he wants to pay too much?

Mr. FEINSINGER. Yes.

Senator BENTON. Was that the part of the question and the answer? Because if so, I have a better understanding of your response. It is in line with the case we had here the other day of the fine of $40,000.

Mr. FEINSINGER. The Hedin case. I think in proper answer to the chairman's question I would have to distinguish between an ordinary expression of industry opinion through associations and what particular employers tell me when they come in to my office about their problems.

Senator BENTON. I think that is a very needed distinction. Thank you, Mr. Chairman.

The CHAIRMAN. Proceed.

Mr. FEINSINGER. Let me illustrate the diversity of problems which our regulations must meet. Here is an employer who is opening a new defense plant. He wants to know what rates he can lawfully pay. He would like to pay a sufficiently high rate to attract the best qualified labor even though that rate might exceed the highest prevailing rates. Other employers in the same labor market area, however, could properly object to the Board's approving a rate so high as to result in a "pirating" of the labor employed in the established plants.

These considerations are balanced in our new-plant regulation. Or, here is an employer who wishes to replace his hourly rate sytsem with an incentive rate system so as to produce more goods at the same or lower unit labor cost. We should have and do have a policy which permits the establishment of sound incentive systems within stabilized limits. Or, here is a businessman—this is a very common case—who wishes to shift from civilian to defense production. His present rates do not permit him to obtain the necessary quality and quantity of labor. We cannot conscientiously deny him any relief. We cannot, however, permit him to pay the top rates without creating a problem for other employers in the labor market area who also may have important defense contracts. Our policy on interplant inequities is designed to meet this problem.

These are only a few examples of the problems which employers, employees, and their unions face every day in a defense economy, and which we must, therefore, consider in the development of an effective wage stabilization program.

Our policies may be broadly grouped into three classes: stabilization of the general wage level; stabilization of fringe benefits; and stabilization of adjustments to correct inequities within and between plants. I will talk about them in that order.

A. STABILIZATION OF GENERAL WAGE LEVEL

The President in his Economic Report said:

> Adjustments to take account of increases in the cost of living are a matter of simple equity, because price inflation is not a fair way to impose the burden of national defense. The fair way to impose the burden of national defense is by taxation and other restraints which can be equitably imposed.

Regulations of the Board which embody this concept are General Wage Regulation 6 and General Wage Regulation 8, revised.

The heart of General Wage Regulation 6 is the so-called 10 percent or "catch up" formula. This formula was designed to permit the restoration of the normal relationships between different wage groups which had been disturbed by post-Korean developments. It was also designed as an interim cost-of-living policy.

Regulation 8, revised, states our established cost-of-living policy. It permits adjustments in wage rates to correspond with changes in the cost of living calculated, as a general rule, since January 15, 1951. As the President has stated, the policy of relating wage changes to the cost of living is fair and equitable.

These policies are simple and clear and are expressed in regulations which can be administered by the parties themselves instead of requiring prior Board approval.

B. STABILIZATION OF FRINGE BENEFIT ADJUSTMENTS

The term "fringe benefits" refers to such practices as vacations, paid holidays, night-shift differentials, premium pay and the like. General Wage Regulation 13 permits the adjustment of such fringe benefits up to a level which does not exceed industry-area practice. The effect of this regulation is chiefly to permit "laggards" to catch up to prevailing standards. In General Wage Regulation 19, similarly, we have established standards for health and welfare plans which do not exceed the limits of sound industrial practice.

C. STABILIZATION OF ADJUSTMENTS DESIGNED TO CORRECT INEQUITIES IN WAGE RELATIONSHIPS WITHIN AND BETWEEN PLANTS

Wage differentials are normal in American industry. The Board's regulations are designed not to upset established historical differentials. Some differentials, however, involve inequities which, if uncorrected, would impede defense production. There are, for example, certain kinds of inequities which are widely recognized as tending to impair employee efficiency and morale, increase grievances and hinder the most effective uses of manpower.

This type of problem is dealt with specifically by our regulations on interplant and intraplant inequities. Related problems are dealt with in other regulations such as our regulation dealing with increases based on merit, length of service, and similar factors. These regulations establish stabilized limits within which inequities may be corrected. Their impact does not appreciably affect the general wage level. On the contrary, such adjustments may more than pay for themselves in more efficient production. These regulations, I want to emphasize, are designed primarily to help the smaller employer whose compensation practices had not matured at the time of the wage freeze. They also help employers generally who, because of changes brought about by the defense program, are confronted by these problems for the first time.

I would like to go into a question the chairman raised earlier with respect to prices, the impact of Board policies on wage rates.

January 1950 was a relatively stable period in our economy. It is therefore used as one basis for comparison. During the period from January 1950 to February 1951, the approximate date of the wage freeze, adjusted coverage hourly earnings—that is the usual standard for comparison—excluding overtime and interindustry shifts, for production and related workers increased monthly by an average of nine-tenths of 1 cent (0.7 percent) per hour. Contrasted with this figure, adjusted hourly earnings between February 1951, the freeze date, and November 1951, the last date for which we have figures available, with wage controls in effect, increased monthly by an average of one-half of 1 cent (0.4 percent), as contrasted with nine-tenths of a cent or seven-tenths of 1 percent.

Another basis of comparison is the post-Korean period and the period of controls for which data are available—through November 1951. In the former period, the monthly rate of increase was 1 2/10 cents (0.9 percent) per hour. In the latter period, the monthly rate of increase was one-half of 1 cent (0.4 percent) per hour.

I might say, parenthetically, Mr. Chairman, that the same sort of comparison with controls in World War II, maintained by the War Labor Board—though we had a "no strike" pledge, it was an all-out shooting war, and we had a tighter price control program—I say the same comparison will produce about the same result. Our record is at least as good as if not better than the record of control during any comparable period of World War II.

Now, it is much too early to pass final judgment on the effectiveness of Board policies in stabilizing wages.

The CHAIRMAN. May I interrupt to ask you this: In general what has been your experience with respect to the effect on the necessity for granting wage increases of the raising of ceilings by OPS?

Mr. FEINSINGER. Since your basic policy is to gear changes in wages to changes in the cost of living which have already occurred, obviously to a large extent the lifting of ceiling on prices results in automatic wage increases.

Now, I want to be fair to the Price people in saying that unquestionably some of the wage increases, cost-of-living wage increases, although they followed previous price increases, to some extent contribute to the next price increase. We recognize that.

The CHAIRMAN. That leads to the other question I had in mind. To what extent have increased ceilings, which resulted in increased costs, been absorbed by industry instead of being reflected immediately in a demand for increased wages?

Mr. FEINSINGER. I wish you had kept Mr. DiSalle here. I think he could answer that question. I would say this: on the wage side any increase in price ceilings as reflected in the monthly Consumers Price Index, which is our guide, automatically generates demand for wage increases the next time wage contracts are opened, and in fact where the contracts have escalator clauses automatically result in a wage increase.

The CHAIRMAN. So that it follows, I take it, that to prevent an upward trend, a continuous upward trend of wages, it is necessary to keep the price level very stable; is that right?

Mr. FEINSINGER. Yes, sir.

The CHAIRMAN. What, in your opinion, would be the effect of the lifting of price controls?

Mr. FEINSINGER. I think that for the foreseeable future the lifting of price controls, with a tightening market for labor and goods, would result in virtually automatic price increases, which, in turn, would result in automatic wage increases, and a demand on the part of workers for a new wage formula because this must be pointed out: the Board's cost-of-living policy does not guarantee the worker that he will maintain his standard of living. It merely maintains that he will preserve his real wage rate. His standard of living may be down in many ways even though his wage rate remains constant.

Payment of higher taxes and all of the other burdens of a defense economy must be met by the worker just like the rest of us.

The CHAIRMAN. It is obvious from your paper and your testimony that the Wage Stabilization Board is dealing with one of the most complex and difficult of all the defense problems. May I ask you your own judgment as to how relatively successful it has been?

Mr. FEINSINGER. I think I could give you a modest estimate—about 102 percent of what was expected. I think on the basis of my own experience, Mr. Chairman, in World War II in a situation much more calculated to lead to success, to repeat, we had a no-strike pledge, we had a rather tight price-control program, we had patriotic stimulus of an all-out war.

I think on the basis of that experience, I would have expected that in this period, with a relatively loose price-control program, no no-strike pledge, a limited shooting war, much smaller proportion of our output allocated to defense—I would not have been surprised had the rate of increase in wages been twice as high as it is now.

So while it might have sounded flippant, I meant it quite seriously when I said our performance to date, having in mind, as you accurately pointed out, the many-faceted nature of our duties, has been quite a bit better, if not substantially better, than any impartial expert would have predicted.

The CHAIRMAN. I would judge from the fact that not too many controversies have raged in this field, compared with controversies in other fields, that you are getting a relatively high degree of cooperation both from labor and from management; is that correct?

Mr. FEINSINGER. That is correct; sir.

The CHAIRMAN. And your Board is set up to represent both of these groups as well as the public?

Mr. FEINSINGER. That is correct, and I don't think anything but the tripartite system that we have could have accomplished the results that have been accomplished, because both labor and management feel comfortable and assured in having their representatives sit in with the public members in the formulation and administration of policy, and they can explain our actions to their constituents.

Even though they themselves may have voted against the policy or against the decision, once that policy is formulated and that decision made, it becomes the policy or the decision of the Board, and all three sides stand behind it. I don't think an all-public board could have done the job, sir.

The CHAIRMAN. Perhaps Members of Congress would enjoy having such an agency to explain congressional policies to the constituents.

Mr. FEINSINGER. It has only bipartite character, that is true, sir. Shall I continue? I have only a short way to go.

The CHAIRMAN. You may proceed.

Mr. FEINSINGER. I started to say it is much too early to pass final judgment on the effectiveness of Board policies in stabilizing wages. These comparisons do indicate, however, that wage controls have contributed to a reduction in the rate of wage increases. Interpretations of these comparative figures are difficult and may vary, depending on who is trying to prove what. I am not trying to prove anything. I believe it can fairly be said, however, that the control of the movement of wage rates since the establishment of our program is as good as if not better than hoped for by experienced and objective observers. A statistical analysis is, of course, only one measure to appraise the Board's success in helping to attain the over-all objectives of the Defense Production Act, which include the maintenance of sound labor relations, including collective bargaining, the preservation of industrial peace and the fostering of defense production. That is a man-sized job for any single agency.

Finally we have these policies in the process of development.

The CHAIRMAN. Before you go to that, I might remark that Eric Johnston, when he was in the Stabilization Agency, seemed to feel that there should be an absorption of wage increases, and I think that he used as his standard 85 percent of the 1947 to 1949 profits. Is that still the rule?

Mr. FEINSINGER. That is still the rule of the OPS, sir, the industry earning standard. That relates to absorption of all kinds of cost increases, labor, material, et cetera.

Coming to the relationship between absorption and one of our policies still under development—and I think you might be interested in it—in his Economic Report the President said:

> Wage adjustments to allow for increases in productivity, if carefully limited and firmly administered, can provide incentives which outweigh any possible inflationary effect.

The granting of incentives designed to encourage more efficient production is not a new principle in any segment of the American economy. The need for such incentives is greater rather than less in a defense economy. The problem of the Board is how best to express this principle in the form of a general wage policy for use in this period of defense emergency.

This principle of rewarding more efficient production has traditionally been recognized in wage setting, through collective bargaining and otherwise. Incentive systems are one example. In hourly rated plants, for another example, it has been recognized in the General Motors-UAW-CIO contract under the description of annual "improvement factor." Last June the Board approved this type of payment, under specified conditions, if provided for in agreements in effect on or before January 25, 1951. This is as far as the Board has taken action to date in the formulation of a general productivity policy.

The varying, and to some extent conflicting, considerations which must be kept in mind in the formulation of a productivity policy have been very thoughtfully analyzed in the report of Mr. Keyserling's committee, the Council of Economic Advisers (pp. 147–48). The Board is giving careful consideration to these and other guideposts in connection with this portion of the President's report.

Another important policy presented before the Board is that relating to pensions. During World War II, pension payments were not subject to control. In the Defense Production Act, however, Congress expressly directed that pension payments be stabilized. The Board is well advanced in its consideration of this subject.

The next point is self-regulation, a point Mr. DiSalle said his organization is coming to, and we have already come some distance.

In World War II, every wage adjustment required prior approval by the War Labor Board. This Wage Stabilization Board, however, has provided for a large measure of self-administration by setting standards which the parties may apply, without coming to the Board for prior approval. This reduces administrative delay and eliminates considerable expense to employers, unions, and the Government.

Our present standards relating to general wage levels, "housekeeping" wage adjustments, health and welfare benefits, and bonuses are self-administering. The Board has also before it proposals to increase the area for self-administration for small employers and for low-paying employers who wish to raise their wage rates within stabilized limits.

RELATION BETWEEN WAGE AND OTHER CONTROLS

The Board is only one member of the economic stabilization team. We recognize that coordination of our wage stabilization functions with the functions of other ESA agencies is the responsibility of the Economic Stabilization Administrator. We appreciate the sincere efforts of the Administrator to increase the effectiveness of the over-all program of direct economic controls. There is excellent cooperation and understanding between the Administrator and the Board.

The Board's responsibilities, for example, in the area of disputes, also bring it into contact with virtually every other phase of the defense effort. This statement, however, does not deal with these relationships because they are not pertinent to the subject I have been asked to discuss.

CONCLUSION

As the President stated in his Economic Report:

> The policies of the Wage Stabilization Board are designed to put a brake upon excessive wage adjustments, while at the same time recognizing that some adjustments in a free and dynamic economy are essential from the viewpoint both of equity and of incentive.

This quotation is a concise summary of the Board's program, I believe on the basis of results to date that the Board's efforts have been effective in accomplishing the objectives Congress set forth in the Defense Production Act.

Also, I have a one-page table which contains the data, a breakdown of the data which I have summarized, and also some of the data that your questions led to.

The CHAIRMAN. Very well.

(The table referred to above is as follows:)

Selected measures bearing on wage stabilization

I. AVERAGE MONTHLY INCREASE IN ADJUSTED[1] HOURLY EARNINGS

	Percent	Dollars
A. Current emergency:		
1. Post-Korea prefreeze (June 1950–February 1951)	0.885	0.012
2. Post-freeze (February–November 1951)	.363	.0054
B. World War II:		
1. Prestabilization (January 1941–October 1942)	1.025	.0068
2. Post-stabilization (October 1942–July 1943) (a 9-month period equivalent to February–November 1951)	.591	.0048
3. October 1941 to October 1942 (first year)	.91	.0066
4. October 1942 to October 1943 (second year)	.57	.0046
5. October 1943 to October 1944 (third year)	.43	.0037
6. October 1944 to July 1945 (fourth year)	.31	.0027
C. Postwar:		
1. July 1945 to July 1946	1.19	.0111
2. July 1946 to July 1947	.99	.0105
3. July 1947 to July 1948	.73	.0086
4. July 1948 to May 1949 (10 months)	.37	.0048

II. CHANGES IN CONSUMERS' PRICE INDEX

Increase in old series, January 15–November 15, 1951 (maximum allowable under regulation 8)	4.2	-------------

III. CHANGES IN ADJUSTED HOURLY EARNINGS AND CPI

	Earnings	Cost of living	
		Old	New
	Percent	*Percent*	*Percent*
January 1950 to February 1951	8.5	8.8	7.9
February 1951 to November 1951	3.3	2.8	3.9
January 1950 to November 1951	12.0	13.4	12.1

IV. MAN-DAYS LOST THROUGH DISPUTES

	Percent of estimated working time
February–December 1951	0.25
February–December 1950	.46
February–December 1949	.63

[1] Adjusted average hourly earnings following January 1950 represent gross average hourly earnings which exclude overtime and the effect of interindustry shifts in employment after January 1950. Adjusted average hourly earnings prior to January 1950 exclude overtime and the effect of interindustry shifts in employment after January 1941.

The CHAIRMAN. Congressman McKinnon.

Representative MCKINNON. I think it would be well for the record to show average hourly earnings in 1946, 1947, 1948—that period back there when wage rates, for instance, went up between 1946 and 1947 by approximately——

Mr. FEINSINGER. One percent.

Representative MCKINNON. Thirteen cents an hour.

Mr. FEINSINGER. Yes.

Representative MCKINNON. And then for the next couple of years they slowed down to perhaps 5 cents an hour, but when you relate that to the increase in the last year of adjustment and great stress, the actual net increase has only been about 50 percent as great as your figures show, because there is that normal increase which would have been the case in ordinary times.

Mr. FEINSINGER. That is a very acute observation. Even in a normal period, without the stresses of a defense economy, collective bargaining would produce a rate of increase higher than the actual rate of increase under controls, and in a period of stress obviously without controls the rate of increase would have been a good deal better.

You can see what was happening to it. It had gotten up to a point which is more than twice as high as the monthly rate during controls, and would certainly have spiraled had there not been price controls.

Senator BENTON. What would the normal be under collective bargaining, the normal annual increase?

Mr. FEINSINGER. You have here, as the Congressman has pointed out, these figures. From July 1945 to July 1946, in percent, it was 1.19. The figure to keep in mind for our period of controls now is 0.35. In 1945 to 1946 it was 1.19. Ours is roughly three-tenths of 1 percent. In 1945 to 1946 it was 1 percent, 1.19 percent; 1946 to 1947, 0.99—about 1 percent; 1947 to 1948, 0.73; 1948 to 1949, 0.37.

Representative MCKINNON. Is this monthly?

Mr. FEINSINGER. Yes, the monthly rate in percent, monthly rate of increase in adjusted average hourly earnings.

Senator BENTON. If it is 0.35, that would make it about what, 5 percent for the year, 4¼ percent for the year, in contrast to Mr. DiSalle's figure of a 3 percent rise in prices?

Mr. FEINSINGER. Our 0.363 percent is the monthly rate of increase. It would not change by adding another couple of months. This was from February to November. It would remain substantially the same. The percentage increase in cost of living is 4.2 percent, but we use different bases. We use 4.2 percent because that is the total increase in the cost of living.

Senator BENTON. For the past year?

Mr. FEINSINGER. From January 15 to November 15, 1951. We used for our experience in arriving at this percentage figure to the monthly rate of increase from February to November, because controls didn't go into effect until February.

Senator BENTON. He testified that prices had gone up 3 percent in a year. You say the cost of living went up 4.2 percent in about 9 months.

Mr. FEINSINGER. That is right. From January 15 to November 15, 1951. I think those are the two indexes we talked about. The indexes from January 15——

Senator BENTON. What is the difference between the price index and the cost-of-living index?

Mr. FEINSINGER. The cost-of-living index is a misnomer. The consumers' price index is the index which is used officially to determine cost-of-living increase.

Senator BENTON. That is what I thought, but didn't Mr. DiSalle say the increase over the last year was only 3 percent?

Mr. FEINSINGER. That is from February to November. It would be roughly 3 percent. We used a different period. Our figures are the same.

Senator BENTON. What I was aiming at, in line with Mr. McKinnon's very interesting question—you showed the way wages have been kept down with this Stabilization Board effort. Have they kept up with the increase in prices?

Mr. FEINSINGER. Roughly the same.

Senator BENTON. They are roughly parallel?

Mr. FEINSINGER. They are roughly parallel.

Senator BENTON. Don't you think that is the test, Mr. Chairman, that they do roughly parallel?

Is there much criticism about the present formula and system being used by the Board?

Mr. FEINSINGER. Yes, the labor groups feel that our policies are too tight in that at best they merely enable them, talking about general wage increases now, to maintain the same real wage rate instead of permitting labor to share in the general improvement in our economy from year to year.

They also feel it is not fair to fail to recognize the increased burden of taxation, for example, in our formula. That is one of the major complaints of some segments of organized labor.

Senator BENTON. Has your Board taken a position on the escalator clause method of adjusting wages?

Mr. FEINSINGER. Yes, our policy permits labor and management the option of the standard escalator clause approach, reopening every 3 months, up or down, or in the alternative, to open it no more than once in 6 months without any requirement of downward revision; but we have not taken any position on the question of whether to recognize increases in taxation as part of the increase in the cost of living.

Senator BENTON. You haven't taken a position affirmatively recommending the escalator clause? It is just that you have approved it?

Mr. FEINSINGER. That is right.

Senator BENTON. That is an important distinction. Are you prepared to make any observations on the subject?

Mr. FEINSINGER. Not at this time, not in advance of tripartite consideration.

Senator BENTON. Senator Sparkman left me a question. Shall I put his question now, Mr. Chairman?

The CHAIRMAN. Yes; proceed.

Senator BENTON. Senator Sparkman wants to know if the steel case he reads about in the papers will come before your Board.

Mr. FEINSINGER. Yes; it will. The President certified the steel case to the Board, asking us to make recommendations for a fair and equitable settlement, and that is just what we are going to do. We have established a tripartite panel to receive the evidence and the arguments, summarize them, pass them on to us.

Senator BENTON. This is what you are doing after the Atlantic City decision of the workers not to go on strike but to hold off while you make this review?

Mr. FEINSINGER. We would not have handled the case had the union not cooperated by agreeing to postpone its strike. That is our firm policy.

Senator BENTON. This is what you mean by the fact that you are getting cooperation from the unions as well as from management?

Mr. FEINSINGER. I think we couldn't ask for any better cooperation on both sides, speaking Nation-wide now, and speaking on the basis of experience to date. What the future holds, I don't know.

Senator BENTON. In the midst of the scandals and other things that plague us, Mr. Chairman, I submit that is a great record of achievement.

The CHAIRMAN. And it is to be devoutly hoped that it continues to be the experience of the Board.

Senator BENTON. It certainly is. Why don't you have this railroad case that I hear so much about? According to the railroad workers, the case has bogged down for 2½ years and they have been frozen while other workers, even in railroad unions, have been getting adjustments and raises, and this particular case is sunk according to allegation. The allegations certainly sound reasonable when you are talking to the men themselves. Why doesn't that thing come out and get before your Board for the kind of settlement you have been making in other cases?

Mr. FEINSINGER. Well, sir, if given the task, we wouldn't shirk it; but there are reasons why we don't have it.

On the stabilization front, the Economic Stabilization Administrator has established a special railroad and airplane panel to hand stabilization questions in that industry.

On the disputes front Congress has established a procedure, an emergency Board procedure, for the handling of those disputes, and that prevails.

And so unless the system were changed somehow or other, that dispute would not find its way to our Board in the first instance, and after a settlement has been made, the settlement would not find its way to our Board for approval.

Senator BENTON. Are there other major areas that are excluded by law?

Mr. FEINSINGER. Salaries, salary stabilization is handled by a separate salary board. The line of distinction in jurisdiction is simply this: Executive, professional, administrative people who are exempt from the Fair Labor Standards Act go to the salary board unless organized. Those people if organized and all other workers come to our Board. Now those are the two areas I think.

Senator BENTON. Are you prepared to say whether you would favor an escalator clause applied to Government workers? I am thinking now of the great attention Congress was recently called upon to give the post-office clerks, and the final decision by the committee of picking an arbitrary percentage which had to go through by act of Congress. I wondered at that time whether in the long-range interest of the post-office clerks and other Government employees some escalator provision wouldn't be an equitable and improved method of handling wage adjustments over and above the present methods.

Mr. FEINSINGER. Senator, I am not an expert on the subject, but I could make this observation.

Without suggesting that that be the limit of adjustments, because there are all sorts of special inequities, as a basic factor in any wage policy maintained by the Government, I would recommend very strongly the use of the so-called escalator clause because it is simple, it is understandable, it is uniform, and everybody knows in advance just what is going to happen. I want to emphasize I am not suggesting that as of the sole or exclusive measure; but certainly a measure of determining general wage movements. The employees understand it, Government understands it, it is easily administered.

Senator BENTON. I told the post-office clerks it seems to me they ought to look into it. I haven't studied it enough to pass judgment on whether their base rate is high enough right now, but it seems to me they would be in a better position over the next decade. Teachers or any other fixed Government salary group might be better off if they could tie up to an escalator clause as was first done on a big scale by General Motors.

Mr. FEINSINGER. Yes; although, of course, it had been used.

Senator BENTON. You have what is perhaps our most famous and distinguished private industry setting the pattern here.

Mr. FEINSINGER. Of course, the General Motors contract had some other features to it. It also included the well-known annual improvement factor, and in the consideration General Motors got a 5-year contract plus an agreement to cooperate in the introduction of new machinery, et cetera.

Senator BENTON. I would like even to see the United States Senate salary scale put on an escalator clause. Coming from a family of teachers, I speak with some feeling on this subject.

Mr. FEINSINGER. As a teacher, I would join you in that feeling.

Representative MCKINNON. It has been your experience, I imagine, that in the case of organized labor and most kinds of labor they wouldn't want indefinitely to tie themselves merely to an increase in living costs, because they want to earn a greater portion, a greater percentage, out of the total production.

Mr. FEINSINGER. That is right.

Senator BENTON. That is a good point. If productivity is going ahead 2½ percent a year, an escalator clause would only be a guide because, as Mr. McKinnon points out, they also have a claim for part of that 2½-percent annual increase in total productivity.

Mr. FEINSINGER. All the escalator clause does is to protect a rate which has already been negotiated. It does not provide for any improvement or advancement, so labor would never be satisfied with that as a long-range policy. It permits them merely to stand still.

Senator BENTON. How would you adjust the teachers' share of the increase in annual productivity as an addition to an escalator factor on adjusting teachers' salaries?

Mr. FEINSINGER. Of course, I think, as I am sure you recognize, that the teachers are a good deal more productive than they are being credited with being and a good deal more overworked and underpaid than most people generally realize.

Representative MCKINNON. Do you not think, Mr. Feinsinger, that on this productivity schedule in industry, at least, it would be far more applicable and far more reasonable if it were tied directly to the line of endeavor the man is working in instead of being based on the national average? Wouldn't that be more incentive to the man and more reflected in cost of operation?

Mr. FEINSINGER. It would be, and that is one of the difficult problems the Board is struggling with in trying to evolve a productivity policy. There is this difficulty. Supposing in a given industry it can be demonstrated by scientific proof, which isn't often possible, that productivity has increased 10 percent a year and will continue to increase 10 percent a year.

Well, taking your approach, Mr. Congressman, you would then permit a 10-percent wage increase on the ground that there is no increase in unit labor cost. Certainly you would allow a 5- or 6-percent increase for that reason.

Well, what about the competitor, let's say, in the same industry, or let's say in a related industry, which is competing for labor in the same labor-market area?

Representative McKINNON. Isn't this a free competition system, so called?

Mr. FEINSINGER. Under wage and price controls, don't you have to——

Representative McKINNON. I am talking not about the emergency, but I am talking about the long run.

Mr. FEINSINGER. Under the long run, I know General Motors figured 2 percent, not because it didn't think it was going to get more than that; Mr. Wilson has since said it was a good buy, that he has gotten a good deal more than that for his money.

The CHAIRMAN. What about the general effect of this whole procedure upon the position of the small operator who is also the owner and manager of his enterprise, who has none of the aspects of managed collectivist industry like General Motors? What is the effect upon the wage situation there and the price situation?

Mr. FEINSINGER. It depends, sir, on whether again you are talking about this period of controls or the period of completely free competition. In the period of so-called completely free competition, your little fellow doesn't have as much chance as he has in a period of controls. With so-called national patterns established, he has his choice of paying or being shut down or getting the less efficient workers.

Now, we feel that we have some responsibility in the period of controls in looking out for the little fellow and middle-sized fellow.

As long as we are running the show, even within the narrow limits within which we are running it, if we had only the big producer and the big profit maker to consider, we could afford to have a good deal more liberal wage policy than we are actually contemplating right now.

On the other hand, you cannot permit the little fellow or the middle-sized fellow to establish the ceilings for the total economy. And so it is a matter of weighing and balancing and coming up with something that is fair to all segments of our economy.

The CHAIRMAN. When Mr. Charles E. Wilson was testifying here Saturday, the question arose with respect to small business, and he said that in the defense picture that sometimes meant a business able to swing a capital of 1 or 2 million dollars. That is not small business in the minds of the general public, as we all know.

With that preliminary, I ask, to what extent have you dealt with problems affecting really local business in which the capital involved is measured by thousands rather than by tens of thousands?

Mr. FEINSINGER. We have given very serious consideration to allowing that man to fix his own wages, which is one way of saying decontrol. Of course, you have got two kinds of small-business men—the small-business man who complains that the present wage ceilings are too high and he can't pay them, even though he is not required to pay them; and the small-business man who says, "I want to be rid of all this red tape and stuff; you can trust me; I am not going to shoot my wages sky high; I am not a fool; I have to compete and make money."

We are considering for that kind of businessman who wants to be relieved of all the controls, if possible, we are considering letting him take the responsibility. But when we started adding up the exceptions that would be necessary in order to prevent pirating of labor away from war plants, et cetera, the exceptions almost ate up the exclusion.

I don't know if I make myself clear. In World War II we exempted the employer of eight or fewer workers from all wage controls. By the time we got through excluding from the exemptions such things as tool and die shops, et cetera, we had over 64 exceptions to the exemption.

What we are doing now is trying to get out a single regulation that will go the limit of what we call self-administration, because that is what it amounts to. It is not really decontrol, because the little fellow will control it himself. He is not going to give away his business just because the law says, "You are now free." I don't know whether there will be enough left after we get through taking out all the exclusions from the exemption to make it worth while having any exemption.

The CHAIRMAN. Are there any other questions?

Representative MCKINNON. There is one thing I don't believe is very well understood by the general public; that is your statement that says that your cost-of-living policy permits adjustments in wage rates to correspond with the changes in cost of living.

Now, these escalator clauses we hear so much about in the automobile industry are no different from that which you have in your regular policy. The difference is in the contract between management and labor or the relationship between employer and employee, is it not? The employer is still free to make these adjustments automatically in accordance with the schedule you set forth?

Mr. FEINSINGER. That is correct.

Representative MCKINNON. And he doesn't have to come to your Board to do it?

Mr. FEINSINGER. That is right. He just has to keep records, doesn't even have to make reports.

Representative MCKINNON. All industries can make cost-of-living adjustments that the automobile industry is making if they want to; is that right?

Mr. FEINSINGER. On the cost-of-living aspect; yes. On productivity we haven't yet developed a policy. There is an annual improvement factor in the General Motors contract embracing what is called the productivity factor. Sometimes it is called one thing and sometimes another.

Senator BENTON. Is that the 2 percent?

Mr. FEINSINGER. That is the 2 percent. A great many employers want the same portion.

Senator BENTON. If you look at General Motors, as many do, as the most brilliant and glistening jewel in the crown of private enterprise, it would seem to me it would be very helpful if your Board came out with recommendations in this field of the escalator clause. Is that contemplated?

Mr. FEINSINGER. Well, I would rather not express an opinion again in advance of tripartite consideration.

Senator BENTON. I have no further questions, Mr. Chairman.

The CHAIRMAN. That, Mr. Feinsinger, concludes the questioning.

On my own behalf and on behalf of the committee I want to compliment you most highly on your presentation.

Senator BENTON. I join in that.

The CHAIRMAN. I think this prepared paper is one of the best that we have received. Let me say it is a credit to the law profession which you represent. As one lawyer to another, I want to say it was really a most excellent paper. We are grateful indeed for your presentation.

The next meeting of this committee will be held Wednesday morning at 10 o'clock in room G–16 in the Senate wing. That is the Interstate Commerce Committee hearing room.

We shall then have a panel discussion on the nature and the magnitude of the problems of mobilization and economic stabilization. The participants will be Thomas Blaisdell, of the University of California; Roy F. Foulke, of Dun & Bradstreet; Martin Gainsbrugh, of the National Industrial Conference Board; Edwin G. Nourse, who is a consultant economist in Washington, D. C.; Boris Shishkin, of the American Federation of Labor; Caroline F. Ware, professor, Howard University, school of social work, Washington, D. C.; and Donald Woodward, of the Mutual Life Insurance Co. of New York.

(Whereupon, at 12:40 p. m., the joint committee recessed, to reconvene at 10 a. m., Wednesday, January 30, 1952, in room G–16, the Capitol.)

JANUARY 1952 ECONOMIC REPORT OF THE PRESIDENT

WEDNESDAY, JANUARY 30, 1952

Congress of the United States,
Joint Committee on the Economic Report,
Washington, D. C.

The joint committee met, pursuant to adjournment, at 10:20 a. m., in room G–16, Senate wing of the Capitol Building, Senator Joseph C. O'Mahoney (chairman) presiding.

Present: Senators O'Mahoney, Benton, Taft, and Flanders; Representative Patman.

Also present: Grover W. Ensley, staff director; and John W. Lehman, clerk.

The Chairman. The committee will please come to order.

The session this morning has been assembled according to the practice of the Joint Economic Committee to make an objective search for facts and opinions.

The economic report of the President has been submitted to Congress. We have had several hearings, some of them public, with respect to the recommendations and the text, both of the President's report and of the economic review of the counsel.

The committee has arranged for open discussions of the report from ladies and gentlemen who have gained destinction in the economic world and whose opinions and analyses of the report will be of great public value.

This morning we have with us Dr. Edwin G. Nourse, consultant economist in Washington, formerly chairman of the Council of Economic Advisers; Dr. Thomas C. Blaisdell, Jr., of the University of California; Dr. Donald Woodward, Mutual Life Insurance Co., New York; Mr. Roy F. Foulke, of Dun and Bradstreet; Martin Gainsbrugh, of the National Industrial Conference Board, New York; Mr. Boris Shishkin, who has not yet arrived but who is on his way, economist of the American Federation of Labor; and Dr. Caroline F. Ware, professor, Howard University, School of Social Work, Washington, D. C.

I shall insert in the record at this point a brief biographical sketch of each of the participants.

(The biographical sketch of the participants is as follows:)

Participants in the Panel Discussion on the Nature and Magnitude of the Problem of Mobilization and Economic Stabilization, January 30, 1952

Blaisdell, Thomas C., Jr., economist, University of California; b. Pittsburgh, Pa.; student Alma (Mich.) College 1912–13 and 1914–15; Konigstadtische Oberrealschule, Berlin, 1913–14; B. A., Pa. State College, 1916; grad. New York

School of Social Work, 1922; M. A., Columbia University, 1922, Ph. D., 1932. History teacher, Ewing Christian College, Allahabad University, U. P., India, 1916–19; teacher, economics, Yenching U., Peking, Columbia University, 1925–33; asst. director National Resources Planning Board, 1939–43; War Production Board, 1942–44; director, Bureau of Plans and Statistics, Office of War Mobilization and Reconversion, 1944–46; chief, mission for economic affairs, with rank of minister, London, England, 1945–47; Assistant Secretary of Commerce, 1949–50; director, Office of International Trade, 1947–48. Author: Federal Trade Commission, An Experiment in Control of Business, 1932; Peking Rugs and Peking Boys (with C. C. Chu), 1924. Contr. to govt. bulletins, etc.

FOULKE, ROY A., business executive; b. New York, N. Y.; B. S. Bowdoin College, 1919, M. A. (honorary), 1939. With credit department, Liberty National Bank, New York City, 1919–22; manager, bank service department, National Credit Office, Inc., New York City, 1922–28; analyst, Paine Webber & Co., New York City, 1928–31; manager of specialized report department, Dun & Bradstreet, Inc., New York City, 1931–44; vice president, since 1944. Member editorial advisory board, the American Journal of Economics and Sociology. Author: Commercial Paper Market, 1931; Behind the Scenes of Business, 1933; Practical Bank Credit, 1939 (coauthor); the Sinews of American Commerce, 1941; Practical Financial Statement Analysis, 1945. Home: Bronxville, N. Y. Office, New York City.

MARTIN R. GAINSBRUGH, University of Rochester, 1924–1928; Columbia University, 1929–1932. Business experience: Economic Analyst, Trade-Ways (industrial consultants), 1933–1938. Chief Economist, National Industrial Conference Board, 1939 to date. Additional activities: Adjunct Professor of Economics, School of Commerce, Accounts and Finance, and Graduate School of Business Administration, New York University. Technical Advisor, Bureau of the Census and Bureau of Labor Statistics. Member, Business Advisory Committee, Council of Economic Advisers; Hoover Committee on Government Statistics; Special Committee on Post Office Reorganization of the Citizens Committee for the Hoover Report; Economic Advisory Council, National Association of Manufacturers; Committee on Business Statistics, American Statistical Association; American Economic Association; American Finance Association; Phi Beta Kappa; The Econometric Society; Secretary-Treasurer, Conference of Business Economists; Research Advisory Council, Credit Research Foundation. Recent publications: Productivity and Living Standard, 1949; Wages, Prices, Profits, 1949; Economic Expansion—Patterns, Problems, Potentials, 1950; Defense Economics: The First Year, 1951. (Co-author:) Studies in Income and Wealth, Volume 12, National Bureau of Economic Research, 1950; Pensions for Employees, Chamber of Commerce of the State of New York, 1950; Economic Effects of Section 102, Tax Institute, Inc., Princeton, N. J., 1951; Studies in Income and Wealth, Volume 14, National Bureau of Economic Research, 1951. Articles: What Price Economic Expansion, The Analysts Journal, Third Quarter, 1950; Techniques of the Economic Expansionists, Purchasing, August, 1950; A Survey View of Business in 1951, The Commercial and Financial Chronicle, Thursday, January 4, 1951; Defense Spending's Impact Analyzed, The Controller, January, 1951; The World's Biggest Business, The Commercial and Financial Chronicle, Thursday, April 19, 1951; Business Holds Two Hands, National Furniture Review, June, 1951, p. 66; The Consumer Durable Goods Picture for The Coming Six Months, Finish, July 1951, p. 39; Inventories Still High, New York Journal-American, August 14, 1951; What's Ahead for Business in 1952?, The Management Review, December, 1951. Congressional hearings: Joint Committee on the Economic Report, Testimony, February 16–17, 1949; January 17–20, 1950; January 29, 1951; January 30, 1952. Local newspapers: Mamaroneck Daily Times; New Rochelle Standard Star.

NOURSE, EDWIN G., economist; b. Lockport, N. Y., graduate Lewis Institute, Chicago, 1904; A. B., Cornell University, 1906; Ph. D., University of Chicago, 1915. Instructor in finance, Wharton School of Finance and Commerce (University of Pennsylvania), 1909–10; professor and head department economics and sociology, University of South Dakota, 1910–12; same, University of Arkansas, 1915–18; professor agricultural economics, Iowa State College, and chief of agricultural economics section, Iowa Experimental Station, 1918–23; chief of agricultural division, 1923–29, director, 1929–42; instructor of economics of the Brookings Institution, Washington; vice president Brookings Institution, 1942–46; Chairman Council of Economic Advisers, Executive office of the President, 1946–49. Author: Agricultural Economics, 1916; Chicago Produce Market, 1918; American Agriculture and the European Market, 1924; the Legal Status of Agricultural Cooperation, 1927; the Cooperative Marketing of Livestock (with J. G. Knapp), 1931; America's Capacity To Produce (with associates), 1934; Marketing Agreements Under the Agricultural Adjustment Act, 1935; 3 years of the Agricultural Adjustment Administration (with J. S. Davis and J. D. Black), 1937; Industrial Price Policies and Economic Progress (with H. B. Drury), 1938; Price Making in a Democracy, 1944. Home: Chevy Chase, Md. Office: Washington, D. C.

SHISHKIN, BORIS, economist; A. B., with honors, Columbia, 1930, M. A., 1931. Fellow Brookings Institution, 1932–33; research asso. Columbia, 1932; economist Am. Fed. Labor, since 1933; sec. housing com. since 1939; labor adv. NRA, 1933–35; mem. President's Adv. Com. on Unemployment Census, 1937; consultant U. S. Housing Authority and Fed. Pub. Housing Authority 1937–48; consultant Defense Housing Coordinator, 1941–42; labor adv. Office Production Management, 1941–42; consultant WPB 1942–46; cochairman labor policy com. OPA, 1942–46; mem. President's com. on Fair Employment Practice, 1942–46; Director, European Labor Division, Econ. Coop. Admin., 1948–50; vice chairman, National Commission on Children and Youth, 1944–48; mem, President's Com. on Civil Rights, 1946; Chairman of the Board, National Bureau Economic Research; mem. board directors Nat. Housing Conf., Food for Freedom, Inc. Contr. to Am. Federationist, also to various magazines; author of labor problem pamphlets; radio commentator.

WARE, CAROLINE F. (Mrs. Gardiner C. Means), college professor; b. Brookline, Mass., diploma Winsor Sch., Boston, 1916; A. B., Vassar, 1920; post grad. work, Oxford University, England, 1922–23; A. M. Radcliffe, 1924, Ph. D., 1925. Teacher Baldwin School Bryn Mawr, Pa., 1920–22. Affiliated School for Workers, 1922, 30, 37, 42, 44; asso. prof. history, Vassar, 1925–30 and 1932–34; dir. of a sociol. study, Columbia University. Council for Research on Social Science, 1932–33; sp. asst. U. S. Consumers Advisory Bd. of NRA and Consumers Div. of Nat. Emergency Council, 1934–35; sr. social science analyst, Nat. Resources Com., 1938; teacher of social science, Sarah Lawrence College, 1935–37; asso. prof. of social economy and history, American University Graduate School, 1936–40; lecturer American University School of Social Sciences and Public Affairs since 1940; asst. to Consumer Commissioner, National Defense Advisory Commission, 1940–41; head program planning unit, Consumer Div., Office of Price Administration, 1941–42; prof. history, Howard University, Washington, D. C., 1942–45; prof. Howard University School Social Work since 1945; mem. faculty Vassar Summer Inst. 1942, 43, 44; visiting prof. Univ. of Puerto Rico, summer 1945, 46, 47, 48. Chairman Consumer Clearing House since 1943; chairman exec. com. OPA Consumer Adv. Com. 1943–46; chairman Consumer Adv. Com. to Council of Economic Advisers 1947–52. Author: The Early New England Cotton Manufacture, 1931; Greenwich Village, 1920–30, 1935; (with Gardiner C. Means) The Modern Economy in Action, 1936; The Consumer Goes to War, 1942; the Consumer in the Postwar Economy, 1945; Labor Education in Universities, 1946; Estudio de la Comunidad (1947). Asso. author of The Structure of the American Economy (Nat. Resources Com.), 1939. Editor, The Cultural Approach to History, 1940. Also articles in Ency. of Social Sciences and various journals.

WOODWARD, DONALD, A. B., University of Indiana. Reporter on Wall St. Journal, financial editor of Business Week; economist, Moody's Investors Service; research assistant to the president of the Mutual Life Insurance Co. of New York. 1940–46; second vice president of the Mutual Life Insurance Co. of New York since 1946; also special consultant for the Board of Governors Federal Reserve System, Natl. Recovery Administration, United States Treasury, United States Department of State. Coauthor (with Marc A. Rose) Primer of Money, Inflation; (with Murray Shields) Prosperity—We Can Have It If We Want It. Office: Mutual Life Insurance Co. of New York, N. Y.

The CHAIRMAN. Our plan usually is to open with 5-minute statements from each member of the panel, to be followed by discussion among the panelists and with members of the committee.

Dr. Nourse, you have been elected to open.

STATEMENT OF EDWIN G. NOURSE, CONSULTANT ECONOMIST, WASHINGTON, D. C.

Mr. NOURSE. Mr. Chairman and gentlemen of the committee, I shall devote my opening statement primarily to the issue raised in the first question suggested for discussion by this panel, namely: What are the general economic implications, short-run and long-run, of a "gradual" versus a "quick" military build-up? I believe this to be the major policy question posed by the budget now before the Congress, by the Economic Report of the President which the joint committee is now considering, and by recent statements of the Director of Defense Mobilization. And my reply is that a program of maximum speed involves unwarranted inflationary strains in the short run and entails serious deflationary dangers in the long run. A more gradual program would build the necessary military component into our total economic structure on a more stable basis.

The actual experiences of 1952 should prove enlightening to your committee and to the Congress in arriving at a sound policy for 1952 and 1953. Last year we were trying for a quick build-up so as to get maximum preparedness in 1953. We accepted as a calculated risk such inflation as might develop from that rate of mobilization. Events proved that even industrial America could not get the rearmament program rolling that fast, primarily because of the very long "lead time" required for many types of modern armament and because of metal shortages and a few skilled-labor bottlenecks. The involuntary slowing of the program left enough labor and nondefense materails available so that the civilian economy had a larger supply of goods to buy with their disposable income than had been expected. This favorable supply-and-demand situation, together with a budget surplus in fiscal 1951 and the credit restraints imposed by the Federal Reserve System, backed up by the voluntary program of the local banks damped off the process of inflation. This was a desirable development from the economic standpoint, but, as Director Wilson has pointed out, it has pushed the "hump" of the preparedness effort along by at least a year's time and perhaps 2 years.

The question which confronts this Congress is whether to attempt to accelerate rearmament deliveries or to take the program approximately in the stride of 1951. In my judgment the latter course is the sound one. It would involve a substantial cut in the budget of 85.4 billion dollars for fiscal 1953, which has been presented to this Congress.

A "quick" rearmament program, with budget deficits of 8 to 14 billion dollars a year, would put excess purchasing power in the hands of the public at the same time that it sharply reduced the supply of goods in the civilian market. Experience indicates that we would not be very successful in controlling prices under these conditions through such direct measures as would be accepted by the country when not actually at war. We have to count the psychological factor there. Hence the inflationary consequences would be considerable. This would not only increase the total cost of rearmament but put the price and wage structure in a most vulnerable situation when military expenditures were cut back sharply on the completion of the build-up program. In other words, a quick military build-up program contains great danger of an inflationary boom in later 1952 and in 1953, and followed by a deflationary crash by 1954 or 1955.

I believe that the sound goal of public policy is to keep the general pattern of 1952 and fiscal 1953 as close as possible to the general character of 1951, in which "rolling deflation" approximately offset such inflation as was engendered by the defense program—on a scale much less than contemplated for next year.

This involved a moderate check to the housing industry, some unemployment of automobile workers though without undermining the industry, a rather unprosperous year for cotton textiles, and a sharp downward readjustment of the television industry, with release of workers and materials to war uses. These developments have been viewed by some companies or branches of industry, by certain unions, and by various communities as ad hoc depression, "profitless prosperity," or a breach of the principle of "equality and sacrifice." And they are now looking to an acceleration of the military build-up as a means of correcting it. From the standpoint of the economy and sound national economic policy, these pressures should be resisted. So far as military exigencies permit, the build-up should be handled in such a way as to facilitate or even require civilian industries to readjust currently to the long-time basis of consumer demand which will be possible simultaneously with the drains of a military establishment of the size which we expect to maintain more or less indefinitely.

Such a policy is rather neatly illustrated by the present automobile situation, characterized as it is by substantial unemployment in the Detroit area. In the catching-up period after World War II, we pushed the production of automobiles up to a peak of 6.6 million cars in 1950. During the early months of 1951, production was maintained at this high rate but declined by the close of the year to less than half the rate of the peak month of 1950. For the whole year 1951 we produced 5.3 million cars, and the most competent statisticians in this field estimate that that is more than can be absorbed yearly by a normal peacetime market. Some scale the number down to four and a half million or even less. Because considerable unemployment has developed in Detroit, there is now a demand that military spending be brought up to the level which would (or channelled to the Detroit district in such a way as would) absorb all this labor, or pay it, if it was not absorbed. This is asking the defense effort to perpetuate and aggravate an industrial and labor situation which grew out of the peculiar conditions of the postwar inflation boom rather than administering and scaling the defense effort on a basis which would permit the economy to move as skillfully and as smoothly as possible toward stabilized prosperity as the defense build-up gives way to the period of continued preparedness.

This way of stating the case implies an answer to question (4) suggested for this panel: Can the economy support and maintain over the long run an armed force of the size contemplated? It seems to me the obvious answer is: Of course this economy of ours can maintain an armed force of 4 or even 5 million year after year. But we must take a realistic view of what will then be left for civilian consumers and they must adapt themselves to that reality by working enough harder to produce additional goods to compensate for military drains or else reconcile themselves to the enjoyment of fewer goods. This implies a disbelief on my rather easy assumption that we are getting increased productivity and national product currently, to enable us to absorb increases in the military expenditures, such as are contemplated. Another member of the panel will speak to that point, I think, in the same vein that I have suggested.

That seems to me the crux of the uncertainties and the struggles by which we are confronted today. Too many people are still trying to beat the economic game and dodge the real costs of an unwanted war or the preparedness by which to prevent its spread.

The CHAIRMAN. The Chair is prompted to remark that this discussion must be based upon a weighing of two political assumptions: One, that the Soviets intend an early attack upon the free world, or two, that the Soviets do not intend an early attack upon the free world.

I would assume that the economic implications would be altogether different in the two cases?

Mr. NOURSE. Obviously, and I think it is clear from my remarks that I am proceeding from the second of those assumptions, namely, that from the evidence we have had during the past 2 years we can take the calculated risk that they do not contemplate an early attack.

Senator FLANDERS. Would there not be a third assumption, Mr. Chairman, to the effect that if we make a rapid build-up, then the Soviets will not attack? That is a sort of combination of the two positions you have taken.

The CHAIRMAN. You know I think that, of course, is the basic assumption.

Senator FLANDERS. That is the assumption.

The CHAIRMAN. I think you are quite right.

Senator FLANDERS. Not that the Soviets will attack, but they can be prevented from attacking by the build-up.

Mr. NOURSE. The assumption underlying by remarks was that the rate which we have already been working on, if maintained rather than accelerated, would produce that result in terms of their policy?

The CHAIRMAN. So far as I know, nobody in Government, in the executive or in the legislative branch, has taken the position that the United States should not prepare militarily. Even those who say we should withdraw from Europe nevertheless maintain that we should prepare for defense. Am I not right in that?

Mr. NOURSE. Yes; I thing if we start from the assumption of an early attack, then we should do more rather than maintain the present rate or abate it any.

I think that is the implication of the President's economic report and the budget which he submitted.

The CHAIRMAN. This makes it clear that in your discussion you are assuming that the Russians do not plan to attack the Western World in the reasonably near future, and that it is more important, therefore, to keep a sound economy, to avoid inflation, than it is to build up a reserve supply of military weapons and the like?

Mr. NOURSE. Yes, sir.

Senator FLANDERS. May I again just restate that a little? Is it not Dr. Nourse's assumption that if we proceed with a steady but less drastic military preparation then the Soviet Government will not attack?

Mr. NOURSE. Yes.

Senator FLANDERS. That is, you do not just simply say they will not attack, you say that at our present rate of preparation they will not attack.

Mr. NOURSE. What we have already done in the maintenance of the gradual rate would be sufficient.

Senator BENTON. I should like to inquire whether you have thought out your own feeling about the caluculated risk; one needs to figure more exactly what the risk is; if the chance of attack is 1 in 100, that might lead you to one set of conclusions; if it is one chance in two, it might lead you to another set of conclusions.

So the phrase covers a wide range.

I wondered if you have ever tried to pin it down more definitely?

Mr. NOURSE. Yes. I am ready in my own mind to accept and advocate a policy which is based on the definite and explicit assumption that they will not attack; not that it is a 50–50 proposition. I would not say it is absolutely certain that they will not, but there is abundant evidence that we are already in a state of growing preparedness that makes it inexpedient for them to attack.

Senator BENTON. Your thinking is that the chance is not 1 in 100 that they will attack?

Mr. NOURSE. I do not think I could put it in a fixed percentage.

Senator BENTON. If it becomes 1 in 10, it becomes a very different kind of proposition, because if you have 1 chance in 10 that you are going to die tomorrow you may do a lot of things that you are not going to do if it is 1 chance in 100 that you will die tomorrow.

Mr. NOURSE. I would be inclined to accept that sort of an idea of the 1-in-10 ratio and then weigh against it the dangers and the difficulties which we incur in reference to our own economy, if we take the more rapid rate of build-up, when there is only 1-to-10 chance that we will actually need it at an early date.

Senator FLANDERS. I would assume that was a major point in your approach to the question of the dangers of the rapid build-up, that you weigh the dangers of the rapid build-up against the chances of immediate attack.

Mr. NOURSE. Yes. And the dangers, if you will notice in the line of my argument, not merely in terms of our ability to live through a couple of years of further inflation now, but the dangers that accelerated (or deficit) build-up would entail on the economy of a crash at a time when, instead, we want to get a smoother transition from the preparation period to the maintenance period.

Senator BENTON. On the other hand, the more evidence of threatened attack that may be in the hands of people who are making the political decisions of the risk of attack the more you would, I assume, move ahead rapidly. Thus to a certain extent any group of this kind is greatly handicapped in reaching a judgment because all of the incoming intelligence and evidence on the degree of risk is not available to it.

Mr. NOURSE. That is right.

Senator FLANDERS. May I ask one more question?

The CHAIRMAN. Certainly.

Senator FLANDERS. Dr. Nourse, do you consider the administration program as being on the side of being too rapid a preparation for the dangers that you have just said we should try to avoid; do you think they have gone into the present program too fast?

Mr. NOURSE. Yes, I frankly think that the basing of national policy by the President or by the Congress on the acceptance of an $8 billion deficit this year and $14 billion deficit next year is one which entails definitely undesirable consequences on the economy.

I would make my first attack there an attempt to avoid such deficits by the introduction of strict economies in the administration, both of the military program and of all other parts of Federal spending. And I think that several billions of dollars can be squeezed out; the inflationary gap can be narrowed. If it were narrowed by half through administrative economies, further relief could be secured by holding in abeyance some of the military expansion. Then looking at the cash budget rather than the conventional budget, we would not have a seriously inflationary situation or, perhaps, not at all from that side. Of course there are other sources of inflation.

Senator FLANDERS. Would you feel satisfied if we kept the administrative budget balance somewhere near balance, so that we would run a cash deficit in immediate years, but that would tend to wipe out as the authorizations were caught up with? Would you feel that such an overspending in the cash budget on that basis would be unfortunate?

Mr. NOURSE. Well, inflationwise, of course, it is the cash budget which is of most importance.

Senator FLANDERS. Yes; that is the most important.

Mr. NOURSE. I should feel reasonably content if we brought the cash budget to a balance. My personal policy would be to keep the conventional or administrative budget in balance at this time. But that seems beyond the range of practical possibility.

The CHAIRMAN. I am glad you brought that up. I was going to quote from Dr. Nourse's statement, to raise the same issue. And I think it may be well, so that the other members of the panel who may not be familiar with our hearing last Saturday, that I read not only the statement that you have just made, but some questions and answers that were propounded and given during the hearing last Saturday when Mr. Charles E. Wilson, Director of Defense Mobilization, was on the stand.

Your statement which is a complete answer to Senator Flanders' question as to your attitude is your statement on page 2 and reads as follows:

> The question which confronts this Congress is whether to attempt to accelerate rearmament deliveries or to take the program approximately in the stride of 1951.

Then you went on:

> In my judgment, the latter course is the sound one. It would involve a substantial cut in the budget of $85.4 billion for fiscal 1953 which has been presented to this Congress.

That is a clear statement of your preference to return to the stride of 1951 so far as preparedness is concerned.

Mr. NOURSE. Yes, sir.

The CHAIRMAN. Congressman Herter last Saturday addressed this question to Mr. Wilson:

> Representative HERTER. Might I ask one question that I was going to reserve for the end? It is rather a detailed question.
>
> In the hearings that we have had up to date, from the Bureau of the Budget and others it is clear that Congress has itself lost the power to adjust the rate

of expenditures of amounts appropriated for the military departments for all of the things you have been talking about.

Mr. WILSON. Yes.

Representative HERTER. A great deal more money than was expendable in the immediate calendar year for which the appropriation was made?

Mr. WILSON. They have been obligated, but not expended.

Representative HERTER. That is right. So it has been carried over.

The rate of expenditure for this year was not determined by the Congress in any way whatsoever. It was determined by the executive department. And when we asked the head of the Bureau of the Budget whether he had any control over that, he said none whatsoever. The appropriations had been made to the Government departments and they determined the rate of expenditure, especially; that is, the military.

We said then, "Is there no control at all?" and he said, "Yes; the only control there is is Mr. Wilson's control over the rate at which they can actually produce the things, because he controls the allocation of materials."

Mr. WILSON. Well, that is only partly so. The rate of expenditure to a very considerable degree may be determined by what Mr. Lawton hinted at, that is, the rate at which we get them the materials and resources with which to go ahead, but the rate—and I hope you will note this, because it is absolutely correct—is determined by the time requirement of designing and preparing to turn the stuff out.

Representative HERTER. Then may I ask you this question: We are studying the economic aspects of this thing.

The gap, apparently, between the expected rate of expenditure and income is, roughly, $15 billion. That gap is reduced roughly by five, I have little less than that, by surplus cash in the trust funds that is collected as a form of taxation. That leaves the gap of $10 billion that you might call the inflationary gap.

Mr. WILSON. Yes.

Representative HERTER. The President has recommended that one-half of that gap be filled by additional taxation. The leaders of the Congress have said there will be no additional taxation. And the economic experts who come before us say that without that one-half gap being filled there will be unnecessary inflation.

This is the question, and it is a mean one: If the economists are right that that question of $5 billion one way or the other is going to determine whether there is unnecessary, excessive inflation in our economic system, from your point of view would it be better to slow down our expenditures $5 billion, rather than do nothing, if we cannot get additional taxes?

Mr. WILSON. I do not think I would slow down. Having in mind first and foremost the security of the country, I do not think I would slow down.

I read that because I think that it means a great deal to you members of the panel in the discussion.

Representative PATMAN. I wish you would read the question you asked.

Senator BENTON. It is very appropriate.

The CHAIRMAN. When I read it at your suggestion you will see why I did not go quite that far.

Representative PATMAN. I thought I heard you. Possibly, I misunderstood you.

The CHAIRMAN. No, I think you understood it.

Senator BENTON. While Senator O'Mahoney is looking up his quotation; is it correct, Dr. Nourse, that the $15 billion, minus the $5 billion leaves us $10 billion deficit?

Mr. NOURSE. Well, yes, in terms of arithmetic. I believe it is in that general magnitude. I think that a member of this joint committee has pointed out that it would be possible to effect economies of $7 billion in the total program without reducing he amount of fire power, as I think he put it, or actual preparedness.

Senator BENTON. It has to come out of the military programs, there is no doubt about that.

The opening charts that we saw here show that there is only about $6½ billion that is not tied up with commitments of one kind or another.

Mr. NOURSE. Of course, it is an assumption in my remarks that I think there is substantial slack in that military budget.

The CHAIRMAN. I have found the quotation, Mr. Patman. Let me read:

> The CHAIRMAN. If I understand your answer to Congressman Herter's question, which was a very searching question and one for which we must find the answer, it is that you would rather have this production, and lacking the taxes to pay for it you would choose a deficit rather than not get the production which we hope can be purchased by the $5 billion of which the Congressman spoke?
>
> Mr. WILSON. As usual, Mr. Chairman, you stated it most succinctly and exactly, as I wish I had been able to answer it.

Now, where are we going to cut the military budget, Dr. Nourse?

Mr. NOURSE. Well, I would make two points there. The first one I made in response to Senator Benton. I think there is considerable slack in that budget which, without reducing the efficiency or the speed of the military build-up, could be cut out, a very difficult job as a practical matter we all recognize. Second is the actual trimming of military requests.

Senator BENTON. It looks now as if we are going to raise the military pay 10 percent, so that does not sound like cuts on the way.

Mr. NOURSE. That raises the question as to what the implications of raising the pay would be or the necessity or possibility of doing it this time, however desirable it may be from certain criteria.

The CHAIRMAN. There is also talk of universal military training; a very strong report has been filed by Congressman Wadsworth of New York for universal military training. Some say that will increase the cost of maintaining the military forces; others say that it will be an economy.

Senator BENTON. Ultimately—ultimately an economy, 3 or 4 years from now.

Mr. NOURSE. If we start out off on the assumption that these additions are going to be made, which would offset any economies that might be introduced, and if we assume that the economies are not going to be made, then the whole thing is lost; in other words, the remark which is made outside that the Congress has lost control of the budget would be borne out.

That is a crucial issue right now.

The CHAIRMAN. Perhaps, I ought to make the observation that one of the reasons for the increased military burden, in addition to inflation, is the fact that the modern weapons which we are building are themselves much more expensive, even on the basis of the 1944 dollar, than the instruments that were built during the Second World War.

We have the modern airplane, the 1952, 1953 model which is much larger, much more complex, requiring much more material and much more expensive than the bombers which were used to destroy the industrial plant of Hitler Germany.

We talk about guided missiles. We talk about fantastic new weapons. Those who have sat on the Appropriations Committee know that they are vastly more expensive than anything that was ever used in war before.

And so we are confronted by plain evidence that war and preparation for war are both economic burdens beyond imagination. And Congress has, as you say, to answer the question of whether to attempt to accelerate rearmament in modern weapons or just take the calculated risk.

Senator BENTON. I think it is an uncalculated risk.

The CHAIRMAN. It is a risk.

Senator BENTON. The risk is uncalculable.

Mr. NOURSE. That is partly true. No one can demonstrate what is going to happen from the Kremlin.

Senator FLANDERS. I have never seen one of these calculated risks which we have presented to us so often, that was calculable.

Senator BENTON. I agree.

Senator FLANDERS. This is no different from any of them. You have to use judgment.

Mr. NOURSE. A better word would be to say "conscious" risk. We recognize there is some risk on that side. My emphasis is on the need that we get a proper evaluation, at the same time, of the risk on the other side, the risk to the economy.

Senator BENTON. I think that is true.

The CHAIRMAN. It is all a very great dilemma.

Representative PATMAN. Could we go ahead and hear all of these people, and then interrogate them later; otherwise, we will not get to them before noon. It is possible that some of us cannot be here this afternoon.

The CHAIRMAN. We will next hear from Dr. Blaisdell.

STATEMENT OF THOMAS BLAISDELL, UNIVERSITY OF CALIFORNIA

Mr. BLAISDELL. Mr. Chairman and gentlemen of the committee, I would like to address myself primarily to some of the international aspects of the proposals that are before the Congress in terms of the economic report. And I would like to summarize what I have to say just in a phrase which I call "the world crisis of confidence."

The place of the United States in the world economy today is so tremendous that we lose, I think, very often, to put it more accurately, we forget the significance to the world economy of what we do here; the extent to which people turn to the United States and say, "What are you going to do," becomes the dominant factor in what happens.

The reason that this is true is because we do function on the basis of the private activities of a great many thousands and hundreds of thousands of firms that operate all over the world. Our American economy has its own tenacles that go everywhere.

The fundamental program that we started on as a country some years back involved an attempt to rebuild, after the war, the so-called world economy. We are still at it.

The institutions that were anticipated 5 or 6 years ago, might be of some use, have proved of some help, but I think not nearly as much as some of us had hoped. I refer specifically to the monetary fund, the International Bank, and the program which was anticipated in terms of the International Trade Organization but which became the General Agreement on Trade and Tariffs. In other words, a program of opening up trade, of freeing the movement of funds back and forth between countries, of creating the conditions under which investment would move freely, have not developed.

The first and major deviation from this program was the development of the European recovery program. This was based on the assumption that the European countries needed a chance to recover and that it was in our interest to see that they did.

This program in turn was accomplished with very great success, in fact, in a period short of that of anything that anybody who had a part in developing it estimated could take place; in other words, a 4- to 5-year program was accomplished some place in the neighborhood of 3 to 4 years.

In the meantime other things had happened. And the development in Europe which was the trading center of this world trading economy indicated that as a matter of economic strategy we felt the increase in development of production in Europe would do this trick.

Senator TAFT. Who felt so?

Mr. BLAISDELL. This was the decision as I understand that was made by the Government of the United States?

Senator TAFT. To do what trick?

Mr. BLAISDELL. I am sorry.

Senator TAFT. To do what trick?

Mr. BLAISDELL. I am sorry.

Senator TAFT. I would say that ECA was undertaken to prevent the spread of communism in France and Italy, that is its greatest success. I do not think there was anything about general rebuilding of the world. Certainly, that was not what the majority of Congress voted for.

It seems to me that the basis of your statement is questionable, to begin with. The whole theory we were trying to rebuild the world economy, I mean. I do not think anybody ever consciously undertook such a task. They did particular things that they thought might help particular places and would be helpful, but we never undertook to rebuild the world economy.

I think you are starting the whole thesis of your whole discussion on the wrong foundation.

Mr. BLAISDELL. I did not mean to indicate that we were rebuilding the world. What I was saying——

Senator TAFT. You said rebuild the world economy.

Mr. BLAISDELL. What I am talking about is the world trading economy, an economy based upon world trading. That is what I am talking about, which was not a question of rebuilding the world. That is not the point. It is a question of the way in which we conduct our world trade. That is the point that I was trying to make.

This period of development then which we have proceeded through was brought to a halt which I would call the crisis of confidence, as a result of the Korean war; that this demonstrated in terms of its effect on the activities of private individuals around the world the impossibility, the uncertainty of the reestablishment of a free flow of funds and the free flow of trade which was, also, conditioned by many other things. The Korean war was simply the incident which made this clear.

This was followed during the past year and the year immediately following by a rush to secure goods which was inflationary in character and which was, also, worldwide in character. It's implications were reflected in the European countries. They went into our own country. And we have felt the repercussions of that just as much as we have felt the repercussions on our own economy of the military program. The military program that has gone along with this economic program has also been concerned with the reestablishment of this confidence, necessarily, on a world scale. Not that we were to run the world, but that we are to establish places within the world in which the private economy can function with the security of property as the basis on which we operate.

This is the only basis on which capital can move freely here, there or elsewhere.

In these terms then the monetary system under which this world trading economy has functioned, has been that of the pound sterling. More recently it has been built around the dollar. It has been finding ways of exchanging the dollar with the pound sterling, and the other currencies in such a way that the movement of capital can take place. But it does not flow freely as it used to flow.

We have been trying to find some way to underwrite this fundamental condition. My own feeling is that until we have a world situation with areas of solidity where capital can move, where trading can take place with ease and the feeling of security on the part of people, that we are not going to deal with this domestic situation that has to do with our stability with anything near surety that we would like to see.

This is something that takes a series of steps. It rests on the military strength as well as on the series of economic activity.

Against that general background I would like to make just one or two statements.

The first is with regard to the impact of the military program insofar as it is shipped to Europe, I mean, the amount of arms aid which we make available. The economic impact of this, except insofar as we could cut back by that amount, has no different effect than though we were producing the arms for use here by our own troops, or putting them into reserve. The economic impact is exactly the same. The only difference is that you put them in storage or you put them in use in Europe or some place else in the world, rather than here.

Senator TAFT. Does that apply to that part of the dollars—that 10,400,000,000 foreign-aid dollars—that are spent to buy French airfields and to do a lot of other expenditures in France, and to pay duties on our military goods that go into France?

Mr. BLAISDELL. The expenditures in France have exactly the same effect as any other exports that might be made from France, and——

Senator TAFT. You did not say exports. You said the same as our construction of military weapons in this country.

Mr. BLAISDELL. Yes, sir. What I was talking about was the transfer of military equipment from this country to Europe.

Senator TAFT. That has the same effect, that is true enough.

Mr. BLAISDELL. That was my point.

Senator TAFT. I am saying that that foreign aid $10,400,000,000 does not apply, as I see it, to the purchasing of airfields in France and other payments to France which are being made——

Mr. BLAISDELL. I would agree.

Senator TAFT. The same as if made directly to manufacturers in this country.

Mr. BLAISDELL. The same, exactly the same as any other export from those countries.

Senator TAFT. Those are not the same as exports, because when we export something we pay American workmen with the cash. When we go over and pay the French money for airfields, I do not know where the money goes. They have got about $4 billion in gold, apparently. I do not think you can say that that kind of foreign aid has the same effect as the manufacture of goods in this country. Do you not think so? The dollars may be later used to buy civilian goods, I support, which is a possibility.

Senator BENTON. I do not see how you can deny Senator Taft's point.

Mr. BLAISDELL. I would not deny it for a moment.

Senator BENTON. I thought there was some misunderstanding between you.

Mr. BLAISDELL. I was agreeing.

The other and last point that I would make is that in this American program for the rebuilding of a world system of private trading one of the most important things is the reaction in other countries to the development in this country of a program of restriction of imports in this country. These tariffs and other hindrances interfere with other countries' ability to earn their way.

Just as we have pressed on other countries the necessity for opening of trade channels, we, ourselves, are in a position of being able to aid this development by freeing trade channels here and creating conditions which will make importing easier rather than more difficult.

This is the substance of what I have to say.

The CHAIRMAN. There is an inflationary effect of the expenditures that are recommended in the budget before us, both here in the United States and in those countries in which those military expenditures are made, is there not?

Mr. BLAISDELL. Correct.

The CHAIRMAN. And then do you agree with what Dr. Nourse said at the outset—that this is a double-barreled question which the Congress must answer whether or not to continue to promote the military expenditures which are in themselves acknowledged to be inflationary, or whether to invite a deficit in order to carry on these expenditures at a particular rate rather than to slow them up too much; and, finally, of course, whether or not it is possible in the dilemma that confronts the free world to abandon military expenditures and go to some other method of trying to win the minds of men all over the world?

Mr. BLAISDELL. I would certainly agree, first, on the inflationary character and the impact of the proposed program.

I would like to comment very briefly on the question of the rate of expenditure.

I would agree that the rate of expenditure can hardly be determined by any act of Congress. The total over a period of time, yes, but with regard to the rate of expenditures in the foreign program the rate has been remarkably stable; it has run at a rate, if my memory is correct, of about $6 billion a year steadily for the last 6 years, and this has been irrespective of the exact level of the appropriation that has been made. This has been the rate at which it apparently could be fed into this kind of series of economic transactions.

By the same token with the military program the rate of production of the military program seems to me to be determined very largely by character of the techniques that are involved in the production, and there is very little that can be done either to speed it up much or slow it down much.

The lead time on most of these items is so great that the expenditure in large amounts for heavy equipment is something that takes months. It runs into years for some of the equipment, as you know only too well.

So that this is something where, in my judgment, the more pressure there is to produce fast the better. Whether the rate, as it has worked out, has been the best it could be, I do not know. I have the feeling that the greater the pressure the better in view of these very long lead times there are.

The CHAIRMAN. What reason have you to believe that if it were pressed with greater rapidity than was followed in 1951 or than is recommended in the President's budget that you could reach a conclusion? Now, the conclusion that you have got to reach, according to your premise, is a world in which normal trade to which we have been accustomed in the capitalistic world shall be restored.

Mr. BLAISDELL. That is exactly right.

The CHAIRMAN. But we are faced by the blunt fact that the leaders of the Kremlin have announced that they are engaged on a program of world conquest.

Mr. BLAISDELL. Right.

The CHAIRMAN. Based upon their conclusions that the capitalistic system is outmoded——

Mr. BLAISDELL. Right.

The CHAIRMAN. That it cannot last and that free peoples are too selfish and too greedy to preserve their own system, and that mankind must be told what to do instead of being free to decide for itself what it desires to do.

You agree with that, do you not?

Mr. BLAISDELL. Definitely.

The CHAIRMAN. Then what is the basis upon which we can hope to bring this thing to any speedy conclusion by speeding up the rate?

Mr. BLAISDELL. My own feeling is that the sooner we can feel in our own minds and hearts that we have a Military Establishment which is reasonably able to take care of us and can see security growing in various places, the sooner we are going to have the opportunity to roll back the progress that has been made on the part of the Soviet forces. And I think this is a process that is going to take time, but for my judgment I would say that the quicker the better. And the quicker the less chance there is of serious trouble developing.

The CHAIRMAN. Do any members of the panel desire to comment?

Senator TAFT. There are so many more things than the size of the Army that have to do with it. It seems to me it depends on what the Army is for, what you will undertake to do. Certainly there are wide ranges of proposals. Some people want to stay in this country entirely.

I read a speech of Mr. Dulles' the other day and he said that our whole theory should be based on one striking force, we should not try to meet every possible advance of Russia around the borders of the Russian Empire.

It seems to me that the whole question of how big this ought to be is a question that is capable of judgment in an entirely different way from just bigger and better. I do not think you can approach it from that standpoint which you seem to suggest.

I do not say what that policy ought to be, but it seems to me that you have various policies as to the military, a foreign policy, you might call it, some of which are much more expensive than others, and it requires a very broad judgment, I think, as to how big that must be.

You could, I suppose, spend $150 billion a year without the slightest difficulty on projects that the Army will say are desirable, if you want to have an Army ready to hit Russia wherever they happen to move anywhere in the world.

The whole thing depends, not on modern weapons—it depends on what your foreign policy is. What will you do with the Army, where will you fight a third world war, if you have to fight it, how will you fight it?

Those are the questions that seem to me to determine how big this effort ought to be.

Certainly, we have to face inflation and everything else, if it is to do something absolutely necessary.

There is certainly a wide range of possibilities and different sizes of military effort.

Mr. BLAISDELL. I was addressing myself in my remarks here primarily to the question as to the rate at which a program could be built up, a program of the magnitude of 50, 60, 70, 80 billion dollars a year and the rate at which this can be done. The point I was making is that the evidence would seem to indicate that there is very little you can do in terms of the appropriation process in determining the rate at which that can take place. That was the only point I was making.

Senator TAFT. That may be. You can slow the thing down. I agree to that for the first year, but I do not agree to it as to the second year. I think there is a very material difference as to what you appropriate how fast you go there.

Senator FLANDERS. May I just revert to a remark of yours for a moment?

I understood you to suggest there was an alternative to the military arm in the effort to affect the minds and hearts of men.

Would it not be better to suggest that the second process can be supplementary and complementary to the military arm and not present them as alternatives?

The CHAIRMAN. I would agree to that. That is realistic.

Senator TAFT. That is one-half of 1 percent.

The CHAIRMAN. That is the process of education. I think the Senator from Vermont and I are in pretty good agreement on that.

Senator FLANDERS. I think so.

The CHAIRMAN. The suggestion of Congressman Patman is that we proceed a little bit more rapidly with the opening statements, because it will be necessary, perhaps, for him and other members to leave this session at noon.

The next panelist in order is Mr. Woodward of the Mutual Life Insurance Co.

STATEMENT OF DONALD B. WOODWARD, SECOND VICE PRESIDENT, MUTUAL LIFE INSURANCE CO. OF NEW YORK

Mr. WOODWARD. Mr. Chairman and gentlemen, the fundamental problem this country faces is how to prevent its really wounderful achievement thus far, and its fabulously promising future, from being fouled up by anyone—Russia, itself, or anyone else. Already—and this is my fundamental proposition—we are better off than any other country in the world, and the scientific revolution now under way offers us a future of life so much longer, so much healthier and so much happier as to dwarf the highest hopes of today's optimists—and the whole world can come with us if it wishes. The gloom that one so frequently encounters today is subject to more vigorous challenge than perhaps gloom has ever been in history.

The first of the two main risks of our being fouled up comes from abroad. This is, conditions might arise there in which we could not maintain our present welfare nor realize our future promise. We try to prevent this development by increasing our power and that of our allies and friends. The objective is unchallengeable, but I have some qualifications about methods.

The second of the two main risks to our good fortune and our happy future is at home. It is that we may inadvertently take some action that will impair, or fail to take some action that is necessary for, our present and our inspiring future.

But "foreign affairs" and "domestic affairs" are simply two sides to the same coin. The risk of getting fouled up encompass both alike and together.

The non-Communist nations need to make themselves strong enough, and keep themselves strong enough, to repel Communists in any way they try to move: Subversion or sabotage, perversion of elections, coups d'etat, satellites, small or large-scale attacks. Adequate military strength is, of course, required, but so are economic strength, political strength, and moral strength—and not only now but for many years, and not only here but among the non-Communist nations. Achievement and maintenance of that strength will require satisfaction, and at least some degree of enthusiasm, about our system. People must like it and want it if it is to succeed and continue.

A great, and perhaps the greatest, enemy to maintenance of strength of our system would be marked instability over time in the income and employment of people here and elsewhere in the non-Communist world. Major instability will not win nor hold support either at home or abroad for our system.

Our reputation is not good in this regard. Our record is unsavory; however, war has been a cause of much of this instability. You gentlemen are aware that during the past generation we have had one awful depression, two severe ones and three disturbing ones. In addition, we have had three heartbreaking inflations, one financial bacchanalia and assorted lurches and bumps. Even since World War II, though we have done better than many expected, we have further complicated the existence of our friends abroad by subjecting them to what to them was a very distressing slump in 1949, and a violent inflation since. The Communists are very fond of this prominent part of our record—but no one else is.

The committee is very wise in directing attention to economic instability. The subject needs the most serious and searching attention. It is true that over the past 20 years this country has erected a number of defenses against major instability, some of them truly impressive. And, to repeat, our performance since 1945 has been much better than many expected. But that is only one side of the story. The other side includes a vast inflation of money, of private and public debt, the huge expansion in productivity capacity, the great increase in commodity and land prices, the ruinous increase in the cost of imports to the older nations, and serious disequilibria in balances of payments. The world economic system was wrecked by two wars and nothing that is viable, that can stand on its own feet, has been erected since.

That is the point that Dr. Blaisdell made.

Internally we have had high activity—but first, mostly as a consequence of deferred demands and then mostly as a consequence of rearmament. Neither internationally nor domestically do these appear to be enduring bases for high rising and stable activity. I know that by reasonable definitions the needs for goods and services are so great that output and employment should never decline—but that was also ture in 1920, 1924, 1927, 1929, 1938, and 1949. And I am not suggesting the gloomy economic maturity theses, which I disbelieve. I know that there are very persuasive and plausible explanations of the inflations, and doubtless there always will be; but words, however good, will not remedy their very harmful effects.

We certainly should follow the expansionist road, as this country happily has so long done. I think that we need to examine carefully, and I expect do some more work on the road and the car to be as sure as possible that the bumps are kept down to bearable size for ourselves and our friends.

There are eight or nine things that I think we could do to be moving in a useful direction.

Some of the things I think would help here:

1. Spread the military expansion program out over the maximum time the experts believe prudent. This is not solely a military decision—it is also a political one.
2. Curtail the expansibility and contractability of the monetary system.
3. Decentralize decision making, so that little mistakes have little importance and even big mistakes do not shake the world.
4. Let markets make decisions instead of men, to the utmost possible extent.
5. Encourage savings to stay put, instead of flopping around, causing instability.
6. Restrain public expenditure to the utmost possible degree.
7. Seek to bring about conditions most conducive to regularization of business investment at a high level.
8. Open much wider the channels of trade among countries.
9. Give added encouragement to scientific and technological development both at home and abroad.

And I think we need to lift the tone and the sights of our relations with our friends and allies. The objective of a viable and growing economy which the Marshall plan sought was far more inspiring and attractive than an international program so preponderantly military. We need the rest of the world and it needs us for far more happy, exciting, and satisfying experiences than just digging trenches.

I don't suggest these points as a complete program, nor that they or any program would or could or should eliminate all business fluctuations. But I think they would help, with additions and alterations which discussion would develop, to lessen the risks of fouling up our splendid achievement of living standards and the grand promise of a better—far, far better—future.

The CHAIRMAN. Your point No. 3, decentralize decision making.

Mr. WOODWARD. Yes, sir.

The CHAIRMAN. So that little mistakes have little importance and even big mistakes do not shake the world.

Mr. WOODWARD. Yes, sir.

The CHAIRMAN. How can you decentralize decisions which affect the world?

Mr. WOODWARD. Well, sir, I can mention several examples. One is the stockpiling program.

It is quite evident to me that we need a stockpiling program for scarce and critical materials.

It is also quite evident to me and I believe to any one of our foreign friends that the way our program has been carried out has been to create very serious instability in a number of countries and commodities.

I think it should be possible to develop some sort of system in which the decisions on speed of acquisition and method of acquisition could perhaps be made at a number of points instead of one point.

The CHAIRMAN. Let us make it specific.

Mr. Wilson is the Director of Defense Mobilization, and under the concept of that organization set up under the Defense Production Act on him falls the responsibility for innumerable decisions. Of course, they come up to him through a widespreading organization, the details are worked out below. He does a lot of coordinating, but, essentially, decisions are centralized.

Could we decentralize that bureau?

Mr. WOODWARD. I should think that if we put our ingenuity to it we would find ways to bring about some decentralization, perhaps through subcontracting, perhaps through subsidiary organizations. I cannot give a blueprint on it.

The CHAIRMAN. Of course, the allocation of materials appears to be a very essential elements in getting the military production that we seek.

Assuming that we are going to get the military production, can we avoid having a centralized decision with respect to the allocation of materials?

Mr. WOODWARD. As to total quantities, I expect not.

As to the details of how the part not required by the military is distributed, I should think we could; yes, sir.

The CHAIRMAN. We will next hear from Mr. Foulke of Dun & Bradstreet.

STATEMENT OF ROY F. FOULKE, DUN & BRADSTREET, NEW YORK

Mr. FOULKE. Mr. Chairman and gentlemen, I shall address myself primarily to point No. 3, "What are some of the regional and special industry problems?"

From January 7 to 18, Dun & Bradstreet, Inc., undertook a survey of businessmen's expectations for the second quarter of 1952 compared with the second quarter of 1951. This survey was undertaken by a staff of 128 men who interviewed a sample of larger manufacturers, wholesalers, and retailers in all parts of the country. The executives were asked whether in their opinion net sales of their respective businesses, net profits after taxes, level of selling prices in their respective lines, level of inventories, number of employees, and in the case of manufacturers, volume of orders, would be greater, smaller, or about the same for or at the end of the second quarter of 1952 compared with the second quarter of 1951.

I would like to present the details of this current businessmen's expectation survey for the record. It indicates that of the industrial and commercial business men interviewed, 58 out of every 100 expect increased sales for the second quarter of 1952 compared with the second quarter of 1951, 25 about the same, and 17 smaller sales; 35 out of every 100 expect increased profits after taxes, 29 the same, and 36 smaller profits. These figures and similar figures regarding orders, number of employees, level of inventories, and level of selling prices, would seem to indicate sustained industrial and commercial activity, substantial profits, and high level of employment in the second quarter of this year.

These expectations are all contained in more detail in a table that I have here.

The CHAIRMAN. It will be inserted in the record at this point.

(The table entitled "January 1952 Survey of Businessmen's Expectations," is as follows:)

January 1952, survey of businessmen's expectations—Percent of businessmen expecting increases, no changes, and decreases, second quarter of 1952 compared with second quarter of 1951

Items and classification	Number of concerns reporting	Percent of businessmen interviewed who expect—		
		Increases	No change	Decreases
Dollar volume of net sales:				
All concerns	1,090	58	25	17
All manufacturers	547	62	21	17
Durable goods	294	63	22	15
Nondurable goods	253	60	21	19
Wholesalers	331	50	30	20
Retailers	157	62	23	15
Dollar amount of new orders received:				
All manufacturers	468	60	23	17
Durable goods	259	62	22	16
Nondurable goods	209	57	24	19
Net profits after taxes:				
All concerns	979	35	29	36
All manufacturers	488	39	27	34
Durable goods	267	40	27	33
Nondurable goods	221	39	35	26
Wholesalers	292	28	30	42
Retailers	150	34	34	32
	End of June 1952 compared with end of June 1951			
Number of employees:				
All concerns	1,105	19	75	6
All manufacturers	553	25	66	9
Durable goods	288	34	59	7
Nondurable goods	265	17	73	10
Wholesalers	332	10	88	2
Retailers	160	14	81	5
Dollar level of inventories:				
All concerns	1,051	28	38	34
All manufacturers	533	31	41	28
Durable goods	282	36	39	25
Nondurable goods	251	26	44	30
Wholesalers	318	24	33	43
Retailers	155	26	36	38
Level of selling prices:				
All concerns	1,036	28	58	14
All manufacturers	513	27	63	10
Durable goods	270	26	68	6
Nondurable goods	243	27	58	15
Wholesalers	319	30	52	17
Retailers	154	28	48	24

Mr. FOULKE. Further indication of a favorable business environment is evident in the relatively low failure record last year. In 1951 there occurred 8,058 business failures, a decrease of 12.1 percent from the 9,162 failures in 1950.

Failures for both 1950 and 1951 were materially below the average number of failures over the past 50 years and even more below the average index of failures over the past 50 years.

I have here a table which gives the number of business failures by months, from 1948–51 with the percent change each month of 1951 compared with 1950.

The CHAIRMAN. It will be inserted in the record.

(The table entitled "Number of Commercial and Industrial Failures by Months, 1948–51," is as follows:)

Number of commercial and industrial failures, by months, 1948–51

	1948	1949	1950	1951	Percent change monthly, 1951 compared with 1950
January	356	566	864	775	−10.3
February	417	685	811	599	−26.2
March	477	847	884	732	−17.2
April	404	877	806	693	−14.0
May	426	775	874	755	−13.6
June	463	828	725	699	−3.6
July	420	719	694	665	−4.2
August	439	810	787	678	−13.9
September	398	732	648	620	−4.3
October	459	802	707	643	−9.1
November	460	835	683	587	−14.1
December	531	770	679	612	−9.9
Total	5,250	9,246	9,162	8,058	−12.1

Mr. FOULKE. While the immediate outlook of all commercial and industrial activity is favorable, that does not mean problems do not exist.

In the current businessmen's expectation survey, we also asked the question, "What are the major problems affecting your business today?" The problems mentioned most frequently fell into 10 categories ranging from inadequate supplies of materials to anticipated results of reduction in the building construction.

I would like to present a summary of that survey for the records.

The CHAIRMAN. It will be received for the record.

(The statement entitled, "Principal Problems of Businessmen as Reflected by the Survey of 'Businessmen's Expectations'" is as follows:)

PRINCIPAL PROBLEMS OF BUSINESSMEN AS REFLECTED BY THE SURVEY OF "BUSINESSMEN'S EXPECTATIONS," JANUARY 7–18, 1952

A survey of businessmen's expectations was made by Dun & Bradstreet, Inc., during the period January 7–18, 1952. In addition to questions regarding expected trends of sales, earnings, employment, and levels of their inventories and prices, the business executives interviewed were requested to comment on the question "What are the major problems affecting your business today?"

The problems which were mentioned most frequently and which are apparently most vexing to business in general fall within 10 principal categories. They are:

1. *Inadequate supplies of materials.*—This particular response was given by 17 percent of the executives interviewed. It was a particular problem for those whose businesses are engaged in hard-goods lines, and especially for those directly or indirectly engaged in production of military goods under Government contracts. The principal shortages mentioned were metals such as steel, copper, brass, bronze, aluminum, and finished products such as tools, machinery, electrical supplies, hardware, auto parts, household appliances, and mill supplies. Other goods mentioned as in short supply were certain chemicals, paper, leather, nylon, and bottles.

2. *Increased costs of goods, labor, and general operations, not compensated by corresponding price increases.*—The rising costs of doing business were cited as a matter of concern by 14 percent of the businessmen interviewed. As a corollary to this particular problem, an additional 4 percent of all executives interviewed referred to OPS regulations, or made the statement that their present margins of gross profit on sales were "too narrow."

3. *Increased Federal income tax rates.*—Approximately 10 percent of the executives were sensitive to the downward pull on their earnings exerted by increased Federal income taxes. What lends emphasis to this "problem" is the fact that income taxes were mentioned as a major factor more often in the January survey than in any previous survey in which this particular question was asked. In a similar survey made in April 1951, for instance, only 3 percent of those interviewed mentioned income taxes as a major business problem.

4. *Shortage in skilled or competent help.*—This particular problem was mentioned by approximately 8 percent of the executives interviewed. The shortage in skilled help was of special concern to a number of manufacturers of durable goods, but others, including retail concerns, referred to a scarcity of clerical and office personnel.

5. *Increased severity of competition.*—Four percent of the executives, particularly those engaged in producing textiles and other soft-goods lines, mentioned increased competition as their particular problem.

6. *Declining sales.*—Three percent of the businessmen, represented by those engaged in consumer goods industries, reported that their main concern was a reduction in the level of sales thus far in 1952 as compared with year-ago levels, or else felt that sales would decline as the year developed in comparison with 1951 dollar-volume levels.

7. *Development of buyer's resistance to prevailing price levels.*—Buyers' resistance was mentioned most frequently by businessmen engaged in retail lines. About 3 percent of the businessmen stressed this problem.

8. *Actual or potential declines in price levels of their products.*—About 3 percent of the executives mentioned actual or potential declines in prices as their major concern.

It is rather interesting to find that problems Nos. 5, 6, 7, and 8, while tabulated separately in the subject memorandum, are all corollary problems. Where so considered, the aggregate percentage of the businessmen who expressed special concern over the questions of severity of competition, declining sales, consumer resistance, and actual or potential declines in prices, represented 14 percent of all the executives interviewed.

9. *Slow collection of accounts receivable.*—Slow collections were mentioned as a problem by 3 percent of the executives interviewed.

10. *Threatened reductions in building construction.*—Slightly more than 2 percent of the businessmen, primarily those engaged in building construction and contracting, or those selling building materials, brought up the question of threatened reductions in the volume of building construction as a matter of concern.

Mr. FOULKE. I also have a study of area problems throughout the United States, dividing the United States into eight areas. For instance, in Senator Flanders' region of New England, New England still depends to a great extent on the textile and leather industries, although there is a substantial hard-goods industry in Connecticut.

Senator FLANDERS. Also in Vermont. It is a machine-tool-building State.

Mr. FOULKE. The problems of New England are a little bit different than, let us say, those of Ohio, which is reported to have some 7 percent of the total amount of prime contracts awarded by the defense arm of the Government.

Moreover, approximately $1 billion in plant expansion has been undertaken in Ohio under certificates of necessity.

Also there is the fact that the South depends so much on textiles. The textile mills today are operating at 3 to 4 days per week and there was a period just a short time ago when they were operating 2 to 3 days a week.

I should like to present for the record this series of area problems in the United States.

The CHAIRMAN. That will be received for the record.

(The paper entitled, "Summary of Area Problems", is as follows:)

SUMMARY OF AREA PROBLEMS

NEW ENGLAND

Except for Connecticut, the New England economy is geared closely to the production of shoes and textiles. Both industries are affected strongly by lower labor costs and greater availability of raw materials in other parts of the country, particularly in the Southern States. The exodus of cotton mills to the South is apparently a precedent for a similar move under consideration by manufacturers of woolens. American Woolen Co. announced only last week that it would not renew its contracts with the CIO Textile Workers Union when they expire March 15, 1952, and that it was considering moving all of its 21 New England mills southward. According to a representative of this company, southern mills are in a position to sell their cloth for 30 to 50 cents less per yard than American Woolen Co. Some 20 other woolen and worsted mills also have filed intention of canceling their union contracts.

Some local textile mills have been working on contracts to produce cloth for the Federal Government, but the substantial decline in civilian demand which followed the peak surge early in 1951 has been accompanied by unemployment in such cities as Lawrence, Mass., and Providence, R. I.

Similar problems are apparently affecting manufacturers of shoes in Massachusetts. In Providence, R. I., manufacturers of jewelry are restricted as to use of certain base metals. Some of the larger manufacturers of jewelry hold subcontracts on Government work, but the smaller manufacturers either have been unable to obtain contracts or are not equipped for precision work. Connecticut has a strong nucleus of durable goods industry in New Haven and Bridgeport.

NEW YORK STATE

As an important economic area, New York State is actually two regions within one, with a sharp demarcation between New York City as an important manufacturing and distributing center for soft goods, and upper New York State with its important hard goods manufacturing plants along the route of the old Erie Canal, as well as its important agricultural activities in the rural areas.

The economic patterns of New York City's soft goods industries followed those in other producing centers of consumer's goods in 1951. First, there were the results of the final surges of scare buying in January and February 1951, resulting in sharp first-quarter rises in sales, and these in turn were followed by the inevitable inventory accumulations which resulted from overbuying. For the year as a whole, however, the city didn't do too badly, and it is interesting to note that the most recent figures as to sales of department stores would indicate that the rise in dollar volume of the New York City stores was almost identical with the national average.

New York City does, however, reflect one particular municipal pattern which appears to be a typical result of the inflationary influences of recent years. This pattern is the difficulty which the city faces in raising revenue from its customary sources to finance rising costs of municipal payrolls, particularly as regards transportation, police and fire departments, teachers' salaries, and hospitals. In 1951, the city increased its city-wide retail sales tax from 2 percent of retail sales to 3 percent. Other sources of revenue are under discussion, including assessment of a new county tax of 1½ percent of assessed real-estate valuations, provided the New York State Legislature and a city-wide referendum were to approve.

In up-State New York, cities such as Schenectady, Syracuse, and Buffalo are in the throes of a boom resulting from the production of goods under contract with various agencies of the Federal Government. The major problems there are the acute shortages of skilled labor, the lack of machine tools and parts in certain areas, and slow deliveries of goods which are under allocation.

PENNSYLVANIA

The principal industry directly related to defense mobilization is, of course, the steel industry. Reports from Pittsburgh are that the current labor negotiations represent the principal problem at present. Otherwise, steel men are reported to be criticizing the controlled materials plan, contending that some of the shortages of ferroalloys such as cobalt steel and nickel steel are the result of hoarding which has accompanied the operation of the plan.

