FISCAL POLICY IMPLICATIONS OF THE CURRENT ECONOMIC OUTLOOK

HEARINGS

BEFORE THE

SUBCOMMITTEE ON FISCAL POLICY

OF THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

EIGHTY-FIFTH CONGRESS

SECOND SESSION

PURSUANT TO

Sec. 5 (a) of Public Law 304
(79TH CONGRESS)

APRIL 28, 29, 30, AND MAY 1, 1958

Printed for the use of the Joint Economic Committee

UNITED STATES
GOVERNMENT PRINTING OFFICE
25780 WASHINGTON : 1958

For sale by the Superintendent of Documents, U. S. Government Printing Office
Washington 25, D. C. - Price 55 cents

JOINT ECONOMIC COMMITTEE

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

WRIGHT PATMAN, Representative from Texas, *Chairman*
JOHN J. SPARKMAN, Senator from Alabama, *Vice Chairman*

HOUSE OF REPRESENTATIVES

RICHARD BOLLING, Missouri
HALE BOGGS, Louisiana
HENRY S. REUSS, Wisconsin
HENRY O. TALLE, Iowa
THOMAS B. CURTIS, Missouri
CLARENCE E. KILBURN, New York

SENATE

PAUL H. DOUGLAS, Illinois
J. WILLIAM FULBRIGHT, Arkansas
JOSEPH C. O'MAHONEY, Wyoming
RALPH E. FLANDERS, Vermont
ARTHUR V. WATKINS, Utah
JOHN D. HOBLITZELL, Jr., West Virginia

RODERICK H. RILEY, *Executive Director*
JOHN W. LEHMAN, *Clerk*

SUBCOMMITTEE ON FISCAL POLICY

Senator PAUL H. DOUGLAS, *Chairman*

Representative HALE BOGGS
Representative THOMAS B. CURTIS
Senator JOSEPH C. O'MAHONEY
Senator JOHN D. HOBLITZELL, Jr.

NORMAN B. TURE, *Economist*

CONTENTS

PANEL DISCUSSIONS AND INDIVIDUAL WITNESSES IN ORDER OF APPEARANCE

STATEMENTS AND EXHIBITS

STATEMENTS AND EXHIBITS—Continued

FISCAL POLICY IMPLICATIONS OF THE CURRENT ECONOMIC OUTLOOK

MONDAY, APRIL 28, 1958

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON FISCAL POLICY OF THE
JOINT ECONOMIC COMMITTEE,
Washington, D. C.

The subcommittee met at 10 a. m., pursuant to notice, in room P-63, the Capitol Building, Hon. Paul H. Douglas (chairman of the subcommittee) presiding.

Present: Senators Paul H. Douglas, John D. Hoblitzell, Jr., and Representative Thomas B. Curtis.

Also present: Norman B. Ture, staff economist, and Roderick H. Riley, executive director.

Senator DOUGLAS. On behalf of the subcommittee on fiscal policy I want to welcome you to these hearings on the fiscal policy implications of the current economic outlook. All of us are greatly concerned over the recession which began last fall and which has proceeded rapidly since then. I need hardly point out that there has been a wide variety of interpretations placed upon these economic developments, upon economic prospects for the near future and upon the proper course of Federal governmental policy. Unfortunately too much of the public discussion of these problems and issues has been distorted by irrelevant considerations.

While I am not in the least adverse to participating in political controversy in other connections, as I am sure you all know, I believe that such controversy should proceed from a clear and objective exposition of facts and issues.

This is the purpose of these hearings.

We are seeking the facts about the current economic situation of the Nation and a careful appraisal of the prospects for the economy in the remainder of this year and in 1959. We hope that the answers we find during these hearings will be helpful in arriving at a realistic policy for dealing with the recession.

This committee and its subcommittees have established, I believe, a reputation for providing a forum in which facts and issues may be set forth without the reservations of entrenched interests and in which opposing viewpoints may be tested with cold and sober analysis rather than with rhetoric. I am confident that those who have been invited to participate in these hearings will enhance this reputation.

The Joint Economic Committee has a continuing responsibility to follow economic developments and to advise Congress on adjustments in public policies which may be desirable for economic stability and growth. I am sure that all members of the subcommittee share my interest in seeking such adjustments which also will be consistent with considerations of economy in Government and stability of the price level. We shall be concerned in these hearings with the broad outlines of fiscal action appropriate to current and foreseeable economic conditions. Responsibility for any specific actions which may be desirable rests, of course, with the legislative committees of Congress.

The plan for these hearings has been detailed in pubic releases by the subcommittee. Today we are to hear from a panel of distinguished economists on recent economic developments and the outlook for the coming months. We will hear the opening statement of each witness before proceeding with a general discussion. If there is no objection, I will invite each of the witnesses to submit for the record any prepared materials which he does not include in his opening statement.

Our first witness is Prof. V. Lewis Bassie, Director of the Bureau of Economic and Business Research of the University of Illinois, a citizen of my own State.

Professor Bassie, we are very happy to have you with us.

STATEMENT OF LEWIS BASSIE, DIRECTOR, BUREAU OF ECONOMIC AND BUSINESS RESEARCH, UNIVERSITY OF ILLINOIS

Mr. Bassie. Mr. Chairman, I welcome the opportunity to join with you and the others here in considering what should be done about the difficult problems that lie ahead of us.

Today the economy is in serious danger. We are in the beginning of a major contraction that might last several years and double the present high level of unemployment.

What is most disturbing to me is the inaction of the Government up to this point. Six months of decline have resulted in a loss of real gross national product of $20 billion and a rise in the seasonally adjusted rate of unemployment to almost 8 percent.

Yet no effective action has been taken. High officials are fiddling a pointless tune about confidence, hoping that the recession will go away of its own accord. This is the sure way to let things get out of hand.

I can even see the possibility that many will be encouraged to continue this futile waiting game by the developments of the next few months. The decline has progressed faster than anyone expected, largely as the result of a very sharp reversal in inventory policy. The latest estimates place the rate of liquidation at over $7 billion.

Possibly liquidation of this magnitude is, as some claim, fully as much as the decline in sales warrants. But this does not imply a quick recovery. The rate of liquidation should not be confused with the amount of liquidation. To liquidate $7 billion of inventories at this rate would require a whole year.

Nevertheless, it does hold the prospect that pressure on inventory account may ease in the next few months. If the rate of liquidation dropped just a little, it might be enough, in conjunction with rising Government expenditures to offset further declines in capital expenditures.

The optimists are using this potential slowing of the decline as the basis for a "saucer theory" of the recession. This, it seems to me, is going too far. We cannot say that the decline is "bottoming out."

All that can be said is that there may be some flattening, after which business may go either up or down.

My own judgment on this point is that in the absence of more effective Federal action the decline will be resumed. I base this on the character of the present decline. This recession differs from those we have experienced earlier in the postwar period because it marks the end of the postwar boom in fixed investment.

Every major war has been followed by a great boom which in turn ended in a severe depression. These developments are not accidental. They represent an inescapable cyclical pattern that develops out of a succession of imbalances in the relationships between stocks and flows of investment goods of all kinds.

At the peak of the boom investment is lifted to a rate beyond the needs for long-term growth; and the capital goods created by that rate of investment approach the point of excess; that is, the market approaches saturation. For both reasons, investment has to be cut back and the reaction of the cutback is to make the existing stocks still more excessive, further intensifying the curtailment of investment and driving the economy deeper into depression. We are in such a situation today.

These cyclical declines have always been long, drawn out and severe. After the post-Civil War boom ended in 1873, depression persisted through the remainder of the decade. In the 1930's we were still enduring a depression of substantial magnitude when the war broke out in Europe 10 years after the stock market collapse of 1929.

I think the current setback is not going to be so bad as that of the 1930's. But I see no reason to think that it will soon be over, with no worse than the present difficulties to trouble us.

If the economy is permitted to drift in the period of potential leveling off just ahead, the chances are that the continued downward thrust of capital expenditures will reinstate the drive for inventory liquidation at a new extreme. Declining expenditures for housing and durable goods will then add to the forces of recession. The likely consequence of such a policy will be a conjuncture of deflationary forces near the end of the year that will make for an even bigger decline in 1959.

In other words, it seems that there is just a chance to avert the most extreme phase of the depression. Decisive action in the months ahead might turn the economy back up. I do not think it is a very good chance. But any chance seems worth taking in preference to waiting for the slump to be resumed in the typical manner.

Thank you.

Senator DOUGLAS. Thank you very much, Mr. Bassie.

The discussion will be continued by Mr. William F. Butler, vice president of the Chase Manhattan Bank.

We are very glad to have you with us.

STATEMENT OF WILLIAM F. BUTLER, VICE PRESIDENT, CHASE MANHATTAN BANK

Mr. BUTLER. Mr. Chairman, I propose to try to do two things this morning. The first is to set forth my appraisal of the immediate outlook for Federal Government receipts and expenditures and their impact on the economy. The second task I have set for myself is that of providing a somewhat longer perspective on Government expenditures by looking both backward and forward over a span of years. Actually, I consider the second task to be the more challenging one.

However, let us turn first to the outlook for the immediate future, say, through mid-1959. As a first step I will set forth the projections of Federal receipts and expenditures I have been using in trying to assess the business outlook:

[Billions of Dollars]

	January to June 1958	July to December 1958	January to June 1959
Cash receipts	$47.3	$35.1	$46.8
Cash expenditures	44.3	45.1	46.5
Surplus or deficit	+3.0	−10.0	+0.3

It seems clear that we are moving into a period of substantial deficit financing. Moreover, we are just beginning to feel the economic impact of this shift to deficits. In the first half of this calendar year, the Federal Government will run a surplus at an annual rate of approximately $3 billion. But in the second half a deficit on cash account of perhaps $10 billion at annual rates is in prospect.

In other words, Federal fiscal operations will siphon cash out of the economy at an annual rate of $3 billion in the first half and will add to consumer and business purchasing power at a $10 billion rate in the second half. I believe there is general agreement among economists that such a shift in Government fiscal operations provides one of our important defenses against recessions.

If you will turn to the table on the last page of the prepared statement, you can see how this shift in Federal fiscal policy compares with the shift in the last two recessions.

Federal fiscal policy in 3 recessions

	Shift in Federal fiscal policy		
	Billion	As percent of prior year's gross national product	As percent of change in gross national product
1948–49	−$9.3	3.7	110
1953–54	+4.9	[1] 2.0	[1] 75
1958 1st half–1958 2d half	−13.0	3.0	81

[1] Tax cut of $7.4 billion as percent of prior year's gross national product and change in gross national product.

As you can see it is generally of the same dimension as the shift that took place on those two occasions.

I do not wish to attach undue importance to the historical parallels. Nevertheless I think that it is worth making the point that the shift to deficit spending now underway is of the same general order of magnitude as the fiscal policy measures adopted in the two previous recessions.

Now whether Government should take more vigorous action this time depends on what is likely to happen in the private economy.

If you will turn to page 3 of the prepared statement you can see what changes have already taken place between the third quarter of last year and the first quarter of this year.

As you can see the major change was the shift to inventory liquidation which accounts for two-thirds of the decline.

We have had a reduction of $2.6 billion in the rate of consumption; $2.5 billion in fixed investment; $1.7 billion in net foreign investment; and the main offsetting factor has been an increase of $1.3 billion in Government, chiefly at the State and local levels.

Now, how the prospects ahead line up in each of these fields:

Clearly further reductions lie ahead in business investment in new plant and equipment and in exports. These two items yield minus pressures of about $6 billion to $7 billion in the next year.

However, Government expenditures might rise by as much as $8 billion in the coming year with perhaps $5 billion of the increase coming at the Federal level.

Housing might rise a bit. I will defer to Mr. Newcomb on housing.

If these projections prove reasonably accurate it is unlikely that consumption will decline much and it could increase later in the year.

All these developments could produce a turnabout in the inventory sector leading to a resumption of inventory accumulation by early 1959.

These projections obviously involve a series of assumptions that cannot as yet be fully documented. However, it is my personal opinion that the business curve is now bottoming out and that we shall see a renewed advance before year's end.

In my view this is the most probable course of events. It is, however, part of the law of probabilities that the improbable occasionally happens. So one cannot rule out the possibility that the downtrend might begin to accumulate. To my mind the next month or two will be the test period.

But I confidently expect that in this period we will begin to see the early signs, first of the leveling, and then of the upturn. Because of this belief and because I believe we are likely to see some further increases in Government expenditures in the years ahead, it is my judgment that an immediate tax cut would be unwise.

Now to turn to the longer term outlook for Government expenditures, I would like to direct your attention to the chart which follows page 5 of the prepared material. This chart shows Government purchases of goods and services on a per capita basis measured in constant 1957 dollars for the period since 1913. Since the purpose of Government in our society is to serve the people, it seems appropriate to use the per capita measure in looking at long-term trends. I would draw the following conclusions from these data.

First, national security expenditures clearly dominate the picture. If they could be reduced as the result of the attainment of a viable relaxation of world political tensions the burden of taxation could be substantially reduced.

Second, Government expenditures on civilian activities have increased. But the rate of increase has fallen short of past trends.

In looking ahead it seems to me that these trends pose very real problems of choice to our society. In the short run we can quite properly hold back other programs to give priority to the needs of national security. But if the external threat is to persist we must be concerned about the adequacy of our efforts in other necessary directions.

For example, the long-term trend shows an increase of 4 percent per year per pupil in expenditures for education. It shows an increase of 4½ percent per year per person in expenditures for public works. In recent years we have about matched the trend in education. We have fallen well short of the trend in public works.

If our economy is to grow and prosper we must provide the public assets and public services needed to support growth.

In making these points I don't wish to imply that I favor any and all Government expenditures. To the contrary, I believe we need to scrutinize most carefully existing programs.

In the meantime we must seize every opportunity to encourage the growth of the private economy. If we can match or hopefully exceed past rates of economic growth, we can meet necessary requirements in Government fields and still achieve a substantial growth in the private economy.

Thus we should reform our tax system to remove the impediments to growth and we should orient other Government policies and procedures to the general objectives of increasing our rate of economic advance.

Thank you.

Senator DOUGLAS. Thank you very much Mr. Butler.

(Mr. Butler's prepared statement follows:)

REMARKS BY WILLIAM F. BUTLER, VICE PRESIDENT, CHASE MANHATTAN BANK

I propose to try to do two things this morning. The first is to set forth my appraisal of the immediate outlook for Federal Government receipts and expenditures and their impact on the economy. The second task I have set for myself is that of providing a somewhat longer perspective on Government expenditures by looking both backward and forward over a span of years. Actually, I consider the second task to be the more challenging one.

However, let us turn first to the outlook for the immediate future—say through mid-1959. As a first step I'll set forth the projections of Federal receipts and expenditures I have been using in trying to assess the business outlook:

[Billions of Dollars]

	January to June 1958	July to December 1958	January to June 1959
Cash receipts	$47.3	$35.1	$46.8
Cash expenditures	44.3	45.1	46.5
Surplus or deficit	+3.0	−10.0	+0.3

It seems clear that we are moving into a period of substantial deficit financing. Moreover, we are just beginning to feel the economic impact of this shift to deficits. In the first half of this calendar year, the Federal Government will run a surplus of approximately $3 billion. But in the second half a deficit on cash account of perhaps $10.0 billion is in prospect. In other words, Federal fiscal operations will siphon cash out of the economy at an annual rate of $3.0 billion in the first half and will add to consumer and business purchasing power at a $10 billion rate in the second half. I believe there is general agreement among economists that such a shift in Government fiscal operations provides one of our important defenses against recessions.