In the bituminous coal-producing areas nearby, there is a fear that industrial change-overs to gas and other fuels will create long-range problems for the coal industry, but increased demands for soft coal currently have offset the results of competition from these other fuels. Moreover, export sales of bituminous coal have been increasing.

In another heavy industry, namely, production of industrial machinery, there is a predominant shortage of machine tools. Allocation of materials to producers of the tools themselves has in turn resulted in a shortage of raw materials for the machinery manufacturers even after they receive the tools.

The soft-goods industries in the State, such as hosiery, luggage, men's clothing, and dry goods report a surplus of supply of finished goods over demand, and relatively large inventories on hand.

Most lines of business in the State have a personnel problem, aggravated in Philadelphia by the hiring of an increasing number of people by Federal and local government agencies. The printing and publishing industry in Philadelphia, which is the fifth largest employer in that city, has been particularly hard hit by employee turn-over.

Rising operating costs in the State have been reported by public utilities, particularly in transportation and communications. To date they have not been able to obtain the rate increases which they consider necessary to offset these cost rises, which, in turn, have caused the utilities to postpone or reduce programs for purchase of new equipment.

Many businessmen in the area complain of difficulties in financing created because of high Federal income taxes. The smaller concerns have been unable to build up this working capital out of earnings as rapidly as they would like because of taxes and some businessmen expect that collections of their accounts receivable will become delayed as income taxes fall due, since increased portions of their present working capital are absorbed by rising costs of inventories.

THE SOUTHERN STATES

Many of the southern textile mills are operating on a 3- or 4-day week. Exceptions are those textile mills which are working on orders from the Federal Government.

The hardwood lumber industry reports that sales of hardwood lumber have fallen in recent months because of a decline in the volume of residential building late in 1951 as compared with the activity of building earlier in the year. Opinion among lumbermen is that present inventories are high and that supply in 1952 will exceed demand and result in lower prices. A number of mills in the Southeast have been closed.

Furniture manufacturers who attended the annual show in Chicago in January 1952 reported that prices of bedroom suites were $20 to $30 lower than in January 1951.

There is a feeling of uneasiness among some southern businessmen. They seem to think that a Korean truce might start a severe downward business trend although they also recognize the possible inflationary influence of present high levels of savings.

THE MIDWEST

Industrial activities throughout the Midwest are characterized by a tremendous productivity bounded only by shortages of materials, tools, and labor.

The State of Ohio alone is reported to have some 7 percent of the total amount of prime contracts awarded by the military agencies. More than $1,000,000,000 in plant expansion has been undertaken under certificates of necessity in that State. The machine tool industry in Ohio has a backlog of unfilled orders sufficient to keep the machine-tool industry active for 20 months. The defense effort there has caused shifts in working population, such as in Columbus, where one aircraft factory increased its payroll from 1,500 to 10,000 employees in the year ended January 1, 1952.

Elsewhere in the Midwest, there are similar reports of shortages of skilled labor, tools, and material. Detroit manufacturers have tremendous backlogs in defense contracts, but with constant adjustments in design it is difficult to get the full go-ahead on defense production. Des Moines, Iowa, has a backlog of $30 million in industrial building construction, but the construction is being delayed by shortages of materials there.

On the other hand, manufacturers in the St. Paul, Minn., area have few defense contracts, attributed to high freight rates. The smaller factories have been laying off some help because they are unable to obtain material needed for producing civilian-type goods. There are also reports of a decline in over-all population in this area, with people moving to the west coast.

Small manufacturers around St. Louis, Mo., also complain of inability to obtain defense contracts. The smaller concerns have been unable to obtain machine tools and are having difficulty in financing contracts when they are received.

The midwestern offices report that one of the major reactions of local businessmen takes the form of criticism over the complexity of actions by the Federal Government in administering controls over prices and allocations of materials. There is also considerable criticism over deficit financing and of prevailing high tax rates.

In some instances, local unemployment has been reported as the result in difficulties involved in the change-over from production of civilian to military-type production. Delays in obtaining tools and materials, along with changes in designs, are said to have contributed to the unemployment, most of which affects unskilled rather than skilled labor.

THE SOUTHWEST

One of the major problems in this area is the unfavorable agricultural outlook which has resulted from prolonged unseasonably warm and dry weather. Continuation of such weather conditions could have a profound effect on the economy of the Southwest because of crop failures.

For the rest, business in the Dallas area is booming, but local businessmen complain of excessive governmental regulations which they feel contribute unnecessarily to costs of operations. There is a shortage of agricultural labor because of attraction to defense plants, and a high rate of labor turn-over, attributed in part to salary and wage stabilization.

The usual shortages of metals such as aluminum, copper, and certain types of steels are reported. Smaller builders of homes find it difficult to obtain building materials and there is also a feeling that regulation X is contributing to a lower volume of building.

In Houston, where primary industries are petroleum chemicals, and lumber, the stresses and strains of mobilization appear not so pronounced. However, retailers complain that the price regulations of Office of Price Stabilization make it difficult to operate profitably. The labor situation is well balanced. There is a shortage of tubular goods for oil wells, but drilling continues at a high level.

THE WEST COAST

Among the principal industries are aircraft production, agriculture, petroleum, and food canning.

The aircraft industry has had to cut back production of air frames by 30 to 50 percent. The reason is a serious shortage of electronic components and of aircraft engines, together with frequent changes in design and contract specification by the military. There are shortages of material, including steel. The aircraft industry is about 15 months behind military orders.

In agriculture, there is concern over ability to obtain adequate seasonal labor from Mexico. The agreement with the Mexican Government regarding migratory labor expires in February 1952, and since California supplies one-third of the country's fresh fruits and vegetables, growers are disturbed lest there be delay in reaching a new agreement. There are shortages of agricultural chemicals, and the industry feels that nitrogenous chemicals and sulfuric acid should be allocated more equitably.

Petroleum producers report shortages of seamless tubing which hamper production. At present, 50 percent of western production of oil goes to military agencies. Expansion of facilities requires substantial capital, but net income after dividends and taxes is said to be insufficient to permit capital accumulations.

Food canners have adequate labor now but report a tightening. Labor costs have increased, exerting pressure toward higher prices. Some small canners in the area have contracted their total output to the Armed Forces in the form of K and C rations.

A new record of employment was registered in Los Angeles in December 1951. Aircraft employment is on a two-shift basis. The industry could use at least

2,000 more engineers and some piracy of aircraft engineers has taken place between Los Angeles and Detroit.

There are 1,123 different industries around Los Angeles, of which half employ less than 25 persons. If allocation of materials is not balanced properly, it is anticipated that the smaller industries will suffer proportionately.

In Arizona, there are conflicting reports of unemployment in Phoenix, with 6,000 persons unemployed, and of manpower shortages in Tucson where two aircraft factories are situated.

San Francisco reports that only three prime contracts have been placed in that area, one for $177 million, one for $47 million, one for $20 million. Local manufacturers feel they have been neglected in the placing of defense contracts. Shipping has increased because of Korea, 1951 volume of tonnage being 20.9 million tons compared with 18.1 million tons in 1949.

Skilled manpower is in short supply, and workers hesitate to leave civilian employment where they feel more secure. The feeling in San Francisco is that there is too much "business as usual," and that more food and equipment should be produced. Practically no requests for price relief under the Capehart Act have been made by manufacturers.

PACIFIC NORTHWEST

Local industry feels that allocation of steel is maladjusted because the base period for allocation is the first 9 months of 1950, which was not representative of steel usage in the area. At that time, local economic activity was at a low rate because of strikes and a local slump in business. Moreover, the allocations have not provided for unusual rate of business growth in the area. Many businesses which use steel may have to close because of lack of materials.

There are few large industries in the area. Many local industries look to Small Defense Plants Administration for help in obtaining defense contracts. The area lacks a full integration of industries. The local economy is built around lumber, fishing, and agriculture. No large expansion of facilities for fabrication of products from raw materials has been made. Creation of new enterprises to effect this integration is not believed feasible under present programs of controlled economy.

Mr. FOULKE. The soft-goods industries have had problems of heavy inventories, and the hard-goods-industries problems of getting trained manpower, of setting up production lines of contractors to subcontractors, and planning, in general, for increased production.

I would also like to present for the record summaries of problems which exist today in 11 selected divisions of soft-good industries and 12 selected divisions of hard-goods industries.

For your information, I shall condense these over-all summaries very briefly.

First, the soft-goods industries.

As a result of the outbreak of the Korean war and the consequent defense program, many segments of the textile industry speculated in inventories during the second half of 1950 and early 1951.

After OPS was instituted and after consumer scare buying subsided, practically all textile lines faced the problem of adjusting these inventory accumulations. Some lines and some concerns have accomplished this objective more successfully than others by restraining purchasing programs and cutting down on production schedules.

The hard-goods industries problems are of a different character.

Manufacturers whose products are fabricated largely of metal have been affected in one of three ways by the rearmament program, (1) some that were operating at practical capacity have continued to do so, (2) some have experienced a recent reduction in volume in consumer goods without a corresponding increase in defense orders, (3) some that were operating at much less than capacity prior to June 30, 1950, have received a tremendous volume of defense orders, and have now reached capacity.

Two circumstances are responsible.

In respect to consumer goods, the pattern is the same as that manifested by the producers of soft goods—(1) a rush to buy after the outbreak of the Korean conflict, and (2) a secondary rush when Communist China entered the war, the sharp increase in prices, subsequent satisfaction of the demand followed by a sharp falling off in purchasing.

Secondly, the materials required by the Government for rearmament differ materially from the output of many factories in their normal activity. Because of the different techniques and talents required, it would be impossible to assure that every company would be the recipient of defense orders to counterbalance the decline in civilian production that followed the let-down in demand or in ability to obtain an adequate supply of scarce metal. The factory which performs a simple soldering operation in assembling an electronic phonograph from purchased components is not qualified, either in terms of manpower, equipment, or engineering, to produce an airborne radio receiving set that demands the highest skills in its production.

Here are the more detailed summaries of the important lines in both soft goods and hard goods.

The CHAIRMAN. That will be made a part of the record.

(The paper entitled "Problems in Eleven Selected Divisions of Soft-Goods Industries and Twelve Selected Divisions of Hard-Goods Industries," is as follows:)

PROBLEMS IN 11 SELECTED DIVISIONS OF SOFT-GOODS INDUSTRIES AND 12 SELECTED DIVISIONS OF HARD-GOODS INDUSTRIES

SOFT-GOODS INDUSTRIES

As a result of the outbreak of the Korean war and the consequent defense program, many segments of the textile industry speculated in inventories during the second half of 1950 and early 1951. After OPS was instituted and after consumer scare buying subsided, practically all textile lines faced the problem of digesting these inventory accumulations. Some lines and some concerns have accomplished this objective more successfully than others by restraining purchasing programs and cutting down on production schedules. Details by industry follow:

Cotton and rayon converters

The converting section of the textile industry has just gone through one of the most difficult 9 months in its existence. Because of a functional requirement, the converter anticipates the needs of his customers from 3 to 6 months ahead of actual demand, so his own purchase commitments are placed early.

Many converters were severely restricted by greige goods shortages during World War II and with that experience in mind when the Korean war started, they plunged heavily into the greige goods market. Orders were placed ahead as far as three to four quarters. This forward buying was given added stimulus by rapidly advancing prices on all constructions of grey goods.

OPS put on the brakes in the spring of 1951. Grey goods prices receded almost as quickly as they had advanced. When the so-called bottom was reached, prices were back to pre-Korea and the converters were loaded with high-price purchase commitments. Grey goods mills, factors, and bankers were forced to cooperate with the converters to avert a catastrophe. The mills postponed deliveries, and granted extra time in payment. Factors made merchandise advances and over-advances, and bankers aided in the financing.

Substantial inventory losses have been taken and will be reflected by the December 31, 1951, balance sheets. Some converters are still taking in the high-priced contracts. Forward buying by the converter has ceased. There is plenty of greige goods available in the market and a number of the larger mills have cut back on production.

Cotton knit underwear mills

A boom in orders developed after June 1950. The mills bought raw materials heavily because of the war and because of a reported short cotton crop for 1950. Heavy mill inventories resulted but were relieved by substantial Government buying. Underwear prices have been fairly steady. Announcement for new lines indicate some to be moderately up in price and some moderately down. The competitive situation and consumer demand are the controlling factors. There seems to be no shortage of raw material. This section of the mill industry is expected to show moderate profits for 1951.

Hosiery mills

Hosiery manufacturers received very large orders in the late summer of 1950. This necessitated a sharp step-up of production as the summer months are ordinarily the lowest shipping seasons for the industry. The primary motivating factor for the spurt in business was the widespread supposition that the Government would require enormous quantities of textiles. Consumers started to buy immediate needs as the memory of shortages during World War II lingered in their minds. Wholesalers and retailers, also anticipating shortages, began stockpiling goods.

When shortages did not appear imminent, scare buying faded. In the meantime, the hosiery mills were producing beyond normal consumption and many found themselves heavily stocked in a declining market. At the same time, wholesalers and retailers, conscious of past inventory losses began selling from stockpiles and restricting purchases to fill-in needs.

With few exceptions, the hosiery mills enjoyed very good business during the first quarter of 1951. In the second quarter, sales started to decline and a wave of competitive price reductions developed. The usual slow summer season was experienced and contrary to the expectations of the mills of a pick-up in the fall, hosiery continued to soften rather than to firm up. The last quarter was disappointing. Both unit and dollar volume were below levels normally experienced at that time of the year.

Ladies full-fashioned mills maintained high production schedules up to the last quarter of 1951 in face of declining sales. In December full-fashioned goods were being sold at unprecedented low prices, due to overproduction and dumping of large quantities of goods at distressed prices to ease strained financial positions. Employment in the hosiery mills dropped off sharply in 1951, as in addition to curtailment of production schedules, new automatic innovations were developed in hosiery machines, eliminating certain manual operations.

The men's hosiery mills represents the only segment of the industry to derive any direct benefit from Government work, but volume of contracts awarded has not been of sufficient consequence to have any appreciable influence on the industry, as a whole.

Men's wool clothing, manufacturers

Virtually no dislocation has taken place in this industry. The Korean conflict itself had little effect on the industry as a whole, since only a small percentage of concerns took Government orders. These concerns in most cases were able to handle the extra volume in their own plants because of the lag in civilian orders. A few opened their own contract shops, while others passed the work to outside contractors. Very little expansion was made in plant or equipment.

Two segments of the industry, however, enjoyed substantial rise in volume and moderate increase in profit. The manufacturers of uniforms and manufacturers of caps have always worked with the armed services. Consequently, they were in a position to take more and larger Government contracts. In addition, their contacts with Ship Stores and PX's presented a ready-made expanding market.

Rayon and cotton dress industry

Immediately after the start of the Korean war the dress industry in most cases overbought. The dress-manufacturing business was good during the fall of 1950 and the early spring of 1951. However, this scare buying did not extend to the consumer level, and manufacturers' inventories rapidly built up owing to the lack of expected reorders by retailers and department stores.

The heavy early buying by the cutters drove piece-goods and raw-material prices swiftly upward; but when business dropped off before Easter, 1951, and spot goods became available in all types of fabrics, prices again dropped swiftly. From Easter through August 1951 manufacturers bought very little, usually only for fill-in purposes. Business throughout the dress industry started improving in early fall and was generally good throughout the fall. Cutters are still buying very cautiously, on a spot-delivery basis, against orders.

Shirts, men's, manufacturers

Heavy inventories had an adverse effect on operations in 1951. Substantial forward commitments of piece goods in 1950, which were delivered in 1951, brought about a fairly serious condition from April through August. Through the succeeding months of 1951 improvement was noted in sales. That, combined with curtailment of piece-goods purchases, has brought back seasonably satisfactory financial conditions for the general industry group. Government contracts have not been large, considering the size of our Armed Forces.

Synthetic-fiber fabrics, weavers

In the spring of 1951, because of sluggishness in the movement of inventories at cutting-up and converting levels, many mills granted deferments to their customers. Prices in the secondary-fabric market dropped below pre-Korean levels. In July 1951 the mills curtailed operations to less than 50-percent capacity because of a lack of orders. Except in a few isolated instances, Government buying has had no influence in this field. Generally good earnings during the first half of 1951 should largely offset the losses sustained during the last 6 months of the year. These profits shown for 1951 in general will be moderate at best and will be substantially lower than those of 1950.

Synthetic filaments, producers

Rayon and other synthetic filament producers were in abnormally low inventory position for years until July and August 1951 when the weaving mills curtailed buying. Then inventories increased substantially with the producers who gave out announcements of moderate cut-backs in production. Nevertheless their inventories have continued to increase. In this particular field Government requirements and procurement have no appreciable effect on conditions.

Women's coat and suit industry

When hostilities started, the coat and suit industry expected a return to the World War II days. Cutters were eager to buy and this eagerness was encouraged by the mills, who advised cutters to buy early and heavily in view of expected shortages in 1951. These shortages never actually became real as the woolen and worsted mills produced more than enough to supply the cutters.

Cutters immediately began to place heavy commitments for the fall of 1951 at rising prices. At the end of February business eased although wool top prices kept going up. Then the wool market collapsed. In June 1951 leading mills announced reductions in piece goods prices on all new commitments placed but not yet delivered. This had a definite effect on the cutters, who were holding high-priced goods. They were immediately forced to take inventory losses from which they have not recovered. Those who were holding gabardines were hurt substantially as there was no market for this fabric.

September first maturities could not be met by most cutters and mills were forced to carry them from 30 to 60 days. Business picked up considerably in October and November and the cutters managed to reduce inventories to a great extent although this was not always done at profit. Those holding gabardines were forced to carry 1951 fall merchandise over into 1952. The defense program has had little or no direct effect on the coat and suit industry. Only a few cutters have received substantial Government business and in these cases most of the materials are furnished by the Government.

Woolen and worsted mills

Immediately after Korea, the mills plunged into the market and overbought during the second half of 1950. Wool and tops prices reached new highs because of this demand coupled with large Government buying and stockpiling plans. This movement was checked by OPS late in January. When the Government withdrew from the market in April 1951 the wool market collapsed and has not yet recovered stability. Wool top prices today are about 50 percent below the peak reached in March 1951.

Except for the relatively few mills actively engaged in Government work, business has been at a low level with the worsted mills in recent months. The woolen mills, because of a growing shift from worsted to woolens, have seen a pick-up in demand in the past 2 months. Wool consumption for the year has dropped off. (Figures for the 11 months through November show 23 percent drop.) Mill employment is down seriously. Generally, mill civilian goods inventories are low at this time but few mills on nonmilitary goods will show a profit for 1951.

Work clothing manufacturers

This textile manufacturing segment reflects heavy industrial agricultural and structural activity. The industry supplies the functional and work clothing to workers which in heavy use is subject to frequent replacement. The unfavorable influences have been higher inventory costs, both original purchase and carrying costs; higher labor and incidental costs while ceilings have been imposed on wholesale prices. So far this industry group has maintained moderatly profitable operations due to manufacturing efficiency.

HARD GOODS INDUSTRIES

Manufacturers whose products are fabricated largely of metal have been affected in one of three ways by the rearmament program: (1) some that were operating at practical capacity have continued to do so, (2) some have experienced a recent reduction in volume in consumer goods without a corresponding increase in defense orders, (3) some that were operating at much less than capacity prior to June 30, 1950, have received a tremendous volume of defense orders and have now reached capacity. Two circumstances are responsible. In respect to consumer goods, the pattern is the same as that manifested by the producers of soft goods—a rush to buy immediately after the outbreak of the Korean conflict, the sharp increase in prices, subsequent satisfaction of the demand followed by a sharp falling off in purchasing.

Secondly, the materials required by the Government for rearmament differ materially from the output of many factories in their normal activity. Because of the different techniques and talents required, it would be impossible to assure that every company would be the recipient of defense orders to counterbalance the decline in civilian production that followed the let-down in demand or inability to obtain an adequate supply of scarce metal. The factory which performs a simple soldering operation in assemblying an electronic phonograph from purchased components is not qualified, either in terms of manpower, equipment, or engineering, to produce an airborne radio receiving set that demands the highest skills in its production.

Against this brief background, there follows summaries of the major industries which are the largest consumers of metal, ferrous and nonferrous:

Aircraft industry

The problems in attaining the goals set for the industry by the Government to a considerable degree were beyond the control of the industry itself. On the procurement end, the industry has been plagued with the impossibility of obtaining machine tools rapidly enough in the required quantities. Because strategic manufacturers of aircraft parts were similarly unable to obtain machine tools, the effort to increase production rapidly through an extension of subcontracting was similarly handicapped. And at the other end of the funnel, the services showed a reluctance to freeze designs so that production lines could operate without interruption. The design question is always one of paramount importance whenever the aircraft industry is called upon to expand rapidly. The nature of the industry is such that some further engineering refinement will always be in prospect but there comes a time when the design, as at the present moment, must be put into production. That decision is beyond the control of the airframe factory for they must abide by the instructions of the Air Force and the Navy. A sufficient staff of engineers also has been a difficult goal to obtain. The complexity of the modern aircraft has increased to an extent that a considerably larger number of engineers is required than heretofore.

Automobile parts, manufacturers

Those who sell to the automobile and truck manufacturers are faced with declining production because of Government regulations that are expected to result in a curtailment by at least 20 percent of the number of automobiles to be produced in 1952, in comparison with the output in 1951. These manufacturers are largely so specialized there is no other type of production to which many of them can turn.

The demand for replacement automotive parts, however, has increased. Because of high prices of new automobiles, many are continuing to keep their old automobiles in use and the demand for replacement parts is thus increased. Against this strong demand, however, available supplies of copper and aluminum, especially the former which is used in wiring and in radiators, are becoming tighter and production is limited accordingly.

Farm equipment, manufacturers

The postwar demand was high, but had been satisfied by the beginning of the year 1950. Orders were declining and output was off. With the outbreak of hostilities in Korea, farmers became apprehensive about the availability of farm hands, and to circumvent a shortage, immediately placed new orders for farm equipment; 1951, consequently, was an excellent year. The larger manufacturers in the industry having huge plants with a variety of flexible metal-working machinery, have had no difficulty in obtaining war orders. Many of the smaller specialized plants, however, have not found it as easy to obtain defense work. Allocation of scarce materials to this industry has been relatively good so far.

Gas ranges, manufacturers

1949 output was 2,000,119 units; 1950, 3,043,000 units; and 1951, 2,400,000. Because of the decline in output last year, there have been adequate supplies of raw materials. Sales have picked up since November 1951, largely as the result of a strengthened advertising program by most manufacturers. The number of new homes to be built in 1952 and 1953 will have a bearing on the demand in this industry.

Heating equipment, manufacturers

The allocation for steel with which to manufacture pipe for gas transmission lines has not been as much as the industry would like to have. Consequently, the introduction of natural gas to many communities has been delayed. As a result, many new homes have had to install oil or coal furnaces in lieu of gas furnaces. Manufacturers of the latter have suffered and those of the former have benefited. From this point on, as the number of new homes permitted to be constructed declines, the demand for heating equipment will be reduced correspondingly. The manufacturers of heating equipment have not been in a strong position for obtaining Government work because of the limitations of their type of equipment.

Household refrigerators, manufacturers

There has been strong sales resistance since April 1951, following the preceding 9 months of stimulated consumer buying. Demand improved a little last fall, but not enough to absorb the heavy accumulated inventories. In 1949 there had been produced 3,704,000 refrigerators; 1950 output skyrocketed to 5,637,000 units; 1951 had dropped off to 3,740,000. Although the latter figure was almost identical with the production in 1949, earnings were lower because of greater competition, increased costs, and higher taxes. The larger manufacturers who have extensive machine-tool equipment have been successful in obtaining large subcontracts, particularly from the airplane industry, for the fabrication of such parts as wings, elevators, and rudders. The small companies, however, have had a difficult time in obtaining defense contracts.

House trailers, manufacturers

The manufacturers who receive war orders are not always located in high population centers. This induces a migration of workers, who require housing. The house trailer serves as a temporary, if not entirely comfortable abode. Consequently, demand for house trailers increased in 1951; it was a successful year for most manufacturers. However, substantial amounts of aluminum are required by this industry and the supply is short.

Machine tools, manufacturers

Much time was lost by a failure to follow a realistic course. The industry had operated at only 20 percent of capacity in the first 6 months of 1950, and, accordingly, prices were much depressed. Further, the industry originally was given very little help in overcoming its need for rapid expansion of trained personnel by being permitted to pay labor premiums. Despite these problems, output in 1951 represented a 100-percent increase over that for 1950. The industry now enjoys a top priority on material. The extent of the expansion which some manufacturers are called upon to make has imposed a strain upon the working capital position that had been reduced by losses in 1949 and 1948.

Radio and television industry

The fluctuation of this industry was made more severe because of the fact that Korea coincided with the newness of the television receiver. Demand was already high. It was made even more so by Korea, and the entire industry expanded its capacity terrifically because of the high profit possibilities which this combination of circumstances created. 1950 output was 7,500,000 television receivers. Since it was so new an industry, there was no experience to fall back upon in determining whether the demand was at its peak and, consequently, the companies continued to operate at capacity during the first quarter of 1951. In April when demand plummeted the entire industry at the manufacturing, wholesaling, and retailing level was holding tremendous inventories. Price reductions were such that receivers have sold far below the ceiling prices ever since. Business picked up somewhat in the fall but not enough to rectify the situation so that there still is a surplus of sets. Moreover, current selling prices are not firm enough to assure profits. It will probably be another 6 months before the supply of materials dries up to the extent that a reasonable balance between supply and demand is attained.

The availability of defense contracts has not been the answer to this industry. This is partly because of the much higher degree of skill required in the manufacture of some of the electronic equipment which the Government buys; and partly it is due to the fact that in 1950 and early 1951, when some of the manufacturers were experiencing such terrifically high earnings on civilian business, they turned a cold shoulder to Government contracts. Those who were at that time willing to accept Government orders obtained a disproportionately high share. And so, many concerns which were at first indifferent to defense orders found, when they went looking later, that business was not available.

A very substantial amount of the electronic communication equipment which the Government buys is in the high-frequency range, requiring a greater degree of precision and engineering knowledge than is utilized in the production of television and radio sets. There are specialists who make this type of equipment. They have been the beneficiaries of some of the largest orders so that their present unfilled orders are higher than their normal rate of production.

Railroad equipment, manufacturers

Output of railroad equipment had declined in 1949 and early 1950 because of deterioration in earnings by the railway carriers. Substantial orders for rolling stock were placed immediately after Korea in anticipation of a substantial increase in freight traffic. The industry contends it has been unfairly treated in the allocation of steel. The Government allocators respond that the allotments have been more than generous.

Trucks, manufacturers

1951 was closed with high inventories of completed trucks, following an all-time high level of production. The use of strategic materials in the early part of 1951 was not restricted in output of trucks, and therefore, manufacturers making both automobiles and trucks endeavored to offset loss of automobile production by increasing the truck output. Demand for the heavier models slowed down very perceptively in the second half of 1951. With such large investment in finished inventories, truck manufacturers who received war orders had to arrange financing for such war contracts since their own working funds are largely tied up in slow-moving inventory.

Washing machine manufacturers

Production in 1949 was 3,003,00 units; 1950, 4,290,000 units; and 1951, 3,300,000. The industry was caught with a very heavy inventory in June 1951. Much progress has been made since in liquidating that inventory, but at the expense of operating profits. Some of the independent producers especially have had a difficult time, and several will report losses for 1951, the first red year since the end of the war. Conversion to war production is just now getting under way.

Mr. Foulke. These problems are important to individual businesses. But before the days of mobilizing for defense there were other problems of importance to individual businesses, problems of competition, of law gross profit, or heavy inventories and light inventories, of rising prices and falling prices, of excessive sales and too few sales, of turning employees into a team, of collecting receivables during downturns in particular areas or divisions of industry or commerce.

Business management has the job of constantly solving new problems, and the organizations which solve the new problems the earliest and in the most efficient manner make the most progress.

Those organizations, on the other hand, which do not solve their problems drop by the wayside, and their places are taken by new ventures.

So, although in the summaries of problems presented for the record, many problems are stated, they are not stated from the viewpoint that problems are unnatural in business. These problems will be solved by aggressive skilled management, just as business problems have been solved by capable management in the past.

In addition to these industry problems, I would like to emphasize what appear to be three underlying economic problems.

The first of these is the long-run trend of inflation if deficit spending is continued.

The second is the problem of greater redemptions than sales in United States savings bonds. That is probably the result of the increase in rates of interest of all classes of securities and borrowing during the past year and a half.

Senator FLANDERS. Do you not think there is some question in the minds of prospective purchasers as to the future value of the dollar?

Mr. FOULKE. I certainly do.

Senator FLANDERS. Of course, that applies to savings of every sort, so that it should not apply specifically to savings bonds.

Mr. FOULKE. But the big difference, it seems to me, Senator Flanders, is that, during the past year and a half in particular, so many building and loan associations and savings and loan associations—in contrast to the small number of savings banks although there are quite a few large savings banks—particularly those in the South and in the West, have raised interest rates not only to 3 percent but a reasonable number to 3½ percent, and an occasional one to 4 percent. And you get that interest from the day the money is deposited. Of course, with United States savings bonds you get 2.9 percent over 10 years, but the first few years or two the rate is very low, and last year, 1951, the redemptions over purchases was $1,690,000,000.

Senator FLANDERS. Is the remedy for the Government to raise the rate on savings bonds?

Mr. FOULKE. The point I am raising is that it is an area which needs very careful examination.

Senator FLANDERS. That is a very good answer.

Mr. FOULKE. And, if I may say it, the final third point of the problem, which, I believe, is an underlying economic problem, is the relatively greater increase in food prices than in other items of consumer expenditures, whether we take the records from the January 1952 Economic Report of the President or whether it is taken from Charles Wilson's fourth quarterly report of the Office of Defense

Mobilization, or whether it is taken from the tables which were prepared for the Joint Committee of Congress on the Economic Report by the Council of Economic Advisers. Each one of these tables has a different base. One is June 1950; one, January 1950; and one of January 1946. And in all cases the food prices have gone up much faster and more rapidly than all other consumer items.

The CHAIRMAN. I wanted to ask you one question, Mr Foulke. What recommendation you would care to make on the basic problem here as to whether or not the economy can support and maintain over the long run an Armed Force of the size contemplated.

Mr. FOULKE. Well, I feel like Dr. Nourse: that it can be done, but the decision is one as to whether it is practical and expedient. If it is done by deficit spending, that will be more inflation and less and less for the laborer's dollar.

The CHAIRMAN. Thank you. If you have any more charts or any further information, you may place it in the record.

Mr. FOULKE. Thank you, sir; I shall do so.

(The additional information and charts are as follow:)

Deficit spending.—The current budget for the fiscal year beginning July 1, 1952, indicates a deficit of $12 billion to $14 billion without considering requests for additional expenditures for the Atomc Energy Commssion and for the Navy, and without making any allowances for possible tax increases. Wholesale prices reached an all-time high since 1779, last March. Since then wholesale prices have leveled off, but the latest figures show prices about 13 percent above June 1950. Consumer prices moved upward every month last year and are now the highest in our history. To the extent that continued deficits are financed by the commercial banks of the country, purchasing media of the country is expanded, and that means higher prices and less for the laboring man's dollar.

Our economic life will be stronger for a longer period of years if we operate within our budget. Moreover, moral fiber becomes more and more weakened as deficit spending finds its way into inflation. History indicates that every year that deficit spending continues, the more difficult it becomes to break the habit. In that process the savings of individuals are taken away from them without their knowledge.

Redemption of United States savings bonds.—In the calendar year of 1949, sales of United States savings bonds exceeded redemptions by $731 million, and in 1950 by $235 million. In 1951, redemptions exceeded sales by $1,690 million.

Many savings and loan associations and building and loan associations, particularly in the South and West, paid 3 percent interest in 1950; additional associations raised their rates to 3 percent, some to 3½ percent in 1951 and, in an occasional instance, to 4 percent. The upward trend in interest payments in these associations, the steady upward trend in the yield on high-grade bonds from 2.54 percent in January and February 1951 to 3.03 percent in December 1952, and the trend in interest rates on business loans from 2.60 percent in the first quarter of 1951 to 3.27 percent in the fourth quarter of 1951 indicate a need for a study of the rate structure of United States savings bonds. To the extent that sales of United States savings bonds decrease or hold down an increase in bank holdings of Federal securities, we have a means of restricting inflation.

Relatively greater increase in farm and food prices.—I would like to call attention to a chart of consumers' prices on page 61 of the Economic Report of the President. That chart shows the percentage increases in food, apparel, rent, and "all items" from June 1950 to November 1951. With the exception of two brief periods, consumer food prices have consistently shown a greater increase from June 1950 prices as a base.

Comparison of net sales and redemptions of United States savings bonds, 1949–51

[Millions of dollars]

	1949		1950		1951	
	Sales	Redemptions	Sales	Redemptions	Sales	Redemptions
January	$647	$476+$171	$707	$618+$89	$475	$653− $178
February	599	369+ 230	581	418+163	386	528− 142
March	590	440+ 150	524	510+ 14	359	560− 201
April	454	398+ 56	423	413+ 10	310	472− 162
May	433	415+ 18	416	454− 38	296	478− 182
June	485	451+ 34	398	456− 58	290	476− 186
July	511	425+ 86	417	505− 88	311	482− 171
August	449	439+ 10	350	537−187	314	437− 123
September	398	411− 13	310	475−165	273	390− 117
October	388	396− 8	971	496+475	334	410− 76
November	383	415− 32	436	448− 12	316	364− 48
December	495	466+ 29	541	509+ 32	297	401− 104
Total	5,832	5,101+ 731	6,074	5,839+235	3,961	5,651−1,690

Source: Federal Reserve Board.

Bond yields, corporate (high grade)

[Percent per annum]

	1949	1950	1951		1949	1950	1951
January	2.73	2.54	2.64	July	2.66	2.61	2.93
February	2.73	2.54	2.66	August	2.60	2.58	2.86
March	2.71	2.55	2.78	September	2.59	2.62	2.85
April	2.70	2.57	2.88	October	2.59	2.65	2.92
May	2.71	2.57	2.89	November	2.56	2.66	2.98
June	2.72	2.59	2.95	December	2.55	2.66	3.03

Source: U. S. Treasury Department.

Bank interest rates on business loans—Average of rates charged on short-term loans to businesses, by banks, in 19 cities

[Percent per annum]

	1949	1950	1951		1949	1950	1951
First quarter	2.70	2.60	3.02	Third quarter	2.63	2.63	3.06
Second quarter	2.74	2.68	3.07	Fourth quarter	2.65	2.84	3.27

Source: Federal Reserve Board.

I would like also to call attention to the charts on pages 37 and 38 of the Fourth Quarterly Report by the Director of Defense Mobilization dated January 1, 1952. A chart on page 37 shows the percentage increases in these same consumer items but with January 1950 prices as a base. Consumer food prices with the exception of January and February 1950 have consistently had the greatest percentage price rise.

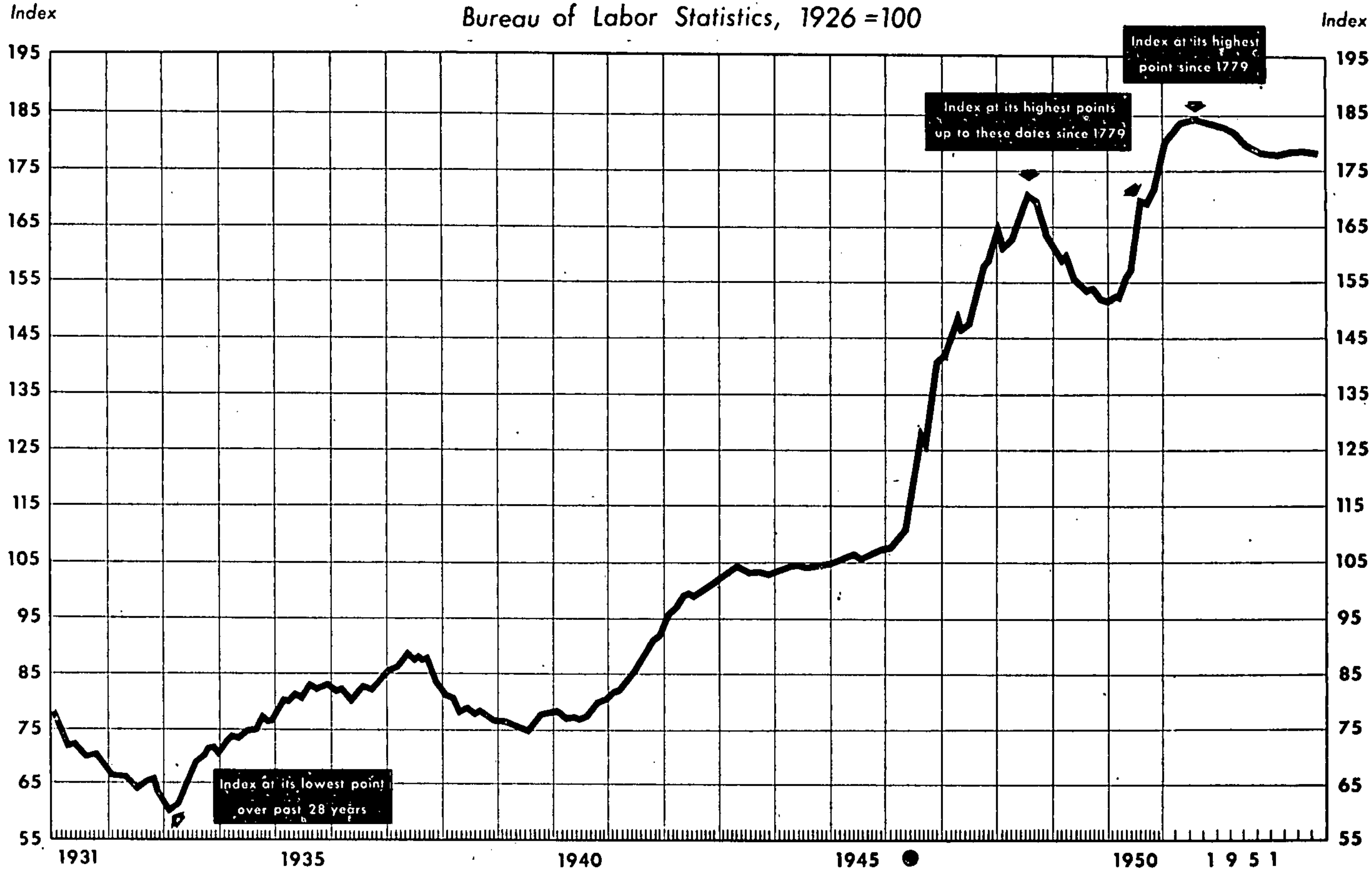
The chart on page 38 of the Fourth Quarterly Report by the Director of Defense Mobilization shows how prices, on items which are exempt from control and which are partially controlled, have risen since February 1951. Items under OPS retail control but subject to parity pass-through show the greatest percentage increase up to October 1951. Items in the Consumer Price Index, such as many agricultural commodities selling below parity, are by law exempt from effective control.

It does seem as though in a period when consumer prices are the highest in our history, and when food prices have shown the greatest percentage increase, that the advantages conferred by law on farmers to collect a tribute from all consumers should be carefully and painstakingly reexamined.

94757—52——17

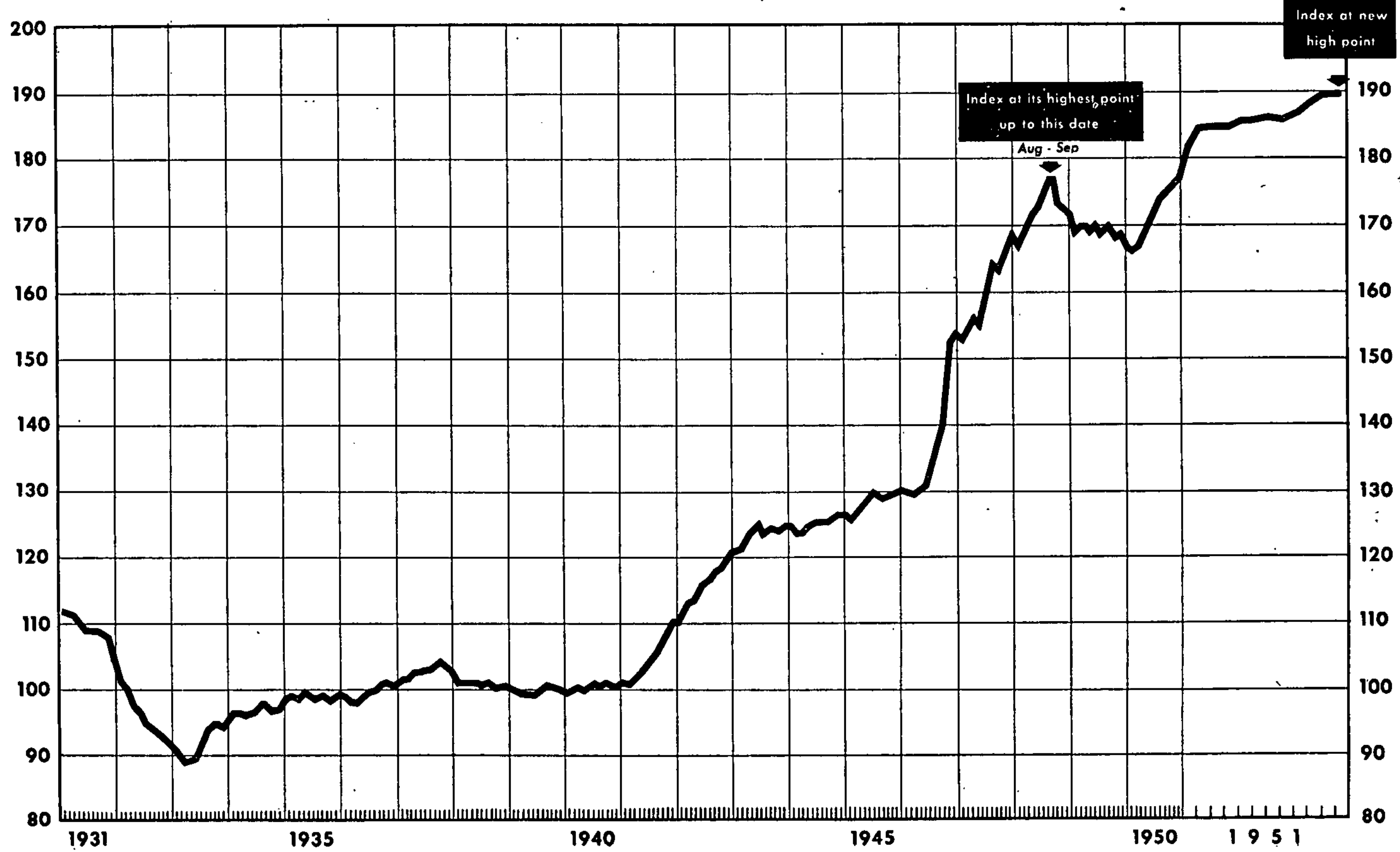
WHOLESALE PRICE INDEX

Bureau of Labor Statistics, 1926 = 100



CONSUMERS' PRICE INDEX

Bureau of Labor Statistics, 1935-39=100



The CHAIRMAN. We will next hear from Mr. Gainsbrugh.

STATEMENT OF MARTIN R. GAINSBRUGH, CHIEF ECONOMIST, NATIONAL INDUSTRIAL CONFERENCE BOARD

Mr. GAINSBRUGH. Mr. Chairman and gentlemen, my comments are directed to point 2 and in part to point 6.

In that connection, I would first like to submit, as I have over the past, I believe, 4 years, the Conference Board Economic Forum discussion of The Business Outlook, 1952. Our session this year was led by Murray Shields; and Malcolm P. McNair; Bradford B. Smith, of the United States Steel; Louis H. Bean, of Washington fame; and numerous others, known to the joint committee and to this panel, participated.

The CHAIRMAN. That will be received.

(The booklet entitled "The Business Outlook, 1952" is on file in the office of the Joint Committee on the Economic Report.)

Mr. GAINSBRUGH. The salient point, perhaps, for the committee's consideration is the summary of the Forum's views on page 45. Their "guesses" were that GNP—gross national product—for 1952 would be of the magnitude of $335 billion to $340 billion (p. 47).

The CHAIRMAN. Is that calendar or fiscal?

Mr. GAINSBRUGH. For the calendar year. That is slightly lower than the estimate or the objective cited by the Council of Economic Advisers in their report, page 113. They anticipate or call for an increase of 5 percent in constant prices, whereas the Forum's estimate is in 1952 dollars.

I think the primary difference between the views of our economic forum and the Council of Economic Advisers was that they did not foresee as rapid a rise in productivity as is anticipated by the Council. I will refer later to a very recent survey by the board of experience with productivity since the start of the Korean war, showing little if any gain.

I would like to offer next in connection with the outlook for 1952 a survey of business expectations of our membership. This conforms closely with Mr. Foulke's findings on what business anticipates for 1952. It is contained in The Conference Board Business Record, January, for 1952, pages 35 ff.

The salient point of that survey is that business plans for expansion of new plant and equipment in the first half of 1952 at the same or higher rate than in 1951.

I might say without violating deadlines too seriously the McGraw-Hill Survey of Plans for Plant and Equipment in 1952 has now become available as of February 1. That survey indicates a 13 percent rise in new plant and equipment in 1952.

The CHAIRMAN. That again is the calendar year?

Mr. GAINSBRUGH. The calendar year. That would be the highest rate of such capital formation, I think, in our national history, if those plans are carried out.

The CHAIRMAN. The booklet to which you referred will be made a part of the record.

(The document entitled, "The Conference Board Business Record," is on file in the office of the Joint Committee on the Economic Report.)

The CHAIRMAN. Two very important points have been made by yourself and Mr. Foulke. Mr. Foulke's statement was that the rate of failures of business last year was the lowest in a considerable period of time. What period was that?

Mr. FOULKE. The statement I made was that the failures last year were well below the average over the past 50 years.

The CHAIRMAN. Well below the average over the last 50 years?

Mr. FOULKE. 12.1 percent below the previous year.

The CHAIRMAN. Mr. Gainsbrugh's statement is that capital formation is now at a peak.

Mr. GAINSBRUGH. That is right.

Business in the opening weeks of 1952 still remains at dead center. The "lull in inflation"—first labeled as temporary or transient, but now almost a year old—still correctly describes the business scene. Declines or soft spots in the civilian sectors continue to offset the steady upward climb of defense and defense-related industries.

Production in the civilian sector actually declined a bit in the fourth quarter, after taking account of seasonal factors. Advances in ordnance, machinery, and other defense-related activities were offset by declines in the civilian sector. Output in lumber, coal, and paperboard ran behind year-ago levels throughout the quarter and into the new year. Factory employment showed little change in aggregate, although the shift to defense employment continued. While farm prices staged a more or less steady recovery in the fourth quarter, industrial prices were extraordinarily stable from October into January. And the latest figures on both new orders and business inventories likewise show no marked changes. Retail inventories were still going down slowly and manufacturing inventories had flattened out. Manufacturers' backlogs were also stable.

On this Weekly Desk Sheet we list 20 business indicators that are most revealing for purposes of determining current position of business in general. For the week ending January 26, two out of every three were lower than they were a year ago. Let me read just a few of the items that are below last year's rate of operations.

Engineering construction down 21 percent.

Automotive production down 39 percent.

Lumber production down 9 percent.

Paper production down 2 percent.

Paperboard production down 17 percent.

Car loadings down 4 percent.

Sales of department stores, reflecting the scare buying of a year ago, down 14 percent.

And the budget deficit continuing upward to reach $8.1 billion in the week of January 18.

I should like to offer this entire sheet for your information.

The CHAIRMAN. It will be made a part of the record.

(The sheet entitled "Weekly Desk Sheet of Current Business Indications," is as follows:)

NATIONAL INDUSTRIAL CONFERENCE BOARD

247 Park Avenue, New York 17, N. Y.

WEEKLY DESK SHEET OF CURRENT BUSINESS INDICATIONS, JANUARY 26, 1952

SPECIAL INFORMATION FOR THE ASSOCIATES—NOT FOR PUBLICATION

Prices of commodities have moved irregularly downward since the beginning of the year. After a sharp recovery in the first few days of January they fell off, then advanced with the announcement of the $85 billion Federal budget, and at midweek were moving down again. During January fats and oils have been among the weakest groups (they led the fall of commodities in 1951). Textile prices have also been shaky, and are off slightly from their year-end levels. Wool prices have weakened since the beginning of the year. (Rayon and silk prices have moved up slightly.)

Grains have been relatively strong, but most wholesale food prices have slipped. On average, January has thus far marked an end of the rapid rise of farm prices that ran from September through December, pushing the farm parity ratio from 103 to 107. Farm income has apparently entered the new year relatively stable.

For consumers' goods, the new year has as yet shown little price change. Wholesale apparel prices are reported to offer better buys. Furniture manufacturers are concentrating on lower price lines, and the weakness of the hides market has raised the possibility of a further small reduction in shoe prices. During December, retail food prices continued up, but the rate of advance was much slower than during the late months of 1951, and the trend in wholesale food prices suggests no further rise at retail in January. It seems probable now that the renewed rapid rise in the consumers' price indext that began last August tapered off in December. The index may have flattened out in January.

The business scoreboard

Industrial production (1935-39=100; seasons adjusted):

December 1951 (estimated)	218
November 1951 [1]	218
December 1950	218

	Week ended—		Prior week	Year ago	Percent change year ago
Bank debits (millions)[2]	Jan. 16	$27,296	[3] $26,517	$27,459	−$0.6
Business loans (millions)[2]	do	$21,441	$21,267	$17,983	+$19.2
Steel production (thousand net tons)	Jan. 21 [4]	2,065	2,051	2,017	+2.4
Engineering construction (thousands)	Jan. 24 [5]	$249,583	$215,638	$316,723	−$21.2
Automotive production [6]	Jan. 19	92,994	[3] 85,630	152,783	−39.1
Electric power output (million kilowatt-hours)	do	7,540	7,666	6,909	+9.1
Bituminous coal output (thousand tons)	do	11,325	[3] 11,760	11,175	+1.3
Petroleum output (thousand barrels)[7]	do	6,101	6,084	5,973	+2.1
Lumber production (thousand board feet)	Jan. 12	201,124	127,105	221,703	−9.3
Paper production rate (percent of capacity)	Jan. 19	99.1	[3] 98.6	101.3	−2.2
Paperboard production (tons)	do	204,021	210,349	244,416	−16.5
Carloadings, total	do	747,662	742,757	779,750	−4.1
Carloadings, miscellaneous	do	371,166	364,226	391,655	−5.2
Sales, department store (1935-39=100)	do	259	[3] 265	301	[8]−14.0
Prices, weekly wholesale (1926=100)	Jan. 22	175.9	176.5	181.4	−3.0
Prices, daily spot (August 1939=100)[9]	Jan. 23 [4]	322.7	323.1	389.5	−17.2
Stock prices (1926=100)[10]	Jan. 24 [4]	195.0	192.1	168.0	+16.1
Defense expenditures (millions)[11]	Jan. 18 [5]	$788	$771	$394	+$100.2
Budget surplus or deficit (millions)	do.[4]	−$8,132	−$7,797	−$822	

[1] Preliminary.
[2] Weekly reporting member banks.
[3] Revised.
[4] Steel production scheduled for week starting date indicated; daily spot commodity and stock prices as of dates indicated; budget surplus or deficit is cumulative from July 1.
[5] Four weeks' average.
[6] Ward's Reports, United States.
[7] Daily average.
[8] Comparison with 1950 is plus 12.6 percent for the current week, plus 13.7 percent for the preceding week.
[9] BLS.
[10] Standard & Poor's.
[11] Federal budget expenditures for military activities of the Defense Department, Atomic Energy Commission, Mutual Defense Assistance, Maritime Activities, Coast Guard, Defense Production.

For monthly data, see the Conference Board Business Record (Selected Business Indicators); for annual data, since 1929, The Economic Almanac, 1951-52 (pp. 230-231).

Mr. Gainsbrugh. Against this background it is not surprising that personal income went down somewhat in November, and possibly again in December, even as personal taxes rose.

Price trends and profits: Prices paid by consumers have not yet conformed with this general business pattern, with the Consumers' Price Index again moving up slightly in December. Consumer prices rose by 4 percent in 1951, although wholesale prices have been consistently below their early 1951 peak for the past 6 months.

Why have consumer prices continued to be so high in the face of lower raw material costs? Two factors appear to have kept retail prices high. In part, rising wage costs have offset declines in cost of raw materials. Also, once output stopped rising in the civilian sector, as it did early in 1951, higher indirect costs and expenses were no longer being spread over a greater number of units—or even the same number in some industries—as they were in the first 9 months after Korea.

The CHAIRMAN. Did you say that output in the civilian sector stopped rising early in 1951 or 1952?

Mr. GAINSBRUGH. I meant 1951.

As a result, the cost basis of the current retail—as well as semi-finished and finished wholesale—price level now appears to be fairly well established. It seems unlikely that there can again be a further significant decline in the level of prices at the expense of business earnings, as in the last half of 1951.

I want to talk next about the profit position of industry.

Aggregate operating profits of manufacturing corporations have shown a sharp decline since the first quarter of 1951, even on a pretax basis. Despite the rise in the price level since Korea, unit profit margins (before taxes) of manufacturing corporations are no longer much above levels prevailing just before Korea.

If you divide the profits by physical output you will find that profits per unit output are shrinking steadily.

On average, profit margins before taxes are now at about the same level as in the second quarter of 1950; in some industries—textiles, apparel, automobiles—they are below anything experienced in 1950.

I append a table showing their relative positions at the end of my statement.

After taxes the decline in earnings and margins in the manufacturing sector is much more pronounced, particularly in that part of the manufacturing sector tied closely to consumer markets. Retailers' profits have also been hard hit by rising costs and subsiding physical volume.

This leads me to two general conclusions relative to point 6 of your outline.

Profits figures for recent months make the inescapable point that manufacturers' selling prices are now uncomfortably close to cost of production. Two conclusions are therefore pertinent:

(1) Profits after taxes are now at levels that make it almost imperative that any further cost rises, particularly wage increases, be reflected in prices.

(2) Whether or not taxes are now being passed into prices, a further hike in business taxes now would compel many sectors of industry to seek higher prices. Price ceilings may restrain the more profitable areas—but prices are below ceiling in most of the non-defense sectors.

Factors behind high savings: There is no indication as yet that the unanticipated upsurge in savings has lost its imeptus. Ever since the second quarter of 1950 personal expenditures have apparently advanced sluggishly and reluctantly with rises in living costs. Strong price resistance and a tendency to trade down to lower price lines has featured consumer markets for about a year, and was particularly conspicuous at Christmas.

The lull in buying has not stemmed from lack of mass purchasing power. The mammoth saving rate the department of Commerce has reported for the last three quarters suggests that consumers have elected to save rather than been compelled to contract their purchases for lack of income. I cite the Economic Report, page 20, by way of support.

For most of 1951 the picture of the consumer as an unhappy and conservative spender has run side by side with a contradictory picture of him as a well-fixed saver. When the rate of personal savings first rose to 9 percent of income in the second quarter of 1951, that was assumed to be a reaction to overbuying in the first quarter. By late summer or early fall, consumers, it was felt, would again prefer goods to savings. The consumer would soon have his fill of stuffing mattresses and defying economists and would then return tractably to the market place to send retail trade (and civilian production) back to boom levels. Even now the Council of Economic Advisers, among others, stresses the fact that a return to a "normal," 5 percent savings rate is a major inflationary threat ahead. President Truman in his Economic Report referred to the extraordinarily high level of personal savings as a—

> precarious situation and any day some combination of events could cause consumers to reverse the prudent attitude of recent months. It is essential that we maintain and perfect the policies which will effectively curb such an inflationary outburst.

He did not specify the program to be followed to assure continued high savings.

There is no generally accepted explanation as yet for this high rate. We have progressed, in my mind, by shifting the area in which the explanation is being sought from consumer overbuying to the study of the structure and composition of such savings. Is this savings compulsory, reflecting the drain on consumer income of repayment of debt? How much of the savings derived as a "residual" by the Department tof Commerce is actually available to consumers in liquid form? What is the distribution of savings by income and debt groups? Who holds the assets? Who holds the debts?

As these studies continue—this is one of my salient conclusions—I believe we will find that consumers are saving more for permanent rather than transient reasons—more because they have grown increasingly aware, Senator Flanders, of the extent to which inflation has cut the value of their past savings rather than through saturation of their current wants. In any event, the saving rate is now being viewed increasingly as relatively stable at its present level, at least for the months ahead. Barring any more international scares, our own Economic Forum, among others, looks for only a slight decline in the percentage saved.

In summary, three factors are beginning to temper the business outlook for the current quarter, and perhaps well into 1952:

(1) The current and prospective pressure of costs and taxes on selling prices, in the light of tight profit margins. Most manufacturers are already earning less after taxes per unit produced than pre-Korea, and in many industries—food, textiles, lumber, motor vehicles—profit margins are less even before taxes.

(2) Because of tight profit margins, manufacturers cannot readily absorb either higher wage costs or higher business taxes. As a result, such increases could mean higher prices in the civilian sector where prices are generally below ceilings, as well as price increases in the defense or defense-related sectors.

(3) The record of the past year indicates that personal consumption has advanced only reluctantly as the cost of living rose. The evidence of the past 9 months, quarter by quarter, strongly suggests that consumers will not radically alter their savings rate in the near future. The trend toward high, if not higher, savings in the first half of 1952 should be strengthened by the influence of cut-backs in civilian durable goods.

Summing it up, therefore, in four sentences:

The emerging picture for the early months of 1952, therefore, is relative stability of total output in the consumer sector. This in turn should bring with it accompanying stability of employment and consumer income. As a result, price pressures from the demand side do not seem imminent. Pressures upon the price structure would be sharply intensified, however, if either wage costs or business taxes are increased.

The CHAIRMAN. The table attached to your paper will be made a part of the record.

(The table entitled "Profits (After Taxes) Per Unit of Output" is as follows:)

Profits (after taxes) per unit of output

Industry:	*Percentage change second quarter 1950–third quarter 1951*
All manufacturing	—34
Food	—33
Tobacco	—29
Textiles and products	—37
Lumber	—31
Furniture	—20
Paper	—5
Printing and publishing	+53
Chemicals	—43
Petroleum and coal	0
Rubber	—9
Leather	+8
Stone, clay and glass	—40
Metals and projects	—37
Machinery	—45
Transportation equipment excluding autos	—63
Motor vehicles and parts	—62

Example of how profits per unit of output are derived for the food industry:

	Second quarter 1950	Third quarter 1951
1. Profits after taxes (millions of dollars)	265	204
2. Profits after taxes (second quarter 1950=100)	100	77
3. Production (1935-39=100)	161	185
4. Production (second quarter 1950=100)	100	115
Profits per unit of output (line 2÷line 4)	100	67

Percentage change from second quarter 1950 to third quarter 1951, —33 percent.

Sources: Securities and Exchange Commission; Federal Trade Commission; Federal Reserve Board; the Conference Board.

Senator FLANDERS. I hope we get an opportunity, Mr. Chairman, to raise questions on the way in which, how, and whether corporation income taxes are necessarily reflected in prices.

Mr. GAINSBRUGH. I would like to speak to that. We have given some consideration to that question.

The CHAIRMAN. I think that we should first finish with our panelists.

Dr. Ware, we will call upon you now.

STATEMENT OF CAROLINE F. WARE, PROFESSOR, HOWARD UNIVERSITY, SCHOOL OF SOCIAL WORK, WASHINGTON, D. C.

Miss WARE. Mr. Chairman and gentlemen, I would like to discuss an aspect of the mobilization program that seems to be important and neglected. It is one that falls within the scope of this committee and on which this committee is especially well situated to act. I wish to focus on the way in which resources are being distributed and used within the civilian segment of the economy, not as between the civilian and the military, and on the way that the defense burden is falling on particular groups in the population, rather than on the consuming public as a whole.

It seems obvious that the civilian economy, as a whole, can stand the burden of defense now placed upon it and likely to be placed by projected programs, whether of the quick build-up or long-pull type. The position of the average American consumer, in real terms, is as good as it has ever been, except perhaps for the wartime peak when consumer incomes were swollen by considerable overtime work. The expansion of productive capacity during the past 2 years should sustain the civilian economy at an adequate level even though the defense program makes heavier inroads into supplies. I am assuming, of course, the maintenance of credit controls to damp down total purchasing power, the maintenance of price and rent controls to assure that though the cost of living may creep upward it will not leap, and the maintenance of production and allocation controls. These several controls should, in my opinion, be improved; but at least I assume that they will be maintained.

My concern is that beneath these averages there may be serious inequities, there may be unrecognized maladjustments, and there may be a failure to make essential investments in training, health, and basic facilities.

The mobilization program has already pinched many groups in the population whose incomes have not kept pace with rising prices. According to estimates of the Bureau of Labor Statistics, nearly 45 percent of the Nation's wage earners have not experienced an increase in income as great as the increase in the cost of living since Korea. These include workers in industry, agriculture, Government, domestic service, and elsewhere. Their loss in real income in the year after Korea was estimated as having averaged around $150 per capita. For persons receiving fixed incomes from various sources, each small increase in the cost of living means a cut in real income.

Some of the more vulnerable groups are those receiving social security benefits—benefits that were increased on the basis of pre-Korea conditions and were already out of date when they went into effect in August 1950; workers receiving the 75-cent minimum wage, which was less in real terms when it was enacted than the 40-cent minimum set by the original act 15 years before, and is certainly a poor defense against present living costs; families receiving public assistance whose grants, though based upon so-called need, are not apt to be calculated in current terms—in the District of Columbia, for instance, need for public assistance is now figured in April 1950 prices, with actual grants 10 percent below the budget thus figured because of insufficient funds, while average assistance grants are even lower in nearly two-thirds of the States; other types of low-income families living at or below the margin, as the studies of this committee's Subcommittee on Low Income Problems have revealed, including the migratory workers described in the recent report of the President's Commission on Migratory Labor whose jobs measure up to none of the generally accepted labor standards of efficiency, productivity, or responsibility and who are outside the whole field of protective legislation.

An adequate evaluation of the mobilization program, in short-run and, especially, in long-run terms, should, it seems to me, include a study of the effects of the program on these segments of the population and an evaluation of the consequences for national strength.

The mobilization program appears to be worsening an already serious situation with respect to the supply and training of certain types of essential workers. The shortage of teachers and the failure of the profession to attract new recruits is well recognized, but it is only one among many examples of the potentially serious maladjustments resulting from the successive impact on the labor force of war, postwar inflation, and now the mobilization program. Public health positions of all sorts in community after community are unfilled. The need to expand medical education is apparent from the fact that though medical schools are filled to overflowing, the ratio of doctors to the population remains below that of 1910. At a recent meeting devoted to the impact of the mobilization program on higher education, spokesmen from all fields warned that we are in danger of falling behind in basic scientific research, without which our applied science must soon become sterile.

Attention should be given to determining what efforts are required to make sure that enough people enter and are trained for these and other essential fields.

The mobilization program, moreover, will fall short of full effectiveness if it leaves potentially valuable labor resources untapped. An estimated 3 million persons over 65 years of age are a burden on the economy when they could be workers, making an economic contribution and enjoying the status of productive members of society. It will require a positive approach to the use of older workers to overcome the barriers of employer attitudes and retirement systems, often dating from the days of mass unemployment. The part-time employment of women with home responsibilities is another enormous resource, but work planning and community services will be needed to make it available.

Another aspect that needs systematic consideration is the allocation of materials for the provision of basic community facilities. The general idea at present is that such facilities should be postponed as far as possible since those which involve construction compete for materials needed in defense. But just what is the necessary and wise course, especially since we have passed through the first phase of defense plant construction?

Take the problem of school construction, for example, not only in defense communities but in other areas as well. I think of a school in one of the older sections of Baltimore which is still conducted in three World War I temporary buildings, one of which does not even have toilet facilities, where, understandably, truancy runs as high as 20 percent, or of the 80-year-old firetraps used here in the District. I think, too, of the classes at the school in my rapidly growing Fairfax County community that are held in the school bus during the time that their usual meeting place, the cafeteria, is in use. The problem of steel allocations for school construction became so serious last fall that a special congressional subcommittee held hearings in response to public demand in order to look into the actions of the Defense Production Administration. One-half of the Members of Congress appeared before that committee or filed statements indicating that the school situation was acute in their areas. As a result of this hearing, some 15,000 additional tons of steel were included in the allotment for schools in the first quarter of 1952. But this brought the total allocation to only two-thirds of that needed to provide space for the additional children who will be entering school next fall, without doing anything to relieve present congestion and part-time sessions, or to replace dangerous firetraps.

With respect to housing and all types of community facilities—hospitals, sewers, highways, et cetera, as well as schools—the President's budget message indicates that some aid and encouragement is to be given to defense-affected areas, but that such construction is to be sharply curtailed or eliminated elsewhere. While the defense areas—approximately 140 have been so designated—are in obvious need, thought should also be given to the implications for other communities which find it virtually impossible to carry out plans for meeting their community needs because they cannot get priorities on materials. For though they may not feel the direct impact of defense production or military installations, they must meet the impact of the war and postwar "baby crop" which is starting to hit the schools and, like a tidal wave, will overflow all facilities. Few if any communities will be unaffected by what has been aptly termed "the crowded generation"; all share responsibility for equipping this generation for whatever tasks, civilian and military, and whatever strains the future may place upon them.

The CHAIRMAN. It may be appropriate for me to interrupt you at that point to remark that an Associated Press compilation of the bond elections which were held in municipal communities throughout the United States on November 6, last, shows that bond issues amounting to about $1,200,000,000 were presented to the voting public for decision.

After the election the Associated Press reported, as I recall, that almost 90 percent of these bond issues were approved by the electorate in the various communities.

As I recall, most of these bond issues were either for schools or hospitals, the greater proportion for schools.

Miss Ware. They do indicate the feeling of many, many communities that they must meet their basic needs for community facilities, if they can get the material.

The Chairman. I was reminded of it by your reference to the baby crop. Schools and hospitals, apparently, were designed to catch up with that.

Miss Ware. I do not know what the answer is to the problems I have raised in these and other aspects of the civilian economy. It is certainly not simply "social programs as usual" and more than it is "business as usual." But it seems to me that these are the kinds of problems that call for direct and systematic consideration.

More is required than merely to consider each aspect on its separate merit—social-security benefits, school construction, medical education, teachers' salaries, et cetera, or to wait until public clamor produces a congressional hearing. The civilian economy should be approached in terms of "tooling up," just as the defense program has been making sure that the investment in training, in services, in health and in the basic economic and social conditions for an effective population represent a sound use of resources to meet the long pull. It is only as the whole set of interrelationships within the civilian economy are considered that an adequate framework for considering individual policies can be developed. And so far as I have been able to determine, nobody is giving the civilian economy this kind of systematic study. The Joint Economic Committee is in a position to do so.

I, therefore, suggest that this committee undertake to study the impact of the mobilization program on the civilian economy from the point of view of the possible maladjustments and inequities that the programs may be producing or enhancing and of the need to invest current resources in the development of future strength. The Subcommittee on the Low Income Problem might broaden its scope and adjust its focus to carry out this assignment, or another subcommittee might be created. By furnishing a frame work for policy decisions through such study, the Joint Economic Committee would be carrying out its function and would render a much-needed service to the Nation at this time.

The Chairman. Thank you, Dr. Ware.

We will now hear from Mr. Shishkin.

STATEMENT OF BORIS SHISHKIN, AMERICAN FEDERATION OF LABOR

Mr. Shishkin. Mr. Chairman and gentlemen, I appreciate the opportunity to come to this committee.

I would like to submit several general observations with regard to the problem posed.

One has to do with our fundamental problem of today and the most immediate problem with which we are faced in terms of economic policy, that is, the problem of division of our resources between the military and the civilian economies.

There has been a good deal of discussion in the light of the budget presented, asserting that the maladjustments that arise in the economy are to a very large extent the result of excessive spending for nondefense needs, and that very sharp curtailments can take place.

I would like to point out the salient fact that seems to us outstanding, that the bulk of Federal spending is in the area which is either related to the present defense programs or is related to the past war expenditures or expenditures related to war.

The most conservative estimate of the budget dollar as proposed for the coming year is that between 88 and 89 cents of the Federal Government's budget dollar is related to war or defense spending of one kind to another.

On the side of labor, in relation to the needs for defense I do not think there is much of a dissenting opinion with the fact that this kind of expenditure at this time, in order to assure national security and to provide the necessary means for national defense, are essential and are supported by the vast majority of the workers. It is fair to say that this is so even in the face of the fact that the high tax rates and the incidence of taxation upon the workers have created a burden heavier than the workers have maintained. Even so, labor is behind the basic proposition that we have to provide on a very urgent basis both the increase in military expenditures as well as support our allies in terms of those expenditures which will diminish our own outlay at home and will, in a way, be an economy, and that these expenditures are essential and necessary.

Senator TAFT. You mean the workers have formed a conclusion that you have got to spend 51 billion for arms? Have they formed any such conclusion at all? They have not studied it. They do not know. Does anybody here know? That is the question that I would ask.

Mr. SHISHKIN. I mean simply, Senator Taft, in terms of the program that has been proposed—in terms of the policies that are pursued, and the policies that are necessary to carry it out, I think that there is every evidence in the way in which we are in a position to judge, in a more effective way than anybody else, the response and the sense on the part of the average worker. And certainly on the part of our membership there has been a great deal of question, a great deal of criticism, but there has not been dissent, complaint, or challenge of the basic purposes that this kind of budget represents.

Senator TAFT. That is the question I raised, because after all that is the basis of this whole thing: Is the 51 billion necessary? In whose judgment is it necessary? I am just talking about the military end of it. It runs up to 65 when you add the foreign aid and all of the rest of it.

But does 51 billion for our own forces cover it?

The question arises with the Joint Chiefs of Staff themselves. They said that 15 billion was amply sufficient to secure the security of the United States. Now you say 51 billion cannot be questioned. That is what I take it you are saying. General Bradley testified in March 1950 that in his opinin 13½ billion was substantially enough to assure the security of the United States against Russia—the same Russia, exactly the same Russia—the same number of divisions.

We are further along with the Air Force today.

How can you say that 51 is an assumption? I am only objecting to the theory.

I think in approaching our problem that we cannot accept without qualification that 51 is necessary for the security you are talking about or that the workmen think so. I do not think he knows. I do not think there is any question about that.

Mr. SHISHKIN. Let me say on this point that I do not want to leave the impression that either I or the organization which I represent are looking upon this kind of an outlay unquestioningly or uncritically. Surely, the military decisions are those that on the labor side or in the community as a whole, if there is a question of security in the defense of the United States involved, cannot be questioned, cannot be challenged. Those in military authority in this country are in the position to indicate the military targets and the necessity to provide the policy assumptions within which they operate.

Senator TAFT. I deny that altogether. I do not think that is so.

Senator FLANDERS. I would like to join with you, Senator Taft, in completely denying that assumption.

Mr. SHISHKIN. If you would bear with me for a minute I would like to point out, however, there is a major problem presented within those assumptions.

Senator TAFT. Yes; I do not want to interrupt your main point.

Mr. SHISHKIN. Which has to do actually with technological aspects of our conduct of national policy with which the military are confronted as well as the civilian economy, and that is the rapid and increasing technological change. If Secretary Finletter or those working with him discover that very wide-reaching changes are needed in production of aircraft as a part of that particular segment of the defense program these changes must be made. The repercussions in the economy can be enermous and will be very substantial in terms of change-overs, changes of models, and the whole reallocation of supply of materials needed for that product. But again I accept the necessity of that kind of an outlay, because I think it serves no useful purpose for the United States to be engaged in the production of obsolete aircraft for defense purposes.

The CHAIRMAN. That brings up one of our fundamental questions as to whether or not the program to expand air power in terms of modern weapons can be safely retarded or pushed ahead.

There was a time when the military and the administration, including the Secretary of War, were adhering very closely to the demand for curtailed military expenditures, and they cut down military expenditures.

Secretary Forrestal, as is well known publicly, had great difficulty in curtailing the recommendations of the various branches of the military service to meet the low sights that had been fixed by the Bureau of the Budget.

And then when Secretary Louis Johnson succeeded him, he made further cuts. And there were those who thought that Secretary Johnson was making extraordinary statements when he said to various business gatherings—I think one was the Industrial Conference Board, Dr. Gainsbrugh—that if Russia struck at 2 a. m., we would be ready to respond at 4 a. m., but after that incident had passed we discovered that Russia was manufacturing atomic bombs and through the utilization of German technological skill was building modern planes, of course, the whole point of view changed.

Last year the Congress wrote into the military appropriation bill and unbudgeted item of about a billion dollars for the purpose of expediting the production of a modern air force, both on the part of the United States Air Force and the Navy, all of which changed the outlook and raised again the question of the judgment which must be made finally by Congress as to how much military spending we shall have.

Mr. SHISHKIN. Mr. Chairman, the point that I wanted to emphasize particularly in that connection is that there is actually more important and a larger area of expenditure which today is very closely related to the problem that you have raised. The question is—for the meeting of the actual targets of the military equipment and supply production, how much in the way of allocation of critical materials in the whole procurement program goes to the military in order to be able to carry out that particular form of programing.

The problem that we have and, I think, the area in which we can provide, on the military side, a considerable degree of economy. I do not know how much, but there is evidence that a good deal can be done. It stems from the fact that actually, on the military side, in the Military Establishment, there is no outside review of the requirements that are stated by the military in order to support the operation of the Military Establishment in terms of procurement, in terms of critical materials, in terms of all of the necessary construction facilities, equipment, and other things necessary for the operation.

I would suggest, and we rather strongly feel that the division of responsibility between the Military Establishment and the Office of Defense Mobilization in which in effect the Office of Defense Mobilization takes the recommendations made by the military, and their decisions, and goes on from there to deal with the civilian aspects of the economy, provides a very serious shortcoming in economic planning. Exploration of this problem may lead us into an area in which a great deal of economy can be achieved.

In respect to that particular problem I would like to recommend for consideration the possibility of establishing within the Military Establishment a civilian board which would be reporting to the President of the United States, which would have the responsibility of reviewing and screening the requirements developed within the Military Establishment for critical materials, and also for supporting activity which, upon review, can be changed, modified.

The CHAIRMAN. I think in actual fact that exists now. The civilian secretariate in the Department of Defense is devoting a great deal of its time to screening the requests of the military or the so-called brass. And repeatedly those requests have been very materially cut.

Mr. SHISHKIN. That is quite true, Senator, but it seems to us that this kind of a screening is different from the kind we really have in mind. The kind of an evidence we have, for example, relates to the construction or the projection of housing units and construction of officers' quarters on a permanent basis on the military side after we have just gone through the war, after we have finished the construction of a lot of construction of this kind and have made expenditures those units called for. Although review does take place, and very searching review, there is a natural tendency on the part of the military to conduct that review within military terms, to place exclusive priority on military requirements and to forget about the needs of the civilian economy for those products.

The only thing that I am really suggesting in effect is that the over-all programing which is necessary and should go on in one central place and which does not go on in one central place now should be remedied, at least, to that extent, so that whenever there is a possibility of actually providing the most economical allocation of critical materials, in the light of the civilian economy, that review would not be responsible to the head of the Military Establishment, but would be responsible to the court of last resort within the Executive branch, which is the President.

A committee of that kind which would have a high degree of responsibility to the community itself, a representative committee of this kind, with competent people drawn from business and from labor, would be able to present a basis of recommendations to the President which then the President would be in a position of taking to Congress, in order to make the kind of adjudication that the Congress in the final analysis should make.

The second area of concern that we have, of course, is one of the most fundamental problems and, that is, the problem of inflation.

I would like to point out very briefly that we are now in the second phase of the inflationary development in our economy.

The first phase which coincided pretty closely to the invasion of the Republic of Korea, being largely the speculative kind of inflation. In other words, I am referring to the speculation and profiteering in raw materials and commodities, which had a secondary response on the consumer side following the invasion of Korea. It resulted in a very sharp rise in prices at the time, largely in response to a kind of expectation which made people want to buy cheap in order to sell dear, and for those who bought for themselves to take advantage of the prices before they did rise.

The secondary stage which we are reaching, or even have not reached yet on the inflationary side, follows a reaction to the kind of a development that has taken place. And we are still in the phase of that reaction.

Some of the figures that Mr. Gainsbrugh cited and some of the indications of the kind of complex which dominates the industrial side of the economy, is the aftermath of the consequences of that development, and the aftermath of the inability of the public policy that we have had so far to deal with that problem effectively.

The second phase is the one that actually stems out of the defense expenditures themselves, and reflects the accretion in the purchasing power and the need to siphon off that purchasing power in order to be able to keep the dollar stable.

I would like to call the attention of the committee to the fact which is inherent in this development, that is, that the bulk of the increase of purchasing power and the maldistribution of it in relation to the rising cost of living is to a major extent the result of the increments of our employed labor force, including the military, rather than that of wage rates as labor costs.

I would like to point out that this is the kind of a factor that calls for measures that go beyond those that have been taken so far, because this is a necessary kind. We have to maintain a certain size of labor force. If we have to increase the military personnel to the extent that we have agreed, this kind of increase in the purchasing power itself which flows into the main stream of the economy will increase. And we simply have to accept that and deal with it effectively, not in terms of any one individual approach or one individual set of measures, but in terms of comprehensive policy, which is both monetary, fiscal, as well as dealing directly with prices.

We are faced with a situation in which we have under the Defense Production Act an operation of several programs that have to do with direct controls.

One of them is the stabilization of wages, the stabilization of wages that has attempted to allow sufficient flexibility for wages to keep up with the increases in the living costs.

I need not go into any detail in the history and development of particular details and particular aspects of this story, but I would like to point out that in the development of wage stabilization policy we are today confronted with a very serious problem of acceptance of wage stabilization on the part of the workers if effective means will not be taken to prevent a sharp rise in prices.

Do we expect that rise in prices? Are the indications such that we will see it as inevitable, as an immediate kind of problem?

Well, I do not think that it is immediate. I do think it is inevitable. In other words, I think that one of the most serious problems of public policy with which we are confronted at the moment is that during the current period and, probably, during the first half of 1952, the economic situation is essentially stable, essentially no sharp changes are to be expected, but if you take into account the point which has been reached in the actual governmental expenditures, the point that has been reached in the differential between the projection of a particular kind of a defense program, the chewing-up stage in which some expenditures rise to a pretty large scale, and the actual production stage after tooling up, we will find that the authorizations previously made and undoubtedly to be made, will result in very heavy inflationary pressures which will show themselves later in the year.

I am calling the attention of the committee to this particular phase because I am very thoroughly aware of the difficulty in the situation which is essentially stable to deal with the future development, but in this kind of a situation it has to be done, because once it hits it is too late to deal with it.

The CHAIRMAN. Your statement that the economy is relatively stable at the present time seems to meet with the approval of the gentlemen sitting around you.

Mr. FOULKE. I would certainly like to raise a question on that point. Every month last year consumer prices went up, and at the end of the year consumer prices were at the highest point they have ever been in our history.

Mr. SHISHKIN. I was coming to that.

Mr. FOULKE. Do you call that stable?

Mr. SHISHKIN. I was coming to that. I have not called it anything.

The CHAIRMAN. Let me finish my question. You did say that the economy was relatively stable, did you not?

Mr. SHISHKIN. That is right.

The CHAIRMAN. I noticed Dr. Gainsbrugh to nod affirmatively. It corresponds with what he said in his statement. Dr. Blaisdell nodded affirmatively. I think Dr. Woodward did.

But this is the thing that Congress has got to pass on. The military program is increasing in its impact upon the economy by reason of increased expenditures.

The expenditures for fiscal 1953 will be greater than the expenditures for fiscal 1952, and therefore, will exert an inflationary effect and will produce the result that you fear unless the inflationary effect is counteracted in some way.

That raises the question, whether that inflationary effect can be counteracted or should be counteracted by a further cutback in military spending.

Mr. SHISHKIN. I think I have indicated pretty plainly our position with regard to the military expenditures and our position is that we have to meet those expenditures.

The CHAIRMAN. You are not passing judgment on what the military expenditures must be?

Mr. SHISHKIN. That is right. There are three points that I would like to make in connection with the statement I made regarding the necessity of dealing with the inflationary pressures.

No. 1, on the wage side, we are very gravely handicapped by the fact that the wage facts as they are generally applied to the economy and generally understood are the wages confined to manufacturing. We are generally dealing with a magnitude which covers only about 16 million workers in manufacturing out of some 45 million workers in total production and trade and services and are taking those figures to apply to the economy as a whole. But even if you take manufacturing wages, the outstanding fact, as far as the attitude of the wage earner and his position, of the employed wage earner now in manufacturing itself is concerned, make the comparison of what has happened to his real earnings—and I am taking real earnings on the gross basis. Making a most generous comparison, as generous as could be made on that, because, actually, what you need to compare in wage rates, not earnings, but even if you take gross earnings, from the peak of gross earnings during the war at a point from which the actual money wages have advanced very substantially, real wages in 1939 dollars have declined by $2.30. And since January 1950, the real gross weekly earnings in manufacturing have declined substantially as well.

So that you will see, in terms of purchasing power with the sharp rise in prices, with the kind of fluctuations that you have seen in the economy—have been very largely up, and to some extent down on the side of profits, even in the most favored situation, in the most favored large segment of the economy, wages have not made progress in terms of purchasing power.

Senator TAFT. You are using the same old argument, starting very high in World War II, when wages were unreasonable, of course.

Mr. SHISHKIN. January 1950.

Senator TAFT. From the period, from 1946, they have gone up—real wages have gone up $6, according to our statistics here. And, of course, as to wages in the war, people were working longer hours. There are all sorts of reasons why they were getting more money.

You see you ran in 1946, $53.97, in 1947, $53.85, in 1948, $54.14, and so on. It has been running around $60. Those are in 1950 dollars, according to our statistics.

I do not think you can fairly start from the middle of World War II.

Mr. SHISHKIN. I made two comparisons. And indicated in both that the workers who are now employed in the defense economy do make the comparison with the military economy of 1945, in the first place. In the second place, they know their earnings have declined in the last two years in terms of the 1939 dollar.

Mr. GAINSBRUGH. Not upon the basis of the data published by the joint committee in its Economic Indicators (see January 1952 issue, pp. 10–11).

Mr. SHISHKIN. I will give you the series in all categories that are available for manufacturing.

Senator TAFT. They are substantially the same.

Mr. SHISHKIN. The Bureau of Labor Statistics is the best measure we have. And no effort can be made by any committee to invent figures that go beyond those in detail.

Senator TAFT. These figures come from the Department of Labor.

Mr. SHISHKIN. The same is true, actually, on the straight-time hourly earnings, exclusive of overtime. I have had a special tabulation made by the Bureau of Labor Statistics on that. And those figures show that the wages in manufacturing, in terms of purchasing power in 1939 dollars, are substantially the same in January 1950 as they are today. That reflects, of course, this 14 percent of increase in the cost-of-living index that has taken place since January 1950. However, the point I want to make very emphatically in that connection is that manufacturing itself has been the most favorable sector of the economy.

Senator TAFT. I agree with that. I believe a lot of other people have a real complaint. I agree to that.

Mr. SHISHKIN. So that one out of three workers who has had this experience that I have just described is more favorably situated than the remaining two workers who are in the service industries, who are in trade, who are in department stores, who are in all kinds of occupations, who have suffered—we do not know exactly how much their set-back is—but have suffered in purchasing power even a greater set-back.

So that by and large, if you look over the record of inflation over the past period of some 12 or 13 years, the record since 1939, you will find that two things have happened:

One, the effect of prices upon the purchasing power of all of those groups, an effect that has been borne most heavily by the earners of fixed incomes, pension recipients, and others in that category. Important to them is the fact actually the prices during the wartime years were held relatively stable for the wartime period itself, and then following 1946 went up very sharply.

So that we have a record of consumer-price index which did go up in the period immediately after the removal of price controls, twice as high as it did during the war when the controls were in effect.

You have had a problem of suppressed inflation. The controls were removed prematurely, adjustments could not be made in the meantime, and you have had that development with some aftermath and recessive effects thereafter.

We have today as against the kind of wage stabilization with which we are dealing a set of price controls enacted in the last session of Congress in which, by and large, in terms of the necessities of life the price levels that are so established that price ceilings are above the effective prices that prevail.

So I think it is fair to say that with all of the language expended by the Office of Price Stabilization in order to square themselves with Senator Capehart and Representative Herlong that actually, in effect, price stabilization is a paper proposition, so far as the consumer is concerned. If anything, there has been a tendency as a result of the operation of the Capehart and Herlong formulas, an up-pricing effect in the economy.

At any rate, we are confronted with the situation in which some wholesale prices in the past 19 months have declined as much as 15 or 16 percent, whereas the consumer-price index during that same period has increased 2½ to 3 percent.

Mr. FOULKE. What percent did you say wholesale prices had declined in the past 19 months?

Mr. SHISHKIN. 16 percent.

Mr. FOULKE. The records show no such figure.

Senator TAFT. It is 4 percent—184 to 177. That is about 4 percent.

Mr. FOULKE. As a matter of fact, wholesale prices reached the highest point we have ever had last March. And even today they are the highest they have ever been in the history of the country for any time prior to January 1951.

Mr. SHISHKIN. I was addressing myself to the discrepancy between wholesale prices of commodities and the consumer prices in relation to the necessities of life.

Mr. FOULKE. But there is no 16 to 17 percent drop in wholesale prices.

Mr. SHISHKIN. In those sectors, there is. I will be glad to submit the figures.

Mr. FOULKE. Maybe you are talking about individual sections of wholesale prices, but the index does not show it.

Mr. SHISHKIN. The consumers purchasing power is not related to the wholesale prices index as a whole. I was making the comparison of commodity prices that actually constitute the major segment of the food segment of the consumer price index.

The CHAIRMAN. The chart in the Economic Indicators for January 1952, on page 4, indicates that the wholesale price level for all commodities in the early months of 1951 went substantially above 180 and in the middle of the year fell below that level and it still remains below 180.

Mr. FOULKE. And still today they are the highest they have been for any time in our history, except since last January.

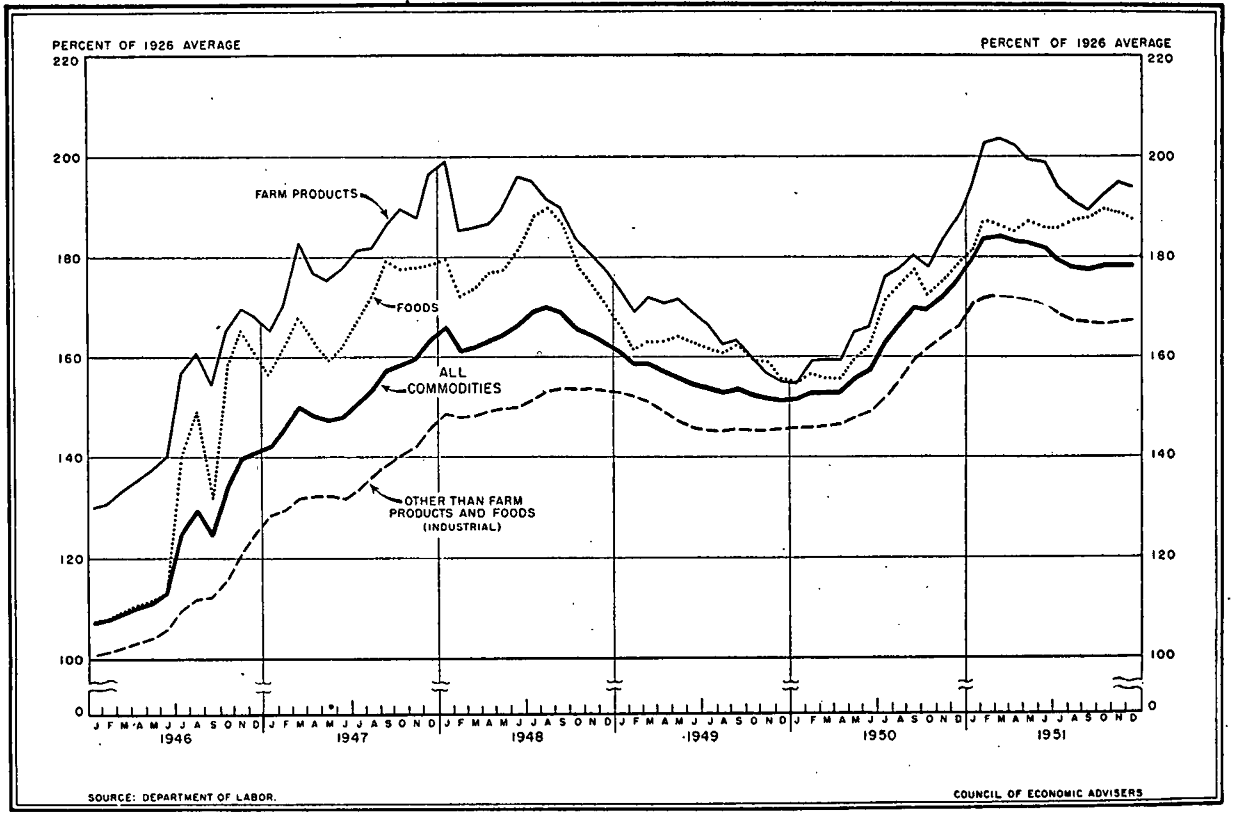
The CHAIRMAN. You are quite right. I was just about to say that the 180 level is much greater, for example, than the peak in 1948, which was about 170, according to this chart.

It might be well to insert this chart and the supporting table in the record at this point.

(The chart, p. 4, of the Economic Indicators, is as follows:)

WHOLESALE PRICES

Aside from some minor fluctuations in farm prices, wholesale prices have been very stable since early November. Industrial prices have been especially noteworthy in this respect.



Wholesale prices

[1926=100]

Period	All commodities	Farm products	Foods	Other than farm products and foods
1942 monthly average	98.8	105.9	99.6	95.5
1946 monthly average	121.1	148.9	130.7	109.5
1947 monthly average	152.1	181.2	168.7	135.2
1948 monthly average	165.1	188.3	179.1	151.0
1949 monthly average	155.0	165.5	161.4	147.3
1950 monthly average	161.5	170.4	166.2	153.2
June	157.3	165.9	162.1	148.7
1951 monthly average	180.5	196.4	186.9	169.4
1950—November	171.7	183.7	175.2	163.7
December	175.3	187.4	179.0	166.7
1951—January	180.1	194.2	182.2	170.3
February	183.6	202.6	187.6	171.8
March	184.0	203.8	186.6	172.4
April	183.6	202.5	185.8	172.3
May	182.9	199.6	187.3	171.6
June	181.7	198.6	186.3	170.5
July	179.4	194.0	186.0	168.6
August	178.0	190.6	187.3	167.2
September	177.6	189.2	188.0	167.0
October	178.1	192.3	189.4	166.7
November	178.3	195.2	188.8	166.9
December [1]	178.3	194.2	187.5	167.4
Week ended:				
1951—Dec. 4	177.1	193.9	187.5	165.5
11	177.1	193.7	188.4	165.6
18	177.0	193.2	188.9	165.6
25	177.3	195.1	189.2	165.5
1952—Jan. 1	177.2	193.7	189.2	165.4
8	177.2	193.9	188.8	165.3

[1] Estimates based on change in weekly data.

Source: Department of Labor.

Mr. SHISHKIN. May I submit a table pointing up the figures that I have mentioned?

The CHAIRMAN. Yes; of course.

(The information to be furnished is as follows:)

1. Index of spot primary market prices for 28 commodities (August 1939=100):

Mar. 26, 1951	379.0
Jan. 25, 1952	322.7
Percentage decrease	−15

2. Consumers' Price Index (revised) (1935–39=100):

March 1951	184.5
December 1952	189.1
Percentage increase	+2.5

3. Food sector of Consumers' Price Index (revised):

March 1951	226.2
December 1952	232.2
Percentage increase	+2.6

Source: Bureau of Labor Statistics.

Senator TAFT. Also, a comparison between wholesale and retail prices, if you go back to the time of the Korean invasion or even pre-Korea, the increase in wholesale prices today is 15 percent over June 1950 and the increase in cost of living is only 10 percent. So really the increase in the cost of living has not yet caught up to the wholesale increase in wholesale prices. It is the wholesale prices that have gone up, that produced that increase in the cost of living.

Mr. SHISHKIN. What has been taking place, of course, is that the increase in the consumer's prices, since January 1951, because some of those increases, as you know, had taken place before the actual invasion of Korea——

Senator TAFT. My only point is that they have not even caught up with the wholesale price increase yet.

Mr. SHISHKIN. One of my points was that adjustments in the consumer price lag behind the adjustments in the commodity prices. There has been a lag on that side, and certainly it has been even a greater lag on the side of wages.

The CHAIRMAN. The Chair will have to interrupt at this point.

I would like very much, of course, to have the questions that the members of the committee would like to ask. I would like to have the interplay among the members of the panel, too.

Would it be agreeable for you to come back at 2:30? If so, then, the committee will stand in recess until 2:30 o'clock.

(Whereupon, at 1 p. m., the committee recessed to reconvene at 2:30 p. m.)

AFTERNOON SESSION

The CHAIRMAN. The committee will now come to order.

Mr. Shishkin, you had, I think, completed your 5-minute opening statement.

Mr. SHISHKIN. I had not quite finished that paragraph, Senator, but I will be glad to defer to the wishes of the committee, and end the discussion.

The CHAIRMAN. It may be that some of the members of the panel want to take up some of the statements that were made by their colleagues. I think that the members of the committee would enjoy listening to your discussion among yourselves.

Mr. Woodward, would you care to kick the ball off? You have been usually pretty expert in that.

Mr. WOODWARD. There seemed to be a very big question that was being talked about a little bit during the intermission that I should think might be worth pursuing, and that is the nature of the second half of this year. We were around the edges of it this morning. On the use of the figures, the projection of the economic budget and fiscal budget figures, one gets an appearance of great tightness in the economy during the latter half of the year. Even with the decline in private investment that would be expected to come about with the shortage of materials, would be more than offset by the budgetary deficit, and there would be more spending power out after goods than there would be goods available, and this would be an inflationary situation.

As I say, a projection of the figures, I think most of us would agree, shows that as the likelihood. But the bothersome question is, How real is that appearance of tightness? I should say that would be one of the significant questions in which we would all be interested. How real is it?

It depends on an appearance of about $16 billion as an annual rate of Government deficit in the fourth quarter of the calendar year 1952. That can be washed away or brought down by a little increase in receipts, by a little less expenditure, if it should happen that way, than is contemplated.

Senator TAFT. The deficit in the last half of the year, though, is at a very much greater rate than for the first half of the year.

Mr. WOODWARD. Oh, yes, indeed. It would be the latter half of the year where the deficit is contemplated.

Senator TAFT. At least $12 billion in 6 months.

Mr. WOODWARD. That is right. But the question is, How real is that appearance of a very tight economy in that period?

The CHAIRMAN. How real do you think it is?

Mr. WOODWARD. I am not clear that it is very real, because I think just a little higher receipts than calculated would not be unlikely.

Senator TAFT. I do not want to cast any doubt on the Treasury estimates, but they were so much lower last year when they were trying to prove that they needed more taxes, and they are so much higher now than they were last year in the same tax bill that we passed. I have just a little doubt as to whether they have not tended to be on the liberal side this time in order to make the deficit appear as small as possible.

The joint committee estimated the receipts from this bill of about $3 billion higher than theTreasury, and they were right now, according to the Treasury figures, or more than right. We never did estimate $71 billion when we considered the bills in the Finance Committee last year. You cannot be sure that you get the $70 billion, particularly if corporation profits are cut, as they will be over their estimate. Then they may be estimated a bigger rate of profit that the Government is going to get under controls and the excess-profits tax.

Mr. WOODWARD. If that were true, then, we would have, other things being equal, a much more inflationary situation during the latter half of this year.

Senator TAFT. That is what I am raising. You say it may well be better. I say it may well be worse. That is all that I am getting at.

Mr. WOODWARD. But this is the critical question, or one of the critical questions.

The CHAIRMAN. What made you say, Mr. Woodward, that the receipts might well be better?

Mr. WOODWARD. On the thesis that the Treasury has seemed to me to be conservative in the past, and I suspect that they may perhaps inherently be that way, and also on the very highly prosperous condition that we are having, we could again have a little more in the way of revenue.

Senator TAFT. I think that the spending is the thing. I admit that they will not spend so much. I think that that is entirely possible. They never have, although sooner or later I suppose we will catch up on that spending. When it will be, I do not know. It may be 1953.

Mr. GAINSBRUGH. May I offer a statistic in that connection? The Federal Government expenditures for fiscal 1953 are shown by the Bureau of the Budget to be 29 percent of the national income. On that basis, the national income they have estimated for fiscal 1953 is $295 billion, and that is roughly 5 percent higher than the national income currently.

So there is indication on the basis of these derived figures from the budget that considerable allowance has been made for expansion in the national income.

The CHAIRMAN. What has the National Industrial Conference Board estimated to be the coming national income?

Mr. GAINSBRUGH. Our forum's view that I expressed this morning was for a 2 to 4 percent increase in the gross national product. I should say our estimates were a little bit lower, but quite close.

The CHAIRMAN. Quite close to the figures of the Bureau of the Budget?

Mr. GAINSBRUGH. Quite close to the Budget Bureau's projection here.

But the point that I was trying to make is that there is allowance in the budget estimates for a higher level of national income for fiscal 1953 of about 5 percent.

Mr. WOODWARD. That is right.

Senator TAFT. Five percent over what? Over last year?

Mr. GAINSBRUGH. Over the current rate of national income, or, to put it in your terminology, the last quarter of 1951, when national income reached an annual rate of $282 billion.

Senator TAFT. Because the total was $276 billion for 1951 as a whole. Excuse me, Mr. Chairman.

The CHAIRMAN. I was about to say that a few years ago, indeed, after the close of the shooting in World War II, with the great peak of national debt, which was greater than the national income, and had been since about the second year of the war, it seemed to me that the country confronted a very great danger that the income, or the gross national product, would not again for some time in the future become as great in a single year as the national debt. But the truth of the matter is now that, according to your figures and according to the Treasury figures, the national income is now greater than the current national debt once more.

Mr. GAINSBRUGH. That is right.

Mr. BLAISDELL. That is right.

The CHAIRMAN. In other words, the national income is enough in a single year to exceed the total national debt, which, of course, makes it easier to carry the debt.

Senator TAFT. We have reached that result by depreciating the value of the dollar.

Mr. NOURSE. Surely.

Senator BENTON. In part.

Senator TAFT. Well, half of it.

The CHAIRMAN. I know. But one can look at the projection chart showing the value of the dollar over 100 years, and one will readily see that the dollar in our times of greatest prosperity before World War II was much lower than the dollar right after the Civil War.

I am not terribly concerned about this talk of decreasing value of the dollar, except from the point of view of that segment of the community which has a stationary income. There, of course, it is a very bad factor, for the pensioners and for the white-collar workers who cannot boost their salaries. But as productivity increases, the value of the dollar tends to decrease all through the economy over a long period of years.

Is that not generally true?

Mr. BLAISDELL. Yes.

Mr. NOURSE. I would like to raise a question along the line of what Mr. Woodward was just saying. Is there not another factor in the inflationary possibilities in the second half of this calendar year in the increase of costs which are coming into the picture? We have had wage increases which have not been fully reflected in prices, and increases in materials costs which still have to be reckoned with. We are now right in the midst of a very key determination in the case of the steelworkers, to be followed by coal, and in all probability wage settlements will be followed by price increases. Also a freight-rate increase is pending.

Are not those things promising to add cumulatively to the inflationary impact by the second half or by the fourth quarter, or sometime along late in this year?

Mr. GAINSBRUGH. I think that Mr. Woodward is trying to lead us to this point, if I may break in. Don was trying to say that in the first 6 months of fiscal year 1953, we may be faced with the prospect of meeting a deficit of some $10 billion, and over the next fiscal year a deficit of some $15 billion.

The question then comes up, Where is the money coming from to finance that deficit?

There is one school which believes that it will be virtually impossible or extremely difficult to secure acceptance of Government bonds in other than commercial bank quarters. This is the point that I would like to see the other members of the panel develop. There is another school which believes that Government bonds may become increasingly attractive to the noncommercial thrift institutions in the second half of 1952 and beyond as the defense industries are able to liquidate some of their inventories.

Is that the essence of what was being said at luncheon, Mr. Blaisdell? You were making that point, as I think several others.

Mr. BLAISDELL. There is one additional phenomenon there which I think tends to get overlooked in the analysis of the figures. We look on deficits in themselves at the particular time as inflationary, whereas the inflationary pressure comes at the time when the buying takes place in anticipation of the Government expenditures. What we have been having over the past months has been very heavy borrowing on the part of private institutions from the banks in order to take care of the orders which they have been getting from the Government, which in turn will be repaid later from the Government's payment of its debts. This is the time when it appears in the Government account, whereas the economic effect of it has already appeared as a result of the expenditures in buying in anticipation of the results.

My feeling was that the pressure for inflation tends to be dampened down somewhat and come in advance of the time when it shows as a Government deficit.

So I had the feeling that in view of the present indication, as of now, of no great, heavy inflationary pressure reflecting itself in the figures day by day and week by week, as we have seen in the past. Perhaps some of this had already made itself felt, and we had, so to speak, discounted the effects of the future Government deficit in this way.

Mr. WOODWARD. This would be that the impact comes with the obligation, more than the spending.

Mr. BLAISDELL. That is right.

Mr. WOODWARD. And it tends to run ahead of the spending.

Senator TAFT. How can you judge anything about when inflation is coming? Isn't it so largely psychological? When you have $250 billion or $350 billion of loose cash that was just poured in after Korea, for instance, and now it is going the other way, why won't the time come that it will go the other way? I do not see how you can guess when it is going to happen.

Apparently you have not had this buying. Why they are not buying, I do not know. Maybe they bought so much just after Korea, that they have not caught up yet. I assume that that is it, up to date.

Sometime that is going to end, and then you are going to have another rush of buying. When you do, then you face your danger of inflation, when added on top of the Government spending.

Mr. Nourse. I would like to raise a point in that connection, Senator, whether they were not merely digesting the overbuying that they had done before, but they also were in a period of sidewise movement of prices, some declines in some areas.

They saw some considerable pressure to sell television sets and some pressure to sell cars, and so forth. That is characteristically a situation for which consumers wait. They hold back. They are coy to the market. We have been talking about consumer resistance.

On the other hand, if we do get an inflationary impact and get an upturn from any one of the series of causes that we have suggested here, don't you then get a change? They have accumulated savings and have digested some of the overbuying. Then they begin to follow the market up, or even to run after it. You cannot evaluate it or time it exactly, but isn't it a kind of influence which we would be likely to see ahead of us after the period of sidewise movement that we have had for over a year now?

Senator Taft. Everybody agrees that the Government deficit is inflationary. The only question is, when does it take effect. The suggestion is that some of it has already taken effect.

Mr. Blaisdell. That is right.

Senator Taft. It may be that it will take effect when the consumers begin to buy more freely. I do not see just how you can foresee it.

Mr. Foulke. I would say that there are two other mild factors that might affect it somewhat. One of those factors, as we mentioned this morning, is that $1,690,000,000 more United States savings bonds were redeemed last year than were sold. That trend will continue into 1952.

The other fact is the one about which Mr. Gainsbrugh asked the question, whether Government securities might not be a little bit more attractive to noncommercial thrift institutions. Well, one of the new factors that started last year for the first time was the fact that many noncommercial thrift institutions and some of the large commercial and industrial concerns that have funds for investment bought tax-exempt securities.

We have a tax on savings banks now. And tax-exempt securities can give to savings banks a greater return, in some cases, than the return as Government securities. Both of these factors tend to be inflationary by throwing back on the commercial banks the necessity of buying the Government bonds to make the deficit.

Senator Taft. There are not many savings banks that are going to have to pay any taxes this year. They are not paying taxes until they get a reserve of 12½ percent or 12 percent. Few of them have it.

Senator Benton. Have you discussed among you the question of how much more prices might have risen during the past year, because of the Government spending and these various pressures, if we had not had forms of control? If Senator Taft is right, it is just a question of when it hits, and if there is no telling when it is going to hit, we are playing a game of blind man's buff on when it is going to hit. It would seem to me that would be an argument to have authority somewhere for pretty rigorous controls to be used when it seems about to hit, even if the experience of the past year or the experience of the present does not yet indicate the need for much stronger controls.

Mr. SHISHKIN. That was pretty much the point that I was trying to make in my opening statement.

Senator BENTON. I was in the Banking and Currency Committee this morning, and I missed your statement. I apologize, Mr. Shishkin. I will read it with very great interest.

Mr. SHISHKIN. Not at all. I was off schedule, Senator.

I was trying to indicate that the likelihood that the impact would come in the second half of 1952 presents a problem to us of dealing with this situation which is relatively soft, compared with the kind of forces that are at work. But apart from the commercial and institutional handling of savings funds, I would like just to inject this one point. That in addition to any pressures that are necessary to be much firmer than they have been heretofore in arresting the effect of the inflation, such as direct controls, it seems to us that it is quite necessary also to deal realistically with the community response on the part of the individual savers to the situation which we have today.

The rate of savings is extremely high, but at the same time, in relation to the economy as a whole, and taking into account the fact that the bulk of the savers are in the higher-income tax brackets and are not in the mass of the consumers, I wonder whether or not in order to be able to siphon off some of the purchasing power that will be accumulating, we should not make the Defense Savings bond more attractive by bringing the interest rate somewhat higher than it is today, and also making additional provisions really to be in a position of increasing a very considerable rate of investment in this form of savings.

Senator BENTON. I think it may be news to Senator Taft. I passed a note to Senator O'Mahoney that I had to leave for the Banking and Currency Committee, and he wrote on it, "The urgent against the important." I think it is a pretty good comment. But I felt it was urgent for me to be there. Mr. Putnam came before the committee for his confirmation this morning, and he did state in answer to questions, I think, from Senator Capehart, that he felt that to do the job he hopes to do, he needed stronger and more authority and more power for stronger controls.

He also said that he thought that the big problem would be behind us a year from today. I thought I would tell you that because he is going into such an important role in the Government that any comments that any of you have to make on his statement might be particularly helpful for the committee this afternoon.

Mr. NOURSE. I find it hard to believe that it will be behind us a year from now.

Senator TAFT. Why a year from today?

Senator BENTON. He just volunteered that.

Senator TAFT. When Mr. Wilson testified before the committee last year, he spoke of 1953 as the peak, and 1954 was definitely to be a very considerable reduction.

Senator BENTON. Yes; I know that.

Senator TAFT. Now the peak has been postponed, and according to the President's message, and everybody else, the peak of 1954 probably will be greater than in 1953, as far as spending is concerned.

Senator BENTON. I think he was referring to the difficulty of this spending-control mechanism. I think he figures if we learn how to do it this year, and get through a year from now, and have the experience and knowledge to get through this year and hold the prices down, that we will be better off, and he seems to have that hope.

Senator TAFT. He is optimistic if he thinks that we will learn how to do it. I do not think that anybody has ever learned how to do it yet. I do not see how he can hope to do that.

Mr. FOULKE. Senator Benton——

Senator BENTON. I agree with you, Senator Taft.

Mr. FOULKE. Practically all the soft goods items are selling way below their "ceilings," and probably the most cogent reason is the fact that the imposition of the ceilings was anticipated by 1 to 2 months by most managements in business. So, around November and early December, there was no small amount of forced sales at prices above the markets, so that those sales would be on record in case ceilings were imposed.

Beginning in the early part of 1951, soft goods prices in most lines started going down, and today they are materially lower than 1 year ago.

Senator BENTON. Do you think that that is an argument for removing the ceilings? The businessmen want the ceilings removed.

Senator TAFT. His argument, I think, is that if it has never been suggested or agitated for, they never would have gone up and would not have had to go down, and it would have been more stable.

Is that the argument?

Mr. FOULKE. That is true, Senator Taft. And I have my doubts whether ceilings are needed on consumer goods, where the capacity today is so much greater than the needs.

Senator TAFT. Would you have it in some fields?

Mr. FOULKE. In most hard goods lines there is a materially different picture.

Senator TAFT. I am referring to the metallic things that we need in the defense program, and so forth. Would you not have to have ceilings on those?

Mr. FOULKE. Yes, both ceilings and allotments are needed. I do not see how the program can be put through without both ceilings and allotments.

Senator TAFT. Ceilings and allotments in that field?

Mr. FOULKE. Yes, because there are so many commodities that are short, even though we have had tremendous increases in production. Copper, steel, aluminum, columbium, tungsten, molybdenum, are still short.

Senator TAFT. And there is no reason to suppose that if you took the ceiling off steel, the steel companies would not want to increase all wages tomorrow and increase the price of steel.

Mr. FOULKE. There is a great big difference between the hard-goods and the soft-goods industries in the past year. They are in entirely different situations.

Senator BENTON. I think that would be a way out of their dilemma.

Senator TAFT. Yes.

Mr. SHISHKIN. Is it not true, Mr. Foulke, that in some segments of the soft-goods industry, particularly in textiles, there has been for some time the operation of a 2-year cycle. This 2-year cycle has been reversed during the war, as a matter of fact, as far as the incidence of the years have been concerned. It has been pretty much reflected and intensified by the extreme buying at the end of 1950 and early in 1951, so that 1951 in that respect followed the pattern pretty much, but in more intense proportions. The likelihood of that experience therefore is that 1952 would reflect a very strong pick-up in buying in those commodities simply because replacement needs will be there and because the consumer, having gone through a period of psychological scaring in this direction and cries of "wolf" which did not materialize, will now come to a point in which his behavior will be more normal. So that we would be likely, as I indicated before, in 1952 to have a pattern there in which the increase in purchasing power and the greater level of production all the way through will reflect itself in wages and you will have a market in which actually price controls will be very much needed in that area as well.

The CHAIRMAN. Before you came this morning, Mr. Shishkin, while Dr. Nourse was testifying, I made reference to the testimony that was given last Saturday by Mr. Wilson, Director of Defense Mobilization. In response to an inquiry by Congressman Herter, he said that, given the choice between a deficit because of lack of revenue by reason of failure to produce added revenue through taxes, and the production of the military goods which he was seeking to mobilize, he would choose the deficit.

Now, you gentlemen were here, with the exception of Mr. Shishkin, throughout the morning session, and I discovered quite accidentally that you all had luncheon together, and when I walked in, I saw you were all smiling; so I assumed that maybe you have come to some sort of common basis of understanding with respect to the problems that are before us. Dr. Nourse, what about it?

Mr. NOURSE. I doubt if there is as much consensus in the panel as you just indicated.

The CHAIRMAN. Not as much as indicated by the smiles, I see?

Mr. NOURSE. No. That was just good fellowship.

I can only speak for myself, on this.

The CHAIRMAN. Surely.

Mr. NOURSE. It seems to me that Director Wilson was speaking from the point of view of the office which he holds and in which he has the responsibility, as a production man, for producing as much as the military have decided on, and that has been ratified by the Congress, as what, will be needed. From his point of view, of course, it would be much more serious to fall down on his production program than to see some deficit result.

The CHAIRMAN. I think I ought to say that I know that the budget figures which have been set up for the three armed services are considerably lower than the estimates or requests prepared by the respective services.

Mr. NOURSE. Yes. Of course.

The CHAIRMAN. That, I think, has consistently been the case. There is a broad sentiment, a wide sentiment, in the Congress that this budget should probably be cut further.

But asuming that the amount of procurement set forth in the budget and the expenditures for the current support of the military, the Army, the Navy, and the Air Force, is a minimum—I do not agree, you understand, but assuming that—would you think that the economy could support the deficit rather than lose the production, if it were really sound judgment that we should not lose the production?

Mr. NOURSE. Yes. We can support a deficit but the economy would be weakened or made more vulnerable in the process.

Senator BENTON. Let us asume that we have a good control law, too.

The CHAIRMAN. Yes.

Mr. NOURSE. I think I indicated this morning that, with the cash budget showing a somewhat better position than the conventional budget, with the $8 billion and the $14 billion deficit, I could conceive myself, as a Member of the Congress, weighing the best of the information as to military needs, saying that we should accept some deficit for next year but hold it down as low as possible. If through savings we can bring it from $8 billion down to $4 billion, I would not think that was imposing an unduly serious strain on the economy this year.

The CHAIRMAN. The economy could do it this year?

Mr. NOURSE. And that decision has been made by Congress for fiscal 1952. As an economist, I cannot attempt to weigh the necessary burden of the military needs for next year.

The CHAIRMAN. Yes. I am not asking your judgment on that.

Mr. NOURSE. All I can do is to help appraise how much of a strain any given size of deficit would impose on the economy.

But in line with what Mr. Shishkin was saying this morning, we cannot leave that other question to the determination merely of military men.

The CHAIRMAN. Oh, no.

Mr. NOURSE. Nor, I think, can we regard the civilian audit of the Secretary of Defense as adequate, because that responsibility comes right back to the Congress.

The CHAIRMAN. I quite agree with you on that.

Senator BENTON. When you pick $4 billion, are you doing it deliberately, because I think that $8 billion——

Mr. NOURSE. Any such figure is always plus or minus.

Senator BENTON. Yes. But I was wondering if you had given any thought to answer that question specifically, and it was an excellent question that the chairman just asked. If you think that we can carry $4 billion without perhaps the economy cracking from an undue strain, could we carry $8 billion?

Mr. NOURSE. Yes. I think the point of this is that we could carry $8 billion or even carry more than $8 billion this year without an immediate breakdown.

The CHAIRMAN. That was the significant point of your answer.

Mr. NOURSE. Absolutely.

The CHAIRMAN. You said for this year.

Mr. NOURSE. Yes; and perhaps for 2 years.

The CHAIRMAN. That, of course, leads to the next step.

Mr. NOURSE. But we would make a much more difficult situation to cope with in 1954, 1955, and beyond.

The CHAIRMAN. That is right.

Now, I want to know first whether there is any dissent among the members of the panel from that judgment for this year?

Mr. GAINSBRUGH. I would dissent.

The CHAIRMAN. You do not think that the economy could carry it, Mr. Gainsbrugh?

Mr. GAINSBRUGH. I have in mind the total cost of the Government, Senator, rather than just the cost of defense alone.

The CHAIRMAN. But my question was directed toward defense alone.

Mr. GAINSBRUGH. I want to look at it in the aggregate first, and then come back to the defense item as a component of the total.

The CHAIRMAN. All right.

Mr. GAINSBRUGH. We have not yet talked about the full dimensions of Government costs in the fiscal year ahead of us. The program as outlined is $85,400,000,000 for Federal expenditures, coupled with some $21,000,000,000 or $22,000,000,000 of State and local expenditures. That means that we as a people are being asked to carry the burden of some $105,000,000,000 to $110,000,000,000 for the next fiscal year and for a series of fiscal years thereafter.

I was stunned to read in the Council's report, page 97, for example, that not only is this burden contemplated, but that after the defense build-up—after we have completed the defense expansion of raw material and fabricating capacity, the likely burden, just for maintenance of the garrison state will fall between $40,000,000,000 and $50,000,000,000. That excludes all Federal civilian expenditures and excludes consideration of the expansion of the State and local expenditures that will go on under the influence of the baby crop that Dr. Ware spoke of. Putting forms of public spending all together, then, we are asked to set aside to carry in fiscal 1953—this figure needs to be checked more accurately, but I will put it in rough terms—some 35 percent of our national income for public purposes including defense. Over and against that particular aggregate, we are near the ceiling, I am quite inclined to believe, of taxable capacity, or the desire of our people to carry a higher tax load.

$105,000,000,000 to $110,000,000,000 would be a back-breaking tax load, if the bill of public spending is to be met on a pay-as-we-go basis.

We then come down to my point of dissent, that in this program, therefore, we must give increasing consideration to the inflationary aspects on the domestic front of a defense program, not only over the next year, but sustained over a series of years running well into the fifties.

The CHAIRMAN. That is what I was leading up to.

Mr. GAINSBRUGH. And I want to be convinced more fully than I am that the defense expenditures of the size indicated are absolutely required in the light of the inflationary potential involved.

You once took a position as a joint committee that defense would have to be looked at within the aggregate receipts or foreseeable revenues of the Federal Government. I think you took that position unanimously in your report last year.

Senator BENTON. No; not unanimous.

Mr. GAINSBRUGH. Was there any dissent?

The CHAIRMAN. On the whole, I would say that the committee unanimously advocated the pay-as-you-go system, with some qualifications by various members.

Senator BENTON. Yes.

The CHAIRMAN. But I know the statement in the report on which you base that judgment.

Senator BENTON. The difference is that there was difference in the group on the vigor with which taxes should be levied in order to meet the proposed expenditures, in contrast to the viewpoint that we should set up the revenues and operate within the revenues.

The CHAIRMAN. I am trying to get down to the bare bones of this dilemma.

Mr. NOURSE. For the record, I say that I agree wholeheartedly with what Mr. Gainsbrugh has been saying on this question. But that is not, as I understood it, the question that you asked me.

The CHAIRMAN. No; it was not. But it was the next step.

Mr. GAINSBRUGH. I do not think we see the question in its perspective, however, unless we put it in the aggregate of Government spending.

Mr. NOURSE. That is right.

The CHAIRMAN. I think you are right.

Mr. SHISHKIN. But, Mr. Chairman, I think Mr. Gainsbrugh has fallen short on the real perspective of that, because actually if his logic is to be applied to this analysis, the big question is the relative impact upon the cost of the average American or on the people of preventing a war, and the question that is not answered, and I do not think this group is in the realm of prophecy to be able to look forward to the extent of answering it, the real question confronting the Nation is, if we bank, as we must, on winning the peace by all these actions that we are taking, what will be confronting our economy in terms of the VP-day, victory for peace? What pressures can be taken in order to enable the economy to sustain a high rate of output in order to be able to shoulder a diminished burden and at the same time begin the task at full level of employment of liquidating the excessive burden that we have assumed during this mobilization period?

The CHAIRMAN. Of course, it is quite conceivable, and I think this is what Dr. Gainsbrugh has in mind, that any nation could launch on a military program of such proportions that it would necessitate losing the free economy which we all cherish. I do not think there is anybody in this group that will not agree to that.

In the hearings that this committee has held to date, even Mr. DiSalle, the head of the Office of Price Stabilization——

Senator TAFT. He is a conservative.

The CHAIRMAN. Surely. But he spoke of the appointment of a committee to appraise the possibilities of decontrol in certain items. I think maybe that is what Senator Taft has in mind.

But everybody who testifies, testifies in terms of desiring, first, to preserve the free economy.

Now, my question to Dr. Nourse was intended to develop the opinion of the panel, first, as to whether or not the American economy could withstand the budget program that is laid before us for this year, because that is what we first decide upon, and then later, of course, I was going to find out what your opinions happen to be with respect to the period during which it could be sustained.

The answer to that question, then, would point in the direction of the ultimate results from this heavy burden of the economy.

In another way, we have to decide—and I would like to have the advice of the economists on this—whether Congress has to decide whether national security comes first at all costs or whether the preservation of an economy in which everybody will be free to make as much money as he wants, to make as much profit as he can, to get as high wages as he would like, regardless of what happens to the national security, should be of first consideration.

Senator TAFT. Mr. Chairman, may I make my statement?

Maybe I get the same result. I do not know. But as I see it, the problem is this:

In time of war the conduct of the war supersedes other considerations, and while people have said we should have taxed during the Second World War for the whole cost of the war, I think it was impossible. I think we simply face in time of war the fact that we have to take inflation for a period of time as a necessary evil connected with the war. As a result, we had an inflation of 50 percent, or more, maybe 70 or 75 percent.

Now, the question is, How essential is this particular mobilization program as compared to war? What is the essential mobilization program? If it is necessary to preserve the safety of the United States, of course we have got to say, "All right, we will take the inflation." These countries that have been defeated in war have been forced into socialism. We would be forced into socialism if we were defeated in war, even if we regained our freedom finally.

So it seems to me that the question is, What is really necessary in the way of a defense program?

Now, that is not an economic question . I would hope we could find that we could do it within our capacity without inflation. But the problem is, How do you find that out?

Mr. Nourse says that it is Congress' responsibility. I suppose it is. And yet we simply cannot learn the facts with any confidence of judgment as to what is necessary, because it depends on so many things. It depends on how many divisions there are in Russia. Nobody is going to tell you. It depends on how much they know about the Russian atomic bomb. It depends on all sorts of military programs for the third world war and what you can win and what you cannot win, what weapons you have to win with, and so on. Those are all questions which somebody has to determine.

It is almost impossible for Congress to do it. Mr. Shishkin wants to set up a commission. I suggest that we set up a joint commission of military and civilian men to consider the foreign policy of the United States, considering the fact that we ought in any way possible to hold it within our economic capacity all the time, and not run over even for 1 or 2 years.

If you say you might run over 1 or 2 years as you do in war, there is a great danger.

The CHAIRMAN. After all is said and done, that is just delegating, again, the power of Congress. We have to do that.

Senator TAFT. In a way, that is true. But you at least get a report. How is the war going to be fought? What is the third world war going to look like? Where are you going to fight it? Where are you going? What are you going to do and what are you not going to do? It all depends on that, as I see it.

I think that the only principle that we can establish is that unless the program beyond our permanent economic capacity is absolutely essential for the protection and security of the United States, we ought not to engage in it. If we can find some other way to insure it, we ought to do it. That is about all we can say.

I do not know whether $65,000,000,000 for defense is necessary. I suppose if you take the foreign policy, if you adopted Hoover's policy, maybe it would cost you only $45,000,000,000. Would that be safe? I do not know. Mr. Dulles made a speech the other day which was kind of in between. Maybe his would only cost $50,000,000,000, or $55,000,000,000, instead of $65,000,000,000. That is what it depends on, what you finally decide you are going to do with your military forces, and that is a complex question beyond the scope of this committee.

The CHAIRMAN. Senator, I was assuming much of what you said.

Senator TAFT. Yes; I do not think I was different. I stated it from a different angle.

The CHAIRMAN. Let me state the question so that everybody will understand it as I understand it, if I can make myself clear.

I know that nobody around this table has assumed to speak to us as an expert on the military needs of the country, and I know that you all expect that the Armed Services Committee in the first instance and the Appropriations Committee in the second instance, and finally the Congress itself, will determine how many aircraft carriers we are going to allow the Navy, how large a ground army we are going to sustain, how large an Air Force we are going to sustain. We will have to decide that.

So I was trying to determine the narrow economic question. If, as Dr. Nourse said, for 1 year our economy could stand this budgetary deficit, then how long could we stand such a budgetary deficit, if the military demand should remain constant? Dr. Gainsbrugh said that he was astounded that testimony was given here that after the completion of the mass-production plant, which was described by Mr. Wilson and members of the Council of Economic Advisers as being the greatest factor in the present program of expenditure, has been completed, then the expenditures from then on, assuming that we are still in the cold war, will be confined only to purchasing the equipment that is necessary, and they guessed at that as being about $45,000,000,000.

I am in no position to guess now as to whether or not that much military equipment would be needed. But I think it is important for us, in order to have a congressional understanding of the problem, and perhaps a public understanding, to have the judgment and authority of economists as to how long this economy could stand such expenditures.

Senator TAFT. Mr. Chairman, it coud do it indefinitely, just at a cost. It is a cost of so much inflation. England has not abandoned that project. They have been working on it for a long time. They have been taxing 40 percent, and it seems to me that they have destroyed all initiative and progress. It seems to me that they have maintained a certain amount of freedom. That is not completely gone. You cannot put a time limit on how long this is going to take.

The CHAIRMAN. But it means a constant diversion from the civilian economy to the military economy of goods and services that we produce.

Senator TAFT. That is right; a cost we ought not to pay unless we absolutely have to pay it to keep the country from invasion. That is my theory of it.

Mr. FOULKE. I would say it would do one other thing, and that is to tax people without knowing they are being taxed, and the people that can least afford to be taxed, in the form of inflation, which is what it does.

Miss WARE. I would like to say that any cost of avoiding world war III is to be preferred to whatever may be involved in winning world war III. All our calculations about what we can stand should be within that frame of value.

I would like to say one more thing, and that is that in figuring the total burden, merely to state it in terms of a staggering load of $110 billion, or whatever, without saying $110 billion out of the total ability to produce, is only stating part. If you take that $110 billion off your $330 billion and come out with $220 billion, you still have more than the $167 billion total national income in 1929, measured in the same dollars.

Mr. SHISHKIN. Senator, I was wondering whether I could comment very briefly on what Senator Taft said just now. I very strongly agree with you, that I do not think that this panel can be in a position of going beyond an economic analysis of this sort. But he has raised a question which, as I indicated in my statement, is very fundamental to it all. I think that one thing that needs very clear understanding on this—and as you know, I spent 3 years in Europe just recently—is that those men who are making judgments of this kind in terms of defense, General Eisenhower, Mr. Harriman, and the Joint Chiefs, within the framework of it, must be very keenly aware of one problem. This problem has been brought out by documentation which has not really seen light of day in any general way of the kind of pattern, for example, in Germany, under a totalitarian form that has been followed during the war in the mobilization of its economy, which was far looser than we ever imagined or than was the general conception. The strategic bombing survey, for example, that was completed in 1946, has brought that out. But I think it sheds light on one point; what the Germans did during the war was to capture the resources and factories and rely on the captive economic resources in order to conduct their warfare, and that pattern has stuck, and it is accepted by the Russians. So unless that line of defense is preserved, unless action is taken to preserve it, we are shifting the burden of defense upon our own economy in heavier terms than would be if our allies are participating and can be mobilized to stand with us. And I think that that is the rationale that we must accept.

Senator TAFT. I am not questioning what is right and what is not right. I only say that from an economic standpoint, all we can say is that if we can possibly avoid an excessive expenditure that will certainly bring inflation, sooner or later, one way or another, you cannot avoid it. You can do it for 1 year or 2 years. It has an inflationary effect that must take effect. If you want to avoid it, we ought if possible to have a system of defense that will not cost too much. That is all I say.

Now, whether that includes Europe and throws Asia away, whether it includes everything, whether it does not include land troops, and it does not include others, that is a question that I do not purport to pass on.

Mr. SHISHKIN. But my second point was, Senator, which I wanted to make very emphatically——

The CHAIRMAN. May I interrupt there, because I want to make an observation immediately following Senator Taft's.

My own feeling has been that the United States in its military preparedness should not place as much emphasis as it apparently is doing upon traditional and conventional military programs, but should concentrate rather upon the new weapons, the developments of science, and air power. I feel that by so doing we can cut this expense. But that is a tentative opinion, and one which will have to be tested out in the hearings which the proper committees will have to have later on.

Mr. SHISHKIN. Senator, all I wanted to add to that was a second point. That is that I think in the strategy of the country, which is really in response to the issue presented by communism. They are at the source of our discussion, because it is their initiative. The point which must not be overlooked is the fact that if the defenses are properly provided and we escape the war, part of the fundamental strategy of Stalinism, of Kremlin Stalinism, directed against the free world, is a strategy of wrecking our economy. That is why I laid the emphasis so heavily on the need for economic policies that will take cognizance of the fact of what the victory, what I call VP-day, would be, so that to prevent the wrecking of our defenses in economic terms, in terms of Soviet propaganda and Communist infiltration of ideas, which is a powerful weapon, as it has shown itself all around the world, is equally important as a military defense.

The CHAIRMAN. In other words, the cold war is an economic war and should be fought with economic weapons?

Mr. SHISHKIN. That is right.

The CHAIRMAN. How much of an agreement is there with that point of view?

Mr. BLAISDELL. I would like to agree with it, Senator, and agree very heartily with it, and I would like to make this additional point: That so far the expenses which we have borne in this particular operation have not been such as to bear extremely heavily on the American economy, particularly on the standards of living of the American people. Standards have been maintained, and I believe the record will stand up pretty well that our living standards are not only the highest in the world, but they are the highest they have ever been here.

Senator TAFT. May I raise a question, about part of that, because anybody on a fixed income now has 10 percent less than he had a year and a half ago. Is that not so? And that is millions of American people—millions of them. The manufacturing employee has increased about 10 percent, but you have millions of people who are now living at a standard of living 10 percent lower than they were living 18 months ago. That has been the result so far.

Mr. GAINSBRUGH. I would add to that that we have paid the price in a disturbing lack of confidence in our own Government's securities. Mr. Foulke keeps coming back to the unpopularity of Government bonds. We have falling due in the next year another $4 billion of savings bonds and in the year thereafter another $5 billion. There is a growing lack of confidence in the fiscal stability of Government, as a result of the defense program. I think that that needs to be given consideration in plans for the future.

The CHAIRMAN. What would you do about the defense program?

Mr. GAINSBRUGH. We are talking at the moment, as we did at the outset, about who is going to take up the additional $10 billion or $15 billion of Government bonds that will be seeking a market as a result of the deficit spending program upon which we may embark for fiscal 1953. Most of the thrift institutions are not manifesting a high degree of confidence in Government securities. Possibly some people may buy them, but in the main, they will have to be financed by commercial banks, unless something is done to sweeten them up to make banks more attractive to individuals and thrift institutions.

Mr. SHISHKIN. Would you not say that some of the lack of confidence in the choice between the private and public sources of supply has been contributed to by some of the private quarters, Mr. Gainsbrugh?

Mr. GAINSBRUGH. That question is rather devious. I do not quite get its implications.

Senator BENTON. I do not think that it is devious.

May I make a comment, Mr. Chairman?

The CHAIRMAN. Yes, indeeed.

Senator BENTON. I was about to make it when I had this telephone call, and I may have missed something that bears on it.

The reason I would oppose Senator Taft's commission is that there are not any answers to these questions. When you propound a long list of questions of that kind, you give the American people the thought and the feeling that there are answers to these questions. We all desperately want answers to these questions. Everybody in the United States wants them.

When you start and string down a long list like that and try to set up a list of admirals, generals, and civilians, people say, "Why, we are going to find out the answers to these questions." And even if the Kremlin has the answers today and we had access to the Kremlin and could answer every one of those question, 3 months from now the answer might be different; 6 months from now the answer might be wholly different.

I think it gives the American people a wholly false hope.

What we do know is this——

The CHAIRMAN. May I just interpolate there that——

Senator BENTON. I am sorry that Senator Taft left the room, and I am sorry that I did not get this in earlier. I will try to explain it to him.

The CHAIRMAN. As I indicated earlier when the question came up, that is the constitutional function of Congress, to determine what national policy is, foreign or domestic.

Senator BENTON. I could not agree more wholly on that.

The CHAIRMAN. More than that, in the Defense Department and in the agencies set up under the Defense Production Act, there have been mobilized the best brains that could be found, most of which has come from the high ranks of the business community.

Senator BENTON. Also in the universities all over the world, people are trying to answer these questions. All the journalists are trying to answer these questions. Hundreds of thousands of people all over the world are trying to answer these questions.

The CHAIRMAN. And they do it in the manner that we are doing now, by trying to bring the problem in its true proportions out on the table, and then the Congress has got to decide, and the Congress speaks for the people.

Mr. SHISHKIN. Just so that there will not be any misunderstanding, Senator Benton—I want to make this clear: you were not here when I made the proposal—the proposal that I was advocating was not at all for a commission of the kind Senator Taft was proposing.

Senator BENTON. I did not know that you had a proposal. I just knew Senator Taft had a proposal.

Mr. SHISHKIN. He did mention it. But I did propose the setting up of a commission, a civilian commission within the Defense Establishment, which would report independently to the President in order to screen the military requests and military requirements.

Senator BENTON. That is a wholly different idea. And also to educate the American people would be a secondary purpose, in the complexities of the problem, and to educate the admirals and the generals on some of the economic facts of life, without passing judgment on our proposal at all. I just say it is a wholly different proposal. It is not the same as the one I heard Senator Taft make.

The Congress has to rely on all the experts in the Government, on all the experts we all have back in our own States, on the people we all know in the universities, on all the work the British are doing, trying to answer these questions. The French are trying to get answers to these questions. Men with vast experience and ability are spending their entire lives trying to answer these questions, whereas we in the Congress spend a few hours a week, maybe, anyone of us individually, on the complexities involved.

I think that what we do know is this: We know that the combined judgment of the people who study to try to get the answers to such questions is that we are living in a period of grave risk. Whether the risk is a 10-percent risk or a 90-percent risk, we do not know. Our judgment varies from day to day and week to week, depending on our incoming intelligence and our natural temperaments—how optimistic we tend to feel.

But it is a period of grave risk, if we have the responsibility of world leadership thrust down our reluctant throats, we cannot avoid it, and the turn of history may revolve around what we do here in the next couple of years from the standpoint of this program under discussion today.

We should, it seems to me, in line with our great wealth and natural resources, exert every effort to gear this program up to the optimum and go much further than we have gone in demanding more sacrifices from our people in order to bring it up to an optimum, and quit promising guns and butter at the same time, but say we are going to have less butter in order in order to get the guns, or even no butter in order to get the guns. The stakes for which we are playing are tremendous.

I do not think that any group of men has ever had to make decisions that involved any greater stakes than those involved now and involved in this hearing this afternoon, in an effort to get an understanding of the policy.

So if $4 billion makes any difference one way or the other, or $10 billion makes any difference one way or the other, or $20 billion makes any difference one way or the other, our problem is to get it, if we take it out of our butter and if we take it out of our automobiles. Our problem is to get it. That was the basic difference last year on the committee that made for the objection to your point on unanimity. I think that there are other members of the committee besides myself who feel strongly that we have to gear the program up, not to the maximum that we would be gearing it up to if we were in a hot war, because we do not think that the risk is 100 percent. It is something under 100 percent. So we are willing to make some compromises. But we have to gear it up. And the problem is, How do you provide the funds and allocate the materials in order to get the job done?

I am sorry to make such a long statement. But Senator Taft set me off. I would not have made the statement if I had not heard his proposal.

The CHAIRMAN. This morning, in a question or a comment, you referred to the fact that the House has already passed a bill increasing the compensation of the military by 10 percent. That bill is now before the Senate Committee on Armed Services.

Senator BENTON. And Mrs. Rosenberg says that we are going to pass it. And I have found her to be a woman of very astute judgment.

The CHAIRMAN. Then there is the other bill that is pending to extend to the veterans of Korea the benefits of the GI bill of rights, which, of course, will require additional expenditure.

I very well remember that last year when the floods came in Kansas, the Congress passed relief measures for those who suffered from the losses in that flood. One relief bill carried over $50,000,000; another carried over $25,000,000. And authorizations were then passed for the construction of flood-control dams, which are necessarily long-term items of expenditure.

That brings up something which I think ought to be considered more, and ought to be more broadly known by the public than it is; namely, that the expenditures of this Government in any fisal year are not dependent wholly upon the appropriations that are made for that fiscal year, because there are a number of permanent appropriations; there are a number of obligations which must be met which are fixed by law.

The veterans' benefits determine that. The rate of pension has been fixed by law, and the amount of expenditure, therefore, is measured by the rate of incidence of the conditions which demand the payment of the benefits. The expenditures for the Veterans' Administration decreased last year below what they were before the appropriation, because the number of veterans in school had fallen off. They had completed their education, and that outlay was no longer possible.

But the expenditures predicted for veterans' services and benefits for 1953 in the President's budget is set down at $4,022,000,000, as compared with $5,166,000,000 in 1952. That decrease is due, I think, largely to the fact that the educational program has been practically completed.

But if this Korean bill passes—and I have no hesitation to predict that Congress will not deny to the veterans of Korea the benefits that were granted to the veterans of World War II—that expenditure is likely to go up some.

Senator BENTON. Could I make a comment, Mr. Chairman?

The CHAIRMAN. Yes.

Senator BENTON. This is to me the heart of our whole problem, what the chairman is saying right now. The veterans are bigger than the national debt, because if you have an inflation that tends to depreciate the value of the bonds, the veterans will be in here right away. You may be sure you will not depreciate the value of the veterans, and that $4,000,000,000 will go to $8,000,000,000, and it will go to $12,000,000,000, if your dollar starts to depreciate, because the veterans will be in here and the Congress will promptly enact the legislation, and up she will go.

The veterans are as much of a debt hanging over the country as all our bonds, in my opinion, or more of a debt. I am saying it is a legitimate debt. It is a just debt. That is another part of it, how legitimate or just or how unjust it is. But it is more of a debt, and more fixed, and it is going to cost us more, in all probability, before we get through with it.

The CHAIRMAN. Here is another example. The postal deficit for 1952 was $814,000,000. Congress last year, in trying to cut down that deficit, passed a bill increasing postal rates. But even with the increased rates—and the business in the Post Office Department is far greater now than it was before—even so, the deficit for 1953 is estimated at $669,000,000.

Then here is the question of public assistance grants. That is set down for $1,140,000,000. What are we going to do about public assistance grants? This estimate excludes proposed legislation which is under consideration, but last year this committee in its report, reported in the appendix a whole list of expenditures which could be cut only by passing laws changing the basic procedure which creates the obligation, as for example, the Federal aid for public roads. That is estimated for 1953 at $464,000,000.

When you add to this the interest upon the national debt, which is a continuing appropriation, of $6,255,000,000, and add them all together, you get a total of $14,500,000,000, and when that, together with the military expenditures and the international expenditures, is deducted from the total budget expenditure estimate of $85,400,000,000, you have left for all the other activities of Government, Congress, and the White House, and the regular branches of Government, which are dependent upon current appropriations, $6,342,000,000, out of which it is not possible to make much of a saving to meet our dilemma.

Therefore, it seems to me, from an examination of this budget, we have to find the direction, if at all, to avoid inflation in the military budget.

Senator BENTON. There is not any other conclusion.

The CHAIRMAN. I cannot reach any.

Senator BENTON. All the talk about cutting nondefense expenditures that you hear in all the chambers of commerce, they just do not understand the budget. If you are going to cut to any appreciable extent, it has to come out of the military expenditures. If you eliminate everything in the Government except the military expenditures, as the chairman said, and your fixed commitments, your contractual commitments, you would only eliminate $6,300,000,000, and you would still have a deficit.

I think the problem then on the urgency of cutting out of the military expenditures in view of the gravity of the risk is an assessment of the degree of danger and risk if we do not, and that is what the chairman's questions are so largely directed to Dr. Nourse for.

Whether we could get controls and in other ways handle the domestic economy to avoid a blow-up and at what deficit could we carry with the right controls and avoid the blow-up, are the questions upon which expert opinion would be greatly appreciatel by me.

The CHAIRMAN. Well, now, let's you and I subside and have another go-around here and see what the members of the panel care to say.

Mr. Gainsbrugh, you are making a signal.

Mr. GAINSBRUGH. This will take only a few minutes, but I do want to make our record complete. I do not want to engage in a statistical dog fight, so I will offer the following with very little additional comment.

I quote first from the Survey of Current Business for November 1951, relevant to the point that was made earlier today that most of the increases in labor income have come through employment rather than through increases in wages. This is an official document from which I read:

> For private nonagricultural industries as a whole, somewhat over half of the 1951 expansion in wages and salaries stemmed from advances in average hourly earnings, and roughly two-fifths from increased employment.

There is a chart that goes along with this analysis that might probably be incorporated into the record.

The second, if I may borrow a Fourth Quarterly Report for a minute, is incorporated in the Fourth Quarterly Report to the President, The Battle for Production. In that report is presented a chart comparing the course of wages and the course of the cost of living from January 1950, through November of 1951.

On page 43 of that document the comparison is made in the finest detail, showing the course of average hourly earnings in manufacturing, excluding overtime and excluding the shift in employment among industries. That corrects for the shift from the low value or the low paid to the high paid industries arising under defense.

The chart shows from January 1950, through November of 1951, no loss in purchasing power of straight time wage rates, corrected as best they can be for all of the technical limitations in the measure.

Senator BENTON. Your white-collar workers, as pointed out by the chairman, would show up.

Mr. GAINSBRUGH. That is quite true. I am speaking solely of the manufacturing sector, but again because a comment was offered early today that the manufacturing worker has been disadvantaged by the increase in the cost of living since Korea.

Mr. SHISHKIN. Mr. Chairman, I would like to indicate for the record in my request for the information to be submitted, I would like to be able to include the figures that would disestablish the point made here by Mr. Gainsbrugh. I think his statistics and the way he cites them are——

The CHAIRMAN. We will continue the statistical battle by leave to print.

Mr. SHISHKIN. May I merely indicate here that according to the Bureau of Labor Statistics in manufacturing itself, hourly earnings after the elimination of overtime shift premiums, a special series that they have constructed which is the closest we can come, not wage rates but the closest we can come to wage rates, that the index with 1935–39 as 100 stood in February 1950, at 206.6, in November 1951, at 230.7.

Adjusted for the price changes since prewar level, that index stood in February 1950, at 122.3, and in November 1951, at 121.6, so you will see that in terms of the hourly rates, there was a slight decline.

Mr. GAINSBRUGH. Mr. Chairman, there is an old Chinese proverb to the effect that a chart is worth a thousand words. I submit the chart in this particular document for the record.

The CHAIRMAN. Very well. Mr. Woodward?

Mr. WOODWARD. May I come back to your point? You said this would be continued in print, and it ought to be continued until it is clarified, because this is an important difference.

I do not see, Mr. Chairman and Senator Benton, how it is possible to go further than for the indication which seems to me to have come from this panel and certainly from me, that the budget figures as indicated strain the economy and risk inflation and risk instability in the longer run, probably also in the shorter run.

It seems to me that nearly every one of us in one way or another has indicated one or another of those points of apprehension. We have not said, any of us, that if it is imperative from a defense standpoint that this cannot be carried. The risks have to be taken. Of course they have to be taken.

We are saying to you, therefore, it seems to me, that if it is possible to cut even a bit, a little bit, from the budgeted expenditures, it would be a great contribution to economic stability, and you unhappily will have to listen to the military, as Members of Congress, and hear their story as to how imperative that is, and then make up your mind as to how good their story is versus how much the risk is here.

I am sure we are all fully aware that it is most extremely difficult to nick a cent at any point because somebody feels strongly for it, and so God help you. I do not know how we can go further than that.

The CHAIRMAN. Thanks for the prayer.

Senator BENTON. How about taxes? Are you going to speak of higher revenues?

Mr. WOODWARD. The same kind of problem exists. I would wonder if I have made a fair statement.

Mr. FOULKE. I would like to add a few words. I agree with what Dr. Woodward says, but I might emphasize one or two things a little differently.

I will cut away all the underbrush and say that in my opinion if we have deficit spending next year, we shall have inflation. That means we shall have higher prices.

Those higher prices on a consumer level will be on top of the highest prices we have ever had in our history today, and those prices went up every month last year, so we are adding inflation on top to the highest price level we have had. That simply means taking wealth away from the great majority of people; it is simply an indirect form of taxation.

Senator BENTON. You should see my mail. They know it all right.

Mr. FOULKE. You would know it, Senator, but a lot of your constitutents would not know it consciously.

Senator BENTON. I think they know it.

The CHAIRMAN. Mr. Blaisdell?

Mr. BLAISDELL. Senator, I would like to add this much to what has been said. I think that the whittling to try to find a balanced budget either on a cash basis or on any other basis might lead us astray.

I would anticipate that even if you had a balanced budget, you will have an inflationary situation next year. Whether you balance it by cutting or whether you balance it by taxes, that the inflationary forces which lie in the private economy just as much as they lie in the Government expenditures will make themselves felt. As long as we anticipate capital expenditures of the magnitude suggested, and I think this needs to be thought of seriously, there is a danger in thinking that the balanced budget per se will solve the inflationary problem. Normally the budget is either unbalanced on one side or on the other.

Our figures show, I believe, Senator, that during the past 5 years we have balanced the budget on a cash basis. As a matter of fact we have overbalanced it a little bit.

The CHAIRMAN. Private expenditures for construction are at least twice as great as public expenditures for construction, Federal, State, and local.

Mr. BLAISDELL. This is exactly the point I am making, Senator.

Senator BENTON. Do you, Dr. Blaisdell, agree with Mr. Wilson and his aides on the need of greatly strengthened power in the hands of the men trying to control the inflationary problems, because they are going to be up here this year. They have announced already they are going to be up here asking for much stronger controls.

Mr. BLAISDELL. Personally, I think I am on the unpopular side here. I believe there should be a tax bill and I believe also that there should be greater powers under the control legislation. I do not like them, I do not like the taxes and I do not like the controls, but I think they are necessary.

Senator BENTON. I like the controls less than the taxes, which is saying a good deal.

The CHAIRMAN. Don't you agree, Doctor, that saving has increased tremendously?

Mr. BLAISDELL. I do.

The CHAIRMAN. Dr. Gainsbrugh said this morning, as I recall, that the present rate of saving may have become the permanent standard of saving.

Mr. BLAISDELL. I would hope so under the present situation.

Mr. NOURSE. But I would not be sure.

Mr. BLAISDELL. Exactly.

Mr. GAINSBRUGH. Why not try at least to make certain that it does stick.

The CHAIRMAN. That saving is at least deflationary on the private side of the economy.

Mr. BLAISDELL. Right. I would agree on that completely, and that is the reason I say I hope this rate of saving will continue.

Senator BENTON. Has anybody a theory to explain why it is going up?

The CHAIRMAN. Dr. Gainsbrugh developed that.

Miss WARE. If you look to see who is doing the saving, it is by and large the upper income groups rather than the lower income groups.

The CHAIRMAN. But the striking thing that was developed at one of our first hearings in executive session—I think there is no impropriety in my saying it here—a statement was made that private expenditures in the expansion of defense plants were far greater during the past year than they were during World War II.

In other words, the Government financed the bulk of defense plant expansion during World War II, whereas now private capital is financing that, aided of course by——

Senator BENTON. I wondered when you were going to get to that.

The CHAIRMAN. Accelerated depreciation, which while it may be a sacrifice of tax revenue by the Government for a time, might turn out later to be a heavier tax burden for the private owners after the 5-year period has passed.

Senator BENTON. I think it is a form of Government financing, though. I always think of those certificates as a form of Government financing.

The CHAIRMAN. Dr. Ware?

Miss WARE. I would like to agree in general with what Dr. Blaisdell has just said, and with some of the things which have been said earlier. I do not like military expenditures any better than anybody else. But I would agree with Senator Benton that if we must, we must spend to the limit, whatever that is.

I would certainly subscribe to Mr. Shishkin's emphasis and to Mr. Blaisdell's on the importance of our foreign aid as a useful expenditure and a very important part of our necessary expenditure.

I would also agree with what Mr. Blaisdell said earlier, that if one looks at the average position of the American consumer, one cannot feel too badly even though one does not like to pay those prices for steak or whatever it is. The average position of the American consumer is good. The same appears to be the case with business.

Mr. Gainsbrugh pointed out that profits were almost back to pre-Korea levels, which were after all the highest in history. From what Mr. Foulke said, the expectation of business for the coming year in on the whole good, so that I do not think on the average as we look at the state of our economy we can weep too many big crocodile tears.

As a matter of fact when we are thinking of our total security, we even have to consider how wide a gap between our average level and the rest of the world is consistent with our security. One of the ways to increase our security may be to close the gap between us and other parts of the world in terms of living standards.

Now that still leaves the problem that I emphasized and that Senator Taft mentioned and Mr. Shishkin mentioned the fixed income groups, and other vulnerable groups.

Senator BENTON. None of whom are present in this room today.

Miss WARE. Well, some school teachers are around.

It seems to me that we ought to face the problems of these groups as problems within our total defense program and not use them as an excuse for not doing what is needed.

One more point in relation to what Mr. Blaisdell called attention to. Even before we had the threat of deficit spending, even though we had a budget surplus, we still had inflationary conditions.

It may very well be that inflationary pressures are actually part of a full employment economy, whether in times of the cold war, in times of the hot war, or in times of no kind of war at all, and one of the things we may need to learn to do is to live with controlled inflation in such a way that it does not bring maladjustments, that it does not overburden the vulnerable groups in the population.

Senator BENTON. What does that mean, go up a little bit every year, controlled inflation?

Mr. FOULKE. Do you think it can be done?

Senator BENTON. What does that mean, controlled inflation? Is it just a slow leak?

Miss WARE. Maybe.

Mr. FOULKE. The closest approach to it is France, and I don't know anybody that would envy what is going on in France. They have had a little more inflation, then they stop it, then a little more for 30 years. It is not a country to be envied today.

Senator BENTON. I want to know what Dr. Ware meant by the phrase.

Miss WARE. I would like to answer it, if I might.

Senator BENTON. You just let the steam out of the teakettle but keep the lid on?

Miss WARE. It can mean one of two things. It can mean the use of tax devices and credit-control devices and inducements to saving and various devices to counteract the inflationary pressures which are inherent in the situation, in order to keep a stable price level.

It can mean alternately an escalator pattern which is a gradual pattern, but in which it is not just those workers that can bargain for an escalator clause, those farmers that have a parity formula, those businessmen that can pass on costs, but everybody who is taken care of in some way. It is a perfectly consistent and thinkable way to live with inflationary pressures.

Senator BENTON. We had that controlled inflation for the last 400 years. It is just a little more inflation and a little more control, if I understood what she is saying.

Mr. SHISHKIN. I will be more inclined to agree with Leon Henderson's dictum that inflation is like pregnancy and you can't have a little bit of it.

Senator BENTON. That has always been my view.

Mr. SHISHKIN. As far as the general tendency is concerned, over a long trend, an inflationary trend which is characteristic with the kind of a situation in which we are dealing needs to be accepted and dealt with in those terms rather than in terms of adjustment which would be a deflationary adjustment. With that much I would agree, but I would very strongly disagree with our acceptance of creeping inflation.

Senator BENTON. I wondered by "controlled" if she meant creeping. That is a more accurate word, which has never appealed to me.

Miss WARE. Could I just say one more word? I just wanted to say that the starting point does not seem to me to be "at all costs let us avoid inflationary pressures," and then have as much of the security that we need, or the other things that we need, as we can have after we have taken care of these inflationary pressures.

I would like to approach it the other way around. I would like to do the positive things that are needed, meet the problem, and if the results are inflationary pressures, then keep those pressures in hand.

Senator BENTON. I concur with what you are saying now.

The CHAIRMAN. Now on that point of concurrence, I want to call the meeting closed. I promised you, Dr. Ware, that I would let you be the last speaker. Now the promise has been kept.

Mr. FOULKE. I would suggest an exclamation point at the end of Miss Ware's last sentence.

The CHAIRMAN. The committee is very much indebted to you all, and I think it may be proper to extend to you all an invitation to insert in the record any additional material or comment that you might care to make upon the basis of what has transpired today.

As a matter of fact, I would like to have each of you prepare a one-page summary of what you consider to be the conclusions which may justifiably be drawn from the whole discussion.

(The summaries referred to are as follows:)

THE MUTUAL LIFE INSURANCE CO. OF NEW YORK,
New York 19, N. Y., February 7, 1952.

Hon. JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
Washington 25, D. C.

MY DEAR SENATOR O'MAHONEY: At the conclusion of the panel discussion before the Joint Committee on the Economic Report on January 30, you said: "I would like to have each of you prepare a one-page summary of what you consider to be the conclusions which may justifiably be drawn from the whole discussion."

The preponderant opinion of the panel seemed to me to be that a budget of the size proposed for the fiscal year 1953 would mean a serious strain on the economy, a sizable risk of inflation, and a force for economic instability, both in the short run and in the long run. Consequently, a curtailment of the total of expenditures, either through reduction or at least distribution over a longer period of time, is very desirable. This country must have continuing and growing economic strength if its citizens are to enjoy life, liberty, and the pursuit of happiness, as well as a sufficient armed force adequately equipped.

No one on the panel suggested, however, that the budget could not, if necessary, be met.

The critical point therefore is the necessity. Are all the requirements for Government expenditures set forth in the budget so implacable that all this expenditure must be made, with no delay, despite the risks to the economy?

This question must be answered by Congress, after listening to all the claimants and suppliants and advocates. It is a political decision of the highest order, and the ultimate responsibility can rest nowhere but in Congress.

It is unfortunately likely that the presentations and arguments in favor of the expenditures will be more colorfully and skillfully presented than will be the risks to the economy. A part of the congressional responsibility is to be sure to give proper weight to all considerations.

I am acutely aware, and I am sure that all members of the panel are, that this is an extremely difficult job. At the conclusion of the panel discussion, I said in all reverence, and I repeat, may God help you.

Sincerely yours,

DONALD B. WOODWARD.

The CHAIRMAN. The committee will be in session tomorrow morning at 10 o'clock in this room for a panel discussion on Federal fiscal policy.

Alfred G. Buehler of the University of Pennsylvania, H. Van B. Cleveland of the Committee for Economic Development, Walter W. Heller, of the University of Minnesota, John P. Miller, Yale University, Richard Musgrave, University of Michigan, Carl S. Shoup, Columbia University, Arthur Smithies, Harvard University, and Milton Friedman of the University of Chicago are the panelists for tomorrow.

The committee is now adjourned with the thanks of the chairman and the committee for your participation.

(Whereupon, at 4:15 p. m., the hearing was recessed to reconvene on Thursday, January 31, 1952, at 10 a. m.)

JANUARY 1952 ECONOMIC REPORT OF THE PRESIDENT

THURSDAY, JANUARY 31, 1952

Congress of the United States,
Joint Committee on the Economic Report,
Washington, D. C.

The joint committee met, pursuant to adjournment, at 10:15 a. m., in room G-16, Senate wing of the Capitol Building, Senator Joseph C. O'Mahoney (chairman) presiding.

Present: Senators O'Mahoney, Sparkman, and Flanders; Representative Patman.

Also present: Grover W. Ensley, staff director; and John W. Lehman, clerk.

The Chairman. The committee will come to order.

We welcome the members of the panel who have assembled at our invitation to give the committee and the Congress the benefit of their views on the Federal fiscal policy.

I shall put in the record at this point a brief biographical sketch of each of the participants.

(The biographical sketch of the participants is as follows:)

Participants in the Panel Discussion on Federal Fiscal Policy
January 31, 1952

Buehler, Alfred G. Professor of public finance; b. Swanton, Ohio. A. B., Heidelberg College, 1922, Ph. D., Yale, 1930. Asst. prof. bus. administration, Lawrence College, 1924–25; asst. prof. economics, U. of Vermont, 1925–29; asso. prof. 1929–39; visiting prof. economics, Ohio State U., summer 1932; asso. prof. public finance, U. of Pa., 1939–42, professor since 1942; tax consultant, McConnell Foundation, 1942–43; Smaller War Plants Corp., 1944–45; Joint Committee on Tax Coordination of American Bar Assn., Federation of Tax Administrators, and National Tax Assn., 1945–47; Federal Reserve Bank of Philadelphia, 1947; Tax Study Committee of Pennsylvania, 1951; State of Vermont, 1951–52. Author: General Sales Taxation, 1932; Public Finance, 1936, 3d. ed., 1948; Undistributed Profits Tax, 1937; contributor to various public finance and economic publications.

Cleveland, H. van Buren. Research staff member, Committee for Economic Development; b. Cincinnati, Ohio. Education: Phillips Academy, Andover, Mass., 1931–33; U. S. Naval Academy, 1933–34; Harvard College (A. B. in government and economics, 1938); Harvard Law School (LL. B., 1942; editor Harvard Law Review; graduate study in economics at Harvard while attending the Law School. Experience: War Production Board, 1942–44; Foreign Economic Administration, 1944 (Assistant chief, Middle East Division; Office of Strategic Services, 1944–45 (United States Army); Department of State, 1945–48 (Assistant Chief, Div. of Investment and Economic Development); Economic Cooperation Administration, 1948–51 (Deputy Director, European Program Division). Co-author: Making Western Europe Defensible (1951), National Planning Association.

Friedman, Milton. Economist; b. Brooklyn, N. Y. A. B., Rutgers U., 1932; A. M., U. of Chicago, 1933; Ph. D., Columbia, 1946. Asso. economist, Nat. Resources Com., Washington, 1935–37; mem. research staff, Nat. Bureau of Economic

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Research, New York, 1937–46 and since 1948; visiting professor, economics, U. of Wisconsin, 1940–41; principal economist, div. of tax research, U. S. Treasury Dept., 1941–43; asso. dir. research, statis. research group, div. war research, Columbia, 1943–45; asso. prof. economics and statistics, U. of Minn., 1945–46; asso. prof. economics, U. of Chicago, 1946–48; prof. economics since 1948. Author: Taxing to Prevent Inflation (with Carl Shoup and Ruth P. Mack), 1943; Income from Independent Professional Practice (with Simon S. Kuznets), 1946; Sampling Inspection (with Harold A. Freeman, Frederic Mosteller, W. Allen Wallis), 1948. Contbr. articles to professional journals. Member, Board of Editors, American Economic Review, since 1951. John Bates Clark medallist, American Economic Association, 1951.

HELLER, WALTER W. Economist; b. Buffalo, N. Y., B. A., Oberlin College, 1935; M. A., University of Wisconsin, 1938; Ph. D., University of Wisconsin, 1941. Social Science Research Fellow, 1939–40; Instructor, Univ. of Wis. 1941–42; fiscal economist, U. S. Treasury, 1942–46 and consultant since 1946; asso. prof. of economics, Univ. of Minn., 1946–50, professor since 1950; Chief of Internal Finance, U. S. Military Government in Germany, 1947–48; staff consultant, committee for Economic Development, 1948–49. Author: "Taxation", Encyclopedia Britannica, current ed.; "Economic Policy and Political Equilibrium in Post-War Germany" in Germany and the Future of Europe, 1951; "The Anatomy of Investment Decisions", Harvard Business Review, 1951; "Compulsory Lending: The World War II Experience", National Tax Journal, 1951.

MILLER, JOHN P. B. Lynn, Mass. Harvard University, 1928–35. B. A., 1932, Ph. D., 1937. Former instructor in Economics at Harvard University and Princeton University. At Yale since 1939. At present Professor of Economics, and Director of Graduate Studies in Economics. Economist with OPA, 1941–43. Officer, U. S. Navy 1943–January 1946. Final assignment, Lt. Commander, special assistant to the Deputy for Procurement in the Office of Naval Matériel. Member of the Committee on the New England Economy, appointed by the Council of Economic Advisers, 1950–51. Consultant at various times to the Navy Department, the Munitions Board, and Office of Price Stabilization on problems of military procurement and pricing. Author: Unfair Competition, 1941; Pricing of Military Procurements, 1949; and other economic articles.

MUSGRAVE, RICHARD A., Diplom Volkswirt, Heidelberg University, 1932; M. A. Harvard Univ., 1935; Ph. D., Harvard U., 1937. Professor of Economics, Univ. of Michigan since 1937; economist and chief of Government Finance Section, Div. of Research and Statistics, 1941–48, consultant 1948–49; Federal Reserve System. 1949–50, International Bank for Reconstruction and Development; 1951, ECA; 1952, Treasury Department. Fields of specialization: Public finance, national income and social accounting, money and banking. Author: Voluntary Exchange Theory of Taxation, Quarterly Journal Economics, 1939; Public Finance and Full Employment (Board of Governors, Federal Reserve System, 1946); Interest Rates and Debt Management, in Income, Employment, and Public Policy, 1948.

SHOUP, CARL S. B. San Jose, Calif. A. B., Stanford U., 1924; Ph. D., Columbia, 1930. Prof. economics, Columbia U. Editor, Bulletin of National Tax Assn., 1931–35; staff men, N. Y. State Special Tax Commns., 1930–35; tax study, Dept. of Treasury, U. S., June–Sept. 1934, Aug.–Sept. 1937; asst. to Secretary of Treasury, Dec. 1937–Aug. 1938; research consultant, U. S. Dept. of Treasury, 1938–46; dir. Twentieth Century Fund Survey of Taxation in United States, 1935–37; director, Tax Mission to Japan, 1949–50; co-director, New York City Finance Project, 1950–52; Author: The Sales Tax in France, 1930; (with E. R. A. Seligman); A Report on the Revenue System of Cuba, 1932; (with Robert M. Haig and others); The Sales Tax in American States, 1934; Facing the Tax Problem (with others), 1937; The Fiscal System of Cuba (with Roswell Magill), 1939; Federal Finances in the Coming Decade, 1941; Taxing to Prevent Inflation (with others), 1943; Principles of National Income Analysis, 1947.

SMITHIES, ARTHUR. Economist: b. Hobart, Tasmania, Australia, LL. B., Univ. of Tasmania, 1929; B. S. (Rhodes scholar), Magdalen College, Oxford University, 1932; Commonwealth Fund Fellow, Ph. D., Harvard U., 1934. Instructor economics, U. of Michigan, 1934–35; economist, Treasury Department, Commonwealth of Australia, 1935–38; Assistant and associate professor economics, U. of Michigan, 1938–42; economist and Chief of Economics Br., U. S. Bureau of the

Budget, 1943–48; Dir. Fiscal and Trade Policy Division, Econ. Coop. Adm., 1948–49; prof. of economics, Harvard University, since 1949.

The CHAIRMAN. I understand that the panelists have already had a conference among themselves and have agreed upon an order of appearance.

Representative PATMAN. Mr. Chairman, can we have an understanding at the beginning that we will let them all finish their original statements, which I understand are not very long, before we interrogate them?

The CHAIRMAN. The members of the committee then had better make notes so that they will remember the questions they want to ask.

Representative PATMAN. Yes, sir, that is right.

The CHAIRMAN. We would like to have as full and free a discussion of the points as possible, but it is true that members of the committee are under obligation sometimes to get to the floor when Congress itself opens at noon. We will follow the rule suggested by Congressman Patman.

Dr. Smithies, we understand that you have been elected to open the discussion.

STATEMENT OF ARTHUR SMITHIES, HARVARD UNIVERSITY

Mr. SMITHIES. Mr. Chairman and gentlemen, I am very glad to appear here again and to have another chance to open this discussion.

On the other hand, I feel that I am confronted with the same perplexity that must confront the Congress in considering the fiscal policy of the country for the next year.

With the budget submitted by the President, I think to say the least, we are presented with a challenging document. It points up some of the major difficulties that the country faces at the present time.

As we all know, the budget anticipates a deficit of $14 billion with present rates of taxation expenditures expected to amount to 85 billions and revenues to 71 billions.

I am not sure how much confidence to place in those estimates. We know that the revenue estimates are usually low, and I imagine some increase in the revenue estimates is permissible, unless the Treasury has altered its estimating practices quite radically.

On the other hand, expenditure estimates have tended to be somewhat high, because the estimates have been based mainly on schedules rather than actual performance, although I understand that a new concept called slippage has entered into the official language. I am not quite sure how much slippage has been taken into account in making these estimates.

The CHAIRMAN. Will you put that word in our dictionary, Grover?

Mr. SMITHIES. My general hunch is, therefore, that the estimate of the deficit is, probably, on the high side rather than on the low side.

Nevertheless, it is a large deficit. We do seem to be faced with three more or less irreconcilable objectives.

One is to defend the country.

One is to avoid a deficit.

And one is not to put taxes up.

The CHAIRMAN. Those are irreconcilable objectives?

Mr. SMITHIES. Yes, three irreconcilable objectives.

The CHAIRMAN. Let us get them again.

Mr. SMITHIES. To defend the country, to keep taxes where they are, and avoid a deficit.

The CHAIRMAN. Thank you.

Senator FLANDERS. You have got to reconcile the irreconcilable.

Mr. SMITHIES. Frankly, I do not know how these three things can be reconciled.

It seems to me that the laws of arithmetic prevent reconciliation. And I feel we have to make the best compromise we can in this unfortunate situation.

I agree that the deficit at this particular time is highly undesirable, but it seems to me that we cannot say that we must avoid the deficit at all costs. I would be opposed to avoiding it either by slashing expenditures so as to meet the revenues under existing law and I would, also, be opposed to raising taxes, although if the Congress would raise them I would naturally submit to the wisdom of its judgment. However, my frank opinion is that there should not be an effort to increase taxes to meet a deficit of $14 billion, and there should not be an effort to reduce expenditures down to available revenues, because I do think we would be running grave external risks if we did so.

Of course, one has to take very much the word of the authorities who are in charge of our foreign policy on these matters, but it seems to me there are some facts available to everyone that indicate that our national defenses are not in particularly good shape. We have testimony of the Air Force before the Congress as to its needs, the needs of our greatest security weapon, and we all know that this present budget does not go anywhere near reflecting what the Air Force feels is necessary to defend the country.

Consequently, I think I would view with alarm any drastic cutting of programs in order to tailor our expenditures to available revenues.

The CHAIRMAN. You have two very well-known phrases in your discussion.

Mr. SMITHIES. I am given to cliches.

The CHAIRMAN. The wisdom of Congress and viewing with alarm.

Mr. SMITHIES. Yes. I try to adapt myself to my environment.

I did mention the word "program" which I suppose is another cliche. I would not be in favor of cutting programs. That does not mean that I do not feel there are important economies that can be made in the military program.

It seems to me anyone who has had the remotest connection with it is aware that with better organization, better programing in the military departments, substantial economies could be achieved and we could get the same amount of defense for fewer dollars. I take it that Mr. Miller will, probably, go into that in more detail.

Frankly, I am rather perplexed about what the Congress can do about this.

The CHAIRMAN. So say we all of us.

Mr. SMITHIES. It seems to me that it involves a very far-reaching reorganization throughout the military departments.

On the whole, and judging by results in previous years, I am not particularly optimistic about substantial economies being made on the expenditure side of the budget.

On the tax side we come to a very difficult and perplexing subject.

The President's recommendations I gather include recommendations for closing loopholes in the tax system and for making up the balance of last year's request. I am a good deal more interested in the loophole recommendations than in any general revenue increase at the present time.

It seems to me we do now have a very high revenue system, and if it is to work adequately it is highly important that there be no inequities and loopholes in it. Nothing can debauch a tax system more than public awareness that some people are getting away with things.

Consequently, I feel that the closing of loopholes and the removal of some inequities in the tax system is a major matter that should be undertaken, not necessarily in order to increase revenues but in order to sustain our present tax system.

And quite frankly I am not particularly anxious to have general increases in tax rates at the present time, because I feel that we have to digest the present tax system at the present height before we aim at new heights, assuming that is our objective.

I am, like every other citizen of the country, very much perplexed and disturbed by the Bureau of Internal Revenue situation. I do feel that the public confidence in the Bureau has to be restored before we begin to levy higher income taxes.

And I would remind everyone that it takes two parties to produce a corrupt situation. It takes an official who is amenable to persuasion, and it takes someone who persuades the official.

I do not see how you can have substantial cuts in expenditures, and I do not see how you can have substantial increases in taxation.

It seems to me we must accept a deficit.

I do not feel very alarmed about the inflationary consequences of this deficit, although its influence will, obviously, be on the inflationary side.

We have had quite an extraordinary amount of stability during the last year, and so far there are no trends that seem to be definitely in the skyward direction in this area, and although the deficit looks very large, my hunch is that it is not catastrophic.

Even if it does produce some inflationary consequences, my feeling is they are likely to be small. I would rather have a bit of inflation than take grave risks on the external side.

So I am afraid I have not brought any aid or comfort to the committee, but my general feeling is that we can more or less muddle along on this basis.

The CHAIRMAN. At least, you have rather clearly outlined the dilemma.

We will next hear from Dr. Miller.

STATEMENT OF JOHN P. MILLER, YALE UNIVERSITY

Mr. MILLER. Mr. Chairman and gentlemen of the committee, I want to confine my opening remarks primarily to some aspects of the impact of our large military expenditures on the economy.

I am most certain that I cannot resolve Professor Smithies' dilemma, but we all know that the military budget is at the center of the problem about which we have to worry. As a matter of fact, for over a decade changes in the military expenditures have been among the most important destabilizing factors. I feel that neither the economic report nor the budget have stressed adequately many of the critical problems which arise.

The question has been asked whether we can afford this program, and this is an important question. I think we all agree that we can and will afford it if we have to, if the threat is substantial enough.

One of the most serious problems which you in Congress and the public at large face is to find some ways and means of really estimating the size of the threat, the magnitude of the budget necessary to meet it, and ways for improving the operations of the Department of Defense so as to minimize their effect on the economy.

The Department of Defense has urged quite effectively here on the Hill the need for a great deal of discretion in procurement policies and in their procurement operations. This request has been granted, more particularly by the Armed Services Procurement Act which gave them the power to select their sources of supply, and to arrive at prices and other conditions of sale by administrative discretion.

The amount of power which we have placed in their hands by this act and by the budgets which you have been forced to give them recently is very impressive. It is a power which it seems to me can have a great deal, and is having a good deal, to do with the structure of our industry and the functioning of our markets.

In view of the kind of maintenance costs which seem to be implied in the present programs, the operations of the Military Establishment may be very decisive in charting our economic future.

In its decision in selecting sources of supply they can obviously have a good deal to do with the structure of industry, the degree of concentration, and the vigor of competition.

Much has been said about the problems of small business, and many of you know more about this than I. In particular, there have been some proposals to help small business by differential prices. This may be a very useful device for firms which are genuine casualties of defense production, particularly casualties of the allocations programs on metals and the like.

But I would like to point out—and in this I am reflecting some of my own experiences in the New England scene recently—that this is no time to try to bolster up weak industries and firms whose long-run prospects are not very good by various temporary palliatives. I think the New England textile situation, which is admittedly acute, is a case in point in this respect.

In these days of scarcities, including scarcities of labor, materials, and even useful factory space, it would seem to me wise to encourage the declining industries to decline and to encourage resources to shift over into the areas in which there is a better prospect.

The CHAIRMAN. Would you repeat that, please?

Mr. MILLER. In the case of industries and firms which are declining over the long run in particular areas because of inefficiencies or other reasons, it seems to me that this is the time to let them decline and let their labor and their factories be used for other industries which are critically needed for defense purposes.

I think there is no better time for industries in such areas to make those shifts, which must be made from a long-run point of view than when we have a fairly taut economy.

However, in discussing the effects of military procurement on the structure of industry, I would like to stress equally the effects of policies in placing research and development contracts, and also many production contracts.

The placement of these contracts, it seems to me, can be used to create new centers of initiative among small, medium-sized, or even large-sized firms, centers of initiative which will be a challenge to the entrenched firms.

An unimaginative use of this discretionary power which has been given to the military will simply create a new set of antitrust problems in the future. An imaginative use of it can foster the programs of developing healthy and competitive markets.

But the initiative in these matters generally starts way down in the military organization at the technical and production desks, far back even of the procurement and purchase desks. If we are not going to create antitrust problems by this large military budget, we must bring a good deal of imagination to bear at the very lowest levels in the military organization.

These matters I have spoken about concern the structure of industry, and are not crucial to fiscal policy, but I think it is important to stress them because they are important, it seems to me, in the broad objectives which the Economic Report speaks about.

I want to make a few remarks also on the relations between military expenditures and our program of economic stabilization. I realize that this is on tomorrow's agenda, but I feel that the peculiar position of military expenditures in the stabilization program has been rather neglected by many of my professional colleagues and I hope you will not feel that I am taking this occasion to lecture them, rather than enlighten you.

I would like to make the point, however, that in the absence of direct controls large military expenditures in the economy, when we are close to full employment, with the Congress which is forced generally to vote whatever is necessary for specified programs, may have a cumulative inflationary effect all out of proportion to the expenditures which are involved.

Unless military expenditures and procurements are undertaken with the greatest skill, procurement may well generate a cost inflation through encouraging wage increases and higher prices of basic raw materials in markets where prices are administratively determined. And this, in turn, will force price rises and further requests for appropriations.

At the present time, of course, our direct controls of prices and wages are a great aid to the Military Establishment, since they make cost estimating easier and negotiation of prices a good deal easier than they would be without these direct controls. This, of course, helps to keep the cost of the program and the size of the budget at a minimum.

I myself have a clear preference for moving away from direct controls as soon as we can, and placing maximum reliance upon indirect controls. But I think we have to recognize that if we do so and the

Military Establishment is going to continue to have the size budget which seems to be implied, even in the maintenance cost, we must have a much higher degree of skill than ever before in the Military Establishment in purchasing.

Under a system of indirect controls, they will be essentially responsible for the degree of stability in many of our major raw materials markets, and many labor markets. This, I think, is very important to bear in mind in the whole discussion of the stabilization program.

Another issue I would like to emphasize, and this is related to the size of the budget as well as the impact of the military budget on the economy, is the importance of implementing the purchasing policies which have been pronounced by the Military Establishment to provide maximum incentives to contractors and production, thereby encouraging them to conserve labor and materials, cut down budgetary costs, and maximize the resources which are available for small business and civilian industries.

The policies developed during the World War II and generally carried over into the present emergency point in this direction. But there has been a wide gulf between procurement policies and performance at the operating level.

Some students of World War II experience have concluded that despite elaborate efforts of the military and elaborate policies which were designed to effect incentive pricing we came very close, nevertheless, to putting procurement on a highly disguised cost-plus-percentage-of-cost basis, by very elaborate mechanisms. This tendency, I think, was reinforced by the renegotiation policies during the last war, and we have renegotiation with us again. Fortunately, there are some signs that members of the new Renegotiation Board are aware of this problem and are hoping to improve the incentive effects of renegotiation in the present emergency.

If, as seems probable, we face a long period of high mobilization, it is increasingly important that procurement activities be carried out so as to maximize contractors' incentives.

This is a problem internal to the Military Establishment, but a vital one.

It would be most unfortunate if we should be committed to a long period of mobilization with a defense program carried forward on a basis which encouraged inefficiency in industry and generally weakened our industrial base.

The last matter on which I want to speak has to do with the problems arising from the sharp separation within the Military Establishment between the two functions of determining the requirements necessary for particular programs and doing the purchasing or procurement, on the other hand.

I think most of us in civilian life tend to look upon procurement as procurement. You have strategy and you have procurement. But as a matter of fact there is a quite sharp separation between these two functions organizationally. The degree of separation, of course, varies from one department to another, but it is very important.

I should like to stress two points in this respect: the importance of proper time phasing of the requirements by the military, and the need for a continuous, mutual adaptation of the determination of requirements with the realities of procurement and individual markets.

One of the very important factors in determining the net impact of a procurement program on the economy, in addition to its size, is its phasing, the time at which purchases are made.

There can and should be a good deal of flexibility in the phasing of various components of a procurement program within certain outside limits determined by strategic considerations.

All too often, however, there is a feeling by those responsible for procurement that it is better to get goods now and be safe, rather than to take a chance and try to level out procurement.

But a good deal of flexibility in scheduling and phasing requirements is necessary if we are to avoid being very destabilizing in various markets. The textile situation last spring and others might be cited as extreme examples of poor phasing.

I want also to note the need for improving the technique within the Military Establishment for reviewing requirements constantly in the light of both the changing military strategy and changing conditions in the economy. This was a problem faced during the war and in the early postwar period. Many of the organizations and procedures used to offset such review atrophied after the war but the problem has become increasingly important again.

There are too many instances, it seems to me, where markets have been disturbed and unnecessary expenditures incurred, because procurement officials have acted in purchasing on the erroneous assumption that the requirements which have been submitted to them by other groups within the military who they were not in a position to challenge easily, without going through elaborate procedures, have gone on the assumption that these were real and urgent requirements.

The Military Establishment seems to operate all too often on the assumption that the volume, the form and the timing of requirements are unconditional and independent of costs. But we know that the requirements for defense and security are not absolute. We may have different degrees of security, we may have security based on various strategic and technical plans. We may have a particular degree of security at an earlier date.

In planning for our security we must take calculated risks in the light of the comparative costs to us of alternative programs. And one of these costs is the impact of this procurement upon the economy.

It is essential, I believe, that there be the closest cooperation within the Military Establishment between those who are taking the strategic plans and converting them into requirements, and the other groups who are doing the purchasing so that these requirements may be responsive to changing economic conditions.

In conclusion, I should like to say that I have seen some very encouraging signs that there is an awareness among the high officials in the Military Establishment of their responsibilities to consider their impact on the economy. But I believe that awareness is not enough.

The Military Establishment must take the initiative, it seems to me, in devising policies and, more importantly, practices and procedures, to carry through the policies which will permit it to fulfill its responsibility of providing national security while at the same time, strengthening rather than weakening our basic economic institutions.

This calls, among other things, for the application of the best economic skills within the country at all levels within the Military Establishment, from the highest policy levels down to the lowest procurement desk.

The CHAIRMAN. Thank you.

Professor Miller, before we have finished the discussion today, and the interrogation, if I forget to ask you the question, please remember to answer it, that the presentation which you have now made would seem to contemplate making the military a very important and powerful board of economic planners, because you have said that these various incentives will be largely a matter internal to the military, and you have said nothing at all about the establishment by Congress of any standards which should guide the military.

Mr. MILLER. I am sorry I have not been able to cover that.

The CHAIRMAN. I know that in the short time you probably did not bring in all of the points you had in mind.

Mr. Cleveland is next on the list.

STATEMENT OF H. VAN BUREN CLEVELAND, COMMITTEE FOR ECONOMIC DEVELOPMENT

Mr. CLEVELAND. Mr. Chairman and gentlemen: I would like to make a very few informal observations about the international programs, both with respect to the 1953 budget and with some look further ahead.

Most, of course, of this foreign security and international item is for Europe—for the Mutual Security Program for Europe, economic and military.

I think that of all of the programs of the Government, that is, the foreign programs, this one has probably had the most intensive and scientific, if that word can be applied to a Government activity, work done on it.

It seems to me pretty clear, from my own background and from general observation, that reductions in that program of a substantial character are reductions in European defense, without any question. Our contribution, our part of the bill for European defense is so large in relation to the total that reductions in our part of it come directly out of the military results.

I think once you have accepted the premise of the program, namely, that the effective defense of Western Europe, the creation of reasonably effective forces there within the next 3 or 4 years, is a really important objective of policy—once you have really drawn a military line across Europe, across the middle of Germany, you have taken a political and military commitment which really cannot be altered without a major shift in the premises of American foreign policy.

I do not mean by that, of course, that the program is perfect in detail, that savings might not be made on it. I assume that they probably could, having had something to do with preparing these programs in the past, but I doubt from what I know of the magnitude themselves and from what I see of the figures and hear of the way the program has been prepared that there is much that could be saved there without a real sacrifice of the economic and military objectives themselves.

The CHAIRMAN. There has been a very significant shift from economic aid to military aid.

Mr. CLEVELAND. That is true.

The CHAIRMAN. Do you intend to discuss the effect of that upon our problem and the world's problem?

Mr. CLEVELAND. I would like very much to do so, Mr. Chairman.

I think that the issue, really, between military and economic aid has been exaggerated out of all proportion to its real importance. It is at the margin, so to speak. If you are dealing in terms of shifts of a billion or so, one way or the other, between economic and military aid, the issue is really one of administrative convenience and of helping the Europeans in the most effective way. How we extend our aid to the Europeans—whether we put it in the form of military equipment or in the form of dollars—depends largely upon whether we want them to do a smaller or larger part of the total military equipment production job.

That is really the issue that is involved. It is not an issue of the total amount of aid or of military effort. It is an issue of how big you want their military budgets to be in the military production sector.

If we give them more economic aid and less end-item aid, it means that they have to producer more end items themselves. The economic aid serves to offset the inflationary and balance-of-payments effects and to provide the economic imports necessary for a higher level of military production in Europe.

If, on the other hand, you determine, for reasons of strategy or speed or cost or military convenience or what not, that it makes more sense to produce in the United States a larger portion of the total military equipment required for the European forces, then it makes sense to put a larger portion of our aid into the end-item part of the program and correspondingly to reduce the European military budgets in the equipment procurement sector.

This is not, it does not seem to me, a high issue of policy as much as it is a matter of a difficult judgment of economics and of administrative convenience and miltary strategy.

I would be glad to elaborate that further, Mr. Chairman, if you would like, a little later.

There is one comment I would like to make about the non-European part of the international security and foreign relations item. That is with respect to India.

Of course, I do not have, and I suppose they have not been made public, data on the proposed country distribution of any of these aid figures.

I do have the impression, however, in reading the budget, that what is contemplated for India is really just more or less of a continuation of the kind of assistance they are now receiving under the point 4 program. My judgment would be just that that really does not fill the bill.

The CHAIRMAN. Does not?

Mr. CLEVELAND. Does not fill the bill.

It is not going to do the job we want to do in India.

The CHAIRMAN. You mean the point 4 program?

Mr. CLEVELAND. In its present magnitude. I think they are getting something of the order of 50 million in this fiscal year out of the current appropriations.

The reason I say that is that I think the eyes of Asia are focused on India, if you do not mind another cliche. India is the one country in Asia with a strong, adequate democratic tradition which they have inherited by a long historical process from the British. It is a country of enormous potentiality, and at the same time of enormous internal political problems, and, of course, economic problems.

If India is a success over the next 5 or 10 years it will be an enormously useful contribution to the strength of the free world. In fact, I think it could very well be critical to our whole position in southeast Asia.

If India, on the other hand, goes through a period of increasing internal political difficulties, of economic deterioration such as she has suffered since the end of the war and since partition, I think it will have a very major effect in southeast Asia, an effect which will be of the same order of magnitude as the effect which the loss of China had in that area.

In other words, it seems to me that India is critical in any way you look at it out there.

We do not have, of course, all of the resources in the world to give away to foreign countries or to lend to them, but India surely is one place where our aid can have a critical effect—because you have a reasonably effective, strong government, you have a democratic tradition, you have the beginnings of a real industrial base, you have real national cohesion—at least, in comparison with countries of the same general social character in southeast Asia. You therefore have a real possibility of doing something there. Your money is likely to pay real returns. It therefore seems to me that India is a place where we should undertake a major development program and see what we can really do with our funds.

I would not want to talk figures. The Indians do have a program, I understand, a 3- or 4-year program of requiring aid in the order of a billion dollars. That does not seem to me an unreasonable magnitude.

I should just like to take one more minute to look ahead a little.

I think since the end of the war we have been constantly telling ourselves, and I do not mean insincerely, that this foreign aid business is a short-term, temporary proposition which will pass with the achievement of some kind of normality in the world situation.

It seems to me that, objectively speaking, and apart from our wishful hopes, there is very little reason to think there is going to be any such period of normality within our lifetimes.

The world is in turmoil. Outside of the United States of America and parts of Latin America and parts of the British Commonwealth, the world is in a state of chronic social, economic, and political revolution. And this is the kind of situation in which we are constantly going to be called on for actions both of a military character, an economic character, and a political character. It is bound to cost us a great deal of money—if we do it.

And if we do not do it, it means that we will be resigning from history.

I think there is not any question but that the American people and the American Government will respond to the requirements of the situation and will continue to act. It, therefore, behooves us who are concerned with the economic and fiscal aspects of the problem not to kid ourselves about the possibility of major future reductions in foreign aid, either military or economic.

There will be changes, I think, undoubtedly. And there will be changes in the geographical composition and in the emphasis on military and economic and so on, but there is very little reason, it seems to me, to hope or to believe, and very little sense in hoping or believing, that the over-all burden on our economy resulting from foreign programs is going to decline.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

We will next hear from Professor Musgrave.

STATEMENT OF RICHARD MUSGRAVE, UNIVERSITY OF MICHIGAN

Mr. MUSGRAVE. Mr. Chairman and gentlemen, I would like first to say a few words about the expenditure side of the problem and then about the tax side.

On the expenditure side, it is necessary to divide the problem into two parts, one being the military and the other being the civilian part of the budget.

As far as the military part of the budget is concerned, it is extremely difficult for a person such as myself, without the necessary information, to assess the extent to which the chance of success in our foreign policy would be damaged if expenditures were cut by five or ten billion, or how essential it would be to spend five or ten billion more.

I would, however, like to make two points. One is that this issue cannot be decided on the basis of some imaginary notion of taxable capacity or a 25- or 30-percent upper limit to our tax efforts. There is no such thing. To argue that we could decide the life or death issue of our foreign policy on the basis of such a ratio is merely to avoid the deadly seriousness of this issue. The tax system ought to be adapted to this crucial problem and not vice versa.

However, if we are looking forward in the next decade or so to a continued period of high level military expenditures as we seem to, either by way of expansion or by way of replacement, then it may well be necessary to provide some kind of mechanism by which we can secure the greatest degree of economy in this military effort.

I do not mean to imply that the Army will need be less efficient or less economy-minded than any other huge organization in its place would be, but I just wonder whether, with our present governmental set-up, we have the means by which the necessary kind of check can be applied.

I could visualize that one might set up a civilian organization the continuous function of which it would be to check into and insist on efficiency and economy in military purchases and financing. Such an organization, while working in conjunction with the Bureau of the Budget, might well operate under the direct authority of the Congress.

Now to the foreign part of our defense expenditures. The extent to which we think that we can improve our military position by arming Europe, rather than by securing additional armament for ourselves, is again a question of too much military strategy which I do not wish to judge. I would, however, like to urge that we do not think too lightly of the economic part of foreign aid. If the foreign budget must be cut, I would mostly make this cut in our military assistance than to accept drastic curtailment in economic aid.