What is the economic impact of the shift to deficit spending now in prospect likely to be? First, I think it is important to point out that it is small in relation to the total economy. The projected swing from surplus to deficit works out to 3 percent of last year's gross national product. Interestingly enough, a similar calculation for 1948–49 yields a 3.7 percent figure. In 1953–54 such a swing did not take place, as both expenditures and taxes were cut. However, the reduction in taxes put into effect then amounted to 2 percent of the prior year's GNP.

A second way to measure the impact of a shift to deficit spending is to compare it with the *change* in gross national product. Such a comparison shows that the impact of fiscal policy was large in relation to the decline in GNP in 1948–49 and 1953–54. In 1948–49 it was 10 percent greater than the decline in GNP from the peak quarter to the low quarter. In 1953–54 the tax cut amounted to about three-fourths the decline in GNP from peak to trough.

In the current recession, GNP has already declined by a rate of $16 billion or 4 percent. However, the shift in Federal fiscal operations in prospect for the remainder of the year is about equal to that decline.

In making these comparisons, I do not wish to attach undue importance to the historical parallels. My purpose is simply to make the point that the shift to deficit spending now in prospect is of the same general order of magnitude as the fiscal policy measures adopted in the two previous recessions. This does not necessarily prove that the current recession will prove as moderate and short-lived as the previous two.

Whether Government should take more vigorous action this time depends on what is likely to happen in the private economy. Thus the next step is to review recent economic trends as a prelude to an evaluation of future prospects. Estimates of the Council of Economic Advisers show that the following factors have been operating in the current recession:

Change third quarter 1957 to first quarter 1958 in billions of dollars at annual rates

Gross national product:	—$16.0
Consumption	—2.6
Fixed investment	—2.5
Inventories	—10.5
Net foreign investment	—1.7
Government	+1.3

How do present prospects for the year ahead line up in each of these fields? Clearly further reductions lie ahead in business investment in new plant and equipment and in exports—they might yield minus pressures of $6–7 billion. Government expenditures might rise by as much as $8 billion in the coming year, with $5 billion of the increase coming at the Federal level. Housing might rise a bit. If such trends developed in these key areas, it is unlikely that consumption would decline, and it could increase later in the year. Such trends could produce a turn-about in the inventory sector, leading to a resumption of inventory accumulation by early 1959.

These projections obviously involve a series of assumptions that cannot as yet be firmly documented. We are in the difficult and trying period of the business cycle in which a leveling of the decline may be in the making. But it is still too early to see in the statistics the clear evidence of such a leveling, in part because of the lag in statistics behind the facts.

It is my personal opinion that the business curve is now bottoming out, and that we shall see a renewed advance before year's end. In my view this is the most probable course of events. It is, however, part of the law of probabilities that the improbable occasionally happens. So one cannot rule out the possibility that the downtrend might begin to cumulate. To my mind the next month or two will be the test period, but I confidently expect that in this period we will begin to see the early signs, first of the leveling and later of the upturn.

Because of this belief, and because I believe we are likely to see some further increases in Government expenditures in the years ahead, it is my judgment that an immediate tax cut would be unwise. If, however, signs should appear in the next month or two that the downturn is beginning to snowball, I would think a tax cut would be in order. And I would agree with those who argue that we need to develop greater sophistication in these matters; if we are to deal successfully with recessions and inflations in the future, we must learn to cut taxes when demand sags and to increase them when the economy is under inflationary pressure. Yes, I think we have much to learn about the appropriate timing of tax action and about the problem of securing public support for the use of fiscal policies to combat recession and inflation.

To turn to the longer term outlook for Government expenditures, I should like to introduce some concepts and supporting statistics which may help provide needed perspective. It seems to me that discussions of this subject are frequently misleading because of a failure to take the following three factors into account: (1) inflation, (2) the growth in our population, and (3) the huge increase in national security expenditures. The attached chart presents the picture of Government purchases of goods and services on a per capita basis, measured in constant 1957 dollars, for the period since 1913. Since the purpose of government in our society is to serve the people, it seems to me appropriate to use the per capita measure in looking at long-term trends.

I would draw the following conclusions from these data:

(1) National security expenditures clearly dominate the picture. If they could be reduced as a result of the attainment of a viable relaxation in world political tensions, the burden of taxation could be substantially reduced.

(2) Government expenditures on civilian activities have increased, but the rate of increase has fallen short of past trends.

In looking ahead, it seems to me that these trends pose very real problems of choice to our society. In the short run we can, quite properly, hold back other programs to give priority to the needs of national security. But if the external threat is to persist, we must be concerned about the adequacy of our efforts in other necessary directions. For example, the long-term trend shows that we have increased education expenditures per student about 4 percent per year (in constant dollars) since 1910. Certainly we wish to continue if not accelerate the improvement in our educational system. As another example, the long-term trend shows a 4½-percent per annum increase in our public investment in such fields as highways, hospitals, water-supply systems, and urban betterment.

In recent years, we have about matched the long-term trend of increasing expenditures per person in education, but we have fallen short of it in other fields of civilian government endeavor. If our economy is to grow and prosper, we must provide the public assets and the public services needed to support growth. So long as national security requirements remain high, increases in other areas to meet the needs of our growing population will pose real problems.

In making these points I do not wish to imply that I support any and all Government expenditures. On the contrary, I believe we need to scrutinize most carefully existing programs to see where economies can be achieved. The very magnitude of necessary Government expenditures in the period ahead emphasizes the importance of concentrating on essential fields and of stressing efficiency in Government.

Meantime, we must seize every opportunity to encourage the growth of the private economy. If we can match, or hopefully exceed, past rates of economic growth, we can meet necessary requirements in Government fields and still achieve a substantial growth in the private economy. Thus, we should reform our tax system to reduce the impediments to growth and we should orient other Government policies and procedures to the general objective of increasing our rate of growth.

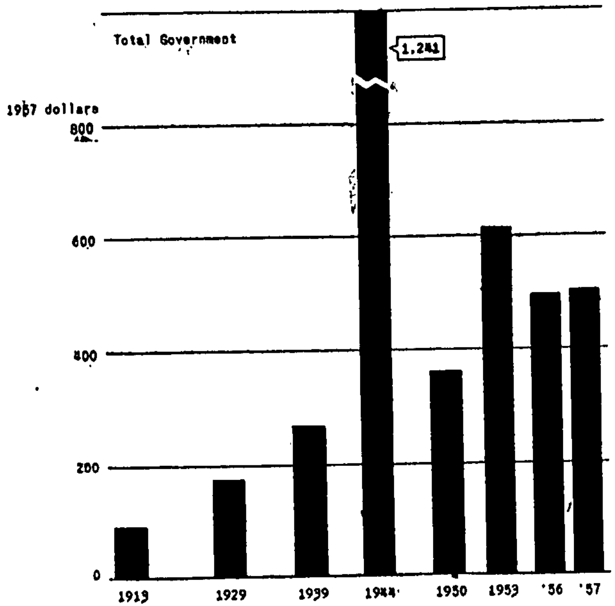
Federal fiscal policy in 3 recessions

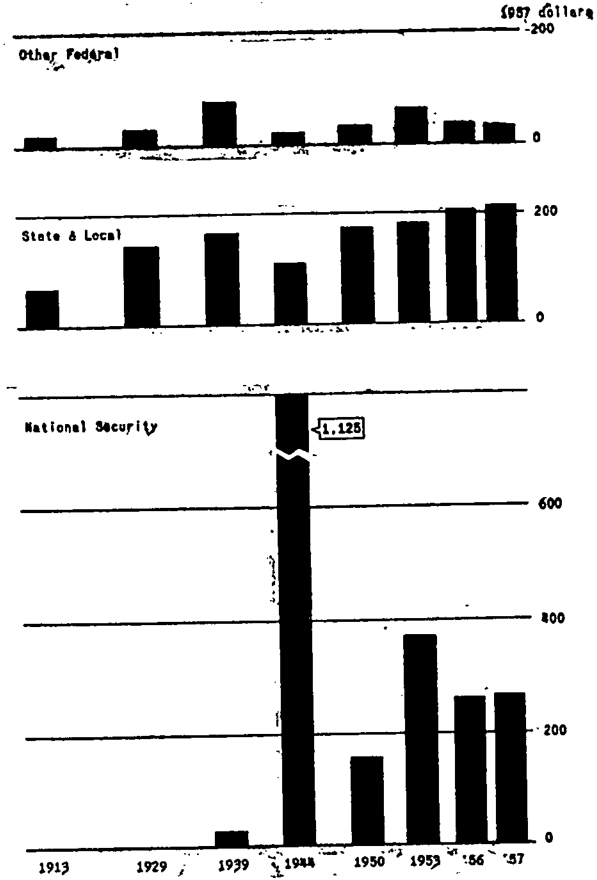
	Shift in Federal fiscal policy		
	Billion	As percent of prior year's gross national product	As percent of change in gross national product
1948–49	–$9.3	3.7	110
1953–54	+4.9	[1] 2.0	[1] 75
1958 1st half–1958 2d half	–13.0	3.0	81

[1] Tax cut of $7.4 billion as percent of prior year's gross national product and change in gross national product.

Government Purchases of Goods and Services

Per Capita -- Constant 1957 Dollars





Senator DOUGLAS. The discussion will be continued by Mr. Irwin Friend, professor of economics at the University of Pennsylvania.

STATEMENT OF IRWIN FRIEND, PROFESSOR OF ECONOMICS AND FINANCE, UNIVERSITY OF PENNSYLVANIA

Mr. FRIEND. In discussing the implications of the economic situation for fiscal policy, it seems to me that the most important points to be considered are these:

First, we have already had for 3 months unemployment approximating 7 percent of the labor force, a proportion which most people would consider quite excessive.

Second, the current downturn in business is potentially more serious than the 1949 and 1954 recessions since it is associated for the first time in the postwar period with a significant weakness in business expenditures on plant and equipment, which in the past have been closely related to major cyclical movements.

Third, while there can be legitimate differences of opinion about the outlook for the next year, the probability of continuing recession seems fully as high as the probability of a significant improvement in business conditions unless remedial action is taken—and there is some danger of a cumulative deterioration in the economic situation which might be avoided by appropriate measures.

These three considerations suggest the desirability of prompt action by the Federal Government to combat recessionary tendencies. On the other hand, there are two reasons which can be advanced in favor of postponing major action apart from a distaste for deficits.

First, prices haven't shown any tendency to decline in the current economic downturn, leading to concern that further Government stimulation of business activity might result in higher prices and might interfere with desirable structural adjustments in the economy.

Second, the type of world we live in is likely to require more Government expenditures for the foreseeable future so that at least one of the most important types of possible action, namely tax relief, may be undesirable since it is difficult to raise taxes once they have been lowered.

The critical question involved in these pros and cons of Government action relates to the present outlook for the next year, say, for the rest of 1958 and early 1959, which is perhaps as far as it is useful to look ahead. If we take the most recent data available as a point of departure—the national product and income series for the first quarter of 1958—and attempt to project the corresponding figures for the fourth quarter of 1958, we arrive at the following results, admittedly with an uncomfortable margin of error.

In the absence of new legislation, the key element in the business situation this year is likely to be the course of Federal Government expenditures on income and product account, for which various fiscal experts have been projecting a rate of increase of $1 billion to $1½ billion a quarter (at annual rates) until mid-1959. This would imply roughly a $4 billion increase by the fourth quarter of 1958.

I might note that the area of uncertainty in this figure is very large. Government officials have been talking lately of a $5 billion increase in the expenditure budget from fiscal 1958 to fiscal 1959, but it is not clear what is included in this increase or what part should be translated into national income and product. I hope as part of these hearings the Government makes available such information.

State and local government expenditures still seem to be rising, though it is doubtful that they will continue to do so at the rapid rate of recent years if the recession persists, and in any case the effect of increased expenditures will be partly offset by increased taxes. The rise in State and local government expenditures by the fourth quarter might tentatively be set at $2 billion. There seems no stronge reason for anticipating much change in residential construction and net farm investment, though one might project a small decline in the latter on the basis of recent trends and some rise in the former.

Turning to business investment, the Commerce-SEC survey of business plans implies that investment in nonresidential construction and producers' durable equipment will probably decline some $5½ billion at annual rates from the first to fourth quarter, at which point such outlays might be expected to level out according to the recent McGraw-Hill survey. There is some reason for believing that the decline may be larger than $5½ billion since in past downturns businessmen have somewhat overestimated their plant and equipment outlays.

The depressant influence of business fixed investment, however, is likely to be fully offset by a rise in business investment in inventories. The reduction or disinvestment in inventories in the first quarter, estimated at $7½ billion, can't be expected to continue for very long if final sales (to ultimate consumers) hold up at recent levels. The ratio of the level of busines inventories to monthly average sales was a little over 1.7 at the end of February compared with an average of somewhat less than 1.6 in 1956 and 1957, which might be taken to imply an excess of over $5 billion at the present level of sales.

A survey of desired inventories just completed by Fortune implies that businessmen would want to reduce their inventories by somewhat less than $5 billion if final sales remain reasonably stable and that under present plans this will take place at progressively lower rates of disinvestment until the last quarter of this year. These plans apparently imply a reduction in the rate of inventory disinvestment of over $6 billion a year.

So far, therefore, we have a picture of a $6 billion stimulation to the economy by the fourth quarter largely emanating from the Government sector. We have, however, left out the final element in the business situation; namely, consumption behavior. Consumption will be effected both by the additional incomes generated by the $6 billion net increase in Government expenditures and by any changes in consumption versus saving propensities.

The personal saving-income ratio in the first quarter of 1958 is estimated at 6.1 percent, which is lower than in 1957 in spite of the influence of net repayment of consumer debt and presumably reflects the attempt by unemployed and underemployed persons to maintain their living standards. The ratio—which is lower than 1954 but higher than in 1949—may decline further giving an additional impetus to consumption, but there does not seem to be any reason to count on this.

If the increase in consumption is quite optimistically assumed to be of the magnitude of $9 billion—since in recent years the increase in consumption has tended to be 1½ times the net increase in other expenditures—the gross national product in the fourth quarter of 1958 would amount to $439 billion which might imply unemployment on the order of 5 million. While these projections could easily err on either side, I think for policy purposes in the context of the current economic situation it should be assumed that they may be too optimistic.

My appraisal of the business situation and of the dangers of action versus inaction leads me to the conclusion that additional action by the Federal Government is required.

Monetary measures designed to ease credit further will not be adequate in my opinion. What seems to be required is the injection of another $5 billion of new spending which in view of its multiplier effect should go far toward achieving a high level of employment without incurring serious inflationary dangers. This stimulation to the economy could be effected either through an additional $5 billion of Federal Government expenditures, or through tax relief and liberalized unemployment benefits which would have to amount to over $5 billion because a dollar of tax reduction probably would not have as much effect as a dollar of expenditure.

Since major expenditure programs as an antidote to depression should be reserved for more serious economic conditions than now confront us and since in any case they cannot be promptly implemented, major reliance will have to be placed on other measures.