I have some feeling for this problem, on the basis of experience gained in two foreign missions with which I have been associated. I think we have to face the fact—and you suddenly realize this over and over again in talking with people abroad—that if the western world is to unite, and to remain united, it can live as a healthy society only if its poorer members feel that the richer members are intensely interested in improving their welfare. No single nation can form a healthy society unless the poorer people feel that the wealthier people are interested in their welfare. We are well aware of this domestically, and I think we will have to become aware of it on the international level. This is something very basic, a point which comes up in thousands of ways whenever you discuss the comparative defense effort, or comparative tax rates, with people abroad. We must not forget it.

The CHAIRMAN. Is it not a fact that one of the worst marks of imperial colonialism has been that the imperialists have supported the ruling classes and the wealthy classes in the colonies to the detriment of the masses of the people in the colonies and has afforded the Kremlin its greatest avenue for propaganda and the stirring up of turbulence?

Mr. MUSGRAVE. You can give foreign aid and damage your position by it, but I think if you give it wisely you will immensely strengthen your position. It is, certainly, a matter of how it is done.

The CHAIRMAN. Will you please tell us sometime who is going to be the source of the wisdom?

Mr. MUSGRAVE. Well, I think we may be able to do better than we have been doing.

As far as the civilian part of the budget is concerned, I think that we should not be too easily carried away by the sheer magnitudes of dollar expenditures made for such purposes.

I have tried a little experiment here. If you combine into one part of the budget all of your expenditures which go for military purposes, for veterans' payments—a somewhat arbitrary group, to be sure—if you combine all these, you have then left those things which we used to think of in the good old days as the ordinary and social functions of Government. Now let us take these functions as a fraction of the gross national product. While many problems are raised by such a comparison, it help to gain a perspective on the problem. In the 1953 budget, this ratio runs up to about 10 percent. This compares with about 12 percent in 1952. It compares with about 9 percent in 1947. It compares with about 16 percent in 1940. Thus the present ratio is about one-third below the level of 1940. It is about at or just slightly below the level of 1929. It is three percentage points or so above the level of 1890.

We have to keep in mind this sort of perspective if we wish to appraise the problem properly. Surely, this is more instructive than arguing that a day's budget expenditures now exceeds total expenditures in the first 10 years of the Republic.

I do not have the time to consider the civilian expenditure program in detail, but I should like to say this much: I am hesitant, looking forward to a long period of high-level defense expenditures, to conclude at the outset that since defense expenditures are high, all sorts of civilian public services must be cut down. In normal times a good argument can be made that these services should retain their proper share within the framework of the total product that is available. This is not to say that we should not postpone some things while we are at the peak of our defense effort. But it might be poor economy to go too far in this direction, especially if the defense effort is drawn out. What we need, perhaps, is some sort of a little steel formula to determine the part of our total product that is to provide for this part of our standard of living.

But I should go on to the tax side. The present outlook, if we take the budget figures, is a deficit of about $4 billion this year, a deficit of about $10 billion for the fiscal year 1953, and I take it about the same or a somewhat larger deficit in fiscal 1954, with the hope of a balanced budget, assuming present tax rates, in fiscal 1955. This is the sort of general picture which we have before us.

Let us assume for a moment that we keep expenditures at the level at which they are proposed in the budget. The extent to which it is necessary to raise taxes, or the penalty which will be imposed by not raising taxes, will depend, of course, to a considerable degree on what we do outside the tax field. The matter might be put this way. Suppose that we have a reasonably effective monetary policy and that we continue direct controls such as we have now, but that we do not raise taxes. Assuming expenditures as proposed in the budget, how much of an increase in the cost of living should we expect over the next year or two? This is difficult to answer, but my guess is that over the next few years prices would rise more than they did last year. Now some are inclined to argue that a price increase of, say, 5 percentage points a year is really not too bad. Well, it is not too bad for 1 or 2 years, but even 4 percent for 10 years adds up to 40 percent, and so it goes.

I feel, therefore, that we should increase taxes if the expenditure level remains as proposed in the budget. It is for public leadership to accomplish this. That means it is the responsibility, primarily, of people like you, and to a small extent also of college professors, to make the people understand that if they wish to have these things, be it defense or civilian services, they will have to pay for them, and that this means higher taxation.

If the people recognize this there will be little to the argument as advanced by Colin Clark and others, that you cannot go beyond 25 percent. In principle, I agree that there is something to the taxable capacity argument. Obviously, if you tax away 99 percent of the total product your economy breaks down. But this is a matter of degree, and I do not think that we are anywhere near the danger point. Nor do I feel that this is what Colin Clark means to say. What he really says is that if tax rates go above 25 percent then the people will be unwilling to raise them further. That is to say, Clark's rule is not a principle in economics, but it is merely a very uncomplimentary appraisal of what public leadership can do in a democracy. We ought to do better than he thinks we can do.

If we raise taxes, the question, of course, is how to do it. If we stay within the limit of a 5-billion-dollar program I think we can get the additional revenue by making more or less piecemeal adjustments in various parts of the tax structure; adjustments which in any case would be desirable from the point of view of the longer run equity of the tax situation. I refer to such things as a revision of the capital gains treatment, a withdrawal of the joint return privilege, dropping or reducing the standard deduction under the personal income tax, cutting depletion, and so forth.

However, this may not be enough in the longer run. We may have to think in terms of opening major, new revenue sources, especially if the international situation gets worse. There can be no doubt that these major new revenue sources will have to come primarily out of the expenditures of the people in the middle income groups and below, say from incomes below $10,000 or $15,000. Now I do not mean to imply that nothing will have to be done above these levels. But I do mean to say that, for the bulk of the yield, we will inevitably have to draw on the mass of the consumers who do not have high incomes.

But it does not follow from this that you must treat all consumers in one big bundle. It does not follow that you must forego more favorable treatment for that part of our community which continues to have a very low standard of living. To be sure, if you cut out everybody with incomes under, say $7,500 you cut out a huge part of consumer purchasing power, and this you cannot do. But you can cut out, or go easy on, people with incomes under, say, $2,000 or $2,500. You can do this and still retain the bulk of your total consumer purchasing power in the tax base.

If the principle of progression is significant at the upper end of the scale, say above $10,000—and I think that most of us agree that it is—there is a pretty powerful argument that it is even more significant under $10,000. The problem then is to reconsider the techniques of taxing the middle and the middle-lower income groups, and to see how this principle can be applied.

As I pointed out last year, the distribution of the tax load over this broad middle range of incomes, going from, say, $2,500 up to, say, $7,000 appears to be more or less proportional. There appears to be very little, if any, progression over this broad middle range. If this is correct, it becomes the more important that the new tax sources or tax techniques, if we have to draw on them, should be adopted to improve this situation, not to make it worse.

There are two possibilities of doing this. One possibility, which probably is the best and most direct, is a more intensive use of the personal income tax in the middle and lower end of the scale, involving such things as a revised treatment of reductions, a breakdown of the lower brackets into a number of brackets with more rapid step-up in basic rates, involving—but only after all of these other things are done—a reduction in exemptions, and so forth. Considering the rise in prices since 1945, the present level of exemption seems plenty low to me. And we must not forget that exemptions are by far the most important factor of progressivity at the lower end of the scale.

The other approach is through the taxation of expenditures. This is a problem to which we should give a good deal of thought. If we could devise a means by which expenditures could be taxed without having to treat everybody's expenditure dollar alike, as is done under the general sales tax approach, we could then bypass this whole debate over whether or not a general sales tax should be introduced.

This points to some such approach as the tax on spending, which was discussed in 1941, or some other techniques might be developed by which the sales tax approach could be adjusted to permit for personal exemptions. This, it seems to me, is the area in which we should be doing most of our current tax thinking.

I thank you.

The CHAIRMAN. Thank you.

We will next hear from Dr. Heller.

STATEMENT OF WALTER W. HELLER, UNIVERSITY OF MINNESOTA

Mr. HELLER. Mr. Chairman and members of the committee, I should like to restrict my comments this morning to the question of the economic limits to taxation. And in that connection, if I may, I should like to submit a longer statement for the record.

The CHAIRMAN. It will be received for the record and inserted at the end of your statement.

Mr. HELLER. The question I should like to address myself specifically to is this, is taxation in the United States at or near limits beyond which further tax increases are self-defeating? That is, would higher tax rates defeat themselves by impairing production and causing inflation?

This is the nub of the question raised by Colin Clark, Australian economist, who suggests that the answer is "Yes" as soon as a nation's taxes rise above 25 percent of its national income.

The CHAIRMAN. May I interrupt you to say that if you are going to discuss Mr. Colin Clark, it might be appropriate for me to read into the record at this point a paragraph from a letter he has written to the staff director of this committee. I will put the whole letter in the record. He states:

> Recently I spent a month in Italy, followed by a short visit to Britain, and could not help being struck by the contrast in fiscal policies between the two countries. It is probably true that in these countries I picked extreme representatives of the two different schools of thought. In Britain the necessaries of life are not only undertaxed, they are strongly subsidized with subsequent need for additional taxation elsewhere.
>
> But on everything else, both direct and indirect taxation fall with extraordinary severity. Most wage earners pay substantial income tax and in addition immense taxation is imposed upon the modest amenities of the English workingman's life, beer, and tobacco. Prohibitive purchase tax falls on many classes of household goods which would be regarded as necessaries in any country, and therefore, as a consequence of all this, production is sluggish and there are constant demands for higher money wages. A high official of the British Treasury agreed with me that the only way to reverse the process was to make the necessaries of life much dearer and the amenities much cheaper. This is what Italy has done and her production is increasing with extraordinary rapidity, while prices are stationary or even falling. The Italian has to work hard to buy the necessaries of life, but a slight further effort will bring him some of theh amenities which are almost unobtainable in Britain. Italy has virtually no income tax and relies upon a system of indirect taxation, which falls, quite shamelessly, upon the necessaries of life.

I will put the entire letter in the record at this point.

(The letter referred to is as follows:)

ECONOMIC SERVICES,
South Brisbane, January 18, 1952.

Mr. GROVER W. ENSLEY,
Staff Director, Joint Committee on the Economic Report,
Washington, United States of America.

DEAR MR. ENSLEY: In reply to your cable of January 9, I would advise that my proposition about the 25-percent limit was originally put forward in an article in Economic Journal, December 1945 (published in England) a copy of which is presumably available to you. The article in Harpers supplemented this and brought it up to date without printing the original information in full detail. I would say that all the reasoning and conclusions of my article in Harpers magazine, to the best of my knowledge, still stand. No information which has become available since that date will effect any important alteration.

There is, however, one point which I should like to emphasize further, and that is the undoubted effect of high marginal rates of income tax on businesses, encouraging them to spend money freely on all those fields of expenditure which are allowed as a deduction for income-tax purposes. To my mind it is significant that so careful and responsible a periodical as Fortune recently published an article by a highly qualified taxation counsel, advising businessmen how to spend what is called 18-cent dollars; i. e., that each dollar spent on maintenance and in certain other ways only made a difference of 18 cents to the firm's net profit after taxation.

It is true that the loss of 18 cents remains a loss of 18 cents, and no business will overmaintain or otherwise spend money on purely unnecessary objects, but when it is in doubt whether or not to spend, it will always be biased in the direction of spending of more rather than less. In many respects such as the payment of higher wages, salaries, and bonuses, the payments for advertisement, entertainments, and public relations, the business can obtain definite advantages for itself in the future at the expense of the United States Treasury in the present.

This now brings us to the question of whether there are any grounds for hope that the 25-percent limit could be safely exceeded, and if so, under what circumstances. As you will see from the original articles in Economic Journal and Harpers the 25 percent is a round figure rather than a precise limit and should certainly be written 24–26 if not 23–27. When, however, your figure is as high as 27 I should say myself, I would be willing to bet, with a fairly high degree of probability on a further increase of money wages and consequent inflation to the national income as a whole.

If taxation of this order of magnitude appears unavoidable, you may then ask whether there is any form or forms of taxation least likely to cause an upward pressure on prices and incomes.

Under circumstances envisaged with an inescapable necessity of imposing taxation at a level of 27 percent or more, on national income, we can minimize the upward pressure by a system which, in general terms, keeps down marginal taxation with consequent necessary raising of average rates of taxation. Such a program, it need hardly be pointed out, would be extremely unpopular. It would mean removing, where possible, the progressive elements in the tax system, charging lower rates on the high incomes and higher rates on the low incomes, relying upon indirect rather than direct taxation, and making indirect taxation fall upon necessaries rather than upon amenities.

Recently I spent a month in Italy, followed by a short visit to Britain, and could not help being struck by the contrast in fiscal policies between the two countries. It is probably true that in these countries I picked extreme representatives of the two different schools of thought. In Britain the necessaries of life are not only undertaxed, they are strongly subsidized with subsequent need for additional taxation elsewhere.

But on everything else, both direct and indirect taxation fall with extraordinary severity. Most wage earners pay substantial income tax and in addition immense taxation is imposed upon the modest amenities of the English workingman's life; beer and tobacco. Prohibitive purchase tax falls on many classes of household goods which would be regarded as necessaries in any country, and therefore, as a consequence of all this, production is sluggish and there are constant demands for higher money wages. A high official of the British Treasury agreed with me that the only way to reverse the process was to make the necessaries of life much dearer and the amenities much cheaper. This is what Italy has done and her production is increasing with extraordinary rapidity, while prices are stationary or even falling. The Italian has to work hard to buy the necessaries of life, but a slight further effort will bring him some of the amenities which are almost unobtainable in Britain. Italy has virtually no income tax and relies upon a system of indirect taxation, which falls, quite shamelessly, upon the necessaries of life.

If therefore, you think that you can advocate such a policy for the United States, you may be able to go a few points beyond the 25-percent limit without causing prices and incomes to rise.

I do not know whether my old friend, Senator Douglas, is a member of your committee. I think he might be interested in this correspondence.

You will notice from this letter that I have resigned from my old post as Director of the State Government's Bureau of Industry and have commenced to practice as an independent economic consultant. The above is my temporary address.

Yours truly,

COLIN CLARK.

Mr. HELLER. May I make one factual point in reference to that specific paragraph and that is, in October Italy inaugurated a basic reform of its income tax structure and administration in order to prepare the way for increasing its reliance on income tax. Apparently the Italians are not quite as enamored of their tax system as Colin Clark is.

The CHAIRMAN. Colin Clark's letter was written on January 18, probably before that change was made.

Mr. HELLER. That may be.

Since total taxes in the United States now exceed the 25-percent critical level suggested by Mr. Clark and since Clark's thesis has been endorsed by many influential opponents of higher taxes, it seems to me that its validity is a rather important issue in United States taxation today.

Professor Musgrave demolished it with one single sentence when he said there just is no such thing. He further suggested that Mr. Clark does not mean it, at least, in economic terms. However, his letter to this commitee seems to me to reaffirm his position and reaffirm the proposition that it is an economic limit. And hence, I have the feeling that it deserves some of the committee's time.

My thought is to examine his 25-percent rule briefly from two main points of view: First, whether the statistics he cites as evidence and on which he fundamentally relies to set up his rule, whether they do, in fact, establish 25 percent of national income as the critical level of taxation beyond which inflation takes hold. And then, secondly, to what extent the basic reasoning that he develops to support his thesis—quite apart from any quibble whether the critical level is 25 percent or, as he suggests in his letter, a range of 23 to 27 percent—whether that reasoning applies to United States taxation today.

Taking up first the statistical evidence on which he relies, we find that this evidence is divided into two main parts: The data for the postwar world, and data for the period between the two world wars.

In the period since World War II he associates the inflationary effects of 1945 to 1948 with high tax rates, citing a number of countries in which tax rates exceeded 25 percent and in which there was, also, inflation. I think only one comment need be made there: That this is certainly no proof that the taxes brought on the inflation. Large wartime deficits, liquid asset accumulations, and postwar dislocations brought on inflation all over the world. And Clark does not show that inflation was worst in the countries where taxes were highest.

With respect to the United States, he associates our inflation of 1946 to 1948 with taxes exceeding the 25-percent level, and asserts that inflation brought taxes back down to 25 percent.

Actually, however, we find in looking at the data that from 1946 to 1947 the ratio of taxes to national income rose at the same time that prices increased. From 1947 to 1949, to be sure, the ratio of taxes to national income did fall at the same time that prices rose. But it would seem to me that this was the action of Congress, and not the action of inflation. Congress reduced taxes by $5 billion. Furthermore, we suffered a business recession starting in 1948.

For that matter, again in 1950 we found—as we would really expect to find with a progressive tax system—that price inflation increased not decreased, the ratio of taxes to national income. With prices rising from about 170 at the end of 1949 to 180 at the end of 1950, the ratio of tax liabilities to national income increased from 26 percent to 29 percent without taking account of the congressional tax increases. This is the exact reverse of what Clark would have us believe. So much for the postwar data.

With respect to his earlier data, he relies heavily on the case of France to show that taxes above 25 percent of national income cause inflation. However, the very figures he presents contradicts his theory. For example, one finds that prices rose more, and average price levels were higher, in the two periods when taxes, plus deficits, fell short of 25 percent than they did in the two main periods when taxes, plus deficits, were above 25 percent, which is again the reverse of what Mr. Clark has asked us to believe.

Well, enough for those data, other than to repeat that his data not only do not support his thesis but in many cases contradicts his thesis.

One might even suggest that perhaps he has looked at the wrong variables. Perhaps he should have looked at the size of surpluses and deficits, instead of at the level of taxes?

The weakness of Clark's data does not necessarily invalidate the reasoning underlying his thesis. In relationship to our United States tax situation today, where Federal, State, and local taxes are running at a rate of about 31 percent of national income, it is this reasoning which may be of primary interest.

On what does he base his proposition that 25 percent is the critical level?

His first argument is that important groups in political, economic, and banking circles will shift their allegiance from price stability to price inflation after taxes cross the 25-percent line.

Quite apart from the difficulty of visualizing how this shift of allegiance takes place, I think it is fair to ask, Why should it take place when taxes exceed a certain limit? For example, with respect to Government—which he says tries to escape the burden of interest charges by inflation—why should the Federal Government, with interest charges amounting to only 2 percent of the national income and 8 percent of its budget, court inflation to throw off that burden? Or for that matter why should landlords, or insurance companies, or various savings institutions, or educational institutions, or local governments—why should they switch their allegiance at or around 25 percent?

It is hard to find any reasonable answer to this question.

His second basis, and the one he emphasizes in his letter to this committee, is free spending by business in response to high rates of taxation.

He states that high tax rates tend to loosen the purse strings of business and that, as a consequence, there is less resistance to wage increases and less resistance to wasteful expenditure.

Ordinarily, the argument is put somewhat this way: That the businessman says to himself, "Well, since the Government takes 82 cents out of each additional dollar of profit"—that is our top marginal rate if he is in the excess-profits bracket—"each additional dollar I spend will cost me only 18 cents. So why not spend more?"

It seems to me equally reasonable to assume that the businessman might say to himself, "Since higher tax rates are cutting down my total profits by leaving me only 18 cents out of each additional dollar of profit, I had better earn as many of these dollars as possible to maintain total profits after taxes at a satisfactory level."

I do not think in the absence of clear-cut, factual information that it is clear which of these two lines of reasoning will govern his action. That does not say that high tax rates do not create some stimulus to additional spending.

Obviously, if the businessman can feather his nest by advertising, by high maintenance, by capital expenditures which benefit from accelerated amortization, he is likely to make these outlays in the interest of realizing future profits taxable at lower rates.

The CHAIRMAN. It occurs to me to remark before you go any further that in the letter to the staff director, and in the articles which have been published by Mr. Clark, so far as I have seen, there has been no reference whatsoever to the fundamental difficulty which makes our problem so grave, namely, that the Nation is confronted with a very serious defense problem. So that the basic question is, when the life of the Nation is at stake, Shall we consider limiting the tax burden?

Mr. HELLER. The third point he makes is that if one pushes taxes too high, one weakens the incentives to work and to invest. People simply will not work as hard, if they retain a smaller part of the dollars paid for additional effort. That is something on which we do not have any acceptable evidence, one way or another. One can only make one or two suggestions on the incentive point.

It is worth noting that there is a reverse incentive effect from taxes in the sense that they may stimulate people to work harder, just as much as they might stimulate them to prefer leisure to additional work. Particularly at present rates of income taxation, which take not more than 22 to 25 percent of the additional dollars earned by the great bulk of the workers in the country, taxes may actually move the worker to work harder to restore the income that is taxed away.

Out of an estimated 52,000,000 taxpayers in 1951, only 7,000,000 have incomes reaching beyond the first bracket of 22.2 percent, and only 2,500,000 reach beyond the second bracket of 24.6 percent. It seems hard to believe that those rates, even if you add State income taxes, will substantially discourage work.

With respect to the qualitative arguments, then, it seems clear that Mr. Clark cannot firmly support any particular critical limit of taxation, whether, it be 25, 35, or higher percentages of national income.

Before closing my comments, let me turn, however, to the question of whether there is really, either in Clark's terms or some other terms, some point at which taxes might actually be inflationary. If additional taxes actually curtailed output—supply—more than they reduced private spending—demand—then their net effect would be inflationary.

How could this take place? As to spending: If people's response to additional taxes in curtailing their spending got weaker and weaker—if they began to say, "No, we will not cut our spending, we will draw on our savings to pay the new taxes"—then the additional taxes would have less and less anti-inflationary effect.

As to production: If at the present time higher taxes discouraged people from working and investing—along the lines of Mr. Clark's third point—then, of course, there would be an impairment of output.

But it seems to me that we are very far from such economic limits to taxation at the present time in terms of the data that have already been cited. In the current situation in which we face a deficit of $10 billion in the cash budget for fiscal 1953, it seems clearly established that further tax increases will have an anti-inflationary effect, not the inflationary effect claimed by Mr. Colin Clark.

Thank you.

The CHAIRMAN. Thank you.

COLIN CLARK AND THE ECONOMIC LIMITS OF TAXATION IN THE UNITED STATES, SUBMITTED BY WALTER W. HELLER

(Notes for panel discussion on fiscal policy before the congressional Joint Committee on the Economic Report, Jan. 31, 1952, Washington, D. C., submitted in accordance with the invitation of the chairman, Senator Joseph C. O'Mahoney.)

Is taxation in the United States at or near limits beyond which further tax increases are self-defeating? That is, would higher tax rates defeat themselves by impairing production and causing inflation? This is the nub of the question raised by Colin Clark, Australian economist, who suggests that the answer is "Yes," as soon as a nation's taxes rise above 25 percent of its national income.[1]

Since total taxes in the United States now equal about 31 percent of national income, and since Clark's thesis has been endorsed by many influential opponents of higher taxes, its validity is an important issue in Federal tax policy today.

This statement will briefly examine Clark's 25-percent rule from two main points of view: (1) Whether the statistics he cites as evidence do, in fact, establish 25 percent as the critical level of taxation beyond which inflation takes hold; and (2) to what extent the basic ideas he develops—quite apart from any quibble about whether 25 percent is the exact critical level—apply to the United States tax situation today.

A. STATISTICAL SUPPORT FOR THE 25-PERCENT RULE

Mr. Clark relies heavily on a variety of tax, price, and national income figures for a number of countries to establish his proposition that 25 percent of national income is the tax threshhold to inflation—that beyond 25 percent, leaders in business, financial, and political circles "transfer their allegiance" to inflation, employers' resistance to wage increases and wasteful expenditures weakens noticeably, and incentives to work and invest are badly impaired.[2] If his statistics bear him out for a large number of countries and over a considerable period of time, his 25-percent rule gains much strength even if one disagrees with his reasoning.

1. Postwar data

Mr. Clark cites figures for both Europe and the United States since World War II to show that taxes exceeding 25 percent of national income result in inflation and that this inflation, in turn, is the instrument which brings the level of taxation back to 25 percent. It is quite true that inflation existed side by side with high taxes all over the world from 1945 to 1948. To muster support

[1] The best-known and most widely cited expression of this thesis is in his brief article, The Danger Point in Taxes, in Harper's magazine, December 1950, pp. 67–69. However, Clark had developed his view at greater length 5 years before in Public Finance and the Value of Money, Economic Journal, December 1945.

[2] It is not entirely clear whether Clark refers only to taxes or to taxes plus deficits (i. e., to expenditures). His earlier article leans to the latter figure, but his article in Harper's stresses the tax figure, and this is the one that is customarily cited.

for his theory, however, Mr. Clark would have to show that inflation was worse in those countries where taxation exceeded 25 percent than in those where it did not, or that the higher the taxes the greater the inflation. Mr. Clark does not demonstrate this and, in fact, it appears that deficit financing, together with war dislocations, is the culprit—under conditions of full employment, the higher the taxes and the lower the deficit (at any given level of expenditures) the less the degree of inflation.

With specific reference to the United States, Clark associates excessively high taxes with the moderate inflation of 1946–48 (after the end of price control and rationing) which, in turn, had the effect of "bringing taxes down to almost exactly the 25 percent level." Leaving aside the fact that the immediate postwar inflation is correlated much more closely with the deficits of 1944–45 than with tax levels, did inflation bring down the ratio of taxes to national income as Clark asserts? The answer is "No." From 1946 to 1947, the ratio rose at the same time that prices increased. From 1947 to 1949, to be sure, the ratio fell—not because prices rose (which they did from 1948 to 1949) but because Congress reduced taxes by over $5 billion in 1948 and because we suffered a business recession starting at the end of 1948. The evidence contradicts rather than supports Mr. Clark—inflation raises the ratio of tax revenue to national income (because we have, on balance, a progressive tax system) even when taxes exceed the 25-percent limit. Taxes and prices demonstrated his error again in calendar 1950: While prices were rising from less than 170 at the end of 1949 to 180 at the end of 1950, the ratio of tax liabilities to national income rose from 26.3 percent in 1949 to 29.0 percent (excluding tax-rate increases) in 1950 with the budget roughly in balance. Inflation clearly appears to have raised, not lowered, the ratio, even though taxes exceeded the 25-percent level.[3]

2. Earlier data

Very briefly, it may be noted that the data Mr. Clark cites for the interwar period also fail to establish his 25-percent rule. In fact, the very figures he relies on most—those for France—prove on close examination to deny his thesis more than they support it. For example, using Clark's own figures[4] one finds that prices rose more and average price levels were higher in the two periods when taxes plus deficits fell short of 25 percent (1925–27 and 1936–38) than they did in the two periods when taxes plus deficits were above 25 percent (1922–24 and 1928–35).

Although Clark cites data for several other countries, these are for the most part not directly relevant to his 25-percent hypothesis. On one hand, many of the cited levels of taxation (plus deficits) were well below 25 percent of national income. On the other, at these levels, both inflationary and deflationary movements occurred, and rising taxes (plus deficits) were sometimes associated with rising, sometimes with falling, prices and vice versa.

Clark's own data, then, fail in significant instances to support the proposition that taxes or expenditures above about 25 percent bring on inflation or that inflation reduces the ratio of taxes to additional income. In fact, some of his most important evidence is more consistent with exactly the reverse position.

It may be that Clark has not looked at the right variables at all. For example, the size of deficits and surpluses (in relation, of course, to levels of employment) may be more important than levels of taxation alone. It may be found—in fact, most economists would expect to find—that higher taxes are anti-inflationary, not inflationary, even above the 25-percent level. Another useful line of inquiry would be to compare price movements at low versus high balanced budgets (again, with employment levels taken into account).

B. ARGUMENTS USED TO SUPPORT THE 25-PERCENT RULE

Showing that Clark's data failed to establish his 25–percent rule removes one important prop from his position but does not necessarily invalidate the arguments underlying the rule. If the arguments prove valid, it may be that his general concept is right but that its application varies in different countries and at different periods of time. It is conceivable, for example, that his reasoning would apply in the United States today at about 31 percent of national income. Clearly, we need to go beyond Clark's quantitative data and examine his qualitative arguments.

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[3] See tables 1 and 8, National income—1951 edition, Department of Commerce, 1951.

[4] In the Economic Journal, op. cit., p. 375.

1. "Transfer of allegiance" to inflation

Clark's major reliance in past writings has been on the "transfer of allegiance" argument. When taxes break over the 25-percent line, some representatives of government, business, finance, and labor switch their allegiance from price stability to price inflation, with the result that the balance tips toward inflation.

Quite apart from the difficulty of visualizing how this transfer of allegiance takes place in practice—and why the individuals concerned should respond to the national average of taxation rather than to their own tax liaiblities—there is no reason to believe that the balance of personal or group advantage will shift from price stability to inflation at any particular level of taxes, whether it be 25, 35, or 45 percent.

With respect to Government representatives, Mr. Clark puts much emphasis on interest on the public debt as a basis for favoring inflation over deflation. But, one may ask, could this possibly be a major factor in the United States where interest constitutes only 2 percent of national income and 8 percent of Federal expenditures? And even if it were more, why would the Government switch its allegiance at or near 25 percent rather than long before this point?

It is equally difficult to make sense out of this point for other groups. To be sure, inflation favors some and penalizes others. Among those whom it penalizes are creditors and fixed-income groups in particular. Why, for example, would landlords, insurance companies, and other savings institutions, charitable and educational institutions, and local governments switch their allegiance to inflation because of high taxes? The vigorous antiinflationary campaigns conducted by insurance companies and, even more strikingly, the excellent cooperation of the banking community with the "voluntary credit restraint program" all contradicted Mr. Clark's argument that allegiance is switching to inflation at rates of taxation averaging above 25 percent of the national income.

2. Free spending by business

The second argument, on which he has placed increasing emphasis, is that high-tax rates tend to loosen the purse strings of business. There is less resistance to wage increases and less vigilance in regard to wasteful spending. It is assumed, that the businessman reasons somewhat as follows: "Since the Government taxes 82 cents (or 70 cents) out of each additional dollars' of profit, each additional dollar I spend will cost me only 18 cents (or 30 cents) so why not spend more?"[5] To be sure, this is one possible response to high marginal tax rates. But an equalily plausible response would be for him to reason as follows: "Since higher-tax rates are cutting down my total profits by leaving me only 18 cents (or 30 cents) out of each additional dollar of profit, I had better earn as many of those dollars as possible to maintain total profits after taxes at satisfactory levels." In the absence of clear-cut factual information one way or the other, it is not clear which of these two lines of reasoning will govern his action.

This is not to deny that high marginal tax rates provide some stimulus to increasing or speeding up expenditures. To the extent that the businessman can make outlays today that will cost him only 18 cents (or 30 cents) on the dollar but will increase his profits in the future when taxes leave him, say, 50 cents or 60 cents on the dollar, he will be stimulated to spend. In other words, to the extent that he can feather his nest for a lower-tax future by high-level maintenance and repairs, by advertising, and by capital outlays which benefit from accelerated amortization, he may increase his total current expenditures and thereby add to current inflationary pressures. Many of these nest-feathering outlays are of course not wasteful in the long run.

When it comes to the category of high living on expense accounts, wasteful use of materials and manpower and the like—a category one might call loose-living expenditures—it is hard to see how the employer's self-interest would lead him to indulge in these to any considerable extent. They do not promise higher profits in the future, in fact, thel will bring him out of the defense period with a bloated cost structure that weakens his competitive position. To be sure, such expenditures cost him little now but they also gain him little, and they may bring him losses in the long run.

With respect to lowered resistance to wage increases, certainly this has been a characteristic of the full-employment periods of World War II and the

[5] For corporations subject to excess profits tax but not at the ceiling rate the combined marginal tax rate is 82 percent. Once the ceiling is reached, it is 70 percent from there on.

early 1950's. However, higher wages may represent higher bids in the scramble for manpower rather than a response to high rates of taxation.

3. Weakening of productive incentives

Turning to Mr. Clark's third main point—the weakening of incentives to work and invest—we find considerably more substance than in his first two. Of course, it cannot be couched in terms of average tax rates alone. Incentives refer to individuals, and individuals in their capacity as workers, savers, and investors react, not to national averages, but to the specific taxes that hit their work, their saving, and their investing. Mr. Clark has recognized this in his letter of January 18, 1952, to this committee which is part of the record of these hearings.[6] In view of his recognition that it is the response to marginal rather than average tax rates which governs individual actions, it is surprising that he holds even to a range of 23 to 27 percent in place of 25 percent as the critical limit of taxation. Merely granting that marginal rates are significant ought to widen this range much further in view of the great differences in tax distribution—in relative reliance on progressive and regressive taxes—that may occur at any given average level of taxation.

Nevertheless the impact of high taxes on incentives, especially work incentives, deserves close scrutiny. Surely, there is some level beyond which further tax increases will reduce output more than they will reduce purchasing power and therefore will be inflationary rather than deflationary. Beyond some level, further taxes may so impair the willingness to work and the incentives to take risks that they will cut the supply of goods and services even more than the demand for them. But it seems highly doubtful that this would occur at or near 25 percent, and there is no acceptable evidence that it is occurring at 30 percent or would occur at, say, 35 percent. However, since it may at some time be a limiting factor to taxation, it is worth further consideration.

What is the individual's reaction to high rates of tax on his additional income? On on hand, he is stimulated to work less and enjoy more leisure and, perhaps more important, to substitute untaxed work for taxed work wherever possible. For example, it may pay him to do plumbing and electrical work, carpentry, and painting around his house or to grow a garden rather than to put in overtime on his job. The overtime is taxable, while his work for himself is not. Whether he substitutes leisure for work, or less efficient for more efficient work, in either case, the economy suffers a loss in total output.

At the same time, it must be recognized that there may be good reason for doing just the reverse of this. If higher taxes cut down the income to which an individual has been accustomed or which he has set as his target, he may work that much harder to achieve it. He may convert some of his leisure into additional work on his job to make up the loss, or he may be stimulated to do for himself the things around the house for which he previously hired others. In either case, there is a gain in output in response to higher taxes.

What evidence is available to prove the strength of one set of motives or the other? Unfortunately, in spite of many assertions regarding absenteeism, unwillingness to work overtime, reluctance to change jobs and other adverse effects of taxes on work, no firm evidence has been developed to prove their relationship to high taxation.

With respect to the responses of executives to high taxes, we do have some relevant evidence from a study made at the Harvard Graduate School of Business Administration by Thomas H. Sanders.[7] Basing his conclusions on intensive interviews, Dr. Sanders notes that executives are in considerable part driven by nonmonetary motives and that, although taxes may make them somewhat less willing to move from one job to another, "for the most part, with considerable exceptions, businessmen are currently working as hard under high tax rates as they did under low tax rates. * * *"

Also, it is important in this connection to know that the greater majority of income recipients are taxable today at marginal rates below 30 percent, even including State income taxes. With respect to the Federal tax alone, figures presented at the Ways and Means Committee hearings a year ago by the Treasury showed that only 6.8 million out of 51.7 million taxpayers would have incomes reaching beyond the first surtax bracket (now 22.2 percent) and only 2.5 million

[6] See above, p. 315.
[7] Effects of Taxation on Executives. Harvard University, 1951.

beyond the second bracket (now 24.6 percent). It does not seem likely that taxes which leave them more than 70 cents out of each additional dollar of earnings will significantly discourage their work. In fact, at these rates of taxation, income-tax increases probably constitute an incentive to work harder and replace lost income rather than work less in order to pay less tax.

All of this assumes that the taxpayer is very conscious of the relation between additional effort and additional taxes and assumes further that he responds mainly to monetary rewards. To the extent that he is not fully aware of the relationship and to the extent that he works for the joy of working or for prestige and recognition, such adverse effects as taxes might have are further reduced.

4. Conclusions

Our conclusions from this review of Mr. Clark's supporting arguments are the following:

(1) It is difficult to conceive why and how high taxes—whether at 25 percent or some higher level—should tip the balance of advantages between inflation and deflation so as to cause any significant group to switch its allegiance to inflation.

(2) The weakening of resistance to wage increases and wasteful expenditure which is alleged to result from high taxes is highly conjectural, through high-tax rates undoubtedly provide a stimulus to incur some additional business expenses currently in the interest of higher future profits.

(3) With respect to work incentives, taxes undoubtedly have adverse effects, though there are substantial offsetting favorable effects at current rates of taxation. How far taxes would have to be pushed before the adverse effects became prohibitively great is a matter of judgment, although it appears that we are not yet close to such limits.

(4) Mr. Clark's major arguments provide even less support for his 25-percent thesis (even when cast into a range of 23–27 percent) than his statistics. They provide no basis for concluding that taxes which cross over this critical line will bring on inflation. In fact, they suggest that no conclusion can be reached at all in terms of an average or aggregate levels of taxation, but that the problem must be thought of in terms of the marginal rates of specific taxes.

C. OTHER CONSIDERATIONS REGARDING LIMITS TO TAXATION OF EXPENDITURES

Even if neither the available data nor Mr. Clark's arguments established 23 to 27 percent of national income as the critical level of taxation, it does not necessarily follow that Clark's conclusions are wrong or, perhaps one should say, it does not follow that there are no economic limits to taxation or that we may not be in the vicinity of those limits in the United States today.[8]

1. Taxation

We have already noted above certain conditions under which further taxation, at stable levels of government expenditure, would have inflationary consequences. In a word, if the tax reduces the total demand for goods and services less than it curtails their supply, its net effect will be inflationary. If $2 billion of new taxes were to reduce total private spending by $1 billion (and saving by $1 billion) but at the same time curtailed the supply of goods and services by $1-1/2 billion, the net result would clearly be inflationary.

Although we are still far from any such point, it may be useful to consider how a result of this sort could be brought about. With respect to the impact on spending versus saving, it is conceivable that as taxes rise beyond a certain point and as individuals accumulate larger amounts of assets, they will be more and more reluctant to cut further into their spending and will prefer to sacrifice current saving or draw on accumulated assets in response to further taxation. If taxes on business reach such high rates that only 5 or 10 percent of the marginal dollar is retained, looser business spending might also result. On the production side, impairment of incentives as discussed above may eventually become serious enough to cause a significant reduction of output in response to additional taxes. In short, at extremely high rates of taxation, the two factors combined might make further rate increases inflationary rather than deflationary.

[8] No attempt is made here to appraise administrative and equity boundaries to taxation, through any comprehensive assessment of the practical limits to taxation would have to do so.

2. Expenditures

If we turn from taxes to expenditures and suggest that beyond a given level, tax-financed additions to expenditures are inflationary, the argument shifts to new ground. By and large, any increase in Government expenditures is expansionary. Whether financed by taxation or not, it tends to increase national income. Especially after full employment is reached, the expansionary effect puts upward pressure on prices. These effects operate at whatever ratio of national income governmental expenditures happen to be—whether it be 15 or 50 percent.

Once full employment is reached, Government economic policy can no longer rely on increases in output but must shift resources from private to public use. No doubt this becomes harder as expenditures rise. As long as heavily regressive taxes or avoided, each dollar of additional taxes (*a*) tend to displace less and less private spending, and (*b*) may have increasingly detrimental effects on output. To shift the resources without causing inflation calls for increasing amounts of taxation or other anti-inflationary measures per dollar of Government spending.

Thus, while not granting the Clark thesis that additional taxes beyond 25 percent of national income become inflationary, one might formulate the following sort of proposition: As Government expenditures rise, their inflationary effects are increasingly difficult to overcome by additional taxation. But, even here, three qualifying points must quickly be made: (1) This is a gradual process, with no reason to believe that there is a sharp breakover to inflation at some particular percent of national income; (2) additional taxes are still seen as anti-inflationary in net effect until levels far above 25 percent are reached (the precise level depending on many factors, including especially the marginal rates of taxation); and (3) in a situation like the present where the level of expenditures is well above 25 percent of national income—total Federal, State and local expenditures in the fiscal year 1953 are likely to be about one-third of the national income—additional taxes to reduce the deficit will still reduce inflationary pressures, not increase them. In addition to their short-run effect, they will slow down the growth of the debt and thereby hold down the volume of liquid assets which would increase the threat of future inflation.

In short, there are economic limits to taxation in terms of adverse effects on output and ineffectiveness in reducing inflationary pressure. But these are not inexorably reached at or near 25 percent of national income, nor do we appear to have reached them in the United States today even at levels of taxation and expenditures exceeding 30 percent of national income.

The CHAIRMAN. We will next hear from Mr. Buehler.

STATEMENT OF ALFRED G. BUEHLER, UNIVERSITY OF PENNSYLVANIA

Mr. BUEHLER. Mr. Chairman and gentlemen of the committee, a current example of the possible effects of increasing taxes on productive activity comes to my mind. I was in a group yesterday in Philadelphia where the manager of the tax department of a medium-sized corporation said that he was going to retire in a very few years, maybe within the next year, because taxes were just more than he could bear. Maybe being manager of a tax department puts him in a specially difficult spot in these days of rising taxes.

This man is of middle age. His health appears to be excellent. He is needed in an essential industry, but he feels that taxes are dulling business incentives and taking funds from individuals which might accumulate into a nest egg for future investment as venture capital.

Probably relatively few businessmen retire merely because of higher taxes. The effects of taxes on economic motives and investment are difficult, if not impossible, to measure. At some point, however, if taxes rise faster than incomes, the funds available for investment and consumption will decline and the purpose to work and otherwise produce will be weakened.

In comment briefly on the Colin Clark thesis, it seems to me that we may have missed a point which is quite important.

Certainly there is no readily determined breaking point at which the psychological and economic limits to taxes will be found.

Certainly taxable capacity is a variable thing. It must vary with not only the total taxes and the national income but, as we know, with the type of taxes, with the suddenness and steepness of tax increases, with the purposes of the budget, how well the people support the budget and other variable factors.

But is there not something in the thought that a point may be reached where the population generally would apparently prefer inflation to more taxation? And are we not at that point now?

Thinking back over the hearings during the last year of the Senate Finance Committee and the House Ways and Means Committee and reflecting on the testimony that was given there, the theme that was repeated over and over again was that taxes on this group, taxes on that class, were excessive, were inflationary, were inequitable. Some of the witnesses did say, "Yes; we should have more taxes," but there were very few, if any, witnesses who came up and said, "Gentlemen, I am one who would like to pay more taxes."

All of these programs, almost without exception, proposed to put any additional taxes which might be required on somebody else.

Taxpayers' complaints are, of course, nothing new. Recently, however, the chorus of complaints has been growing in volume.

And then, too, the inflationary forces are at work. The cost of living is going up. The country is conscious of rising taxes and rising costs of living.

The CHAIRMAN. And the cost of defense.

Mr. BUEHLER. The cost of defense is affected, certainly, by the inflation. And we people back home are reading in the papers that Congress is balking at another tax bill.

After reading the budget message and the economic report of the President's Council it would seem that in a melancholy sort of way perhaps the President and members of the Council were reconciled to some inflation. Maybe Clark's conclusion that eventually a country will prefer currency inflation to higher and higher taxes, does apply in some measure.

The taxation or inflation dilemma was perhaps revealed in the economic report, where Dr. Blough, my good friend, and members of the Council came to the place they were considering the prospects of inflation in 1952, 1953, and 1954. Estimates indicated that the existing sources of revenue, with some improvement, plugging the loopholes, and better enforcement, and so on, would raise approximately $5 billion.

But a deficit of several billion dollars would still remain. There was a reference to a tax source which could yield substantial revenue but which is highly controversial, the general sales tax. The reference said something like this, that the inauguration of a general sales tax would be a very portentious—I believe that was the word—departure from national tax policy.

Upon reflecting on these observations and the acceptance of deficit financing, one might find the implication that inflation is preferable to a general sales tax and is not a departure from national policy. I dislike to accept that conclusion.

I think there is a tendency on the part of the American citizen—it seems to be rather common—to shrink from attacking the problems of inflation. We will do almost anything in our command—will bring out all of the weapons in the fiscal arsenal, to fight depression, but when it comes to inflation we are never quite ready to stop it. I do not know if the analogy of the drinking of alcohol is one that is fair to make, but our attitude toward inflation seems to be somewhat analogous to that of the man who wants just a little more alcohol because of its pleasing effects. We keep thinking that a little more inflation is good for the economy.

So that we, the taxpayers, do shrink from paying more taxes to curb inflation. The country does dislike the unpleasant realities of the problem.

Maybe Clark's thesis is not to be substantiated with statistics. Maybe the meaning of the argument is something like this, that there have been many instances where the point is reached that the Government and the people would prefer inflation to taxation.

I think it is an open question whether we are not there now.

Thinking of the repercussions of inflation on the economy and the inequities, the damaging effects to persons of low income, and considering the effects of some sort of a general sales or expenditures tax, I wonder if inflation in its effect is, after all, not far more cruel, far more inequitable, far more damaging to the level of the living of the low-income groups than some of these unpleasant alternatives that we might consider, such as some sort of a sales-expenditures tax, exempting food, housing, medicine, and maybe some other necessities.

Another unpleasant alternative is that of raising the personal income tax rates, as Professor Musgrave suggested, on the various brackets, including the lower, or reducing the exemptions of the personal income tax.

Those are cruel alternatives, but are they as cruel as inflation which exempts virtually nobody—certainly not the low-income groups and certainly the fixed-income groups.

I think these remarks may show that I am more concerned about inflation, perhaps, than some of the other members of the panel. I have no prescription for the problems of the budget and expenditures, but it does seem to me that in this situation in which we find ourselves in which higher expenditures mean more taxes or more inflation, or both, that we have reached a place where we should examine most carefully all of the items which have leeway in the defense as well as the nondefense budget.

The defense budget is not sacred. After all, dollars can be wasted there, too, with a weakening of national defense.

Better planning and better administration could greatly reduce waste.

I do not feel that squeezing out waste and improving administration would be likely to go far enough to make a sizable cut in expenditures. This is where the difficult question comes.

What services, what projects are we willing to give up?

I heard a gentleman in Philadelphia—and I will go back home to talk about this—proposing a certain project for consideration in Washington a few months ago. He was condemning in very harsh terms similar projects in other parts of the country. But he was speaking very ardently for a certain improvement which would call for Federal money to be spent in our area.

He could see the problem of controlling expenditures requested for the benefit of other areas. He could not see it when it came to demands for money for his own community.

De we not have to give up some of these things which are desirable, some of these things which we would want to do under more propitious circumstances, some public works, and some other projects? We might, as educators, take our own bailiwick, as an example. Could we forego some of the proposed aid? If the budget is going to be reduced by even a few billion dollars many sacrifices will have to be made.

It is very easy in January to talk about cutting the budget 10 or 15 billion dollars, but we usually find that by June the pressures from our friends for projects of one kind or another have been such that expenditures keep on going up and up. It is much more difficult to cut the budget than it is to say it ought to be cut.

So if we find after we have done our best that there still is a deficit, then it seems to me the question is a fair one to put to the country, What now do we prefer? Do we prefer the contemplated spending with the attendant inflationary deficit, or do we prefer to increase taxes and balance the budget?

I am not arguing that defense expenditures can indefinitely be balanced by taxes.

I think that in his article in the Economic Journal, Clark had in mind, Mr. Chairman, that in periods of emergency the tax limit he was talking about would be higher than in so-called peacetime periods. Anyone can see the effects of patriotism and the urge to protect themselves in periods such as this.

Certainly, we have not reached the economic limits of taxable capacity. If we meet the part of the budget not covered in taxes through inflationary borrowing, we are still going to pay for that part. We cannot escape the paying.

Therefore, the question, it seems to me, is, Why not accept the inescapable costs of the budget and pay them through taxes? That is the gist of my thought.

The CHAIRMAN. As I listened to your statement, Professor Buehler, I was reminded of a very frank declaration of Mr. Cleveland that we are living in a time of political and economic revolution. And I suppose when we begin to get the interplay of views this afternoon it would be very well to determine to what extent all of you experts on the panel agree with that very specific statement. And if you do agree, to what extent it is beneficial or productive to engage in purely academic and theoretical discussions of inflation and limitations upon taxes.

What Congress is called upon to do is to act, and it has to act in every session. But theoretical discussions can go on here without end, and nobody is probably any better off for it except, perhaps, by being made a little wiser.

Mr. BUEHLER. I do think that as we discuss these problems, sometimes up in the stratosphere, that we may gain perspective and that out of our discussion may come some constructive proposals.

The CHAIRMAN. I really must be frank to say that I observe that the press table has not been writing very much since we started this morning.

I notice that you have a prepared paper there. Would you like to have it included in the record?

Mr. BUEHLER. Yes; if that is agreeable.

The CHAIRMAN. It will be made a part of the record.

(The prepared statement of Alfred G. Buehler is as follows:)

STATEMENT ON BUDGET AND TAX POLICY TO THE JOINT COMMITTEE ON THE ECONOMIC REPORT, BY ALFRED G. BUEHLER

Sizable deficits are in sight for the fiscal years 1952 and 1953 and perhaps indefinitely unless Federal expenditures can be kept considerably below proposed levels, new taxes are imposed, or both courses are followed. The President's proposed budget anticipates a deficit of $8.2 billion in 1952 and $14.4 billion in 1953. Cash payments to the public are expected to exceed cash receipts from the public by $4 billion in 1952 and $10.4 billion in 1953.

The budget unbalance might be moderated by a slower rate of spending than envisioned or a higher rate of revenue flow resulting from a rising national income. On the other hand, the unbalance might prove to be more serious than that tentatively projected because the President's budget proposals are frequently supplemented subsequently with additional appropriation requests. Furthermore, deficits might continue longer than is now forecast, depending upon world tensions, and produce cumulating reserves of spendable cash that could be released with pronounced inflationary effects at any time the country was in the spending mood.

The deficits would, of course, be reduced if Congress should adopt the approximately $5 billion tax-revision measures suggested by the President. But even the smaller deficits would contribute to the prevailing inflationary tendencies.

It is presumed in the budget and the economic report that the economy can stand more taxes but that it would be unwise to raise taxes sufficiently to balance the budget in the peak defense spending years 1953–54. The conclusion that we have not reached the economic limits of taxable capacity is a reasonable one. If some taxes have reached the limits others have not. If the Nation has the economic capacity to finance a higher budget with deficits and inflation, it also has the capacity to finance it with taxation. The real costs of defense and other services must be met out of present resources as long as they cannot be covered by external aid, just as we must arm against aggression and fight in Korea or elsewhere with our presently available manpower and materials.

While more taxation is within the Nation's economic capacity, it is evident, however, that there is a great and growing resistance to it as the taxpayers realize the extent to which their taxes have been increased. The long parade of witnesses in the hearings last year of the Committee on Ways and Means and the Senate Finance Committee reiterated again and again the theme that the taxes imposed upon the particular groups represented were already excessive, inequitable, inflationary, and damaging to economic incentives and saving. The press has been redundant with stories about the rising tide of taxes and the great inroads they are making upon taxpayers' incomes. Such complaints tend to be exaggerated. They are especially loud after new taxes are imposed. But the widespread and continuing clamor against increased taxes, at a time when tax evasions have become a national scandal, is indicative of the stiffening resistance to new taxes.

Cutting the budget in particular places may, unfortunately, be as unpopular as adding new taxes, depending upon whose purse is being penalized. It is easy to say in January that the budget should be slashed by $10 or $15 billion, but after the pressures for spending have been applied by various groups which hope to gain, the pruning of the budget is found to be most difficult. If the Nation's taxpayers are really in earnest about the necessity for avoiding higher taxes and at the same time really do not want more inflation, however, reducing proposed expenditures should win wide popular approval. The only way that consumers can escape both higher taxes and the higher prices resulting from inflation is through a lowering of contemplated expenditures.

It is true that inflation has both a political and a psychological appeal because it appears to postpone the costs of the budget to some future day and it seems to avoid for a time at least the dilemma of deciding who shall pay for governmental expenditures. But inflation hits hard at those with low and fixed incomes and raises the prices of the necessities of the poor.

Few can escape the inroads of inflation on their incomes. It is more inequitable in its insidious burdens than almost any tax one could devise. It should be endured only as a last resort and as the inescapable price of self-preservation in the war against communism.

Because waste in the Federal budget, whether it be for defense or nondefense spending, contributes needlessly to inflation it is inexcusable in this period of rising taxes and rising prices. It is difficult to draw the line, of course, between essential and nonessential spending. This is a problem of judgment which must be related to the present emergency and which must sometimes be decided rather arbitrarily. While the economies to be realized by governmental reorganization and more efficient administration may be quite significant and are most desirable, they cannot reasonably be expected to bring the budget into balance. Substantial cuts in the expenditures proposed for 1952 and 1953 will require giving up some services which are attractive but are not, strictly speaking, essential. We must choose between those nonessential services and higher taxes or inflation.

If the Nation, as its preferences are expressed through our system of representative government, concludes that it wants particular services regardless of their cost, it should be willing to accept the higher taxes required to pay for those services. It should not be misled into thinking that by borrowing it can escape the costs of those services.

Voluntary saving, investment in Government bonds, and other measures restraining inflationary spending will help to some extent to keep price down, but they do not appear to be adequate to prevent the unbalanced Federal budget from exerting strong inflationary effects. At any time the public may decide to spend rather than to save, regardless of the inflationary consequences. The present need is plainly the balancing of at least the cash paid out to the public by the Government by the cash taken in from the public by taxes and nonborrowing receipts.

Budget and tax policy in this period of the "garrison state" should, so far as possible, be directed toward financing the minimum essential governmental needs in a noninflationary manner which equitably distributes the necessary costs of government over the population. We should reduce Federal expenditures wherever it is rationally possible, comparing the costs in higher taxes or more inflation with the advantages of those expenditures. So long as we are convinced that expenditures are desirable, we should meet them, within our capacity, with taxes.

To the taxpayer, every tax is doubtless an evil. But inflation is an even greater evil for most of the taxpayers and the great majority of our population. If we do not cover the budget by taxes, we must expect to suffer the inflationary consequences, however much we would like to escape the costs of that budget.

Budget and tax policy alone are not adequate, of course, to keep inflation under control. But they are necessary supplements to monetary and credit control, price control, wage control, and other controls in curbing the menace of inflation.

The CHAIRMAN. Professor Shoup is next on the list.

STATEMENT OF CARL S. SHOUP, GRADUATE SCHOOL OF BUSINESS, COLUMBIA UNIVERSITY

Mr. SHOUP. Mr. Chairman and gentlemen: I would like to confine my remarks at this stage to some concrete suggestions for tax legislation. And in the interest of brevity the statement that I am to make does not contain all of the qualifications and reservations that I would like to make in a more extended discussion. It will, therefore, have a dogmatic tone, but I do not really intend that. When I say something should be done, I mean simply that it is my impression under the circumstances, after weighing the pros and cons, that I would favor such a course of action.

Two steps need to be taken in the near future to adapt the Federal tax system to the rearmament program. First, a number of special tax privileges, commonly called loopholes, should be repealed or greatly reduced. Second, from $5 billion to $10 billion additional annual tax revenue is needed in view of the projected rise in defense expenditures, in order to help avert further inflationary price increases. This increase in tax revenue should be enacted some time this year, effective January 1, 1953.

As to the first point, the special rate on capital gains should be raised; the holding period of 6 months should be lengthened to 1 or 2 years; and deductions for capital losses should be liberalized. Percentage depletion should be greatly restricted. Withholding for dividends, and probably also for interest, should be introduced. Business expense account deductions should be limited, either by a flat minimum of so much per day per person stipulated in the law, or by specifying in some detail, in the law, the types of expenditures that are deductible. The standard deduction of 10 percent is probably too large. Disallowance of interest and property taxes as nonbusiness deductions should be at least considered; the income-tax law at present gives a large hidden bonus to investments in the form of owner-occupied houses, discriminating against tenants. Income splitting for married couples is a correct principle, but has probably been carried too far, and might be restricted somewhat. Life insurance companies could reasonably pay more income tax. Future issues of State and local bonds should be subject to Federal income tax; this measure, although it should be enacted this year, would have no appreciable revenue effect for the immediate future. The estate and gift taxes badly need strengthening, especially as a result of the 1948 amendments. (Ultimately, the whole basis of our death- and gift-tax structure should be revised.)

The revenue thus gained should be used, first, to introduce into the personal income tax a working-wife credit, which I will explain, and second, to keep the personal income tax rates in the lower brackets lower than they would otherwise be. But the second step, of raising an added $5 billion to $10 billion revenue, will require, among other things, higher rates in the lower brackets. The net result for low-income taxpayers will be some increase in tax burden.

A working-wife credit should prove helpful in drawing into the defense labor force a considerable number of women who otherwise would not find it worth while to accept jobs outside the home.

The $5 billion to $10 billion added revenue should be obtained in part from an increase in the surtax rate schedule of the personal income tax. This schedule could be raised to a level two percentage points above that now in force for 1952, and, perhaps, higher in the upper or middle brackets. Of course, the rates in the lower and middle levels should not go so high as to affect appreciably the incentives to work overtime, to avoid absenteeism, to work at a reasonable rate under piece rates, and to take full-time rather than part-time jobs.

This latter point is more important than is ordinarily thought. Data for 1950 shows that of the total number of persons 14 years of age and over who worked that year, some 69,000,000, only 56 percent, held year-round full-time jobs, that is, 50 to 52 weeks, including paid vacations and sick leave; 17 percent were part-year full-time workers, 27 to 49 weeks, and 27 percent were part-time workers or intermittent workers.[1] It is at those points that the incentive effects of the marginal tax rates become important. But there seems to be not much danger of such effects at, or somewhat above, present levels. A married man with one child and with an annual wage of $4,000, for instance, pays Federal income tax at a marginal rate of 22.2 percent. If his annual wage or salary is $8,000, he is paying Federal tax at a marginal rate of 24.6 percent. It seems unlikely that a marginal rate short of 30 percent would greatly affect incentives to work.

Corporation taxes are either real burdens on the stockholders, or are shifted to consumers in higher prices, more likely the former. In either case, there is no justification for further increase in the regular corporation tax rates. The present tax structure already is weighted too much against the payment of dividends and in favor of retention of earnings. And, insofar as it is a tax on consumers, the corporation income tax is a most erratic kind of consumption tax. Excess profits taxation is another matter. There is a strong case for retention of this tax during the period when some corporations are bound to be making extraordinary profits, but the base should be altered. The excess-profits tax should be low for any firm whose profits exceed only the base-period standard ("earnings credit"), or exceed only the invested capital standard. But a firm whose profits exceed both standards should be subject to a high excess-profits tax rate on that part of the profits in excess of both standards.

The remaining part of the $5 billion to $10 billion added revenue could be made up by increasing the tax on distilled spirits by a dollar or two per gallon, the tax on beer by 2 or 3 dollars a barrel, the tax on gasoline by 1 cent a gallon (to 3 cents), and the tax on automobiles to 15 or 20 percent (now 10 percent).

I am dealing, Mr. Chairman, with what Mr. Buehler calls the unpleasant realities.

One other point must be mentioned, despite the risk of misunderstanding at the mere mention of it. I refer to the present provisions in the Constitution that, in effect, prohibit the Federal Government from levying a direct tax on property. The Federal Government should not enter the coming years of possibly very great financial strain with no power to use a tax on property. The need for such a tax might arise suddenly. There is much to be said for an annual low-rate tax on individual net worth, coupled with a limitation of income surtax rates to a maximum of 50 or 60 percent. Aside from this point, and simply as a precautionary measure, what we might refer to as disaster insurance, I renew the recommendation made in my address before the Academy of Political Science last April that the Constitution be amended (article I, secs. 2 and 9) to remove the present restrictions on the Federal Government's taxing power. No other national government among the major nations is similarly handicapped for meeting fiscal emergencies.

The CHAIRMAN. Thank you.

We will next hear from Professor Friedman.

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[1] U. S. Department of Commerce, Bureau of the Census, Current Population Reports, Labor Force, Work Experience of the Labor Force in 1950.

STATEMENT OF MILTON FRIEDMAN, UNIVERSITY OF CHICAGO

Mr. FRIEDMAN. Mr. Chairman and gentlemen, I shall direct my comments primarily to the role of fiscal policy in preventing inflation. It may help you to judge my detailed comments on this subject if I preface them with a brief statement of my general position on the control of inflation.

In my view, fiscal policy and general monetary policy are the only appropriate and desirable instruments for controlling inflation. I would assign no role at all to direct controls over prices, wages, specific uses of credit, or other features of the economy.

I think that is broad enough and dogmatic enough to start with.

Mr. BLOUGH. Allocations?

Mr. FRIEDMAN. I do not believe they have any role as a means of controlling inflation.

On the fiscal side, our tax record since the end of World War II, and particularly during the current rearmament period, is extraordinarily good. Except only during the mild recession of 1949, Government cash receipts from the public have consistently exceeded payments to the public, and in several years by substantial amounts. Even in the present fiscal year, despite expenditures about one and three-quarters times those of fiscal 1950, the expectation is that cash receipts will approximately equal cash payments. I doubt that there is any other period in our history in which so large and rapid an increase in expenditures was matched step by step by an increase in tax receipts. This achievement reflects great credit on the Congress and the public.

This excellent record is largely explained by the development among the public at large of a belief that a pay-as-we-go policy prevents inflation.

We have had pay-as-we-got, yet we seem to have had inflation, too. Indeed, some of the most rapid price rises occurred when the Federal Government was running its largest surpluses.

Does this mean that we have been wrong in regarding taxation as a check to inflation? I think not. We have not been wrong; we have been incomplete. In the process of learning a new truth we have forgotten or neglected an older one. Putting more coal on the furnace will tend to raise the temperature in the house, but it may not succeed if at the same time all the windows are left open.

We have been tending the furnace of fiscal policy admirably, but we have at the same time been leaving the windows of monetary policy wide open. In consequence, a large part of our tax effort has been wasted simply in offsetting an inflationary monetary policy. Only in the past year has there been a reasonably adequate monetary policy, partly because of a change in policy, partly because fortuitous events eased the task of monetary policy for the time being. And it is no accident that this shift in monetary policy coincides with reasonable price stability, despite a substantially larger increase in Government expenditures than in Government receipts, and so increased inflationary pressure from this source.

Fiscal policy cannot be considered by itself. It must be considered jointly with monetary policy.

As we have seen in recent years, more than one level of taxation is consistent with no inflation. A surplus and an easy money policy, or a deficit and a tight money policy, may have the same combined effect in preventing inflation. Which combination is best depends on factors other than inflation; in particular on the equity of diverting resources to the Government by means of high interest rates or by taxation and on the longer run problems involved in the two methods.

My own judgment is that at presently expected levels of expenditures we should aim for a roughly balanced cash budget; that we should do so equally for moderately higher levels of expenditures expected to be maintained more or less indefinitely, but that we should borrow to finance any temporary "hump" in expenditures as well as part of any level substantially above those now in prospect. Most important of all, whatever the level of taxation, we should insist that monetary policy be conducted with a view solely to the prevention of inflation.

What does this mean for immediate policy?

I believe that we cannot yet say with any definiteness whether any additional taxes should be imposed, or how much. It is still uncertain what the picture will be for this fiscal year. The Treasury estimates a slight cash deficit; others a slight cash surplus.

The CHAIRMAN. What do you estimate?

Mr. FRIEDMAN. My guess, and it is an off-the-cuff guess, is that we will have a roughly balanced cash budget fiscal 1952. The Treasury estimate is a $4 billion cash deficit.

More important, even without additional legislation, tax receipts will rise in response to the full year effect of the new taxes imposed last year. If Federal expenditures could be kept from rising by any more than this amount, there would be no justification for additional taxes. I am no expert on expenditures, but I find it hard to believe that, given the will, Federal expenditures could not be kept to that level, while yet providing ample funds for the growth of our armed strength, the objective that is at the moment primary and with which I strongly agree.

I am therefore, inclined to urge a wait and see attitude, linked to the rule and determination of providing whatever additional taxes are required to pay for additional expenditures, and matched by a resolve not to let extraordinary tax efforts again be dissipated by inadequate monetary policy.

This means that monetary policy should bear the immediate brunt of any sudden changes in circumstances or sudden emergence of inflationary pressure. It clearly can do so. The monetary authorities have ample power under existing laws to offset readily inflationary pressure from deficits of any size that now seem at all likely. An adequate monetary policy for this purpose should rely predominantly on control of member bank reserves through open market operations, buttressed by appropriate rediscount policies. Such open market operations should be conducted solely in the light of their effect on the stock of money and on prices. The price of Government bonds and the rate of interest should be allowed to vary to whatever extent is required for the far more important objective of preventing inflation.

The CHAIRMAN. It is now 12:30, and unless the members of the committee desire to ask questions now the Chair will recess the meeting until 2:30. There being no objection, the committee stands in recess until 2:30 o'clock.

(Whereupon, at 12:30 p. m. the committee recessed to reconvene at 2:30 p. m.)

AFTERNOON SESSION

The CHAIRMAN. The committee will please come to order.

I would judge by the conversation that I heard going on among the panelists as I was entering the room that there ought to be quite a field for discussion here this afternoon. If you can talk to the committee as actively as you were talking among yourselves on the issues that are up in this Economic Report, perhaps we will have an even more interesting session than we had this morning.

The Chair ventures to suggest that as a stimulus to the opening of the discussion this afternoon, it might be appropriate to suggest that one of the subjects which could be profitably discussed is the effect of a national deficit upon the savings of the people. The record before us indicates that there has been a rather substantial level of savings.

The public, instead of spending its income and to some extent instead of investing in Government bonds, has been investing in insurance, in savings banks, in bank deposits of all kinds, in savings associations, and the like.

It has been suggested that if there should be a Government deficit as a result of the military program and the other Federal programs, that might result in putting an end to the savings program. I would like to know what the views of the group around the panel table are in regard to that issue. Do I hear any volunteers to start the discussion?

Representative PATMAN. I want to cover a different part, Mr. Chairman. I want to interrogate the panel about the 25-percent limitation that has been proposed. If you would like to go ahead with this other first, it is perfectly all right with me.

Mr. FRIEDMAN. I would be glad to make a comment on your question, Mr. Chairman.

The CHAIRMAN. Mr. Friedman.

Mr. FRIEDMAN. Everything depends on how the deficit is financed. If the deficit is financed by printing money directly or indirectly and thereby promoting inflation, the effect may well be to reduce the incentive to save. Recent experience has impressed on the public the fact that rising prices reduce the real value of savings in such forms as Government bonds or insurance.

On the other hand, if the deficit is financed by borrowing from the public at whatever rate of interest is required in order to induce the public to buy the Government bonds, the effect will be rather, I think, to stimulate savings. Such a policy would be consistent with a stable price level, and so would reassure people about the value of their savings.

The CHAIRMAN. An increased rate of interest upon Government savings would increase the annual charge for carrying the debt, which has now reached a level of $6,200,000,000, according to the budget estimate for 1953, and, of course, $6,200,000,000 is approximately the same as the Federal expenditure for general activities of Government after you have deducted military expenditures and the national security expenditures and the expenditures like veterans' benefits and payments, which are required by existing law, the incidence of which could be changed only by repealing or modifying the law.

Mr. FRIEDMAN. But the alternative to a higher interest charge is taxation, on the one hand, or inflation on the other.

You specified that there was to be a deficit, which means that taxes were not being raised adequately to cover expenditures.

The CHAIRMAN. Assuming a deficit, yes.

Mr. FRIEDMAN. Given a deficit, the question is: Is it better to have that deficit without inflation, which can be done by paying the interest rate required to induce people to save and to attract the funds away from competing uses, or it is better to have the deficit and finance it by essentially printing money, which keeps the nominal interest charge down but has the consequence of inflation. It is a choice among bad things, not a choice among good things.

Senator FLANDERS. May I inquire of Mr. Friedman whether he would feel that the Federal Government would save more in purchasing what it needs in uninflated prices than it would lose in the increased interest?

Mr. FRIEDMAN. I think that question is a very much more difficult one than appears on the surface for this reason: Inflation increases Government tax receipts as well as Government expenditures. So I would rather defend the policy of letting the rate of interest reach whatever level is necessary to avoid inflation on the grounds not of what the Government would save in its budget operations, but of the cost to the public at large, and I feel sure on that score that the cost to the public at large of the inequities and hardships of inflation would be greater than the cost to the public at large of the higher interest charge, which would mean that at a later time there would have to be higher taxes perhaps.

Senator FLANDERS. The case for pegging bond prices is put on the necessity or the desirability of holding down the interest charges. So in making a case for or against, you have got to give some counterweight or counterbalance to the increased interest charges.

Mr. FRIEDMAN. But the alternative really is an increased interest charge, on the one hand, in an open form or an increased burden on the public at large in the form of price rises.

I think the tendency to put the case in terms of the money interest payments by the Government diverts attention from the real problem. The real problem is not the number of dollars paid in interest. The real problem is who bears the burden of the cost of providing the goods and services that the Government uses.

Senator FLANDERS. If the net increases in the expenses—if there is a net increase in the expenses of the Government owing to the increased interest charge, and you are supposing that we are not increasing taxes, that at least means a smaller amount of either larger appropriations and a bigger spread due to the increased interest charges, or it means in some way cutting down the appropriations, which is another thing.

It seems to me that the increased interest charges have to be met in some way. It is not favorable to meet them by increasing our Government expenditures. That is inflationary. May I say that I am favorable to the point of view that we shouldn't peg the interest rate, but I want to have good reasons for it.

Mr. FRIEDMAN. The good reasons, I think, are the reasons of the effect of one policy or the other on the distribution of the cost of Government expenditures among the people.

I think the argument about the actual payment of interest is a bad reason for either the one policy or the other. If one feels that borrowing and raising the interest rate raises Government expenditures more than the game is worth, why then the correct implication is that we should levy more taxes instead of borrowing.

Having made the decision not to levy taxes, the alternatives are either to openly pay more interest in the form of actual payments on debt or to make the people pay a larger sum indirectly and not openly through higher prices. In either case you really have the same burden levied on the people.

The CHAIRMAN. Your point is that basically the way to handle the burden of increased expenditures, assuming now that this increased expenditure is the minimum expenditure required for national defense, after Congress has eliminated all unnecessary expenditures and all waste and extravagance and all that, so that we do come down to the naked question of national defense and its cost.

Mr. FRIEDMAN. Yes.

The CHAIRMAN. Your argument is that the best way to meet that is by increased taxation, but barring increased taxation, it should be met, that it must be met either by increased interest rates—that is to say, by monetary policy—or it will be met by inflation.

Mr. FRIEDMAN. Absolutely, except that I would add a footnote, if I may.

The CHAIRMAN. Yes, of course.

Mr. FRIEDMAN. As to the question whether it is necessarily best to do it by increased taxation, there are circumstances under which it would be better to borrow to meet the increased cost than to increase taxation.

The CHAIRMAN. You said this morning that you advocate borrowing to meet the humps, the unexpected rises in expenditures.

Mr. FRIEDMAN. Quite right.

Senator FLANDERS. The increased interest rates put a larger charge on the Government for a given range of undertakings. You have then the alternative of raising taxes of some kind by that degree or of buying less in goods and services.

Mr. FRIEDMAN. I am sorry. I don't believe that is the alternative in the short run. From the longer run point of view, it is true that borrowing more now commits the Government to higher interest payments for some longer period, and in the longer view it will have these alternatives you list; but in the short run, when it borrows the money, it is in the same position as an individual. If he borrows, that provides him wtih funds with which to make additional expenditures over and above what his income brings in, and the same with Government.

Senator FLANDERS. Then you are saying he is going to borrow an increased amount to meet the increased interest payments. What would you advise me to do if I were the Secretary of the Treasury, who is going out of office at the end of this year? That is a short run.

The CHAIRMAN. That is a rather bold assumption, sir.

Mr. FRIEDMAN. If you were a Secretary of the Treasury, regardless of when you were going out of office, and if you were, as you would be, interested primarily in the welfare of the Nation, I would urge you to borrow at whatever price is necessary in order to avoid inflation.

Mr. MUSGRAVE. Mr. Chairman?

The CHAIRMAN. Mr. Musgrave.

Mr. MUSGRAVE. I am a little afraid that this argument might lead us to conclude that it really isn't so important whether we raise the necessary taxes or not. Now, assuming that we do not raise the necessary amount of taxes, Mr. Friedman certainly is correct in arguing that there is some rate of interest at which we will be able to borrow the amount of deficit funds in a way which will be no more inflationary than taxation would be.

As a matter of practical policy, this is not a question of pure principle—Mr. Friedman would agree—but of the degree of adjustment involved. Now, it is reasonable to argue that at a time like this you should have a Federal credit policy which prevents over-expansion of commercial loans. Such a policy is necessary, but one must not overlook the difficulties involved. These difficulties, if we look at them realistically, are substantial. Therefore, it would not seem wise to increase the burden of monetary policy by requiring it to provide for interest-rate adjustments which will be sufficient to assure that a substantial deficit can be absorbed by non-bank investors. If this difficulty is added to the others, you might well end up having no monetary restriction.

It seems to me there is a strong argument on the monetary policy side for making every effort through adequate taxation to minimize the need for additional financing because the larger are the additional financing needs, the more difficult it will be, I think, even to succeed in a fairly modest monetary policy objective. In order to make it possible for monetary policy to be successful in these limits, it should not be saddled with the additional burden of having to place large amounts of new borrowing outside the banks.

The CHAIRMAN. Professor Buehler, do you care to make any comment?

Mr. BUEHLER. I was wondering, considering Senator Flanders' question, what would the increase in interest charges be, just taking that part of the cost? Have you any notion, if I may address this perhaps to Professor Friedman, since he raised the question—what would the rise in the rate of interest be, what is the possibility there? And if the debt increases 10 billion, then how much is involved? It is only a small part of the problem.

Mr. FRIEDMAN. I am hesitant to make any predictions. My own guess is that any rise in the rate of interest would be very small, but that might be wrong and my conclusion would not change. It may help it if I indicate the orders of magnitude involved. We are now talking about the problem for the next fiscal year. Estimates of the size of the cash deficit for fiscal 1953 vary according to whom you get the estimate from; however, I think $10 billion would probably be on the high side rather than on the low side.

Now, a deficit of $10 billion is roughly about 3 to 4 percent of the national income. Aggregate savings are several times that. It seems to me it ought not take a very high interest rate to direct that fraction of the Nation's savings into Government borrowing instead of into other kinds of borrowing.

So my guess is that, given the magnitudes we are now speaking about, it would not require much of a rise in the interest rate to enable the deficit to be financed without inflation.

Representative PATMAN. How would that affect existing long-term bonds?

Mr. FRIEDMAN. Sir?

Representative PATMAN. How would that affect existing long-term bonds?

Mr. FRIEDMAN. Insofar as the interest rate did rise, it would of course mean a decline in their price.

Representative PATMAN. How low would you let them go?

Mr. FRIEDMAN. As low as is necessary to accomplish the objective of preventing inflation.

Representative PATMAN. Suppose it went down as low as 75.

Mr. FRIEDMAN. I think it is exceedingly unlikely that it would go as low as 75. However, if the alternative were to let the bonds go to 75 or to allow inflation to rage, I would take the alternative of allowing the bonds to go to 75.

Representative PATMAN. You wouldn't support them at all?

Mr. FRIEDMAN. No.

Senator FLANDERS. The E bondholder is protected in a way which was not the case in the Liberty bonds.

Mr. FRIEDMAN. Absolutely.

Representative PATMAN. I am not talking about E bonds.

Senator FLANDERS. Other bonds are bought under conditions of caveat emptor by investors who know what it is all about.

Mr. FRIEDMAN. A situation in which bonds would fall as low as you suggest is a situation in which there is great resistance on the part of the public to parting with the resources the Government wants to get control over. This means that you have a hard problem whatever you do.

A situation in which bond prices would fall to 75 would be a situation in which it would take a very large tax increase or strong measures of any other kind to prevent inflation and in which there would be a good deal of inflation if bond prices were supported while nothing else was done. The relative advantage of the different measures would still be the same.

Mr. BUEHLER. You had asked me a question, Senator.

The CHAIRMAN. Yes.

Mr. BUEHLER. Could I say this, please. I had stressed this morning what I considered the needs for additional taxes if the budget were not cut—and that would be a pretty tough job—way back to the existing revenues, and also the improbability that the voluntary savings drive under present conditions would be adequate to induce the saving that we would like to obtain. I think the pleasantest way out of the deficit dilemma would be to have people increase savings and invest voluntarily at, let us say, existing rates of interest, in the E bonds.

But seeing what is happening to the E bonds and how unattractive they are to many persons of modest income, it would seem that unless the patriotic motive somehow could be used to induce people to save beyond the rate at which they are saving—and that can be pushed only so far—we are likely to be driven to higher rates of interest to sell adequate amounts of such bonds.

The CHAIRMAN. What has happened to the E bonds?

Mr. BUEHLER. I was thinking of the reports on the excess of redemptions over sales.

The CHAIRMAN. I am trying to get at what is back of it. The statistical fact is there are more redemptions than sales at the moment. Now, that means—that has not meant a decline in savings. It has been accompanied by an increase in savings.

Mr. BUEHLER. That is so.

The CHAIRMAN. But the savings, instead of going into Government bonds, have been going into other instrumentalities which pay a higher rate of interest.

Mr. BUEHLER. Yes.

The CHAIRMAN. Therefore the argument is made that the Government should increase the rate of interest upon savings bonds so as to attract those savings back into the Government channel. But the question that I would like to see answered is whether or not this proposal of Dr. Friedman to increase the wages of capital would result in diverting savings from the Government need in the great emergency.

Mr. BUEHLER. Well, it seems to me that the radio appeals and the advertising of the Treasury to sell the bonds are certainly appealing to one's patriotic motives and the desire to support his country. The investment appeal is also being made, but people are not buying bonds at the desired rate. I have no information that would answer the difficult question as to just why the great rank of the people do not buy more E bonds.

I do hear conversations here and there that link the purchases of E bonds to inflation, the decline in purchasing power of the bonds, and the feeling that the E bond is not attractive as an investment. I should think that a higher rate of interest would make Government loans more attractive to investors. But the price level should be stabilized to protect purchasing power. Inflation should be curbed.

The CHAIRMAN. The estimate sent up with the budget was that the deficit in 1952 would reach 8 billion, and in 1953 would reach approximately 15 billion. It was suggested, I think by Professor Smithies, this morning that perhaps that is an overestimate of the deficit, because the revenues may be greater and the expenditures may be less than actually estimated in the budget.

But the statistical fact is here that savings have been increased.

So my original question this afternoon was to get your opinions as to what the effect would be upon savings if this deficit, which is estimated, should be permitted by Congress. Would the result of that be to induce people who are now saving by whatever method they choose—because of the attractive interest that is available from Federal savings and loan associations, or, for example, in insurance, or whatever they choose—to stop saving and to go into the market to buy whatever they could and thereby bid up prices and accelerate inflation.

Mr. BUEHLER. It may be that the workingman and those in the middle- and lower-income groups who have bought bonds have seen many of the statements in the press and in periodicals showing that the purchasing power of the $75 used to buy the $100 bonds was greater than the purchasing power of the $100 available after 10 years when the bond matures.

The loss in purchasing power to investors has been given considerable publicity and has probably had some effect.

Mr. SMITHIES. Mr. Chairman?

The CHAIRMAN. Mr. Smithies.

Mr. SMITHIES. I think the answer to your question, of course, depends on what does happen to prices. You are in a bit of a circle here. If the prices do start going up rapidly, I feel—and it is a reasonable presumption—that people's tendency to save will be diminished. How rapidly they have to go up to reduce the rate of savings is somewhat difficult to say. People seem to be rather obstinate about refusing to save, and we haven't much evidence so far that moderate price increases have a very pronounced effect in deterring savings. The increase in saving that occurred during the course of 1951 seemed to go counter to any expectation you would think people would have.

I do want to add some qualifications to Mr. Friedman's remarks on the subject. He has an attractive but, I think, a somewhat dangerous propensity to see things in black and white, and he says dogmatically that an increase in credit means inflation. Well, it is not quite as simple as that in the real world. It may be in Chicago.

The CHAIRMAN. There is no such rule for Boston or Harvard, I presume.

Mr. SMITHIES. We are somewhat more associated with the practical side of life. While I agree entirely that borrowing should be done as far as possible from the public, and while I don't support the idea of absolute rigidity in interest rates, and I would rather see a managed interest rate, I can't really subscribe to the doctrine that any increase in credit is inflationary, and therefore evil, and any policy based on an increased credit ought to be outlawed.

There are several reasons—I think two main concrete reasons—why that proposition can't be fully maintained. One is that we do expect an increase in the output of the community, and I think Mr. Friedman would probably agree when there is an increase in output you can have the increase in the quantity of money without inflationary consequences.

Another factor is that we do have a system of direct controls; and even if one limits oneself to Mr. Friedman's frame of reference, we are using allocations controls to limit the amount of private investment quite drastically.

Shortages of materials such as copper are putting very severe limitations on the rates of private investment just because you can't carry out the projects because of shortages of copper and other critical materials needed for the defense program.

It is quite possible that we might have contractions that will offset the effects of a budget deficit. I don't think the committee should accept the position that any increase in the quantity of money is likely to lead us on the road to disaster.

Mr. FRIEDMAN. I wonder if I could make a comment just to clear up the record on my view. I do not believe I said—and I certainly did not intend to say—what Mr. Smithies interprets me as saying.

I did not say we should borrow in such a way as to have no increase in the supply of money. I said we should borrow in such a way as to have no increase in prices; that we should let the interest rate go to whatever level is required to keep prices from rising. It is certainly true that, by and large, we can have something like a 3- to 4-percent increase per year in the stock of money without any price rise because of increased output.

Consequently, a noninflationary borrowing program would not mean an unchanged stock of money. It would mean that the change in stock of money would not be allowed to go so far as to increase prices.

The second point is on the allocations question. I did not mean and do not want to give wholehearted approval to allocations because I do not believe they have any role in preventing inflation. Under some circumstances, however, there is a limited case for priorities, not allocations, for an altogether different purpose, namely when prices of products needed for government use are rigid and do rise sufficiently rapidly to enable the market to allocate goods efficiently. As you can see, this justification of them is almost precisely the opposite to that offered by those who regard them as an instrument for controlling inflation.

Senator FLANDERS. I might suggest we are moving in rapidly and with very heavy forces into the area of the subcommittee of which Mr. Patman is chairman, and I wonder if it wouldn't be wise if we specialized on that 25-percent limitation, for instance. I think you would like to hear that discussed, wouldn't you?

The CHAIRMAN. He wants to have that discussed, and so indicated at the outset. There is no question about that.

But if Mr. Patman will pardon me for just a moment, I was going to remark that Professor Shoup, who collaborated with Professor Friedman a few years ago in a book entitled, I think, "Taxing To Prevent Inflation," has been conspicuously silent during this little discussion. Have you anything to add to the matter?

Mr. SHOUP. Thank you, Mr. Chairman. I think the issue is precisely as Mr. Friedman has stated it in his last comment. The difficulty is the usual quantitative one of forecasting how much addition to the stock of money we can stand during the next 12 months without generating an increase in prices.

If someone can give me that figure, I can then indicate the kind of policy specifically I would like to follow. But, in brief, let me say that——

The CHAIRMAN. We are trying to get the answer before we give you the quantity of money.

Mr. SHOUP. Certainly. In general I agree with Mr. Friedman except that perhaps I would see a little more use in the short run for some of the direct controls than might be attractive to him. In general I feel that we have no excuse really for going into further inflation.

I can't see that the alternatives to inflation are harsh enough to justify our accepting inflation. Inflation, as opposed to taxation, or as opposed to a higher interest rate, is simply a method of distributing the burden. The burden is going to be there in any case.

The CHAIRMAN. I take it your opinion is that, assuming a large expenditure for defense purposes, which left alone would create inflation, thereby increasing living costs and defense costs, then the Government should take alternative policies rather than to permit inflation to take hold.

Mr. SHOUP. Absolutely; without question.

The CHAIRMAN. Professor Musgrave.

Mr. MUSGRAVE. One way to look at the matter is to compare the dislocations and difficulties which you incur if you put a certain burden on the monetary approach, or if you put it on the tax approach.

Now as I indicated this morning, I think we can put a good deal more burden on the tax approach. Also, I think that we will have a tough time to handle the burden already placed on the monetary approach. We should see the two things in comparison.

One of the main uses of the monetary approach in this situation is that it is more flexible. We have to plan taxes long ahead and don't really know what is going to happen. Monetary adjustments can be made while we go along. It seems to me that this should be its main monetary function, but that if we look at the problem over a 5- or 10-year range, we should try to do as much as we can by way of taxation.

The CHAIRMAN. You agree that monetary policies are a substitute for increased revenue through taxation if it is possible?

Mr. MUSGRAVE. Yes; within certain limits, but not as a one to one alternative. Each function should be seen in its particular framework. The role of monetary policy, I think, is more or less one of backing up tax policy and of meeting the shorter run adjustments, which you can't do by tax policy.

The CHAIRMAN. Mr. Heller.

Mr. HELLER. If we are really convinced that we face an expenditure hump for 2 years, it seems to me the argument for monetary policy is a good deal stronger than if that hump keeps going away from us the way it has in the last couple of years and becomes either a long-run upward trend or possibly a plateau at a good deal higher level than we thought.

In that case, falling into the habit of deficits would have serious long-run consequences in building up a stock of assets from which people would then gradually be moved to spend more and save less.

Therefore, our assessment of the expenditure outlook, it seems to me, is extremely crucial to the evaluation of monetary versus fiscal policy measures.

Mr. SMITHIES. Could I say one more word?

The CHAIRMAN. Mr. Smithies.

Mr. SMITHIES. I do think we ought to get the question we are discussing straight. I suspect if one canvassed this group and asked us all to talk about an ideal policy, you would perhaps find no difference between us. I think Mr. Friedman and I would agree completely on what an ideal policy would look like, and I think we would agree completely on the system of social values that we are trying to preserve by such a policy.

The question that is really confronting us today is this one: We have got a defense budget. It seems to me at any rate very unlikely that taxes will be raised sufficiently to balance that budget. It seems also somewhat unlikely to me that a monetary policy that will avoid inflation will in fact be pursued, given all the circumstances surrounding the case.

I think the question before us is, Are the external dangers to the country sufficiently great to warrant running the risk of some fairly mild inflation? My answer to that question is, they are sufficiently great, and the risks of some mild inflation are not so great as to make that an overriding factor in the situation.

The CHAIRMAN. Thank you very much. Now we will turn the session to the 25 percent limitation on income taxes, which strikes the interest of Congressman Patman and Senator Flanders.

Representative PATMAN. I understand, Mr. Chairman, that the Colin Clark proposition, which has been mentioned by Mr. Heller, is not the same thing as the proposal that has been adopted by many State legislatures, commencing prior to 1940, calling for a limitation of personal and corporate income taxes to not more than 25 percent in any one year. The Clark contention is that in the aggregate not more than 25 percent of the national income may safely be taken in taxes; is that right?

Mr. HELLER. That is correct, sir.

Representative PATMAN. I want to ask about this proposal that has been sponsored by different organizations, one in particular before various legislatures. Now, that proposal, of course, appeals to a lot of people. I have personal knowledge of a meeting in a certain city in the Southwest. They got people at this meeting who were in the high-income brackets, and asked them to take a card and determine for themselves how much money they would save if there were a constitutional limitation against the collection of more than 25 percent in taxes.

Naturally, they found that they would save a lot of money if such a limitation were in effect. The person holding the meeting didn't have any trouble getting a lot of money for his fund to campaign for this limitation before the legislatures. You can see why. That is a selfish reason. We expect people to be selfish up to a point but it shouldn't interfere with the public interest.

There are other reasons, I think, why they are pushing that, but that is not so important as what effect it would have on the country. Personally, I am in favor of a balanced budget. I have always advocated that.

I would be in favor of joining with the majority of the Members of the House in staying in session and we will not adjourn this Congress until the budget is balanced. But we cannot always get done what we want done, because legislation in a democracy is a matter of give and take; compromise and adjustment.

But it occurs to me that it would be a very bad thing for the sovereign power to have a restriction like that of 25 percent. All the States, counties, and cities, the political subdivisions, are restricted by State constitutions. In the event of serious trouble, the only Government that heretofore has been able to bail us out and do what is necessary would, if the limitation were adopted, be restricted in its operations. For that reason I think it would be very bad. What do you think about that, Mr. Heller?

Mr. HELLER. As you spoke, I did not find myself disagreeing with anything you said. In fact, I would go beyond it. If we actually were to cut back to 25 percent today on our existing corporate and individual incomes and estate taxes, we would lose—according to a rough calculation I made a year ago—around $15 billion of revenue. It would certainly be more today. Needless to say, this has to be made up somewhere.

If we follow the tax path, it leads pretty straight to a broad-based consumption tax of some kind, presumably a sales tax. This may very well be exactly what some of the backers of the 25-percent limitation amendment have in mind. From that standpoint it runs counter to our whole tradition of progressivity in taxation and to the whole democratic structure of income distribution. Moreover, in peacetime such heavy reliance on consumption taxes would make serious inroads on the mass-consumer markets which provide the ultimate base for a full-employment economy.

Representative PATMAN. It is true that these amendments vary somewhat in form. I have read every one of them. In most of them there is a provision that in the event of war a three-fourths majority of Congress may suspend the limitation.

The CHAIRMAN. That is, that the Congress could.

Representative PATMAN. That is setting a bad example. That is endorsing minority control. In a democracy I think the majority should rule. Why should we set up any standards whereby a minority would have absolute control of the House or Senate?

For instance, we are now at war with Korea. That war, I think, was accepted by unanimous consent. I don't think a single Member of the House or Senate said a word of opposition to it until later on; when it became a little unpopular in some quarters, some began to criticize.

But now I don't know but what we would have trouble making the appropriations to carry on operations if it required three-fourths of the Members of the House and Senate.

I think that it is equally as bad in a democracy to have minority control as to have the limitation.

Mr. HELLER. As I recall, it is three-fourths of both Houses of Congress.

Representative PATMAN. That is right.

Mr. HELLER. It is not only of those present but of all Members.

Representative PATMAN. That makes it doubly bad, because it is so seldom we have all Members present in either House. Under that proposal, it has to be a constitutional three-fourths of the Members elected to that body, which wouldn't require many to obstruct absolutely.

The CHAIRMAN. And also unless the amendment established a new cloture rule for the Senate, you would never get it through.

Mr. HELLER. Mr. Patman, may I make one comment about the illusions under which I think some States are operating that have supported this amendment? I understand, by the way, the actual number whose memorials to Congress are firm and solid is only about 15 instead of the 26 claimed by the groups pushing for this amendment.

Representative PATMAN. But even those 15—I wonder if they realize this would be driving the Federal Government into the very areas of taxation that they now occupy. It really would not open up the income tax to them because they can't impose high rates of income taxation.

As I understand, some additional ones may rescind. At one time there were more States approving. I took it upon myself, just as a poor humble Member of the House, to make a few speeches and send those speeches to the 7,500 members of the legislatures of the 48 States, and some of these States that had passed this amendment actually passed an amendment stating they were opposed to it; in other words, to cancel it or wipe it off the books. They didn't want to be certified as being in favor of that type of amendment. I think it was seven States that did that.

Investigation will disclose that not a single one of those amendments has passed the legislature of a State after full, free, and fair discussion. Every one of them has passed right at the end of a session, when the opportunity for public consideration was limited.

In one legislature they were ready to pass it; maybe they were foolish in inviting me, but I went over to that legislature and answered questions. One plea I made was, like you did just now, about the taxing power. That legislature, although they were ready to pass it, decided not to pass it. If a Member as ineffective as I am can persuade them against it, I know that when the legislatures and people get the truth and logic and reason against it, very few States will pass or insist upon it. But unanswered, it has an awful appeal. It wouldn't surprise me, if the Congress submitted that amendment to the States, they would probably adopt it right off without sufficient consideration and debate on the theory that the big bureaucracy in Washington ought to be stopped, and if we stop them from taxing, we can tax in our State. It has a tremendous appeal, but when you analyze it like you have, I think the good arguments are all against it, but it is an issue that has got to be met in a forthright manner right away, right now.

This committee, realizing that, has been making a study, which I hope will be available very soon, and that we can begin to circulate this information and place it where it is needed.

The CHAIRMAN. Now let me say for the record that that pamphlet is wholly objective in its purpose. It does not attempt to take sides on this issue, but does attempt to gather together in one compendium, so to speak, all of the facts which seem to have been developed so far.

Representative PATMAN. Since Senator Flanders is interested in this as well as other members, I would like to ask if any of the other members of the panel would like to express an opinion on this proposal.

Mr. BUEHLER. Could I say a word?

The CHAIRMAN. Mr. Buehler.

Mr. BUEHLER. Pennsylvania is one of the States that passed the resolution, and Senator Martin, who was then Governor, vetoed the resolution.

Representative PATMAN. That is right.

Mr. BUEHLER. I think our attorney general has given out the opinion unofficially that the veto would have no legal effect.

Representative PATMAN. That would be up to Congress to decide.

Mr. BUEHLER. I presume so. I thought that was a curious twist. But I think that underneath the agitation for a constitutional tax limit is not only a resistance to the higher taxes on incomes, but also a resistance to the growing Federal budget. I have had the proposed amendment explained to me as a way by which Congress would be forced into reducing the budget, keeping expenditures down. You would have available only the revenues that could be raised under the 25 percent limitation, and therefore you would have to cut the budget. Actually, the total taxes which would be available might support a much larger budget than we now have.

The CHAIRMAN. May I interrupt to say I think from what I have seen that there is a very widespread misapprehension among at least some of those who are supporting this movement, that when the requisite number of States have passed a resolution, it will be mandatory that Congress submit such an amendment for ratification; whereas, that isn't the fact at all.

Congress would be required only to call a constitutional convention, and that convention could at the same time consider and perhaps report and recommend the amendment which was suggested here this morning, that the Federal Government be given the power to tax real property within the boundaries of the several States.

Representative PATMAN. That is under article V of the Constitution, and you are exactly right about it.

Senator FLANDERS. Mr. Chairman.

The CHAIRMAN. Senator Flanders.

Senator FLANDERS. I think this thing might be resolved by a show of hands on the part of the economists. All those in favor of this constitutional amendment, you might ask them to raise their right hands, and those opposed afterward. I can guess very clearly just how the vote would come out.

Representative PATMAN. Suppose you do that.

The CHAIRMAN. At the suggestion of the distinguished and able Senator from Vermont, the chairman invites those who are in favor of the constitutional amendment to limit to 25 percent for every individual the tax burden which may be levied in a single year upon an individual to raise their hands.

There are no hands showing.

Those who are opposed please raise their hands.

The voting is unanimously against.

Senator FLANDERS. Mr. Chairman, I would like to bring the discussion back to Colin Clark's 25 percent. I found myself a little bit dazed as I listened to the professional criticisms and arguments pro and con, and I would like to inquire of these men here whether some practical observations which I can make in a very few words are not pertinent to the question.

The question that I raise is whether there are not already strains showing as a result of high taxation which indicate that it is inadvisable to go further. Now that doesn't say the limit is 25 percent nor does it say how it operates. Take, for instance, the increasing income taxes. We find that we will have to go below the $10,000 net income group and take away and tax all income above that at a hundred percent to get our $5 billion. In other words, confiscate all incomes to a point a little below the 10,000 net income group. You would have to do that to get your $5 billion if that is an objective.

Now my first question is: Doesn't that indicate that we are approaching the limits of personal taxation?

Then I will make the case briefly as it relates to corporate taxation and ask you gentlemen whether the positions are well taken.

On corporate taxation what I think we should be seriously concerned with is its effect on risk investment. It is tied up to an extent with personal taxation. I shall take the illustration of a man in the $50,000 net income bracket and while the quantities are not pertinent, they help the illustration. He spends $15,000 on his personal family expenses.

He has left then $35,000, of this he will have to pay around $21,000 in taxes to the Government, and that leaves him $14,000 to invest.

Out of that investment, we have to finance our production and the rise of our standard of living.

He has $14,000 that he can put, if he wants to, into tax-free State, municipal bonds and get a two and a half percent return. But, suppose he feels some public obligation or hope of higher profit by putting it into a risk investment, what happens?

When I was a young fellow on a risk investment it was supposed to show a possible earning of 10 percent to make it worth while to risk. Suppose he puts it in and after 2 or 3 years it does show 10 percent?

Now, his company has earned 10 percent on the money he put in. But after that 10 percent, the Government takes half of it, so there is 5 percent left. The company has 5 percent to the credit of its stockholders. If it is wise, it won't pay out the 5 percent in dividends. It won't pay out more than a half of it. So our investor gets 2½ percent and the check for 2½ percent is sent to him. But he doesn't get to keep it all. In his top bracket, the Government takes some 75 percent of that. He has left something a little more than six-tenths of 1 percent of his investment of $14,000. He gets somewhere between $80 and $90 annually out of his risk investment of $14,000.

He has either to be a fool or a patriot or both to do that.

It sems to me that constitutes a strain on our economy, a strain on our way of life, a strain on our future, and that is quite irrespective of whether 25 percent is a critical point or not.

The strains are already here at our present rate and the kind of personal and corporate taxation we have.

I wanted to throw out those two situations, if I may, for any comments you may have.

Mr. HELLER. Mr. Chairman, may I address myself to the first of Senator Flanders' two questions about the necessity of confiscating all income above $10,000 in order to get the five billion of taxes. I think we should make clear that the figure of five billion is not taxable income.

Senator FLANDERS. I think I expressed it so. I intended to.

Mr. HELLER. If one were to move to adjusted gross income before deductions and exemptions, the picture doesn't look quite as grim. After taxes people above the $10,000 level had left some $28 billion this year in adjusted gross income in 1951. I think that is pertinent to mention.

Furthermore, neither figure covers those items of income which are excluded from taxation, for example, returns in the form of percentage depletion, returns in the form of tax-exempt interest on State and local bonds, returns in the form of certain parts of capital gains, so that those are not in the tax base.

Senator FLANDERS. They are not in the tax base. On capital gains, if you consider that as a loophole, it is the only way in which an investor in the future of the country can make any investment worth while. Since special treatment of capital gains is now being looked on with suspicion and perhaps will be made very much more drastic, we are thereby penalizing more drastically the only way left in which risk investment is a possible thing for an investor of any size to consider.

Mr. HELLER. Then at least for the present, you would have to increase your category by one—fools, patriots, and those who can make capital gains.

Senator FLANDERS. You think, then, that capital gains men are in good company.

The CHAIRMAN. May I say the principal argument I have heard about the alteration of the capital gains tax formula has to do with the length of the period during which a capital gain may be acquired. The argument is made that, when the period is short, it encourages speculation and not investment, but, when the period is long, it is an actual capital gain and not a speculative gain.

Senator FLANDERS. I wouldn't advise a man of mature age to make any risk investments because he might die before that period has expired.

Mr. HELLER. I don't want to take too much of your limited time. I want to mention one other thing which makes the tax system a good deal less progressive than we assume when we look at the rate structure alone.

For 1951 we find that 70 percent of the surtax net income of all taxpayers is to be found in the first surtax bracket of $2,000. An additional 11 percent is to be found in the second $2,000 bracket. So we find only 19 percent of all taxable income subject to Federal individual income tax rates exceeding 24.6 percent.

Or, put another way, a married man with three dependents, using the standard deduction, has to have an adjusted gross income of more than $12,000 to become subject to a marginal rate exceeding this 24.6 percent. The single person without dependents with the same $12,000 income will be subject to a marginal rate of 42 percent.

Senator FLANDERS. What you are trying to say is, that in general, the $10,000 net income fellow is really getting more than that.

Mr. HELLER. That is correct; that he is paying less than he appears to if we look just at the progressive rate scale.

Just to sum up, the implication of my comments is that there are lots of things in the structure of the income tax that need to be corrected to bring its actual impact more into line with its apparent impact. As it stands, its actual weight on many taxpayers is less than its apparent weight.

The CHAIRMAN. I think Professor Friedman would like to comment.

Mr. FRIEDMAN. I would just like to make a brief comment on Senator Flanders' comments. It seems to me the essential strain on the economy arises not from taxation, but from the expenditures. The real strain on the economy is the size of the Government budget and the fraction of the total resources of the community devoted to Governmental purposes, and not available for private purposes.

The CHAIRMAN. It was stated here yesterday—and I thought very cogently—that, even if Government expenditures are substantially reduced and the rate of private expenditures, which we have had during the past years, the past 2 years, were continued, we would still have a substantial inflationary pressure. That was borne out by the other testimony submitted to this committee to the effect that business expenditures have substantially been higher than they have ever been before.

Mr. FRIEDMAN. The point I had in mind was, taxes are really a means of keeping down the strains of a large Government budget. I think there is little dispute with the general conclusion that the higher the Government budget, the more the strain on the economy.

While a precise figure, such as 25 percent cannot be accepted, surely the more you spend, the more the strain on the economy, the greater the difficulty of getting people to release the corresponding quantity of resources. Beyond some point you will surely get to some kind of an eruption and it may well take the dark envisages, namely, rampant inflation.

Secondly, I think many of the problems that your comment raises, which I think are very real problems, reflect not so much the level of the expenditure as the form that our tax system has taken. I think our tax system has placed altogether too much weight on corporate taxes; indeed I am not sure that there should be any corporate taxes. The ultimate taxpayer is the individual citizen and I would like to see him taxed directly. While I believe in a progressive tax system, there is a problem of the right amount of progression from the long point of view of attracting risk capital and providing the necessary incentives. I think we have probably gone too far in the direction of reducing the incentives not only of the people who are in the risk capital category but also of many managers and executives.

So I would say the fundamental strain is on the side of expenditures. It is a mistake to look at taxes alone, because the strain on the economy would be greater with the same budget and smaller taxes, because of the resultant great inflationary pressure. On the tax side, the problem is not so much the level of taxes as the structure of the system.

The CHAIRMAN. It might be a little beside the point, but there has been substantial evidence before this committee in the past that one of the principal hindrances to the investment of risk capital is that modern business, because of technological and scientific advances, requires such large amounts of capital that the individual finds it difficult to finance any new enterprise as an individual. He must be associated with others. The banking system to enable that association of investment is inadequate. So risk capital now is being channeled largely through insurance companies, investment trusts, and, to some extent, by local investment corporations and State corporations, such as the Maine, New Hampshire, and, I think, now the Massachusetts law, is about to render possible.

Senator FLANDERS. I am sorry I must go, Mr. Chairman.

The CHAIRMAN. Have you completed your questions?

Senator FLANDERS. I have absorbed all that can be given me within the budget of my time. If more is said on this subject, I will read it with interest in the record.

The CHAIRMAN. I hope you are not going out with a deficit of information, sir.

Mr. MUSGRAVE. Mr. Chairman, may I say a word about this.

I am a little perplexed that at this, of all times, we should worry so much about the level of private investment not being adequate. If we had had this discussion in the mid-thirties and had now concluded that Federal taxes should be cut so that private expenditures on consumption and investment would rise, then this would have been perfectly sound reasoning. Also I think that there will again come a time when the major defense effort will be over, when we will be concerned again with assuring that we do have a sufficiently high level of private investment to utilize our resources.

But this is not our worry now. If I am correctly informed, last year's private investment was at a record rate not only in absolute amount, but also as a fraction of the gross national product.

At this point, if anything, our concern is to avoid excessive private investment expenditures as well as it is to avoid excessive consumption expenditures. The function of taxation in this sort of a situation is to hold down private expenditures. That includes private investment expenditures as well as private consumption expenditures.

The difficulty with the corporation taxes at this stage is that they may give rise to wasteful expenditures and may have bad effects on wage policies, and so on. Something may have to be done about this. But I do not follow why we should be concerned at this point about private investment being too low.

Also I would like to say a word about this term "strain." This might appear rather shocking, but I would like to suggest that, if we think of a tax as being a means of holding down the strain which arises from public expenditures—that is to say, the public use of resources—we might also define public expenditures as being a means of holding down the strain which arises from private expenditures, that is to say, the private use of resources.

Now, I do not mean to say at all that in a private-enterprise economy, in a free economy, which we wish to have, there may not be a problem of taxable capacity, tax burden or friction and distortion at some point. Surely there is. But there is so much polemical content in this very term "tax burden," or "tax strain," that we must not forget that there is another side to it.

The CHAIRMAN. Let me change the trend of the discussion a little bit.

Professor Cleveland this morning—and I think you also, Professor Musgrave—referred to expenditures abroad, particularly point 4 expenditures. There is no reason to believe, I suppose, that ethical and moral standards are any higher abroad than they are at home. I would like to ask each of you to discuss, from your experience as well as from your professional background, the possibility of predicting the contributions that we make out of the tax burden, if I may use that word, Professor Musgrave.

Mr. MUSGRAVE. I am sure you do not use it with a bad implication.

The CHAIRMAN. I am talking about the contributions we make out of our tax receipts to both military and economic aid abroad.

When the defense appropriations bill was before the Congress last year, I wrote an amendment to that bill which was unanimously adopted, I am happy to say, to provide that every procurement contract should contain a clause making the contract subject to cancellation if it were found that the contractor had offered or given any gratuity to any officer or employee of the Government for the purpose of securing the contract in the first place or securing favorable treatment under the contract in the second place.

That was designed to put a padlock on the barn door before the horse was stolen by raising a perfectly obvious penalty against influence peddling or graft. So far as I know, there are no such safeguards abroad. I think we have no reason to believe that people and Government officials in other areas abroad have any higher standards than the standards which exist here in the United States.

I recall your reference to India this morning, Professor Cleveland. I think it was you who spoke about the inadequacy of the aid that was given there. But I have the very distinct feeling that the record will show that the British Government in India and also in Egypt, instead of educating the people in the processes of democracy, was actually supporting the ruling class, the maharajahs of India having lost none of their prerogatives by which they exploited the masses of the people of India under British dominion.

I think one of the reasons now that there is so much turbulence in Egypt is the fact that King Farouk and his nobles are—well, they are not distinctive for their regard for the poor people of Egypt.

You served in the Economic Administration, and I think Professor Musgrave served abroad. I would like to have you discuss that.

Mr. CLEVELAND. Mr. Chairman, I would like to comment on what I take to be two rather distinct points which you have made. One is the question of the protection of American aid funds from misappropriation, misuse by foreign officials. The second point, really the much broader and far more important question, I think, is of the extent to which we can use aid, should use aid, can use aid, to avoid making worse a bad political and economic situation in a country—for example, bad income distribution.

On the first point, I certainly agree with you that we cannot expect any higher standards of conduct on the part of foreign officials than of our own. I should think we certainly should try to exact as high a standard as we try to exact from our own. However, there isn't much one can do, I suppose, beyond a certain point in the process.

A lot depends on the way in which the aid is given. If the aid is given in the form of money, it is turned over to the treasury of a foreign country and the controls beyond that point are not special controls relative to American aid. Such controls would not be very practical. It is a question, then, of the Government's internal accounting and accountability procedures. If those are bad, if the Government is highly corrupt, and if we are in a position to do something about changing its whole manner of conducting its fiscal and financial affairs, then I suppose we should do it.

Obviously, there are limits to that. The question is how much leverage do you have, how anxious are you to get other concessions for the aid you are giving, just what is the total political bargaining situation between your government and theirs.

To the extent we give the aid in the form of goods for which we authorize the contracts in this country, as was done, for example, in the European recovery program, our responsibility and control is far greater, and we have a greater responsibility, a greater opportunity, to prevent bad use of funds. I don't mean to imply that I think that is a good reason for always giving aid in that form. I don't think it is, because they may not misappropriate our funds, but they may misappropriate other funds.

Perhaps the importance of the thing as a moral issue is not changed by whose money it is. It is certainly somewhat changed from our political point of view, however.

To turn to your second point, Mr. Chairman, it does seem to me that this is really one of the key, central issues that we have in connection with our foreign aid programs, and in our foreign policy generally. We are in the position of having from time to time to support, by economic or military aid or even by more direct means, governments which are, in our book, not very nice governments. I think we do it sometimes with a striped pants, kid glove attitude, which is unfortunate. I think there are probably many situations in the world where our leverage is sufficient—not only the leverage given to us by our aid, but our total position with respect to particular areas—where we could obtain action of an economic reform character far more than we have ever done.

The famous case of China is one of those. If we had really applied ourselves to that problem, instead of telling ourselves why we couldn't do anything, why we couldn't intervene more actively, it might have made a difference. I don't know. That is history.

It is probably true in parts of Asia now. But I don't think we can afford to blind ourselves to the fact that we are not going to remake completely foreign governments in the image of what we consider to be the proper way of conducting their affairs. We are certainly not going to remake foreign societies.

Questions like land reform, income distribution, and so on, in foreign countries are frequently not matters that governments can legislate about. They are matters, in some cases, that would take a revolution to accomplish; that is, to accomplish what we would like to see accomplished.

In those cases we have to weigh the consequences of our action when we support governments which are in this kind of situation. Can we work for reform, can be afford to let the situation deteriorate, maybe get our revolution? Maybe that will help, maybe it won't. Maybe it will be the wrong kind of revolution, et cetera.

I am saying what is perfectly obvious—that you face situations in foreign countries where you have to make the best of a bad job, making choices of evils, as you often have to do in politics.

I think the Indian case is one of those. I agree with your general comments about British policy. I don't think that we are in a position to do a great deal better than the British. We don't have anything like the leverage they did, of course. We can urge land reforms, we can point out the political explosions that will result if reforms do not take place. We can put pressure up to a point. After that pressure, it will be evident that there isn't a great deal more you can do.

The CHAIRMAN. Aside from the question of policy, the primary question for discussion here today, I suppose, is the inflationary effect of these expenditures.

Did I understand you to take the position this morning that the fact was that it made very little difference so far as the inflationary effect was concerned whether the expenditures were made by way of a military program or as economic aid?

Mr. CLEVELAND. I don't think it makes an enormous difference. Of course, it may make a difference for some bottle-neck scarce materials. It may make a difference for certain types of machinery or equipment, which are in short supply particularly, but the general inflationary effect should not be very different.

I would defer on this question to Arthur Smithies across the table.

Mr. SMITHIES. I think Mr. Cleveland's answer is right. I think it depends upon the particular commodities. If we use scarce copper in order to provide military goods to Britain, that may be more inflationary than providing cotton textiles to Britain or Europe. I don't think whether it is military or civilian makes much difference.

The CHAIRMAN. It seems to me that both of you are taking the position that expenditures for military purposes, which are not productive purposes, are no more inflationary than expenditures for the strengthening of an economy, which could be expected to increase and stimulate production.

Mr. SMITHIES. I think you are carrying the argument rather further than we were. We were talking about the immediate impact on the United States. If you go a step further, I think you are quite right. Military expenditures in that sense are more inflationary in the long run than the expenditures that increase the productive resources either here or abroad. If that is your point, I agree with it entirely.

The CHAIRMAN. Yes, it is.

Mr. SMITHIES. That any military expenditure in the long run is more inflationary than any investment expenditure, because the investment expenditure will result in increasing output.

The CHAIRMAN. What I am trying to illuminate is the feeling I have that Russia is carrying on what we call the cold war against the free nations, but it is actually an economic war, and the basic purpose of the Russian policy is not to take over the world by military invasion per se, but rather by creating the economic conditions or stimulating the economic conditions which the Russian philosophy believes are inseparable from capitalism; that is to say, their purpose is to promote deficits in free countries in order to create the climate in which depressions may occur, in which class conflict can develop, and in which free government and the system of private property are likely to perish.

When one looks around the world, one sees that precise pattern working out.

The Russian military power is not being committed anywhere. The Russians use force, of course, at home against individuals and in the satellite countries against individuals to prevent any deviation from the party line.

They use all of the devices of the conspirator to create these adverse conditions in the free countries, all for the purpose of promoting depressions, hastening depressions.

Therefore the question arises, if we assume that to be correct, in other words, that an economic war is being waged against us, doesn't it boil down to the fact that our principal aim should be to take every step in the world necessary to prevent a deficit or to prevent inflation or to prevent those things which we do know bring about the economic distress which promotes revolution.

Mr. SMITHIES. Can I say a few words in answer to your question, although not directly?

The CHAIRMAN. Please do.

Mr. SMITHIES. I take it, you are concerned about the size of the commitments we may be compelled to make in terms of foreign aid and the inflationary consequences.

The CHAIRMAN. We may be promoting inflation in Western Europe, the very area which we are trying to preserve from Communist aggression, by military expenditures.

Mr. SMITHIES. I agree very much with the general spirit of Mr. Cleveland's remarks this morning, but I am generally perplexed by the foreign-aid question. It seems to me that we must contrive some method—and here I think I am coming to your point—to limit our liability in respect of foreign aid because, if we do not have some rules of the game established, giving aid can work to our disadvantage.

We do not get credit for the amount of aid we do give, we get discredit for the amount we do not give. It may be one of the Russian tactics to get us into unlimited commitments.

I agree with Mr. Cleveland that India is a major area for our attention, but I get perplexed when I talk to Indians about this subject. They are apt to take a point of view that the only limit on the aid we should give to India is the amount of aid that will raise the Indian standard of living to the United States standard of living or reduce ours to theirs. They see no limit short of equality of conditions.

For our aid program to be a success, I think Mr. Cleveland will agree, we must make only limited commitments and we must get other countries to agree that this is the limit of our responsibility: That is why I think the point 4 program was very soundly conceived, since it placed emphasis on other things than merely amounts of dollars. I think it may well have been congressional concern that steered the point 4 program away from dollars pure and simple and toward technical assistance.

I would feel very uneasy if our foreign policy consisted exclusively of writing blank checks to people, because I think that would play into the Russians' hands and would produce the unfortunate consequences that you are talking about.

There is one further point I would like to note before I close. That touches on your other remarks about supporting the wrong people and supporting unequal distribution of income. We are all concerned about the character of some of the governments that we have to deal with, but it is worth recalling that whether formally or not, there is an Anglo-American partnership in this business and what frequently happens is that, if we do not give aid to a country, Britain does give aid to it, and we give aid to Britain.

During the ECA period the sterling balances that Mr. Churchill has now discovered should have been canceled, were used for that purpose. Britain gave aid to India by letting it spend its sterling balances and getting goods from Britain. Great Britain's standing in the sterling balance was a factor in our giving aid to Great Britain.

The CHAIRMAN. Shouldn't we learn something from Britain's experience?

Mr. SMITHIES. There is a question as to whether we should blind our eyes to these unpleasant facts by letting Britain furnish the aid, or we should do it ourselves. I had a professor from a Syrian university in our office the other day, discussing this matter with me. What he said was, leaving out present policies entirely, just getting back to the history, that Britain cannot escape from its history in the Middle East and any British investment dollar that goes into the Middle East will be viewed with suspicion. There isn't the same history with respect to the United States.

Our investment dollars in the Middle East might do some good, whereas British investment dollars might do some harm.

I felt that was a rather significant point that one might bear in mind.

The CHAIRMAN. The Kremlin is busily engaged in its propaganda program to convince the peoples of Asia and north Africa that we are merely ambitious to step into the vacant shoes of British and colonial imperialism.

Mr. SMITHIES. I think it is highly important that we should have a propaganda program—not only a propaganda program—we should have a policy that indicates the contrary to be true.

The CHAIRMAN. Then it is clearly your opinion that we should not do the dirty work.

Mr. SMITHIES. No. It is clear that we should work as cleanly as possible.

The CHAIRMAN. We better have a definition, then, of "dirty work." What do you mean by "dirty work"?

Mr. SMITHIES. What I mean is——

The CHAIRMAN. You do not really mean it is dirty work.

Mr. SMITHIES. No. What I mean is we have to deal with some governments, that we do not like particularly. We should make the best of it and try to get them to reform their ways as rapidly as possible.

The CHAIRMAN. Are there any other comments on this matter?

Mr. CLEVELAND. Mr. Chairman, I might just add one thing to my remarks this morning about economic versus military aid. I agree, I think, substantially with what you said a minute ago about the danger of pushing the European governments too far for military expenditures and getting chronic inflation growing there in the next 2 or 3 years. That is a serious danger. We should give economic aid sufficient to cover their needs and to prevent too serious internal inflationary pressure.

It also means we shouldn't push them too far on military expenditures. I think actually there is more smoke than fire here as far as the strictly economic aspects are concerned. There has been a great deal of talk about pushing the Europeans to higher military expenditures. Outside of Britain, the amount to which their military expenditures have actually increased is not really very great. The real danger is more in the political realm than in the economic; that is, that our pressure on them for military purposes, our identification in the minds of the European public with exclusively military aims, puts us in a bad light and does, in a sense, assist the Communists in their propaganda and political efforts. The remedy for this is not to forget the military, but for the United States to put far more emphasis on positive ends, such as European federation and the achievement of better income distribution in the continental European countries.

The CHAIRMAN. Are there any questions, Congressman Bolling?

Representative BOLLING. No.

The CHAIRMAN. Any further questions, Mr. Patman?

Representative PATMAN. No. Thank you, sir.

The CHAIRMAN. Unfortunately, Professor Miller was called away, so it has been impossible to pursue some questions that were indicated at the outset.

Mr. Blough is gone. Therefore, there would be no point, perhaps, in asking about your quotation this morning from the record of the Economic Review and the implication you drew from it. He seemed to be shifting a little bit in his chair and I was going to give him a chance.

Mr. Buehler. We talked about it and he said he disagreed with my interpretation. The point I was trying to make was this: As I read the Economic Review, there was to me in the recommendations and forecast the implication of continuing inflation, Dr. Blough said that they had in mind methods of voluntary saving and other measures which would curb the inflation.

Of course, if the voluntary saving were successful and Government policies were able to offset the deficit by inducing people to save rather than spend, yes, you would handle the deficit in a noninflationary way. But I personally have some doubts about the ability of the Government to get all that money in a noninflationary way.

The Chairman. I checked the statement to which you referred from the Economic Report. It is to be found at page 135, and it reads as follows:

> The alternative to relying upon the conventional tax sources for the additional revenue requirements would be to introduce a new broad base tax. One new type of taxation which could raise substantial amounts of revenue is a general sales tax. Whether imposed in a frank manner upon retail sales or disguised as a general manufacturers' excise tax, the result of it would be a portentous departure from national tax policy which should not be considered at this time.

To me, that seems to be an argument against the sales tax or against the manufacturers' tax and not an argument for continuous inflation.

Mr. Buehler. The reason I thought inflation was implied, Senator, was that the Council proposes only about 4.6 billion in additional taxes. Additional borrowing would be required because a cash deficit of 10.4 billion is now anticipated in the fiscal year 1953. A similar cash deficit is apparently being forecast in the fiscal year 1954, unless new taxes are imposed.

The Chairman. It would seem as though we were coming to the close of this discussion.

I wonder if it would be a proper summary of the consensus of opinion of the panelists if I were to say that there seems to be a general opinion, one, that national defense expenditures are necessary and must be accepted, but that they should be held to as low a limit as possible; second, that economy should be pursued throughout the Government, that, if there be a deficit, that is to say, a necessary expenditure greater than the revenue, the proper way to clear away that deficit would be, first, to get it by way of taxation, lacking revenue in taxation which would balance the budget and prevent inflation, we should take whatever steps are necessary by way of controls to prevent the inflation.

Professor Friedman, however, felt that monetary and fiscal policies would be sufficient to prevent inflation, except perhaps in the allocation of scarce materials.

Representative Patman. You might add to that, Mr. Chairman, that in the event it is necessary to borrow money, it should first be borrowed from savings of individuals, not banks.

The Chairman. Yes. I think that is a proper addition.

Mr. Friedman. On that last one, it should be borrowed in a way that does not promote inflation, whether from banks or individuals.

Representative PATMAN. You know it is more inflationary from banks.

Mr. FRIEDMAN. From the Federal Reserve bank.

Representative PATMAN. Any bank, commercial bank. That is the most inflationary way, I guess, in the world, of borrowing money. I don't know as much about it as you gentlemen do.

I think it would be equally inflationary as borrowing from the Federal Reserve.

Mr. FRIEDMAN. I am afraid we are verging on a technical topic we ought not to go into at this time.

The CHAIRMAN. I was going to add one more. In these circumstances, the assumption of necessary military expenditures, the Colin Clark theory of a 25 percent limitation on total income to be diverted by taxation is not supported by the panel.

I see no dissent.

Upon that note, then, unless there are further questions, the Chair will thank the members of the panel for their participation on behalf of the committee and himself. I think it has been a very helpful session.

We have appreciated particularly the testimony that was given this morning and your very ready and lucid answers to our questions this afternoon.

Perhaps you want to be invited, as were the panelists yesterday, to provide for the record an additional statement, if you so desire. I think probably each of you can do this. Didn't I put a one-page or two-page limit on it yesterday?

Mr. ENSLEY. One page.

The CHAIRMAN. A one-page summary of your views as a result of the whole discussion. I think it would be helpful to have that inserted in the record.

(The material referred to is as follows:)

SUMMARY STATEMENT OF ALFRED G. BUEHLER

The panel discussion has clearly indicated a number of major issues in Federal fiscal policy. Federal expenditures, primarily on account of the national defense program, are running substantially ahead of tax revenues. Unless sizable cuts in the budget can be accomplished, it can be balanced only by increasing taxes.

The deficit has inflationary consequences because it is bringing new funds into circulation faster than production and supply are increasing. The larger the deficit, the more serious its inflationary effects will be.

The Nation has not reached the economic limits of taxable capacity but there is very strong psychological and political resistance to further tax increases. The recent sharp tax increases have made the citizens more fully aware of the costs of the budget. There is now an inclination to yield to deficit financing and more inflation as a way to avoid higher taxes. But this will increase further the cost of living and compel the citizens to pay for deficit-financed expenditures through higher prices.

In this emergency we should spare no effort to remove waste from the budget by administrative and legislative economies. Large cuts in the budget can be achieved, however, only by sacrificing some of the less essential public services. If the Government and the citizens are unwilling to remove waste from the budget and forego some services, the Nation should be willing to balance the budget by raising taxes.

Inflation knows few or no exemptions. It is more inequitable and more burdensome on the lower incomes than any rationally conceived tax would be. To curb inflation, any excess of Federal expenditures over taxes, considering at least the cash payments to the public and cash receipts from the public, should be met by additional taxes which will lessen private spending sufficiently to offset that excess.

Private saving should be encouraged, private spending discouraged. Monetary and other policies should be directed toward checking inflation. Fiscal policy alone will be inadequate.

SUMMARY STATEMENT OF RICHARD A. MUSGRAVE

There are two distinct aspects of the current fiscal problem: (1) Can or should expenditures be reduced, and (2) what measures of tax policy are required?

(1) I am not in a position to judge how severely our defense effort would be damaged by program cut-backs below the proposed budget figures. Therefore, I am inclined to accept the proposed program. Surely, our economy is in a position to sustain this effort if it is needed. However, it is obvious that all should be done to enforce efficiency and economy in military expenditures. I doubt whether we now have the governmental machinery to do so.

The civilian program occupies so small a part of the budget that cut-backs, even if drastic, will not change the picture greatly. While some cut-backs or postponements might be called for, I am opposed on the whole to a sharp reduction in our standard of civilian public services.

(2) Assuming the expenditure outlook to be as proposed in the budget message, I believe that taxes should be raised to provide for a pay-as-you-go policy. While I do not feel that the revival of strong inflation pressures is imminent, it is more likely than not that such pressures will reoccur as defense spending reaches its peak rate. The main burden in forestalling such a development is on tax policy. Direct controls, necessary though they are, must be relieved; and restrictive monetary policy cannot be very effective in a situation where large new Treasury financing is needed. Hence the need for additional taxation.

I place little store in the argument that the over-all rates of taxation, needed to place defense on a pay-as-you-go basis, will be beyond the country's "taxable capacity." The economy's performance, and the continued high level of civilian consumption are evidence to the contrary. Up to perhaps $5 billion of additional yield may be obtained through piecemeal legislation, including provision for mandatory joint returns (or its equivalent), curtailment of standard deductions, tightened treatment of capital gains, reduced depletion allowances, and so forth. Beyond this, additional sources of tax revenue may have to be opened, drawing on the mass of consumers in the middle and middle-lower (though not lowest) income groups. One of the most important problems of tax policy is to devise techniques by which additional taxation, imposed on these groups, may be distributed equitably.

The CHAIRMAN. The next session of the committee will be held tomorrow morning at 10 a. m. in this room.

This will be a panel discussion on Federal direct controls. The participants will be: Jules Backman, New York University; Kenneth Galbraith, Harvard University; Griffith Johnson, Motion Picture Association of America, Inc.; Richard Lester, Princeton University; Edward Mason, Harvard University; Lloyd B. Reynolds, Yale University; and Stanley Ruttenberg, CIO.

The committee is now in recess until tomorrow morning at 10 o'clock.

(Whereupon, at 4:35 p. m., the joint committee recessed to reconvene at 10 a. m., Friday, February 1, 1952.)

JANUARY 1952 ECONOMIC REPORT OF THE PRESIDENT

FRIDAY, FEBRUARY 1, 1952

CONGRESS OF THE UNITED STATES,
JOINT COMMITTEE ON THE ECONOMIC REPORT,
Washington, D. C.

The joint committee met, pursuant to adjournment, at 10: 30 a. m., in room G–16, United States Capitol, Senator Joseph C. O'Mahoney (chairman) presiding.

Present: Senators O'Mahoney, Sparkman; and Representatives Patman and Bolling.

Also present: Grover W. Ensley, staff director; Theodore Kreps, economic consultant, of the staff; and John W. Lehman, clerk.

The CHAIRMAN. The committee will come to order.

Unfortunately, a large number of members of the committee are unable to be present with us this morning, but fortunately we will have the printed record.

It may be possible to expedite the presentation this morning if the members of the panel, as they are called upon—and I shall call upon them in the order in which I understand they have themselves agreed would be satisfactory—would keep their opening remarks to a minimum.

We have had a 5-minute rule which has been honored more in the breach than in the observance, as the old quotation goes, but if we do hold down these opening statements then it will be possible to develop a better interchange later on.

The committee has found it very helpful just to go around the table, have the opening statements, reserve questions, for the most part, until after the opening statements have been made, and then seek to develop by interrogation, not only by members of the committee of the panelists, but by the panelists themselves, among the whole group. The purpose, of course, is to develop the most objective results that we can, considering the limitations of human nature.

Before I start, I might announce that Secretary Lovett and the three civilian Secretaries of Defense have been invited to appear at a public session of the Senate Subcommittee on Appropriations on Monday next at 10 o'clock. This meeting will be held in the caucus room of the Senate Office Building. Members of the Joint Economic Committee are being invited to attend.

The purpose of that public session is to afford Secretary Lovett, whose ability and objectivity, I think, are well recognized, to explain the steps which have been taken in the preparation of the military budget, the considerations which have been taken into account, the judgments which the civilian leaders of the Department of Defense have with respect to the capacity of our economy to sustain the drain on manpower and material resources which will be required, to discuss the period over which the preparedness program may be expected to continue, and, in short, all of the economic features.

The Secretary will also discuss the steps which have been taken to eliminate unnecessary expenditures, the weight which is given to the types and kinds of weapons which will be purchased in the military procurement program.

The discussion this morning leads directly up to this meeting on Monday, because here we have the general subjects of the effect upon the structure of American business of the mobilization program as it is by a stabilization program.

We have the question of our human material resources, and what the general outlook is of the various controls.

Before we begin, there will be inserted in the record the biographical sketches of the panelists.

(The document above referred to is as follows:)

PARTICIPANTS IN THE PANEL DISCUSSION ON FEDERAL DIRECT CONTROLS, FEBRUARY 1, 1952

BACKMAN, JULES, Professor of Economics, New York University. Research organization: Brookings Institution (Studies of wartime controls); The National Industrial Conference Board (studies of wages and prices); New York Times (formerly editorial writer on economic problems). Government: Securities and Exchange Commission; President's Cost of Living Committee (technical adviser to industry members); New York Milk Shed Price Committee; O. P. A. (consultant). Industry: Economic adviser to: Basic steel industry in national wage cases; railroads in national wage cases and general rate cases; Surety Association of America re surety rate making, retailing in price and wage problems and others. Also have made special studies of the following industries: Cotton textiles, potash, frozen foods, baking, bituminous coal, and several others. Writings: Numerous books and pamphlets dealing with wages, prices, war controls, and industry economics. Just published, *War and Defense Economics* (editor and co-author) (Rinehart). Also *Government Price Fixing* (Pitman); *Wartime Subsidies; Wartime Price Control* (New York University); *Multi Employer Bargaining* (New York University); *Economics of the Cotton Textile Industry* (The Conference Board); *Behavior of Wages* (The Conference Board).

GALBRAITH, JOHN KENNETH, economist; b, Iona Station, Ont., Can.; B. S., Univ. of Toronto, 1931; M. S., Univ. of Calif., 1933, Ph. D., 1934; student, Cambridge Univ., Eng., 1937–38; Asst. prof. economics, Princeton Univ., 1939–42; econ. adviser, Nat. Defense Advisory Comm., 1940–41; asst. adminstr. in charge of Price Division, Office of Price Adm., 1940–41; dep. adminstr., O. P. A. 1942–43; mem. bd. of editors, Fortune Mag., 1943–48. Director, U. S. Strategic Bombing Survey, 1945; dir., Office of Economic Security Policy, State Dept., 1946. Fellow Social Science Research Council, 1937–38. Prof. of economics, Harvard, since 1949. Author: Modern Competition and Business Policy, 1937; The Economic Effects of the Federal Public Works Expenditures, 1940.

JOHNSON, G. GRIFFITH, Harvard U., A. B., 1934; A. M., 1936; Ph. D. 1938, Research assistant, Div. of Research and Statistics, Treasury Dept., 1936–37; Assistant to Fiscal Assistant Secretary, Treasury Dept., 1937–38; Assistant Director, Study of Economic Effects of Federal Public Works Expenditures, National Resources Planning Board, 1939; Economist, Industrial Economics Div., Dept. of Commerce, 1939–40; successively, Chief of Steel Mill Products Section, Chief of Solid Fuels Branch, Special Assistant to Deputy Administrator for Price, Director of Consumer Durable Goods Div. of Office of Price Administration (and predecessor agencies, 1940–46; Consulting economist, Vice President, R. R. Nathan Associates, Inc., 1946–47; Director, Economic Stabilization Div., Nat. Sec. Resources Bd., 1948–49; Chief econ. and assistant division chief of Fiscal Analysis Division, Bureau of the Budget, 1949–50; Economic Adviser, Economic Stabilization Agency, 1950–52; Motion Picture Association of America, Inc., 1952–. Publications: The Treasury and Monetary Policy, 1933–38, Harvard Univ. Press, 1939. Co-author, The Economic Effects of Federal Public Works

Expenditures, U. S. Government Printing Office, 1940; Chapter entitled "Basic Materials," The Effects of Strategic Bombing on the German War Economy, U. S. Government Printing Office, 1946.

LESTER, RICHARD A., economics; b. Blasdell, N. Y. Ph. B., Yale, 1929; A. M., Princeton, 1930, Ph. D., 1936. Instr. econ., Princeton, 1931–32, 1934–38; asst. prof. econ., Haverford Coll. (one term) 1937–38; asst. prof. of labor, U. of Wash., 1938–40; asst. prof. econ., Duke U., 1940–42, asso. prof. 1942–45; asso. prof. and research asso. Industrial Relations Sect., Princeton U., 1945–48; prof. econ., chemn. econ. and social instns., Princeton., since 1948. Asso. chief, chief of branch, labor division O. P. M.-W. P. B., 1941–42; chief of branch War Manpower Commn., 1942; consultant Office of Secretary of War, 1943–44; referee, arbitrator, pub. panel mem. Nat. War Labor Board and Regional Board, 1942–45; chairman, Southern Textile Commn., N. W. L. B., 1945; mem. staff Army Finance Sch. 1943–44; staff, Com. for Economic Development, 1943–45. Author: Monetary Experiments—Early American and Recent Scandinavian, 1939; Economics of Labor, 1941; Providing for Unemployed Workers in the Transition, 1945; Company Wage Policy, 1948; co-author: Wages Under National and Regional Collective Bargaining, 1946; Labor and Industrial Relations, 1951; Constructive Labor Relations, 1948; co-editors; Insights into Labor Issues, 1948. Contributor of numerous articles to school and popular periodicals.

MASON, EDWARD S., Prof. economics; b. Clinton, Iowa. A. B., U. of Ken., 1919; A. M., Harvard U., 1920; B. Litt., Oxford U., Eng., 1923; Ph. D., Harvard U. Graduate Sch., 1925; Litt. D. (hon.), William College, 1948. Engaged as instr. economics, Harvard U., 1923–27; asst. prof. economics, 1927–32; asso. prof. economics, 1932–37, prof. same since 1937, dean, Grad. Sch. Public Administration since 1947; economic consultant to Dept. of Labor, 1938–39. Defense Commn., 1940–41; Office of Strategic Services, Washington, D. C., 1941–45; dep. to asst. sec. of State in charge econ. affairs, 1945; econ. cons. to State Dept., 1946–47; cons. to State Department; chief economic adviser at Moscow Conference, 1947; appointed by President Truman as mem. adv. com. on management improvement to assist in improving government organization. Awarded Medal of Freedom, 1946.

REYNOLDS, LLOYD G., economist, author; b. Wainright, Alberta, Can. A. B., U. of Alberta, 1931; A. M., McGill U., 1933; Ph. D., Harvard, 1936. Instr. econ., Harvard, 1936–39; asso. in political econ., Johns Hopkins U., 1939–41; asso. prof. 1941–45; asso. prof. econ., Yale, 1945–47, professor since 1947; asso. dir., Labor-Management Center, Yale, since 1945; econ. Temporary Nat. Econ. Com., summer 1940; research dir. labor studies 20th Century Fund, 1940–41; cons. Nat. Res. Planning Bd., 1939–42; research sec. to com. on employment, Social Science Res. Coun., 1941–42; chief, elec. machinery sect., OPA, 1941; reg. price exec., Phila., OPA 1942, and state administr. for Maryland, 1942; consultant to planning div., War Manpower Commission, 1942–43; dir. research and statistics div., Food Distribution Administration, 1943; public member panel chairman for textile industry hearings; co-chmn. appeals com., War Labor Bd., 1943–45. Author: The British Immigrant in Canada, 1940; Labor and National Defense, 1941; Determinations of the Volume of Employment, 1942; An Index to Trade Union Publications, 1945; Insights Into Labor Issues, 1947; Job Horizons, 1948; Economics of Labor, 1949. Contributor to journals.

RUTTENBERG, STANLEY, B. S., University of Pittsburgh, 1937. CIO organizer and field representative in Ohio Valley, 1937–38; assistant to the director of Hull House, Chicago, 1938–39; United States Army 1943–46; associate director of research, CIO, 1939–48; director of department of education and research, CIO, since 1948. Office: Washington, D. C.

The CHAIRMAN. With that introductory statement, the Chair will invite Mr. Griffith Johnson, now with the Motion Picture Association of America, Inc., but formerly with Mr. Eric Johnston, when he was the Economic Stabilizer, to open the discussion.

STATEMENT OF G. GRIFFITH JOHNSON, MOTION PICTURE ASSOCIATION OF AMERICA, INC.

Mr. JOHNSON. Mr. Chairman, my brief comments this morning will be concerned mainly with certain aspects of the part which the direct control programs have in over-all stabilization; that is, question 3 on the panel's suggested topics.

In most of the discussions relating to direct control programs, including the one before this committee last year, most of the participants take great pains to emphasize that direct wage and price controls are only a part of the required program for stabilization. Despite agreement on this general proposition, however, it seems to me that there is considerable confusion over just what that part is.

Particularly in recent months, there has been some tendency for people to separate into quite broadly opposed groups. First, there are those who take a rather dim view of the direct control programs in any event, but in this current period, looking at what has happened, particularly in wholesale prices over the last year, they tend more positively to question the need for any such controls now.

The other group are those who basically view the direct-control programs as the first line of defense against inflation. They tend to look at the monthly developments in the cost of living, and view those as the test of whether or not the direct control programs are working.

I would suggest that both of these groups have been somewhat misled by the World War II experience in this area and by the more or less implicit assumption that the objectives, and thus the structure and nature, of direct controls are or should be more or less the same now as they were then.

Those who generally feel that the need for direct controls either does not exist or is very limited at the moment remember the appalling complexity of the control structure in wartime and the aftermath of postwar inflation, while those who place great reliance on direct controls recall quite correctly the considerable success we had during wartime, the fact that that success predominantly stemmed from the direct-control programs, and that it was quite appropriate during wartime to judge the need for and the effectiveness of direct controls primarily by the movement in the cost of living. I personally do not believe that such a test is appropriate under present circumstances.

Even if we should do so, which I do not believe, we cannot duplicate the elaborate wartime structure of controls. It is not only a matter of legislation but more basically of public attitudes and thus administrative feasibility. Since we cannot duplicate that wartime structure of controls which is needed really to assure in that way stability in living costs, it follows that the objective of direct controls under present circumstances has to be something considerably less than it was during World War II, and that their performance cannot be judged by what happens month by month or quarter by quarter in important areas of the cost of living.

The stabilization program as a whole can be judged in that way, but not the direct controls part of it.

Now, this leads to the second point I would like to make. Obviously, since we cannot rely on direct-control programs basically as the first line of defense, so to speak, against price increases, particularly in important cost-of-living areas, we have to place such primary reliance on measures which repress demand to something like an equilibrium point. I am sure there would be rather little disagreement with this general proposition, but the difficulty is, as in so many things, that a program repressing demand to the necessary point involves a lot of hair-shirt measures, and I suspect that for many people the annoyances and inconveniences of a full-fledged program of direct controls are really a lot less objectionable than some of the measures which have to be taken from an over-all standpoint.

For example, it does not seem to me that stability in this type of situation is consistent with the sort of free and easy prosperity which we had during wartime, with sellers' markets across the board, with the inflation of costs, and consequently in many areas of profits, which comes from straining to bring into employment the most marginal resources of the country, and with pretty much eliminating the pressures of competition, and the frequently painful impact of those pressures on particular sectors from time to time, as we witnessed during the past year.

In other words, if we try during this defense economy to have across the board the easy money and income policies—in profits, wages, and credit—which might have been quite appropriate in wartime, we have a situation which is in my view not consistent with stability at the present time.

Now, taxation is usually given the main emphasis in this hair shirt program, and without in any way detracting from its very basic importance, I am inclined to think that this emphasis results in the neglect of some other areas in which things should be done and can be done, perhaps even more practicably than in taxes, particularly in view of the very high tax base we now have.

I might mention specifically, of course, the credit area, credit being merely a way of supplementing the spendable funds of individuals or businesses. I think we should be prepared for much more stringent measures restricting credit, not only in the general sense of the monetary policy of the Federal Reserve bank, but also on such things as consumer credit and loans, mortgage loans on existing, as well as new, buildings, and expanded authority for the Federal Reserve System.

Another area which has not received too much attention is our foreign-trade situation. We have recently developed quite a little export boom, which itself is inflationary, and I think that measures may be needed to restrain the growth or the maintenance of our export surplus, even though it means rather unpleasant repercussions on some domestic industries. If we do not do it in the direction of expanding our imports, other countries are going to do it for us in contracting our exports.

Finally, the major area is the contraction of private and public investment of less essential natures, including housing. We are now in the middle of an investment boom. The present indications are that the level of investment next year may be as high or higher than the record of this last year. While the final word on that will be given by the materials allocations, it seems to me that we should be prepared for much more drastic measures in limiting the volume of capital formation generally. I do not think we can have stability, and a military buildup such as we now plan, and a capital formation boom all at the same time.

But even if these measures were carried to appropriate lengths, there will still be, in my opinion, an inflationary problem of considerable proportions, and this is where the direct-control programs come into the picture.

The problem is that there is a broad area of the economy where the demands of the defense program, particularly during this buildup period, the demands of essential civilian and public investment, and certain consumer requirements, substantially exceed supplies, and where the over-all measures cannot be expected to repress demand to anything like an equilibrium point.

From these shortage areas, which are not in the short run susceptible to any rapid or substantial increase in supply or to any sizable contraction of demand, even from large price increases, from these areas spread out inflationary pressures on both the price and wage side, which could seriously unstabilize the whole economy. They could also distort the economy very badly by blowing up the materials and durable goods sectors, and bringing serious adjustment problems in the future.

The over-all measures, on which we have to place main reliance for stability at the consumer level, cannot handle the problems in this area, and it is for that reason that during this shortage period we must rely on vigorous direct control measures, both on the price and wage side, and on the allocations side; and I think that sometimes too little attention is given to the close relationship between the direct stabilization controls and the allocation controls, and the mutual dependence of both of them on each other for successful operation.

Now, this general picture, I think, leads to some conclusions with respect to the need for strong legislation in Defense Production Act and with respect to the standards which are used in the price and wage stabilization programs. I have taken more than my time, and I will not go into those, but I think some of the implications will come out in the later statements which will deal more directly with those problems.

The CHAIRMAN. Thank you, sir.

Mr. Galbraith?

STATEMENT OF J. KENNETH GALBRAITH, HARVARD UNIVERSITY

Mr. GALBRAITH. Mr. Chairman, when I came to collect my thoughts for this session, I found myself comparing present conditions with those of a year ago, when the committee also met on the President's Economic Report. I was struck with my absence of strong feelings on matters of economic policy—immediate changes in economic policy—as compared with a year ago. Then, as you will recall, we met at the time of a major inflationary upsurge. We were also in the middle of a major controversy of the role of direct controls. It was a period, generally, when there was a good deal of alarm and the general consensus, both of the Committee and of the round table at that time, was that strong action was going to be required, whatever the nature of that action might be.

The present position is a good deal more satisfactory—much more satisfactory. The economy in the short run is not too far out of balance. That is fortunate, considering the timing, because this is a year when strong action is not usually possible in this Republic.

On the other hand, I would like to sound a note of caution not dissimilar to that sounded just now by Mr. Johnson. While the short-run prospect for price stability is not unfavorable, in my judgment, the longer-run prospect is still, to say the least, disconcerting. I would strongly urge that there be no further weakening of direct controls.

I would indeed hope that they might be strengthened, although I realize that those of you who are practitioners of the art of the possible may have a different judgment as to the possibility of doing so at this time.

Let me advert to one of the points under discussion this morning—the structural character of the economy. This reposes an important part of the decision-making process in a relatively few hands.

This is especially so in heavy industry. There decisions on prices of great importance and decisions on wages of great importance are made in a relatively small number of corporations and in a relatively small number of collective bargaining sessions.

There has been a great deal of controversy over the extent of concentration of economic power in the American economy. To the best of my knowledge there is no real controversy over the fact that a very considerable concentration does exist. I have been working on this problem some in the last year or so, and I am impressed with the difference in the way this part of the economy works under conditions which we may be pleased to call normal as compared with conditions when the economy is under tension.

We have been saved, in my judgment, from some of the consequences of a high degree of concentration of decision or of a considerable concentration of economic power by the tendency in the economy for one position of power to be offset by another. Where we have had a strong position by companies, we have tended to get a strong position by labor dealing with those companies. There is something of the same process working in agriculture and, I suspect, that this process, which I have termed countervailing power, has had more to do with the stability of the economy in normal times than we have realized.

It is not a process, however, that works well when the economy is under the kind of tension that it has been under in the past year and a half.

Under those circumstances things become too easy. Under those circumstances disputes between strong bargaining positions can always be resolved by increases in wages and increases in prices. I suspect that as long as the economy is under tension we shall see that result. That leads me to believe that the role of direct controls in the economy at the time when we are seeking, as Mr. Johnson has said, to get at all possible return out of the economy is likely to be strategic.

Those controls at the present time, as we all realize, are not strong. Substantial measures of escalation have been built into the agricultural price controls, into the wage controls, and they have a counterpart in the industrial and retail regulations. I rather regret the extent of this softening of the controls, although quite realizing Mr. Johnson's point that we would make a mistake to assume that they could have anything like the strength or the rigidity that they had in World War II.

Nonetheless the controls still provide, in my judgment, an important drag on the upward bias of prices in the economy—on the tendency to resolve conflicts by price increases and wage increases.

We are seeing something of this sort at the present time in connection with the steel negotiations. However these come out there has been a process of delay in what would otherwise be a very easy decision to grant a steel wage increase, and to have an increase in steel prices. Therefore, I will content myself in these preliminary remarks in urging caution, in urging that we do not further weaken these restraints.

We may well face the need at a later period, which I would define as something beyond the next 6 months, of strengthening these controls. We may also need a much stronger policy on the indirect controls, as military expenditures mount, and especially should we get, as Mr. Johnson suggested, very considerable increase in private investment.

I am not going to comment on that at this time, except to express some concern about that longer period, and to suggest that while the short-run prospect is by no means as alarming as it was a year ago, that should not cause us to be sanguine about the longer run problem.

The CHAIRMAN. The prepared statement of Mr. Galbraith will be placed in the record at this point.

(The prepared statement of Mr. Galbraith is as follows:)

REMARKS OF J. K. GALBRAITH, PROFESSOR OF ECONOMICS, HARVARD UNIVERSITY, BEFORE JOINT COMMITTEE ON ECONOMIC REPORT, FEBRUARY 1, 1952

Mr. Chairman, members of the committee, I shall be very brief in my comments. One of the topics listed for discussion this morning concerns the effect of the mobilization and stabilization efforts on the structure of American business. This is an important question. So is the obverse—the effect of the structure of American enterprise on stabilization and on mobilization. It happens that in the last year or two I have been worrying a good deal about this latter question. Indeed, were it not that I might be accused of using a congressional hearing for commercial purposes, I would confess that I am about to publish a book (American Capitalism: The Concept of Countervailing Power) on the subject. I am going to suggest one or two of my conclusions this morning.

Within the last 15 years there has been a great deal of debate over the extent of concentration—what may roughly be called the dominance of big business—in the American economy and whether this concentration is increasing and whether it is serious. What is not open to debate is that large business units and also unions speaking for large numbers of workers are very important in the economy—that extensively in the capital goods area, less so in the consumers goods field and least of all in agriculture the critical decisions on prices and on wage levels are taken by a relatively small number of firms or are made in a relatively small number of collective bargaining sessions.

When the economy is not under strain this process of rather concentrated decision-making, as it may be called, does not work perfectly—few things in economics do. But it works and by the test results it has worked pretty well. I do not attribute great importance to competition in regulating this process—old-fashioned competition by which prices are kept down by the threat of what a competitor will do—although I do not deny that competition plays a role. Rather I am inclined to stress the tendency of any group, which is endangered by the economic power of any other group, to develop the strength—sometimes with the aid of government—to look after itself. When workers found themselves at a disadvantage in selling their labor viz-á-viz the large corporations they organized and got power to protect themselves. Farmers have done something of the same sort. The large retail organizations represent a development of power designed to exploit the consumer's interest in low prices. So it goes through the economy. This tendency—the tendency for economic power to beget what I have termed "countervailing power"—I regard as the great stabilizing force in the economy. It is the power which enables the buyer (or on occasion the seller) to oppose his own strength to that of any powerful figure on the other side of the market.

Unhappily this is not a process that works equally well at all times and places. Specifically it does not work at all when the economy is under inflationary tensions. Then, with the strong demand and the relative shortage of goods and labor, bargaining power throughout the economy shifts to one side—to the side of the seller. The buyer, whether he be a buyer of labor, of merchandise, or a plain consumer at retail, loses much or all of his strength. When the economy is under pressure, in other words, there is no effective exercise of countervailing power—all increases in prices and costs are passed through to the ultimate consumer with a minimum of resistance.

I draw one obvious conclusion from this and it is not a pleasant one. So long as the American economy remains under pressure—so long as civilian and military demand are strong and there is pressure to get all possible production out of our plant and labor force—the normal, self-regulating machinery of the economy will be at least partially inoperative. There will be a strong tendency toward inflation. I foresee the probability of such pressure on the economy for some time to come. We could siphon it off by heavy taxes and a strong monetary policy—but these would have to be strong enough to introduce some slack into the system. They would have to be strong enough to introduce some slack into the labor market to make steel and other heavy industrial goods hard to sell, to do the same (though here it would be less diffiicult) in consumer's goods markets. But all of this runs somewhat against efforts to increase and maxiimize production. We want to use labor supply and plant capacity to the maximum. We can't have it both ways.

Under these circumstances the only answer is to retain minimum effective control over prices and wages for as long as the economy is under pressure. I have had some experience with these controls; I have better reasons than most people for disliking them. The political pressures they generate are in some respects more insidious and objectionable than their economic consequences. Yet it is my judgment that they are for the immediate future. I would feel happier were the legislative authorization stronger than at present. It would not be safe and conservative policy to weaken it further.

The CHAIRMAN. Mr. Mason?

STATEMENT OF EDWARD S. MASON, HARVARD UNIVERSITY

Mr. MASON. Mr. Chairman, I would like to address myself to question 2: Do we have the human and material resources to support and maintain over the long run an armed force of the size contemplated?

I would like to say a few words about the raw material aspects of that problem, first, and then turn to some observations on the broader problem that I think is involved.

The first point I would like to make is this——

The CHAIRMAN. Perhaps I might interrupt you to say that for the record, as I understand it, you are a member of the so-called Paley Commission appointed by the President on January 22, 1951, to look into the broad aspects of our material resources.

I understand that report is——

Mr. MASON. It will be out sometime in the spring, Senator.

The CHAIRMAN. It is in the process of being completed?

Mr. MASON. That is right; yes.

The CHAIRMAN. Very good, sir.

Representative PATMAN. Is George Brown, of Houston, on that committee?

Mr. MASON. Yes; he is.

Representative PATMAN. How many members of the committee are there, five or seven?

Mr. MASON. Five; Mr. Paley, Arthur Bunker, George Brown, Eric Hodgins, and myself—five men.

Let me say, Mr. Chairman, what I am saying now really does not have much connection with the work of this particular Commission. I am expressing my own views here.

The first point I would like to make is that in an economy in which you have an allocation of resources to armament production, say, of the order of 15 to 20 percent of the gross national product, the over-all material requirements are not necessarily very much larger than they are for the same economy operating at full employment on civilian production.

During World War II, of course, we had a tremendous increase in our material requirements, but that was largely because we were proceeding from a volume of unemployment of 10 or 12 million to full employment during the war.

If you have already got a full employment economy and it shifts toward the military production, once that level of military production has been attained, the over-all material requirements are not very much larger than that same economy would show at full employment.

Why then are we running into such a serious materials problem now? Those shortages, I would say, are not so much the result of the level of armament production to which we are proceeding as they are of the rate of build-up of armament production.

Now, that build-up imposes excessive materials requirements for mainly these reasons: First, because to move into the armament production you have a rapid shift in the mix of materials requirements. The materials you require, the specific materials, are not required in quite the same proportions as they were before. So you have certain specific shortages, which, however, can be overcome through an adjustment of supply in a relatively short period of time.

Secondly, you have this difficulty because during the period of build-up you have a disproportionately large input of materials per unit of output because you have got to build up facilities, and you have got to build up pipelines, and so on.

Now, these considerations lead me to the conclusion that the serious problem of material shortages is going to be of relatively short duration, and it may be that a year or 18 months from now, despite the fact that we are operating at a fairly high level of armament, we will not encounter very serious material shortages.

I think that the basic reason why an armament economy does not consume over all much more materials than a civilian economy at a similar level of employment are these: In the first place, although you have a change in the percentage of labor force employed in manufacture, which is a highly material consuming part of the economy, you have, at the same time, an increase in the degree of fabrication of those raw materials, so that in the armament field your input of materials per dollar of output tends to be smaller than it is in manufacturing, in general. These things have a tendency to counterbalance each other, so again I am saying that the over-all material requirements of an economy which is devoting 15 to 20 percent of its output to military production are not much larger than the civilian economy. But that does not mean at all, in my opinion, that in the long run we will not have a materials problem.

You are going to have a materials problem because of the very rapid rate of growth of American output, whether it is used for military or civilian purposes.

If you look at the figures you will see that as far as minerals are concerned, in 1950 we consumed four times as many minerals as we did in the year 1900. There is a fourfold increase within a 50-year period, and if you include petroleum in mineral products there was a fivefold increase.

Well, now, if gross national product increases at roughly the rate of 3 percent a year, you are going to have a doubling of these material requirements within the next 25 years, so that by the middle of the 1970's you are going to have for the United States economy raw material requirements that are 10 times what they were in 1900; 8 times what they were if you exclude oil from the picture. So it is that very rapid rate of growth that is going to give rise to serious materials problems, and not the fact that we may have indefinitely to look forward to a 15 to 20 percent of our gross national product devoted to military production.

I will, if you want me to a little later, go into this long-run materials question but in these introductory remarks I would now like to turn to the broader problem. I think if you look at this second question you probably would come to the conclusion that it ought to be reinterpreted in some such way as this.

The question that should be asked is probably this: Will an armament program of the size that is contemplated check the rate of economic growth we are all looking forward to?

Certainly the fact that 15 to 20 percent of the gross national product may indefinitely have to be devoted to military production could check the rate of economic growth.

It could check it if it results in a smaller percentage of gross national product going into investment than we have hitherto seen; it could check it if, in order to get the volume of investment that we have seen in the past, you move into an inflationary situation, an inflationary situation that leads to political and social disturbances that check production; and; thirdly, it could check this rate of growth if in the attempt to avoid inflation, while still securing this volume of military expenditures, the combination of taxes and controls seriously handicap production incentives.

Now, as I say, the armament program could check the rate of economic growth, but I see no reason myself why it needs to check the rate of economic growth. If you look at investment you will see that over the last few decades in the American economy gross investment has been roughly 20 percent of the gross national product, and net investment has been roughly 10 to 12 percent of net national product.

Furthermore, if you consider how investment is defined in determining the statistical estimates, you will see that investment includes the whole range of construction expenditures, including for roads, housing, race tracks, casinos, and everything else.

If you eliminate that part of investment that probably does not have anything to do with the rate of increase in productivity, and you probably would come down to a net investment of not more than 6 or 7 percent of net national product; a net investment that is really reproductive investment, investment in plant and equipment, and things that really affect the productivity of the economy.

Certainly, on the face of it there is no reason why an armament expenditure of the sort we are contemplating should prevent that rate of net investment in the economy.

Nevertheless, of course, you might not get that rate of net investment except under inflationary conditions, if you followed a wrong tax policy or followed a wrong stabilization policy, in general.

If you did follow those policies and got into an inflationary situation, certainly the possibility rises of social and political disturbances that would really check the rate of growth of the economy.

The CHAIRMAN. What is the rate that you say is left after deducting the investment in casinos and entertainment?

Mr. MASON. I am just giving you a "guesstimate" here, Senator.

The CHAIRMAN. I understand.

Mr. MASON. I would say probably that not more than 6 to 7 percent of net national product could properly be called reproductive net investment, because in the total investment picture you get, of course, a group of expenditures that have little to do with increasing productivity.

Now, that leads me to the final point, that certainly in the attempt to secure the proper volume of armament expenditures, plus the proper level of investment, without inflation, you might devise a tax system and a system of controls that would seriously handicap production incentives.

I would have to say that this is an area that economists know very little about. So far as I know very few people know very much about the relationship between tax programs and price control programs to production incentives.

All I am saying is that the possibility certainly exists in that area that an improperly devised tax system and an improperly devised system of controls could check productivity, but I do not see any evidence to indicate that the kind of tax system or the kind of price control system contemplated will, in fact, have that result or need have that result.

The CHAIRMAN. Thank you very much.

Mr. Backman?

STATEMENT OF JULES BACKMAN, NEW YORK UNIVERSITY

Mr. BACKMAN. Mr. Chairman, it is a privilege to be invited to participate in these sessions.

I would like to refer to three points of fact first, and then deal very briefly with several items of policy.

Mr. Galbraith referred to the softening of controls. I think it is rather interesting to note that during the past 6 months or since the passage of the Defense Production Act, wholesale prices and raw material prices have shown practically no changes. These prices reached their peak in February and March of 1951, and then declined through August. That has been a broad, sideways movement in prices since August.

In recent weeks these indices have actually declined slightly below the August level, and, in fact, as of January 30, the sensitive price index at 321.6 was just about the lowest point that it had reached in this downward movement.

Since changes in wholesale and raw material prices usually precede those at the retail level, these trends in wholesale prices portend at least stability, if not some moderate decline, in retail prices in the months ahead.

It may be asked why the consumer's price index has continued to rise to new high ground in the light of the trends for basic commodities in recent months.

In that connection, it is important to recognize that the entire rise in retail food prices, as measured by the index, reflects the increase in only one group of commodities, namely, fresh fruits and vegetables which have been really moving upward in the last 2 or 3 months, but if you take all the other components of the food index, the plusses and minuses, they about balanced out. In terms of the total consumers' price index, the rise in fresh fruits and vegetables accounts for almost three-fourths the rise in recent months.

In other words, up to this point the lull in inflation has been reflected in a lull in prices for some 6 months.

Now, that leads to the second fact which to me is most interesting. There are many public comments concerning the relative movements of prices, wages, and profits.

I have calculated the changes from June of 1950 or from the second quarter of 1950 up until the latest available data, which usually will be the fourth quarter of 1951. The accompanying table shows the pertinent data.

TABLE 1.—*Summary of changes in profits, wages, and prices since Korean war started*

	Pre-Korea	Latest date	Percent change
All corporate profits after taxes (billions)	[1] $20.6	[2] $17.0	−17.5
All corporate profits before taxes (billions)	[1] $37.5	[2] $42.0	+12.0
National City Bank—leading manufacturing companies—net income after taxes (millions)	[1] $1,392	[3] $1,099	−21.0
Wholesale prices, all	[4] 157.0	[5] 175.9	+12.0
Wholesale prices, nonfarm, nonfood	[4] 148.6	[5] 165.1	+11.1
Consumers' price index	[6] 170.2	[7] 189.1	+11.1
Average hourly earnings, all manufacturing	[6] $1.453	[7] $1.635	+12.5
Average weekly earnings, all manufacturing	[6] $58.85	[7] $67.36	+14.5
Total employee compensation (billions)	[1] $148.6	[2] $182.5	+22.8

[1] Second quarter, 1950.
[2] Fourth quarter, 1951.
[3] Third quarter, 1951.
[4] June 27, 1950.
[5] Jan. 22, 1952.
[6] June 1950.
[7] December, 1951.

The percentage changes are these: Corporate profits before taxes rose 12 percent; wholesale prices rose 12 percent; the consumer's price index rose 11.1 percent; average hourly earnings rose 12.5 percent; average weekly earnings rose 14.5 percent. In other words, each of these important measures of profits, prices and wages are now in about the same relationship that they were in either the second quarter of 1950 or in June of 1950.

In other words, the entire effect of the rises we have had in prices, wages, and profits before taxes has been to move everything up to a new plateau.

Total employee compensation has risen 22 percent, and profits after taxes have declined 17 percent.

The third point on facts: Although economists give a great deal of emphasis to budget deficits, it is one of the rather paradoxical facts of the past 18 months that in the first 9 months after Korea, that is from June 1950, through March of 1951, the period of the fear of inflation, the Federal administrative budget had a surplus of $5 billion, and the cash budget had a surplus of almost $8 billion.

On the other hand, since March of 1951, the period of the lull and moderate declines in prices, the Federal Government spent 9 billion more than it took in. In other words, this was a period of a substantial budgetary deficit. The cash budget deficit was somewhat smaller.

My point is simply this: that while there are long-term implications attached to budget deficits and budget surpluses, the record of the past 18 months indicates that we cannot rely solely upon the picture of the Federal Budget over a short period of time, as an indication of what will be happening on the price front.

Various fears, fears of shortage, fears of price rise, fears of total war, and other types of fear may play a much more important role in the short run even though, as a long-run proposition, large budgetary deficits are inflationary.

Now, I should like to turn to some points of policy contained in the Economic Report of the President. I would like to talk briefly about wage increases and about the Federal budget.

Large general wage increases are inflationary in an armament economy. The basic issue is not whether or not particular industries or companies can afford to make these higher wage payments. The basic question is can the economy afford these increases.

This is particularly important because of the relatively high corporate tax rates now in effect. Let me spell that out. Companies that are now in the excess profits tax bracket pay wage increases to the extent of 82 cents on the dollar with money that would ordinarily be paid as tax revenues to the Federal Government. In other words, for every dollar that a company's costs go up, taxes go down .82 cents, and so the company pays 18 cents, and the Federal Government pays 82 cents of every dollar of wage increase.

All companies are not in that tax position, of course, but even for those that are in the lowest tax bracket excluding smaller-sized companies, 52 cents of each dollar of taxable income is paid to the Federal Government.

Of course, the Government collects taxes from the wage earner. Such taxes are about 22 cents for the first bracket and 25 cents on the dollar for the second bracket. Thus, for every dollar of wage increase, the Federal Government loses 30 to 60 cents on the dollar in tax revenues.

For the entire private economy a wage increase of 1 cent an hour costs approximately $1 billion.

The 18½ cents an hour requested by steel workers, therefore, would cost $18½ billion, if all workers received similar increases.

Of course, we know that not every worker obtains these wage increases, and, incidentally, these estimates are exclusive of Government employees.

Let us assume that half of the workers obtain these increases, and I think that is a conservative estimate. On the basis of these demands, and I refer to them because they are in the public eye now, the total cost would be $9 billion, and the cost to the Federal Government would range from 2.7 billion to 5.4 billion in tax revenues.

When you add that amount to the $14 billion deficit projected next year, it becomes a pretty big piece of change.

Well, you may say, suppose these higher wages are compensated for by higher prices, then the Government does not lose the tax revenues. That is right.

But in those circumstances, the Federal Government then pays more on the spending side. In the first place, wherever the Government has any of the various forms of cost-plus contracts, whether they be escalator-clause contracts or cost-plus or cost-plus-a-fixed-fee or target price, the Government would pay the higher wage increase because costs would rise.

To the extent that raw materials or other prices go up, the costs of goods the Government will buy goes up, and so the Government pays for these wage increases either in the form of higher spending or smaller revenues. My guess would be that it would be a combination of both.

The point is that when you have a tax structure which takes 52 to 82 cents of the taxable income dollar, the impact on the economy must be measured through the Federal budget, because it is the Federal budget where most of that impact will be felt.

My next point deals with wage policy: The Council and the President advocate increases in wages to allow for increases in productivity. This is a very unsatisfactory basis for wage increases in an armament economy.

Over the long run, it is true that real wages rise as productivity increases. During an armament economy, however, the increases in productivity are diverted largely to the Government to help meet the war needs and the war effort.

The Council points out in its report that there will be no increase in the supply of civilian goods available in 1952, and I think there is general agreement with that conclusion.

In their Mid-Year Report, July 1951, the Council pointed out that as consumers' incomes rise their spending also tends to rise. The Council admits that productivity increases would result, and I quote:

in inflationary redundancy of consumers' buying power, unless compensated for by sufficiently higher taxation and a higher rate of saving.

Since consumers tend to spend increases in incomes, this inflationary pressure which the Council foresees is bound to take place.

The fundamental justification advanced for productivity or annual improvement increases is that labor should share in the increasing output by receiving higher wages.

This basic postulate cannot be supported during an armament or a war economy because the total supply of goods and services available to civilians does not increase at such times.

This was the case during World Wars I and II. Similarly, in light of the high level of production in 1951, some curtailment of civilian supplies or at best no change in civilian supplies, seems certain for 1952.

Thus, the basic underlying conditions which prevail in peacetime, and which are the underlying assumptions of these productivity increases do not exist in an armament economy. Such increases as do take place will be used to meet the needs of the war effort.

Under these circumstances wage increases based upon productivity result in an increase in consumer income which is greater than the increase in the available supply of goods.

In addition to that, under the conditions prevailing in an armament economy, the increases in productivity tend to disappear in many industries, and that is particularly true of civilian goods industries. The net effect of a productivity wage increase, therefore, is an increase in unit labor costs, which adds pressure for price rises from the cost side as well as from the purchasing power side.

To the extent that the companies paying the higher wages sell a large part of their output to the Government, the result would be an increase in the cost of the defense program, and hence expanding pressures to increase the Government deficit.

This budgetary deficit represents the fundamental pressure, the inflationary pressure, on the general price level.

No group can improve its position in an armament economy when the supply of civilian goods is unchanged or decreases, except at the expense of other groups. That is a simple matter of arithmetic. So-called productivity wage increases have no place in our armament economy.

The Council, in its report, hopes that such productivity increases will create incentives for larger production. I believe that hope will prove to be an illusion.

The reason is that when you include wages as part of a basic wage structure, the incentive provided is no different from that obtained by any other general wage increase. If you tie a productivity increase specifically to more output, then you have an incentive payment. But I think in the past there has been pretty general agreement on both sides of the bargaining table, union and management, that rates that are included in the wage structure do not provide the type of incentive that piece rates provide.

Most suggestions in favor of these wage increases of the productivity type are not of the incentive type. In effect, they say, "Let us give a productivity increase of X percent, 2 percent, 2½ percent, 3 percent," and that means a general wage increase that gets into the wage structure.

The fact is that the productivity argument is merely a rationalization for a general wage increase. But a general wage increase by any other name is still a general wage increase.

The President and the Council of Economic Advisers have announced the abandonment of the pay-as-you-go basis for financing our armament program. The President states that, and I quote:

> If the only choice is either to run a deficit of limited size and duration in the Federal budget, or to run a deficit in our national security effort, by far the lesser hazard now is to run a deficit in our budget.

If those are the alternatives, then the statement is true. But I do not believe that those are the alternatives. I believe that the abandonment of the pay-as-you-go program is a major victory for the forces of inflation.

I am convinced that if a real effort were made, it would be possible to balance the Federal budget by a combination of economy in Government spending, plus increases in taxes.

I have prepared a table which shows the tax revenues in the fiscal year 1950 and the estimate for fiscal 1953.

TABLE 2.—*Budget receipts, fiscal years 1950 and 1953*

[In millions of dollars]

	Actual fiscal year 1950	Estimated fiscal year 1953	Increase	Percent distribution op increase
Direct taxes on individuals	18,115	33,005	14,890	43.9
Direct taxes on corporations	10,854	27,800	16,946	49.8
Excise taxes	7,597	9,744	2,147	6.3
Total	36,566	70,549	33,983	

The change is really significant, and here is what it shows:

Direct taxes on individuals increased by about $15 billion; direct taxes on corporations increased by about $17 billion; excise taxes increased about $2.1 billion.

To put it in terms of percentages, of the increase of $34 billion in tax revenues, 43.9 percent came from individual income taxes representing a combination of higher incomes and higher tax rates; 49.8 percent represented direct taxes on corporations, and 6.3 percent represented excise taxes.

Since a major problem in an armament economy is to curb civilian spending, this failure to increase excise taxes is difficult to understand, except in political terms.

The Federal budget can be balanced if we have the courage to cut spending and to raise excise taxes to obtain the required funds.

Finally, it is important to balance the Federal budget because any financing of the deficit probably will mean recourse to the banks, and that means inflation.

Since the start of the Korean war there has been a net redemption of $1,700,000,000 in series E, F, and G bonds. Certainly, up until this point there has been little evidence that this group of nonbanking purchasers would be willing to acquire any substantial quantities of new issues of Government securities.

This reluctance might be overcome by offering more liberal terms, both in terms of redemption values and higher interest rates. This latter factor will become particularly important if mutual savings banks are permitted to raise their interest rates above the 2 percent level as is now being contemplated in many of the Northeastern States. Then the competition between series E bonds yielding a little less than 3 percent as of 10 years from now, and interest deposits that might yield 2½ percent immediately, becomes very direct.

One final observation concerning the Defense Production Act: I believe the Defense Production Act should be extended. There are one or two provisions in that act which, I believe, are inflationary, and in some respects are unworkable.

For example, I think the provision that provides that whenever a price is fixed, a wage must be fixed, is a highly unrealistic provision. I think it is a carry-over of some general observations which economists make concerning the entire economy. They do not apply to individual industries. The provision represents the application to an individual industry of a policy that really applies only to the economy.

For example, suppose that the prices of petroleum were running away and you wanted to fix the price of petroleum. What could you really do to hold down petroleum prices by fixing wage costs which amount to only 6 or 7 cents on the dollar in that industry? It is not the sort of policy that applies too effectively in a particular industry and, I think, one of the items in the Defense Production Act which, in effect, ties the hands of the Economic Stabilization Agency, if it wants to engage in decontrol, is that provision. In other words, I think that provision should be deleted from any new act so that if the agency finds it is desirable to decontrol prices it does not find it cannot decontrol them because there is a barrier in terms of what it must do in connection with wages in that industry.

Finally, one observation concerning agricultural prices: Agricultural prices, of course, provide one of the big gaps in the Defense Production Act.

I think agriculture should be treated the same as every other type of industry. Agricultural incomes have increased substantially. In 1951 the total net income aggregated $17 billion, which was an increase of about 25 percent above 1950.

Agriculture can stand on its own feet, and that applies to agricultural subsidies as well.

Thank you.

Representative PATMAN (presiding). Thank you. We will next hear from Mr. Lloyd G. Reynolds.

STATEMENT OF LLOYD G. REYNOLDS, YALE UNIVERSITY

Mr. REYNOLDS. Mr. Chairman and gentlemen, I would like to address myself first to the wage part of question 3 on the committee's agenda. I have some ideas on the inflation problem in general which I may have a chance to express during the committee discussion. Meanwhile I shall simply assume we are going to be under inflationary pressure for the next couple of years at least, and that we shall have some degree of direct Government control over wages and prices.

There are two main functions of the wage-control system, and I want first to stress a function which is apt to be overlooked. At a time like the present, when we are piling new labor requirements on top of a fully employed labor force, labor shortages are bound to develop in many occupations which are important for military production. These bottlenecks have to be broken if the program is to move forward. In our kind of economic system, where we do not tell anybody where he must work, people must be induced to move voluntarily to the jobs where they are needed. Money is not the only inducement which can be used, but it is an important inducement. There are situations where it is expedient to pay higher wages to attract labor or hold labor in an essential occupation.

These were called rare and unusual causes in the last war. They were not as rare and unusual as we wished they might be, but this was regarded as a legitimate reason for giving wage increases in certain cases.

Wages can be used effectively to get labor into essential work only if we have some control over wages on other kinds of work. Otherwise every time a manufacturer of airplane engine parts raises his wages to attract labor, the manufacturer of juke boxes will raise his wages, too, and we will end up exactly where we were. We must with one hand hold back the advance of most wage rates, while with the other we allow exceptions where necessary to man essential industries. This discretionary power must, of course, be used with caution, otherwise it defeats its own purpose. But with proper caution, one can help to break manpower bottlenecks by localized wage increases without upsetting the general wage level.

The second and more obvious functions of wage controls is to hold back the general advance of prices and wages. I don't think one should exaggerate what can be done in this respect. As long as there is an excess of money demand kicking around in the economy—due to budget deficits, easy credit, and so on—there is going to be an upward trend of wages and prices. But I think one can still do something to fight a delaying action and to reduce the rate of inflation.

Let me illustrate what I mean. If the packing-house workers—or any other group of workers—see the cost of living rising, you can be pretty sure that wages will eventually be raised enough to catch up. This will happen with a union or without a union, with wage controls or without them. But the critical question is: how fast will wages adjust to a rise in living costs? If wages rise after a delay of 6 months, this is better—from a stabilization standpoint—than if they rise after 3 months. If they rise only once a year, this is still better. This means that you are getting "cost absorption" by workers for a limited period of time. It is uncomfortable for them, but it does slow down the pace of an inflationary movement.

This principle should, of course, be applied in both directions. If you apply it to workers you should apply it to industry as well. After the workers in an industry get their wage increase, this will probably give rise in time to a price increase. But the phrase "in time" is important. If the price adjustment can be held back long enough so that you get some cost absorption by the industry, for, say, 6 months or so in each round, this is very helpful from a stabilization standpoint.

Given an underlying excess of money demand, you are going to have price increases which produce wage increases which in turn produce price increases, and so on. But if you can stretch out the length of time between successive rounds of wage and price increases, you may be able to produce a rather gradual spiral instead of a very steep one. This is what I mean by fighting a delaying action.

This carries two morals for wage policy over the next year or two. First, I believe we should require a reasonable delay in the adjustment of wages to changes in living costs. Wages must adjust in time, but I would hate to see them do it every month and I am a little worried about doing it every 3 months. It would be better to have adjustments only every 6 months or even once a year.

Second, we should avoid overcompensating for cost-of-living increases. It is often argued that we should allow wages to rise each year by somewhat more than the cost of living has risen in order to take account of increasing labor productivity. This policy is quite reasonable under normal conditions. The argument for it is that rising productivity means a larger output each year of goods and services available for consumption. The simplest way to provide the extra

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purchasing power needed to buy this larger output is by raising everybody's wages.

This line of reasoning does not apply nearly as well to the present situation, in which the output of consumer goods is likely to be falling rather than rising. Under these conditions, raising money wages rapidly by improvement factors, productivity increases, and so on will not raise the workers' level of living. It will push up the price level at a faster rate than would occur otherwise. Moreover, a policy of allowing all wages to rise at this rate will interfere with the first function of wage control which I mentioned at the beginning—that is, to allow some wage rates to get out ahead of the pack as much as necessary to break manpower bottlenecks.

I would favor holding back most wage rates to the pace at which living costs rise, and I would try to see that cost-of-living adjustments do not occur too frequently. This policy is not as tough as it looks, because, even if we hold back on raising wage rate, workers' earnings will rise considerably because of overtime, loose piece rate and incentive systems, individual merit increases, upgrading of jobs, and so on. Still, it would be a rather tough policy. It could not be sold to workers unless we were prepared to be reasonably tough also on farm prices, business profits, and other types of income. My guess is that most of the American public is rather weary of the inflation merry-go-round at this point and would welcome a tough policy, provided they were convinced it would be applied equitably to all groups in the economy. But this carries me beyond economics into a field with which members of this committee are much better acquainted than I am.

I have a very brief word on question 2 on the agenda which raises the issue of whether we have enough labor and raw materials and industrial capacity to support large military expenditures plus a high level of civilian consumption.

Again I am going to limit myself only to the question of labor supplies.

I believe that we do have quite adequate labor supplies to support a mobilization program of the present size into the indefinite future. I base this mainly on the great expansibility of our labor force exhibited so dramatically during World War II.

I recall that in 1942–43 a great many people, including myself, were writing memos about the imminent crisis in labor supplies and about how we would not be able to get as many people as we needed to meet production requirements and staff the armed services. We, we were wrong. And I think it is interesting to look back and see why we were wrong.

It turned out, in the first place, that a great many more people came into the labor force than we had counted on. Millions of women were drawn into employment, old people did not retire and continued in employment, great numbers of people were drawn in from agriculture to urban industry, hours were extended somewhat, and so on.

And so I believe that we have here a great measure of flexibility and expansibility which will easily carry us through a production program of the present scale.

There are shortages of particular skills and there will be shortages, undoubtedly, of labor in particular occupations and particular places, but at the same time we have surpluses in other areas. There is unemployment, as you know, in some parts of the country, and loose labor markets.

This is basically a training problem, a problem of converting people who do not have the skills we need into people who have those skills, and here it is comforting to realize that the training time for most occupations is really pretty short. There are a few which take 2 or 3 or 4 years, but for most occupations this training problem is not too tough a thing.

To some extent, of course, this is a problem of geography, also. It is a problem of trying to get jobs to the areas where labor supplies are available and of inducing people to migrate from loose labor markets to tight labor markets.

Again, there are a lot of well-known ways of getting at this sort of problem. If one looks a little farther ahead, a matter of 5 or 6 years into the future, we should remember that the number of young people reaching working age each year will rise very substantially beginning in about 1958, or so, because of the very high birth rates of the past 10 years. So that at that stage it is perfectly clear to me that we will have enough labor to carry us along at the present rate of mobilization.

The CHAIRMAN. Thank you. We will next hear from Mr. Lester.

STATEMENT OF RICHARD LESTER, PRINCETON UNIVERSITY

Mr. LESTER. Mr. Chairman and gentlemen, I also will address my remarks mainly to the wage end, but before I do that, I want to say that I am in somewhat the same dilemma that some of the other speakers have been in, particularly Mr. Johnson, that we seem to be in a position where we are not going to be tough on anything, and, therefore, will be mildly restraining on everything.

We also seem to be in the position that we are uncertain what kind of a circumstance we will face.

If you look at the figures you will notice that toward the end of last year the military spending program tended to slack off. You will notice that the hours of work were reduced at the end of the year, relative to the end of 1950, by about 1 hour per week.

And then we are in the kind of a year that Mr. Galbraith indicated politically.

So, in the midst of that sort of a situation it is very difficult to be too certain as to what should be done.

I am more disturbed than perhaps some of the others have been by a continuation of direct controls, especially wage control.

I agree with the Council that—

> The difficult necessity of a sufficiently flexible wage program to maintain equity, incentives, and industrial peace points to the urgency of a sufficiently strong tax, credit, and voluntary savings program to curtail excessive spending.

That is contained on page 148 of the Council's report. It seems to me to point out in one sentence the problems we have been discussing this morning on how many different fronts and to what extent we are going to be restrictive. Consequently, it is disturbing to find that the money supply (currency outside the banks and adjusted demand deposits) expanded by $10 billion, or 9 percent, during the last half of

1951, the greatest rate of increase since World War II, and that it was accompanied by a rise in the rate of personal savings to the unprecedented peacetime figure of $23 billion a year, which could mean the development of a potentially dangerous liquid position.

One reason I am reluctant to make any proposals with respect to direct controls is that we seem to be piling up a situation from the monetary, fiscal, and liquid position point of view that may be dangerous.

Judging from statistical and other information, and by other information I mean in part a study that I have been engaging in, in the Trenton area during the last 3 or 4 months, interviewing companies and unions, it is questionable whether Federal wage controls have served during the past year to keep the general level of wages below the level that would have prevailed without wage controls. By turning top national bargains into approved Federal standards, the Wage Stabilization Board has undoubtedly tended to elevate some wage bargains; it has given a goal approved by the Government for union negotiators to bargain for and against which their members will perhaps test them. In industries like automobiles, the Board has had no apparent effect on wage scales. In some cases, it has had a restraining effect.

In October I was consultant to the then Director of Stabilization, Mr. Valentine, and we had this issue up with respect to the General Motors type of agreement. You may recall that the automobile workers notified the Director of Economic Stabilization that if he abrogated any part of that 5-year contract, all of the rest was in the union's viewpoint null and void.

What has actually happened in connection with wage stabilization, it seems to me, is that the General Motors type agreement set a norm, and that was the normal peacetime norm. The automobile workers signed that contract before Korea. And that is something which we have tended to follow in wage stabilization. Perhaps my friend, Stan Ruttenberg, is more aware than I would be of the industries in which the Board has had a restraining effect. As you know, it has cut down some negotiated increases.

Speaking before the American Economic Association late in December, Prof. Clark Kerr, former vice chairman of the Wage Stabilization Board, expressed the opinion that during the past 6 months the elevating effect of the Board had been greater than the retarding effect. From limited information, including recent interviews with 40 firms and some unions in Trenton, N. J., in connection with a labor-market study, I doubt that the wage-stabilization program is serving, on balance, to curtail the level of wage rates or that it will so during the next few months.

I am thinking of the whole area of soft goods. In your paper this morning you will see that the hosiery workers accepted an average wage cut of 15 percent under voluntary arbitration.

If my view is correct, continuation of wage controls seems justifiable only on the following grounds: (1) As an aid in avoiding strikes in essential industries—you avoid them by having the case go to the Board, and the Board then handles it one way or another to settle the dispute, so that the dispute settlement aspect of the Board's work becomes perhaps the primary one; (2) as a political matter in order to maintain any sort of Government price control, yet in many other countries when they have had price control, they have not had wage control. I would agree with Mr. Backman when he says it was a mistake to tie up in our legislation so closely and directly price and wage control. It has difficulties in connection with decontrol. It has other difficulties that I might mention. And as I say, there is a lot of experience in other countries where you had price control without wage control. Some of these countries have avoided any wage control even during the war. They have a different situation. And I do not want to go into the individual cases. I am not really qualified to do so, but I think it is something that we ought to bear in mind in reviewing this situation. And (3) as a stand-by safeguard in case a serious emergency should arise. In case things should really threaten to get out of hand.

On that aspect of it I would say that if tighter wage controls should prove necessary 6 or 12 months hence, it might be better to start fresh with no hampering precedents.

I think the real restraining effect under wage control occurred in the early months with the freeze. You got the most delay that Professor Reynolds was talking about, and you got an effect there that I think would be very difficult to recapture with a continuation of the direct controls. One of the most difficult things for the Wage Stabilization Board would be to institute a new freeze or even much greater wage restraint.

If it is a question of the first item which I mentioned, avoiding strikes in essential industries, I would raise the question whether other strike settlement machinery might not work better or at least as well as the Wage Stabilization Board. It seems to me that is a debatable issue.

Undoubtedly Federal wage controls are having, and will continue to have, adverse effects upon collective bargaining—I think there can be no doubt about that—the employer is relieved of responsibility, it tends to get the cases going to the Board with little real bargaining—the steel case, perhaps, would be an example of that—and you get those cases going to the Board with a dozen or 2 dozen issues in dispute and there is no real bargaining with respect to them. Such controls also tend to encourage less reliance on strong monetary-fiscal policies. Mr. Johnson indicated the strong need for monetary-fiscal and other types of restraint.

With the prospect for an extended period of military preparedness, characterized by fluctuations in the volume of military expenditures, which may step up fast for a while and then slack off, it seems to me that analyses should be made of the appropriate kinds of economic restraints for that sort of situation and whether they should be continuous or intermittent, general, or selective.

Our present legislation pretty near forces them to be general because of the tie-up between prices and wages, and because of other arrangements in connection therewith that I shall not go into. Consideration needs to be given to selective price controls and limited wage controls—possibly on a local basis for munition items only. Professor Reynolds mentioned these problems in the labor area that are largely local in terms of shortages.

I think a great deal might be done on the local level in terms of wage restraint. If a new plant comes in the local people would be, perhaps, in a better position to determine what wage scale would not be upsetting in that locality than would, perhaps, the Wage Stabilization Board in Washington.

I just raise the question whether it might not be possible to do more on the wage control end if you continue with it in terms of local situations, rather than large national cases. Some of them, I recognize, you cannot avoid, such as the steel case—you cannot avoid that, I think, on a national scale. Consideration should be given to the need for withdrawal of such controls at certain times.

I am worried about the indefinite extension of wage controls in our kind of an economy. I do not know the price end of it so well, so I do not speak to that factor.

So far as wage control is concerned, next summer might prove to be a time for considering withdrawal of wage controls. By next summer a reduction or complete taking off of wage controls might be a possibility. It seems to me that perhaps then provided we do use adequate—and here I, of course, have the reservations that the previous speakers had—if we use adequately the other types of controls, such as monetary-fiscal restraints, a good case might be made for abandoning wage controls temporarily next summer. At least, it seems to me that we ought to go into a careful study of the various alternatives to see whether wage controls should be continued beyond this calendar year.

Finally, I want to make a few remarks with respect to what Mr. Backman and Professor Reynolds said on productivity. It ties up with the wage control.

Let us not fool ourselves. We cannot control wages if employers and workers at the local level really want to give earnings increases, and they have an incentive system, whether it is piece rate or a formal incentive system with production standards. By setting the production standard the employer sets the earnings, or if it is set jointly, the agreement sets them, that is, the earnings, so that you can have in an industry like the ladies' clothing industry where you have frequent changes in the piece rates, or an industry where you have formal incentive systems, you can have the earnings going up with no change in wage scales. You cannot prevent that with the kind of controls that you have at the present time, in my opinion.

What you have actually happening is this in some of these companies: The earnings of the workers on incentive pay are going up relative to those who are paid on the hourly basis, whether it is in the same plant, whether it is in different companies in the same locality, or in different industries.

I was in a plant not long ago in which the piece-rate earnings on jobs which a person can learn—they are practically unskilled—you might call them semiskilled—just an assembly type of thing—you can learn the job in a week or two—the earnings on that kind of a job in that plant were as high as the straight-time hourly earnings for people in the skilled trades, such as electricians and machinists.

A great part of the work force, including the farmers, does get, if you want to call them that, productivity increases. Their income increases with their productivity.

The others are going to try and get that, and if you do not let them, you are going to get some of these unbalances, I think, that

Professor Reynolds mentioned. You have to watch out for that at least.

Furthermore, I will agree with the council that there are some possible incentive factors in even the over-all productivity increases. Take the automobile workers union. They are generally paid not on incentive but on hourly rates. If you keep them at the same rate of pay year in and year out when they are seeing that the equipment that they are working on is turning out more units of product each month or each week, I think you are likely to have some trouble in terms of incentives.

In view of the UAW contract with General Motors, which has spread now throughout most of the automobile industry and many others, I do not think that any Wage Stabilization Board in the near future is likely to abrogate that contract and get into the difficulties that are involved in trying to eliminate productivity increases.

Consequently, I do not look to see much change in the kind of wage stabilization that we have had. And I raise the question whether under those circumstances we ought not to be preparing to eliminate wage stabilization in good part.

The CHAIRMAN. Thank you.

Next we will hear from Mr. Ruttenberg.

STATEMENT OF STANLEY RUTTENBERG, CIO

Mr. RUTTENBERG. Mr. Chairman and gentlemen: I do not quite know where to start with all of these comments that have been made.

The CHAIRMAN. If you have a good idea where to finish, that would be helpful.

Mr. RUTTENBERG. Everything that starts well must end well, you know.

The CHAIRMAN. That is right.

Mr. RUTTENBERG. I am a very latecomer to this panel. It was not until very late yesterday afternoon or early yesterday evening that I was even invited to participate in the panel. The gentlemen at the long table here were the original participants. The two of us sitting at the short table have been recent-comers to this panel and I dare say I am considerably more recent as an addition than the gentleman across from me.

I do not think that this hearing here or this panel ought to engage in debating the wage policy which both Mr. Backman and myself will be debating up in New York next week before the Wage Stabilization Board panel.

Facts and figures which Mr. Backman presents, I have no doubt will be in his brief next week. His brief is an answer to one which we presented to the Wage Stabilization Board about 2 weeks ago called wage policy in our expanding economy.