It seems to me that these measures should include first, liberalization of unemployment compensation, and second, some combination of an increase in personal or family exemptions, a temporary across-the-board tax cut applicable to individual incomes and perhaps temporary selective cuts in excises.

Thank you.

Senator DOUGLAS. Thank you very much.

The discussion will be continued by an old friend of ours, Dr. Martin R. Gainsbrugh, Chief Economist of the National Industrial Conference Board.

I might say, Mr. Gainsbrugh, that you show a great deal of public spirit in coming down here on all occasions and taking the time out from your work. We appreciate it very much.

STATEMENT OF MARTIN R. GAINSBRUGH, CHIEF ECONOMIST, NATIONAL INDUSTRIAL CONFERENCE BOARD

Mr. GAINSBRUGH. I have gained from every exposure.

I propose to concentrate my opening statement on an area which all the participants have mentioned, namely the short term outlook for private business investment. To me the hard core of the business recession is to be found in the decline in business spending for capital goods. The sharp cutbacks of inventory spending of more recent months were induced by rather than the cause of the decline in investment spending. It is incorrect to regard this contraction as an inventory cycle. In attempting to cure the recession, it is imperative that it be recognized as a capital goods cycle.

It is gratifying to note how the surveys of investment spending intentions gave early warning of the decline in the capital goods sector. There are three major series foreshadowing trends in business plant and equipment: the Government survey, prepared by the Department of Commerce-SEC; the McGraw-Hill survey; and the National Industrial Conference Board quarterly survey of capital appropriations of the Nation's largest manufacturers.

The conference board appropriations series as early as the second quarter of 1957 had already called attention to the decline in the rate of manufacturers' new appropriation approvals—decision to spend. The extent of the decline in these figures even at that time suggested to us that a decline in manufacturers' capital goods spending would become evident around the turn of the year.

In early November, the McGraw-Hill survey of preliminary spending plans for 1958 corroborated our finding for the manufacturing sector. In addition, it foreshadowed a 7 percent decline in total business spending for plant and equipment in 1958 compared with 1957.

In December, the Commerce-SEC survey indicated that the first sizable decline in total plant and equipment spending was expected to take place in the first quarter of 1958. By mid-March, however, the final returns were in for all of 1957, and it was discovered that the decline had in fact begun in the closing months of 1957. Total outlays were expected to decline further, both in the first and the second quarters of this year. More important, the overall decline in capital outlays had become 13 percent, almost twice the drop reported in the preliminary McGraw-Hill survey.

The fourth-quarter 1957 conference board appropriations survey reported the rate of new appropriation approvals down very sharply from the corresponding levels of 1956. The early warning system was pointing to declines through all of 1958, at least for capital goods spending for manufacturers.

The second McGraw-Hill survey of spending plans for 1958, released just 10 days ago, reported no appreciable changes from the March findings of the Government agencies.

It is important to note that in the two McGraw-Hill surveys, as well as in that of the Government, the decline in manufacturers' capital goods spending in 1958 is expected to be down about one-sixth. Note how this meshes with our appropriations figures for 1957 which were one-fifth lower than in 1956. The trend in manufacturing capital goods outlays was already foreshadowed by the earlier drop in the rate of new appropriation approvals.

This trend then fanned out from manufacturing. Substantial cuts in the annual capital budgets between last fall and early spring began to take place also in the nonmanufacturing sector, apart from the mining and the electric utility industries.

The current impact of these continuing declines in capital goods spending is certainly clear. The cutback in capital spending is reflected in volume declines in production of the durable goods industries. Total durables output is off 15 percent, and even more so for metals and machinery.

If you will look at the first table I have submitted, you will find that total durables output is already off 15 percent, more severe than in any decline we have experienced since the end of World War II.

And far more so for metals and machinery. Look at the figures for primary metals, off 3.7 percent from its peak, and nearly a third in the course of a year.

Unemployment too is most pronounced in manufacturing, particularly in durables.

TABLE I.—*Changes in industrial production, 1956–58*

[Seasonally adjusted index numbers, 1947–49=100]

Industry	1956–57 peak		March		Percent change	
	Month	Index	1957	1958 [1]	1956–57 peak—March 1958	March 1957–March 1958
1. Industrial production	December 1956	147	145	128	−12.9	−11.7
2. Manufactures	do	149	147	129	−13.4	−12.2
3. Durable manufactures	do	167	163	135	−19.2	−17.2
4. Primary metals	September 1956	148	137	92	−37.8	−32.8
5. Fabricated metals	November 1957	141	138	122	−13.5	−11.6
6. Nonelectrical machinery	December 1956	157	155	126	−19.7	−18.7
7. Electrical machinery	do	216	204	173	−19.9	−15.2
8. Transportation equipment	do	223	219	180	−19.3	−17.8
9. Instruments	August 1957	174	173	160	−8.0	−7.5
10. Stone, clay, and glass	May 1956	162	155	130	−19.8	−16.1
11. Lumber and products	August 1956	130	[2] 115	[2] 107	−17.7	−7.0
12. Furniture and fixtures	August 1957	123	119	111	−9.8	−6.7
13. Miscellaneous manufactures	October 1956	146	140	129	−11.6	−7.9
14. Nondurable manufactures	August 1957	132	131	124	−6.1	−5.3
15. Textile mill products	February 1956	110	[3] 101	[2] 91	−17.3	−9.9
16. Apparel and products	October 1956	117	[3] 110	[3] 103	−12.0	−6.4
17. Rubber products	January 1956	147	[2] 141	[2] 114	−22.4	−19.1
18. Leather and products	February 1956	111	[3] 102	[3] 100	−9.9	−2.0
19. Paper and products	August 1957	163	[3] 159	[3] 154	−5.5	−3.1
20. Printing and publishing	December 1957	142	141	138	−2.8	−2.1
21. Chemicals and products	August 1957	186	[2] 183	[2] 178	−4.3	−2.7
22. Petroleum and coal	January 1957	146	141	129	−11.6	−8.5
23. Food and beverages	December 1957	114	[2] 113	[2] 114	0	+.9
24. Tobacco manufactures	September 1957	114	[3] 112	[3] 112	−1.8	0
25. Minerals	March 1957	132	132	113	−14.4	−14.4
26. Coal	do	92	92	70	−23.9	−23.9
27. Crude oil and natural gas	February 1957	154	151	131	−14.9	−13.2
28. Metal, stone, and earth minerals	September 1956	143	132	120	−16.1	−9.1

[1] Preliminary.
[2] February.
[3] January.

Sources: Federal Reserve Board; the Conference Board.

A basic question we have to face, then, is this: Will the decline in spending for capital goods go beyond 1958? The news from the capital appropriations front is not reassuring as yet. Based upon a sample of early returns, it is already clear that the first-quarter rate of new appropriation approvals will show further deterioration.

Capital appropriations today reflect spending for plant and equipment 6, 9, and 12 months hence.

Remember, too, that the current rate of spending is being supported by the backlogs resulting from decisions to spend made in earlier quarters. The arithmetic of first-quarter appropriations thus suggests the sobering possibility of a drop in manufacturers' capital goods spending which may continue at least into early 1959.

By way of providing perspective on the current decline, we compare in table II the cutback already experienced in investment spending with what happened to capital goods spending in previous recessions. We have already cut business investment more than in 1953–54.

I invite your attention in table 2 to the third and second last items, plant and equipment spending, OBE-SEC; and manufacturers' plant and equipment spending, OBE–SEC.

There you will note from the third quarter of 1957 to the second half of 1958 the indicated drop in total spending for plant and equipment is 18 percent, already more severe than the total decline in 1953–54 and beginning to approach the full extent of the decline in 1948–49. Even more in point, manufacturers' outlays for plant and equipment will be off by 22 percent by the middle of this year as compared with 15 percent in 1953–54—but still considerable to go in terms of 1948–49.

The latest foreshadowing figures now suggest a decline in such spending at least as severe as in the earlier 1948–49 cycle, both declines measured over a period of 4 quarters.

TABLE II.—*Capital goods cycles*

	Peak	Trough	Percent change
Gross private domestic investment:			
1937-38	Year 1937	Year 1938	−43
1948-49	III Q 1948	IV Q 1949	−32
1953-54	II Q 1953	IV Q 1953	−17
1957-58 [1]	IV Q 1956	I Q 1958	−22
Gross private domestic investment excluding change in business inventories:			
1937-38	Year 1937	Year 1938	−19
1948-49	III Q 1948	III Q 1949	−8
1953-54	III Q 1953	I Q 1954	−3
1957-58 [1]	IV Q 1957	I Q 1958	−5
New construction:			
1937-38	Year 1937	Year 1938	−10
1948-49	III Q 1948	II Q 1949	−8
1953-54	II Q 1953	III Q 1953	−2
1957-58 [1]	IV Q 1957	I Q 1958	−2
Residential construction:			
1937-38	Year 1937	Year 1938	6
1948-49	II Q 1948	II Q 1949	−15
1953-54	II Q 1953	IV Q 1953	−4
1957-58 [1]	II Q 1955	I Q 1958 [2]	−15
Other construction:			
1937-38	Year 1937	Year 1938	−22
1948-49	IV Q 1948	III Q 1949	−8
1953-54	II Q 1953	III Q 1953	−1
1957-58 [1]	IV Q 1957	I Q 1958	−3
Producers' durable equipment:			
1937-38	Year 1937	Year 1938	−28
1948-49	III Q 1948	I Q 1950	−16
1953-54	III Q 1953	I Q 1955	−14
1957-58 [1]	I Q 1957	I Q 1958	−10
Plant and equipment (OBE-SEC):			
1948-49	IV Q 1948	IV Q 1949	−20
1953-54	III Q 1953	I Q 1955	−11
1957-58 [1]	III Q 1957	2d half 1958	−18
Manufacturers' plant and equipment (OBE-SEC):			
1948-49	I Q 1948	I Q 1950	−34
1953-54	I Q 1953	I Q 1955	−15
1957-58 [1]	III Q 1957	2d half 1958	−22
Manufacturers' outlay for plant and equipment:			
1937-38			−38
1948-49			−20
1953-54			−7

[1] For 1957-58 period, most recent data as of April 1958 are used.
[2] Trough was reached in the 2d quarter of 1957, or −19 percent from peak to trough.

Sources: Department of Commerce; Securities and Exchange Commission; Council of Economic Advisers.

It is indeed encouraging in the face of these cutbacks in capital goods spending to find the continuing strength in final-product demand. Thus far, the recession has been locked mostly within the hard goods industries. Spending for soft goods and services is steady if not increasing. The inventory cutbacks in the first quarter of this year would seem already about as severe a decline in this area as we are likely to see in the balance of the year. This part of the investment decline should be behind us by the year end.

To repeat what I said at the hearings earlier this year, trends in consumer spending for soft goods and services serve to indicate the extent to which the downtrend in capital goods outlays has infected the rest of the economy. Thus far in 1958, consumer end-product demand is surprisingly high. The current and foreshadowing statistics on plant and equipment now reveal that the economy is undergoing a capital goods adjustment which is at least as severe as in 1948–49. This suggests that part of the cure may have to be directed specifically to this sector. With temporary excess capacity already present in 1957, and with further additions in 1958, the correction may be slow, if not overly prolonged.

With a more favorable tax environment, perhaps investment spending could be stepped up. To me this is an ignored area of tax recommendations thus far in 1958.

Special tax incentives relative to depreciation or to research and development could accelerate the shift in the character of capital goods spending, particularly for modernization, new techniques, and new products. They might speed up the shift from increasing physical capacity to further emphasis on modernizaiton and cost saving. They might not only stimulate the depressed capital goods industries, but they would also contribute toward greater productivity to the benefit of the entire economy.

This is no endorsement for tax relief now. As I have stressed end-product demand continues high even in April.

I suggest, however, that should tax relief be found necessary more consideration be given to the stimulation of business investment via the tax reform, the tax incentive, the tax relief route than has been given to it so far.

Senator DOUGLAS. Thank you very much.

The discussion will be continued by Mr. Nathaniel Goldfinger, research department of the American Federation of Labor and Congress of Industrial Organizations.

STATEMENT OF NATHANIEL GOLDFINGER, ECONOMIST, DEPARTMENT OF RESEARCH, AFL–CIO

Mr. GOLDFINGER. The present recession is the most severe economic decline in 20 years. In March, after 7 months of recession, industrial production had fallen more sharply than at the lowest level of the 1949 and 1954 recessions. Unemployment was a greater percent of the labor force, after adjusting for seasonal and other factors, than in the worst unemployment months of the two previous post-World War II declines.

Furthermore, economic activities at present are continuing to deteriorate. Important indicators of forthcoming economic activities—such as manufacturers' new orders and backlogs, inventory-sales ratios, investment plans, construction contract awards, nonfarm employment, working hours, and personal income—all point to a continuing decline in the weeks immediately ahead.

The recession, indeed, is at a danger point. It has been feeding on itself—as indicated by the continuing drop in retail sales. In the absence of positive Government action to halt the recession, layoffs, short workweeks, and declining incomes seem to be breeding pessimism, falling retail sales, and additional layoffs and short workweeks. Declining consumer spending—at a time when business investment is headed down, and when Government expenditures are merely a relatively small plus factor—presents a dangerous threat that economic activities may be dragged into a downward spiral.

This danger is particularly serious because the Government, to date, has failed to adopt a comprehensive antirecession program that would quickly bolster economic activities and public confidence. The Government's failure to act, in a meaningful way, for more than 7 months of this decline is not only a failure to assume its responsibility under the Employment Act of 1946. It is also in contrast to 1949 and 1954, when tax cuts on individual incomes were automatically put into effect under previously adopted measures.

CAUSES OF THE RECESSION

The major underlying cause of this recession is a lack of balance between consumption and investment that developed in 1955 and 1956. Business outlays for new plant and equipment rose sharply from early 1955 to the end of 1956, while key economic activities—such as hard-goods purchases and residential construction—started to decline.

Growing gaps developed between sales and productive capacity. According to McGraw-Hill estimates, the percent of industrial capacity in use fell from 92 percent at the end of 1955 to 86 percent at the end of 1956, to 82 percent in September 1957. With sales falling in the past half year and additional capacity being installed, only about 70 percent of industrial capacity is now in operation. It is this developing condition that brought a leveling off of business investment at the start of 1957 and the beginning of a long decline—through 1958 and into 1959—in the final quarter of last year.

Behind this lack of balance between investment and consumption has been a sharp rise in the flow of spendable cash to corporations, while spendable consumer income increased at a relatively slow pace. Between 1954 and 1957, after-tax profits and depreciation allowances of nonfinancial corporations rose 32 percent, while disposable personal income increased only 18 percent.

This disparity in the flow of spendable cash rested on business pricing and Government tax policies that stimulated and subsidized business investment while personal consumption lagged. The leading corporations in major industries maintained or widened their profit margins through price increases and administered price structures. These profit margins were imposed on top of cost increases that were largely related to the investment boom and that were, in good part, more apparent than real—rising depreciation per unit of output (that flowed from the 1950 and 1954 tax changes, as well as the capital goods boom), rising interest payments per unit of output (that arose from corporate decisions not to finance any significant portion of business investment from new stock issues), and rising research and development costs per unit of output (that flowed, in part, from the 1954 tax change that permitted these costs to be charged off in the current year rather than to capitalize them).