The CHAIRMAN. Of course, this committee is designated by law to review the President's economic report and the policies and programs which are followed by various agencies of Government are merely incidental to that.

This committee, I think, would not assume to reach a judgment in a particular case.

Mr. RUTTENBERG. I am glad for those comments, Mr. Chairman, because I was going to go on to say that I did not want to choose to debate the question of the steel hearings before this panel. That we will do next week.

I am constrained to remark that I am reminded of a comment that Will Rogers made a considerably long time ago, and I think it goes something like this, and I quote Mr. Rogers:

It ain't that people are ignorant, but it's that they know so very much that ain't so.

The CHAIRMAN. And that they are all ignorant about different things.

Mr. RUTTENBERG. I do not want to get involved in a wage case here. I do want to make, though, a few broad over-all general remarks.

I think when we consider wage and price policy or stabilization policy in its broad aspect we just cannot talk, as Mr. Reynolds has and as Mr. Lester has, almost exclusively of just the wage sector with no mention made, except incidentally, of the price problem and the profit problem and of the general areas of the economy which more or less must remain in some relative form of balance during this period.

Dick Lester excuses himself as, no doubt he should, from a discussion of the price problem by reference to the fact that he spends most of his time in the field of industrial relations and, therefore, in the wage field.

But I do not think from the standpoint of public policy that any of us can really divorce our discussion from the broad aspects of the problem.

We can talk about wage policy and the fact that productivity increases should or should not be given. We can talk about rare and unusual cases in the manpower situation and the fact that maybe wages would move up if you had controls or did not have controls, or the fact that wages would move up, as Mr. Reynolds indicated, even if you did not have unions.

I do not think that we can discuss it within the limited area of just wage policy.

When you have a Defense Production Act which permits for all practical purposes automatic price adjustments at the producer level and pyramided price increases at the distributor and retail levels, specifically the kind of increase permitted by the Capehart amendment which I will not discuss before this committee because it is only too familiar with the problem, and the kinds of increases permitted by the Herlong amendment, that we are going to be getting automatic price increases in the economy.

I think when Mr. DiSalle was up here the other day and appeared in public session before this committee he indicated that there had been some five thousand Capehart amendments, that is, Capehart price increases submitted already to the Office of Price Stabilization.

Mr. Backman can talk about how wholesale prices have fallen or remained relatively stationary in the last 3 or 4 or 5 or 6 months, and that this might portend the fact that consumer prices will fall in coming months and that the consumer price index may not increase in coming months. All of that, of course, is generality.

I think we really have to get down to the crux of the problem which is that under the Defense Production Act the Capehart amendment will permit and has already permitted the passing on of cost increases unrelated to any other factor in the economic picture of the company or corporation involved. For example, I thought we had in America an economic system that prided itself upon the concept of cost absorption, upon the concept of developing a high level of income, a low level of price, so that the mass of people could participate and that as we increased costs, either material costs or wage costs, that industry would be inclined to think that maybe it was a wise policy to absorb those costs, or, if we increase advertising costs or research costs or development costs or entertainment or travel expenses that maybe these are the kinds of costs which ought to be absorbed out of the level of profits. This, of course, as we know, is not the concept of the Capehart amendment. These cost increases up to the cut-off period in July 26 are going to be passed on.

In the soft-goods industry there have not been many applications to take advantage of the Capehart amendment. But let us get into the period, as I think all of us will agree, of mid or late 1952 that consumer durable goods will become less available, that because of curtailments in the use of critical materials we will have fewer numbers of consumer durable goods on the market, and consumers at that point will naturally begin to shift their expenditures from the consumer durable goods to the consumer nondurable or the soft-goods line. At that point, when demand pressures may well begin to develop, not on demand which is going to exceed the supply because the supply of consumer nondurable or soft goods is very great, but when the demand begins to present itself with a transfer of expenditures from the durable area to the nondurable area—at that point I daresay there are going to be Capehart amendment demands coming in to the Office of Price Stabilization from the soft-goods area.

And then let us move over to the Herlong amendment area.

When the excise tax increases were put into effect on November 1, I daresay, I thought it was an accepted practice in the American economy that taxes ought to be absorbed by the people that paid them. An individual worker whose taxes are increased cannot pass them on to somebody else to pay for him.

And in that same regard I do not think it is good economic policy in a competitive economy for corporations to think in terms of passing their taxes on to the consumer or for the retailer to think in terms of passing on, not just the excise tax which he is permitted to pass on, because it is a tax on consumption—a tax which, I disagree with, but I shall not discuss that now—but he passes on not only the tax but he passes on a percentage mark-up upon that excise tax increase.

As long as we have that kind of a situation existing in the price area, and as long as we have in the corporate area the whole problem of accelerated amortization and certificates of necessity where, if Mr. Backman really wanted to make an impartial presentation of the facts—and I daresay I am not impartial, either——

Mr. Backman. Speak for yourself, Stan.

Mr. Ruttenberg (continuing). If he wanted to make an impartial presentation—you do not mind my taking you as an example in this situation—I think if he begins to figure the effect of a wage increase upon the tax revenue of the Federal Government, let us also consider what the effect of the accelerated amortization program is upon the Federal revenue of the Federal Government. And I daresay that in the last analysis it might well be decided that even though accelerated amortization reduces Federal revenue, and even though wage increases may reduce Federal revenue, that it might be good sound Government policy and economic policy to pursue those objectives. And I think that we just cannot talk about the loss—of what was it—if we have a global wage increase of some $5 billion in Federal revenue. I daresay if we really began to make some computations on the loss in revenue that would result from the accelerated amortization program which now has certificates approved beyond $10 billion, only 70 percent of which has been approved for tax purposes, that we compute the effect of that over a 5-year period, that it is considerably greater than the effect of this wage increase.

So that I do not think that we can use those kinds of arguments to make a decision as to what is good sound economic policy during this perid.

Let us just examine another aspect of the problem. What I am really saying is that we cannot talk about wages by themselves. We have to talk about the over-all effect of what an equitable and fair policy might be.

If I were to go into detail, for example, I think it could be very well indicated that in the price area you have automatic adjustments for price increases which the Office of Price Stabilization does not even have to approve. Under the Capehart amendment provision has been made for automatic adjustments, but in the wage area, wage increase bargains that go beyond the cost of living, must be approved directly by the Wage Stabilization Board.

Professor Reynolds, in his comments, indicated it might be good sound policy to get a wage increase that does not come along until 8 months after the price increase. Maybe we ought to have the worker absorb that increased cost to himself for that 6 months' period. That might be one way to put it, but in the interim period the individuals who have increased their prices are certainly benefiting through their increased sales, their increased profits as a result of the increased price during this intervening period, and the poor worker sits back and maybe after 3, 4, 6, or 10 months, or even a year, depending on the collective bargaining contract, eventually gets a wage adjustment that is not retroactive but begins only at the time of the expiration of the old contract. So he really is forced to absorb in many instances when he really is not able.

This concept of holding back on wage increases to me is to say let us put the pressure on the worker to absorb the burden of any inflationary problem that might be confronting us.

I know, Mr. Chairman, that I have gone beyond my 5 minutes, but I think I am not alone in having done that. And I know that time is awasting and you probably want to bring these remarks to a conclusion, but I want to make just one further point, and then I shall be through.

The CHAIRMAN. I will say that time is not wasting, it is passing.

Mr. RUTTENBERG. Time is passing. I will accept your amendment, Mr. Chairman.

I just want to comment on this problem that Dick Lester raised, that maybe we ought to have wage decontrol. Dick did not say what his position would be on prices except, I think he said, there may be some point at which we could have selective-price control.

We have a piece of legislation that exists, the Defense Production Act, that does make this tie-in between price and wage control.

I find myself in agreement with Professor Backman on only one issue, that is, it is very bad Government policy to tie wage and price controls directly together as this act does on a selective basis. That is, if you remember the original act, if you had selective-price control you had to have selective-wage control in the same area. I think that is very bad policy. But then the policy, the act, goes on to say if there is general price control there must be general wage control.

Unless we are prepared to change that concept which I do not think is going to be changed in this election year, I will be a little less polite than I think Mr. Galbraith was when he said your practitioners of the art of reality or the art of possibility——

The CHAIRMAN. The art of the possible.

Mr. RUTTENBERG. You quote him better. I thought that was a very good comment, a very good statement he made.

Mr. GALBRAITH. It is not original.

Mr. RUTTENBERG. I will be more practical. In this election year I do not see this concept of wage and price tie-in being changed.

Faced with that I am not saying that I would not suport it, because I would support the concept of Dick Lester, and I think there is good, sound, economic justification—and this I do not attribute to Mr. Lester because he may not agree with it—there is good sound economic justification, in my judgment, for wage decontrol during this period at the same time we would have selective price control. I think there is good sound economic justification for it, but that is not the reality of the situation. The reality of the problem is that we have some legislation which does tie the two together, and if that legislation remains then our job is not to deny wage increases, not to make it more difficult for wage increases than for price increases, but to have an over-all kind of economic stabilization program, an over-all type of policy which will permit adequate and equitable and fair wage and price policy.

I would like to be able to spell out what I mean by fair and equitable wage and price policy, but I do not have the time to do that now. Maybe in our further discussion we will get into that, but I think that we just cannot, as long as this legislation remains on the books, tying in price and wage control, divorce ourselves from assuming responsibility not only for talking about the wage area but for the price area, the profit area, and all of the other important segments of the economy.

The CHAIRMAN. Thank you very much, Mr. Ruttenberg.

It will be impossible for us to undertake the questioning now, although I may try to indicate a line of discussion among you gentlemen that might be profitable before recessing the committee. We will assemble at 2:30 in this room for the exchange of views.

I do want to say, however, that I think this has been a most productive panel session. A lot of good ideas have been presented here. There has been a very basic and factual discussion of the issues.

Perhaps it may be appropriate for me to say that from the point of view of the committee the common good is the objective that Congress must seek to serve rather than the particular good for any special group, economic group, in the entire economy.

I was particularly impressed by certain facts which seem to have been developed here by the comment of Professor Mason.

In the first place I think everybody agrees, not only here today, but throughout the sessions of the committee, that even in the face of the increasing tax burden there has been an extraordinary increase of private investment.

Hitherto the general assumption has been much as that which was expressed by Mr. Johnson that we cannot have the military build-up and private expansion too. That is not exactly the view that was expressed by Mr. Mason who seemed to indicate, if I understood him correctly, that the military build-up would not seriously interfere with the expansion of private investment provided, however, that we eliminated from that expansion the unnecessary nonproductive investment that goes into mere entertainment. That was not precisely the way you expressed it, but I think I got the idea.

Mr. MASON. That is good enough, yes.

The CHAIRMAN. To me that seems to mean that it is the view of, at least, one member of the panel that within certain limits we can have guns and butter, too.

It was the conviction that that was impossible that brought about, I think, the fall of the recent French Ministry and the fall of the Belgian Ministry, because the Parliaments, in the case of each nation, were unwilling to accept the austerity program that was being asked in order to support the military program.

This idea that 29 percent diversion of our gross product into military preparedness need not stop the expansion of our private economy is a very stimulating idea.

I think that it would be very helpful indeed if the members of the panel will be prepared to discuss that among other things this afternoon.

It will be recalled that during World War II, in the year 1944, if I remember the statistics correctly, the Government was buying approximately 50 percent of all of the goods and services that were produced. Necessarily that meant that increased prices fell equally upon the Government and the taxpayers so far as Government expenditures went as upon the private economy. And since the taxpayers are in the private economy, of course, I would suppose there might be a double impact upon them.

The figures we have before us now on the percentage distribution of Government buying for 1950 was reported to be at 15.9 percent, for 1951 at 16.4 percent, for 1952 at 22.7 percent, and for 1953 it is projected to be 26.3 percent. And then for 1954, 1955, and 1956, if there should be a falling off of military construction and our preparedness program required only the purchase of military products, then it was estimated to us, the opinion was expressed, that the military budden would decline by possibly $20 billion.

There are some other points that occur to one who listened to this very stimulating discussion, namely, the statement of Mr. Galbraith that the economy in the short run is not too far out of balance which would mean that by and large the policies which have been followed have not been too burdensome upon the whole, particularly, when one takes into consideration the facts cited by Mr. Backman about declining wholesale prices at least. Then, I recall the statement of Mr. Lester that wage controls should be used only to prevent strikes, to enable Government to maintain price control and for a stand-by purpose. I wanted to ask him to explain a bit more clearly, if he will, during the afternoon session what he meant by "starting from scratch with a new freeze." With his other assertions I understood it to be that the general policy should be one of selective price controls and limited wage controls, in other words, would be a general freeze applied to all prices and all wages, or how could you have a freeze of that kind and at the same time have selective price control and limited wage control?

With these suggestions for development and cogitation during the lunch hour, the Chair will recess the meeting until 2:30, but not without thanking all of the members of the panel for their very interesting discussion.

(Whereupon, at 12:20 p. m., the joint committee recessed, to reconvene at 2:30 p. m., this same day.)

AFTERNOON SESSION

Senator SPARKMAN (presiding). Let the committee come to order, please. Senator O'Mahoney will be a few minutes late getting here, but he will come in very shortly. He suggested that we go ahead with this discussion. We are all here except Dr. Galbraith, are we not?

Just before we adjourned for lunch the chairman threw out some suggestions. I wonder if any of you care to offer comments at this time on some of the things that he suggested, some of the questions he posed.

Mr. MASON. Mr. Chairman, the Senator made a few remarks about my statement with respect to the conditions necessary for the maintenance of productivity which, in general, I agreed with, but I was a little bit alarmed by one statement he made there that seemed to indicate that I thought that the armament program was completely compatible with maintaining consumption in the United States. He talked about having guns and butter.

I do not think that that is quite true. I would certainly think that the armament program is going to mean that we will have a smaller volume of consumption than we otherwise would have if we could maintain full employment throughout this particular period.

What I wanted to emphasize was really two things: That the magnitude of armament expenditures was not, in my opinion, incompatible with maintaining the volume of investment, the ratio of investment to gross national product, that we have seen in the past, and I wanted to make, secondly, the statement that a lot of what we really call investment has very little to do with productivity.

There is included in the investment figures a great deal of expenditure for construction that has no very close connection with productivity in the American economy, that that part of investment could presumably be eliminated without having much effect on the greater growth of the American economy.

I just thought I would like to have those matters clarified.

Mr. BACKMAN. I would also like to say I was a little disturbed by the implication that either as a group or as individuals, we stated that we are going to have both guns and butter. If what is meant is that we are going to have guns and not quite so much—less—butter, then I agree.

Basically we will have, first a significant change in the structure of consumption and, secondly, we will have a reduction in per capita consumption. Just let me spell that out.

If the total volume of civilian goods remains unchanged and the total size of the population increases or the total number of workers increases, then it follows that even an unchanged total volume of goods and services means a minor reduction in the amount per person. But it is in the changing structure that we really find what happens to consumption.

The Council of Economic Advisers estimated that there will be a drop of 20 percent or more in the so-called hard-goods area. For some types of hard goods the drop will be 50 percent or more.

Now, merely because we can have some more textiles or the possibility of the same amount or more food or more services, it does not necessarily fellow that we have the kind of "butter," if we may use that phrase, that people ordinarily would have wanted.

The kind of butter they may have wanted was a new car and not a new suit. Now, part of the money that would have been spent for cars may flow over into the so-called soft-goods areas, but the experience in the last war indicated that part of it does not flow over. To the extent these funds do not flow over to the purchase of hard goods, then people hold off from consumption of the things they want rather than buy the things that they can get.

So I would agree with Dean Mason that we are not going to have guns and butter in the sense of having as much butter as we would like or the kind of butter we would like. Nevertheless, we are going to have an awful lot of it.

Mr. RUTTENBERG. Did you say that the voluntary holding off of purchasing is a pretty good anti-inflation weapon? Did you mean to say that a good increase in savings is a pretty good anti-inflation weapon?

Mr. BACKMAN. I think there is general agreement among economists that if people do not spend, the impact upon prices now will be much less than if they do spend.

But, let me make this point very clear, and I think the experience after World War II underlines it very dramatically. If you do not spend the income now and hold it to save and to spend tomorrow, then you get that inflationary impact tomorrow. In a recent issue of the Federal Reserve Bulletin, September 1951, pages 1055-1056, the Federal Reserve Board talks about the explosive nature of these liquid savings, and it is these liquid savings which tend to increase. Last year, for example, a major part of the increase in savings was in liquid form.

Now, that is a very timid type of savings. If people become fearful, it is the sort of savings that they can spend quickly. In other words, it is the type of savings which can be stopped very quickly.

Now, it is true that part of the saving does represent buying new homes and installment credit. However, if you take the third quarter of 1951 and compare it with the second quarter of 1950, you will find that most of the increase in savings between those two quarters was in liquid form.

I am one of those who is very much convinced that while we held back the price rise during the last war, we experienced the inflation in the form of a deferred price impact after the war.

Mr. GALBRAITH. But not in the same magnitude.

Mr. BACKMAN. I go along with that, too.

Representative BOLLING. Mr. Chairman, I would like to hear some discussion on the impact of the present inventories in certain hard goods in this situation on a short-term basis, a year basis. What effect, if any, does some of the inventory that I hear about have on the total over-all situation from the point of view of this year?

Mr. BACHMAN. In the year 1951, total inventories of all kinds, whether to be used for armament or civilian use, increased by some $9 billion.

The inventories have been pretty well distributed between hard goods and soft goods. There have been some very interesting studies made by Louis Paradiso, of the Department of Commerce, and the committee might want to get hold of them, which indicates that in 1952, the level of production of hard goods will be substantially less than people would like to buy with prevailing incomes.

I am not convinced that the available inventories will last throughout the year to make up that deficit.

Now, we run into a rather paradoxical situation with inventories, and it is this: Already the number of units produced and going into the pipelines for most hard goods, except automobiles, have been cut by 50 percent or more. However, because you can still walk into a store and get a television set when you want it, and because in so many cases you almost cannot walk out without buying it because the concessions in price become so great, the impression is created that there are plenty of these things. But the fact is that there are not plenty of units going into the pipeline.

There has been a terrific reduction in output already, and that cut will be greater. I do not think the inventories are large enough to offset that.

Representative BOLLING. One other thing. I gather that there was considerable overbuying done at the time when it was thought that restrictions were going to be much more severe than they became, restrictions of material, and so on following within a year after the beginning of Korea. How much impact did that have?

Mr. BACKMAN. I have made some calculations in connection with that point. I think they are very interesting.

If you take the spending for durable goods in the second quarter of 1950, without judging whether that was too low or too high, you will find it was at an annual rate of $26.6 billion. If you take the next three quarters, that is from June 1950 to March 1951, which will take us up through the first quarter of 1951 and the period of the big splurge in buying, you will find that the annual rate of spending was $31.7 billion.

During the last three quarters of 1951, the average rate of spending was back to $25.6 billion or below the prewar Korean rate.

Now, if you take the entire period since Korea, the average rate of spending has been $28.7 billion, that is, the annual rate for the year and a half.

If you examine the increase in spending for nondurable goods and services, you will find that the increase in nondurable goods and services was approximately 11 percent, which, incidentally is another figure which matches those 12-percent increases that I mentioned this morning.

If the durable goods area was to increase 11 percent above the pre-Korean rate, it would now be $29.5 billion instead of $25.5 billion, the rate in the last quarter of 1951. In other words, a major part of the reduction in durable goods buying in the last 9 months of 1951 just about offset the overbuying which took place in the first 9 months after Korea, and that would suggest to me that we have come to a point now where a good part of that overbuying has already been taken care of. Durable goods buying is now likely to return to a more normal relationship to our incomes.

Senator SPARKMAN. I am going to have to leave in a few minutes because I have a committee meeting at 3 o'clock myself. I promised the chairman I would hold this until he got back from an engagement, but before I go I would like to hear a little discussion on the agricultural policy.

Two or three of you this morning indicated some criticism of the present farm policy, and said that we needed to get hard with the farmers.

Having been a farmer all my life, I have felt that the world has been pretty hard on us all these years.

Dr. Galbraith, I wonder if you might lead off with some words regarding agricultural policy. You realize that one of the recommendations of the President in the Economic Report was No. 7 [reading]:

> Repeal the sliding-scale provisions in existing agricultural price-support legislation; provide a workable support program for perishable commodities; and modify the tax on unallocated reserves of farmer cooperatives.

That is the seventh recommendation. I do not care about your restricting it to that, but I just wanted to remind you of that.

Mr. GALBRAITH. I will pass by the question of the taxation of the cooperatives, which I think is a somewhat secondary issue. On the first, I think, on balance that that is a good recommendation, and the problem is this: The present sliding-scale provisions provide, in effect, that if we build up inventories of foodstuffs and feeds, which would obviously be very desirable to do, the support prices would go down, and inasmuch as food, and particularly feeding-stuff inventories are now dangerously—well, I take it back—at a low level, there would be great merit in building them up. I think that we could afford to provide a firm incentive for a period in the near future, at least the next 2 or 3 years, for doing so.

I would like to say, however, Senator Sparkman, that I think the issue is in some respects a theoretical one rather than a practical one for two reasons: First, the chance of getting the inventories up, inventories of corn, wheat, and so on, in the absence of bumper crops, is not too good, so the chances are the support prices will stay around 90 percent of parity.

Senator SPARKMAN. Would you include cotton in that list?

Mr. GALBRAITH. Yes; I think I would be inclined to include cotton in that. The possibilities of expanding cotton production, as you so well know, are considerably greater than for corn and wheat.

On the other hand, we have learned within recent times how great our capacity to consume cotton is, and even if we did a 16 or 17 million bales of cotton production next year, the addition to carry-over, given prospective domestic and foreign demand, may not be very great.

Now, I have one other observation. As I say, that is a practical question. The other point I think that is worth emphasizing is this: I have been nonpersuaded for a long while—as you know, we talked about this up in Des Moines about a year ago—as to the possibility of getting any further great increase in agricultural production out of the commercial farming areas.

I took this position somewhat incautiously at the Farm Institute at Des Moines a year ago, and it was roundly objected to by, I think, almost everybody there.

Nonetheless, last summer, as you know, the Secretary of Agriculture went out for a 90-odd-million-acre corn goal, and fell some 6 or 8 million acres short of the goal. In fact, there was no important increase in corn acreage last year at all.

The meaning of that is, I think, that the agricultural plant of the good commercial farming areas is working something close to capacity at the present time. Given the uncertainties of labor supply, given also the fact that farmers are not under pressure, under the financial pressure, that they were 10 years ago, which, parenthetically, I think is a good thing, given also possibly the tax problem, the incentives for a big expansion and the possibilities for a big expansion in that part of the agricultural plant are not there.

It leads me to believe, and I have believed for a year or more, that we need a much greater emphasis on agricultural expansion in the secondary agricultural areas, in those parts of the country where agricultural manpower is not now being used effectively.

You have addressed yourself to the problem, Senator, in terms of the effect of that ineffective use of manpower on the people themselves, on the poverty in which they live.

The other part of that problem is that society, the Nation, is losing the effective manpower in those areas as compared with the commercial farming areas.

We have great sections of the country where the productivity is of the order of a fifth or a tenth of what it is in a State like Iowa, and I must say that while it is a longer and more difficult job, I do have the feeling that the long-run possibilities for increasing agricultural production are in that area, and that the measures for doing it are not price guarantees and price supports. They are not unimportant, but they are not at the heart of the problem, of that part of the agricultural problem.

Senator SPARKMAN. Doctor, you said that I stressed the effect of it on the people themselves. I did, but you may recall I also stressed this wastefulness of manpower.

Mr. GALBRAITH. I quite agree with you.

Senator SPARKMAN. Remember, I gave the figures of 2½ million. I noticed in the paper, in some paper, just this week, where some organization had come out with a finding that we were wasting 2 million people on our farms—the National Planning Association just this week came out with a figure of 2 million. We gave the figure of 2½ million, if you will recall.

Mr. Ensley says that is a measure of improvement in a year's time. Let us hope that may be true.

Does anyone else have any comment on the agricultural policy or this particular recommendation or anything pertaining to the agricultural policy?

Mr. RUTTENBERG. Senator Sparkman, I would like to say just one word that does not relate to it—it relates only indirectly to this problem.

I think when Mike DiSalle testified before the joint committee he indicated that one of the main reasons why the CPI, Consumers' Price Index, had gone up in recent months, has been because of the inability to do anything about food prices. He said, to use an example of one commodity, I forget which one it was, he kept saying that every time he had hoped—maybe it was hogs—every time he had hoped that it would get to parity, parity would move up a little higher, and the hog price would move up just a little toward it, and they would never catch up, so they could never quite do anything about the price.

I do not know quite what the proper public policy ought to be, but I do know this: That it is going to be impossible to have adequate and effective wage stabilization programs as long as the cost of living continues to move up, and I think everybody has come around to believe, with very rare exceptions, that wages ought to move as the cost of living moves, at least that much.

Some people say not any more than that; others say more, but so far as the cost of living index is concerned, they say wages ought to move along with the price structure; but if the price structure is going to move up at the retail level because of the inability to do anything about controlling food prices, then I think you have a problem, a problem that is going to deserve some pretty careful attention and consideration in Congress, and it relates to the provision in the Defense Production Act that prohibits price ceilings from being placed on any commodity whose price is below a hundred percent of parity.

I do not know whether the concept of food subsidies is the way to handle it or not. That certainly would be the recommendation that I would make, that we ought to have a food subsidy program. That would permit the farmer to still retain his adequate income from the farm commodity he produces and, at the same time, not permit that increased price to be passed on to the consumer; that this be absorbed the way it was during World War II, in part when OPA had the authority to use the food subsidy.

Mr. BACKMAN. It seems to me in connection with this food price movement, that Mr. Ruttenberg referred to, that the committee might find it advantageous to have the Bureau of Labor Statistics make an analysis of the changes in food prices, say, since last September when the latest move started.

I have done that, and you can have this confirmed easily enough. You will find that the entire change in level of food prices was accounted for by fresh fruits and vegetables. All the other foods show changes of plus a half percent, minus a half, and they all cancel out. I think you will also find if you examine the history of price control in this country and in other countries that regardless of what power was given to the agency by Congress, or regardless of what powers the price-control agencies may have, the ability to control fresh fruits and vegetables is practically nil.

In England fresh fruits and vegetables were only controlled after standardized packaging was introduced.[1] The problem of controlling almost any perishable item, when it comes to price control, is one of the most difficult, technically and actually, of any problem faced in the entire price-control field.

Now, as far as the question of farm prices is concerned, the record shows that in the last quarter of 1951 the income of farmers or farm proprietors rose to an annual rate of 18 billion dollars. This is a higher annual rate than the previous peak in 1948.

I am inclined to agree with Mr. Galbraith that you do not obtain the best incentives to higher production by the meat-ax technique of saying, "Here is a higher price; whoever comes up to it, comes up to it."

I think incentives very frequently work better when you dangle the carrot and say, "Those who stick their heads up a little further get a little snip at the carrot."

Basically we are spending a lot of money on a farm price program even though farm incomes have risen significantly.

I was looking at the President's budget message, and I find in there, for example, we are going to spend 188 million dollars on the International Wheat Agreement. Why are we going to spend as much as 188 million dollars on the International Wheat Agreement? Because if we export wheat we must export it at $1.80 and make up the difference between $1.80 and any higher price in the form of subsidy.

Why are we concerned about its being higher than $1.80?

One reason is that we have a subsidy or price support program on wheat which comes in another piece of the budget. This support program helps to hold the price above $1.80. Thus, by the payment of one subsidy to hold up the price of wheat, we make it imperative to pay another subsidy in order to send some of that wheat out of the country.

Mr. Galbraith. That is not quite accurate, Jules. We have a treaty commitment under the wheat agreement, and since we are a country that honors treaties, we are obliged to honor that. The market price is above the wheat-agreement level, and that is the basic reason why we are going to have and are having subsidies.

Mr. Backman. That is right; that is what I say.

Mr. Galbraith. Maybe the wheat agreement was unwise, but the fact is that we have a commitment for another year.

Mr. Backman. I understand that, Ken.

My point is that if you use price supports to hold up the price of wheat, then in the process of honoring that treaty commitment you get involved in a larger subsidy on the wheat picture.

Mr. Galbraith. Well, wheat is well above the support price, though.

Mr. Backman. That is right. We started out with this international agreement, as I recall—the figures are not all here—with a commitment that appeared to involve less than a hundred million dollars. When the wheat gets above the support price, or above this $1.80 price, we must make up the difference through the public treasury, and to the extent that a price-support agreement helps to

[1] Jules Backman, Rationing and Price Control in Great Britain, the Brookings Institution, 1943, pp. 16–17.

keep it above, every cent we keep it above means a cent more in subsidy when the wheat is shipped out of the country.

Mr. GALBRAITH. $2.10—that is only 30 cents above the agreement price.

I am advised that the price of wheat has always gone above the support level every year before the end of the season, so what we are talking about is really market price versus this international agreement.

Mr. BACKMAN. That is right, but the market price is influenced by the support-price program.

Mr. RUTTENBERG. I wonder, Senator, if I might come back to a point Mr. Backman makes when he talks about fruits and vegetables.

I was very much amused as to his reasons why the cost of living of the consumer in the Consumer's Price Index went up.

During the lunch hour I made a little calculation, going back to February, which is where you went to this morning in your discussion, if we go back to the point where the prices went down, you said you would find that the total cost of living could be explained by what is happening with the fruits and vegetables.

Mr. BACKMAN. I did not say that.

Mr. RUTTENBERG. What did you say?

Mr. BACKMAN. I said the change in food prices in the last several months can be explained by that. That is exactly what I said.

Mr. RUTTENBERG. Let us look at the facts. Fruits and vegetables constitute about 12 percent of the food component of the Consumers' Price Index. That means that it represents about 4 percent of the total, index, the total Consumers' Price Index, so that for every 1 percent that the cost of living index goes up, fruits and vegetables would have to go up 25 percent to account for a 1 percent increase in the index.

That means, therefore, that since February, when the cost of living index has gone up 3 percent, that fruits and vegetables would have had to go up 75 percent to tbe responsible for the cost of living index going up. Actually, since that time, they have gone up 10 percent, fruits and vegetables.

Mr. BACKMAN. Just to make sure the record is clear, Mr. Ruttenberg, I referred to the change in the last few months and not since February, but in the last few months—and I have the precise figures here——

Mr. RUTTENBERG. Let us pick any period. Have they gone up 75 percent to justify the use in the cost of living index?

Mr. BACKMAN. They do not have to go up 75 percent if you are talking about what happened in the last few months.

The cost of living index was 183.8 in February; it was 185.5 in August; it was 186.6 in September; and it was 188.6 in November.

Mr. RUTTENBERG. And it is 189.1 the next month.

Mr. BACKMAN. That is right.

Mr. MASON. You had better get clear whether you are talking about the index of food prices or you are talking about the Consumer's Price Index.

Mr. RUTTENBERG. I am talking about the Consumers' Price Index, and in the food component of the index, fruits and vegetables represent 12 percent but they represent 4 percent of the total index.

Mr. BACKMAN. To give you the precise figure from September to December, which figures I happen to have at hand, the food index rose from 227.3 to 232.2. The entire rise was accounted for by fresh fruits and vegetables during that period. They rose 25 percent, and accounted for 12 percent of the index.

Mr. RUTTENBERG. Four percent.

Mr. BECKMAN. The food index. That was accounted for entirely by fruits and vegetables. That was the rise.

Mr. RUTTENBERG. I think that could bear some examination by the committee.

Mr. BACKMAN. Table 3 shows the changes in the important components of the retail food price index between September and December 1951. It will be noted that many of the food groups listed showed declines in prices. The increase of 25 percent for fresh fruits and vegetables overshadowed by a wide margin the changes in other items. All of the increase in the food price index from September to December was accounted for by the 25 percent rise in prices of fresh fruits and vegetables. Exclusive of the changes for this group, the food index would have declined by 1.2 percentage points. The over-all rise in the Consumers' Price Index from September to December was 2.5 points. Of this rise, 2.2 points were accounted for by the sharp increase in the prices of fresh fruits and vegetables. Clearly, there is no evidence in these data of the emergence of a new price spiral. As new supplies of fresh fruits and vegetables come to the market, it would be expected that this recent upsurge in prices would be reversed in whole or in part.

TABLE 3.—*Retail food price index, September–December 1951*

[1935-39=100]

	September 1951	December 1951	Percent change		September 1951	December 1951	Percent change
Cereals and bakery products	189.4	190.4	0.5	Fruits and vegetables: All	205.1	236.5	15.3
Meats, poultry, and fish	275.6	270.1	−2.0	(Fresh)	(204.3)	(255.4)	(25.0)
Meats	277.6	274.6	−1.1	Beverages	345.0	346.8	.5
Poultry	195.1	181.9	−6.8	Fats and oils	161.5	157.8	−2.3
Fish	353.2	351.2	−.6	Sugar and sweets	188.2	186.4	−1.0
Dairy products	206.4	213.2	3.3	All foods	277.3	232.2	2.2
Eggs	239.3	216.7	−9.4				

Source: U. S. Bureau of Labor Statistics.

Senator SPARKMAN. Of course, we could go into this endlessly, I suppose. Naturally some questions go through my mind as to how much of that rise the farmer got and how much of it went to transportation, and all those other things.

I bought a little head of cabbage the other night at the store, such as we used to throw into the pigpen, weighing exactly 1 pound, and I paid 18 cents for it. It used to be that we could get them by the bushel for 18 cents.

Mr. KREPS. Mr. Chairman, I was intrigued this morning by Mr. Backman's statement and checked with the Bureau of Labor Statistics, and we found that while it is time that fruits and vegetables always do go up in the fall, a good part of this is seasonal, and that, therefore, there may be a seasonal decline in some of these fresh fruits and vegetables that Mr. Backman has been talking about, and that it did not account for the total rise in the total index of any CPI, as Mr. Ruttenberg put it, but it did account for the increase in food.

During the same period as shown by our indicators on page 3, in that same period there was a continuing rise in miscellaneous items from 165 to Mr. Backman's last statement, 165.4 on August 15 to 168. There is a 3-point rise there. There was a rise in rent from 136.8 to 138.9. In other words, there were other rises that accounted—helped to account for the increase in the Consumers' Price Index, and that this increase in the price of foods is probably substantially seasonal.

Senator SPARKMAN. Do you have anything further to say, Mr. Backman?

Mr. BACKMAN. I do not want to belabor the record, Senator. My calculations were for September, and for September it is accurate.

Mr. RUTTENBERG. In the fall season fruits and vegetables normally increase. I thought you were going back over the years.

Senator SPARKMAN. In his original statement he said for the last several months, is the way he stated it.

I am not trying to cut you off, but there is another question I want to get in before I have to leave.

I am running late now at being at this other committee meeting that I am supposed to be at.

Mr. Mason, I believe it was you who said something about what is happening to the structure of American business as a result of the cost of mobilization and the stabilization program.

You said, I think, with reference to our resources that you thought that it was tight now, but would loosen up sometime after the pipeline is filled, and so on and so forth; and I think you said in about 18 months.

The thought that went through my mind during that time was this: What is going to happen to thousands of small businesses during those 18 months? I just wonder. I am very much interested in this thing, particularly from the small-business viewpoint. Our Small Business Committee has been giving a great deal of study to it, and I wonder if you gentlemen might take a few minutes to discuss this problem from the small-business standpoint.

Mr. MASON. There certainly is going to be over the next year to 18 months a cut-back in the amount of certain materials, the important ones, steel, copper, and aluminum, going into civilian production.

Now, whether or not those cut-backs are going to have a more adverse effect on small business than large business, I just do not know, Senator. I have not paid much attention to that particular problem.

I would suspect, though, that probably the small-business firms, as they usually do, are going to get the short end of the deal, and probably the cut-backs are going to affect them more adversely than they will the larger firms operating in the civilian sector of the economy.

Whether or not one can prevent that from happening by any effective method of allocation, I just do not know. I think that is likely to be the outcome.

Senator SPARKMAN. Does anyone else have a comment on that?

Mr. KREPS. Mr. Chairman, I wonder whether Mr. Galbraith would elaborate a bit on the book to which he referred this morning, in which he deals partly with this problem, not so much with respect to small and large business—insofar as they are concerned, as this whole problem of the structural change. His book is called American Capitalism; the Theory of Countervailing Power, and as he elaborates in it, I believe, there are two sets of controls: One that is formal and governmental, and the other that is informal or autogenerative.

Small business, being a part of that picture, I would like to know what he feels the impact, what Mr. Mason just talked about, is likely to be on the chance for these informal autogenerative counterbalances to grow up in the economy.

Mr. GALBRAITH. Mr. Chairman, that is a formidable question.

Senator SPARKMAN. It sounds like it to me, with all of these autogenerative processes.

Mr. KREPS. You started it, sir.

Mr. GALBRAITH. I must confess I am somewhat at a loss as to where to take hold of that, but, perhaps, I might do so without running the risk of verbally putting the whole book into the record by picking up where Professor Mason left off.

The problem here goes back, I think, to one of technology. Within any large firm there are great technical resources for improvisation. That exists in several different forms. The mere existence of a multiproduct line gives a great possibility for shifting under circumstances where the supply of resources, the supply of minerals and metals, is restricted.

If one product line suffers there is always a chance that another one is expanding, and equally important, possibly more important, is the technical resource and research and scientists that the large firm has back of the production process, which the small single-product firm does not have.

Now, that leaves me very little doubt that in the period such as you face in the next 18 months, the position of the large firm is better than that of the small firm, quite apart from the fact that the procurement agencies—and I do not criticize them for this; I think it is perfectly natural and normal that the procurement agencies will always find it easy or easier to deal with a few large firms than a great number of small ones.

As to whether there is any answer to that or not, I may make only one suggestion. Incantation will not work. I am quite sure of that, and incantation is the resource, the weapon of a Federal Government principally on this matter. The Department of Commerce, the RFC, the other agencies of Government, come before congressional committees, and they will without exception explain how much they love small business and how good their advisory service is, how effectively they can pray for the small-business man.

Senator SPARKMAN. May I say that I want to agree with you most heartily, and, in fact, it was our philosophy, in line with that, that prompted us to urge the setting up last year of a Small Defense Plants Administration in the hope that it would do something more than pray.

Mr. GALBRAITH. Well, that is my final point. If there is a real determination to do something for the smaller concerns, then we will have to be faced, I think, with the fact that this will cost money; that it will cost more to get contracts and, particularly subcontracts, up to these firms than following the easy route of going to the larger prime contractors.

It will take organization, and also it may take what look like dubious measures from the point of view of conserving the over-all supply of material as, for example, making specific allocation-free provision of materials for the very small producer quite without regard to what he is producing. That means that the war agencies or the Congressmen who sponsor that proposal or proposals of that sort, will have to face up to defending the use of copper, aluminum, and steel, which, from the point of view of the mobilization effort, look very, very unimportant or even frivolous. We cannot have it both ways. That is what it will take.

Senator SPARKMAN. I want to apologize to the panel, but I am going to have to go to this other committee meeting that I am running late for.

Congressman Bolling, will you take the chair? Senator O'Mahoney thought he would be back long before this time. I am sure he will be in in a few minutes.

Mr. GALBRAITH. I would like to say one word in conclusion, Mr. Kreps, and that this has only the more marginal relation to anything I have said in a recent book to which he so kindly refers.

Representative Bolling (presiding). Dr. Mason, I understand you have to leave very shortly, and I thought, perhaps, you would like to take advantage of summarizing your views before you leave.

Mr. MASON. Yes, I have to leave at 3:30.

I do not think I want to go over ground I have already covered, Congressman.

On this point that Mr. Galbraith just made, I would certainly agree with him. There really seem to be two points to it, though: One, whether small business can somehow or other get a fair deal on the letting of contracts that are connected with the defense program; and I would agree wholeheartedly with him that if they are going to get an equitable treatment it is going to cost the Government substantially more than it would otherwise do to fulfill these requirements.

The other point has to do with what is done with the amount of material that is left over after armament production is undertaken, and whether or not small firms are likely to get an equitable share of those materials in their civilian work.

Now, that problem just leaves me baffled as to how to handle that. I think I am of the opinion that they are not likely to get a fair deal, but I am incapable really of suggesting any particular device that would make it possible for them to do so.

Representative BOLLING. Would you care to comment on the point that I raised a little earlier with reference to the question of the impact of present inventories and the significance, if any, of the overbuying that took place, if it did, and what the significance is from your point of view?

Mr. MASON. Of course, you have got to distinguish—if you are talking about inventories—between consumer inventories and business inventories.

On the consumer inventory side my own impression is, and it is just an impression, that stocks are quite high.

My own guess would be that the automobile industry is going to find it hard this year to sell all the cars that can be produced with materials that are allocated to it.

Now, that is probably not true with respect to a lot of producers of consumers' durables.

Certainly, also consumers stocked up very heavily in textiles and soft goods, and I think it is going to be probably several months yet before those excessive inventories are exhausted.

On the business inventory side, I think there has been a very substantial accumulation during 1951 of inventories, but I think you would have to come to a very specific set of conclusions industry by industry as to whether those inventories are likely over the next year or two seriously to affect the amount of buying, and I just do not know enough about the situation industry by industry to have an opinion on that.

The CHAIRMAN (presiding). I am sorry to have missed what must have been a very interesting discussion.

Representative BOLLING. I have been raising a point of overbuying and inventories, and their effect on the year ahead.

Dr. Mason has to leave early, and he was making a statement.

The CHAIRMAN. I am not going to open any new vistas here.

Were the subjects that I mentioned at the close of the session this morning discussed?

Mr. LESTER. I think I have some open, Senator, but I do not want to take Mr. Mason's time, if there is anything left for him to say.

Mr. MASON. I think I have said everything I want to say, Senator, unless you have any particular questions to address to me.

Mr. JOHNSON. Mr. Chairman, may I just refer to your comment, which indicated, perhaps, some inconsistency in what I had said on the capital formation side with what Dean Mason had said, and I would just like to point out that I do not think there was any inconsistency there.

Dean Mason's remarks indicated that the possibility—and I would extend that to say the eminent desirability—of maintaining even through the short-run period, but certainly over the longer-run period, the level of investment required to expand our productivity in this country. This is not inconsistent with the proposal that, particularly during the next 18 months and possibly for some time thereafter, we should take much more vigorous efforts to prevent types of capital formation which do not fall into that category. The possibilities of restriction there are very great.

He indicated his guesstimate was that, perhaps, 50 percent or less of the amount of investment fell into the category of reproductive investment.

The CHAIRMAN. What impressed me about the discussion this morning, and, in fact, about all of the testimony before this committee and what happens in Congress, is that Congress reluctantly puts on controls. When it does put on controls, it usually attaches some strings to the controls by which they can be withdrawn, and the control laws are specifically limited in time, and are seldom extended until they are just about expiring, and sometimes until after they have actually expired.

The officials appointed to enforce the control laws seem to do so reluctantly, and even while they are enforcing the controls they come up and testify to this committee, as Mike DiSalle did just a few days ago, that the committees looking toward decontrol are about to be appointed, and so forth.

In other words, we have what might be called a split personality in our Government. We adopt a rigid or semirigid control or we adopt controls which are required to equip a nation to fight a war upon the one hand, while we are struggling to get back to what we call a free economy upon the other hand. The consequence is that we do not do a good job of totalitarian controls nor do we do as good a job as we would like of a free economy, so if it be true that the productive capacity, the human and material resources of the United States, are so great that we can maintain a diversion of 20 to 30 percent of our output to the purposes of war, and, at the same time, maintain an expanding economy, it leads directly to the question as to how long such a dual operation may continue, how long can our human and material resources maintain such an operation.

There are those, I said this the other day, who believe that we ought to end it all now by a sudden and overwhelming military attack. There have been those who have advocated preventive war. No person in Government with responsibility in Government has advocated that, and the President's economic report and his message on the state of the Union are all based upon the reverse, that we should maintain a preparedness status to repel attack if it should come.

Now, there are others, like former President Hoover, who advocate abandoning the support of European armament and the support of European economy, of retiring behind our own ocean bastions, and maintaining our preparedness here.

How long, in the judgment of a group like this, could we continue military and civilian production under either one of the two latter alternatives?

Mr. MASON. Mr. Chairman, I cannot answer all that question, but before I go I would like to make a comment on price controls.

It does seem to me that the primary function of price controls at this particular juncture is a stand-by function. I think it is quite possible that at some time within the next year or 18 months there could be a rush from money into goods of the sort that you saw in the fall of 1950. I mean there could be a change in the military situation for the worse, which would lead people to the conclusion that we are going to make a marked increase in the military program, which might very well have those anticipatory consequences, and I do think that in order effectively to exercise the stand-by function you have got to have a law in existence, and I think you have got to have ceilings, because those things cannot be improvised very rapidly.

My own impression would be of the existing price-control law that it certainly permits plenty of flexibility within the limits of those ceilings to make the kinds of adjustments that you have in mind, and which are quite necessary if you are going to maintain productivity.

I do not think that the present price-control law can exercise very serious limitations on those adjustments. I think it does perform a very useful function in this stand-by way that I mentioned.

The CHAIRMAN. Then, it is your opinion that the controls in the Defense Production Act should be strengthened?

Mr. MASON. I think I would leave them just about as they are now, if I were to offer an opinion. I certainly would maintain the law; I certainly would maintain the ceilings. The ceilings are awfully flexible as they exist now, but they could exercise a very important restraining influence on the price level if we did have a rush from money into goods of the sort——

The CHAIRMAN. Mr. Galbraith was of the opinoin this morning that while that would be perfectly acceptable for the short run, he is very much concerned about its efficiency for the long run; is that right?

Mr. GALBRAITH. Yes; although I was addressing myself primarily to the short run.

The CHAIRMAN. How long is the short run that you had in mind?

Mr. GALBRAITH. I should say, to be quite specific, I see the prospect of reasonable balance in the economy for the next 6 months or a year. If we get a continuing and large bulging in the military expenditures, and also in this, it seems to me, interesting fact, should there be any general withdrawal of the regulations, should the American people come to think that things were going wild again or there was danger of it so they began to change the liquid assets that they now hold into goods, the situation might become very much more dangerous.

The CHAIRMAN. All right. But your answer, then, is that for the next 6 months, maybe 5 months, until July 1, which is the beginning of the fiscal year 1953, we can sail along on a fairly even keel, barring some unexpected developments; but during the next 12 months the question is: Can we hope within that period beginning on the 1st of July 1953 that the international situation will have so settled as to enable us to abandon controls or maintain the present system?

Mr. GALBRAITH. Let me make just one qualification of that. There are a number of things which I would like to see done. I would like, for example, to see the present congressional restraints in the discretionary control of consumer credit eliminated—I think that was a mistake.

There are a number of holes in the tax structure that I would like to see plugged. There are a whole range of those things which are the continuing——

The CHAIRMAN. Those are details.

Mr. GALBRAITH (continuing). Unfinished business of stabilization.

The CHAIRMAN. I am not talking about details.

Mr. GALBRAITH. I am certain that the Congress is not going to pass a tax bill in the next 6 months, nor eliminate the Capehart amendment nor the escalation amendment, nor knock out priority with respect to agricultural products, but I do not feel deeply alarmed about that.

Mr. JOHNSON. Mr. Chairman, may I make a comment here?

The CHAIRMAN. Surely.

Mr. JOHNSON. I am a little disturbed about the comments of Mr. Mason about the stand-by function of controls, and the general impression that the economy is now in reasonable balance.

Mr. Backman this morning also referred to the trend in the wholesale price index during the course of 1951. I think it would be very unfortunate if people operated on the impression that this current balance, so-called, is the result of market forces primarily or entirely.

I think that the balance we have is probably more attributable to the present controls than it is to market forces.

I am sorry I do not have recent figures on this, but several months ago, we had a quick detailed analysis of the BLS wholesale index made, going back to the actual prices of the items in that index. This was in September, as I recall, and we checked the prices of the individual items in September as against those in February right after the freeze.

Now, in that same 8-month period the index, as a whole, had declined in the neighborhood of 3 percent, and one might think that the market forces were taking very good care of the situation.

But of the individual nonagricultural items priced, if I recall the approximate percentages correctly, about 60 percent were at the same level as they had been in February—that is, the freeze level; and about 12 percent or so were somewhat higher than they had been in February. It was only approximately a quarter of the items which were below their February level, mainly in the soft goods area. I think that an analysis commodity by commodity like that will indicate that in a very substantial proportion of items at the wholesale level today the thing that is restraining their price is the existence of price control and not the let-up of market demand. The general impression you get from looking at the total wholesale price index, which has declined, is misleading in terms of the real bite that the controls have at the present time. The impact of controls may not currently be directly important in consumer goods, but it is important in those industrial areas where the combined demands of Government, business, and consumers have created real shortages.

I would also, despite what Mr. Lester said, extend that to the wage side as well. I think that had we not had wage stabilization we would have had a marked swelling up in wage increases. It is not that, if you decontrol wages tomorrow, employers across the country would go out and raise them; but what you would get is a gradual accretion of excessive increases at points where the pressures are greatest, in the aircraft factory areas, in the shipbuilding areas, in the machine tool areas, and so on, which would gradually extend throughout the other companies in the industrial area.

Mr. BACKMAN. I would like to register a very vigorous dissent from that last statement. I think prices stopped going up early last year because people stopped being afraid that total war was going to take place immediately.

If you follow the course of these prices and the course of events about a year ago or a year and several months ago, we find a picture that looks something like this: Upon the outbreak of war a very substantial amount of scare buying developed, largely because of the fear that people could not get goods. It was not so much fear of a price rise. Rather, it was fear that they could not get goods. This fear developed because the memory of World War II, shortages, when we did not produce many of these hard goods, was very strong.

The figures I cited earlier concerning durable goods expenditures immediately after Korea support this interpretation.

We began to get a little bit of a lull, very minor one, as we came into the fall of 1950. Then the Chinese intervention late in 1950 started off the second splurge of buying.

During that period it seemed as though we were going to lose a good part of our equipment and if we judged by the newspaper head-lines that we might be pushed out of Korea. The resulting fears that we were embarked upon an adventure that immediately meant total war, and hence immediately meant that many of these hard goods would not be available, led many people to rush out to buy.

Now, we come along into the early part of 1951, about February or March, and it becomes apparent that, instead of being pushed out of Korea, we are there to stay; instead of moving backward we are moving forward. As a result the fears, which led to scare buying, began to subside, so much so that within practically a matter of days, almost accompanying the turn-around of movements of the Armed Forces, we found discounts offered to induce the purchase of automobiles rather than the charging of premiums. We found instead of premiums and a rush to buy many types of hard goods, all sorts of price wars which, by May, I believe it was, May or June, really began to become a national factor, and I think this committee issued a study at that time dealing with the magnitude of price cutting.

Now, that was not only soft goods, it was hard goods. Why did it take place? Because when people believe there would be available 3 or 4 million cars, the rush to buy will not be the same as when they are afraid that there are going to be none available as in World War II.

Now, I for one, am convinced that it was not the imposition of price control which held down prices; I think it was this change in buying attitudes on the part of consumers.

I pointed out this morning that we have had this apparent paradox, namely, a fairly large budget surplus from June 1950 until March 1951, with prices moving up sharply; then a fairly large budgetary deficit, and prices moved down moderately from March until December 1951. I think the explanation is found in this whole area of consumer psychology.

In the Economic Report, the Council of Economic Advisers talks about consumers voluntarily electing to save. I do not think we can ignore that factor. I think the most important single factor in the price picture in 1951, and I agree completely with the Council on this, was the fact that people did not go out and spend all of their higher incomes; if they had we would have continued to have the price pressure. It was not price control that stopped consumers' spending. It was the cessation, the subsiding of fears that what started out, if I may quote it, to be a police action and then developed into a larger area of action, was not immediately going to degenerate into total war.

It seems to me that was the most important factor, the psychological factor.

The CHAIRMAN. Is it your opinion, then, that, generally speaking, the program of preparedness as announced by Mr. Charles E. Wilson is a sound one, that we can spend a small portion, from 20 to 29 percent of the national income, for military purposes, and with present laws keep the situation pretty well in balance?

Mr. BACHMAN. It is my judgment that the soundness of this program depends upon one's view as to the nature of the threat to our national security.

I believe it is a very serious threat. I think if we had to spend 40 percent or 50 or 60 percent, we would spend it, and that the Nation could stand it.

The question is not can we stand this as an adventure nor whether we can stand this program as something which we are doing for the sake of doing it. We are engaged in an armament program because we have to do it; we have to prepare as a matter of national survival. I think it is a real tribute to the vitality of the economy that not only have we been increasing these armaments and really getting on a make-ready basis, but we have been able to do it and cut so little into our consumers' goods output.

The CHAIRMAN. You think that that can be maintained for some time in the future?

Mr. BACKMAN. I think that the armament program must be maintained, and if the price of maintaining it is a moderate drop in the level of living, that is a very cheap price in comparison with the alternatives.

None of us like these things—in fact, in connection with all of these policies, and although I speak only for myself—I am certain the other members of the panel would agree with this—it is not a question of what is best, but which is the least worst. All the alternatives are bad, and to my way of thinking it is the least worst to make sure that we are strong and ready.

The CHAIRMAN. On the basis of the present appraisal of the threat to our national security, there is no doubt in your mind that the economy of the United States is strong enough to carry the military expenditures presently projected?

Mr. BACKMAN. I think we are strong enough to carry it, and I go along with Ken Galbraith that this lull can continue.

The CHAIRMAN. If there is a greater threat to our national security, and then that compels us to pay a higher price for national security, the economy can then stand it provided we are willing to bear the hardships that will be essential?

Mr. BACKMAN. Well, Senator, the analogy I like to use is that of a person who is sick. If you are only a little sick, you spend a little money to get better; but if you are very sick, you spend everything you have got to get better. But I think the less we have to spend, the better, but we should spend every cent we have to spend to do the job right.

Mr. GALBRAITH. Mr. Chairman, could I say just a word about clarifying the previous position? I must say I find very much with which to agree in what Griff Johnson has just said, and my own reference to the situation of comparative stability in the months ahead, and I do not minimize the importance of the existing structure of controls in that stability.

I think they are important. The one point where I would be concerned with what Dick Lester suggested this morning about decontrolling wages, it is not so much the effect of the decontrol on wage levels, although I think it would—with Johnson it would be considerable—but rather the effect of that on public attitudes.

If people generally were to assume or were to come to the view that the brakes were off, that they had better spend now in anticipation of price increases, that could become a very serious factor, a very alarming factor, and that leads me to make a suggestion with reference to what Mr. Backman has just said.

He attributes the cessation of consumer buying to the change in the military picture in Korea. I cannot but think he is partly right on that; but I cannot but think that anyone who deals in anything so intangible as consumer psychology has to allow for many factors, and I would want, for example, to emphasize very importantly as one of the factors the decision of the administration a year ago to put on the freeze and to stabilize wages.

I think that, more than anything else, gave the people of the United States the feeling that the United States Government was moving in on their side; that there was a powerful influence that was coming to their protection; that things were not going to go wild, and that they could stop a frenzied sort of buying which they felt obliged to do as long as the future was unknown, but which they really did not want to do.

Mr. Lester. I want to explain my position, which apparently is not as clear as it might be. The thing that impresses me in discussing commodity prices and wages is the difference between them. They are determined usually in a different way and quite different considerations enter into increases or decreases of wages and increases or decreases of prices, or wage ceiling and price ceilings.

You have collective bargaining with respect to many of the wage elements and you have the possibility of strikes; you have a whole host of factors around the wage matter which do not apply to the same extent in the price matter. Negotiated wage agreements run for as long as 5 years. There is no price counterpart.

The same thing would be true with the stand-by argument. I think there is much more need for stand-by price controls than there is stand-by wage control. It is really prices you are trying to hold down. Wages are only an accessory to that fact.

You need experts in price. I do not think you really need experts on the wage side in the same sense in a stand-by capacity. The expertness on the labor side has much more to do with the nonwage issues in dispute.

You can recruit people pretty rapidly in an emergency for wage control. You can use them around the country on a part-time basis. Delay is not so difficult with retroactivity. For price ceilings you need experts in that particular commodity. Price ceilings and wage ceilings are in practice quite different animals. There is a tendency over time as is quite clear for wages to rise relative to prices, and it is things of that sort that I think we want to look into, because it seems to me our thinking on this thing, if we are not careful, is going to be, so to speak, right down the groove. It is the easiest thing to think of all direct controls in the same terms as we have over the past year, think of them continuing as usual next year and the year after, and I think we ought to take into account what that may mean, especially to collective bargaining and the threat of compulsory arbitration of labor disputes, and whether there are not possibilities over any length of time for taking off the wage controls or for some combination of selective price controls and local or no wage controls.

You asked whether I thought in terms of selective price and wage controls. It seems to me there are all kinds of possibilities.

It is possible to have a general price control with no wage controls, or general price control and selective or local wage control.

It is possible to have selective price control and general wage control.

It is possible to have no price control, if you want it that way, and general wage control.

Those countries that I referred to abroad, in general, have had price control but not governmental wage control.

So it seems to me there are all kinds of possible combinations, and which one you select may depend upon the circumstances—certainly it will depend upon the political climate and the attitude of the people in the country.

I do not anticipate that we will during this calendar year, let us say, have a separation of price and wage controls.

I raise the question whether over any long-time period there ought not to be. Selective control in prices is much more possible in some respects than selective control in wages, depending on how far you go through with it.

Local control of wages makes some sense, whereas local control of prices may not. That is the sort of thing that I had in mind.

The CHAIRMAN. You spoke of taking a new start. When would you think such a new start could be taken?

Mr. LESTER. Suppose you took off wage controls and for some reason or other the price controls could not hold, I see no real difficulty in slapping on wage controls with a wage freeze on at that time, if it is really necessary. I think you would not have anything like the problem, perhaps, that you would have if you disbanded your price control and had to slap on price controls suddenly. Wage agreements are generally fixed for periods of time and delays can be worked out. The abandonment of wage controls could be complete, whereas at a minimum you might want to keep price controls on any materials under allocation and might want to maintain some price ceilings on other lines. In other words, the abandonment of wage control perhaps should be sudden but the abandonment of price control should be a gradual and piecemeal process.

Secondly, it seems to me that on the disputes end of it, you do have other alternatives. I do not say they are necessarily the best ones under the present circumstances, but with the Wage Stabilization Board in charge of disputes, you have a single Board continuing over a period of time and with the same personnel and you may get precedents established and you may get people feeling in a certain way about that Board, which would not be the case if you had ad hoc boards, for instance, settling each dispute.

I think the realm of possibilities ought to be opened up and examined. That was my point.

The CHAIRMAN. Have you anything to add at this time, Mr. Ruttenberg?

Mr. RUTTENBERG. No.

The CHAIRMAN. Mr. Reynolds?

Mr. REYNOLDS. I am not sure that I would agree entirely with Mr. Lester's proposal to shelve wage controls for the time being. I think it would be hard to show that they have had much effect up to this point. It is quite possible they have raised some wages as much as they have retarded other wages, and yet I feel there is a net gain in keeping the apparatus in being.

It does to some extent have the retarding influence which I was arguing for this morning of holding things back a little bit, of acting as a brake on the upward movement.

It does handle the problem of disputes in war industries, which has to be handled by some method or other. And I am sure that, if you did knock it out for the time being, you could recruit a new group to handle it and get it going again just as fast as Mr. Lester indicated:

This takes time. Even granted there are lots of labor experts around the country that can be brought into this, it takes time to assemble them and get them in operation.

Mr. LESTER. That is part of your delay.

Could I just make one remark in connection with that?

It is true that you delay, but if you have retroactivity your delay may not be really so effective as it is implied. The workers may get it all in one bunch.

Mr. REYNOLDS. Yes.

I disagree a little bit, too, I think, with the notion that everything is now in balance and will stay there for the next 6 to 9 months. I am not at all convinced that we are out of the woods.

What I said this morning about wage policy was oriented toward the short run and toward the threat of inflation, which I think is very much alive.

That is why I advocated that we hold back a little bit on rapid wage increases and on very large wage increases.

I would take quite a different view, obviously, if I were talking about a long-run policy and how things should run in normal times.

I did not want to give any impression that I advocated shifting the whole burden of inflation onto labor. I think the mere fact that I talked wages and for the sake of saving time did not talk of prices, profits, and so on, may have conveyed that impression, which I certainly did not intend.

I would argue, rather, for a general policy of restraint by all groups in the economy and some equitable sharing of whatever burdens we have to take on.

The CHAIRMAN. Did you have anything more to say?

Mr. GALBRAITH. For the sake of the record, I want to differ with Mr. Lester on one question of fact.

He said that, in general, other countries during World War II did not couple wage and price policy. Of the countries that had an effective stabilization policy in World War II, I think we can think mainly of the British Dominions, the United Kingdom itself, Germany, and the United States.

In all of those countries, Australia, Canada, Germany, and the United States, there was wage control in connection with the price control. There was not, to be sure, in the United Kingdom, but they had, also, a voluntary system of wage control through the union standstill agreement which was the practical counterpart of an effective wage control.

So I think that Professor Lester leaves an unfortunate impression when he says that the coupling of wage and price control, not in the sense of the Defense Production Act, I hasten to say, but the coupling of the two measures, in general, is not common practice. I would be inclined to argue that it was common practice.

Mr. LESTER. I was thinking particularly of England and the Scandinavian countries, and I was not only thinking of the war period, but this more recent period since the Korean outbreak. Australia, incidentally, has had compulsory arbitration of wages for over five decades and that system has remained unchanged during that 50-year period. Canada, since the Korean outbreak, has had neither price nor wage controls but has attempted to rely largely on monetary fiscal controls, which I generally favor.

England and Sweden have had some of the same problems that we do.

I recognize that they have a different situation in their whole labor movement. They have, particularly in the Scandinavian countries, much more control by the central federation.

The only thing that I wanted to bring out is that there is not any real compulsion, as I see it, to link wage and price controls anything like as rigidly as they are linked in this present legislation. And I think there are some real disadvantages of it particularly over any long period of time.

I would call to the committee's attention an article by E. H. Phelps Brown and B. C. Roberts of the London School of Economics on Wages Policy in Great Britain, which has just appeared in the January 1952 issue of Lloyds Bank Review. They state:

> It is a remarkable feature of the British economy during and since the Second World War that amid controls of many kinds there has been virtually no control of wages. The month after Pearl Harbor, President Roosevelt set up the National War Labor Board, with complete jurisdiction over labor disputes, and again in January 1951, President Truman set up a Wage Stabilization Board. But in Great Britain the fixing of wages has continued since the war began to be carried out very largely through the same private and public processes as before.

And they add:

> So at a time when all manner of direct controls have been imposed, and we have had direction of labor even in years of peace, we have not imposed direct controls on wages.

Reviewing the British experience they do not find that it affords good grounds for national wage control under the conditions that prevail in Britain.

I repeat, gentlemen, I am very worried about the effects on collective bargaining and labor relations in this country of continuous Government control of wages extending year after year in the absence of all-out war. The current steel case is only one indication of the consequences of extended Government regulation of labor agreements.

The CHAIRMAN. I think this brings us pretty close to the conclusion. Professor Backman wants to add something to what has been said.

Mr. BACKMAN. I want to make one point clear for the record since I may be partly responsible for the constant return to the term "balance."

When I pointed out that the increases in prices, wages, and profits before taxes since before Korea all were of equal magnitude, I think I said they had now moved up to a new plateau.

I made no assumptions concerning whether or not they were in balance when they started, and to the extent they were out of balance when they started, they could still be out of balance at this point.

I would like to close my own comments by saying to the committee that I think this procedure which the joint committee has taken the time to undertake is a very constructive approach to meeting your responsibilities. I hope that the comments we have made will be helpful. The idea of calling in a group of outside technicians and having them sort of kick the ball around a little bit, and the committee taking the time to listen to them, it seems to me to be a very constructive development.

The CHAIRMAN. You can make it much more helpful if you will follow the suggestion which we have given to previous panels, and that is that you prepare now for printing in the record a 1-page summary of your views, following the panel discussion. If you will direct those summaries to Mr. Ensley, we will have them printed in the record.

Representative BOLLING. You said something, Dr. Reynolds, about equitable sharing of the burden. I think that was the phrase that you used.

Mr. REYNOLDS. Yes.

Representative BOLLING. I would like to get some comment from the panel as to whether they feel that since Korea there has been an equality of sacrifice on the part of the various economic elements in this country.

Mr. LESTER. Well, you know professors do not feel as though there has been a completely equitable sharing of the burden under this condition.

Representative BOLLING. Do not limit it only to the white collar people.

Mr. LESTER. If we go into that in any lengthy discussion, I am afraid we will be here some time, but I would say that between the larger groups, agriculture, labor, and industry, it may not have been so bad as we might have thought sometime ago.

It depends on what base you are measuring it from, but it looks as though most of the large groups have fared pretty well under the present circumstances.

Mr. REYNOLDS. I would agree with that. I do not think it has been too bad. I think there has been hardship on some white-collared groups, and some of the fixed-income groups, pensioners, and so on, but apart from that I think we have done a relatively good job up to this point.

(The following statement was submitted for the record:)

STATEMENT OF STANLEY H. RUTTENBERG, ON CONGRESSMAN BOLLING'S QUESTION ON EQUALITY OF SACRIFICE

At the close of the panel discussion, Congressman Bolling asked whether there had been equality of sacrifice by all of the groups in our population. Because of the lateness of the hour, I did not at the time the question was posed, state my position.

It seems to me to be perfectly clear that one of the big problems of the whole economic stabilization program to date has been that very little equality of sacrifice has taken place. The phrase "equality of service" has been mouthed by many people, but very few groups have actually been called upon to sacrifice very much.

At a time when the normal corporate tax rates have been increased, and when, in addition, an excess profits tax has been imposed, many corporations, because of the accelerated amortization program, are not paying their full share of our Federal tax revenue. It can be conservatively estimated that close to $1 billion in Federal revenue will be lost in each of the next 5 years because of the tax amortization program.

In addition, many corporations are able to secure automatic price adjustments and thereby improve their own profit position at the expense of the general public. The Capehart and Herlong amendments, which permit the passing on of all cost increases and the pyramiding of these increases by the maintenance of normal profit margins, do not require much sacrifice on the part of the manufacturer, producer, distributor, wholesaler, or retailer.

Provisions have been made by the Office of Price Stabilization to permit almost automatic price adjustments. There is not even the formality required, in the majority of instances, for the individual to submit his determination of the higher price for review by OPS. Price increases can be passed on, and the seller is required only to submit the facts for later review by OPS.

Equality of sacrifice can be given considerable lip service by the manufacturers, producers, wholesalers, and retailers, because it does not require very much, if anything, of them.

On the other hand, in the wage stabilization field, the American worker can execute a collective bargaining contract with his employer wherein both voluntarily agree to a specific wage increase, but this must be submitted to the Wage Stabilization Board for approval before it can be put into effect.

There are very few types of wage increases which can be automatically put into effect without prior approval. This is in direct contrast to the automatic nature of putting price increases into effect without approval by OPS.

In addition, the existence of a collective bargaining contract prevents the worker from even securing the benefits of those few wage increases which can be put into effect automatically because of the requirement that changes cannot be made during the life of the contract. Even those wage increases based upon rises in the cost of living which can be automatically put into effect without prior approval must wait until the contract expiration date. The only exception to this is the existence of an escalator clause in the contract. However, if a union has a collective bargaining contract which has another 6 months, 9 months or a year to run and does not have an escalator clause incorporated into the contract, the worker must wait until the expiration of the contract before he is able to secure the benefits of even this automatic cost-of-living adjustment. This obviously involves considerable sacrifice on the part of the individual worker.

If, on the other hand, we had an adequate Defense Production Act that held prices in check and prevented the cost of living from rising, the need for automatic wage increases based upon rises in the cost of living would become academic.

It would be my recommendation, therefore, that the Joint Committee on the Economic Report strongly support the extension of the Defense Production Act and that specific improving amendments, which I outlined in my original statement before the panel, be incorporated in the act.

The CHAIRMAN. Well, again I want to thank you all for your presence here and for the patience that you have displayed in sitting here all morning and all afternoon. The committee is very grateful to you.

I want to insert in the record a copy of a letter which I addressed to the heads of various institutions and organizations and the replies we have received in response to our inquiry.

(The materials referred to are as follows:)

CONGRESS OF THE UNITED STATES

JOINT COMMITTEE ON THE ECONOMIC REPORT

LETTER ADDRESSED TO REPRESENTATIVES OF ECONOMIC INTEREST GROUPS

JANUARY 16, 1952.

Dear Mr. ————: The Joint Committee on the Economic Report is again calling upon a number of leaders of consumer, labor, agricultural, and business organizations in order to secure economic facts and counsel for consideration by the committee in the preparation of its annual report on the President's Economic Report. As you recall, the Employment Act of 1946 directs the Joint Economic Committee "as a guide to the several committees of the Congress dealing with legislation relating to the Economic Report, not later than March 1 of each year * * * to file a report with the Senate and the House of Representatives containing its findings and recommendations with respect to each of the main recommendations made by the President in the Economic Report * * *."

We would appreciate having your comments on the materials and recommendations contained in the 1952 Economic Report of the President and are enclosing a copy of the report for convenience in preparing your reply. In addition, we are including with this letter an outline of the hearings the committee plans to conduct and a list of the persons to whom this letter is addressed.

To be of maximum assistance to the committee in preparing its report to the Congress, and to be included in the printed compendium of views to be published by the committee, your reply should be received by February 6.

Sincerely yours,

JOSEPH C. O'MAHONEY,
Chairman.

CONSUMERS

Consumers Union of the United States, Inc., Colston Warne, president, % Amherst College, Amherst, Mass.

League of Women Voters of the United States, Mrs. John G. Lee, president, 1026 Seventeenth Street NW., Washington 6, D. C.

LABOR

American Federation of Labor, William Green, president, 901 Massachusetts Avenue NW., Washington, D. C.

Brotherhood of Railroad Trainmen, W. P. Kennedy, president, 1528 Standard Building, Cleveland, Ohio.

Congress of Industrial Organizations, Philip Murray, president, 718 Jackson Place NW., Washington 6, D. C.

United Mine Workers of America, John L. Lewis, president, 900 Fifteenth Street NW., Washington, D. C.

AGRICULTURE

American Farm Bureau Federation, Allan B. Kline, president, 221 North La Salle Street, Chicago, Ill.

The National Farmers Union, James G. Patton, president, 300 Independence Avenue SE., Washington, D. C.

The National Grange, Herschel D. Newson, master, 744 Jackson Place NW., Washington, D. C.

BUSINESS

Chamber of Commerce of the United States of America, Dechard A. Hulcy, 1615 H Street NW., Washington 6, D. C.

Committee for Economic Development, Marion B. Folsom, president, % Eastman Kodak Co., Rochester 4, N. Y.

National Association of Manufacturers, William Grede, president, 14 West Forty-ninth Street, New York 20, N. Y.

Machinery and Allied Products Institute, George Terborgh, 1236 Twentieth Street NW., Washington 6, D. C.

National Federation of Independent Business, C. Wilson Harder, president, Drawer 473, Burlingame, Calif.

National Tool and Die Manufacturers Association, George S. Eaton, president, 906 Public Square Building, Cleveland 13, Ohio.

Small Business Association of New England, Inc., S. Abbot Smith, Thomas Strahan Co., Chelsea 50, Mass.

New Council of American Business, Inc., Miles Pennybacker, president, % Voltarc Tubes, Inc., 44 Cross Street, Norwalk, Conn.

Dexter M. Keezer, Director, Department of Economics, McGraw-Hill Publishing Co., Inc., 330 West Forty-second Street, New York 18, N. Y.

STATEMENT OF CONSUMERS UNION OF UNITED STATES CONCERNING THE ECONOMIC REPORT OF THE PRESIDENT

(Submitted to the Joint Committee on the Economic Report at the request of Joseph C. O'Mahoney, chairman)

This past year has been one of confusion to most consumers and it was a year of wrong guesses on the economic front. Official prophesies were belied by events. What the average citizen experienced in his local shopping center during most of the year was not consistent with the headlined warnings from his Nation's Capital. Though abundance, not shortage, was evident, prices that had risen in expectation of shortages stayed high at the consumer level.

This year 1951 was, in short, one that called for careful economic analysis in retrospect. Thus Consumers Union, along with other observers of the economy, looked forward to this Economic Report of the President with particular interest.

Perhaps because the questions that have arisen out of the past year's events are so crucial to our over-all economic welfare, the present report both in its analysis and its recommendations appears inadequate. With the committee's permission, Consumers Union proposes to submit later, for the record, a more detailed description of the questions raised but not answered by the report and of questions not raised but needing answers from the President's Council of Economic Advisers. In this present statement, however, the areas Consumers Union hopes to cover in its later presentation will be digested under the following headings:

1. RECOMMENDATIONS MADE IN THE REPORT

A. *Sacrifice of social needs.*—In the light of the mounting evidence of excess capacity in a growing number of civilian goods industries, the President's statement that we "must hold back on the construction" of schools, hospitals, flood-control projects, low-cost housing, etc., needs much more factual documentation than the report gives. Certificates of necessity and amortization privileges have already been granted to industries, such as the textile industry, for example, where excess capacity is already a burden. Indeed, in most sectors of the economy, both production goals and existing production capacity appear to be still in the realm of guesses. Concrete evidence is lacking. It is asking a great deal of a nation that it sacrifice its educational and health needs. Such a sacrifice hits at the roots of people's lives. If it is necessary, that necessity should be made clear beyond doubt.

B. *Policies to encourage a broader base of public participation.*—Consumers Union has long been a champion of widespread public participation in government. Consumers Union also agrees with the statement in the report that a broader base of participation is needed and with the judgment made there that a solution to this problem has not been found. However, to meet this need the report has no recommendation to make beyond the expressed hope that the National Advisory Board on Mobilization Policy will serve as a vehicle for a more broadly based participation. Consumers Union agrees that the creation of machinery does not solve such a problem, but would like to point out that some machinery is needed for widespread popular participation in the defense effort and that, at the present time, existing machinery is so administered that it is available almost exclusively to highly organized minorities—minorities organized around their interests as sellers and so organized that they tend to promote the growth of monopoly power. On economic matters, the interests of the general public as a whole are vested in the consumer's interest. Today, in Washington, the consumer's interest, the citizen's interest in economic matters, has available to it only limited avenues of expression at a time when public understanding and participation is of cardinal importance.

C. *Price control recommendations.*—The report's recommendations on price control legislation were seriously inadequate in terms of the emphasis on the threat of inflation that ran like a dominant thread throughout the whole of the President's analysis. If the shortages predicted occur together with the rise in personal income foreseen, and if the evidence of high liquid savings actually indicates a backlog of consumer spending power, then adequate price control legislation is a crucial need. The President's recommendation that the Capehart and Herlong amendments be repealed is one that consumers generally would support. But these minimal changes in the existing price control legislation—and only these changes—fail to provide the people of the Nation with adequate protection of their living standards should the inflationary spiral mount rapidly. For some time before the Capehart and Herlong amendments were added to the Defense Production Act in July 1951, price ceilings had been hailed as price goals in the trade and business press. Taken together, the basic legislation and the administrative policies of the Office of Price Stabilization had gutted price control of effective power from the day of the general freeze, January 26, 1951. Therefore, besides the changes recommended in the report, Consumers Union would add, as a minimum, further legislative changes to insure the following:

(*a*) That ceilings be based on reasonable cost, not padded costs or profits, and that reasonable costs be so defined as to include standards of efficiency.

(*b*) That the principle of reasonable cost absorption be explicitly required and that the control agency be given power to determine fair and adequate bases for cost analysis.

(*c*) That where ceilings are necessary, dollars-and-cents ceilings be set and such ceilings posted.

(*d*) That the control agency be empowered to use specifications and standards, where necessary to define the goods subject to ceilings, and that it also be empowered to exercise control over the introduction of new "lines" where the purpose is to evade ceilings. Quality standards should, in other words, accompany price stabilization.

(*e*) That industry representatives be prohibited from taking Government posts in control of their own industry.

(*f*) That minutes of all industry advisory committee meetings be made available in full to the press and the public.

(*g*) That consumer representation at policy levels be assured and that avenues for widespread public participation and public education be provided in order to promote public morale and make fair and effective enforcement possible.

(*h*) That in cases where goods are subject to excise taxes no profits or margins be permitted to pyramid tax costs.

(*i*) That under no circumstances should price-control measures be used to promote monopoly, private price fixing, encouragement of waste of resources, discrimination against small business, or the misleading of the public.

(*j*) That price ceilings shall not be made price supports, or price basements, through the use for this purpose of Government stockpiling policies, or through other National or State legislative or administrative policies.

(*k*) That, step by step with the imposition of any ceilings the control agency be assisted by other Government agencies through programs to build adequate supplies of critically short goods through any one or a number of such actions as subsidies of new productive capacity, lower tariffs, etc.

D. *Need for rationalization of military procurement in spending.*—In light of the magnitude of the sums now allocated to the military in the new budget, and in face of the growing number of newspaper reports about wasteful policies in military buying Consumers Union feels that some recommendation for rationalizing military procurement is long overdue. This question is one of those not mentioned in the report. It is of great significance not only on the simple grounds of waste, but also because a demand on the economy so great as that now reperesented by the military budget can, unless it is handled wisely, create a serious imbalance and hinder the productive power of our whole, interlaced industrial system.

E. *Deflation fears.*—The recommendations made in the report were all based on the assumption that either inflation, or a high level of business activity stabilized at current price levels, was the future prospect. Only by indirection was there any evidence that either the President or the Council of Economic Advisers gave serious consideration to the growing fears of deflation and depression that have been recently expressed by spokesmen from such differing walks of life as John L. Lewis of the United Mine Workers and R. P. Ettinger, president and chairman of the board of Prentice-Hall, Inc. Although the Council may be sincerely convinced that deflation is not probable, or even possible, the uneasiness expressed by a growing number of business leaders cannot be stilled by exhortations to have faith in, as the President put it, or "ingenuity and imagination to utilize this increasing abundance." The memory of the dark 1930's, although not so sharp as the picture of the shortages and inflation in the 1940's, is still alive. Consumers Union feels that the Council should have given more serious consideration to deflation fears and a more detailed program of how such a turn in events might be handled.

II. ANALYSES IN THE REPORT

A. *Consumer savings from disposable income.*—Although the rising rate of liquid savings as pictured in Government income statistics was repeatedly mentioned in the report, the significant fact about such savings received no attention at all; namely, their distribution through income ranks. If, as it would appear from scattered indications, there is a sizable shift in savings further up the income scale, that fact is of great significance to those determining Government policy on a whole range of questions involving price control, taxation policies, wage policies, allocation of Government-sponsored investment, and all actions taken with regard to assumptions about consumer demand for types and kinds of goods. Consumers Union had hoped that this aspect of consumer savings would receive serious consideration from the President's Economic Council.

B. *Economic concentration.*—Since private plant expansion for the production of civilian goods is potentially as inflationary, in the short run, as military expenditures; and since credit control for such expansion is still on a voluntary, not compulsory, basis; a review of how much private expansion has taken place in particular lines of production is sorely needed. The report simply gives totals in dollar terms. If, as the President's economic advisers say, part of the private expansion has resulted from excess profits tax policies; and if, as the business press indicates, the private expansion has been dominated by the very largest companies; a combination of present, lax credit controls for business, together with tax policies and policies followed in the placement of military orders, may be fostering a rapid concentration of economic control that is wholly undesirable from a public policy point of view. Certainly this trend needs more searching analysis, accompanied by a careful review of existing policies.

C. *The incidence of the tax burden.*—The actual incidence of current taxes is not discussed or analyzed nor is consideration given to the role that State and local taxes now play in the whole picture of how tax policies are effecting income shifts. The deflationary power that may be generated from a downward shift of the tax burden (to say nothing of the inequity, or the deprivation of low-income groups that is involved) is a matter worthy of careful analysis.

D. *Need for specific production goals.*—Since the total of tax amortization benefits has now mounted to $12 billions and since these benefits, together with certificates of necessity, give some producers a first claim on resources as well as easing their individual tax burdens, an over-all analysis of production goals in specific terms, with specific references to: (*a*) Existing capacity, (*b*) the current market position of individual companies, (*c*) the over-all organization of the industry, etc., is long overdue. Government-guaranteed markets, Government loans, tax benefits, and Government-sponsored claims on materials are all, in the last analysis, diversions of goods and business opportunities that can reshape our economic existence for some time to come. After nearly 2 years of Government program planning, as the Council calls it, broad generalized production objectives serve more to conceal, than to reveal, the actual effect of the whole program. And yet, to date, only such broad estimates have been made public or subject to analysis. A searching inquiry is needed which will make clear the pattern of present productive capacity.

LEAGUE OF WOMEN VOTERS OF THE UNITED STATES,
Washington, D. C., February 7, 1952.

Hon. JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
Senate Office Building, Washington, D. C.

MY DEAR SENATOR O'MAHONEY: We are happy to submit our comments on a portion of the materials and recommendations contained in the 1952 Economic Report of the President. We notice that the league is once again referred to as a "consumer" organization. While members of the league are, of course, "consumers" the interests of the organization are much broader. Because of our work in many different areas of current affairs, I think the league can be described more accurately as a "public interest" group. Our views are as follows:

(1) In the international field, the league will continue to work for and support authorization and appropriations for the mutual security program. We believe that the funds involved in this program are "a necessary investment in United States security," and that we must move forward in a cooperative effort to strengthen the collective defense system of the free world and to improve conditions in underdeveloped areas .

(2) In the field of domestic economics, we are particularly interested in the following matters and expect to provide our membership with information on them.

(*a*) The proposal to examine and tighten the loopholes in existing tax legislation.

(*b*) The extension of the Defense Production Act. We shall place particular emphasis on the authority to control credit, on the purchase of durable consumers' goods, and new housing. The league has officially supported these indirect controls since November 1950.

(*c*) The Lodge resolution, or similar proposals, which would establish a joint congressional committee to examine requests for defense spending and to supervise defense expenditures.

We realize that these points relate to only a small portion of the Economic Report, but they are some of the major national issues on which the league expects to concentrate during the present session of Congress.

Respectfully yours,

PERCY (MRS. JOHN G.) MAXIM LEE, *President.*

AMERICAN FEDERATION OF LABOR,
Washington, D. C., February 6, 1952.

Hon. JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
Congress of the United States, Washington, D. C.

DEAR SENATOR O'MAHONEY: In accordance with your letter of January 16, I am enclosing a memorandum outlining the views of the American Federation of Labor on the issues raised by the President's Economic Report.

Included with the memorandum are three statements, giving in more detail the views of the American Federation of Labor on the questions of taxation, procurement of critical materials, and housing. I hope that these statements will receive consideration by your committee and can be incorporated in the printed report to which your letter refers.

Sincerely yours,

WILLIAM GREEN,
President, American Federation of Labor.

MEMORANDUM TO THE JOINT COMMITTEE ON THE ECONOMIC REPORT SUBMITTED BY WILLIAM GREEN, PRESIDENT, AMERICAN FEDERATION OF LABOR

The American Federation of Labor welcomes this opportunity to present a brief statement of its views on the issues raised in the Economic Report of the President.

Three major issues in the Economic Report are discussed below under the following three headings:

I. The President's budget.
II. Programs for direct controls.
III. Strengthening the civilian economy.

I. *The President's budget.*—In analyzing the President's budget, we start with the assumption that the United States today is facing a critical situation in international affairs requiring extensive outlays for our national security. We have reached this conclusion independently and after careful study of the problems making up the present world crisis. Detailed, on-the-spot reports from our own A. F. of L. representatives in Europe and Asia emphasize the necessity for a military and economic program to strengthen the entire free world. These reports provide conclusive evidence that there is no basis for an optimistic assumption that the ruthless character of Kremlin-directed aggression will undergo any substantial change in the foreseeable future.

We are convinced that the gravity of the international situation requires very heavy expenditures for both military and economic programs to strengthen ourselves and our allies. The President's budget emphasizes this by earmarking over three-fourths of the 1952 expenditures for our security programs.

We are alarmed by recent statements made in the Congress purporting that billions of dollars could be painlessly cut from the President's budget without impairment of our national security. We regard such estimates to be unfounded and dangerous. While we realize that many desirable economies can be made, particularly in the Defense Department, there is a very real limit beyond which cuts in the budget would affect substantive programs. We therefore fell that it is an extreme disservice to the country to say that without injuring our defense effort, the budget can be cut as much as $5 or $7 billion.

In this connection, we wish to emphasize our view that the President has overestimated the budget deficit for fiscal 1952 and 1953. We suggest that in the budget revenues are underestimated and expenditures are overestimated. This is precisely what has occurred in previous years.

Moreover, the President's estimates of the deficit do not reflect the real impact of the budget on our economy. The Joint Committee on the Economic Report should be most concerned, not with the particular deficit occurring in the budget, but with the flow of money between the Federal Government and the general public. Because a number of important trust funds, particularly those for unemployment compensation and old-age insurance, show a substantial surplus at the present time, the balance between receipts and payments to the public is much smaller than the deficit appearing in the budget.

Taking these facts into account, it is clear that the 1952 budget will have no inflationary impact on our economy while the inflationary impact of the 1953 budget will be only about half the estimate included in the President's budget.

The American Federation of Labor favors a balanced budget, if that is feasible under existing conditions. At the present time, it is unlikely that the 1953 budget can be balanced. The foreseeable deficit, however, is not by any means unmanageable. The choice is between a balanced budget and a timely and adequate provision for national security and national defense in the face of the present danger. We cannot sacrifice the speed and scope of our preparedness program.

The American Federation of Labor has proposed a practical and realistic program for meeting most of the expected deficit. This program, emphasizing the closing of various loopholes in our present tax structure, was outlined in a recent letter to President Truman. This letter sets forth the following estimates of additional revenue that can be raised by closing certain tax loopholes:

	Billions
Recapture loss due to split-income provision	$2.5
Withholding tax on dividends and interest	.3
Eliminate depletion allowance	.7
Integrate and revise estate and gift tax laws	1.0
Close various other loopholes	.75
Total	5.25

The full text of this letter giving the reasoning behind these recommendations is attached to this memorandum (A).

II. *Programs for direct controls.*—The slack conditions currently prevailing in certain industries do not mean we can be complacent or optimistic regarding the threat of inflation during the coming year. The heavy tax revenues in the first quarter of this year will also tend to obscure the fact that during the last half of this calendar year the country will face a severe inflationary threat. The rate of spending by the military is accelerating each month and unless Congress acts promptly, this spending will not be balanced by additional taxes.

Obviously, a continuing program of direct controls is essential if we are to manage the stresses and strains that inevitably develop from the expanding defense program. The shortage of certain metals and materials will continue to require an effective allocations and priorities program.

We have been increasingly anxious to make sure, however, that this allocations program be administered in an equitable manner. While it is clear that the operations of the civilian economy have been closely screened to make certain that available supplies of materials are used most efficiently, the procedure with regard to the military program has not been nearly so effective. We feel quite strongly that the military requests for materials require more careful screening to make certain that procurement for the Armed Forces is not consuming excessive quantities of scarce materials. We recently proposed the establishment of an independent civilian board within the Defense Department, reporting directly to the President, that would help coordinate and screen the military requests for materials. A full text of the recent statement by the A. F. of L. of executive council making this recommendation is attached (B).

To meet the increasing threat of inflation, the entire legislative framework set forth in the Defense Production Act needs to be strengthened. The Defense Production Act had certain inherent weaknesses as it was first passed in September 1950, but these have been aggravated by the action taken by Congress in renewing the law last year.

The country does not have a comprehensive and effective anti-inflation program today. In order to reach this objective the A. F. of L. makes the following recommendations for changes in the Defense Production Act:

1. Repeal of the cost-plus Capehart amendment which forces OPS to allow manufacturers to pass along to the public unwarranted increases in costs.
2. Repeal of the Herlong amendment which maintains historical margins for retailers, regardless of their volume of business.
3. Repeal of the Butler-Hope amendment which prevents OPS from utilizing livestock slaughter quotas as a means of enforcing meat price control.
4. Granting authority to the President to initiate a food subsidy program if food prices should once again begin to increase sharply, and
5. Repeal of certain sections of the law which prevent OPS from exercising adequate control over the quality of goods under price control.

Only if these changes are made will it be possible to control effectively the rising cost of living. Unless this is done, workers' support for the very effective wage stabilization program is endangered.

We have one additional suggestion which we believe should be helpful in the fight against inflation.

Consumers are now saving a larger part of their income than they have since 1945. If these additional savings could be channeled into defense bonds, they would help meet the threat of inflation by reducing the Government deficit.

Unfortunately, the defense bonds designed before World War II are no longer able to attract a large volume of savings. Although general level of interest rates on other types of savings has risen substantially, the defense bond has remained unchanged. We suggest that the Treasury Department issue a new type of defense bond carrying a higher rate of interest and designed particularly to attract additional savings from moderate-income families.

III. *Strengthening the civilian economy.*—There is a tendency to think of the defense program only in military terms. It is certainly true that perhaps the single most important objective of the program is to make this country and our allies strong against attack.

However, the defense effort involves more than our Armed Forces, more than military equipment. It also means increasing the productive capacity and improving the living standards of ourselves and our allies so that the entire free world is better equipped and more willing to fight against communism.

On the international side, the defense program must include economic aid where it is most needed and a program for technical assistance to help raise the standards of living for underdeveloped areas.

Here at home, the defense program should not be an excuse for stifling urgently required programs in the fields of housing, health, and education. The need for action in these fields is far more acute today than ever before. While the inauguration of some programs involving excessive expenditure of funds may have to be deferred, we should move ahead as rapidly as conditions permit and make sure that the needs intensified by defense are met.

We are particularly concerned about the growing crisis in housing. The success of the defense program depends in large measure on our ability to make available decent housing for defense workers at prices they can afford to pay. Unfortunately, even a minimum defense-housing program has not yet been developed.

We have made specific recommendations on this issue involving a full-scale program for moderate-rental defense housing units to be constructed if possible by private builders, but if necessary through publicly financed operations. The full text of these recent recommendations by the A. F. of L. executive council is attached (C).

The country's health needs require immediate attention. We endorse the President's Health Commission and hope it will move promptly to investigate and make recommendations for bringing preventable and remedial medicine within the means of every American family. Meanwhile, Congress must act at this session to assure training of additional doctors and construction of needed hospitals and health centers.

The program of Federal aid to education is long overdue. We have actively supported the President's program and hope Congress will act soon so that educational standards can be raised and equalized among the various States.

TEXT OF LETTER ADDRESSED BY PRESIDENT WILLIAM GREEN OF THE AMERICAN FEDERATION OF LABOR TO PRESIDENT TRUMAN ON JANUARY 22, 1952, ON FEDERAL TAX POLICY

The American Federation of Labor has consistently maintained since the end of World War II that Federal tax policy should be on a pay-as-you-go basis. For this reason we have urged that Congress adopt tax measures that would yield revenues necessary to balance the Federal budget.

Unfortunately, Congress has not only failed to vote tax increases sufficient to keep the budget in balance but has approved measures which are distinctly contrary to the "equality of sacrifice" principle enunciated by you when you referred to the necessity of increased taxes in 1950.

Federal tax revenue is now at an all time high with the recent tax increase approved by Congress estimated to yield an additional $5.4 billion in revenue annually. However, it is our understanding that total anticipated tax revenues will fall considerably short of balancing the budget during fiscal year 1952. We recognize, therefore, that you are again confronted with the problem of whether or not to recommend the enactment of still higher taxes.

It is our considered opinion that a balanced budget is essential in the present period of high employment, high prices, and high profits. Moreover, whether it is necessary to levy taxes to provide additional funds over and above existing tax revenue or to correct glaring inequities that exist in present tax law we believe certain changes are urgently necessary in the revenue structure.

We base this conclusion on following facts:

1. Present tax laws discriminate against certain classes of taxpayers. While single taxpayers with one dependent pay up to 5 percent more in income taxes than they did when taxes were at their highest point during World War II under the 1944 act, married taxpayers pay up to 28 percent less in the income groups below $25,000. At the $100,000 income level the married taxpayers enjoy a $13,000 tax saving under the present law as contrasted to tax obligations of a single person in the same income group.

2. Workers at the present minimum wage of 75 cents per hour if fully employed may earn $1,560 a year. Deducting Federal taxes only and making adjustments for decline in value of the dollar such workers in 1952 earn $738 or $94 less than the $832 similar workers earned in 1938, 1939, and 1940 under the 40-cent minimum which was not subject to Federal income tax. All low-income workers are similarly disadvantaged because the combined impact of high prices and Federal, State, and local taxes is cutting into basic living standards.

3. While the living standards of millions of Americans have been slashed during the past several years old tax loopholes have been perpetuated and new loopholes have been opened up which according to conservative estimate would enable the Federal Government to raise additional revenue of at least $5.25 billion made up as follows:

	Billions
Recapture loss due to split income provision	$2.5
Withholding tax on dividends and interest	.3
Eliminate depletion allowance	.7
Integration and revision estate and gift tax laws	1.0
Closing various loopholes	.75
Total	5.25

The officers and members of the American Federation of Labor urge you to give highest priority in any tax recommendation you present to Congress in 1952 on ways and means of easing the tax burden of millions of Americans in the low-income groups, particularly those with income below $2,000 whose basic living standards have been so depressed by the tax policy adopted by Congress. Further, and even more important in terms of the possible realization of a balanced budget we sincerely trust you will make earnest recommendation to Congress that it recapture the $5 to $6 billion in additional revenue that could be so easily secured eliminating special tax advantages favoring certain classes of taxpayers.

We assure you of our wholehearted support in the promotion of these and all other measures directed at distributing the burden of supporting necessary Government service more evenly in accordance with the ability-to-pay principle.

Statement by the A. F. of L. Executive Council on the Need for Screening Requests of Military Forces for Critical Materials, January 29, 1952

Until now our industry has been able to maintain most lines of civilian production at near-peak levels. From now on, however, the defense program will be making the first substantial inroads into the civilian economy.

In its early stages the defense program could progress at only a limited pace. Moreover, emphasis was placed on the need for machine tools, new plants, and plant conversion, all of which were necessary before we could attain high-level output of tanks, guns, and planes.

This tooling-up stage of the defense program is now merging—gradually here, suddenly there—into high-level armament output. By mid-year enough new tools, equipment, and converted plants will be ready to begin to turn out huge quantities of hard goods for the military forces. Because we will not have enough copper, aluminum, steel, and other critical materials for both peak civilian output and expanded defense production, the civilian economy for the first time in the current rearmament effort will feel a real pinch.

Recent statements of defense mobilization officials have indicated the dimensions of the changes that will take place in the shift from civilian to defense production. For example, in the second quarter, the military and atomic energy programs will take more than 50 percent of our supplies of such critical materials as brass-mill copper, stainless steel, and aluminum. Necessarily, the expansion of the defense sector of the economy will be accompanied by reductions in civilian output.

These cut-backs in the civilian economy have a twofold importance to workers. They mean deprivation for themselves and their families of essential goods and services—worse schooling for their children, inadequate medical care, deferment of plans for improved housing and fewer refrigerators, stoves, and other essential civilian products. Moreover, where reductions in civilian output are not dovetailed with expanding defense production, workers will face the serious threat of unemployment and loss of livelihood.

To sustain the defense effort, workers are willing to make all necessary sacrifices. Yet they recognize that maintenance of the civilian economy at the highest level consistent with defense needs and maximum use of the skills of the working force are essential not only to meet minimum civilian needs but also for the success of the defense program itself.

Workers want to be sure that our limited supply of critical materials is being used to meet the most essential military and civilian requirements. Within the civilian economy, this means that little or no materials should be made available for such nonessential uses as luxury housing, luxury automobiles, and the like. Neither should allocations be increased for certain favored industries simply because they are able to bring to bear powerful political pressures. Critical materials left over for the civilian economy must be allocated strictly according to principles of equity and essentiality.

Fair screening of requirements for the civilian aconomy is necessary, but it is not enough. From now on the military will be consuming the major share of many critical materials. It would be the height of folly to assure the most economic use of critical materials in the civilian economy while permitting the military to make extravagant use of such materials as if we had an unlimited supply of them.

There have been disturbing indications of a tendency in programing and procurement by the military services to "reach for the moon," often disregarding the limited supply of critical materials and the imperative need that they be used most economically.

Although detailed information of this character is withheld, suspicions are inevitably aroused when it is known that for many items, allotments to the military are at about the same level as at the peak of World War II. The request of the military for enough materials to construct permanent housing equal to more than one-fourth of the total national housing goal for 1952 also seems far out of line.

At present the Defense Production Administration attempts to screen military requirements only in terms of the materials needed to produce the end products requested by the military without any attempt to measure the need for these end products against the stated military objectives. This means that only half the job is being done.

After careful study of the entire problem, we have come to the conclusion that proper screening of defense requirements—which can only be done in the light of the essential requirements of the entire economy—requires the establishment within the Department of Defense of a special Civilian Board on Military Requirements and Allocation to report to the President. This Board should consist of civilian experts, including men drawn from business and labor, who would have the job of making sure that the military requests are confined to materials actually needed to accomplish the accepted military objectives. It would be their job to deflate bloated requests and sift out gratuitous and superfluous requests for materials from legitimate requests to meet actual military needs. Because of its tremendous stake in this entire sphere, labor should be represented on this Board.

The Government has already taken steps to restrict the use of essential materials by industry and consumers. A civilian screening board within the Defense Department should be set up to insure the most economic use of critical materials by their largest single consumer—the military services.

STATEMENT BY THE A. F. OF L. EXECUTIVE COUNCIL ON A HOUSING PROGRAM FOR THE DEFENSE EMERGENCY

A growing weakness in the national defense program threatening to undermine the defense production effort is the failure to provide housing for defense workers.

Defense housing is not a nonessential luxury. It is as important a requirement of the defense program as the copper and steel used to produce the implements of war. World War II experience provides ample warning that the defense program would be seriously hampered unless workers moving into mushrooming defense areas could find adequate housing for themselves and their families.

These are known facts, but the record to date shows they have been largely ignored. Congress did not enact the so-called defense housing bill until the late summer of last year—more than a whole year after the outbreak of the Korean war. Its provisions are shamefully inadequate. It places primary reliance on a program of special aids for private builders of sales and rental housing in defense areas. Even while the bill was being considered, it was clear that the monthly cost of the units to be constructed would be far more than most defense workers could afford. Provision for publicly financed construction of moderate-rental defense housing was so limited as to authorize construction of only about 5,000 such units for the entire country.

This pitifully inadequate action has thus far produced practically no defense housing. It is clear that the units that will eventually be constructed by speculative builders, assisted by the special aids contained in this act, will produce houses far too high priced for most defense workers.

Only about 300 privately built defense housing units have actually been completed. An additional 2,500 are now under construction and a total of about 67,000 are scheduled for construction.

The President's budget message reflects the hope that 275,000 to 300,000 more units will be "programed" for the next 18 months. Experience to date provides no ground for believing that this hope will be realized. But even if that many units were constructed by speculative builders in defense areas, they would require monthly payments far beyond the financial reach of most defense workers.

Congressional appropriations for publicly financed moderate-rental defense housing have been so low that they are being used exclusively for trailers and other temporary housing. Even so, only about 5,700 units of this type have been planned for 25 areas. Our experience during World War II makes it certain that such makeshift housing will be extremely unsatisfactory.

While the critical need for defense housing has been largely ignored, the resources of the housing industry have been devoted largely to the construction of high-priced luxury housing. This type of housing not only contributes to inflation, but constitutes a serious drain on critical materials needed for essential defense housing construction.

At the same time, with the encouragement of the real-estate lobby, the reactionary coalition in Congress almost succeeded in killing low-rent public housing which provides the only means for low-income families to obtain decent homes. Congress actually placed a limitation of 50,000 units a year on that program although in the Housing Act of 1949, 135,000 units a year had been authorized.

Congress did not even consider the urgent need for a housing program for middle-income families despite the enthusiasm which this A. F. of L. initiated program generated in the months just before the Korean war and the urgent need for it.

America needs a housing program geared to the requirements of the defense emergency. The cut-back in materials which has recently been announced emphasizes the necessity to utilize the skilled working force and critical materials available for housing construction to meet our most urgent housing needs. The A. F. of L. therefore calls upon the Congress to adopt the following minimum housing program:

1. Provide a genuine defense housing program to provide moderate-rental homes for defense workers—if possible, by private builders, but if not, through publicly financed construction. The President's request for funds to build about 10,000 units of moderate-rental units before June 30 and about 35,000 during the fiscal year 1953 beginning July 1, 1952, represents

a good start. However, there is every evidence that many more units of this type will be needed if defense workers are to be adequately housed.

2. Authorize 135,000 units of low-rent public housing. The need of low-income families for decent homes has not diminished. The minimum program authorized by the Housing Act of 1949 must proceed without limitation.

3. Approve special aids for cooperative and other nonprofit housing projects for middle-income families.

Adequate housing for defense can no longer be postponed. The delay in attacking this problem has already been costly in terms of manpower and production cost to the defense program. The success of the entire rearmament effort will be jeopardized unless Congress acts now to meet the Nation's critical housing needs.

STATEMENT OF EMIL RIEVE, ADMINISTRATIVE CHAIRMAN OF CIO COMMITTEE ON ECONOMIC POLICY, TO CONGRESSIONAL JOINT COMMTTEE ON THE ECONOMIC REPORT

The major domestic task facing the American people in 1952 remains the same as last year:

1. The partial mobilization of our economic and military might to strengthen the security of our Nation and the other nations of the free world.

2. The maintenance of an expanding and stabilized national economy.

The Communist threat to our Nation and the free world makes it of vital importance that we succeed in our effort. The preservation and extension of democratic values and our world leadership depend, to a great extent, upon our ability to strengthen our national defenses and maintain a sound economy.

The mobilization effort should continue, whether or not a truce is achieved in Korea. Our Nation and the free world are compelled to be prepared for the possibility of all-out war, so long as the threat of Communist aggression persists.

There have been many advances in the defense production effort in the past year. Enormous strides have been taken toward the expansion of the productive capacity of our economy. Total output and business investment in new plant and equipment are at record heights.

But defense production has encountered serious problems and bottlenecks. There has been a slowing down and rephasing of the pace of defense production schedules, with the result that the scheduled peak level of defense output has been pushed back about 6 months. The essential task of over-all planning and program development—the meshing together of the individual programs in the light of long-range defense and civilian requirements—has not been performed.

The wave of inflationary pressures after Korea reached its peak in February to March 1951 and was followed by a lull. The Congress had the opportunity to take advantage of this lull in price pressures by strengthening the inadequate Defense Production Act, the basic stabilization statute, to provide the Government with adequate authority to curb potential inflation in he period ahead. Instead, the Congress weakened the law and provided business with assurances of higher ceiling prices if inflationary pressures develop.

Congressional action is weakening the Defense Production Act last summer underscored the lack of equitable treatment of the various civilian groups of our Nation. Equality of sacrifice is as far from having been achieved as ever in this mobilization period.

Business has been handed a guaranty of higher prices, whenever markets get tight. In addition, upper income and business groups have privileged advantages under the loopholes of our tax structure. And industry has been granted the special privilege—through accelerated depreciation—of writing off a good deal of the new plant and equipment in 5 years, instead of the normal 20 years.

Workers and low-income groups, on the other hand, feel the full impact of taxation, without loopholes or other privileges. Consumer credit control directly hits the lower-income groups. And wage stabilization policies have established a cumbersome machinery that frequently ties up workers and their unions in lengthy, complicated proceedings. In contrast with the privileges of business and upper-income groups, workers and their unions are compelled to attempt to negotiate wage adjustments with employers and then to go through the Wage Stabilization Board's obstacle course.

Several paradoxical situations have developed in the national economy in recent months. There is the possibility of new-price pressures in some economic areas—growing out of the strain on strategic raw materials, resulting from the rise in defense production and the high level of business expenditures for new plant and equipment. On the other hand, the consumers' goods industries—such as textile, clothing, and shoe—have been suffering from soft markets, due to the decline in consumer spending.

While total employment is high, there is the concentration of unemployment in several industries and areas. A lack of sufficient sales volume has caused varying degrees of unemployment in the consumers' goods industries. The cutbacks in the civilian use of key raw materials—before defense production takes up the slack—has brought unemployment to several metal-consuming civilian industries. Centers of consumers' goods and metal-consuming civilian industries—including New York, Detroit, and Providence, R. I.—have reported substantial labor surpluses in the past several months. Unemployment has continued to be heavy in areas of long-standing economic weakness—such as Lawrence, Mass., and Cumberland, Md.

The granting of certificates of necessity for accelerated amortization has been handled loosely and without proper Government planning and foresight. The location of new plants—and their impact of manpower—has not been given adequate consideration. Nor have there been precautionary measures to weigh the real need for new industrial facilities before granting rapid write-off tax privileges.

While the economy as a whole has moved forward to new strength, old weak spots have remained and new weaknesses have appeared. Equality of sacrifice is a long way from achievement. There has been no adequate planning for the long-run needs of an expanding and stabilized economy, beyond the current military build-up of the next 2 or 3 years.

MOBILIZATION

Our total output of goods and services has been rising rapidly. From the pre-Korean second quarter of 1950 to the fourth quarter of 1951, the total output of the American economy rose, in 1951 prices, from an annual rate of $298.6 billion to a rate of $331.1 billion—a rise of almost 11 percent. The annual rate of output in the last 3 months of 1951 was 18 percent greater, in constant prices, than in 1948—the peak peacetime year.

The rapid growth of total output was made possible by rising productivity and the increase in new plant and equipment. There is every evidence that total output will continue forward to a new high in 1952.

Business expenditures for new plant and equipment jumped from $17.8 billion in 1950 to $23.1 billion in 1951. In the first quarter of this year, business is spending at an annual rate of $22.9 billion for new facilites. And output per man-hour—which rose rapidly in 1950 and 1951—should continue to increase this year.

The rise in output eases the burden of the defense effort. It means that less drastic cuts in civilian output will be needed to continue the momentum of military production. Our expanding economy enables us to assume the responsibilities of world leadership.

By the end of 1951, defense expenditures—for military output and construction, foreign military and economic aid, payrolls and upkeep for the Armed Forces, and atomic energy projects—were at the annual rate of $45 billion, representing over 13 percent of total output. In the period before Korea, defense expenditures were approximately 6 percent of total output.

According to current schedules, the plateau of defense spending should be reached by the end of this year. At that time, defense expenditures are expected to be at an annual rate of $65 billion—18 percent of total output. This rate of high-level defense expenditures should continue through 1953 and begin to taper off in 1954.

The achievements of the national economy and the American people in this mobilization effort have been enormous. But there is little occasion for smug self-satisfaction.

Thus far, only $20 billion of military equipment has been delivered since Korea. The major tasks of production and delivery are still ahead.

In the past several months, we have seen the acknowledged slowing down in the pace of defense production schedules. The high-level plateau of defense spending—which was scheduled to be reached in mid-1952—will not be attained until the end of the year or later. While some of the difficulties are inherent in a partial mobilization effort in a democratic society, other difficulties arose from a lack of proper programing and direction of the effort.

An over-all defense production program is essential—to determine what military goods and productive capacity are needed for partial mobilization, how fast we should move to reach that point, to mesh together both defense and civilian requirements, to dovetail defense orders with available manpower, and to integrate the long-run needs of an expanding economy with the short-run requirements of the military build-up. Such planning has not been accomplished.

Ever since the mobilization effort began, the CIO has called upon the defense agencies to develop defense production programing and planning. The need for proper mobilization planning is now recognized by industry groups. On January 23, 1952, the Office of Defense Mobilization released the recommendations of a Steel Task Group, which stated:

"* * * it should be possible to compile more accurate estimates of total steel requirements of present military programs properly phased to conform with the expected production schedules and including factual estimates for components, machinery and equipment, classed as B products, which represent a substantial proportion of the total military needs. It should also be possible to make an accurate appraisal of steel requirements for full mobilization. While considerable effort has been given to the computation of military requirements, it has been impossible to uncover any source that could provide a really comprehensive estimate of total steel requirements, broken down into mill products, properly phased by quarters for the next 4 or 5 years. We respectfully point out that the lack of such information makes it impossible to give you anything more than conditional or approximate answers to your questions regarding the adequacy of steel."

The defense agencies are compelled to spend a good deal of time in breaking bottlenecks and solving problems that suddenly arise. Had they developed defense production programing, many of those bottlenecks and problems could have been foreseen and solved before they appeared.

Critical materials have been allocated faster than the defense-producing plants can use them. As a result, we have had drastic cuts in civilian production, on the one hand, and inventories of key materials on the other.

Government orders have curtailed the civilian use of critical materials before defense production has taken up the slack. Military output—to some extent is being held up until new end-item manufacturing plants have been constructed, while plants and manpower are idle or underutilized in existing manufacturing centers.

Current unemployment of over a hundred thousand in Detroit, for example, is expected to rise to 150,000 in several months. This growth of unemployment in several major industrial centers represents a waste of manpower and industrial facilities.

Military requirements apparently are not adequately screened by the mobilization agencies. While we must meet the needs of the military build-up, we should not permit the development of a military sacred cow in America.

Accelerated depreciation has been a stimulus to economic expansion since Korea. But it has been handled with extreme looseness. Certificates of necessity for the rapid write-off of new facilities have been granted without careful scrutiny as to the real need, the location, or defense relation of the new plants.

As of November 30, 1951, $10.8 billion of new plant and equipment was authorized under the accelerated depreciation program. Some 65 to 70 percent of that total amount was approved for rapid write-off in 5 years.

Although there is sufficient textile capacity in this country, textile firms have been granted the privileged subsidy of accelerated depreciation of new plants. There has been little, if any, effort to direct the construction of new facilities into weak economic areas—where skilled manpower, homes, and community facilities already exist.

There is the need for expanded capacity in such basic economic areas as steel, aluminum, copper, and electric power. But nonessential construction should not be given Government encouragement and subsidy, when key materials are needed for essential defense and civilian needs.

Over-all programing and planning are essential for the success of the mobilization effort. Procurement policies should flow from such programs and plans; they should be based on the placement of defense orders in areas of existing manpower and facilities. The conversion of some industrial facilities to military production should be given Government encouragement in order to reduce the dislocations inherent in mobilization. Maximum civilian output and social legislation programs—consistent with meeting our defense needs—should be maintained. In the period ahead, we should not lose sight of the fact that a strong economy is the foundation of military power and a healthy society.

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FISCAL AND MONETARY POLICY

The cost of the defense effort represents a financial burden to the Government. It has been the view of the CIO that the burden should be met on a pay-as-we-go basis, to the greatest extent possible.

Under the prodding of business groups last year, Congress failed to raise sufficient tax revenue to meet the costs of Government operations. The business groups have consistently opposed realistic and equitable tax increases, whatever the need may be. Their success in tax legislation makes inevitable a budget deficit for the fiscal year, ending June 30, 1952; it also has continued and aggravated the inequities in our tax structure.

President Truman estimates that the budget deficit for the fiscal year ending June 30, 1952, will be about $8 billion. Not only is insufficient Federal revenue being raised, but the tax structure places a heavy burden on low income groups, while upper income families and high-profit corporations enjoy the benefits of tax loopholes.

The proposed Federal budget of $85.4 billion for the fiscal year, ending June 30, 1953, will result in a budget deficit of some $14 billion, it is anticipated, under the present tax structure. It is probable that this mobilizaion budget could not possibly be met on a pay-as-we-go basis. But this does not eliminate the need for plugging loopholes and making our tax structure more equitable.

The loopholes of the tax structure should be plugged. Elimination of these loopholes would enable the Government to raise an additional 4 to 5 billion dollars in revenue.

Any contemplated further rise in tax rates must not go below family incomes of $4,000 a year and less. Such families are compelled to spend a large share of their incomes on food, shelter, and other necessities of life. The current tax rate already cuts their incomes below the requirements for a decent standard of living.

A sales tax, as proposed by the National Association of Manufacturers, would hit low income families most directly. It would add a grossly inequitable feature to the inequities of the existing tax structure.

Although the budgetary requirements of the mobilization effort are large, we should not trim the budget down to anticipated Government revenue. This would be most dangerous to the entire national security program. The problems posed by large budgets in this mobilization period should be met by fair and equitable taxes and an over-all stabilization program to curb the possible inflationary effects of a budget deficit. But it should not be met by eliminating any part of our essential military and civilian requirements. This does not mean, however, that sincere and honest efforts should not be made to cut unnecessary Federal expenditures.

An important part of an effective over-all anti-inflation program must be the control of bank credit—to curb the flow of bank loans. Present Government methods to control bank credit have proven unsatisfactory. Bank loans have risen, despite the rise in the interest rate and the so-called voluntary credit restraint program, supervised by the financial community itself.

Commercial and industrial loans of commercial banks were relatively stable in the early months of the price lull following February-March 1951. But after July, they started to rise again. By December, they were 13 percent above July.

The so-called self-restraint program has not curbed the expansion of business loans. But it gives the financial community a position of special privilege. And it sets the possible basis for black-balling prospective borrowers on insufficient or discriminatory grounds.

The Government's program to control should be completely overhauled. The effective curtailment of business credit requires the establishment of increased bank reserves designed to immobilize part of the great sum of United States Government securities in bank reserves. It also requires some measure of direct controls over the extension of bank loans.

Selective consumer credit controls should be truly selective—aimed at reducing inflationary pressures, in cases where consumers' durables may be in short supply—rather than aimed at depressing specific industries. Consumer credit controls should, therefore, be flexible enough to move up or down, depending on the degree of price pressures. Such consumer credit control must not be discriminatory.

PRICES AND WAGES

Despite the lull in inflationary pressures since February-March 1951, prices have remained high. At the end of the year, wholesale prices were 13 percent above June 1950. And the Consumers' Price Index reached a peak, 11.6 percent above the level of the month of the Communist invasion of South Korea.

Except for a flurry of price cuts last summer, there has been little attempt by business to boost consumer spending through price reductions. The inflated price level appears to have become inflated into the national economy. Business reaped the harvest from high prices. Although the decline in consumer spending since last March has affected the soft goods industries, average profits before taxes for all corporations for the years as a whole were at a record level.

Corporate profits before taxes, in 1951, were at an all-time record level of $44.8 billion. If we apply the excess profits tax exemption of 83 percent of the best 3 years of 1946–49, we find that 1951's corporate profits before taxes were 75 percent above Congress' concept of "normal" profits. Despite increased taxes, corporate profits of $18 billion, after taxes, were 16 percent above "normal."

The high price level, the price-rising possibilities of the Defense Production Act, and high levels of defense spending by the Government lend assurance to business that 1952 will be another year of high-level profits.

The amended Defense Production Act which went into effect on August 1, 1951, did nothing to make possible the effective control of retail food prices. It permitted, in areas under rent control, automatic rent increases up to 20 percent above June 30, 1947, plus any increases since the base date that were premised on major repairs.

Among other major loopholes in the amended statute were—

(1) The Capehart amendment which places a sky-high floor under future ceiling prices on manufactured goods and establishes the procedure whereby all cost increases between Korea and July 26, 1951, may be added automatically to ceiling prices.

(2) The Herlong amendment which declares that future ceiling prices for wholesalers and retailers must be based on customary pre-Korean percentage mark-ups.

The act makes firm controls over living costs impossible. It establishes guaranties to business that ceiling prices can rise to new heights if the market situation gets tight. Defense Mobilizer Director Charles E. Wilson, former Economic Stabilization Director Eric Johnston, and Director of Price Stabilization Michael V. DiSalle predicted that the amended law would permit prices to rise to a new high level.

The excise taxes, effective last November 1, have been passed through to the consumer. On many commodities, excise taxes have been passed through to consumers on a Herlong percentage mark-up basis, compelling them to pay more than the excise tax itself. In recent months, OPS has been establishing procedures to allow manufacturers to calculate upward adjustments of their price ceilings under the Capehart amendment. Many of these procedures are automatic and self-executing.

The new procedures for increasing ceiling prices do not mean that they will be translated immediately into boosts in the actual price level. In many lines, selling prices are somewhat below OPS ceilings—as a result of an insufficient sales volume. But the procedures for price rises are available, to be used whenever business believes that market conditions will permit rises in selling prices.

The consumers have as yet felt only a small part of the impact of the Capehart and Herlong amendments. The full impact is yet to be felt. The procedures for price rises are written into the law, available for the use of business whenever it wishes.

Wages, on the other hand, are entitled to no privileges under the Defense Production Act. Unions must first attempt to negotiate wage adjustments with employers—no easy task, in most cases. Under present arrangements, that is usually the first hurdle. In most cases, the negotiated wage adjustments have to be approved by the Wage Stabilization Board, where the case may wait for weeks or months before it receives Board action.

There are no Capehart and Herlong procedures for workers. Prices can move up almost at will as a result of the many loopholes in the Defense Production Act. But wages—the sole means of livelihood of the largest segment of the American people—are tied down by contractual obligations for three, four, five, or more months.

Through their unions, workers can attempt to catch up to previous price rises. The Wage Stabilization Board now allows cost-of-living wage adjustments. But there is a delay of several months, at least, before the lag between prior price rises and wages can be narrowed.

Workers' wages—excluding overtime and premium pay—have lagged somewhat behind the rise in retail prices since January 1950—the base date for wage stabilization. And the average wages of workers have not reflected the rise in output per man-hour of work.

The workers' right to share in rising productivity has become a recognized principle. Even some business groups—such as General Motors—endorse the concept. But workers have not shared in rising productivity in the past 2 years.

If workers' incomes are not permitted to keep pace with rising output per man-hour, the mass consumption base of our economy will be undermined. The improved efficiency of industry will carry forward beyond the military build-up period. Unless workers share in increased productivity, their incomes will not be sufficient to maintain the more efficient economy at high levels of production and employment. If workers do not share in the fruits of industrial progress, the benefits derived from efficiency of production will go to business alone. Failure by the Wage Stabilization Board to permit workers to share in the benefits of the increased productivity of the economy can turn industrial efficiency into unemployment and depression, instead of improved living standards. Equitable treatment of workers' demands that they be given the opportunity to maintain at least their relative share of national income—by sharing in the fruits of industrial progress.

We can see the effects of declining buying power from the current condition of the soft goods industries at present. The impact of high prices, tax rises, and payment of debts and obligations have cut into the buying power of large groups of people.

Per capita disposable personal income (after taxes) was lower in the last quarter of 1951 than it had been a year before. In the fourth quarter of 1950, per capita disposable personal income was at a yearly rate of $1,469; in the last 3 months of 1951 the rate of disposable personal income for each person in the country was $1 455.

The soft goods industries—such as textiles and clothing—are directly affected by declines in consumer spending. These industries have been depressed in recent months as a result of insufficient sales.

EQUALITY OF SACRIFICE

The impact of the inequitable treatment of workers has not only affected them and their families. It has affected the national economy.

Justice requires equality of sacrifice in this mobilization effort. So do the needs of an expanding economy.

Possible inflationary pressures should be curbed by an over-all economic stabilization program based on the principle of equality of sacrifice. Such stabilization program is needed as long as the possibility of inflation continues. The current patchwork of controls and economic legislation is inequitable. It serves to undermine public morale and confidence, as well as weaken the base of our economic structure.

Ever since the mobilization effort got under way, the CIO has urged an equitable and effective program to stabilize the economy. We do not have such a program at present. Consumers and the national economy need protection against possible inflation ahead, arising out of the high level of defense expenditures and capital investment.

Such a program should include (1) increased output; (2) allocation and priorities of key raw materials; (3) effective price controls and rent controls; (4) fair wage stabilization; (5) equitable taxes to raise adequate revenue; (6) credit control; (7) savings program.

AMERICAN FARM BUREAU FEDERATION,
Washington, D. C., February 5, 1952.

Hon. JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
Senate Office Building, Washington, D. C.

DEAR SENATOR O'MAHONEY: This is in response to your request for comments on the materials and recommendations contained in the 1952 Economic Report of the President.

These are preliminary comments on a few of the most important items in the report on which the American Farm Bureau Federation has developed definite policies through democratic processes at county, State, and National meetings.

We find ourselves in disagreement with what seems to be the underlying philosophy of the report and with the direction in which many of its major recommendations appear to point. In this connection we note on page 1 the statement that the people of the United States are "substantially in agreement" on our national effort to preserve peace "but our foreign policy cannot succeed if there is excessive division on domestic matters." This comes close to suggesting that it is unpatriotic and opposed to the national welfare to disagree with the administration's recommendations on domestic matters. This is an unfortunate attitude and entirely inconsistent with our democratic traditions. We are confident that the Congress does not share this attitude, for to do so would mean the abdication of legislative responsibility in favor of the complete centralization of power in the hands of the Executive. The objections which we feel compelled to raise to some of the recommendations contained in the Economic Report are based on careful study and sincere convictions with respect to what must be done if we are to preserve our freedom and continue the progress that has thus far characterized our national development.

The Federal budget

The most important single thing in the 1952 Economic Report is the indication that the President and his Economic Council contemplate a huge Federal deficit in the 1953 fiscal year. On the basis of the budget, which has since become available, this deficit is estimated at $14.4 billion. A budget deficit of this size will create strong inflationary pressures regardless of anything else that we may do.

The President has recommended that $5 billion of this prospective deficit be covered by additional revenues to be obtained "by eliminating loopholes and special privileges and by some tax-rate increases." While it may be possible to obtain some additional revenue "by eliminating loopholes and special privileges," the President's request for new revenue could not be met without a substantial increase in tax rates. Extremely drastic tax increases would be required to bring revenue up to present spending estimates. Furthermore, we are near, and possibly at, the level of diminishing returns with existing tax rates.

The thing that must be done is for Congress to regain control of appropriations and bring the Federal budget into balance, at least on a cash consolidated basis.

Our views on Government spending and tax policies are summarized in the following excerpt from the resolutions adopted at our recent annual meeting:

"There is no possibility of avoiding inflation if we fail to balance the Federal budget and keep it balanced for the duration of the defense program. Government spending must be paid for either by taxes or by inflation. We prefer to pay it with taxes. It is apparent, however, that the problem of balancing the budget requires a dual approach. Taxes cannot be raised sufficiently to cover unlimited appropriations. We must continue to pay high taxes, but we also must bring Government expenditures under control. To this end we insist that the legislative and executive branches of the Government cooperate on a program of reducing Government spending to the level necessary to balance the budget without any substantial further increases in our already heavy tax burden.

"We are confident that this can be done without impairing the national interest. Indeed, sound fiscal policies will greatly add to our national strength.

"Nonessential Federal expenditures must be eliminated; all expenditures must be reduced to the minimum necessary for the national interest; economy and efficiency must be achieved throughout the Government.

"Groups opposing the elimination of nonessential Federal expenditures must realize that failure to bring Federal expenditures under control may force Congress to take the undesirable step of enacting a Federal sales tax.

"No Government expenditure should be exempt from scrutiny by both Congress and the administration to determine whether it can be reduced or eliminated without impairing an essential Government function. With military expenditures constituting the major part of the Federal budget, it is urgent that every effort be made to get the most out of the money appropriated for defense.

"Costly new programs should be deferred except where immediate action is essential for the national defense. Now, during a period of high employment and scarcities of many essential materials, is not the time to add new services or construct works which can be deferred."

Farm price supports

The President has recommended the repeal of what he calls "the sliding-scale provisions of the present agricultural legislation." It is suggested in the Economic Report that the flexible price-support provisions of the Agricultural Act of 1949 are a deterrent to maximum agricultural production. Farm price supports are an appropriate and necessary protection against unreasonable price declines. It would be a mistake, however, to base our efforts to increase farm production on a system of Government-guaranteed and Government-administered farm prices. Such a system would place agriculture in a strait-jacket. If the Government is going to guarantee incentive prices, it follows that Government planners must decide how much of each commodity we need and who is to produce it. This would completely destroy the flexibility and individual incentive which are essential to agricultural progress. Furthermore, it could lead to serious surpluses in some commodities and serious shortages in others.

The price-support provisions of the Agricultural Act of 1949 are adequate for the present situation. As a result of the national defense program and our present high level of employment, our citizens have a need for, and the ability to buy, a record volume of farm produce. We ought to meet this demand in the American way by advising farmers of the economic outlook and then letting each individual decide how he can use his available resources so as to make the greatest contribution to total agricultural production. If farmers know that their products are needed in the market, and if they can obtain the necessary production prerequisites and farm labor and free access to the market, the Nation will have the best possible assurance that our agricultural resources will be fully and efficiently used to meet national needs.

The voting delegates at our last annual meeting went on record in opposition to higher price supports as follows:

"Farm supports are an appropriate and necessary protection against unreasonable price declines. It is not, however, the responsibility of the Government to guarantee profitable prices to any economic group.

"We favor the maintenance of the present price-support features of the Agricultural Act of 1949 which are designed to provide protection against extreme price declines without going to the opposite extreme of Government price fixing. We do not believe that action to raise the level of price support above that now provided in the Agricultural Act of 1949 is in the long-run interest of farm people."

The President has suggested that direct payments to farmers be given further consideration. We believe the Congress gave this subject adequate consideration before rejecting it in favor of the Agricultural Act of 1949. The applicable portion of our resolutions is as follows:

"Government payments to farmers are not a desirable substitute for price supports or a satisfactory means of bringing income into agriculture."

We are pleased to note that the Council of Economic Advisers is aware of the fact that farmers must be able to obtain fertilizer and adequate supplies of farm machinery if we are to achieve maximum agricultural production. We were disappointed, however, to note that the Council failed to mention the importance of an adequate supply of farm labor. The number of workers available to agriculture is now the smallest in several decades. Total employment on farms, according to the Bureau of Agricultural Economics, was 6,524,000 in December 1951, in comparison with a 1945–49 December average of 7,353,000.

Although we do have an underemployment problem in some areas due to the existence of a substantial number of farm families who are farming with inadequate resources, this is not the answer to our farm-labor problem. For the most part these underemployed families are more likely to go into industry than to migrate long distances for seasonal agricultural work.

In recent years we have been forced to supplement our declining agricultural labor force by using migratory workers from Mexico. The present Mexican labor program is scheduled to expire February 11. It is imperative that this program be temporarily extended and that Congress enact legislation for a more permanent program as soon as possible. If this is not done, our ability to maintain the production goals which the Department of Agriculture has established for 1952 will be seriously impaired.

Price controls

The Economic Report recommends that price and wage controls be renewed for 2 years.

We have been repeatedly told that the present period of tension and mobilization may be of extended duration and that we must be prepared to maintain a state of readiness for 5, 10, 15 years, or perhaps longer. In the light of this fact we must make sure that our policies will not only meet present needs but will be policies under which the American system can operate over a long period of time. While we recognize that in the present situation the Government must be allowed to exercise certain powers not necessary or appropriate to more normal conditions, we are convinced that, in an emergency which may prove to be of long duration, direct Government controls must be held to a minimum and we must seek to minimize Government interference with the things that have made our economic system the most efficient in the world. Price and wage controls constitute a maximum interference with our present economic system. In fact, carried to their logical conclusion, price-and-wage controls, rationing, and subsidies would mean the complete abandonment of our present system and the loss of the freedom we are arming to preserve.

Furthermore, price and wage controls do not prevent inflation. As a matter of fact, price and wage controls make the control of inflation more difficult by concealing from the people the fact that inflation is destroying the purchasing power of their money and by diverting attention from the things that must be done if we really want to control inflation.

The attendant evils of price and wage controls are many. Reduced production, less efficient processing and distribution, poorer quality products, black markets, rationing, proposals for subsidies in lieu of prices, and expanded controls of every sort are natural consequences. Controls also waste manpower, our scarcest resource, not only in the Government where millions of man-hours must be spent on the unproductive job of writing regulations and the impossible job of enforcing them, but at every level of industry where people subject to regulations must try to interpret and comply with them.

It seems to us that the Economic Report is most unrealistic in ignoring the serious problems which inevitably result when political decisions are substituted for the automatic functioning of free markets. It is totally unrealistic to discuss price control without pointing out that any successful effort to depress prices below the free market level will inevitably lead to shortages and rationing or maldistribution. Whenever we decide not to use prices to distribute goods, some sort of rationing is inevitable. We must either ration by Government regulation, by voluntary action of sellers, or by a mad scramble in which each customer tries to get their first.

We are for the adoption of a sound inflation-control program based on effective use of the real antidotes to inflation which, as you know, are strict Government economy, a balanced Federal budget, increased production, effective credit control, intelligent management of the public debt, and increased private savings. We are opposed to any further extension of price and wage controls beyond their present expiration date of June 30, 1952.

With this background we wish to comment briefly on some of the report's specific statements with reference to price control.

We note on page 13 of the report a statement that "We contained inflation, under more difficult circumstances, during World War II, although we did not do a good enough job of forestalling postwar inflation."

The fact of the matter is that we created inflation during World War II when we unbalanced the Federal budget and created new money by selling bonds to the banks. While the fighting lasted, this inflation of our money supply was partially concealed by price controls, rationing, the unavailability of goods, and increased savings. After the war, controls were removed and we went back to a free-choice system. It proved to be productive. Of course, prices rose as people began to use the dollars that had been added to our money supply by the inflationary policies of the war period, but the alternative would have been continuation of controls which would have hampered production and prevented the operation of a free-choice system.

On page 147 it is said that "Wage policy is even more difficult than price policy because it involves the very livelihood of millions of families."

Prices also involve the livelihood of millions of people. It should not be necessary to point out that the prices of farm products determine farm income or that the prices industry can get for its products determines its ability to pay wages.

On page 23 we find it said that "The Office of Price Stabilization has made great progress during the past year toward a balanced price structure which can be held firmly. It is developing simple, enforceable regulations to cover individual industries and commodities."

OPS does not deserve credit for the stabilization achieved in 1951. The important factors which acted to check the rise of prices last year were a phenomenal output of goods and services; a realization on the part of the people that shortages were not as imminent as had been expected; increased taxes and a Government surplus in the 1951 fiscal year; increased personal savings; and last, but not least, a general tightening of money and credit which followed when the Federal Reserve System stopped pegging the Government bond market last spring.

We have not seen any simple OPS regulations and do not believe that it is possible to write a simple price-control regulation.

The President has recommended the reestablishment of slaughter quotas. We believe that this would be a mistake. Quotas are intended to counteract the disruptive effect of price controls, but experience has demonstrated that they only create further disruptions.

Credit control

The Economic Report recommends that Congress restore the administrative discretion that was formerly available to the Board of Governors of the Federal Reserve System in the exercise of the selective credit controls authorized by the Defense Production Act. We agree that this should be done. Effective credit controls are one of the essentials of a sound anti-inflation program, and the Federal Reserve Board should be free to adjust these controls to the needs of changing conditions.

The Economic Report also recommends that the powers of the Board of Governors of the Federal Reserve System to impose reserve requirements be enlarged.

The voting delegates at our last annual meeting adopted a resolution on this subjct as follows:

"The Federal Reserve's authority to vary member bank reserve requirements should be increased. If the inflation threat continues and conditions warrant, reserve requirements for banks should be raised."

While we believe that it would be desirable to give the Federal Reserve banks additional authority to increase member bank reserves, we wish to point out that higher reserve requirements will not make a real contribution to the control of inflation if the Federal Reserve System, after raising requirements, then proceeds to provide banks with the required additions to their reserves by open-market purchases of Government securities. On this point we are in disagreement with the Economic Council's apparent belief that it is appropriate for the Federal Reserve System to create unneeded bank reserves by buying Government securities and then to offset the inflationary effects of this process by raising reserve requirements. We believe that Federal Reserve purchases of Government securities should be related to the Nation's need for money and credit and that it is fundamentally unsound for the Reserve System to buy Government securities for the sole purpose of keeping interest rates low.

The President has also asked for authority to control commodity-exchange margins. We do not believe this is necessary or desirable.

Import controls

The President has recommended the repeal of section 104 of the Defense Production Act, which restricts imports of certain commodities, particularly dairy products. It is the policy of the American Farm Bureau Federation to support continuation and expansion of the reciprocal trade agreements program, provided effective administrative action is taken to implement section 22 of the Agricultural Adjustment Act and the escape clause of the Reciprocal Trade Agreements Act of 1951 so as to protect affected interests against excessive imports to the full extent of the law.

Since the President has given assurance in a letter to Hon. Ernest McFarland, which has been made public, that "these procedures shall be fully implemented and promptly applied, in accordance with the spirit of the law," we are supporting the repeal of section 104.

Farmer cooperatives

The President has asked that the tax on unallocated reserves of farmer cooperatives be modified to provide an exemption for newly organized cooperatives for a limited period of years.

The applicable portion of our resolutions reads as follows:

"We commend Congress for the enactment of the provisions of the Revenue Act of 1951 which (1) make it clear that cooperative savings allocated to member patrons are taxable in the hands of such patrons and (2) provide that savings held by cooperatives in the form of unassigned surpluses shall be taxed in the same manner as the profits of other corporations. These provisions constitute a great safeguard to the interest of true cooperatives. We will insist on the proper interpretation and administration of these provisions."

We believe that the law with regard to the tax treatment of unallocated reserves of farmer cooperatives is fair and equitable and that it would be a mistake for Congress to reopen this question at this time.

Under the law a cooperative can retain needed savings without paying the corporation income tax, provided such savings are allocated to reserve accounts in accordance with normal accounting procedures or are allocated to member patrons and taxable in their hands. It therefore appears that the proposed tax law modification is unnecessary.

In conclusion, I want to express our appreciation for the opportunity you have given us to comment upon this important Presidential report.

Sincerely yours,

ALLAN B. KLINE, *President.*

NATIONAL FARMERS UNION,
Washington D. C., February 6, 1952.

Hon. JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
Senate Office Building, Washington, D. C.

DEAR SENATOR O'MAHONEY: We appreciate having the opportunity, extended by your letter of January 16, 1952, to submit to your Joint Committee on the Economic Report the recommendations of National Farmers Union with respect to the main recommendations made by President Truman in his Economic Report.

Improved farm price supports essential

The President's Economic Report and the Council's Annual Economic Review correctly, in our opinion, direct attention to improvement needed in existing price-support legislation. Although the Nation currently enjoys very favorable circumstances with respect to food and fiber supply, this may not long continue. We are using up our cotton and feed grains at a faster rate than we are producing them. The sudden development of a shortage of Irish potatoes, the doubling of the retail price of potatoes, and the consequent need to improve price ceilings present a stern warning and a pertinent illustration of how suddenly a scarcity situation can descend upon us if we do not carefully consider the important role of adequate farm price supports in our national food and fiber policy. The potato price-support program was abolished by law prior to the 1951 planting season. Faced with an uncertain future, farmers reduced their acreage of potatoes by more than 300,000 acres and apparently expended less fertilizer, insecticides, and labor on the potato acreage that was planted. Average per-acre yields dropped from 253 bushels per acre in 1950 to 241 bushels in 1951. Result was that total production of potatoes dropped by more than 100 million bushels, or about one-fourth.

The experience with potatoes indicates that the course of wisdom would be to reexamine the price-support program for cotton, wheat, peanuts, dairy, poultry, and livestock products and for corn and the other feed grains. Currently our annual domestic consumption of these commodities exceeds the annual production, with the result that we are eating into our safety reserve stockpiles. Each year's carry-over is less than that of the year before. If these trends continue, we face the possibility of a feed grain, food, and fiber shortage that will endanger not only our present standard of living but also our ability to maintain the economic stabilization program.

In this situation, in light of our experience this year with potatoes, it is imperative that farm price-support legislation be consistent with the need for increased farm production. The President's Economic Report recommends the correction of one of the weaknesses in existing price-support legislation. The Agricultural Act of 1949 sets up a sliding scale of supports whereby the level of supports drops from 90 percent of the parity price to 75 percent as the supply percentage of the commodity increases. We concur in the President's recommendation that this sliding-scale provision be repealed. We feel that farmers are entitled to a parity of income with other economic groups and that steps should be taken to assure support prices at 100 percent of parity.

The 1949 act also has a parity cut-off date set at January 1, 1954, which will result in decreasing the parity price of cotton, wheat, peanuts, and corn. Most of the feed grains and many other important farm commodities are already being subjected to transitional parity whereby the parity price is dropped by 5 percent each year until they reach a new parity level calculated by a new and lower formula. This new parity formula, while desirable for use with dairy products, tobacco, rice, and some other commodities, puts an undue penalty upon many farm commodities, the production of which in greater supply is now needed and has been requested by the Department of Agriculture. This new parity price formula with its 10-year moving average insures that the increased production to meet 1952 and 1953 production goals will not only hold prices down in the year of the increased production but will also result in holding down the calculated parity price of that commodity for a full decade following. The Young-Russell bill to eliminate this weakness of present legislation should be adopted at an early date.

Not only is the needed increase in food and fiber production endangered by the sliding scale and parity roll-back provisions of the Agricultural Act of 1949 but also by the circumstances that this act provides definite assurances to only a small handful of commodities and does not authorize the use of a fully workable and efficient method of carrying out a support program for meat, eggs, dairy products, and other perishables. The 75 percent of parity assured supports for dairy products is not only too low to encourage the maintenance and expansion of dairy production but also does not provide this assurance direct to the dairy farmer. In the absence of such direct assurance, some dairy farmers, particularly in view of the tightening of farm-labor supply and the high price for beef, may become discouraged and sell off their milk cows.

Repeal the penalty tax on farmer cooperatives

Farmers Union is gratified to note that the President has recommended a change in the recently adopted penalty tax on farmer-owned and farmer-controlled cooperative associations. This penalty tax on cooperatives should be repealed and taken off the books. While the enactment of the revision recommended by President Truman would be an improvement over the existing situation, we do not feel that any farmer cooperative should be subjected to such a penalty tax.

Recommend pay-as-we-go taxes and savings

In a practically full-employment economy, each dollar of increased Government expenditures for materials or services which do not directly result in an increased supply of consumer goods should be counterbalanced by approximately an additional $2 of increased tax revenue and personal savings. To reduce this prospective inflationary gap in the present and next fiscal year, Farmers Union will support the President's recommendation that sufficient tax loopholes should be closed, and sufficient tax rate increases for those groups best able to pay should be enacted.

Farmers Union further recommends that any remaining gap of increased expenditures not covered by increased revenues in twice the amount should be filled by the establishment of a compulsory savings program based upon an ability-to-save schedule similar to an improved ability-to-pay principle incorporated in the personal income tax schedule. These savings should be put into the form of bonds owned by the individual saver, and have redemption values which would fluctuate with the value of the dollar.

Selective credit controls

Farmers Union views with alarm the apparent tendency for indiscriminate shortening of credit facilities available for increased production, and the indiscriminate up-creep in interest rates. Short credit and rising interest rates applied across the board contain not only a limiting influence upon essential plant expansion and improvement, enlargement and development of farms, but also harbors the embryo of a disastrous deflationary development. Congress should restore the authority for more selective credit controls so that unessential expenditures and investments can be discouraged while desirable production increasing investments will not be hampered.

Price and wage controls

Farmers Union has reserved its position relative to extension of the price- and wage-control provisions of the Defense Production Act as amended, pending the final settlement of the steel price and wage case and similar situations that may develop this winter and spring. Farmers Union does not believe it is fair or equitable, nor shall we stand idly by to accept strict price-ceiling regulations over farm commodities at a time when no effective price control exists for the manufactured products that farmers have to buy to maintain production and family living standards.

Farmers Union has repeatedly recommended the absolute freeze of wholesale and retail prices with posted specific dollar and cents ceilings coupled with only such wage increases as will reflect changes in the cost of living and economy wide increases in productivity per man-hour and farm commodity prices that will reflect parity.

We realize that such a system will require a certain amount of cost absorption on the part of everyone including manufacturers and middlemen. We think that industrial profits before taxes are now at such a level that considerable cost absorption can be accomplished without undue hardship to owners of common stock. If undue hardship were involved in particular cases, this hardship could be relieved by issuance of tax certificates to be used in payment of future tax obligations of the concern suffering the hardship. Specifically, the mobilization authorities should stand strongly against the attempt of the steel companies to rape the economy by demanding of the Office of Defense Mobilization and the Office of Price Stabilization a pass through to steel-price increases of any wage increases granted to labor by the Wage Stabilization Board as well as increased profit margins. Moreover, Congress must resist the attempts of selfish groups to move forward the cut-off date of the Capehart and Herlong amendments.

Measures to increase farm production

One of the most glaring and serious omissions of the President's Economic Report and of the Council's Economic Review is the complete absence of any consideration of special measures essential to increasing the productivity of the some two or two and a half million farm families whose present resources and farming methods do not allow them to make their maximum contribution to national production.

A distinguished member of the joint committee has just published an article on this important subject in the January issue of the Farm Policy Forum, a publication of the Iowa State College. Senator Sparkman's article is entitled "Our Underutilized Rural Resources." This article brings out an astounding and very important fact. As much as we are now doing to bring about increased farm production, the Nation is still largely overlooking a most important and almost untouched source of increased production of food and fiber.

A few years ago the joint committee set up a Subcommittee on Low-income Families. This subcommittee, under Senator Sparkman's chairmanship, put its staff to work on the problem of low-income families in agriculture and also held extensive hearings. Secretary of Agriculture Brannan among others gave extensive testimony indicating the magnitude of the problem, and potentialities involved for greater production, and recommended public action that should be taken to more fully release the productive energy of these more than 2 million fine farm families. Staff reports of the subcommittee have shown the possibilities.

Effective employment for these low-income rural families would add the equivalent of 2.3 million workers to our labor force. It is tragic that we continue to sleep on our oars on this matter.

Senator Sparkman's words are clear, concise, and to the point. The facts revealed are amazing. Here is what Senator Sparkman says in his article: "Here are the challenging figures. Suppose we put out our best efforts along traditional lines, intensifying our educational programs on improved land use, better disease and pest control, and feeding of better balanced rations together with making needed supplies of fertilizer, farm machinery, and pesticides available. We may be able to increase our national farm output by 10 to 15 percent in the next 5 years.

"At best, using this traditional approach, we cannot expect to increase farm output by more than 20 percent in any section of the country. In contrast, if, through some new approach, we could increase the productivity of farm workers (able-bodied people of working age) in the smaller than medium-sized family farms up to the level of productivity of the workers on the medium-sized family farms, Bureau of Agricultural Economics data indicate total output would be increased in the Appalachian and Southeastern States by 75 to 80 percent.

"National output would be increased 40 percent—rather than 10 or 15 if the production of all farm workers in the United States on these small farms could be raised to the level of productivity of workers on the medium-sized farms."

Not all of this production increase would be in farm products; some would come in industry. "But manpower is the over-all limiting factor in mobilization."

It is tragic that this Nation does not take the necessary steps to improve the productivity and opportunity to earn higher incomes of these 2½ million low-income underemployed farm families.

The techniques are known. In fact, a skeleton program of the type required has been operated by Farmers Home Administration and other agencies for many years. These techniques have been tried and proven, as the statistics on the debt repayment, and increased production and income of these borrowers indicate. What is needed is a rapid large-scale expansion of the farm purchase, enlargement, development, and improvement-loan program. The unique contribution of Farmers Home Administration is the combination in a single package of the technical advisory assistance in farm management and credit resources required by these low-income farm families to greatly expand their productivity per man and per acre. I urge that, in whatever report your committee makes to this session of Congress, you strongly urge adequate increased appropriations for Farmers Home Administration technical advisory services and loan authorization to make a really important start toward the solution of this important problem. Correlary expanded programs of the Agricultural Extension Service, the United States and State employment services, and vocational agricultural education should be studied and recommended along with legislation to encourage the development and location of industry in areas now characterized by a heavy concentration of low-income farm families.

Cooperation with other free nations in building a better world

Farmers Union continues to urge the adoption of all measures that will contribute to the earliest possible attainment of a world brotherhood of prosperous democratic nations living at peace with one another under a world government with sovereign powers derived directly from the people. To attain this aim means that the acknowledged prestige, influence, and preeminent economic productive ability of the United States should be geared in with those of other free nations to uproot injustice, correct inequities, and abolish despotism wherever it may exist in the world and to expand productivity capacity and raise living standards everywhere. This is why such important elements of our foreign policy as emphasis upon agricultural land reform, free trade labor unions, farmer-owned and controlled cooperatives, free farm organizations, and abolishment of cartels and other monopolistic arrangement must be supported and continued, both in our bilateral programs and through the international organizations.

Adequate financial provision should be made to develop and maintain an expanded point 4 program of required technical assistance and international investments requirement to greatly speed up the lagging tempo of international economic and social development.

Needed increase in expansion of domestic plant capacity

The present goals for expansion of domestic industrial plant capacity are much too low in the face of present imperatives of the world situation. Instead of 125 million tons of steel capacity, we should be planning for 150 million tons. With stepped-up military requirements, the Nation is taking a grave chance of a food and fiber famine because we are not planning for enough plant capacity for fertilizer, nitrogen, phosphate, and potash. The prospective supply of insecticides and weed killers is just barely sufficient for current needs. Steel, aluminum, and farm machinery plants are currently and prospectively unable to supply even the minimum needs for farm machinery and spare parts, roofing, fencing, and other farm supplies required if farmers are to meet record high production goals requested of them by the Department of Agriculture.

Farm programs must be maintained and improved

The current need for increased farm production not only demands immediate enactment of improved farm price support legislation but a greatly expanded program for increasing the productivity of low-income farm families. If we are not to lose much of the ground we have already gained, the Congress must be every careful not to apply a broadax to the appropriations for the important programs administered by the Department of Agriculture. While these programs require improvements along the lines I have recommended, they do now provide a solid necessary foundation for continued expansion in the productivity of United States agriculture.

The period into which we as a Nation are moving is one of unusual effort of indefinite duration. If we knew we were facing only a brief period of extra effort we could possibly afford the luxury of setting aside for the period of emergency some of our fundamental basic efforts relating to research, agricultural soil, water, and forest conservation, the school-lunch activity, and the other long-term farm programs that contribute so vitally to national strength. However, if I am reading the signs right, we must gear ourselves to develop and maintain maximum national strength for an extended period. To do that we have to keep our schools open and improve them, we've got to keep our basic research going, we've go to improve and save our soil and water resources. We must continue to do all of these things that are necessary to give the Nation the strong democratic bulwark of a sound, healthy, productive agricultural pattern of family farms.

If farmers are not to be penalized for patriotic effort, but on the contrary to be encouraged to make the maximum sustained effort, we must continue and strengthen the democratically elected farmer committee system by which major farm programs are administered, preserve and expand the experimental crop-insurance program to additional counties, and authorize the Commodity Exchange Authority to expand its activities to eliminate inflation-stimulating speculation in the great commodity markets while preserving them for safe and constructive hedging operations.

Conclusion

The challenge of world service to the United States at this time requires that the Nation go all out to increase our productive ability and maintain economic stability. Farmers stand ready to cooperate and extend their utmost efforts. However, it should be understandable to all fair-minded men that working farmers can take no other course than to demand an equality of effort and sacrifice on the part of all segments of the national economy. Working farmers cannot make their maximum contribution nor can they with dignity accept production goals or stabilization measures that subject farmers to greater risks with chance of lesser rewards than other citizens of our great Nation.

In the preceding paragraphs, I have indicated several general areas in which, in our opinion, the Nation is not doing as well as it could. However, a point that should be made in respect to the Economic Report is this. The United States and its people, in the year 1952, are in relatively good shape economically. Although the rate has been too slow, we have continued to build our basic productive capacity; while our inflation control efforts have not been completely successful, they have maintained a tolerable degree of stability; programs and policies developed over the years have held down economic tensions and group conflicts.

I do not want to convey the impression that Farmers Union thinks everything is in nearly as good shape as it could be from an economic standpoint, but I do want to emphasize that our Nation is in the most favorable economic condition in its history, and with the greatest current economic attainment of any nation in the world.

United States consumers currently are able to buy with their incomes the widest variety and greatest quantity of nutritious foods and warm clothing. This favorable condition is due in large part of the magnificent growth in the productive capacity of United States family farmers. With very few new acres of land, and with much less labor, United States family farmers have increased their output of marketable food and fiber products by more than two-thirds in the past two decades.

This remarkable achievement was possible because farm families in the country have gone all out in productive efforts. Farm families were able to make these added efforts count in increased production because their energies were released and strengthened by food, fiber, and farm programs, developed over the years by the Federal Government, responding to the needs of the times and the aspirations of the people. This Nation now has a good farm program that will help greatly to maintain the Nation's productive strength and economic well-being in the indefinite period of partial mobilization and world tension that apparently lies ahead. Our farm program was developed by trial and error and has constantly been changed to meet changing national needs. Good as it is, however, the present farm program needs some additional adaptation to gear it to current and foreseeable future needs.

I appreciate this opportunity to have informed your committee of the position of Farmers Union on the many subjects discussed in the Economic Report. I hope that your committee will give each of these matters the full consideration they require. I feel that your own impartial study of these problems will lead a majority of the committee to recommend the immediate initiation of the measures this letter urges in the national interest.

Kindest personal regards,

JAMES G. PATTON, *President.*

CHAMBER OF COMMERCE OF THE UNITED STATES,
Washington, D. C., February 7, 1952.

Hon. JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
Congress of the United States, Washington 25, D. C.

MY DEAR SENATOR: The attached memorandum is in response to your letter of January 16.

It was prepared by our economic research department, in consultation with other Chamber officials, and represents the views of our member organizations.

I hope it will be possible for you to include this statement in the printed record of your committee hearings.

Yours sincerely,

D. A. HULCY, *President.*

ECONOMIC REPORT OF THE PRESIDENT [1]

President Truman, in his Economic Report to the Congress, reiterated the basic objective of a program of defense readiness in which increased industrial capacity over the next several years would be sufficient to carry the defense program as well as maintain and gradually increase pre-Korean standards of living.

The President, as well as most competent experts, has pointed out that we must pay for the defense program on a current basis if we are to have any effective control over inflation in the long run. In spite of this, the President admitted in his Economic Report that pay-as-we-go was no longer possible. As he says: "The sound course in these times is to base outlays upon essential national needs, and then obtain the funds to cover these needs by current taxation insofar as possible. But if the only choice is either to run a deficit of limited size and duration in the Federal budget, or to run a deficit in our national security effort, by far the lesser hazard now is to run a deficit in the budget."

This analysis of the situation overlooks the basic fact that we may so seriously weaken our economic strength, the real foundation of our military power, through a long-run program of spending and deficits as to largely nullify the results of rearmament.

The security program of the administration, embracing both our defense program and military and economic aid to our allies, is of such magnitude that it is impossible to adhere to a policy of paying-as-we-go. This is in spite of the fact that we have had three revenue acts since Korea, raising income taxes on both individuals and corporations to dangerously high levels.

Mr. Herbert Hoover, in a radio address in January 1952, calling for the limitation of our defense and foreign aid commitments to what we could carry without seriously weakening our economy, pointed out this fact. He said: "A man can carry a 300-pound weight across the room. But he would break his back if he tried to carry it around the block."

Our economy can stand a tremendous load for a short time, but we may break our backs if we try to carry indefinitely a defense load greater than we can pay for out of current income.

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[1] Prepared by Economic Research Department, Chamber of Commerce of the United States, Washington 6, D. C.

ECONOMIC CONTROLS

Instead of recognizing this, the President in his Economic Report proposes a comprehensive system of direct controls to combat inflation while paying little more than lip service to those economic measures that strike at the heart of this disease. In fact one of the most important anti-inflationary devices was not even mentioned.

To combat inflation, President Truman has asked for tighter price controls, tighter credit controls, control over business investment, higher bank reserve requirements and control over margin requirements for commodity exchanges.

But, he failed to mention a most important element in inflation control—debt management policy. The support of Government bond prices at par by the Federal Reserve System, which was ended by the accord reached in March 1951 by the Federal Reserve and the United States Treasury, had been one of the most inflationary phenomena in our economy. Such a policy weakened the ability of the banking system to control and regulate cost and particularly the volume of money and credit. The sharp price increases after Korea were financed by the expansion of bank credit.

After last March, when the Federal Reserve System withdrew its peg from under Government bond prices, the ability to control credit creation and to effectively use traditional instruments for regulating the supply of money and credit once more became effective. Yet, the President in his Economic Report, while pointing out the inflationary strains inherent in the defense period and giving a comprehensive program for controlling inflation, failed to mention this important matter.

The President recommended that efforts be made to increase private sales of Government bonds, presumably at prevailing interest rates, in spite of the fact that the structure of market rates has been rising. The continuation of an easy money policy to facilitate Government financing while using direct controls to regulate private credit appears to be the objective. Direct and selective credit controls will be used to hold down consumer and business borrowing, but no obstacles, such as rising interest rates, are to be placed in the way of Federal borrowing. Such a policy facilitates deficit financing while giving the appearance of attempting to control inflation.

BUILT-IN INFLATION

President Truman's Economic Report carries many proposals that would build more inflation into the economy. He asks an abandonment of the flexible farm price supports inaugurated in the Agricultural Act of 1948, in spite of the fact that this has been a sound approach to the problem of price supports. High price supports, President Truman said, were necessary in order not to penalize farmers for attaining the production goals set by the Government. This is an indirect plea for the Brannan plan. The report even mentioned direct payments to farmers as one method of supporting prices of perishable products.

High, rigid price supports are built-in inflation and will certainly create more fiascos such as the potato scandals of a few years ago. They inevitably entail production and marketing controls. These allow for an inadequate shift of resources from less efficient uses and less efficient operators. Such a program continued over any period of time would destroy the vitality of American agriculture. More and more, competent experts in the field of agriculture are pointing this out.

At a time when unemployment is at an almost irreducible minimum; the President requests a higher level of benefit payments, and legislation to strengthen the Federal-State unemployment insurance system. This proposal in reality is for Federal domination of unemployment compensation insurance. It ignores the successful record of State unemployment compensation plans and that average unemployment benefits have more than kept pace with the rise in the cost of living. Furthermore, the States' employment compensation reserve funds have reached an all-time high while the United States Treasury is getting ready for deficit spending.

Nationalized unemployment compensation insurance speeds the end of experience rating for employer tax rates and the end of benefit formulas geared to State and local conditions. If benefit payments are substantially raised by Federal contributions to State unemployment payments, any semblance of financial soundness in unemployment insurance is at an end. Such legislation would reduce incentives to work if it liberalized benefits at a time when the maximum contribution of every worker is needed.

WAGE AND PRICE CONTROLS

The Economic Report ascribes the price stability of 1951 mainly to the program of price controls originated last February. The President says that "price and wage controls are directed both to restraining income increases, and to holding the price line against unavoidable increases in demand."

The report states that prices and profits are, in general, high enough to provide ample incentives and to permit absorption of cost increases. He asks that the law be tightened.

But if this is so, if producers have ample incentives, why was it necessary for OPS to increase price ceilings on machine tools last summer in order to get adequate production?

The Herlong amendment to the Defense Production Act of 1951, requiring the maintenance of customary margins for distributors, the President said, virtually guaranteed that every dollar in cost increase would become much more than a dollar to be paid by the consumer. This, of course, ignores the distributor's margin as a cost. It is furthermore designed as a cost absorption measure, since distributors must maintain reasonable percentage margins if they are to cover costs. Many of their most important costs (rents, commissions on sales, insurance, and certain taxes) are based upon dollar volume of sales and sale prices. Competition should and can be relied upon to keep margins under control. Earnings of retailers in 1951 show that this has been the result.

Many prices are now below the ceilings established last winter and spring by OPS. There is now much talk of making these ceilings more realistic by reducing them nearer to current market levels. Measures such as these completely hamstring market forces and prevent shifts in resource use and production that could most efficiently utilize productive facilities.

The original intent of OPS was that it would use its power to prevent extreme and destrictive price increases and just as soon as the necessity for its operations disappeared, it would be abolished. The President's Council of Economic Advisers has stated:

"Except in an emergency period, such as the present, the benefits of general price controls are outweighed by their draw-backs."

Now that many prices are below ceilings and business in many lines is slack, it is difficult to see the benefits of price controls.

Regarding wage stability, a different tack is taken in the President's report. In fact, he speaks of price control but wage stabilization. While noting that wage controls prevent buying power from rising too far above available supplies of civilian goods and cut at the source of inflation by limiting rises in costs and prices, the report points out that wage policy should do no more than put a brake upon excessive wage adjustments, while at the same time recognizing that some adjustments in a free and dynamic economy are essential from the viewpoint of both equity and incentives. This concept of equity and incentive seems to be largely ignored in the case of price controls.

In pointing out that the burden of defense should be shared fairly, the President says that adjustments in wages, to take account of increases in the cost of living, are a matter of simple equity. This is so, he says, because price inflation is not a fair way to impose the burden of national defense.

Price inflation is unfair, but not in the way the Economic Report indicates. Price inflation harms people on fixed or lagging incomes, the most conspicuous of whom are not among the great body of industrial employees.

When a minority of all organized workers are able to obtain cost-of-living increases, it means they are largely able to avoid the burden of defense. By definition, cost-of-living increases allow for undiminished purchasing power with respect to some prior base period. This means that the command over goods and services of those receiving such increases will not diminish, at a time when the total supply of goods and services, according to the President's own statement, is bound to fall.

The result, of course, is that other groups not fortunate enough to gain cost-of-living wage increases must shoulder the full burden in terms of diminished real income. This is the equitable way of sharing the burden of which the President speaks. If, on the other hand, all workers are to receive cost-of-living increases, then other groups in the economy, dependent upon other types of income, will have to carry the burden. If a universal cost-of-living adjustment is allowed for all types of income, then no one benefits and price inflation runs rampant.

The President also says that wage adjustments to allow for increases in productivity can provide incentives that outweigh the possible inflationary effects, if carefully used and administered. Once again the question of incentives is raised with respect to wages, when cost absorption is the strong element in the price-control program. It is true that productivity increases in wage payments, if they were matched by actual increased civilian production that occurred simultaneously with the wage increase, would have little inflationary effect. No formula or method devised has yet approached this objective. Productivity formulas in most wage contracts, on the whole, are inflationary, since they are predicated upon the basis of fixed yearly increases in productivity. No such thing, of course, occurs.

There is an implication running through the Economic Report that consumer prices have outpaced wages and that profits have been maintained. The exact reverse is true.

The accompanying tabulation indicates that since August 1948, the pre-Korean postwar peak in consumer prices, both average hourly earnings and average weekly earnings in manufacturing have gone up about twice as rapidly as have consumer prices percentagewise.

Relative price and manufacturing wage changes

	Consumers' Price Index	Average hourly earnings	Average weekly earnings
1929	122.5	$0.566	$25.03
1939	99.4	0.633	23.86
August 1948 [1]	174.5	1.349	54.05
June 1950	170.2	1.453	58.85
December 1951	189.1	1.635	67.36

[1] Pre-Korean peak in prices (1935–39=100).

Percentage rise in earnings and prices from selected dates to December 1951 [1]

[Percent]

	Consumer prices	Hourly earnings	Weekly earnings
1929	+54.4	+188.9	+169.1
1939	+90.2	+158.3	+182.3
August 1948	+8.4	+22.5	+24.6
June 1950	+11.1	+12.5	+14.5

[1] Most recent data. All data from U. S. Department of Labor.

Since June 1950, wage earnings have kept ahead of price increases. To complete the record, data going back to 1939 and 1929 are also included in the tabulation. It is gratifying to note that in the last 12 years, while consumer prices have gone up about 90 percent, average hourly earnings in manufacturing have gone up about 158 percent, and average weekly earnings about 182 percent. The record since 1929 is even more startling.

On the other hand, corporate net profits have declined steadily since the peak fourth quarter of 1950 when they reached nearly $28 billion at annual rates, although they came to about $23 billion for the year 1950.

In 1951 net profits were about $18 billion. One would have to go back to 1946 to find a lower level of corporate net profits. These matters are important in appraising proper public policy with regard to the complicated fields of wages, prices, costs, and profits.

FOREIGN AID

Next to the military part of the budget, proposed expenditures for foreign aid are the largest item in the new budget. In pointing out the need for aiding foreign countries, the fiction of separating aid into "military aid and economic aid" is admitted. They both are for the same function and have the same objective.

As the President states: "When we supply military goods, some of the most dangerous cut-backs in European civilian production can be avoided. When we supply economic aid, some European productive facilities and foreign exchange are released for defense."

What this means is that when we supply military aid, we are enabling foreign countries to rearm at a faster rate than they think advisable on the basis of their own internal conditions. The welfare schemes of many European countries are perpetuated with American tax dollars as a consequence.

While the chamber of commerce has supported foreign aid programs, we cannot refrain from noting that after several years of tremendous foreign aid on the part of this country, the European economies appear little stronger than after the war. Furthermore, it seems that our foreign aid in many cases has prevented these nations from making the necessary economic adjustments required if they are ever to stand on their own feet. Much of the spending we have done in this realm may have done more harm than good.

We must maintain a strong, dynamic domestic economy. This is as important from the standpoint of national defense as building up our military power, since the foundation of military power is our economic strength. We cannot afford commitments that will maintain for the indefinite future present high-tax burdens and continued Federal deficits.

COMMITTEE FOR ECONOMIC DEVELOPMENT,
Rochester 4, N. Y., February 6, 1952.

Hon. JOSEPH C. O'MAHONEY,
United States Senate, Washington, D. C.

DEAR SENATOR O'MAHONEY: This is in reply to your letter of January 16, asking my comments, as chairman of the Committee for Economic Development, on the Economic Report of the President.

It is the practice of CED to state its views on questions of national policy only after study and discussion by the members of its research and policy committee. The committee has not reviewed the President's Economic Report; hence I am not in a position to submit comments concerning the report on the committee's behalf. During the past year, however, the committee has issued several statements of national policy which bear directly on the subject matter of the report. Particularly relevant to your committee's present deliberations are the statement, Economic Aspects of North Atlantic Security (May 1951), and the statement, Price and Wage Controls (December 1951).[1] A copy of each of these statements is attached, and I shall be happy to submit additional copies if you wish them.

I am pleased to supplement the views expressed by our committee with some comments of my own. I believe that the President has properly called attention to some of our major economic objectives for the coming year. These are to continue to strengthen our security and that of our allies, to increase our production and our productive capacity, and to maintain adequate defenses against the threat of renewed inflation. I feel that we should also include as an important objective, increasing the efficiency of Government operations, both defense and nondefense.

It is essential that we continue rapidly to increase our military strength. It is also important that we do not subject our economy to unnecessary strain by wasteful expenditure or by building huge stockpiles of weapons which rapidly become obsolete. Whether the military program, as now conceived, is too large, too small, or of the right size to contribute most to our over-all security is a matter of judgment which depends largely on information not now available to me. I do believe, however, that too little attention has been given to nonmilitary security measures—diplomatic, psychological, and economic. For example, we have devoted too little effort to measures for the economic development of underdeveloped areas. Such measures can increase the world's wealth through expanded production and trade. They can, in the long run, provide an important measure of security for this country.

We in CED are seriously concerned at the mounting indications of waste and inefficiency in military spending. While it is encouraging to note the efforts already being made to achieve economy by the heads of the Department of

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[1] The documents referred to are available in the files of the Joint Committee on the Economic Report.

Defense, it would seem to me possible to reduce military expenditures by several billions annually without reducing the planned size of the program, by such means as more careful calculation of matériel requirements, greater attention in the development of specifications to conservation of materials and labor, the achievement of better balance in the procurement of complementary items, and more effective utilization of military manpower. I feel that a systematic and searching examination of the operation of the military program with a view to effecting all possible economies is a matter of major importance. It would not only save money now but also, by making military operations more efficient, increase our ability to mount an all-out effort if that should be necessary.

The nonmilitary expenditures proposed in the budget should also be reviewed with special care. Strict economy in all programs and the deferral of all nonessential expenditures are called for in a period when the strains on our economy are as great as at present.

I believe that a pay-as-we-go fiscal policy is desirable and achievable in the present situation, when the level of employment and production is high and we face the possibility of further inflation. I do not believe that it is desirable to add further at the present time to our already heavy burden of taxation. The answer to a balance in the cash budget without additional taxes is in a program of rigorous economy applied to both military and nonmilitary expenditures. The CED is now studying this matter with a view to making specific recommendations as to where reductions can be made.

To balance the cash budget would require expenditure reductions of something like $6 billion from the expenditure level proposed for fiscal 1953 by the budget message. The budget estimates do not appear to make sufficient allowance for the effects of bottlenecks in slowing the rate of increase of military expenditures, and they appear to have made inadequate allowance for the effects of our expected economic growth in increasing the yield of present taxes. Our preliminary calculations indicate that the probable cash deficit for fiscal 1953, on the basis of expenditure proposals carried in the budget and present tax rates, is likely to approximate $6 billion, rather than the $10.4 billion projected in the budget message.

In addition to maintaining a pay-as-you-go fiscal policy, I believe that other steps should be taken to protect the economy against the risk of further inflation. The Government should move at once on an intensive campaign to promote savings. For this campaign there is need for a new savings bond, bearing a higher interest rate and adapted as to its terms to the present desires of savers.

We should continue to utilize restrictive credit policies as a major means of inflation control. As CED said last year, "No program to stabilize the economy and control inflation can be effective unless it includes measures for limiting the expansion in the money supply and bank credit." Effective use of existing Federal Reserve policies to control credit may again become a matter of controversy in the months ahead, particularly if large-scale deficit financing is resorted to. In my opinion no action should be taken to undermine the authority of the Federal Reserve Board or to curtail its freedom of action in the control of credit and the money supply. In this connection it is my hope that the hearings next March before a subcommittee of your committee, under the chairmanship of Congressman Patman, will contribute to a better and broader understanding of the importance of monetary controls in a stabilization program.

CED has stated in some detail its position with respect to the use of price and wage controls in its recent policy statement on the subject. As we and others have many times pointed out, such controls do not deal effectively with the basic causes of inflation. Their use involves serious costs to the economy, especially if long continued. I believe that we should move as rapidly as possible to strengthen fiscal and monetary measures to the point where price and wage controls can be dispensed with. It should be possible soon to begin the release of some of these controls on a selective basis. The recent announcement by the Office of Price Stabilization of a decontrol board is a move in the right direction; the board should make a careful study of the operation of the control system, with a view to prompt initiation of decontrol measures. During the period in which controls are continued, I believe that the price control system should be modified to provide greater flexibility, along the lines proposed by CED in the attached statement.

While our primary concern during this year must be the strengthening of our security, it is time to begin to give attention to the longer-range problems of increasing the strength and stability of our economy. Important among the matters which require attention is the overhaul of the tax system. Our present system of taxation has been developed haphazardly, with little consideration of long-run needs. It imposes needless burdens on production and investment and it contains serious injustices. In view of the fact that the total burden of taxation now seems likely to be very heavy for a long time to come, it is important for our future welfare that our tax structure be thoroughly reviewed and redesigned in the interest of progress and equity. What is needed is a general reconsideration of the tax system as a whole, starting from agreement on desirable principles of taxation, rather than concentration upon particular aspects of the system.

I hope that the report prepared by your committee will urge that a thorough study of the tax system be undertaken now.

Very truly yours,

MARION B. FOLSOM,
Chairman, Board of Trustees.

NATIONAL ASSOCIATION OF MANUFACTURERS,
Washington 6, D. C., February 7, 1952.

Senator JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
Senate Office Building, Washington, D. C.

DEAR SIR: Herewith are comments of the National Association of Manufacturers on the materials and recommendations contained in the 1952 Economic Report.

We thank you for the opportunity of submitting our views, requested in your January 16 letter to Mr. William J. Grede, president of the association.

Sincerely yours,

JAMES W. DOUTHAT.

THE PRESIDENT'S MIDDLE COURSE

COMMENTS ON THE JANUARY 1952 ECONOMIC REPORT [1]

Near the beginning of the President's economic message to Congress the following statement appears: "* * * for the time being and perhaps for a long time, we must sail a middle course in an uncertain sea."

The purpose of this commentary is to take a close look at this middle course as it is embodied in the President's specific proposals. Is it truly a middle course? How well has it been charted? Where will it lead us if, as suggested we pursue it "perhaps for a long time"?

In what follows the President's own report and the report of his Council of Economic Advisers are treated as one document. The President's report states in brief outline the arguments and policy recommendations spelled out in detail by the Council.

Confusion in the report

Some parts of the report present very clearly a philosophy of economics and government. Just what that philosophy is will be discussed further on. But some parts of the discussion leave the reader confused as to just what is intended. These will be examined first, since obviously the "middle course" cannot lead us to any goal, desirable or undesirable, if it points in more than one direction.

An example of this type of confusion is the discussion of taxation. The Council states that it "* * * continues to attach great importance to the principle of the balanced budget during periods of heavy expenditure and inflationary pressure such as characterize defense mobilization." But apparently it does not attach enough importance to this principle to advocate its application in the immediate future. Tax increases are to be limited to "completion of the program proposed by the President a year ago." That is an increase of about $5 billion annually. The whole discussion is plainly an adroit attempt to place the blame for an unbalanced budget on Congress which did not grant in full the President's request, rather than to discuss the issues of the present moment.

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[1] The Economic Report of the President, transmitted to the Congress January 1952; together with a report to the President, The Annual Economic Review, by the Council of Economic Advisers.

Another example of statements which confuse the issue is the President's discussion of the Real Meaning of Economy. The following paragraph appears under this head:

"When we look at the whole picture, we find that true economy embraces two equally important elements: The first is the avoidance of unnecessary outlays; but the second, and equally important, is the making of necessary outlays. A nation which spent its resources foolishly would dissipate its strength. *But a nation which was too timid or miserly in applying its resources to urgent needs would fail to build up its strength*" (p. 13). [Emphasis added.]

A sensible person would not disagree with the underscored sentence. But why confuse the issue by calling this economy? Economy is a plain word and it means saving money. Why make it mean something else? The inclusion of these statements is evidence that the administration realizes that public sentiment for Government economy has become very strong and it is anxious to come out in favor of this "good word," even at the expense of changing its meaning.

Similar confusion exists on the fundamental objectives of economic stabilization. The following two statements appear about a hundred pages apart:

1. "* * * it is important to recognize that the problem of inflation does not exist in isolation, and that stabilizaion measures cannot be effectively administered in a vacuum. Stabilization, in large measure, is a means to other ends" (p. 42).

2. "However inflation may be defined, there is no dissent from the view that the ultimate consequence which gives concern is the increase in prices, and especially the increase in prices paid by consumers" (p. 140).

These two statements, while they are not diametrically opposed, present a convenient alternative of attitudes. Where the WSB permits the wage line to be breached, he adminisration can point out that after all "stabilization is not an end in itself." But in discussing cost absorption by producers it can be asserted that "the increase in prices paid by consumers" is the thing to be avoided.

Further confusion is caused by the fact that, while some of the recommendations are set in a context of economic argument, others are simply dicta pronounced by the President or his Council. Thus on the subject of sales taxes the question is brought up and dismissed in one paragraph:

"The alternative to relying upon the conventional tax sources for the additional revenue requirements would be to introduce a new, broad-base tax. One new type of taxation, which could raise substantial amounts of revenue, is a general sales tax. Whether imposed in frank manner upon retail sales or disguised as a general manufacturers' excise tax, resort to it would be a portentous departure from national tax policy which should not be considered at this time" (p. 135).

Surely the proposal for a general manufacturers' excise is not so palpably absurd that it can be brushed off this lightly.

Another case of similar quick dismissal of a major problem is contained in the following:

"* * * the Council does not claim any special competence to make recommendations regarding the size, composition, or timing of the basic defense program that may be required by the international situation—except in the event that the program became so large that there was real doubt about the adequacy of the Nation's economic resources to meet it. The program for this emergency, promising at the most to involve about half the relative burden shouldered at the peak of World War II, has not, in the Council's judgment, reached that size" (p. 40).

The question of how big a defense program the economy can stand is the chief economic problem of our day and deserves fuller treatment. Colin Clark has argued that a nation in which more than 25 percent of the national income is taken in taxes (a point we have already passed) is headed for disaster. Perhaps this simplified rule of thumb should not be taken too seriously, but there certainly is a danger point. The Nation is entitled to know on what grounds the Council formed its "judgment" that we have not reached it.

The most startling of the Council's dicta is its attitude toward foreign aid:

"As a logical consequence of processing and consuming a major share of the free world's resources, the United States must make available to others some of its resources, including its productive techniques and skills" (p. 43).

It is one thing to urge that it is expedient, under present conditions, to assist the economic and military build-up abroad. It is quite another to argue that foreign aid is a "logical consequence" of our superior wealth and productivity.

The philosophy of big government

Although some sections of the report show confusion of thought, several facts emerge clearly from the document as a whole. One is that the President and his Council are enthusiastic supporters of the philosophy of big government—that is, that the central government should play an increasingly important role in directing our economic life and should spend an increasing portion of the national income for us.

The keynote of this theme is struck in the following paragraph:

"Striking this balance also requires a judicious comparison of services rendered through the private economy and those rendered by government. Undoubtedly, at all levels of government, there are peacetime programs which must be cut. True economy and efficiency in public operations, desirable at all times, is imperative at a time when our resources face a persisting strain and when public financial burdens are unavoidably heavy. *Yet there can be no general presumption that public outlays are wasteful or nonessential compared with private outlays.* The building of a highway or a school may be far more essential to the conservation and advancement of our national strength than the building of a motion picture house or the production of luxuries. In an emergency, a sense of priority is highly important, and whole many desirable public services need to be restrained until we can affort more of them, *it would be false economy to strip them excessively in order to preserve materials and manpower for nonessential or wasteful private investment and consumption*" (p. 41). [Emphasis added.]

At first reading this paragraph seems innocent enough. It is difficult to take issue with any single statement in it. But it is pervaded with the view that the Government can make our economic decisions for us better than we can make them ourselves. Is there no "general presumption" that the people themselves are best qualified to judge which expenditures are "wasteful and nonessential?"

Although the President pays lip service to the objective of Government economy, 8 out of his 12 specific recommendations involve increases in Government spending.

The chart included in page 133 of the Council's report shows that, while defense outlays are increasing at an enormous rate, there is no sizable reduction in Federal budget expenditures for nondefense programs. The latter will be at about the same level in the first half of 1952 as n the first half of 1950—about 11 billion dollars. This despite the Council's recognition that "True economy and efficiency * * * is imperative."

The report endorses "power development by public agencies" especially where "Federal multipurpose river developments can provide large additions to power capacity along with other desirable results." No consideration is given to the question of whether private enterprise might not do a better job and whether the residents of the localities really desire the "other desirable results." This type of river basin development is recommended at a time when there is a desperate necessity to conserve materials.

Other recommendations involving increased spending even during the defense period include public financing of low-rent housing for low-income familities, Federal scholarships, and Federal aid to medical education. For the somewhat more distant future a program is recommended for a program of health insurance to "provide protection to meet costs of medical care and loss of earnings due to illness."

Such cuts in spending plans as are made represent not the elimination of programs but only their postponement. The President takes some satisfaction in the fact that he is building up a backlog of projects on which the Government can spend money—"When the defense program levels off, the resumption of these programs can help to take up any slack" (p. 12).

Not only must we submit to the program for bigger government, we must be made to like it. "The leadership of our great economic groups, while functioning as such, must be brought into a sympathetic relationship to some of the great decisions of national economic policy" (p. 44).

The President requests that the Defense Produce Act—with its broad grant of powers to him—be extended not for 1 year but 2.

On the subject of industrial dispersal the Council wants to go much further than military needs require. The program now in effect provides for dispersal within particular marketing areas, which is all that defense against bombing requires. But, the Council recommends a program of "regional decentralization of industry. In other words, the Government would, by some formula of its own, influence economic growth in favor of some regions and at the expense of others.

The purpose of such a program would be the "* * * further development of cores of economic strength in the less developed large regions of the country."

An especially ominous note appears near the end of the Council's report. The Council raises the question of our economic problems after the defense effort has passed its peak. It is unwilling to draw up any precise blueprint for meeting those problems but merely states "* * * we may draw assurance from the knowledge that the general techniques to be used when conditions change are fairly well-known and accepted" (p. 149). From the general tone we must conclude that the general techniques will involve more big government and more big budgets.

Monetary and credit policy

In its discussion of monetary and credit policy the Council is less than forthright. One senses a tendency to skirt around embarrassing questions. Either the Council members could not reach agreement with each other, or they were fearful of offending the President or other powerful persons.

Two things are recommended positively: "Greater reliance on selective credit controls" and increased use of "the instrument of reserve requirements." It is recommended that: "It will be sound policy for the Treasury to borrow new funds insofar as possible from nonbank sources, to minimize the inflationary potential of the deficit" (p. 141). However, there is no explanation of how this can be done since nonbank investors show no inclination to absorb a greater amount of the Government debt.

One of the chief economic questions of the day is whether the Federal Reserve System is to be permitted to retain its independence and carry out its function of maintaining economic stability, or whether it should be required to support the market for Government bonds at low interest rates. On this question the Council seems reluctant to commit itself. At one point it states: "It will be an important goal of economic policy to develop and maintain market conditions favorable to the flotation of the largest feasible quantity of long-term obligations" (p. 142). Does this mean Federal Reserve support of the bond market? If so, why doesn't the Council say so clearly?

The report includes a "separate note by Mr. Clark upon monetary and credit policy." In this note Mr. Clark bitterly condemns the abandonment of the Federal Reserve tie with the Treasury. He argues that the higher interest rates resulted in greater profits for banks and higher interest costs for the Government. He concludes that "if these miscarriages were the unavoidable results of a monetary policy which is a successful instrument to stabilize the economy, they might be accepted. I do not believe that monetary policy can be successfully used for that purpose in the kind of economy and institutions which we now have" (p. 143).

This is a strange conclusion. Most economists agree that inflation is fundamentally a monetary problem, but Mr. Clark argues that monetary measures cannot help to solve it.

All this is especially disturbing in view of the threat to the independence of the Federal Reserve involved in the projected activities of the Patman subcommittee.

The status of Mr. Clark's separate note is puzzling. Do the other two Council members agree with it? If so why does it appear as a separate note under one name? If the other two Council members do not agree with it why don't they say so and give their own views?

One can only conclude that there is no disposition on the part of the President or his economic advisers to deal with inflation at the only point where it can successfully be dealt with—at its source in the expansion of the money supply.

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The middle course charted by the President and his advisers is confused, erratic, and opportunistic. It heads us in the general direction of more big government, more expensive government, and inflation.

NATIONAL FEDERATION OF INDEPENDENT BUSINESS,
Burlingame, Calif., January 31, 1952.

Hon. JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
Senate Office Building, Washington, D. C.

DEAR SENATOR O'MAHONEY: We are happy to comply with your request of January 16, and give you this organization's views on the materials and recommendations contained in the 1952 Economic Report of the President. Of course, you understand that our expressions reflect only the opinion of our members, determined in regular Nation-wide polls which we have conducted over the past year.

At this point, let us note that we are pleased at the progress that has been made in line with our recommendations of February 1, 1951, to your committee. The Small Defense Plants Administration has been established. Steps have been taken to close the loopholes through which cooperatives have escaped a fair share of taxation. The excess-profits tax on new and growing independent businesses has been eased. Greater representation has been given small, independent business on boards and committees of defense agencies. And the antitrust agencies have been permitted to do some significant work on behalf of free, competitive enterprise.

But, pleased as we are with this progress, we are still very much concerned over the outlook for 1952. And much of our concern springs from certain recommendations and materials in the President's 1952 Economic Report.

First, there is a request for higher taxes. Our members feel that taxes on independent, small-business, and professional people have, for all practical purposes, reached the point of diminishing returns. Their report to us indicate that present rates are cutting dangerously into what are actually shrinking profits and incomes, and that by so doing they are both endangering and discouraging independent, competitive enterprise. These reports also indicate that there is great resentment that the Congress has not gone further to equalize the tax burdens between individually-owned and corporate-form enterprise on the one hand, and cooperative enterprise on the other.

On the subject of the impact of taxes, we could cite the cases of:

The federation members engaged as partners in the depressed television business. During the past 9 months they have made very little profit, have seen their original capital investment shrink from $25,000 to $12,500.

The federation members in the stationery and office-supply field who have seen their unit volume hold up, their gross sales climb, but their yearly profits shrink by two-thirds from 1947 to 1951.

The federation members in the aluminum and steel jobbing business, whose once flourishing firm is now, through lack of supplies, almost at a standstill, and whose profits are cut to the bone.

The federation member in the venetian blind manufacturing business whose profits have passed almost to the vanishing point.

Not one of these members would claim that increased taxes alone are responsiblt for their discouraging and dangerous outlook. But all do say—and thousands of our members agree with them—that increasingly heavy taxes are eating into their remaining profits at such a rate as to further deprive them of reason for operating as independent, competitive enterprises. In short, it's the story of the straw breaking the camel's back all over again.

However, set as they are against higher taxes, all federation members realize as businessmen that Government must pay the bills it runs up, and that these bills can be paid only in current taxation or ruinous inflation. This being so, they believe that Government must, following the dictates of prudence, bring the expenditures into line with its income.

Federation members believe this can be done by both (*a*) elimination of all unnecessary Federal activities and spending, and (*b*) making more efficient remaining Federal activities and spending. They believe further that if worthwhile economies are to be effected, defense and defense-supporting activities must come in for as great an overhauling as nondefense activities—and perhaps ever greater overhauling.

Let us look at the matter this way: During the coming year the budget calls for expenditures totaling $85 billion. Of this total, some 90 percent—or approximately $76 billion—are for defense and defense-supporting activities. In face of this, revenues will approximate $71 billions. Assuming no rise during 1952, the deficit would amount to about $14 billion. Now, even if all nondefense activities were to be eliminated—and action that would be both irrational and illogical—there would still be a remaining deficit of approximately $6 billion.

In view of the above we make the following recommendations:

That Congress inspect closely, and reduce, recommended appropriations for foreign aid, under whatever heading they may appear. We do not make this recommendation because we are unmindful of the needs of the peoples of foreign lands, nor because we are unmindful of the real threat posed by Communist aggression. We do make it because we feel that in the past this aid has accomplished no lasting good, and that it promises little lasting good in the future. We do make it because we feel that so much of this aid has gone, and is going, down the greedy maws of monopoly business systems and has not been translated into advancement either for defense or for the people themselves.

That Congress inspect closely, and reduce, appropriations for procurement and hiring in both the defense and defense-supporting and nondefense fields. We make this recommendation because we are convinced that such economies—which might total as much as $5 billion in the defense and defense-supporting fields alone—can be achieved without dangerous interference with either defense or nondefense activities.

That Congress inspect closely, and eliminate, all duplications in Government effort, and that it eliminate all programs in the defense, defense-supporting, and nondefense categories which are, under present circumstances, needless. We make this recommendation because we believe that money is now being spent where there is no need. For instance, there seems little need for maintenance of the defense program small-business activities by the Department of Commerce in face of the existence and activities of the Small Defense Plants Administration.

That Congress inspect closely, and eliminate, tax favors to giant business where the existence of small business facilities make these favors needless. Reports of both the House and Senate Small Business Committees have told of instances where contracts for defense production have been given to giant enterprise, wherein giant enterprise has had to retool or build, while small-business facilities capable of fulfilling all or a part of such contracts have been allowed to lie idle.

That Congress inspect closely, and eliminate wherever practicable, subsidies which are given to any and all segments of the economy. For instance, it is indeed difficult to understand the farm price support program which keeps consumer costs high at a time when all national effort is directed toward the reverse—especially when farm income is very comfortable. It is equally difficult to understand the subsidies which are paid to public carriers, when their incomes are good and assured by continuing defense activities.

That Congress increase Government revenues by further action to close the loopholes through which cooperatives continue to escape taxation.

Our members believe that by such action, Congress will be able to wring the water out of Government spending to the point, and increase income to the point, that the budget will be in balance with revenues without the need for additional taxes on independent, small-business and professional men.

Second, there is a request for strengthening controls connected with the defense and defense-supporting programs. Particularly there is a request for stiffening of price-control powers. Our members are unalterably opposed to such action on two grounds: (*a*) because they feel that, to a great degree, the control program has been made superfluous by economic developments themselves, and (*b*) because they feel that the only use to which such controls will be put is a use that can only, by its very nature, discriminate against independent, small business.

Visit, if you will, any automobile dealer, any grocer, any appliance dealer, or any other of the whole host of businessmen who comprise the independent, small segment of the retail and wholesale trades, and ask them just what price controls mean. They will tell you that their prices are below ceiling prices, that because of this their profits are not favorable, and that the only thing accomplished by the controls is to pile costly and time-consuming paper work on their operations. They will also tell you of the fear that, in an apparent effort to justify its continued operation, the price control agency seems bent on freezing ceilings at present profitless levels, a move which would prevent realization of normal profits should conditions improve in the future.

Visit, if you will, any small, independent manufacturer, either in the oversupply or short-supply fields, and ask him what price control means. He will tell you that any grant by Congress to price controllers of the power to force absorption of increased costs could be used only to cut into his already slimmed profits. He will also tell you that use of such power would amount, in many cases, to nothing more than control agency-sponsored contradiction. For, in most cases, the increases he would be forced to absorb would be increases already approved by Government agencies.

Both retailers and wholesalers would tell you that if price controls are extended they need the protections afforded by the Herlong amendment, guaranteeing them the same percentage mark-up on cost as they enjoyed in the not-too-profitable period before Korea. Manufacturers would tell you they need the protections afforded by the Capehart amendment, which protect them against enforced cost absorptions. And both would tell you that from their reasoned point of view there is little or no need for continued price controls over their activities.