The Government's tight money policy did little, if anything, to restrain the investment boom or the price rises of large corporations, while it succeeded in keeping down the growth of overall output through its restraining effect on small businesses, State and local governments.

What is needed now is the prompt release of several billion dollars of purchasing power into the economy's spending stream—to boost sales, to halt the drastic inventory cuts of recent months, and to put a larger percent of productive capacity into operation.

A basic remedy for the current recession—to help prevent a recurrence of similar declines in the future—requires an overhauling of the Federal tax structure, in order to provide a more equitable flow of spendable cash to corporations and to consumers.

UNEMPLOYMENT

I have been asked to concentrate on the employment situation and shall attempt to do so in the remainder of this statement.

Unemployment has been rising, month after month, since last July—after accounting for seasonal changes. Unless seasonal factors are taken into account, it is impossible to make any adequate analysis of unemployment or employment trends.

There were those who attempted to emphasize the decline in the number of jobless last fall, when these declines were less than usual for that time of the year, and when analysis of the unemployment figures indicated that the economic situation was deteriorating.

This type of confusion will probably be prevalent in the next month or two, because unemployment should normally decline some 200,000 to 300,000 in April, followed by a smaller decline in May. A counter-seasonal movement of unemployment in April—relative stability or a small decline—that indicates a continued worsening of the economic situation will probably be presented by some people as a cheerful or hopeful sign—as occurred when unemployment rose from 6.7 percent of the labor force in February to 7 percent in March, after accounting for seasonal variations, although the numerical increase was small.

This recession started at a point when unemployment was already relatively high—4.2 percent of the labor force in the first half of 1957, after accounting for seasonal changes. This was higher than it was before the 1949 recession when 3.7 percent of the labor force was unemployed, or before the 1954 recession, when 2.7 percent were unemployed.

The number of totally jobless has risen from 2.6 million in August or 4.3 percent of the labor force, to 5.2 million in March, or 7 percent, after accounting for seasonal changes. This is a larger jobless percentage of the labor force than at any time during the 1949 or 1954 recessions, after adjusting for seasonal and other factors. Furthermore, in March, there were 2.3 million persons who were jobless over 10 weeks—44 percent of the total number of jobless.

In addition, short workweeks were more widespread than in the previous post-World War II recessions. The length of the workweek in manufacturing industries in recent months has been the lowest for comparable months since 1941.

There were 3.5 million people compelled, because of economic conditions, to work 34 hours or less per week in March. The number of full-time workers on part-time schedules, because of economic factors, was at a new postwar peak.

With these layoffs and short workweeks, it is no wonder that wage and salary income has dropped more sharply than in either the 1949 or 1954 recessions. Neither is it any wonder that retail sales have been falling—and have been falling more sharply than the dollar totals would indicate because retail prices have been rising.

Labor income has dropped $8.7 billion (annual rate) between August and March. Only about one-quarter of this decline has been offset by rising unemployment insurance payments. This decline in wages and salaries has affected a large percentage of low- and middle-income families—those with little or no liquid savings.

UNEMPLOYMENT IS DEPRESSING CONSUMER ACTIVITIES

These totals of unemployment and part-time work, I believe, have had a depressing effect on retail sales and residential construction. But an examination of the composition of the unemployment is even more revealing in terms of present and future consumer activities.

Unemployment has risen sharply among men, and particularly among younger men who would normally be buyers of homes, house furnishings, and hard goods. There is relatively greater unemployment now among men who are family breadwinners. Furthermore, unemployment is greatest among the prime age group, young men between 20 and 34 years of age. (See attached table.)

While 7.7 percent of the total labor force (not adjusted) was unemployed in March, 8 percent of all men in the labor force were jobless. In both March 1956 and 1957, the jobless percentage of the male labor force was approximately the same as total unemployment.

Of all men, aged 20–24 in the labor force, 16.4 percent were unemployed in March—up from 7.3 percent in March 1957. This is a greater rise than the increase in total unemployment, from 4.3 to 7.7 percent in that same period.

Of all men, aged 25–34 in the labor force, 8.3 percent were unemployed in March—an increase from 3.3 percent in March 1957.

While there were somewhat similar trends in 1949 and 1954, the jobless percentages in these age groups are now substantially greater than in the previous post-World War II period.

The present recession has seriously affected the spending potential of the group in the population that is normally a major consumer of house furnishings, hard goods, and a large part of the housing market. This unemployment situation among men aged 20–34 has a current depressing effect on consumer activities and probably will continue to have a depressing effect in the period immediately ahead.

In addition, high unemployment among young men seems to have resulted in a postponement of marriages. An examination of marriages, in comparable months of the previous year, reveals a consistent decline in the number of marriages, performed each month, beginning last September. This decline in marriages occurred at a time when the 18–24 age group is beginning to feel the effects of the increased birth rate since 1939; the number of girls in that age group increased slightly in 1957, for the first time since 1946.

Marriage postponement, as well as high unemployment among young men, has a depressing effect on consumption and housing. Both of these factors may also reduce the number of births—something the optimists have been counting on to strengthen consumer activities in the months ahead.

SEASONAL FACTORS AFFECT TOTAL EMPLOYMENT

Total employment has been declining—it has been moving counter-seasonally. But the economic significance of these movements is hidden in the data, since total employment figures include farm employment, self-employed, household jobs, and unpaid family workers. For the purpose of economic analysis, it is impossible to use total employment figures without making adjustments for seasonal changes.

Farm employment tells us nothing about economic trends. It rises and falls in response to the weather conditions—regardless of economic conditions or farm prices. The only significance is that it is declining from year to year, so that the nonfarm economy has to provide jobs for those who are displaced from agriculture.

To include month-to-month movements of farm employment in an analysis of current economic trends, without adequate adjustment for seasonal changes, is merely to get lost in confusion. A warning against this possible confusion is necessary because there are those who have, and will, use month-to-month movements of total employment, without analysis, as a basis for commenting on economic trends.

For example, between February and March total employment increased only 300,000—in farm and construction. This increase occurred at a time when seasonal factors alone should have raised total employment by about 700,000. Rather than a sign of hope, the 300,000 increase in total employment in March indicated a continuing deterioration of economic conditions.

In the next few months, total employment will rise because of improving weather conditions, unless there is a catastrophe. Agricultural employment will go up, as in the past years, by about 2 million or more between January and June, regardless of trends in the economy or in farm prices. This rise in farm employment and in total employment—most of which occurs in April, May, and June—will tell us nothing at all about economic trends unless it is adjusted for seasonal changes and adequately analyzed.

In the past 2 years, total employment increased 400,000 to 900,000 between March and April—with a normal seasonal increase of about 600,000. Any rise in total employment this April must be viewed against the normal seasonal increase of about 600,000, for the purpose of making an analysis of economic trends.

Between April and May, the rise in total employment in the past 2 years has been 900,000 to 1.2 million—with a normal seasonal increase of about 1 million. The normal seasonal rise in total employment between May and June should be about 1.2 million.

I emphasize the importance of analyzing total employment figures because they have frequently been misinterpreted and distorted in the past. There is a likelihood that they will be misinterpreted and distorted again in the coming weeks.

NONFARM EMPLOYMENT IS FALLING

Nonfarm wage and salary employment has dropped 2.1 million between August and March, after accounting for seasonal changes. The only type of nonfarm employment that has been expanding, in recent months, is in State and local governments (see attached table on nonfarm employment).

The decline has been sharpest in manufacturing, where employment started to decline in January 1957 and has been falling for 16 months. In addition, jobs of nonproduction workers in manufacturing have begun to fall. The recession, however, has not been located in manufacturing alone, as an examination of employment trends indicates. Jobs in trade and services have not risen at all to offset the declines in other parts of the economy.

Indeed, employment in trade, as well as in manufacturing, mining, construction, transportation, and public utilities has fallen. Jobs in trade dropped 259,000 between August and March, after accounting for seasonal changes—reflecting the decline in retail sales. This is in contrast with 1954, when consumer activities and trade employment held up fairly well. It is in contrast, too, with 1949 when trade employment held more strongly than in recent months.

Wage and salary jobs in service and finance have remained relatively stable between August and March after seasonal adjustment. This is in contrast with 1954 when both finance and service employment increased. It is more in line with developments in service and finance employment in 1949.

An analysis of nonfarm employment trends, however, reveals the weakness of the present economic situation.

If we examine nonfarm employment from 1953 to 1957, we find an increase of 2.8 million. Employment in manufacturing fell 400,000 in that period—production worker employment dropped 900,000, while nonproduction jobs rose. There was a decline, as well, in mining, while in transportation and public utilities, employment was the same in 1957 as in 1953. The increase in nonfarm jobs came from other sectors.

Jobs in contract construction rose in 1955 and 1956, but then leveled off in 1957.

The significant increase in nonfarm employment between 1953 and 1957 came in trade (1 million), services (1 million), Government (700,000), and finance (300,000).

Since the start of the recession, however, the types of employment that were weak in the 1953 to 1957 period have continued to decline; contract construction has fallen, too, while the areas of employment that were strong in the past 4 years have also begun to weaken except Government, services, and finance.

An improvement in the overall employment situation in the period ahead will require substantial increases. Can we be confident of substantial employment increases in the coming year or so, even in the event of an economic pickup?

Manufacturing employment is all the way down—15.4 million in March, after seasonal adjustment. (See table on manufacturing employment.)

In durable goods, total jobs in March were the lowest since 1950, while production jobs alone were the lowest since 1949. There were fewer jobs in durable goods than in 1942.

In nondurable goods, total employment in March was the lowest since 1949, while production-worker jobs were the lowest since 1941.

With working hours lower than at any time since before World War

II, a pickup in output will first be reflected in an increase in working hours. It will take a substantial rise in manufacturing output to bring a significant increase in manufacturing employment. This is particularly true, because there is so much new and improved plant and equipment available to increase productivity substantially. Furthermore, even a relatively good-sized rise in output in the coming year or two will probably fail to bring the number of manufacturing jobs back to anything close to the 17.2 million who were employed in manufacturing in 1953—or even to the 16.9 million manufacturing jobs of 1956.

The employment picture in mining and on the railroads is rather similar to the job prospects in manufacturing. If anything, job prospects are worse in mining and on the railroads.

There were 3.5 million persons compelled to work part time in March—in addition there were 5.2 million totally unemployed. To approach a full employment level, now, it would be necessary to provide full-time work for most of those who are now totally unemployed and to create additional full-time job opportunities for those working part time. Furthermore, there are several hundred thousand youngsters who will be added to the labor force in June after the end of the school year. We will need some 4 million full-time jobs to absorb most of the unemployed, part-time workers, and additions to the labor force. This is merely a rough idea of the magnitude of the employment problem at present—a problem that will grow more serious as the recession continues, with further additions to the labor force and productivity apt to rise rapidly in an economic pickup.

What sectors of the economy, in the coming year, can be expected to absorb the unemployed and part-time workers, while providing job opportunities for new entrants to the labor force, as well as for those who may be displaced by technological changes?

Trade? Jobs in retail and wholesale trade have fallen rather sharply in recent months. Certainly a pickup in sales will raise the number of jobs in trade. But, can one expect jobs in trade to rise by 1 to 1.5 million in the coming year—when they increased only by 1 million in the 3 years before 1957?

Services? Employment in services has leveled off as a result of the recession. If economic conditions pick up, can we expect the number of jobs in services to increase by 1 to 1.5 million in the coming year—when these jobs increased 900,000 in the 3 years prior to 1957?

Even with Government employment rising, it is not likely that this sector will provide anything like a million jobs in the year ahead.

The difficulty is that the economy moved down sharply from a point at which unemployment was already relatively high. The deeper the recession goes, the more serious the employment problem grows—not only the present level of unemployment, but the possibility that unemployment will remain high for the next year or two, even with a pickup, unless output and sales bound up very sharply.

THE OPTIMISTIC VIEW—HIGH EMPLOYMENT

The optimists seem to be saying that there will be a turnaround from drastic inventory cuts to smaller inventory cutbacks in the next few months, to inventory building toward the end of the year—as a result of anticipated small increases in Government expenditures and some pickup in consumer spending. This would mean, according to their view, that output should begin to move up some time about midyear or in the fall and to increase slowly—with industrial production back to the predownturn level in the summer of 1959.

Without examining their premises, what are the optimists saying, in effect, about employment? Such a pickup—as any pickup—will first be reflected in increased working hours. Furthermore, productivity, which usually lags in the downturn phase of a recession, can be expected to rise sharply in a pickup. This occurred after the 1949 and 1954 recessions and can be expected to occur, probably more sharply, in a pickup from the present recession.

Employment, therefore, would probably rise very slowly in the event that the optimists are right. Unemployment would remain high—there would be about the same number or more jobless in the first months of 1959 than there were at the start of 1958—unemployment would be about 5 million or more in January and February 1959.

The optimists may or may not be too optimistic about their predictions of a pickup—in the light of current trends and the lack of a comprehensive antirecession program by the Government. But their optimism—as it relates to employment—is, by no means, good enough. To permit unemployment to remain that high in the coming year will be a tragedy for hundreds of thousands of families, and a waste of manpower and productive facilities.

It should be recalled that in April 1950, when industrial production reached the predownturn peak, seasonally adjusted unemployment was 1.4 million above the predownturn level—5.8 percent of the labor force in April 1950 compared with 3.7 percent in October 1948.

In May 1955, when industrial production rebounded to the predownturn peak, seasonally adjusted unemployment was 1.1 million above the predownturn level—4.3 percent of the labor force in March 1955, contrasted with 2.6 percent in July 1953.

Unemployment was already high when the present recession started—4.3 percent of the labor force, after accounting for seasonal changes. On the basis of past experience, unemployment will probably be about 6 to 6½ percent of the labor force, after the predownturn level of industrial production is reached. That would mean well over 4 million unemployed, if and when the economy reaches the predownturn level of industrial output within the coming 12 to 18 months.

It is for that reason that a comprehensive antirecession program by the Government is so urgently needed: to boost output and sales quickly and to speed up the time when industrial production is back to the predownturn level, to speed up the recovery so that the period of large-scale unemployment may be shortened substantially.

CONCLUSION

The trouble, at the moment, is that even this bleak prediction of the optimists appears to be without much foundation. The recession is continuing to deepen.

Industrial production which, in March, was almost 12 percent below August, seems to have fallen another 1½ percent in April. This, in turn, means a further decline in wages and salaries—the buying power of the consuming public.

The current economic trend—and the slow drift of Government policy—presents the threat of a continued deepening of the recession, with falling retail sales pulling down business activities even further. This is a threat of 6 million or more unemployed at the start of 1959.

It is not my function here to dwell on suggestions for a comprehensive antirecession program. Stanley Ruttenberg, director of research of the AFL–CIO, will present the organization's views on this subject in another panel. I do find it necessary, however, to state briefly that such an antirecession program must be centered on a tax cut for low- and middle-income families, an improvement in the unemployment insurance system to extend the duration and level of benefit payments, and a public-works program that will slowly provide jobs and the demand for goods at a time when business investment is in a continuing decline.

The economic policy task at the moment, it seems to me, is to halt the continuing economic decline promptly and to provide the basis for sound and rapid recovery. That task should come before any other consideration, in viewing the Government's economic policy responsibilities.

Relatively greater unemployment among men, particularly in ages 20 to 34

	March 1958	March 1957	March 1956
Total unemployed (million)	5.2	2.9	2.8
Percent of labor force	7.7	4.3	4.3
Unemployed males (million)	3.7	2.0	1.9
Percent of labor force	8.2	4.3	4.2
Unemployed men (20 to 24)	598,000	255,000	401,000
Percent of labor force	16.4	7.3	7.0
Unemployed men (25 to 34)	870,000	350,000	599,000
Percent of labor force	8.3	3.3	4.0

Source: Census Bureau.

Nonfarm wage and salary employment

Year and month	Total	Manufacturing		Mining	Contract construction	Transportation and public utilities	Trade	Finance	Services	Government
		Production workers	Nonproduction workers							
	Million	*Million*	*Million*		*Million*	*Million*	*Million*	*Million*	*Million*	*Million*
1953	49.7	13.8	3.4	852,000	2.6	4.2	10.5	2.0	5.5	6.7
1954	48.4	12.6	3.4	777,000	2.6	4.0	10.5	2.1	5.6	6.8
1955	50.1	13.1	3.5	777,000	2.8	4.1	10.8	2.2	5.9	6.9
1956	51.9	13.2	3.7	816,000	3.0	4.2	11.3	2.3	6.2	7.2
1957	52.5	12.9	3.9	840,000	3.0	4.2	11.5	2.3	6.5	7.4
August 1957 [1]	52.8	12.9	3.9	853,000	3.0	4.2	11.7	2.4	6.5	7.4
March 1957 [1]	50.7	11.6	3.8	769,000	2.8	4.0	11.4	2.4	6.5	7.5

[1] Adjusted for seasonal variations.

Source: Bureau of Labor Statistics and Federal Reserve Board.

The long decline in manufacturing employment

[In millions]

	Durable goods		Nondurable goods	
	Total	Production worker	Total	Production worker
1939	4.7	3.9	5.4	4.3
1940	5.3	4.5	5.4	4.4
1941	6.9	5.9	6.0	4.9
1942	8.8	7.6	6.2	5.3
1945	9.1	7.6	6.2	5.3
1946	7.7	6.4	6.7	5.7
1947	8.4	7.0	6.9	5.8
1948	8.3	6.9	7.0	5.8
1949	7.5	6.1	6.7	5.5
1950	8.1	6.7	6.9	5.6
1951	9.1	7.6	7.0	5.7
1952	9.3	7.5	7.0	5.6
1953	10.1	8.1	7.1	5.7
1954	9.1	7.2	6.9	5.4
1955	9.5	7.6	7.0	5.5
1956	9.8	7.7	7.1	5.5
1957	9.8	7.5	7.0	5.4
August 1957 [1]	9.8	7.5	7.0	5.4
March 1958 [1]	8.7	6.5	6.7	5.2

[1] Adjusted for seasonal variations.

Source: Bureau of Labor Statistics and Federal Reserve Board.

Senator DOUGLAS. Thank you very much, Mr. Goldfinger. The next statement will be by Mr. Robinson Newcomb.

STATEMENT OF ROBINSON NEWCOMB, ECONOMIC CONSULTANT, WASHINGTON, D. C.

Mr. NEWCOMB. Housing is facing an unfortunate concatenation of circumstances which may make a sizable increase in starts difficult to secure in 1958.

One difficulty is the fact that the housing market is in transition. The age distribution of the population has been such as to make the major housing demand in recent years a rehousing demand. That is, most of the recent net increase in the number of households has been occurring in families whose heads were 30 to 55 years of age. These are families whose incomes are rising and whose size is growing. They want bigger and better houses, and are able to pay for them. The rate of growth in the number of these households has been running at an apparent rate of over 425,000 per year.

We are now moving into a situation in which there will be a decrease in the number of households between the ages of 30 to 45, and an increase of less than 200,000 per year in the ages from 45 to 55. The net increase from 30 to 55 may be in the neighborhood of less than 175,000 per year, in contrast to the over 425,000 per year which has prevailed recently. But there will be an increase in the number of households over 55, and there should be an increase in the number under 30.

But the households over 55 and and under 30 want a different type of home from those from 30 to 55. They tend to want smaller and less costly homes. It takes builders, as it takes automobile manufacturers, considerable time to adjust to changing markets. Builders may have trouble adjusting in 1958.

The second difficulty this year is, of course, the economy. The policy of spreading the work is being replaced by a policy of concentrating work and concentrating unemployment. When employment drops, those who get hit are the young families, those with the least seniority. Young families who, under previous economic conditions, would be forming their own households and buying or renting quarters which suit them are hesitating to do so.

The number of births started rising after 1933. As girls tend to get married around the age of 20 and men around the age of 22, we might have expected marriages to rise by 1955. Actually, they did—they rose in 1955 and in 1956. But, by September of 1957, they turned down. The marriage rate in September was 10.4 percent; in October, 7.7 percent; in November, 7.7 percent; in December, 9.7 percent; and, in January 1958, 8.5 percent, below the rate a year earlier. So, family formation at the low-age groups is turning down instead of continuing to rise. With the sharp decline in the net increase in households from 30 to 55, and without the rise that had been expected in the younger age groups, the market in 1958 will be tough.

A third obstacle this year is the fact that, at a time when incomes are weakening, the industry which can provide the best bargains has a big advantage. In a boom time, almost anything may sell, but in slack times the bargain has the advantage. Productivity has not been rising in the home-building industry as it has in many other industries, so that it is somewhat more difficult to cut prices in the housing industry than elsewhere. As an illustration, a bricklayer, despite some reports to the contrary, lays as many bricks today as he did 50 years ago, but he does not lay much, if any, more. If productivity in other areas had risen no more than productivity in the bricklaying trade, our standard of living would be about where it was 50 years ago. The home buyer, therefore, has had to support the rising in the standard of living of the bricklayer without receiving more bricks per hour in exchange for the higher standard of living he is supporting. The slack economy of 1958 makes it more difficult to do this.

A fourth trouble is the fact that mortgage-interest rates are still up. They are not high because mortgagees are gouging the public. Home mortgages come largely from life-insurance companies, mutual savings banks, and savings and loan associations. Practically all of these institutions are, in effect, mutual institutions. They get their money from families of average incomes. The return on the investment which they make in home mortgages goes back to these families. When the flow of funds to such institutions which can be invested in home mortgages is inadequate, the obligation of these institutions to their owners require them to charge the current rate of interest on home-mortgage investments. As a result, in considerable part, of actions of Federal agencies, the interest rate in the home-mortgage field in higher than in other, somewhat comparable, fields. And the rate is not dropping as fast as it is in some other fields. Whereas the rate on bills has dropped by over 2 percentage points from the peak, the rate on mortgages has not dropped 1 percentage point.

As the interest rate is such an important factor in cost to the buyer, sluggishness on the way down means that housing costs are held up and buyers are weeded out by the high price.

Agencies of the Federal Government, not mortgagees, are responsible for a good proportion of the causes of high interest rates on home mortgages. One agency primarily responsible is the Congress. Congress set up institutions in the thirties designed to meet the home-financing problems of the thirties. Congress has tinkered with these institutions since then, but has not basically reoriented them to the problems of the fifties. May I point out one example? The newer, growing types of financial institutions find it very difficult to invest legally in home mortgages, and the Federal Government has taken positive steps to maintain that difficulty.

The tables at the end of my statement show sources of long-term investment as reported by the latest Bankers Trust Co. study, Investment Outlook for 1958. The institutions are grouped into three categories: (1) Financial institutions which favor home mortgages; (2) financial institutions which do not favor home mortgages; and (3) internal sources of nonfinancial institutions.

The first part of the table deals with the financial institutions only. The group which favors home mortgages had a net flow of $10.6 billion in 1953 and $12.6 billion in 1955. The flow dropped to $11.8 billion in 1957 and is estimated to approximate $12.2 billion in 1958. The second group—financial institutions which do not favor home mortgages—grew from $4.3 billion in 1953 to $5.5 billion in 1955, to $5.8 billion in 1957, and is estimated to reach $6 billion in 1958.

Institutions favoring mortgages grew from 1953 to 1955, but are not as potent now as they were in 1955. Institutions not favoring home mortgages grew from 1953 to 1955, and this year are expected to increase their assets 20 percent more than they did in 1955 and 40 percent more than they did in 1953.

If nonfinancial corporations are examined, it will be seen that their internal sources grew by nearly a third from 1953 to 1955 and by another 5 percent from 1955 to 1957. Their growth is expected to drop in 1958, but to remain somewhat larger than it was even in 1955.

From the standpoint of home financing, the implication is simple. Financial institutions that favor home mortgages are not growing to the extent that other institutions are growing. The laws have not kept abreast of the situation and have not made it as easy for the institutions that are growing to be as interested in home mortgages as in other types of investment. It has been pointed out often, for instance, that pension funds cannot invest readily in home mortgages.

It would be very simple to change this situation. One method would be for Congress to make it clear that pension funds and similar institutions could loan directly to insured savings and loan associations, and that these loans would be protected. Or these institutions could be authorized to deposit in savings and loan associations with their full deposit insured.

The purpose of insuring deposits up to $10,000 in savings and loans was to encourage individuals to invest in institutions making home mortgages. A problem now is to encourage the new type of financial institutions, such as pension funds, retirement funds of State and local governments, investment companies and others, to put their funds at the disposal of institutions investing in mortgages. Unless the laws keep abreast of the times, progress is hindered. I believe progress is being hindered now because laws are not facilitating the flow of funds from the newer financial institutions to home financing organizations, such as savings and loan.

If funds could flow readily from these new financial institutions to home-financing organizations, interest rates on home financing would drop, even though operating margins would remain the same. The cost to the home buyer thereby would be reduced. This would make VA mortgages more attractive because their rates would be more nearly equal to going market charges. Instead of trying to force people to buy VA's, we would be creating competition for these mortgages which would make them more interesting. With a bigger pool of funds flowing more readily to home-financing institutions, these organizations would find their resources greater, and their costs less. The homebuyer would benefit, and so would the economy.

Unless and until laws are changed to facilitate the flow of funds to financial institutions favoring home loans, interest rates on home mortgages will continue sluggish and drop only slowly. This will reduce the potential market for housing in 1958.

Without a bigger pool, interest rates will fall slowly, and the volume of starts will rise only slowly, if at all, for some time.

Sources of investment funds, selected financial institutions [1]

INSTITUTIONS FAVORING HOME MORTGAGES

	1953	1955	1957 [2]	1958 [3]
GROUP 1				
Life insurance companies [4]	5.2	5.9	5.2	5.4
Mutual savings banks [5]	1.8	1.8	1.7	1.7
Savings and loan	3.6	4.9	4.9	5.1
Subtotal	10.6	12.6	11.8	12.2

INSTITUTIONS NOT FAVORING HOME MORTGAGES

	1953	1955	1957 [2]	1958 [3]
GROUP 2				
State and local retirement funds	0.9	1.2	1.5	1.7
Investment companies	.4	.6	1.0	.8
Corporation pension funds [6]	1.7	2.1	2.7	2.7
Other insurance companies	1.3	1.1	.6	.8
Subtotal	4.3	5.0	5.8	6.0
Grand total	14.9	17.6	17.6	18.2
Percent of total in—				
Group 1	71.1	71.6	67.0	67.0
Group 2	28.9	28.4	33.0	33.0
Total	100.0	100.0	100.0	100.0
Internal sources of nonfinancial corporations	18.3	24.0	25.4	24.6
Group 1	10.6	12.6	11.8	12.2
Group 2	4.3	5.0	5.8	6.0
Total	33.2	41.6	43.0	42.8
Percent of total nonfinancial corporations	55.1	57.7	59.1	57.5
Group 1	31.9	30.3	27.4	28.5
Group 2	13.0	12.0	13.5	14.0
Total	100.0	100.0	100.0	100.0

[1] Taken from Bankers Trust Co., the Investment Outlook for 1958.
[2] Estimated.
[3] Projected.
[4] Increase in admitted assets.
[5] Increase in deposits.
[6] Net receipts.

Senator DOUGLAS. Thank you very much, Mr. Newcomb.

The discussion will be continued by Prof. Paul A. Samuelson of the Massachusetts Institute of Technology.

STATEMENT OF PAUL A. SAMUELSON, PROFESSOR OF ECONOMICS, MASSACHUSETTS INSTITUTE OF TECHNOLOGY

Mr. SAMUELSON. The present recession is the worst of our three postwar recessions. Already production, employment, and incomes have fallen more than they did in the recession of 1953–54. And the end is not yet in sight. The economy is still sliding downward in this second quarter of 1958.

Although there were signs of stagnation in the real output of the economy all through the year 1957, the downturn itself has to be dated from about last August. Many economists outside the Government—in business and in the universities—were alert to the developing recession and warned against it. But within the Government itself, there seems to have been a rather shocking failure to recognize the seriousness of the situation. And the Federal Reserve System, which was commendably quick in its timing during the 1953–54 recession, was so obsessed by the mild, steady increases in consumers' prices which characterized the economy since 1956 that it pursued too-tight money well into the fall of last year.

The administration, helped by its opposition in Congress, acted to keep the 1953–54 recession from becoming serious. The results were generally happy and raised the prestige of both America and the capitalistic system in the eyes of the uncommitted nations abroad.

This time the reluctance of the Government to admit the magnitude of the recession threat has inhibited needed constructive programs, and the resulting downward momentum of the economy has been noted with glee in the Soviet Union and has been watched with apprehension by America's allies.

Why this failure to diagnose the situation correctly and to recommend appropriate actions?

Administration spokesmen have shopped hungrily for the least sign of good news and so far have found mighty lean pickings. Indeed they have been thrown back onto the futile game of trying to discern decreases in the rate at which the economy's decline is beginning to decline—and the more desperate ones have had to look for "changes in the rate of change of the rate of change of the rate of change" and for "beginnings of the beginning of the end."

The most notable cause of the present recession has been the substantial drop in plant and equipment spending of business. In that such investment had been high ever since the war, and was particularly high in 1956–57, it is perhaps not surprising that excess capacity should have developed in a number of industries. Until the economy assumes a strong rate of growth, we may for a while face a relaxation of our investment needs.

Other contributing causes of the recession were the drop in 1957 defense spending and the turn to inventory decumulation which began late last year and which followed on 3 full years of inventory accumulation. Has the consumer also been to blame by saving too

25780—58——3

much? Although consumers have been buying less cars and consumers durables, they are today far from being on a buyer's strike. Actually, they are spending some 94 percent of their after-tax income—which is something of a recent record.

There is a distinct possibility that the economy will stop sliding downward before the end of 1958. The FRB production index may bottom out and perhaps begin a slow rise. This could be due primarily to lessened rate of inventory accumulation, to maintained construction, and to greater and greater expansionary Government programs. At best, part of the increase will be due to fictitious paper increases in prices and wages—a trend still going on despite the recession.

This may sound like an optimistic forecast. But even if realized—and it is almost an even bet that the economy will not live up to these expectations—this is still a pessimistic forecast. It assumes that plant and equipment spending will continue downward. It implies that seasonally adjusted unemployment will remain at its high current levels and perhaps steadily grow some as 80,000 new people come into the labor force each month. It assumes that much of the spark for our weak recovery will have come from Government efforts and not from private initiative. It assumes that we shall have a sizable Government deficit, as tax collections languish and expenditures mount. The deficit will be small though compared to a $450 billion potential GNP.