While on the matter of the general control program, we would mention complaints which have been received from members constantly on both distribution of defense contracts and allocations of materials in short supply. These complaints support our conclusion that by and large small, independent business is not securing a fair share of defense contracts and that small firms denied these contracts are not securing near enough materials to continue normal production. This condition, in our estimation, does not contribute either to the national security in time of all-out war or to the expansion of production sought by the President. It demonstrates, again in our opinion, the practical bankruptcy of effort taken to date on small business problems by the Department of Commerce and other defense agencies. By the same token it affirms the President's request for stronger congressional support of the new Small Defense Plants Administration, which is only now beginning to swing into stride. And by the same token it highlights the pressing need for maintenance of the Small Busines Committees of both the House and the Senate as watchdogs of the Federal small business effort, as the overseers on action on small-business problems in general. It is as true as it is obvious that the security small business has achieved to date would not have been achieved had it not been for the constant vigilance of these congressional agencies. And if we were to make recommendations as to these committees our recommendations would be only as follows:

That Congress establish the House Small Business Committee on the same permanent basis as the Senate Small Business Committee.

And that Congress elevate both permanent committees to the status of full permanent committees, with the power to consider and pass judgment on legislation designed to aid small business.

Finally, we repeat our recommendations of last year on antitrust enforcement. We believe, with the President, that our country must remain strong and become stronger. We believe, however, that our country can be no stronger than its small business system, which is the practical expression of our free, competitive enterprise system at work, and which has helped so tremendously to make us the storehouse of advancement which we are today. We believe further that full, effective antitrust enforcement is one of the most certain safeguards for our free, competitive enterprise system. Unless such enforcement takes place, and to the full extent of its capabilities, we are doomed to monopoly domination, and to eventual Government dictatorship. Unless such enforcement takes place, the vast productive powers of this Nation will never be really freed to serve the needs of consumers, and at reasonable prices and on reasonable terms. Unless such enforcement takes place, we will have lost that which is the soul of the American dream—equal rights for all before the law.

We repeat these recommendations in these terms because, in the past month, disturbing reports have been heard. The first that the appropriations for one antitrust agency have been cut below the year past, resulting in a further hamstringing of its potential to enforce the law to protect the rights of competitive, independent enterprise. The second that pressures have been applied in a quarter where they should be least expected to tone down investigations into the reasons why antitrust enforcement has not been more effective over the past years. The third because the continued effective existence of one agency, which has been a champion of fair antitrust enforcement in the past, has been threatened—largely because, we believe, its advocacy of antitrust and antimonopoly action. We fear these are but straws which show which way the wind in Government is blowing. And if our fear is justified, we want to make the fact known plainly, just as we want it known plainly that we question the lack of specific mention in the report of the necessity for antitrust enforcement.

We believe that the only alternative to this antitrust enforcement is a system of endless Government subsidy and finally, complete Government domination. We are more than pleased at the success of the Federal Trade Commission, in this direction, through affirmative action on the so-called tire maximum discount case. We hope this action will survive all tests. But at the same time, we feel that grave dangers exist in the absence of a really effective national fair trade law. We hope the Congress, in its wisdom, will see fit this year to revive this law.

In this connection, we call your attention again to the fact that our vice president, George J. Burger, a member of the Business Advisory Committee to the President's Council of Economic Advisers, has repeatedly stressed our observations in Business Advisory Committee meetings.

We thank you for this opportunity to present our viewpoint to your committee, as we are thankful for the opportunity of working constantly with the President's Council of Economic Advisers. We assure you of our continued cooperation in any and all of your committee's important endeavors.

Sincerely yours,

C. WILSON HARDER, *President.*

NATIONAL TOOL AND DIE MANUFACTURERS ASSOCIATION,
Cleveland 13, Ohio, February 7, 1952.

Senator JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
Congress of the United States, Washington 25, D. C.

MY DEAR MR. CHAIRMAN: In commenting upon the Economic Report of the President as transmitted to the Congress on January 16, 1952, we do not feel that it is within our province to include foreign relations, and therefore will confine ourselves to domestic policies.

Manufacturers of special tooling were greatly pleased to note the President's recommendations for economy but feel that it would have been very appropriate for him to insist upon the elimination of nonessential Government services and activities especially in the regular Government departments and independent agencies.

The lack of any genuine interest in curtailing Government expenditures is a matter of great concern to these small-business men as the ever increasing tax load threatens to make it impossible for them to plow back into their businesses any considerable sums to purchase the new equipment and buildings which are so vitally needed if they are to meet the soaring demands from defense contractors for special tooling, without which mass production cannot even start.

We were pleased to note the President's realization that shortages now exist in certain categories of skill. This applies especially in the case of the tool and die makers, die sinkers, tool room machinists, and tool and die designers, without whom stamping and forging dies, jigs, fixtures, special gages, special cutting tools, and especially designed machines cannot be made. And without this special tooling, machine tools, presses and forging hammers will stand idle.

We trust that this realization of the shortage will be reflected in appropriate action by Selective Service to keep these journeymen in the shop until the urgent need for special tooling will allow their release for service with the Armed Forces, and that the proposed policy to allow apprentices in these trades to complete their course of training will be made effective as soon as possible.

Tool and die manufacturers cannot agree with the President's statement that our "basic labor-management statute hampers the maintenance of the sound and healthy labor relations and the uninterrupted production which are so essential to a sustained mobilization effort." They strongly believe that with suitable amendments—such as have already been offered—this statute will continue to contribute greatly to the maintenance of equitable labor relations.

Those in the special tool and die industry see few signs of the firm wage policies which the President stated to be necessary. Nor do they see signs that the "equality of sacrifice" which the President calls for is meant to apply to members of the labor unions. Neither can tool and die manufacturers agree that another favored group—the farmers—should now be further favored by direct payments. On the contrary, we feel that equity demands the establishment of a reasonable basis for the taxation of cooperatives which are in competition with private enterprise to require them to bear a fair share of the tax load.

In sharp contrast, when the President turns to business, he demands absorption of cost increases—ignoring the equities of the situation; the fact that any considerable cost absorption will take away the only source of funds available to many businesses for the expansion in productive capacity which he calls for; and the further fact that the great part of cost absorption will be represented by a heavy decrease in the high income and excess profits taxes and renegotiation refunds paid by business.

While the Capehart amendment to the Defense Production Act may not mean a great deal to tool and die manufacturers, they feel strongly that it should be retained in any extension of the Defense Production Act as it symbolizes some regard for fairness in establishing price stabilization policies and regulations.

In keeping with the large increases in wage and salary levels of the last few years, we agree with the President's recommendation that the taxable wage base for the old-age and survivors insurance should be raised. The difficulties confronting small businesses when they consider installing private pension plans are tremendous and in many cases appear insurmountable. This is particularly true in the case of an industry like the special tooling industry which is subject to unusually large cyclical swings in business. But we do not approve other proposed revisions of the old-age and survivors insurance program, nor the establishment of Nation-wide minimum levels for amounts and duration of unemployment benefits.

Tool and die manufacturers—who, for the most part started as journeymen working at the bench—through the creation of their own businesses, exemplify the best in our American system of free enterprise.

These manufacturers were pleased to note the President's urgent recommendation that Congress make available funds for the effective operation of the Small Defense Plants Administration. While the shops that make special tooling are at present so deluged with orders that except in rare cases they have no need for assistance in obtaining business, there are other fields—such as obtaining vitally needed machine tools and financing—in which the help of an agency created to see that small businesses are treated fairly may be of great value.

And it is certainly to the best interests of the American people that other small businesses less fortunately situated as regards orders may be utilized in the defense effort and kept vigorous both for taking part in an all-out productive effort if that should become necessary and for reestablishing our full civilian production when that again becomes possible.

Respectfully submitted.

George S. Eaton,
Executive Secretary.

Statement of S. Abbot Smith to the Joint Committee on the Economic Report on the Economic Report of the President, February 6, 1952

My name is S. Abbot Smith. I am president of Thomas Strahan Co., a small company manufacturing fine wallpapers in Chelsea, Mass., a director of the Smaller Business Association of New England and chairman of its legislative committee.

We small-business men are one with all the people of the United States in the quest of peace. As the President says, "We all know that we must stand firm against aggression, build up our defenses, cooperate with other free peoples, and hold the door open for the fair settlement of international disputes." But we and all the people want a foreign policy which is more specific, one which we can recognize and stand behind wholeheartedly. The people want to know and must be made to understand the urgent needs of the defense program so that when the husband and wife want a new car, they'll understand they cannot have it because the materials are needed for arms for Korea, that Junior cannot have a new bicycle because the metal is needed for planes. We recognize the truth of the President's statement, "The nub of the problem is to maintain a mutual security program which in total is adequate to the danger confronting us." But just how big is that danger? What is "adequate"? We'll meet it, make whatever sacrifices may be necessary if only we know or are told. We are Americans, first, last, and all the time, ready to defend our country and our way of life at all cost.

Referring to the President's recommendations, we believe that the Defense Production Act must of course be renewed. Its powers are essential under present conditions, the output of basic materials must be expanded to meet the needs of our defense program and our restricted civilian requirements, but already many people are worrying about what will be done with the flood of goods when the armament program tapers off and can no longer soak up these enormous supplies, when there is no great accumulated backlog of shortages as there was after World War II. We believe thought should be given to that problem.

It seems to us that the present provisions in the act regarding the controlling of prices and credit are workable and should be continued as is. However, we do believe that it would be advisable to restore to the Federal Reserve Board full administrative discretion with regard to credit controls over durable consumers' goods and housing.

We believe that military and economic aid should be continued to the free nations as an essential part of our defense program, but we also believe that they, too, should do their part within their capacity. They should also indicate by their actions that they intend to play along with us. For instance, we have the greatest sympathy for India and her troubles but the statements and actions of her officials have antagonized many people in this country and have made them wonder why she should think she is entitled to this aid if she is not willing to cooperate with us to whatever extent she can.

We also want to point out our belief that all such spending abroad should be thoroughly screened to be sure that every dollar is spent effectively producing the maximum amount of military or economic aid rather than being frittered away nonproductively.

We vigorously support the President's recommendation that adequate funds be provided for the Small Defense Plants Administration, so it can properly carry out the instructions of the Congress. This is another example of "too little, too late." The amendment creating SDPA should have been passed sooner, funds should have been provided at once to set up the kind of organization necessary to do the job assigned to it. It wasn't; they weren't. Now SDPA must try to make up for lost time to protect and aid the small concerns still left, and to bring as many as possible within the defense program so as to broaden the base of potential production in case of all-out war.

We do not believe the St. Lawrence seaway should be started now, as we think the money, men, materials, engineers, etc., it would require will be far more valuable to the country if used in the present defense program than if sunk in this project which would not be completed or of any use or value for years. Our thinking may be somewhat biased by our geographical location but it is backed by many sound arguments you have already heard. If, however, such men, money, materials, etc., can be spared from the direct defense effort, then we believe it would be more advantageous to channel them into building a steel mill in New England. This would not only produce for the defense effort now but would be advantageous to New England for years to come.

Some additional housing is undoubtedly needed in some defense areas but we believe such new housing, especially if Government funds or credit are used, should be kept to an absolute minimum, both to conserve materials and labor and also for reasons of equity. It seems a little rough to so control rents and materials as well as credit that the landlord who would ordinarily build such a house no longer finds it desirable to do so, yet he is taxed to provide the money for such housing built through other channels. Also, it should be remembered that much of the housing deferred now will help provide a backlog of orders for labor and materials later when the defense works tapers off. And, finally, the peak of demand for housing in defense areas may be passed before all the projected housing is completed.

In our opinion, the Taft-Hartley Act was a step in the right direction toward bringing the rights of management and labor more into balance from the excessive unbalance created by the old Wagner Act. It seems to be functioning pretty well, so we suggest it be continued as is, with revisions to be made from time to time as and if proved necessary.

It seems to us it would be better to leave the farm-price program alone rather than weight it still more heavily in the farmer's favor. It is our feeling that most farmers want to be protected against catastrophe but are not anxious to profit at the expense of other segments of the economy, nor do they want to increase the inflationary pressures.

As regards cooperatives, we still see no reason why they should not pay the same taxes paid by individual businessmen or companies with whom they compete. However, we can agree with the recommendation that all new businesses should be subject to much lower taxes for a limited number of years to give them a chance to get started. In fact we favor a small exemption of profits from Federal income tax so long as the money is retained in the business. This will be explained more fully a little later.

We are strongly opposed to any increase in taxes at this time. We should like to see as near a balanced budget as possible, but want to see it brought about by a reduction of expenditures.

We believe the military should be given every dollar needed for a completely adequate armament program. However, we believe that program should be thoroughly studied, first to coordinate it with our foreign policy, i. e., to be sure it is just what is needed to carry it out, no more, no less; second, to provide proper defense at home; third to be certain it is balanced within the Defense Department itself as between the services; fourth, that all weapons and components are properly scheduled so that all parts will be kept in balance—for instance the right number of engines for each airframe and vice versa, etc.; that every part of each item is properly designed and engineered to perform its function; and, finally, to be sure that the projected program is feasible if carried out to its ultimate conclusion. Are there engineers, materials, and facilities enough in the United States to produce all of what is wanted, and are there supporting facilities enough to maintain and operate all the various items after they have been produced?

We sometimes wonder if State tells Defense just what they expect Defense to do. If Defense doesn't know what State is planning, how can Defense plan as to what kind of arms are needed when or where?

Parenthetically, it is quite possible in our opinion that a relatively small amount of money spent on psychological warfare, such as the Voice of America, aiding our friends in satellite countries, etc., may actually be worth more than several times that amount spent on armaments, millions versus billions).

There seems to be increasing evidence of serious waste within the services. For instance, our manufacturing friends tell us that if the service would tell them what they want a gadget to do, they could often design one which would do the job but which would be easier to make, cost less, and use less critical material than the gadget which the service engineers developed. The latter is frequently not properly designed for mass production, calls for better materials than actually needed, and may be more precise than it actually requires, frequently so complicated they are difficult if not impossible to service in the field, etc.

The new move to make officers cost conscious is highly commendable and will undoubtedly result in very marked reductions in expenditures all along the line. Cataloging items the same for all three services when finished will result in big savings. Closer control of inventories, spares, etc., much closer screening of requirements starting at the very bottom and following through all the way to the top, all will help. In other words, all the business principles for efficient administration, all the business techniques for cutting costs must be applied throughout the services. Every advantage must be taken of business know-how. If private business can do something better and cheaper, that job should be given to private business unless there are very compelling reasons to the contrary.

The President says 85 percent of the budget goes to our security program, so that is obviously the place to make the big savings. Nevertheless, substantial savings can also be made, we believe, by putting into effect the remaining recommendations of the Hoover Commission.

With regard to the Federal Reserve Board, we believe it should have complete freedom to exercise its existing powers, but we are not prepared at this time to make further recommendations.

The social, health, and educational programs outlined are all doubtless excellent, but at this time when every effort is being devoted to the defense program, these expenditures would seem to come under the head of "unnecessary outlays" and "nonessential spending," which should be avoided and cut.

Referring to the President's recommendation as to savings, especially investment in Government bonds as one important weapon against inflation as well as providing needed funds for the Government, we are in hearty agreement. However, we feel strongly that if the Treasury really wants to sell savings bonds to the people, those bonds must be made more attractive. Our savings banks are offering 2¾ percent interest on deposits. The money is available at any time. The E bonds just can't compete unless they are "sweetened" to make them more attractive.

In closing, we should like to make several suggestions which would be of especial benefit to small businesses, though they would also help businesses.

First, we recommend the exemption from Federal income taxes of the first $25,000 of corporate profits each year so long as the money is retained in the business.

Second, we recommend that when drafting control regulations careful consideration always be given to their impact on the smaller units of business. Larger businesses usually have larger inventories, more diversified products, and stronger finances. The small concerns may be dependent on one product. They buy and sell on a hand-to-mouth basis and cannot wait weeks for approvals from agencies in Washington, whether it be materials, prices, or what have you.

I thank you gentlemen for the opportunity to present this statement to you and know that you will give the welfare of the millions of small businesses in this country the full and careful consideration it merits because of their importance in maintaining a strong productive economy.

NEW COUNCIL OF AMERICAN BUSINESS, INC.,
New York, N. Y., February 5, 1952.

Senator JOSEPH C. O'MAHONEY,
Joint Committee on the Economic Report,
United States Senate, Washington, D. C.

DEAR SENATOR O'MAHONEY: We appreciate the opportunity afforded us by the Joint Committee on the Economic Report to present our comments on the President's Economic Report. We assume that your invitation extends also to the report by the Council of Economic Advisers.

It is understood that any evaluation of current economic policy must be focused on the nature of the defense mobilization program and its impact. As we see it, there are four general categories of policy which should be taken into account in any such evaluation:

1. The organization of production and shift of productive resources needed to get the military output and construction asked for by the military authorities.
2. Protection of the health and productivity of the population. (Any shift in production resources or other impact of the mobilization program which endangers the health and efficiency of the population may defeat the ultimate ends desired by the defense activity.)
3. Equitable distribution of the burdens and benefits of the defense program among the various groups in the population and the different sections of the country.
4. Effect of the defense program (and the way it is handled) on the future prosperity of the Nation.

Since we cannot on this occasion take up all four of the above points at equal length, we feel we should confine our comments to the last point. An evaluation of this question is essential to the development of sound policies on the other three points listed above, and we feel that the problem of future economic stability requires a greater amount of thinking through than is generally given to it. In discussing this question, the report states:

"Adjustments, of course, will have to be made. We cannot expect all economic activities to continue at all times on an equally high level. *However, recent experience illustrates the capacity of our economic system for flexible adjustment to a decline in defense outlays.* Although World War II was unfortunately succeeded by the cold war, the annual level of public outlays was reduced by more than $60 billion between 1944 and 1947, and sustained at this lower level until well into 1950. With only minor faltering, these years evidenced new high levels of peacetime production and employment. A rising standard of living absorbed quite fully our expanded productive facilities in factory and field" (p. 150). [Our italics.]

This seems to imply that since we had prosperity during the post-World War II decline in military expenditures, we can expect the same thing to happen again. It is quite true that a rising standard of living absorbed our expanded productive facilities in the postwar years. One of the chief reasons for this was the substantial lift given to consumer income during the war years. Thus, disposable personal income (consumer income after taxes)—in constant prices—increased by over 24 percent in the 3 years between 1941 and 1944. The maintenance of this high level of income together with the availability of huge savings accumulated during the war years and the rise in consumer credit provided the markets for the large volume of goods and services turned out in recent years.

But we are impressed with the fact that the situation today is quite different. The purchasing power of the 1951 disposable personal income was only 9 percent higher than in 1944—an increase which was less than the growth of the population in the intervening years. Thus, the 1951 per capita disposable income—in constant dollars—was slightly below that of 1944. Where then will the markets for the products of the now rapidly expanding industrial capacity come from?

It hardly seems likely that accumulated consumer savings will play a decisive role in future markets. During the four war years consumers set aside almost $120 billion in savings. In the six following years, from 1946 to 1951, consumer savings totaled $62 billion. However, in terms of 1951 prices this 6-year accumulation has a purchasing power that is only one-third of the previous $120 billion. From that lower accumulated savings we do not see how it would be possible to sustain markets during the next decline in military spending in the same way as it did right after World War II. Nor should we expect a significant change in the savings picture as long as taxes keep going up and consumer income is slow to rise.

Experience during the last 6 months seems to shed some light on what may be expected in the future. A decline of over 40 percent in output of consumer durable goods from former peak production has occurred without resulting shortages of these goods at retailers' outlets, which may indicate that capacity in such lines are already far beyond present domestic market demand.

It would seem, in the absence of further investigation, that the market—as presently constituted—will no longer absorb the full capacity of consumer durable goods industries as it did right after the war when capacity was gradually being built up. Some may say that the major decline in output without concurrent shortages at retail levels came about because of the intensive effort by manufacturers to get out as much production as possible after Korea in anticipation of future raw materials shortages. Even if this were the case it still does not contradict—rather, it supports—the conclusion that already the public is lacking the means to purchase what we have the capacity to produce.

Undoubtedly, the accumulated unsatisfied demand for consumer durables played a key role in the postwar prosperity period. But as this abnormal demand was gradually satisfied, the so-called normal demand in the future may be insufficient to purchase everything the consumer goods manufacturing plants can turn out with the available equipment. This shift in consumer demand from the war-induced abnormal to the normal may be at the root of the high savings rate discussed in the annual report; the high rate of personal savings in recent months is hardly a reflection of consumer idiosyncrasies.

The major part of personal savings is accounted for by the high-income families. These are the same families that buy the luxuries and most of the consumer durables. If it is true that their primary demands for consumer durables (and housing) has been met and that they are in the market right now mostly to replace equipment, then it is natural that the savings rate should show some rise. Another factor in the higher savings rate figures is the decline in consumer borrowing.

Yet, despite the fact that (*a*) purchasing power is not keeping pace with population and productivity growth, and (*b*) there are signs of serious weakness in crucial consumer markets, we are currently witnessing a major boom in the expansion of industrial capacity—stimulated by the permission to accelerate amortization. While a substantial part of this expansion is directly tied to defense mobilization, a significant amount of this expansion will need the support of consumer markets after the present emergency is over.

As we see the situation, the expansion phase of the present boom in industrial capacity will soon be completed and will be followed by a period of declining business investment. Furthermore, the chances are that this forthcoming decline in business spending will coincide with the projected reduction in defense spending. This along with insufficient consumption may very well contribute to a serious business decline, assuming inadequate counteracting steps are meanwhile taken.

We do not pretend to know all the answers to these questions. But we are very concerned about what such an economic decline would mean for the business community and for the economy as a whole. We therefore urge that your committee look into the problem at greater length and initiate and encourage the investigations leading to the development of sound policies.

We believe that doing so will require recognizing the fact that the situation today and of the period ahead cannot safely be equated with the experiences following World War II, when accumulated savings were so much more important and when—in contrast with today's picture—real income kept pace, or even outdistanced, the rise in production and productivity. If we recognize the key differences between the two periods, and want to do something about it, we will have to also reevaluate our materials allocation, taxation, and stabilization policies from the point of view of preventing future major economic dislocations.

Sincerely yours,

MILES PENNYBACKER, *President.*

McGRAW-HILL PUBLISHING CO., INC.,
New York, N. Y., February 6, 1952.

Hon. JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
Congress of the United States, Washington, D. C.

DEAR SENATOR O'MAHONEY: I have delayed in acknowledging your letter of January 21 in the hope that I might, in acknowledging, avail myself of the opportunity extended. Unhappily, however, my commitments have been such that I have not been able to prepare comments on the materials and recommendations contained in the 1952 Economic Report of the President.

Nonetheless, I appreciate the opportunity and regard it as a salubrious manifestation of both the democratic process and constructive cooperation in the field of the social sciences.

Since I am sure it has an important bearing on the work of your committee, I attach a copy of the Business Week (February 2, 1952) report of the results of a survey of business plans for investment in new plant and equipment in the years 1952 through 1955 which has just been completed by my department at McGraw-Hill.

Yours sincerely,

DEXTER M. KEEZER.

BUSINESS WEEK REPORTS TO EXECUTIVES ON INDUSTRY'S EXPANSION PLANS FOR 1952 THROUGH 1955

Two things stand out today from industry's detailed plans for plant and equipment spending:

The year ahead will set a record. Companies plan to lay out more for capital goods, $21.2 billion, than ever before in history.

After 1952, investment will still be big. Although mobilization expansion will have passed its peak, business already plans to spend more than $14 billion in 1955—a level well above pre-Korean years.

These are the major conclusions of the fifth annual survey of investment plans by the McGraw-Hill department of economics.

This year will probably be the highwater mark in what has been the greatest wave of expansion ever in the United States. Industry spending may drop quite a bit in 1953. Right now the only industries whose capital expenditures are rising are those with defense contracts or defense-supporting priorities. By the end of the year their spending, too, will have passed the crest.

No drying up.—But the idea that after mobilization capital investment will dry up, as it did in the 1930's, can now be written off. The increase in capacity during the defense build-up will be tremendous, certainly. For manufacturing companies, it will amount to a jump of 16 percent since the end of 1950 and more than 100 percent since 1939. In the 6 years since 1945 manufacturers have invested $50 billion in new facilities—a total roughly equal to the gross amount they had invested in capital assets at the end of World War II.

	Millions of dollars				
	Actual 1951	Planned 1952	Preliminary plans—		
			1953	1954	1955
Steel	1,310	1,638	1,048	934	901
Machinery	638	636	443	424	414
Electrical machinery	355	809	712	372	299
Autos (including defense)	797	781	406	297	289
Transport equipment	227	404	145	40	40
Food	930	769	710	816	754
Petroleum and coal products	2,040	2,815	2,477	2,111	2,055
Chemicals	1,266	1,464	1,323	1,191	1,179
Textiles	676	396	396	383	394
Other manufacturing	2,902	3,209	2,368	1,957	1,869
All manufacturing	11,141	12,921	10,028	8,525	8,194
Mining	806	943	415	321	358
Railroads	1,564	1,642	1,248	1,117	1,002
Electric and gas utilities	3,676	3,948	3,360	3,204	2,748
Other transportation, communications	1,592	1,721	1,671	1,943	1,839
All industry	18,779	21,175	16,722	15,110	14,141

Source: 1951 figures from U. S. Department of Commerce; Electrical and gas utilities figures from Electrical World, American Gas Association.

After 1952, though, industry will still be spending a vast amount of money on plant and equipment—primarily for replacement and modernization. Preliminary plans right now point to a total of $16.7 billion in capital expenditures in 1953, $15.1 billion in 1954, and $14.1 billion in 1955.

Thus, when you remember that distant-future plans are always less complete, the actual drop in capital spending from 1952 to 1955 may amount to no more than 20 to 25 percent. That would still leave investment within 10 to 15 percent of 1951, and well above pre-Korea years.

Continuing boom.—For this year the survey indicates a continued boom for the capital-goods industries. This survey is not a forecast, but a summary of industry's plans as reported to McGraw-Hill this month. It shows:

Plans for expenditures by all industry in 1952 call for a jump in dollar outlays of 13 percent over last year.

Manufacturing industries will spend $12.9 billion to replace old equipment and build new factories. Expenditures in 1951 were $11.1 billion.

The 13 percent jump that will take capital spending to its record $21.2 billion in 1952 is by no means uniform throughout industry. In electrical manufacturing the increase in spending over 1951 will be more than 100 percent; in transportation and communications it will be a modest 8 percent. Some industries will actually spend less in 1952 than in 1951.

Capacity.—Translated into terms of plant, the capital outlays of the manufacturing industries will add 8.4 percent to capacity. (The rise in 1951 was 7 percent.) The big increases will be in defense and defense-supporting lines; outside of some building materials, capacity won't increase much in nondefense industry.

Expansion.—Defense industries are the big ones in terms of capital spending. So industry—on balance—is still expanding this year. Of the capital investment dollar, 52 percent will go for expansion; 48 percent is ticketed for modernization.

Financing.—Raising capital won't be a big obstacle in 1952. Companies generally have—or can get—enough money to carry through their investment plans. Four out of five intend to finance entirely out of retained earnings, depreciation, and reserves—no outside money.

The big year.—Unquestionably, 1952 is the big year for defense-supporting expansion. It started in 1951. But as Business Week checks revealed (Business Week, July 14, 1951, p. 21), the biggest defense projects got going late, and completion was pushed off into 1952. Department of Commerce figures show spending is running unusually high right now—18 percent more than the first quarter of 1951. However, the McGraw-Hill survey shows expenditures, at least in manufacturing, will be fairly even throughout the year—52 percent in the first half, 48 percent in the second.

This year, despite bottlenecks, industry feels it can get the job done. Few companies in defense-related lines expect materials or equipment shortages to limit their spending. In most cases, construction of new facilities is well along now; much of the tooling is on order.

How product lines will invest in 1952

These industries will spend—	Percent change from 1951		These industries will spend—	Percent change from 1951	
	More in 1952	Less in 1952		More in 1952	Less in 1952
Agricultural machinery	+47		Lumber	+2	
General industrial machinery	+19		Glass	+28	
Metalworking machinery		−17	Cement		−53
Office and store machinery		−16	Baking	No change	
Service industry machinery		−32	Canning		−17
Special industry machinery		−1	Dairy products		−21
Paper		−4	Nonferrous metals (mining and manufacturing)	+62	
Rubber	+44		Oil (total)	+38	
			Production	+13	
			Refining	+118	
			Transportation	+106	
			Marketing	+10	

MINING, MANUFACTURING ARE LEADERS

Within the major industry groupings, the biggest increases in capital spending this year are in mining (17 percent) and manufacturing (16 percent), where defense expansion is heavy. Electric and gas utilities plan a 7 percent increase in spending; transportation and communications see an 8 percent hike. Railroads will spend only 5 percent more.

The utility figure, however, doesn't show a completely true picture. Electric utilities are actually expanding faster than manufacturing; power companies plan a whopping 24 percent increase in investment in 1952. What brings the over-all figure down is a drop in the plans of gas utilities.

Spending by private electric utilities will total $2.6 billion in 1952. If the outlays by public power agencies were added in, the total would be $3.8 billion—the largest single expenditure for capital goods.

Among manufacturing industries, the biggest spending will come from the oil companies. Plans for new producing, refining, transportation, and marketing facilities add up to $2.8 billion—38 percent more than actually spent in 1951.

Longest leap.—The biggest increase in spending—as distinct from the biggest spending—among manufacturers shows up in electrical manufacturing. Plans call for 1952 expenditures that are more than double those of last year.

Transportation equipment, which is dominated by defense-swollen aircraft, shows a 78 percent increase. In steel, spending is up 25 percent, in chemicals, the rise is 16 percent. Autos will keep spending close to last year's high level, as will machinery. Nonferrous metals companies are spending 60 percent more than last year.

Shift in planning.—Over-all, there won't be quite so much concentration on expansion this year as there was in 1951. Last January companies planned to put 58 cents of every investment dollar into expansion, actually wound up investing 53 cents. Now only 52 cents out of the capital spending dollar is earmarked for expansion; the rest will go for modernization.

The reason for the shift in planning this year is this: Late in 1950 and early in 1951 small companies, particularly those in nondefense industries, speeded up their expansion plans to get under the wire ahead of materials shortages. At the time, many of the companies were making record profits; adding new capacity seemed to be a logical decision.

After the controlled materials plan came into operation in the second half of 1951, nondefense industries had a harder time getting materials, both for building and for their products. For many, profits slipped badly. Thus, few of these companies are expanding now. And the fact that they aren't holds down the proportion of expansion in the total manufacturing picture.

For defense.—Expansion in defense industries is tremendous. In the automobile industry—long on arms work—73 percent of all capital expenditures will go for expansion. Chemical companies are spending 78 percent of their investment funds to expand. The transport equipment group, which includes aircraft manufacturing, is investing almost entirely for new capacity.

On the other hand, the food and textile industries are ticketing three-fourths of their 1952 spending for replacement and modernization. Apparel and furniture companies plan to spend almost nothing for expansion.

Capacity.—By the end of this year United States manufacturing industries will have added 8.4 percent to capacity, if they carry through their present plans. Coupled with the new plant brought in in 1951, this will add up to an impressive record, 16 percent, for 2 years of mobilization. In electrical manufacturing, chemicals, and autos, capacity will be up almost one-fourth since the end of 1950. In machinery, the jump will be nearly one-third; in transport equipment, over 50 percent. Steel capacity will be up 12 percent, electric power 20 percent.

In 1952 alone, the planned increases over capacity on December 31, 1951, will be 12 percent for chemicals, 13 percent for machinery, 9 percent for steel, 8 percent for autos, 14 percent for electrical manufacturing, and 33 percent for transport equipment. Electric power capacity is slated to rise 11 percent. Although capacity figures for mining aren't available, there will certainly be a big rise. Expenditures by coal and nonferrous metals companies are up sharply. Petroleum, too, will show gains since most of its planned spending is for developing new wells.

Nondefense cuts.—Outside of defense industries, however, you can't expect much of an increase in capacity. Capital spending, generally, will be down from last year. Food companies will spend 17 percent less this year than in 1951; textile manufacturers plan a drop of 41 percent. There also will be big cuts by apparel, furniture, and some small machinery makers. Materials troubles are very definitely a factor here; machinery, food, and some chemical companies say they would spend substantially more in 1952 if they could get their hands on the needed supplies and equipment.

Spending for new capacity will be lower in the gas utilities and communications industries, too. The shortage of materials hurts badly here. Gas pipelines are being postponed for lack of steel plate and pipe. Telephone construction is held up by shortages of copper wire and other key materials. Railroads have the same trouble. With plates and structurals short, they can't see any big increase in freight car deliveries this year.

What companies are spending for

	Expansion versus modernization			
	1951	1952	1951	1952
	Percent	*Percent*	*Percent*	*Percent*
Steel	67	56	33	44
Machinery	56	54	44	46
Electrical machinery	49	67	51	33
Autos	73	73	27	27
Transport equipment	77	90	23	10
Food	41	24	59	76
Chemicals	77	78	23	22
Oil and coal products	32	32	68	68
Textiles	43	24	57	76
Other manufacturing	48	53	52	47
Total	53	52	47	48

Why companies will spend in 1953, 1954, 1955

	Percent of companies saying				
	More capacity for present products	Capacity for new products	Plants to serve new market areas	Replacement and modernization	Other reasons
Steel	38	0	0	88	13
Machinery	39	31	4	87	0
Electrical machinery	57	71	14	100	0
Autos	67	33	33	83	0
Transport equipment	57	43	14	71	0
Food	50	21	17	88	13
Chemicals	60	60	27	47	7
Textiles	16	26	5	89	0
Other Manufacturing	49	38	11	91	0
All manufacturing	48	33	13	83	4

Note.—Totals add to more than 100 percent because some companies gave more than one answer.

How companies plan ahead

	Do you regularly plan capital expenditures several years in advance?		If so, how far ahead do you plan?		
	Percent of companies answering yes	Percent of companies answering no	More than 2 years	More than 4 years	More than 5 years
Steel	88	12	100	80	0
Machinery	41	59	100	64	5
Electric machinery	63	37	100	50	0
Automobiles	71	29	100	16	0
Transportation equipment	43	57	100	33	0
Food	68	32	81	38	6
Chemicals	82	18	93	71	0
Oil, coal products	60	40	67	50	0
Textiles	65	35	100	21	3
Other manufacturing	68	32	92	34	0
All manufacturing	61	39	93	45	2
Mining	62	38	92	50	0
Airlines	100	0	100	40	0
Railroads	57	43	100	67	10

MONEY NO PROBLEM

Financing isn't going to be a big problem for industry in 1952. Most companies have enough cash to carry through their investment plans, or can get it. Four out of five intend to cover their capital spending out of retained earnings and reserves. A good many others have already sold the securities to pay for at least part of their 1952 programs.

In some industries, however, plant expenditures are so big that companies will have to lean more heavily on the money market than they did in the past. This is true of aircraft, petroleum, steel, chemicals, and electrical machinery.

It's normal to expect that aircraft companies would go outside for money—some of it in the form of Government aid. But a year ago oil and electrical machinery companies were financing almost entirely from internal sources. Steel and chemicals companies planned to get more than 90 percent of their 1951 funds from depreciation and retained earnings.

This year 11 percent of electrical machinery companies will borrow or sell new stock to help finance capitl spending. One-fourth of the petroleum companies, one-third of the chemical companies, and almost three-fourths of the steel companies expect to sell new securities to raise part of their funds. Chemicals are the only group relying heavily on equity financing. Other industires will borrow almost all the outside money they need.

Troubles—Small companies are apparently having a harder time in planning capital expenditures than larger companies. The survey, although it concentrates on the larger companies, includes a broad sample of smaller firms in the fields in which they are important—such as metalworking and food. In many cases, the smaller firms indicate the squeeze on profits—and materials shortages—have cut into their plans.

PLANS STAY HIGH FOR YEARS AHEAD

Industry already has plans for substantial capital spending in the years to follow mobilization. Four out of five manufacturing companies that answered the McGraw-Hill survey gave some plans for the years beyond 1952.

They add up to considerably less than the superboom expected this year. But there's already more new plant on the drawing boards for 1955 than was installed in any year but 1948 or 1951. Thus, even when the forced draft of mobilization ends, there's a good chance industry's spending will level out well above pre-Korea.

McGraw-Hill asked businessmen how much they would spend in 1953-55 if business stays reasonably good, and if corporate taxes continue at the present 52 percent rate (but without an excess profits tax). Here's what their plans for the future show:

Capital expenditures will start down in 1953. The big drop will be in defense industries—steel, machinery, autos, and transport equipment. These industries may be producing a lot of defense goods in 1953. But their plant expansion will be largely finished this year. And when it's done, they evidently don't expect to add much new plant for some time.

Carry-over—In some fields, particularly defense-supporting industries, expansion will carry over into 1953. This is especially true of petroleum and chemicals. The petroleum refinery and pipeline program won't hit full stride until late this year; the really big additions to capacity are slated to come in 1953. The same timetable holds true for chemical plants.

Actually, both the oil and chemical industries are expanding on a long-term basis anyway. Their spending is scheduled to hold at a high level right through 1955. In that year they plan to put out just as much money as they did in 1951.

In nondefense lines, the adjustment to lower capital spending will come this year. In both food and textiles, plans for 1952 are down to a normal, or maybe subnormal, level. Neither industry figures on further cut-backs in 1953–55. In fact, if profits pick up—companies have been hard hit by the inventory recession and by price controls—spending stands a fair chance of rising above plans later in 1952 and in the future.

Utilities high—The utility group looks like a sure bet to hold up well. Electric utilities, particularly, plan to continue their present spending pace through 1954. Peak additions to generating capacity will come in 1953. But companies will carry on for another year with high expenditures for transmission and distribution equipment.

Although gas utilities have much less definite plans for the years after 1952, electric and gas companies together plan to spend only 18 percent less in 1955 than they will this year. In telephones—restricted now by materials shortages—the big backlog of demand for phones and other communications services probably means more spending after 1952. Mining companies are making unusual outlays right now to develop new sources of supply. They don't count on this to continue. Planned investment in the field shows more than a 60-percent drop by 1955.

Railroad plans also trail off—down 29 percent from 1952 to 1955. But as in manufacturing, this probably reflects uncertainty about future conditions. If traffic holds up, railroads may spend considerably more.

Airlines are definitely planning on bigger capital expenditures in 1953–55 than they're making now. The reason: the big new fleets of superplanes now in design or on order.

More to come.—Add it all up, and you get industry spending 20 percent less than 1952 in 1953; 33 percent less by 1955. But in practice neither drop is likely to be that sharp. As more plans take form, 1953 could easily come within 10 percent to 15 percent of the 1952 level: 1955 might be off no more than 20 percent to 25 percent. If this holds true, we'll have the foundation for a relatively high level of business, if not the hectic boom of mobilization.

Reasons.—The overwhelming reason for big capital spending in the future is replacement and modernization. The shift from expansion—hardly perceptible for industry as a whole in 1952—will gather momentum as mobilization tapers off.

Eight out of nine companies in steel, machinery, and the auto industries give modernization as a primary reason for their 1953–55 programs. In food, textiles, and other soft goods industries, it's 9 out of 10. Railroads and airlines, too, will concentrate on modernization, although they expect some incidental increase in capacity.

Only the chemical group will still be expanding so fast that new capacity—for both new and present products—will be its primary aim.

New products.—However, this doesn't mean that there won't be a substantial amount of expansion. A majority of companies in the electrical machinery, auto, and transport equipment industries is planning more capacity for present products. And at least one-third of the companies in every line—except steel, food, and textiles—have some plans for new products after mobilization.

A substantial minority of companies also plans factories to serve new market areas. Auto and chemical companies, especially, are in this class. Together, new products and new market areas account for a big part of industry's post-mobilization plans for new plants and equipment.

Taking all three—the modernization, the new products, and the new markets—you can draw a picture of high-level capital spending for a long time to come.

EVERYTHING DEPENDS ON PROFITS

Of course, it's not guaranteed. Plenty of things can happen to knock industry's plans for the future into a cocked hat. Here are the ifs and buts that businessmen stressed in replying to the McGraw-Hill questionnaire:

(1) Everything depends on profits—after taxes. They'll be the source of funds for most capital expenditures. If there's a general business slide, many capital spending projects would be dropped.

Over 40 percent of the companies answering the survey said that it takes longer now for an investment in new equipment to pay off than it did 2 or 3 years ago. Equipment costs are up, and taxes cut into the additional profit you get from more efficient machines. Many companies also say they have exhausted the backlog of obvious, quick-paying improvements that they had right after World War II; they're getting into more marginal projects now that don't pay so quickly. Thus, if profits dropped much, a good many projects might be junked.

(2) There may be financing problems. The industries with the largest spending plans for after 1952—steel, utilities, electrical machinery, chemicals, and petroleum—will rely on the public money market to finance a big chunk of their program. In the chemical industry, 19 percent of the companies covered by the survey plan to borrow; 25 percent expect to sell stock. In petroleum, 17 percent count on borrowing, in steel 29 percent, and in electrical manufacturing 14 percent.

Less financing.—As a group, manufacturers expect to use the money market slightly less in 1953–55 than in 1952. But that's only because some industries are cutting their capital spending and expect to finance the smaller amounts out of retained earnings. However, expansion will still be heavily dependent on outside financing. And this makes plans vulnerable—because it's impossible to predict the markets so far ahead.

Tax limits.—The thing that would boost capital spending most is a cut in taxes. Manufacturers say again and again that the present tax level limits the number of projects that will pay out quickly; often they are reluctant to do any planning far into the future. A tax cut after mobilization would make a lot of projects more attractive. Capital expenditures might hold up even if profits were somewhat lower.

Foresighted.—One of the most significant findings of the McGraw-Hill survey is that most manufacturing companies make it a regular practice to plan capital expenditures several years in advance. The fact that more companies are planning on a long-term basis may dampen the sharp swings in capital investment. More than 60 percent of the companies in most industries, and more than 80 percent in steel and chemicals, use advance planning. So does a majority of companies in mining and transportation. Almost all electric utilities budget ahead.

This advance planning—where it occurs—is generally for 3 to 5 years ahead. However, in steel, machinery, and chemicals, and among the railroads, many companies plan more than 4 years ahead, and many more look beyond 3 years.

How the money will be raised

	1952			1953–55		
	Percent of companies planning to—			Percent of companies planning to—		
	Finance from profits and reserves	Borrow part of funds	Sell stock to raise part of funds	Finance from profits and reserves	Borrow part of funds	Sell stock to raise part of funds
Steel	29	71	-----	71	29	-----
Machinery	78	17	5	87	6	7
Electrical machinery	89	11	-----	86	14	-----
Autos	100	-----	-----	100	-----	-----
Transport equipment	86	14	-----	100	-----	-----
Food	89	11	-----	91	-----	9
Chemicals	67	22	11	56	19	25
Petroleum and coal products	75	25	-----	83	17	-----
Textiles	86	14	-----	93	7	-----
Other manufacturing	83	14	3	84	12	4
All manufacturing	80	17	3	85	9	6

HOW THIS SURVEY WAS MADE

Other companies evidently formulate some advance plans for capital expenditures as a guide to financial planning and the raising of new money. But they do not set a definite schedule for actually making the expenditures. Others that used to plan spending well in advance have stopped. They blame the uncertainties of taxes and controls.

All in all, it adds up to this: Industry now does a great deal more long-range planning than it used to—and much more than most people have suspected. This explains the relatively high level of plans for investment after mobilization. Industry is not just planning for 1952. Companies are laying the groundwork for new products and new markets in the years ahead—simply because they figure this is sound business practice.

Stabilizing.—All this offers new hope for stabilizing capital expenditures without the bust that usually follows the boom. Plans can change, of course. But at least industry has the plans. And this could be something that might change the shape of future business cycles.

The capital expenditures survey made by the McGraw-Hill department of economics is a report on the spending plans of industry for 1952 through 1955. It is solely a report on where and how industry now intends to spend on capital goods.

The companies cooperating in this survey employ more than 60 percent of all workers in industries where capital investment is highest. That includes chemicals, oil, railroads, electrical machinery, autos, utilities, and steel. These industries account for about two-thirds of all spending for capital goods. The companies included are mostly the bigger companies in these industries.

Selective.—In other industries, coverage was not so complete. But the participating companies were carefully picked to make up a representative cross-section.

In all, the samples include companies employing more than 5 million workers. That is about one-quarter of the total employment of all industry.

Physical capacity was measured by figures supplied by the cooperating companies themselves. All companies were asked to select their own measures of physical output.

The figures on capital expenditures in this report are not directly comparable with those given in previous McGraw-Hill reports on capital spending. Instead, survey data for 1952, and succeeding years, have been put on the same basis as the revised series published by the Department of Commerce for 1945–51. Figures on industries' plans are therefore comparable with the Commerce figures for back years. Figures on capacity are comparable with those published in last year's (Business Week, March 31, 1951, p. 67) report.

Capital spending for the electric utility companies was obtained through the cooperation of Electrical World, a McGraw-Hill publication. Figures on gas utilities are from the American Gas Association. Correspondents of Business Week personally interviewed many company executives. Other McGraw-Hill magazines helped in conducting the survey in their own particular fields.

(The material referred to on page 118 is as follows:)

FEBRUARY 19, 1952.

Hon. JOSEPH C. O'MAHONEY,
Chairman, Joint Committee on the Economic Report,
United States Senate, Washington 25, D. C.

MY DEAR MR. CHAIRMAN: Enclosed is a copy of a letter I have written to Senator Byrd and several tabulations regarding budget expenditures which are relatively uncontrollable in any one year. These materials have been prepared pursuant to a request made by Senator Byrd on January 8. They also provide information you requested when I appeared before your committee on January 24.

Sincerely yours,

——— ———, *Director.*

EXECUTIVE OFFICE OF THE PRESIDENT,
BUREAU OF THE BUDGET,
Washington, D. C., February 18, 1952.

Hon. HARRY F. BYRD,
United States Senate, Washington, D. C.

MY DEAR SENATOR BYRD: Pursuant to the request made in your letter of January 8, Bureau staff have prepared a number of tabulations setting forth certain details regarding the estimated 1953 budget expenditures which are relatively uncontrollable in any one year. These tabulations are similar to those prepared for the fiscal year 1952 which were sent to you on May 16, 1951. The kinds of programs classified as relatively uncontrollable and the breakdowns shown were determined last year after consultations between Bureau staff and Mr. Heywood Bell of the staff of the Joint Committee on Reduction of Nonessential Federal Expenditures.

The relationship of the programs analyzed in the attached tabulations to the budget totals is shown in the following table:

	Fiscal year 1953 estimates (in millions)	
	New obligational authority	Expenditures
(1) Budget totals, estimated (see 1953 budget, pp. A5–A6)	$84, 260	$85, 444
(2) Less: Expenditures from obligational authority granted in prior years		41, 867
(3) Military services program (part not included in (2) above)	52, 359	20, 692
(4) International security and foreign relations program (part not included in (2) above)	8, 238	3, 567
(5) Existing programs relatively uncontrollable because of legal or implied commitments (not included in (2), (3), or (4) above)	15, 770	14, 436
(6) Equals: Programs relatively controllable by the Congress for fiscal year 1953 (not included in (3) or (4) above)	7, 893	4, 882

The relatively uncontrollable programs (line (5) above) can be classified as follows:

	Fiscal year 1953 estimates (in millions)		
	New (1953) obligational authority	Expenditures	
		Total	Out of 1953 new obligational authority
(*a*) Interest, contributions to trust funds, payments of claims, and payments required by treaties and international agreements (table 1)	$7,689	$7,738	$7,681
(*b*) Grants-in-aid, shared revenues, and loans and advances to States (table 2)	2,702	2,611	1,911
(*c*) Veterans' Administration (table 3)	4,000	4,011	3,818
(*d*) Programs of Government enterprises which are not subject to annual Congressional control (net) (table 4)	539	36	36
(*e*) Miscellaneous relatively uncontrollable items (table 5)	1,233	1,140	1,033
(*f*) Adjustment for duplicating items in (a) through (e) (table 6)	−393	−43	−43
Total	15,770	15,493	14,436

As in last year's tabulations, the items included in line (*a*) above are listed in table 1 without the statutory references which accompany the items listed in other tables.

Table 2 divides grants-in-aid programs (line (*b*) above) into two major groups: Those which are not subject to annual appropriation control and those which can be legally controlled through the annual appropriation process. It is assumed, however, that even grant programs which are subject to annual appropriation control represent an implied commitment of the Federal Government to the States for continuance of the programs, although not necessarily at the current level. The grant-in-aid programs are further divided to indicate those which require some State matching of Federal funds and those which do not.

Detailed information is supplied in table 3 for all programs of the Veterans' Administration, despite the fact that part of the activities included—such as for hospital and medical care and for administration and other services—can legally be controlled through the annual appropriation process. As in the case of grants-in-aid, these activities are included because their existence seems to represent an implied commitment of the Federal Government to veterans for their continuation, although not necessarily at the current levels, or because they are necessary to administer benefit programs required by law.

Table 4 presents data for programs of Government enterprises. The table lists obligational authority and net expenditures for all such programs except those requiring new legislation proposed by the President and those involving less than $500,000 in net expenditures or receipts. From these totals, deductions have been made for (1) expenditures from prior-year authorizations and operating receipts (already included in line (2) of the table on the first page of this letter); and (2) expenditures from relatively controllable new authorizations requested for 1953. The remaining total represents net expenditures by Government enterprises from relatively uncontrollable new authority.

In table 5 there are listed a number of miscellaneous programs not included in tables 1 to 4 which also may not be effectively controlled in the fiscal year 1953 by the Congress.

Sincerely yours,

F. J. LAWTON, *Director.*

TABLE 1.—*Interest, contributions to trust funds, payment of claims, and payments required by treaties and international agreements, under existing legislation*

Agency, program, or appropriation	1953 budget estimates (in millions)			Comments
	New obligational authority	Expenditures		
		Total	Out of 1953 new obligational authority	
INTEREST				
Treasury Department:				
Interest on the public debt	$6,150	$6,150	$6,150	Expenditures depend on total debt and on interest rate policy.
Interest on refunds	101	101	101	Interest rate is set by statute at 6 percent, the same rate as for tax deficiencies.
Interest on uninvested trust funds.	5	5	5	Interest rates for most of these funds are fixed by law.
CONTRIBUTIONS TO TRUST FUNDS AND OTHER RETIREMENT PAYMENTS [1]				
Civil Service Commission:				
Payment to civil service retirement and disability fund.	458	458	458	The Government payment for civil-service employees is based on an estimated covered employment of 1,700,000. It is equal to 2.78 percent of covered payrolls plus interest on the accrued liability and an amount to amortize the accrued liability over the next 30 years.
Annuities under special acts.	3	3	2	Annuities are paid to persons employed on construction of the Panama Canal or to their widows and to widows of former employees of the Lighthouse Service.
Railroad Retirement Board:				
Payment to railroad retirement account.	690	690	690	The annual appropriation is based on estimated tax collections from railroad employees and employers. This appropriation is on an indefinite basis, and payments are made each month equal to the taxes collected.
Payment to railroad retirement account on account of military service credits.	33	33	33	Permanent definite appropriation required by Public Law 141, 81st Cong.
Department of Labor: Employees' compensation fund.	35	33	33	Benefit payments are made to civil employees of the United States disabled from injuries sustained on the job. The appropriation is on an indefinite basis.
Treasury Department: Coast Guard, retired pay.	18	18	18	Payments to retired personnel of the Coast Guard.
PAYMENTS OF CLAIMS				
Department of Commerce: Claims, Federal Airport Act	--------	1	---------	
Treasury Department: Payment of certified claims	--------	50	---------	
PAYMENTS REQUIRED BY TREATIES AND INTERNATIONAL AGREEMENTS [2]				
Department of Agriculture: International Wheat Agreement.	$182	182	182	Reimbursement to Commodity Credit Corporation for 1951 costs of International Wheat Agreement.
Department of State: International Boundary and Water Commission, construction.	14	14	9	
Total	7,689	7,738	7,681	

[1] Excludes payment to Foreign Service retirement and disability fund, classified under "International security and foreign relations."

[2] Excludes contributions to international organizations, classified under "International security and foreign relations."

TABLE 2.—*Grants-in-aid, shared revenues, and loans and advances to States, under existing legislation*

Appropriation and program	1953 budget estimates (in millions)			Statutes establishing program	Comments
	New obligational authority	Expenditures			
		Total	Out of 1953 new obligational authority		
EXISTING GRANT PROGRAMS RELATIVELY UNCONTROLLABLE THROUGH ANNUAL APPROPRIATION PROCESS					
Programs requiring some State matching of Federal funds:					
Federal Security Agency:					
Public assistance	$1,140	$1,140	$1,140	42 U. S. C. 301–6, 601–6, 1201–6	The Federal Government reimburses the States according to a statutory formula for a share of the public assistance payments made. The expenditure estimates are based on case-load forecasts.
Vocational education	7	7	7	20 U. S. C. 11–14	Permanent indefinite appropriation for training in agriculture, home economics, trades, and industry.
Housing and Home Finance Agency:					
U. S. Housing Act program: Annual contributions (also listed in table 4, p. 6).	36	36	36	42 U. S. C. 1401–22, 1427–31, 1433	Annual Federal contributions pursuant to contracts made with local public agencies are made to cover operating deficits of housing projects developed under the U. S. Housing Act of 1937, as amended. State-local financial participation takes the form of tax exemptions for the housing projects.
Slum clearance and urban redevelopment (also listed in table 4, p. 4).	100			42 U. S. C. 1451	The Housing Act of 1949 provides permanent contract authorizations of $100,000,000 a year for 5 years. The program is still largely in the planning and land-acquisition stage and no expenditures for grants are anticipated in 1953.
Department of Agriculture: Cooperative agricultural extension work.	5	5	5	7 U. S. C. 341–348, 386b–f	This permanent definite appropriation is distributed on the basis of rural population.
Department of Commerce: Federal-aid postwar highway construction.[1]		388		23 U. S. C. 1–22, 41–114	Proposed extension of Federal-aid Highway Act would provide $400 million of new authority for 1953; expenditures in 1953 will be from prior year obligational authority.
Programs not requiring State matching of Federal funds:					
Veterans' Administration: Aid to State homes (also listed in table 3, p. 5).[2]	4	4	3	24 U. S. C. 134	Federal expenditure is based on estimate of case load and on a statutory payment not to exceed one-half the cost for each inmate.

Federal Security Agency: Colleges for agriculture and the mechanic arts.	3	3	3	7 U. S. C. 301-308, 321-328	This permanent definite appropriation provides $50,000 for each State and Territory.
Department of Agriculture:					
Removal of surplus agricultural commodities.[3]	40	30	24	7 U. S. C. 612	Perishable commodities acquired through price support activities are distributed to schools, institutions, and welfare agencies.
Commodity Credit Corporation: Donation of commodities (also listed in table 4, p. 8).[3]	5	5		7 U. S. C. 1431	
EXISTING GRANT PROGRAMS REPRESENTING IMPLIED COMMITMENTS TO THE STATES WHICH CAN BE LEGALLY CONTROLLED THROUGH THE ANNUAL APPROPRIATION PROCESS					
Programs requiring some State matching of Federal funds:					
Funds appropriated to the President: Disaster relief.		13		42 U. S. C. 1855-1855-G, Public Law 80. 202, 82d Cong.	Grants to State and local governments in areas stricken by major disasters.
Federal Civil Defense Administration:					
Federal contributions	[3] 50	50	22	Public Law 920, 81st Cong.	Grants for procurement of civil defense supplies and equipment.
Protective facilities	[3] 250	50	44	do.	Grants are primarily for shelters.
Housing and Home Finance Agency: Defense community facilities and services		23		Title III, Public Law 139, 82d Cong.	Funds for direct Federal construction, loans to State and local governments, and administration, as well as for grants-in-aid. The largest part is expected to be for grants.
Federal Security Agency:					
Vocational rehabilitation	23	23	18	29 U. S. C. 31-44	States are reimbursed for 50 percent of the cost of case services for disabled persons and 100 percent of the cost of counseling, guidance, and placement services and administration.
Maternal and child welfare	30	33	29	42 U. S. C. 701-31, 1301	$85,000 is allotted to each State and the remainder according to various standards such as rural population, number of live births, and financial need.
Control of venereal disease[2]	8	8	8	42 U. S. C. 232, 246, 287	The amounts are allocated to the States on the basis of financial need, the extent of the disease proglem, population, and related factors.
Control of tuberculosis[2]	6	6	6		
Mental health activities[2]	3	3	3		
General public health assistance[2]	14	14	14		
National Heart Institute[2]	2	2	2		
Education of children on Federal property and in emergency and critical defense areas:					
Maintenance and operation of schools.	40	44	34	20 U.S.C. 236-244	The statute specifies eligibility standards and the formula for determining amounts for eligible school districts. It also specifies priorities if funds appropriated are insufficient to pay all eligible school districts.
School construction	150	141	100	20 U.S.C. 271-280	

See footnotes at end of table.

TABLE 2.—*Grants-in-aid, shared revenues, and loans and advances to States, under existing legislation*—Continued

Appropriation and program	1953 budget estimates (in millions)			Statutes establishing program	Comments
	New obligational authority	Expenditures			
		Total	Out of 1953 new obligational authority		
Programs requiring some State matching of Federal funds—Continued.					
Federal Security Agency—Continued.					
Vocational education	$19	$19	$19	20 U.S.C. 11–14	Grants are made for training in agriculture, home economics, trades and industry, and distributive occupations.
Disease and sanitation control, Alaska.[2]	1	1	1	42 U.S.C., ch. 6A	This grant supplements Alaska health activities.
Defense community facilities and services.		15		Title III, Public Law 139, 82d Cong.	Funds for direct Federal construction, loans to State and local governments, and administration, as well as for grants-in-aid. The largest part is expected to be for grants.
Hospital construction	75	126		42 U. S. C. 291	The Federal share of any approved hospital project may be no greater than ⅔ nor less than ⅓ of the cost. The annual appropriation determines the extent to which new projects can be approved for Federal matching grants.
National Cancer Institute[2]	3	3	3	42 U. S. C. 281–6	Federal funds are allocated on a formula basis.
Water-pollution control	1	1	1	33 U. S. C. 466	Grants are made to States and interstate water-pollution agencies.
Colleges for agriculture and the mechanic arts.	2	2	2	7 U. S. C. 321–6, 328–9, 331	Each State receives a minimum of $20,000. The remainder is distributed on the basis of population.
Department of Agriculture:					
National school lunch program	83	83	82	42 U. S. C. 1751–60	Funds available are allocated by means of a formula which takes into account the number of children aged 5 to 17 in the State and the State's per capita income.
Cooperative agricultural extension work.	27	27	27	7 U. S. C. 341–8, 386; 42 U. S. C. 1476	Funds are distributed on the basis of rural population and matched by the State or Territory receiving payment.
Agricultural experiment stations	12	12	12	7 U. S. C. 361–82, 386, 427	Allotments to States are made partly on the basis of pr scribed amounts and partly on the basis of rural and farm population and the need for research in smaller States.
Agricultural Marketing Act: Cooperative projects in marketing.[2]	1	1	1	7 U. S. C. 1621–9	The funds are used for projects designed to expand the markets for farm products.
State and private forestry cooperation.[2]	10	10	9	16 U. S. C. 564–568, 581	Assistance is furnished States in preventing and suppressing forest fires, and other forestry management work. Expenditures by States, counties, and private forest owners are generally in excess of Federal expenditures.

Department of Commerce: Federal-aid airport program.[2]	14	27	7	49 U. S. C. 1101-19	Grants are made to local sponsors for projects at airports which are part of a national airport system capable of meeting the needs of civil aviation and nontactical military air operations.
Department of the Interior:					
Wildlife restoration [2]	8	16		16 U. S. C. 669-669j	The Federal Aid in Wildlife Restoration Act authorizes the appropriation of funds collected through the excise tax on firearms, shells, and cartridges for assistance to the States in wildlife restoration projects.
Fish restoration and management [2]	2	2	2	64 Stat. 430	The Federal Aid to Fish Restoration Act authorizes the appropriation of the funds collected through the excise tax on fishing rods, reels, and artificial baits for assistance to States in restoring fish and improving fish management.
Programs not requiring State matching of Federal funds:					
Veterans' Administration:					
Supervision of training establishments (also listed in table 3, p. 1 under "Readjustment benefits").[2]	2	2	2	38 U. S. C., ch. 12	Grants are made to reimburse State and local agencies for expenses incurred in supervising establishments furnishing training for veterans.
Administration of unemployment and self-employment benefits (also included in table 3, p. 1 under "Readjustment benefits").[2]	1	1	1	38 U. S. C. 696	100 percent of the State's expenditures for this activity are reimbursed by the Federal Government.
Department of Labor: Unemployment compensation and unemployment service administration.	196	184	180	29 Stat. 49	Grants are based on estimated workload and the State average annual salary rates for employees administering this program.
District of Columbia: Federal contribution.	12	12	12	61 Stat. 361	An annual Federal contribution of $12 million is authorized by the District of Columbia Revenue Act of 1947.
MISCELLANEOUS GRANT PROGRAMS REQUIRING NO NEW OBLIGATIONAL AUTHORITY IN 1953		4		Various	
Shared revenues:					
Department of Agriculture: National forests fund.	15	15	15	16 U. S. C. 500	With minor exceptions, 25 percent of all money received from the national forests is paid to the States and Territories for the benefit of public schools and roads.
Department of Defense: Flood Control Act of 1938.	1	1	1	33 U. S. C. 701C-3	Permanent indefinite appropriation of 75 percent of the moneys received from lease of Federal lands acquired in connection with flood-control reservoirs. These moneys to be used for public schools and roads.
Department of the Interior:					
Oregon and California land grant fund.	7	7	7	39 Stat. 218	Permanent indefinite appropriation of 50 percent of all moneys deposited in the Oregon and California land-grant fund to specified counties.
Mineral Leasing Act	18	18	18	30 U. S. C. 191, 285	Permanent indefinite appropriation of 37½ percent of the amounts received under the Mineral Leasing Act and from leases of potash deposits.

See footnote at end of table.

TABLE 2.—*Grants-in-aid, shared revenues, and loans and advances to States, under existing legislation*—Continued

Appropriation and program	1953 budget estimates (in millions)			Statutes establishing program	Comments
	New obligational authority	Expenditures			
		Total	Out of 1953 new obligational authority		
MISCELLANEOUS GRANT PROGRAMS REQUIRING NO NEW OBLIGATIONAL AUTHORITY IN 1953—continued					
Shared revenues—Continued.					
Deprtment of the Interior:					
Boulder Canyon project, payments to Arizona and Nevada.	$1	$1	$1	43 U. S. C. 12A	Permanent definite appropriation for payments in lieu of taxes from revenues from operation of Boulder Canyon project.
Tennessee Valley Authority: Payments in lieu of taxes (also included in table 4, p. 3).		4		16 U. S. C 831e	The statute sets payments at 5 percent of gross power proceeds, with certain minimum payments.
Total, grants and shared revenues[4]	2,427	2,622	1,901	Various	These programs are all included in table 4 (Government enterprises) and are shown here in total because they provide aid to State and local governments. They are civil defense and provision of community facilities (included in public agency loans) in the Reconstruction Finance Corporation; advance planning of non-Federal public works (included in slum clearance and urban redevelopment), Alaska housing, and the United States Housing Act program in the Housing and Home Finance Agency.
Loans and repayable advances	275	[5] 11	10		
Total, Federal aid to State and local governments.[6]	2,702	2,611	1,911		

[1] Part of a larger appropriation account.
[2] Part of a larger appropriation account. The amount shown here for new obligational authority is based on the estimate of expenditures.
[3] 1953 appropriations are to be immediately available.
[4] Some relatively small grant-in-aid and shared-revenue programs have been omitted from this table. Their omission, however, does not affect totals shown.
[5] Deduct.
[6] Total of expenditures differs from total shown in special analysis G of the 1953 budget because of omission of proposed legislation.

TABLE 3.—*Veterans' Administration, under existing legislation*

Appropriation and program	1953 budget estimates (in millions)			Statutes establishing program	Comments
	New obligational authority	Expenditures			
		Total	Out of 1953 new obligational authority		
PROGRAMS RELATIVELY UNCONTROLLABLE THROUGH ANNUAL APPROPRIATION PROCESS					
Compensation and pensions:					
Compensation [1]	$1,531	$1,531	$1,531	10 U. S. C. 456, 1091a; 34 U. S. C. 696-687, 855c 1-3, 1036a; 38 U. S. C. 11a-2, 21-583, 631, 661, 700-741, 744 foll. ch. 12 V. R. 1 (a), VII, V. R. 3 (a) par. 11, V. R. 1 (a) pt. 1, par. 11, subpar. (a)-(j), V. R. 1 (a), pt. 1, par. 4, V. R. 10, par. 8; 42 U. S. C. 410.	Expenditures for each type of payment are based on statutory rates and on forecasts of numbers of eligible applicants. The figures for compensation exclude $100 million for proposed legislation to increase rates. Subsistence payments to disabled veteran trainees under Public Law 16 account for almost all expenditures classified in "Other."
Pensions	618	618	618		
Other	55	55	55		
Readjustment benefits:					
Education and training (also listed in part in table 2, p. 8).	624	626	697	12 U. S. C. 1716 (a) (1), note; 25 U. S. C. 331 note; 38 U. S. C. 693, 694a, 694b, 694d, 694e, 697, foll. ch. 12, V. R. 1 (a), pt. VIII; act of July 13, 1950, Public Law 610.	The estimates are based on enrollment, loans approved, and similar forecasts and on statutory rates. They exclude the cost of proposed legislation to provide education and training benefits for veterans of the Korean conflict.
Other	74	74			
Military and naval insurance	7	7	7	34 U. S. C. 841f, 853c-6; 38 U. S. C. 32a, 36, 445b, 472b, 503, 511-518, 717, 722.	These expenditures are mainly payments to beneficiaries of World War I service life insurance.
National service life insurance	55	55	55	34 U. S. C. 841f, 853c-6, 1020, 1020k; 38 U. S. C. 32a, 38, 512, 801-818.	These expenditures are almost entirely for transfers to the NSLI trust fund for death and disability insurance claims traceable to extra hazards of military service.
Veterans' miscellaneous benefits	27	37	17	38 U. S. C. 701g, 724, foll. ch. 12, V. R. 1 (a), pt. VII note, and pt. IX, par. 1.	These benefits include burial allowances, tuition, supplies, and equipment for disabled veteran trainees, and housing grants for paraplegic veterans. Expenditures are based on estimates of number of veterans eligible who apply for these benefits.
Servicemen's indemnities	9	9	9	38 U. S. C. 851-858; act of Oct. 11, 1951, Public Law 169.	Payments of $10,000 to the survivors of each deceased serviceman as required by the Servicemen's Indemnity Act.
Automobiles and other conveyances for disabled veterans.	5	5	5	Act of Oct. 20, 1951, Public Law 187	Up to $1,600 is paid toward the purchase of automobiles for certain blind or amputee veterans.

See footnote at end of table

TABLE 3.—*Veterans' Administration, under existing legislation*—Continued

Appropriation and program	1953 budget estimates (in millions)			Statutes establishing program	Comments
	New obligational authority	Expenditures			
		Total	Out of 1953 new obligational authority		
PROGRAMS REPRESENTING AN IMPLIED COMMITMENT TO VETERANS WHICH CAN BE LEGALLY CONTROLLED THROUGH ANNUAL APPROPRIATION PROCESS					
Nonmedical administration	$198	$198	$172	Based on statutory authorizations for programs administered (above).	Includes cost of administering the following activities: Claims, insurance, vocational rehabilitation and eudcation, loan guaranty, readjustment allowance, general administration and contract, and executive direction. About 85 percent of the estimate is based on workload forecasts for the programs involved (veteran enrollment, rating actions, loans processed, etc.). The balance of the estimate represents overhead or items not determinable on a workload basis.
Medical, hospital, and domiciliary services:					
Hospitalization:					
In Veterans' Administration hospitals.	524	518	476	38 U. S. C. 434, 479, 483, 484, 492, 493, 706, 706 (b).	Veterans having service-connected disabilities must be treated. Non-service-connected disabilities may be treated if veteran was discharged for line-of-duty disability or if he is in receipt of compensation for a service-connected disability. Otherwise hospitalization for non-service-connected disabilities requires war service and inability to defray expenses of hospitalization, subject to availability of beds in VA or other Government hospitals and honorable discharge.
In hospitals other than those of the Veterans' Administration.	24	26	21	38 U. S. C. 434–483	Contract care in hospitals other than Federal hospitals is limited to (1) service-connected disabilities, (2) non-service-connected disabilities in the case of women, (3) emergency cases and (4) those engaged in vocational rehabilitation under Public Law 16, 78th Cong. The 1952 estimated contemplate care for an average daily load of 102,000 in VA hospitals (of which approximately ⅔ are estimated to be non-service-connected) and 6,588 in other than VA hospitals.

Domiciliary care:					
In Veterans' Administration homes.	20	20	18	38 U. S. C. 706, 706 (b)	Same eligibility is required as for hospitalization except that applicant must be incapacitated, unable to earn a living, and (in peacetime cases) have no adequate means of support. Need for domiciliary care to be medically determined.
In State Homes (also listed in table 2).	4	4	3	24 U. S. C. 134	For payment of not to exceed one-half of cost to State Homes, veteran must be declared eligible by VA on same basis as that for VA Homes. Major factors controlling expenditures for institutional care are the number, type, and distribution of patients, the number of facilities to be operated, determination of adequate standards of care, personnel required to render such care, quality of meals to be served, adequate inventory of supplies and equipment, extent to which recreational and non-medical activities are desirable and the rapidity with which new institutions are activated.
Out-patient care (medical and dental care).	106	108	90	38 U. S. C. 434, 459 (c), 479, 492, 493, 706 (a), 706 (b).	To be eligible, veterans must need medical or dental treatment for service-connected disability and have discharge other than dishonorable. Also, veterans engaged in vocational rehabilitation under Public Law 16, 78th Congress and veterans of Spanish-American War are eligible for treatment of non-service-connected disabilities. Examinations are also provided on an out-patient basis for those insured by the VA insurance funds and to determine eligibility for compensation and pensions and need of hospitalization or domiciliary care.
All other medical programs	18	17	15	38 U. S. C. 11-11 (a), 15 through 15 (n), 434.	Includes departmental medical administration, research and education, and establishment of supply depots.
Additional services included in programs listed above:					
Employment of medical consultants				38 U. S. C. 11a-1	
Provision of prosthetic appliances				38 U. S. C. 241-250, 479, 483, 484, 693 (d)	
Acquisition of recreational facilities for patients and employees at isolated stations.				38 U. S. C. 434	
Garages for hospital employees				38 U. S. C. 438 (e)	
Courses of instruction for professional personnel.				38 U. S. C. 15 (i), 459	
Provision of patients' clothing for those unable to pay.				38 U. S. C. 492-493	
Furnishing and laundering of wearing apparel for certain employees.				38 U. S. C. 11(j)	
Hospital and domiciliary facilities, construction and repairs.	99	104	28	38 U. S. C. 434, 438 (j) (k) (l), 693 (a)	The new obligational authority for 1953 will provide for 3 new hospitals and for some modernization and conversion of existing facilities.

See footnote at end of table.

TABLE 3.—*Veterans' Administration, under existing legislation*—Continued

Appropriation and program	1953 budget estimates (in millions)			Statutes establishing program	Comments
	New obligational authority	Expenditures			
		Total	Out of 1953 new obligational authority		
PROGRAMS REPRESENTING AN IMPLIED COMMITMENT TO VETERANS WHICH CAN BE LEGALLY CONTROLLED THROUGH ANNUAL APPROPRIATION PROCESS—con.					
Grants to the Republic of the Philippines: For construction of new hospitals		$4		50 U. S. C. 1991, 1993	This program is limited to a maximum of $22,500,000 for new hospital construction of which $9,400,000 has been appropriated to date. This is believed to be sufficient to meet all construction costs through the fiscal year 1952.
For hospital care of Philippine veterans	$2	2	$1	50 U. S. C. 1991, 1992, 1994–96	This program reimburses the Philippine Government for the care and treatment of veterans who were in the organized forces of the Republic of the Philippines while such forces were in the service of the U. S. Armed Forces. It is limited to a maximum of $3,285,000 a year for not to exceed 5 years (last fiscal year 1951).
Miscellaneous veterans' programs (also listed in part in table 4, p. 3).		−7		Various	Mainly loan repayments by veterans.
Total [1]	4,000	4,011	3,818		

[1] Differs from total shown in Budget Document because of omission of proposed legislation.

TABLE 4.—*Programs of Government enterprises (under existing legislation) not subject to annual congressional control*

Agency and program	1953 budget estimates (in millions)					Statutes authorizing program	Comments
	Carry-over of prior authority July 1, 1952	New obligational authority in 1953	Gross disbursements	Gross receipts	Net expenditures		
Funds appropriated to the President: Expansion of defense production.			$301		$301	Public Law 774, 81st Cong.; Public Law 96, 82d Cong.	Includes only net expenditures to meet loan obligations and commitments to purchase made prior to June 30, 1952. Excludes expenditures under proposed extension and increased authority.
Export-Import Bank of Washington	$1,350		325	$240	85	12 U. S. C. 635 b, d, e, as amended by Public Law 158, 82d Cong.	The bank is permitted to have outstanding at any one time not more than $4.5 billion in loans and guaranties. Gross disbursements reflect loans estimated to be made during the year.
Federal Civil Defense Administration: Civil defense procurement fund.	5	[1] 10	104	94	10	Public Law 920, 81st Cong.	Fund advances to manufacturers for procurement items and collects from State and local governments for the items. From the requested 1953 appropriation of $25 million, it is estimated that $15 million will be made available during 1952, of which $10 million will be obligated in 1952.
Reconstruction Finance Corporation:							
Public agency loans	134		23	4	19	Reconstruction Finance Corporation Act, as amended by sec. 4 (a), Public Law 548, 80th Cong.	Disbursements will be principally from prior-year commitments.
Loans to railroads	134		2	15	−13		Estimated loan repayments will substantially exceed new disbursemnets.
Business loans and guaranties			325	344	−19		Excludes loans made under sec. 302 of the Defense Production Act and $18.5 million of administrative expenses limited in annual appropriation legislation.
Aid to private financial institutions	12			3	−3		Primarily repayments on depression investments in preferred stock of banks.
Catastrophe loans	61		7	4	3		Mainly disbursements on loans previously authorized for 1951 Kansas-Missouri-Oklahoma flood disasters.
Aids to private housing				13	−13		Consists mainly of liquidation of mortgages taken over from RFC Mortgage Company.
Public housing loans				1	−1		Repayments on loans made by Defense Homes Corporation.
Tin, fiber, and rubber production and liquidation of other World War II programs.	111		643	685	−42	Act of Mar. 31, 1948, as amended by act of June 24, 1950, Public Law 125, 80th Cong., as amended by act of June 29, 1948; act of June 30, 1949; act of Aug. 21, 1950; act of Aug. 10, 1950.	Operations are financed from current revenues. Net expenditures reflect excess of sales over operating expenses.

See footnotes at end of table.

TABLE 4.—*Programs of Government enterprises (under existing legislation) not subject to annual congressional control*—Continued

Agency and program	1953 budget estimates (in millions)					Statutes authorizing program	Comments
	Carry-over of prior authority July 1, 1952	New obligational authority in 1953	Gross disbursements	Gross receipts	Net expenditures		
Tennessee Valley Authority (also listed in part in table 2, p. 11).	$37	$200	$348	$148	$200	TVA Act of 1933, as amended (16 U. S. C., ch. 12a).	Expenditures include $25 million net reductions in unliquidated obligations.
Veterans' Administration: Direct loans to veterans and reserves (also listed in table 3, p. 7).	----------	----------	109	114	−5	38 U. S. C. 6941m; 12 U. S. C. 17471 (o).	New loans will be financed from the sale of loans as well as from loan repayments and income.
General Services Administration: General supply fund (see comment).	----------	----------	267	257	10	41 U. S. C., 7a–c	Fund purchases materials and services for other Federal agencies and is reimbursed at cost by the agencies. Inventories and cash on hand June 30, 1952, estimated at $46 million.
Housing and Home Finance Agency:							
Slum clearance and urban redevelopment (grant portion also listed in table 2, p. 2).[2]	699	350	29	4	25	42 U. S. C. 1451	Disbursements represent advances to plan projects, and temporary loans for acquisition and preparation of sites (126 planning advance commitments and 74 temporary loan commitments estimated for 1953). Redevelopment expenditures are confined to those specifically determined to be consistent with defense effort.
Housing loans to educational institutions.	269	----------	33	1	32	12 U. S. C. 1749	Will place an estimated 10,300 units under construction in 1953, confined exclusively to defense-relating housing. (All other college housing loans suspended.)
Federal National Mortgage Association.	490	----------	746	685	61	12 U. S. C. 1716 et seq.	Assumes drop in purchases of mortgages from current rate, together with sharply higher sales. Excludes administrative expenses of $4 million.
Loans for prefabricated housing	25	----------	33	40	−7	12 U. S. C. 1701g; reorganization plan No. 23, 1950; title V, Public Law 139, 82d Cong.	Expenditures mainly on new defense-connected program authorized by title V, Public Law 139, 82d Cong. Expenditures on previously authorized program expected to decline.
Federal Savings and Loan Insurance Corporation.	750	----------	2	18	−16	12 U. S. C. 1724 et seq.	Corporation insures savings accounts in Federal savings and loan associations. To pay losses, it can use its earnings and borrow up to a total of $750 million from the U. S. Treasury. No insurance losses are anticipated in 1953. Estimated receipts shown consist primarily of premiums and earned interest.
Federal Housing Administration	----------	----------	76	89	−13	12 U. S. C. 1701 et seq.; title II, Public Law 139, 82d Cong.	Basic legislation authorizes insurance of private loans. Unused insurance authorizations for all FHA funds on July 1, 1952, estimated at $4 billion (including proposed $1 billion). Disbursements exclude $5,631,000 for administrative expenses, which are limited by annual appropriation legislation. Net receipts shown represent essentially excess of premium income over other expenses and losses for all except the mutual mortgage insurance fund (classified under trust accounts).

U. S. Housing Act program (including annual contributions also listed in table 2, page 1).[3]	115	86	317	392	−75	42 U. S. C. 1401 et seq.	Based on estimated 75,000 starts in 1953, with an increased percentage financed privately by local housing authorities, together with substantial private refinancing of temporary public loans. Excludes administrative expense of $11 million.
Public war housing program (including defense housing).	15		46	58	−12	42 U. S. C. 1521 et seq.; title III, Public Law 139, 82d Cong.	Title III, Public Law 139, 82d Cong. authorized Federal construction of defense houses. 2d Supplemental Appropriation Act, 1952 provided $25 million, $15 million estimated to be spent in fiscal 1953. Merged for accounting purposes with World War II program. Authorization for new projects on World War II program expired in 1945. Expenses of operating and disposing of projects expected to be less than income.[1]
Veterans' reuse housing program			2	4	−2	42 U. S. C. 1521 et seq.	Authorized construction completed. Income from property expected to exceed administrative expenses.
Subsistence homesteads and greentowns.			1	2	−1	5 U. S. C. 55	Liquidation of depression program.
Department of Agriculture:							
Disaster loans revolving fund	17		45	34	11	11 U. S. C. 1148	Estimates are based on need for disaster loans. Disbursements are from repayments and unexpended balance from prior years. They include $2.4 million for administrative expenses.
Federal Crop Insurance Corporation	108		24	29	−5	7 U. S. C. 1501–19	Insurance losses financed by premiums. Estimates for 1953 assume that 90 percent of premiums earned will be paid out in indemnities. Thus a 10-percent reserve is established for unforeseen losses.
Federal intermediate credit banks	235	20	2,332	2,291	41	12 U. S. C. 1041	Banks finance their lending operations by borrowing in the private market. Debentures outstanding may not exceed 10 times the surplus and paid-in capital. Excludes $1.7 million administrative expenses.
Commodity Credit Corporation:							
Price support, supply, and purchase programs (also listed in part in table 2, p. 3).	4,251	120	1,942	1,720	222	Secs. 5 (a) and (d) of CCC Charter Act, as amended by act of June 28, 1950; Public Law 439, 81st Cong., supplemented by Public Law 163, 79th Cong., Public Law 471, 81st Cong.	1953 expenditures will be largely determined by price support operations for 1952 crops, as required under the Agricultural Act of 1949. The volume of such expenditures depends on the level of crop production, consumption, and exports. Excludes administrative expenses of $18 million.
Net expenditure for Bureau of Animal Industry for eradication of foot-and-mouth disease.		11	7		7	21 U. S. C. 114a	Represents net advance to defray the 1953 cost of the foot-and-mouth disease program.
International Wheat Agreement			188	182	6	7 U. S. C. 1641–42	Estimated disbursements of $188 million will be required to supply wheat to foreign importers at fixed price established by the agreement. An offset of $182 million is anticipated as reimbursement from appropriated funds for 1951 costs.
Federal Farm Mortgage Corporation (see comment).				9	−9	12 U. S. C. 1020 et. seq.	Consists of receipts from mortgage repayments. Corporation is in liquidation and available authority, therefore, cannot be used for new loans.

See footnotes at end of table.

TABLE 4.—*Programs of Government enterprises (under existing legislation) not subject to annual congressional control*—Continued

Agency and program	1953 budget estimates (in millions): Carry-over of prior authority July 1, 1952	New obligational authority in 1953	Gross disbursements	Gross receipts	Net expenditures	Statutes authorizing program	Comments
Department of Agriculture—Continued							
Production credit corporations	$54	$2	$2	$5	−$3	12 U. S. C. 1131 et. seq.	Consists of net receipts from repayments of stock in production credit associations.
Production and Marketing Administration: Local administration: sec. 388, Agricultural Adjustment Act of 1938.			48	49	−1		Under the AAA of 1938, funds available to PMA are transferred to this account to enable the PMA county committees to carry out the programs assigned to them. In the 1953 budget, expenditures appear under the parent appropriation accounts.
Department of Commerce: Vessel operations revolving fund (see comment).			422	521	−99	Public Law 45, 82d Cong.	A fleet of cargo vessels will be operated almost entirely from current revenue.
Department of Defense: Panama Canal Company.	7	3	85	76	9	Public Law 808, 80th Cong., as amended by Public Law 841, 81st Cong.	Operations will be financed mainly from estimated tolls, commodity sales and other services. Capital expansion will be mainly financed by borrowing $7 million and by new appropriations of $3 million.
Department of the Interior:							
Bureau of Indian Affairs, revolving fund for loans.	(3)	1	3	2	1	25 U. S. C. 470, 471	Approximately $2 million of total disbursements will be paid from receipts and $1 million from appropriations.
Bureau of Reclamation: Fort Peck project emergency fund.			2	3	−1	16 U. S. C. 833	Estimated receipts from sale of power expected to exceed purchase of power delivered to the Bureau.
Department of Justice: Federal Prison Industries, Inc.			19	23	−4	18 U. S. C. 4121–4128	Operations are financed from sales of products and services. Net expenditures reflect profit from sales of prison-made goods. Excludes administrative expenses of $800,000.
Subtotal	8,879	753	8,858	8,159	699		
Deduct:							
(1) Amounts from prior-year authority and receipts of enterprise.	8,879				449		
(2) Amounts from relatively controllable new authority.		214			214		
Equals: Amounts from relatively uncontrollable new authority.		539			36		

[1] Requested 1953 appropriation of $25 million to be partially used in 1952. $10 million is estimated part of appropriation not used in 1952.
[2] All or part of these programs are also included in table 2, p. 11, as loans and repayable advances to State and local governments.
[3] Less than $500,000.

TABLE 5.—*Miscellaneous relatively uncontrollable items,*[1] *under existing legislation*

Agency, program, or appropriation	1953 budget estimates (in millions)			Statutes establishing program	Comments
	New obligational authority	Expenditures			
		Total	Out of 1953 new obligational authority		
Railroad Retirement Board: Railroad unemployment insurance administration fund.	$12	$11	$6	45 U. S. C. 361	The administrative costs of the railroad unemployment system are provided through this permanent indefinite appropriation equal to 3/10 of 1 percent of the taxable railroad payroll.
Federal Security Agency:					
Bureau of Federal Credit Unions: Salaries and expenses.	1	1	1	12 U. S. C. 1751–1772	Fees collected from Federal credit unions are appropriated annually to provide most of the cost of supervising the operations of the credit unions.
Food and Drug Administration: Salaries and expenses, certification services.	1	1	1	Federal Food, Drug, and Cosmetic Act, as amended (21 U. S. C. 346, 354, 357, 364, 372a, 376).	These services are wholly supported by fees charged against advance deposits, which are appropriated annually to cover the service costs or refunds of unearned deposits.
Department of Agriculture:					
Forest Service:					
Expenses and refunds, brush disposal.	1	....	....	16 U. S. C. 490	Permanent indefinite appropriation of amounts received from purchasers of national forest timber, to be used for disposal of brush and other debris from cutting operations.
Cooperative range improvements	1	1	1	16 U. S. C. 580h	A part of the grazing fees from national forests is earmarked to provide funds for various range improvements.
Roads and trails for States, national forests fund.	6	6	2	16 U. S. C. 501	Permanent indefinite appropriation of 10 percent of receipts from national forest activities for the construction and maintenance of roads and trails within the national forests of the States from which the receipts are derived.
Farm Credit Administration: Administrative expenses and refunds.	2	2	1	12 U. S. C. 636; 832	Assessments collected from farm credit banks and corporations are earmarked (annual indefinite appropriation) to provide funds to cover supervisory expenses of farm credit agencies.
Production and Marketing Administration: Removal of surplus agricultural commodities (excluding grants to States).	141	20	16	Permanent appropriation of Aug. 24, 1935; sec. 32 of the Agricultural Adjustment Act, as amended (7 U. S. C. 612c).	The total appropriation (including the portion for grants to States) is equal to 30 percent of customs duties and, if not spent, accumulates to $300 million. The carry-over on June 30, 1952, is estimated at $176 million.

TABLE 5.—*Miscellaneous relatively uncontrollable items,*[1] *under existing legislation*—Continued

Agency, program or appropriation	1953 budget estimates (in millions)			Statutes establishing program	Comments
	New obligational authority	Expenditures			
		Total	Out of 1953 new obligational authority		
Production and Marketing—Continued					
Sugar Act program	$70	$70	$55	Sugar Act of 1948 (7 U. S. C. 1101–1160).	Rates of payment to sugar producers are specified in the Sugar Act of 1948. Total expenditures, except for administrative expenses, depend on volume of sugar production.
Conservation and use of agricultural land resources.	257	262	218	Soil Conservation and Domestic Allotment Act of 1936 as amended (16 U. S. C. 590g–q).	The 1952 Appropriation Act authorized use of 1952 funds for formulation and administration of a 1952 crop-year program of $257 million, to be paid from the 1953 appropriation. Similarly, the proposed 1953 appropriation language specifies a $257 million program for the 1953 crop-year, to be financed in the 1954 appropriation. By the time the 1953 appropriation is acted upon, farmers will have largely completed planting of 1952 crops and advances will have been made for application of lime and fertilizers.
Replacement of personal property sold	1	1	----------	41 U. S. C. 231 (c)	Permanent indefinite appropriation of proceeds from sale of agency property which are available to purchase replacements.
Department of Commerce: Maritime activities: Operating differential subsidies.	50	75	50	Merchant Marine Act of 1936 (46 U. S. C. 1101).	The statute provides authority for entering into long-term subsidy contracts with shipping companies and to compensate them for higher costs of American-flag operations. Expenditures in any given year are largely fixed by the long-term contracts in force.
Department of the Interior:					
Replacement of personal property sold	1	1	----------	41 U. S. C. 231 (c)	Permanent indefinite appropriation of proceeds from sale of agency property which are available to purchase replacements.
Bureau of Reclamation: Colorado River Dam fund, Boulder Canyon project, payment of interest on advances from the Treasury.	3	3	3	43 U. S. C., ch. 12A	Permanent indefinite appropriation to pay interest to the Treasury for moneys advanced for the construction of the Boulder Canyon project.
Fish and Wildlife Service:					
Administration of Pribilof Islands	2	1	1	64 Stat. 1071; act of Sept. 27, 1950 (16 U. S. C. 631a–631q).	Annual indefinite appropriation of an amount not exceeding 60 percent of the proceeds from the sale of sealskins and other products. Amount is 60 percent of estimated proceeds in 1953.

Management of national wildlife refuges.	1	1	....	16 U. S. C. 703-11, 715s	Permanent indefinite appropriation of 75 percent of proceeds from sale of wildlife-refuge products are appropriated for refuge maintenance and enforcement activities.
Migratory bird conservation fund..	4	4	3	16 U. S. C. 718-718h; 63 Stat. 599	Permanent indefinite appropriation of receipts from the sale of Federal hunting stamps.
Bureau of Indian Affairs:					
Operation and maintenance:					
Indian irrigation systems	2	2	....	Act of Aug. 7, 1946	Permanent indefinite appropriation of revenues derived from charges for operation and maintenance of Indian irrigation projects.
Indian irrigation projects	2	2	1	31 U. S. C. 725s-3	Permanent indefinite appropriation of revenues from sale of electric power for operation and maintenance of these projects.
National Park Service: Authorized expenditure of collections made by National Park Service.	1	1	....	16 U. S. C. 40c; 64 Stat. 849; 65 Stat. 644; 62 Stat. 232.	Permanent indefinite appropriation of park fees for operation and maintenance of buildings in Independence National Historical Park, Pa., and for other purposes.
Post Office Department	669	669	669	Title 39 U. S. Code	There is an extremely large number of laws regulating postal services. The President has recommended postal-rate increases to yield $225 million in 1953 with further increase in following year.
Treasury Department:					
Bureau of Customs: Customs duties and taxes, Puerto Rico.	4	4	4	Tariff Act of 1930, as amended	Permanent indefinite appropriation of customs duties, taxes, and fees collected in Puerto Rico. Available balances are transferred to the treasurer of Puerto Rico.
Bureau of the Mint:					
Minor coinage profits, etc	1	1	1	31 U. S. C. 340; Revised Statute 3528, as amended.	Permanent indefinite appropriation of receipts resulting from minor coinage. Fund is charged with cost of distributing such coins and wastage and recoinage losses.
Silver-profit fund	....	1	....	31 U. S. C. 335; Revised Statute 3526 and 64 Stat. 157.	Permanent indefinite appropriation of receipts from coinage of silver bullion. Fund is charged with cost of distributing such coins and wastage and recoinage losses.
Total	1,233	1,140	1,033		

[1] This tabulation excludes certain items relatively uncontrollable through the annual appropriation process such as salaries and expenses of Congressmen ($8 million), salaries of judges ($6 million), and the salary and expenses of the President ($150,000) and of the Cabinet members, which are fixed by law.

TABLE 6.—*Items appearing in more than 1 of the preceding 5 tables*

Item	1953 budget estimates (in millions)			Tables in which item appears
	New obligational authority	Expenditures		
		Total	Out of 1953 new obligational authority	
Veterans' Administration:				
Aid to State homes	$4	$4	$4	Table 2, grants-in-aid. Table 3, Veterans' Administration.
Administration of unemployment and self-employment benefits	1	1	1	
Supervision of on-the-job training	2	2	2	
Direct loans to veterans and reserves	(1)	(1)	(1)	Table 3, Veterans' Administration; table 4, Government enterprises.
Housing and Home Finance Agency:				
Slum clearance and urban redevelopment	100			Table 2, grants-in-aid. Table 4, Government enterprises.
U. S. Housing Act program: Annual contributions	36	36	36	
Department of Agriculture:				
Commodity Credit Corporation: Donation of surplus commodities	(2)	(2)	(2)	
Tennessee Valley Authority: Payments in lieu of taxes	(2)	(2)	(2)	
Loans and repayable advances to State and local governments by Reconstruction Finance Corporation, Housing and Home Finance Agency, and Federal Civil Defense Administration.	[3] 250	(2)	(2)	
Total [4]	393	43	43	

[1] Although these items are listed in both table 3 and table 4, the relevant amounts are excluded from the final table 4 totals.
[2] Although these items are listed in both table 2 and table 4, the relevant amounts are excluded from the final table 4 totals.
[3] Excludes $25 million for this item which has been eliminated from the final total of table 4.
[4] Represents total adjustment for duplicating items in tables 1 through 5.

The CHAIRMAN. The next meeting of this committee will be as the guests of the Subcommittee on Defense Appropriations when the Secretary of Defense and the Secretaries of the three departments will appear in the caucus room of the Senate Office Building.

The committee stands adjourned.

(Whereupon, at 3:55 p. m., the joint committee adjourned.)

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