Such a forecast assumes also that we shall have some continuation of the "new inflation," which a number of us economists testifying last June before this committee rather aptly christened and characterized. The rise in money wages, and in lesser degree in prices, will be modest and will not touch off any avalanche of inflation-consciousness among the American people.

But what it will do is create dilemmas for conscientious Congressman, and I fear that overconcern over the admitted evil of price inflation will in some measure inhibit Government fiscal and monetary policies needed to restore us on the trend of progressively growing real national income.

Speaking for myself, and after much weighing of the relative evils involved, I would say that the primary concern at this time should not be with an intensification of inflation that may come tomorrow if high employment and production is restored.

But rather we should be most concerned to avoid the risk of a more serious slump's developing and to prevent the wastage of national resources implied by an attempt to fight the "new inflation" through deliberate creation of a "low pressure" economy in which overall demand is so weak that labor's attempt to get higher money wages will be punished by sizable unemployment.

In this case when our system must compete with the Soviet Union, that way—I fear—lies disaster.

Senator DOUGLAS. Thank you very much, Mr. Samuelson.

The next witness is Mr. Silbert, vice president of the Federated Department Stores, Cincinnati, Ohio.

STATEMENT OF MYRON S. SILBERT, VICE PRESIDENT, FEDERATED DEPARTMENT STORES, CINCINNATI, OHIO

Mr. SILBERT. Mr. Chairman, my prepared comments are concentrated on the trend and outlook for retail sales.

The recession in business, the drop in employment, and the reduction in hours worked per week have had an unfavorable impact on retail sales. This is the case in department store sales and in total retail sales of all types of stores combined. There has been an important drop from the peak of last August in both department store sales and total retail sales for the current spring of 1958 are below the sales of the spring of 1957.

First let us look at the current trend in department store sales. Easter was 2 weeks earlier this year, but if we take the combined figures for March and April together we can correct for this difference. For these 2 months combined the Federal Reserve figures for United States department stores will be approximately 3 to 4 percent below last year and about 7 percent below last summer's peak allowing for seasonal adjustment. This 3 to 4 percent drop from last year is after including sales of new branch stores so that the drop in the identical stores in existence the year before is still larger.

Now what is the current trend for all retail sales, and for types of retailers other than department stores?

Total retail sales were 2 percent below last year in March and were about 7 percent below last summer's peak. I have no figures for these total retail sales for April but believe the drop will be larger than for March and for March and April combined will be about the same as the 3 to 4 percent drop in department store sales.

There is a great deal of variation in the results in the different types of retail stores.

Food sales have shown substantial increases over the same months of last year, partly due to higher prices for food.

Drugstore sales are ahead of last year. The furniture and appliance group is moderately below last year, and the lumber, building, and hardware group is off more than moderately.

The most serious drop has been the sales of automotive dealers, and this includes the sale of both new and used cars.

The automotive total in dollars was 16 percent below last year in February, 18 percent below in March and off substantially in April.

The number of new cars sold has been very substantially under last year in February and March, and the sharp decreases seem to be continuing in April.

I am not close to the automobile field. The figures I have given are from published census reports and from trade publications. I refer to them, because in a picture of the retail trade as a whole they represent the largest decreases.

In making an estimate of sales for the balance of the year we would use the following approach:

1. We cannot count on an upturn in the present trend of sales until we see substantial evidence in the advance indicators that a stop in the decline is at hand and that an upturn in general business is in sight.

2. We do not have enough evidence of a stop in the decline of business nor any advance signs of an upturn. There is a possibility we may see such signs in the months ahead but we cannot see them at the present.

3. Until such advance signs of upturn do occur our estimate for the balance of the year is that total retail sales of all types for stores will continue about 3 to 4 percent behind last year. In July and August the year to year drop may be even greater.

Personal consumption may be somewhat better than the sales of all retail stores because they include rent in other sources. And that drop for the balance of the year may be about 2 percent, from a year ago.

4. An estimate of the trend of United States department sales would also be 3 to 4 percent behind last year after including the sales of new branches opened within the year.

These drops are after considering that the normal gain would be 3 to 4 percent over the previous year.

I have tried to analyze the trends in our company for clues as to how we might combat this recession.

In our company, Federated Department Stores, the March-April sales results have been approximately equal to last year in dollar volume, but these results include the sales of four new suburban branches that have been opened since last spring.

Some of our units have done better than others. We have tried to examine the results in the various cities in a search for steps that would counteract the nationwide volume trend.

One factor contributing to stronger volume in some of our stores has been the setting of vigorously competitive selling prices. An illustration of this has been the program in several of our departments selling large and small electrical appliances. Here there has been a streamlining of handling expenses so that we could reflect the savings in sharply lower prices. In many cases there has been an immediate and substantial response in increased sales. This same principal has been extended to other types of merchandise.

Here is another example of an effort to increase sales. In some of our downtown stores, we have recently changed to 2 night openings instead of 1 per week to make it more convenient for customers to shop. These additional openings have helped sales.

One other approach to greater sales volume can be explained only in general terms but nevertheless is of real significance. This is an intensified program in our stores to determine the direction of customer preferences so that we can offer customers particular kinds of merchandise that they wish.

In those of our stores that have been more skillful in doing this customer preference job volume has held up better. There still remains much for us to do in this field.

Senator DOUGLAS. We want to thank all of you for the testimony you have given.

We know it is a great sacrifice for you to come here.

Congressman Curtis.

Representative CURTIS. Thank you, Mr. Chairman.

I appreciate these papers very much.

I am tempted to ask a general question, though, in light of what seems to me a lot of conflicting statistics and certainly conflicting conclusions to be drawn from them.

The question I have in mind is the limitation of our economic statistics.

Now, I wonder just how I can get an appraisal from the panel on the subject of just how much can we rely on the statistics? What is their limitations?

Let me illustrate in one degree:

There have been comparisons between the 1949–50 recession and the 1954 and the present recession. And I think comparisons are very helpful. But let me confine the question to unemployment.

Would the panel agree that our statistics on unemployment are considerably better in 1958 than they were in either 1954 or 1949?

Haven't we been getting better statistics in that area?

Mr. GAINSBRUGH. I would agree.

Mr. GOLDFINGER. I would agree.

Representative CURTIS. Would anyone disagree?

I assume no one would.

Then, those who would address themselves to pointing out the limitations of our statistics on unemployment in 1958—and I think the panel would agree that there are considerable limitations—we could have a lot better statistics in that area, could we not?

Well, certainly, then, in pointing out those limitations of 1958, if the comparison of 1949 and 1954 is to have any meaning, we should point out the similar limitations in that period, should we not?

I might address that to Mr. Goldfinger and Mr. Samuelson, particularly Mr. Goldfinger.

Mr. GOLDFINGER. Yes, sir.

I have already taken that into consideration in the comments in the prepared text and in my oral presentation.

Representative CURTIS. Well, I did not find it. That is the reason I asked the question.

Mr. GOLDFINGER. The figures I refer to in my prepared text and in my oral presentation, sir, were based upon adjustments for the unemployment figures of 1948, 1949, and 1950, and for 1953–54, adjustments to bring the figures up to date, and comparable with the new 1957–58 figures based on the new definitions.

Representative CURTIS. Just how can you do that completely?

I mean isn't that really an estimate to a large degree? And isn't it a personal estimate rather than actually an economic statistic?

Mr. GOLDFINGER. These are estimates. All economic estimates are rough estimates.

Representative CURTIS. Some of it is based on samplings, of course.

Now, if the samples were not taken for your 1949–50 unemployment figures, you can only make an estimate to adjust. That is the point I would have you develop.

Mr. GOLDFINGER. The estimates I have used were made by the Census Bureau. The Census Bureau has made up estimates to bring all of these figures into some kind of comparable use.

On the basis of these comparable estimates of unemployment, unemployment in March as a percentage of the labor force, after adjustment for seasonal changes and other factors, was at a higher level than at any time either in the 1949 recession or in the 1954 recession.

Representative CURTIS. I note that in there you point out that the workweek has declined.

Wouldn't you agree that the decline in the workweek to a large degree has been the result of a technological development and higher standard of living rather than an indication of or in relation to unemployment?

I am talking about the trend now.

Mr. GOLDFINGER. The decline in the workweek in the past several months has been——

Representative CURTIS. No, no, I am talking about first over a period of years. Because it has been declining over a period of some years, has it not?

Mr. GOLDFINGER. If you are talking about the long pull, yes, sir, certainly.

Representative CURTIS. That is right.

Now, did you adjust your figure to include that long pull. In other words, that is what I am getting at. Did you compensate for that?

Mr. GOLDFINGER. The length of the workweek in the postwar period has largely been about the same. If you are talking about the workweek in manufacturing——

Representative CURTIS. Yes.

Mr. GOLDFINGER. The point I would like to make is that the decline in working hours and the increase in part-time employment—and it has increased substantially—in the past number of months has been due to falling demand and falling output.

Representative CURTIS. Well, I appreciate that.

All I am trying to do is relate it to these other trends. I am trying to see how much relation you have made to that, because one of the difficulties in following any economic figures is, No. 1, limitation of statistics and the fact that the statistics that we use today in comparison to previous years should be better and I think generally are. That is one of the problems.

The other is some of these longtime trends, like the decline of the farm economy in relation to the economy as a whole—I dare say a lot of these figures that have to do with the decline in various phases of manufacturing in industry are a longtime trend. Then, there is the other difficulty of taking absolute figures as opposed to percentage figures.

Absolute figures can be of value, but percentage figures for relationship are more meaningful. And I find, incidentally, as I was checking through your paper, it was very difficult to follow the trends, because you relate in your conclusions to a comparions of 1949, 1954, and 1958; yet many times you revert to absolute figures rather than percentage figures and also some of these other underlying long-range economic trends.

Mr. GOLDFINGER. I tried to give percentage figures, and I thought I did in all cases, sir.

Representative CURTIS. Well, of course, naturally, listening and reading very quickly, I could be in error.

I was influenced in asking this general question to some degree by Mr. Samuelson's opening statement. I began to wonder whether it was a political document or an economic report. There are so many adjectives and adverbs in it.

It struck me that Mr. Samuelson referred to "a shocking failure to recognize," "a reluctance to admit," and "hungrily looking for the least signs of good news," and so forth, which implied to me that you felt, Mr. Samuelson, that economics was a very exact science, and failure to do these things was not a difference in judgment in a field where so much judgment is necessary, but something that was done deliberately.

Do you think that the economic signs are so absolute that these things are done deliberately, this failure to look at this, or shocking failure to recognize, and so on?

Is that absolute?

Mr. SAMUELSON. I will speak as a professor of economics and not as a political expert.

Representative CURTIS. That is what I prefer.

Mr. SAMUELSON. And I realize that there are grave responsibilities upon public spokesmen, even to state a fact completely as it is a fact, because somebody may say that if a man in power admits this, then things must be much worse than he admits.

And so we expect any administration in power to lean over backward in interpreting current events. But I think that most economists in the universities studying the statistics of what has been happening since the end of the year and comparing that with the statements made have been a little bit shocked.

Take, for example, the March unemployment figures. The March unemployment figures, when you seasonally corrected them, looked to most technicians of the subject quite terrible. And yet the publicity releases which announced those suggested there was a tapering off.

Now, let me illustrate with a example.

Representative CURTIS. May I say this first:

That, of course, in this political scene you have to get the statements on the other side by allegedly responsible people in the opposition. And I might agree—in fact, I do agree—that there is a tendency in the political arena to make statements that are a little more extreme than economic judgment.

That is what disturbed me. Because, coupled with this statement you are making that maybe some official statement looked a little bit rose colored, there certainly were some statements of the other side that have been constantly in the press too which created a balance the other way.

Do you think those statements were also extreme?

Mr. SAMUELSON. I think that over the past years I have noted wolf cries of recessions which did not develop on the part of the opposition.

I think that the adversary procedure is an important part of our Government.

Representative CURTIS. I do too.

But this is an economic panel. That is why I was a little disturbed at the adjectives and adverbs you had in here, although the latter part of your paper I thought was very valuable. But you felt that—and you do feel now—as an economist that the statements made by the administration spokesmen have been this extreme in light of what economists do know and can rely on as economic indicators?

Mr. SAMUELSON. I think so.

And I think that I report a feeling of a large number of academic economists who are not not of any particular political complexion.

Representative CURTIS. Are there any on the panel who disagree with that observation of the general feeling of economists throughout the country, that there has been overoptimism expressed by the administration spokesmen?

Or do you all agree that there has been—do you agree with Mr. Samuelson's observation?

Mr. BASSIE. I would be inclined to agree with him, with considerable emphasis.

It seems to me that this decline can in no sense be interpreted as a figment of the statistics. There is something behind these statistics. Yet, even though we are going into this recession with our eyes open, there is a persistent refusal on the part of many executives to admit that the problem exists.

Representative CURTIS. Well, I might say this: You do recognize, I think—I do not think there is any one who says there is no recession—am I not correct in that?

The question is what extent? And where is it? Isn't that right?

Mr. BASSIE. Yes.

Representative CURTIS. The administration spokesmen say there is a recession, do they not, and have said so?

Mr. BASSIE. Yes.

Representative CURTIS. So, we are arguing about degree.

Mr. Gainsbrugh.

Mr. GAINSBRUGH. My comment would relate to the official releases as distinct from the interpretations. I do not find in the Bureau of the Census releases each month dealing with employment or unemployment or in Mr. Clague's comment speaking for the United States Department of Labor about the employment statistics they collect any tendency to be pollyannish or to fudge the figures.

You have to work awfully hard at times to find out what the trend is that is being reported. But it is there, if you dig for it. It is when you move outside the civil-service sector, I believe, that perhaps you start getting this overtone of adversary economics.

Representative CURTIS. What we are trying to do is to measure economic phenomena. And in doing that we have got statistics that help us, but which, of course, are limited.

It is just a question of how to do that and do it as carefully as possible.

Thank you, Mr. Chairman.

Senator DOUGLAS. Senator Hoblitzell.

Senator HOBLITZELL. Mr. Goldfinger mentioned about the younger elements being unemployed.

Isn't that caused more or less by the rigid seniority rules of unions?

Mr. GOLDFINGER. To some extent that would be true, yes.

It would result from the seniority rules in collective bargaining agreements. But it is also related to the relative lack of work experience on the part of the younger group.

And, furthermore, in almost any kind of recession, the younger people in the labor force or at least those with less service with a firm would tend to be laid off first.

The basic thing here is falling demand, falling sales and falling output.

As a result of that, these people have been laid off temporarily or permanently.

Senator HOBLITZELL. Is it true that the productivity, for instance, in the automobile industry, has not kept pace with the wage increases and the price of the cars have become such that perhaps people aren't willing to pay that price?

Mr. GOLDFINGER. I would challenge that statement, sir.

I would challenge this whole concept that has been bandied about concerning wages and productivity. If you are talking about economic statistics, one of the poorest series of economic statistics is the series on productivity.

The data are relatively poor. They are relatively poor for all kinds of reasons, because productivity is difficult to measure. Another thing is that even considering the difficulties in measuring productivity, whatever data are available would have to be analyzed. And unfortunately, all too many people who make comments about wages and productivity fail to analyze the productivity data.

For example, the productivity data of the last few years would have led one to believe that, for example, in 1956 and 1957 there was a serious slowdown—or at least in 1956, there was a very slow increase in productive efficiency in the American economy.

I think that conclusion is erroneous, at least in good part, because it is not based on a proper analysis of what the data are and of what data show. If you wish me to, I can go on and make some further comments on productivity.

Senator HOBLITZELL. During the Easter recess—I happen to be a banker, and I asked to take the desk two mornings. When you talk to people coming in, you are talking about what they are going to do in terms of purchases.

And when you talk about automobile purchases, they say "I am not going to pay the price. It is too high."

I am no economist, but I have been involved in mortgage and banking financing for over 20 years. You talk to the average citizen, and he feels that way about it. The gentleman from Federated mentioned it, that when you try to get the prices down and give the public something, they will buy.

That is true in the automobile industry. They price themselves out of the market.

The cost-wage spiral has made it difficult to give the public something they can afford to buy, with the rest of the economy not getting a similar increase.

Mr. GOLDFINGER. Sir, we in the trade union movement do not establish prices. Prices are established by business firms and not by the trade unions. So that if we are talking about prices, we are talking about business price policies and profits, in addition to costs.

Another thing is that the wage-cost is only one element of cost.

The wage rate, furthermore, is not the cost element. It is the unit labor cost that is the cost element. The wage rate has to be related to output. Furthermore, I think that if we were to make a—if we were to perform a serious examination of the cost factors in recent years—we would find that the major cost increases in recent years did not come from the production worker unit labor cost; this shows up in all kinds of data that you wish to look at.

The unit labor costs of production workers in manufacturing industries, for example, were only slightly higher in 1957 than they were in 1953.

I think that if you are looking for major cost increases, you would have to look elsewhere.

And the picture becomes more complicated.

You would have to look at depreciation costs per unit of output which increased substantially in recent years. You would have to look at interest payments per unit of output, which increased substantially in recent years.

You would also have to look at research and development costs per unit of output that increased substantially in recent years.

And some of those cost increases, as I said in my text, were more apparent than real, because they were due to bookkeeping changes rather than real changes.

Senator HOBLITZELL. I certainly don't believe that the management is blameless either in the automobile industry.

I would not agree that interest rates are the primary problem in the housing industry. I think that Congress itself has been unrealistic in not realizing that money has a right to earn in keeping with other commodities within our economy.

And I think that if the rates had been able to reach a common level of the market, that you would have had a demand for VA and FHA loans. They were prohibited from doing that.

You have to encourage people to save if you are going to create capital to reinvest in these new factories and new equipment and so forth.

That is all, Mr. Chairman.

Senator DOUGLAS. I have a question I would like to ask of the panel as a whole.

It seems to be generally admitted that there was a decline in production, employment, and investment from August until March, although there may well be different opinions as to the precise rates of decline or the precise changes in that rate of decline—this is virtually the end of April, and the most recent figures seldom go beyond the middle of March. I would like to ask this group if they would be able to express judgment as to what has happend since the middle of March?

You have access to current figures to a greater degree than we as legislators do. I wonder if we could have a quick poll of the group starting with Mr. Bassie.

Mr. BASSIE. I think the situation has worsened somewhat.

I used the figure in my opening statement that the seasonally adjusted rate of unemployment has increased to almost 8 percent. This is largely due to the fact that the weekly figures show no decline in unemployment, whereas the seasonal rate of decline should be about 8 or 9 percent during this month.

So in that respect, at least it has worsened. Other weekly data give the same indication, and there is no evidence in any of the figures I have observed of any definite improvement. As far as statistics are available, there is no indication of a turnaround.

Senator DOUGLAS. Mr. Butler.

Mr. BUTLER. Well, I would agree.

It is our estimate that there will be some further decline from March to April in production employment. However, it is our current view that April may well be the bottom.

Senator DOUGLAS. That is one of the next questions I am going to ask.

Mr. Friend.

Mr. FRIEND. I would agree that all the economic indicators I have seen suggest that there has been no recent improvement in the business situation. While March figures are not yet out, the rate of inventory disinvestment apparently has been proceeding at about the same rate as it did in the first 2 months of the year. And I would guess that unemployment seasonally adjusted would be over 7 percent in April, though I doubt that I would buy a figure as high as 8.

Senator DOUGLAS. Mr. Gainsbrugh.

Mr. GAINSBRUGH. I would point to two areas in which I think the scene has improved a little bit since March.

The first of these is Government spending and Government contract placement. My job takes me around the country a lot, and I have heard in area after area of the stimulating influence of contracts placed for missiles, for aircraft, et cetera.

Second, I would differ a little bit from Mr. Silbert in his reading of the curve for retail trade and department store sales. I think the department store sales thus far in April compare favorably with department store sales a year ago.

Senator DOUGLAS. Well, what would you say, taking all factors in balance?

Mr. GAINSBRUGH. I would buy Mr. Butler's picture for the second quarter, some further decline in the index of industrial production and in the gross national product figures.

Senator DOUGLAS. Mr. Goldfinger.

Mr. GOLDFINGER. I would think that industrial production has probably declined another 2 points between March and April, from 128 to 126, which would be a decline of about a little better than 1½ percent. With industrial production going down, that would mean to me that labor income and personal income has gone down again.

It would also mean to me that seasonally adjusted unemployment is up. And that seasonally adjusted employment is down.

There probably will be—and I think everybody should be aware of this—there is going to be an increase in total employment on the next few months. And that increase in total employment is largely related to what goes on on the farms. It is connected with weather changes.

Month to month changes of total employment are of no significance and of no meaning unless they are adjusted and analyzed. I would think that the increase in employment between March and April will be much less than seasonal.

Senator DOUGLAS. Mr. Newcomb.

Mr. NEWCOMB. Contracts in March—private contracts dropped 15 percent as against 10 percent for the 3 months. Public contracts did not drop as much.

So, there has been a slight improvement in the public segment. And that may be improved further as the highway program gets under way.

Senator DOUGLAS. Do you have the current figures for that?

Mr. NEWCOMB. Yes. These figures haven't been released.

Senator DOUGLAS. You gave March figures, did you?

Mr. NEWCOMB. That is right.

Senator DOUGLAS. You have no April figures?

Mr. NEWCOMB. No.

The Dodge figures on March will be released this week. That is the latest that have come out.

Senator DOUGLAS. You regard the Dodge figures as accurate, do you?

Mr. NEWCOMB. As the most reliable we have.

Senator DOUGLAS. Better than the Engineering News Index?

Mr. NEWCOMB. For this purpose, yes.

Senator DOUGLAS. Mr. Samuelson.

Mr. SAMUELSON. I suspect that there has been a continued slide in April.

Steel has been down. Automobiles have been down. It is hard to think that the Federal Reserve Board Index of Production, which was 128 when last reported, won't be down 1 or 2 points.

I think this is true of a number of indicators of current activity. Of course, the question that is often asked is not whether we continue to go down, but do we go down at the same rate as previously, because some lessening in that rate of decline ought to show itself before a reversal takes place.

I can shop as hungrily as the next man for good news. And you can pick up a few items. New orders—I have seen a private series that has bottomed out at a very low level, but is no longer falling. There is some evidence that machine-tool orders are up, probably related to the defense contracts that have been awarded.

You can certainly get a quarrel on the department-store sales adjustment of the last week or two as to whether there isn't a little bit of good news there.

The VA applications—I would like Mr. Newcomb's interpretation of that. But they do seem to be up slightly. And I thought that in March—I almost detected on a seasonally corrected basis, which is the only interesting basis—that disposable income had, at least temporarily, fallen only by negligible amounts. I do not know whether April will continue that good news or not.

Senator DOUGLAS. Mr. Silbert.

Mr. SILBERT. Mr. Chairman, there are a few composite indexes which are published weekly. One of them is the New York Times business index. And that shows lower for April than for March.

Moody's also publishes a weekly set of indicators. And those show no strengthening in April. They show a continued decline. One index that seemed to be slightly better is the initial claims for uninsured employment.

The total claims have not shown improvement. But the initial claims in some weeks in April look a bit better than they were before.

A most valuable indicator is that of new orders, published monthly, but 1 month after the end of each month. The latest Government figures for new orders are for the month of February. And I would be rash enough to suggest that the Government develop a weekly report of new orders, because it is the most important advance indicator. I do not think that will be too expensive to do. And I think that the leading companies would cooperate in that endeavor.

Senator DOUGLAS. I think that is a very constructive suggestion. We will see that it is passed on to the Subcommittee on Statistics.

Mr. SILBERT. Now, in retail sales, I think both March and April show the same trend, but the weather was not quite as favorable in March. One must take that into consideration.

Senator DOUGLAS. There is another question I would like to ask: I think it is, undoubtedly, true that the coming of better weather will mean an increase in construction and out-of-doors work, and, of course, an increase in farm labor.

Is there any danger that this seasonal upturn may be mistaken for a permanent upswing, so that both Congress and the administration will decide that no further action is needed? The figures for June will not come out until July. By that time it is possible that Congress may have adjourned and the time for action will have passed.

I will not poll you on this question, but do any of you feel that this is a danger, that the seasonal upswing may be mistaken for a basic improvement in the situation?

Mr. GAINSBRUGH. Not in this day and age of adversary economics.

Senator DOUGLAS. Well, the adversary is often discredited.

Mr. GOLDFINGER. I would hope Mr. Gainsbrugh is right. But I am afraid, Senator, that there will be a good deal of confusion and misinterpretation of this increase in employment that is to be expected in the next few months. And, without some picture of what the seasonal trends are and should be, I think we can get way off.

Now, for example, between March and April there is a normal seasonal increase in employment of about 600,000. So that any rise in employment between March and April, as reported by the Census Bureau, has to be measured against this normal seasonal rise of 600,000.

Now, between April and May, total employment should rise seasonally by about a million. And between May and June it should rise seasonally by about 1.2 million. And, unless we are aware of these seasonal factors here and measure the actual rise in employment against the seasonals involved, I think we can go way off.

Senator DOUGLAS. Does anybody wish to add any further comments?

Mr. NEWCOMB. I can make it even worse.

Senator DOUGLAS. We hope you won't do that maliciously.

Mr. NEWCOMB. Suppose the weather suddenly improves and we get the starts we should have had in January, February, and March, and they come in in April and May, people may say "Look, it is just shooting up."

Nobody knows what is happening. And it takes one figure here that BLS puts out that 890,000, and another figure here at 1,200,000, and they draw a line. They say maybe both of them should have been a million. That happens in highways. Public roads have been ready and able to let contracts for highways for a long time, but they are held back by their interpretation or the Treasury's interpretation of the Byrd amendment.

With that out of the way, they can start letting contracts in a hurry and get that volume that is ready to let out of the way. You cannot project a line drawn between the old and new rates here, either.

Senator DOUGLAS. Any other comments?

Mr. FRIEND. Isn't it true that unemployment will actually be up markedly by June if you don't seasonally adjust?

Mr. GOLDFINGER. Well, if you are talking about June, yes. In June you get a seasonal rise in unemployment, with the youngsters coming into the labor force.

But between March and April, and April to May, there are normal seasonal declines. For instance, from February to March there should have been a fairly substantial decline in unemployment. Instead, there was a 25,000 increase in unemployment, and some people took that as a cheerful sign.

Now, unless you measure the 25,000 increase in unemployment against the normal seasonal decline, there should have been a decline of about, I think, 300,000 between February and March—unless you take that into consideration, you can go astray. Between May and June, there should be, seasonally, a rise in unemployment.

Mr. FRIEND. You may actually have a real shock effect induced by the unadjusted unemployment figure in June.

Mr. SILBERT. Mr. Chairman, the Bureau of the Census has recently issued a special study on the seasonal factors in employment and unemployment. And I think it is particularly helpful at this time, because I am sure that they do not intend to confuse the figures, but to clarify them.

Senator DOUGLAS. Of course, you professional economists and statisticians are sophisticated people. We who have to legislate on the basis of these figures are unsophisticated people. I wonder if you could increase our degree of sophistication on that subject so that we might be forearmed against possible misinterpretations.

I have a general question that I should like to ask: Am I correct in understanding that generally there is a seasonal summer decline?

Mr. GAINSBRUGH. Yes. The level of employment will be seasonally lower in the summer and also the level of industrial production, particularly in July. Some of the shops shut down for several weeks for vacation purposes. All of that contributes toward a summer seasonal softening—nonfarm, that is.

Senator DOUGLAS. What tangible signs are there of a pickup toward the end of the summer?

Mr. Bassie.

Mr. BASSIE. Well I do not think there are in the present picture any tangible signs of a pickup. I think it is possible to infer that there may be such a pickup in the summer. The point concerning a possible shift in inventory policy has been emphasized by a number of speakers besides myself. This, it seems to me, is the best basis on which we might infer such a change. I do not go along, however, with the easy notion that we are going to get a reversal in inventory policy again.

What has usually happened in these situations in the past is that there is a first surge toward liquidation, such as we have had and then after a temporary lessening of pressure, there is another surge. Inventories tend to move this way. Short-lived reversals come rather abruptly sometimes. But in a series of steps as long as the recession lasts we can look for continuation of inventory liquidation at increasing rates.

Senator DOUGLAS. Does anybody else wish to make any comments?

Mr. FRIEND. I think that we are going to have somewhat lower economic activity in the second quarter of this year, and this seems to be the general consensus around this table. I do not expect the second quarter to be significantly different from the first quarter. Then I would expect a pick up in the third and fourth quarters.

The pickup however, will still be consistent with unemployment, seasonally adjusted, of about 7 percent of the labor force.

I do think that more than inventories are involved. Government expenditures will be going up after the first quarter for the rest of this year. There is some question about how much the rise will be, but that it will be significant seems clear.

When inventories will turn—that is, when inventory disinvestment will diminish—is more of a question. But judging from business surveys, and I think from a fairly realistic analysis of the business situation, there is a high likelihood that they will turn by some time in the third quarter.

Senator DOUGLAS. Anybody else?

Mr. GAINSBRUGH. I would look for an upturn in (*a*) Federal spending for goods and services at least by the third quarter of 1958. The orders have already been placed at an accelerated rate. Some of that is going to be paid for in increasing amount as the year moves along; (*b*) in the home building area in the second half; (*c*) for the end of the process of inventory liquidation. This to me is perhaps the most important single phenomenon to keep watching—the strength of end-product demand in the face of a massive inventory liquidation.

So far as I can see, the picture is still that we are chewing up goods (steel for example) at a rate faster than we produce them. Before the year is out, we may start filling more orders from new production rather than from off the shelf.

Mr. GOLDFINGER. It seems to me that there may well be some kind of upturn in the third or fourth quarter, but this is mystical. I mean it is mystical in the sense that it does not seem to be based upon any solid foundation. A lot of people feel there will be an upturn in the third or fourth quarter.

Some people felt there was going to be an upturn or bottoming out in March. It did not come.

We can keep feeling there is going to be an upturn in the third and fourth quarter, and perhaps there won't be. I think that this is a dangerous aspect of this situation. For example, we keep talking about the forthcoming turnaround from inventory reductions. But yet the inventory sales ratios are now higher than they were when they began to cut inventories.

I think that one of the dangerous aspects in this situation is what is happening to consumption. And I just do not understand why more people haven't been concerned about the consumption aspect of this recession.

I think that there is a danger here that while Government spending may be increasing and no doubt will be, that consumption may be pulling the economy down now and in the next few months.

We may get some further cuts in consumer spending. The reduction in consumer spending so far has been sharper, more drastic.

than in any other of the recessions—either the 1949 or the 1954 recessions.

This is particularly true in volume, after making adjustments for price changes. I think that this is an extremely dangerous aspect of the current discussion about the recession. Altogether too many people are thinking that there probably will be an upturn because there should be an upturn, and yet are leaving out the possibility that this thing may get worse. All of us hope for an upturn, but yet it may get worse because consumption may pull us down.

Senator DOUGLAS. Does anybody else wish to make a comment?

Mr. SAMUELSON. Examining the gross national product accounts and making a little model of prediction, I would be rather surprised if the money magnitudes by the third quarter do not begin to show at least a weak recovery.

I would expect the Federal Reserve Board index to bottom out by that time.

However, this is all on the basis of a prior reasoning with respect to inventory decumulation, such as has been used at this table.

If you actually examine the indicators which economists have looked at, thinking that they in the past have been early turners, we have the precedent that perhaps Senator Douglas will remember of the old Harvard ABC barometer which did so poorly in the 1929 crash.

But the philosophy in new garb has been carried forward by the Bureau of Economic Research under Geoffrey Moore and Arthur F. Burns. And if my memory is correct they have found about 7- or 8-time series which tend to show a lead over general business. This lead is not systematic and exact but there is some empirical basis for it.

My memory is faulty, and I will not remember all the items in it. But I will list some of them in the approximate order of their importance, as I see them.

Average hours worked per week; new orders; residential contracts—some indicator of housing activity; stock market prices; new incorporations; failure liabilities inverted. And perhaps I have missed 1 or 2.

Now, if you look at those, they have not up to this moment shown too cheerful a picture.

Senator DOUGLAS. Not stock market prices?

Mr. SAMUELSON. The stock market may be an exception in that for the first quarter of this year it is actually up.

Mr. GAINSBRUGH. Raw material prices.

Mr. SAMUELSON. What does that show? I missed that one.

Mr. GAINSBRUGH. Up.

Mr. SAMUELSON. Raw material prices up.

On the other hand, most of them are still downward. So it is surmise based upon our national income models that makes us think there probably would be a weak recovery in the last part of the year. But that does not imply a recovery of the unemployment situation necessarily.

Senator DOUGLAS. Mr. Silbert.

Mr. SILBERT. If we were to take as an example the two postwar recessions and use their length of time as a measure of when this recession might turn, there could be a turn after the middle of the year if we use just the length of those two previous ones.

Length of previous recessions is not an exact measure of this one. In addition we place reliance on advance indicators to get a clue. There has been a little bit of stirring in some of those advance indicators. But if we were to go on the theory of "Don't count your improvements until you see the whites of the increases," we would have to say that time has not yet appeared.

Senator DOUGLAS. I think I have been taking up a good deal of time in questioning.

Congressman Curtis.

Representative CURTIS. Thank you, Mr. Chairman.

I have been very interested in these discussions.

The one thing I find that no one has mentioned—I don't believe there is any mention in the papers either—but to me it is a very important and significant figure. That is the amount of money being spent on research and development, which is up higher this year than the highest year, which was 1957.

Now, here is what I gather from that: that evidently there is a basic confidence in the private sector of the economy. And, No. 2, aren't expenditures in research and development a forerunner of expenditures in capital investment and capital goods?

Does anyone care to comment on that?

And particularly how you—well, we will start around the table, Mr. Bassie—how you fit this figure of the amounts of money being spent on research and development.

Mr. BASSIE. Well, I don't have enough detail on that to really make any good analysis of it.

Representative CURTIS. Do you think it is a significant indicator? Is it an indicator that should be weighed in this?

Mr. BASSIE. I have never seen any basis for putting a favorable interpretation on research at this stage of the cycle. The studies of the cycle that make an analysis in terms of rates of innovation, or development processes, show that they fit very closely the theory of the cycle; that is to say, with a theory, not of stability, but of a very substantial wave motion. We have always had that factor playing a part in a major cycle.

And it also plays a part in the succeeding depression. So that it does not seem to me that this figure by itself is of considerable significance.

Representative CURTIS. I don't know—I am asking this for information—have we had any statistics of the previous recessions as to the amounts of money being spent in research and development which would give us any indication?

Mr. BASSIE. Well, my own observation of industry, which is admittedly limited, indicates that they are currently making cuts wherever they can. And this applies to research as well as to other things.

The exception in this field is largely in the area stimulated by Government contracts.

Representative CURTIS. No. I don't believe your figures indicate that. Someone can correct me.

I don't have them right in front of me. But although there has been an increase in Government and military, still there is an increase in the private sector. And the highest year was 1957 and 1958 is projected even higher. I think I am right.

Mr. BASSIE. I am aware that McGraw-Hill has got out a survey in which they show such figures. There is no breakdown on the source of the increases shown there.

Representative CURTIS. These aren't just McGraw-Hill figures, although they conform to it. It comes from about three different series, as I recall.

Mr. BASSIE. I do not believe there are any actual figures on 1958 expenditures.

There are only anticipated rates of expenditures. And to my knowledge the main source of them is McGraw-Hill, though I wouldn't question the fact that there may be other surveys of the same kind.

Representative CURTIS. Mr. Butler, would you care to comment on the general question as to the significance of the increase in expenditures in research and development?

Mr. BUTLER. Well, I think it has great significance for the longer-term future.

I think it will have some impact this year. The McGraw-Hill figures show an increase from 7.3 billion in 1957 to 8.3 billion in 1958. That will provide some increase in employment in that area.

Over the longer run, it seems to me that we are just beginning to get some of the fruits of the research that has been carried on since, say, about 1950.

I think one of the reasons for being confident about an upturn in business investments some time in 1959 is the amount that was spent on research and development in recent years.

Representative CURTIS. Mr. Friend, do you want to comment on that?

Mr. FRIEND. I would agree that research and development expenditures are extremely important in terms of their longer run implications. They are highly relevant to the matter of economic growth.

But I do not think that research and development expenditures are likely to be sufficient to turn around this recession or to have major implications for the recession.

Representative CURTIS. Even in respect to the fact that it might show business confidence—well, would you agree or disagree that an increased expenditure would indicate business confidence?

Or don't you think——

Mr. FRIEND. I just think we have better indicators of what is likely to happen to business spending in plans reported for plant and equipment expenditures and inventory investment.

In the same surveys where businessmen indicate the extent of their confidence in terms of research and development expenditures, they are doing it in more important terms—so far as any forecast of the next year is concerned—in their projected or planned investment.

Representative CURTIS. I think it was the McGraw-Hill figures I saw that asked for questions of when the various industries by groups expected to recoup the moneys spent in there.

And that is shown within, I think, 3 years in some instances. Maybe an average of 4 or 5 years. Which would indicate also that—although it might not have an immediate application—using the word "immediate" to mean monthly—but certainly in the period of several months it would have some effect.

Mr. FRIEND. I think one thing which is directly relevant to this question of longer run business confidence—by longer run I mean something beyond this year—would be the replies to the McGraw-Hill survey of business intentions to invest in plant and equipment over the next couple of years.

These data suggest, as I indicated earlier, a bottoming out in such investment at the end of this year. I do not think they can be taken with the same degree of seriousness as the shorter run forecast for the rest of 1958. But they suggest, at least at this stage, a considerable degree of business confidence in the subsequent period.

Representative CURTIS. They had a minimum figure and then a maximum figure for that.

Mr. BASSIE. May I add just a point to this discussion: These McGraw-Hill figures show an increase in planned research expenditures of about a billion dollars.

Of that, $800 million is in aircraft and parts. And another hundred million is in electrical equipment.

These are precisely the field which, as I indicated before, are stimulated by Government contracts.

Representative CURTIS. I agreed with you that a great deal of it was.

But I said even taking that out, there still was an increase. That was my comment.

Mr. Gainsbrugh.

Mr. GAINSBRUGH. I think the figures I gave you on capital appropriations and the figures that have been mentioned on plant and equipment expenditures already incorporate the beneficial aspects of the increase that has been going on in research and development expenditures.

Without them we might have had an even more severe cut.

To them I would add adherence by management to long-range planning. Those are two reasons why I think there is more likelihood of an earlier bottoming out in this particular decline in capital formation than in some of the other secondary postwar major recessions that Mr. Bassie made reference to.

Representative CURTIS. I have more comment on these McGraw-Hill figures.

I wish I could remember the other series.

Mr. GAINSBRUGH. National Science Foundation?

Representative CURTIS. No. But the other point I was going to make is that the McGraw-Hill figures of course are limited largely to large companies.

I personally felt for some time the real road in which we have seen the decline is in your small business field where they, because of the tight-money situation, had to put their plans on the shelf for growth and expansion. And I queried in my own mind and still do whether really there isn't more advance in the field of your small- and medium-sized businesses.

There is more growth going on there, it seems to me, than—percentagewise—than your established concerns. And if so it would be very valuable if we had some way of measuring what these smaller concerns are doing or are not doing.

Mr. GAINSBRUGH. The primary reason why I stressed tax incentives relative to research and development expenditures was in the belief that the area of shrinkage may have been in the medium- and smaller-sized firms. And if, for example, you allowed them to take research outlays out as a business cost and perhaps also as a special deductible item—that is, allow them to take it off twice for a limited period—it might be extremely stimulative to capital expenditures of small firms.

Representative CURTIS. I am happy to hear you say that because that has been my belief to the extent that I have a tax bill today, exactly that, sitting over in the Ways and Means Committee. Because I believed that is where a great deal of cutback has occurred; and it will be a very stimulating thing.

Mr. Goldfinger.

Mr. GOLDFINGER. I think the increase in research and development—to the extent that it is in the private sector and after taking out the Government research and development—that this expresses confidence in the long-run development of the American economy. And I am sure that all of us here would feel the same way.

However, I don't place too much weight on this development in terms of the short run. By "short run" I mean the next year or so. And that is the important factor here.

Furthermore, for example, if you look at research and development in terms of employment, it doesn't necessarily mean very much in terms of employment, because those salaries are high. It may mean that of the 400,000-odd college graduates this year, perhaps those who graduate with science and engineering degrees will find it a good deal easier to get jobs than the majority of graduates, with arts, social science, and business administration degrees.

Representative CURTIS. It wouldn't mean anything unless you could see that there is a connection between research and development, as I have suggested there might be, as a forerunner of capital—further capital expenditures.

If it were that: But——

Mr. GOLDFINGER. There is a fairly substantial lag of perhaps 3, 5, 7 years, something in that order. I don't know exactly. Some of these other gentlemen may have better ideas on the lag.

Representative CURTIS. Thank you.

Mr. NEWCOMB. I think this is the only basis we have for expecting a rise in 1959. With almost every family owning an automobile the only reason we are going to buy new ones is to get something better. And research and development expenditures is a major basis for continued sales, I think.

Representative CURTIS. That is the reason I mentioned it. But I was surprised at the panelists in all their discussions not mentioning it.

I think it is only one factor. But it seemed to me a very significant factor. I was surprised that it hadn't been mentioned which might indicate that maybe the professional economists tend to be pessimists by nature.

Could you comment?

Mr. SAMUELSON. We try to let cheerfulness break in occasionally. I think most of us at this table will be surprised if when we get a recovery from this recession in the short run it turns out to be sparked by the capital-goods spending on plant and equipment of business.

And it is on the basis of the actual facts of the situation and the surveys of plant and equipment expenditures that we make these projections.

The research and development is important for the long run but I don't think it will cause any of us to revise our figures upward even though our figures might have been lower had we information that research and development was being slashed.

Mr. SILBERT. I think the Congressman has touched on a very important factor over the long run. And why we in our long-range figuring count on an increase in the total economy of 3 to 4 percent a year over the next 10 or 20 years. And this growth of research has had a very definite factor in that.

Research usually requires a plant. When a new process is developed it requires a plant.

Over the years ahead research will lead to that. And this expansion will take place not only in manufacturing, but even in retailing there will be continued expansion in the suburban areas. We must not forget that manufacturing is only a small part of this total picture.

Also there will be expansion in utilities and transportation.

Representative CURTIS. Thank you.

I have one specific question. I didn't hear it mentioned.

In the housing field, of course, there has been quite a rise in applications in the FHA-VA sector, is that not true?

Mr. NEWCOMB. That is right, yes.

Representative CURTIS. Of course that is the basis on which it is assumed, I presume it is assumed, that that will reflect itself in the increased housing starts.

Mr. NEWCOMB. Yes.

Representative CURTIS. Is there any indication to discount that it might, that this increased application would not result in increased housing starts?

Mr. NEWCOMB. The average cost of housing is dropping. So far this year there has been an increase of 22 percent according to Dodge in the number of multifamily units. The average price of the multifamily is $8,000. The average price of the single family is about $14,000.

We are getting this change in the demand for housing in part because the middle-age family that wants to buy a big house is dropping out of the market.

The younger families want to buy or rent the smaller or middle-priced house. Last year the industry sold for permanent housing about 125,000 mobile homes.

Representative CURTIS. Would you give that again? I just heard that the other day. The mobile homes have been increasing; haven't they?

Mr. NEWCOMB. That is right. The young girls when they get married, don't want to give up an income until after the first baby comes. She wants only a small house to take care of.

There are two alternatives, multifamily apartment houses which are small, or a trailer. And the trailer isn't so small. It may be 50 feet long and 10 feet wide. But it is a home.

Representative CURTIS. May I interrupt you a minute? Do we include those in our figures?

Mr. NEWCOMB. No. When the census made their account in December of 1956 they found 24 percent more housing than the BLS had reported, without reference to mobile homes. If you add the mobile homes and everything else, the remodeling, additions, and alterations, you get a big difference. The BLS does the best it can do with the limited money it gets. Unless and until they get more money, they are stuck.

Here is an area of 125,000 or more per year, which is 10 or 12 percent of the total which BLS is reporting. So they are missing the total, we know now, by at least 10 percent, and we may guess by 25 percent or more.

If families shift from the $14,000 single family to the $8,000 mobile home, or from the $14,000 single family to the $8,000 multi-family home, the GNP is not going to rise as much as the number of units.

Representative CURTIS. I have one other little question. I think your paper mentions it. This is in regard to your marriage rates.

That is sort of seasonally adjusted; is it not?

Mr. NEWCOMB. Those figures were month by month comparison. So there would be no problem with that, sir.

Representative CURTIS. That is the previous year.

Mr. NEWCOMB. Yes.

Representative CURTIS. Of course those are very interesting figures over a period of many years, and certainly all of the projections of the thirties were thrown out of kilter because no one anticipated what was going to happen before.

It may be that economic factors are at play in that highly emotional area.

Mr. NEWCOMB. There were more people, as the census expresses it, "exposed" to the hazards of marriage in 1957 than in 1956 or 1955.

Representative CURTIS. Thank you.

Senator DOUGLAS. I want to apologize to the panel for keeping you so long, but I would like to have the privilege of addressing a final question to the group as a whole.

When the great depression of 1929 broke out there was fairly general agreement among legislators and economists that the proper governmental policy was to decrease Government expenditures in order to have a balanced budget.

We still have some very eminent colleagues who believe that we should have a balanced budget and therefore we should reduce expenditures.

Now, I would like to ask the panel to express themselves on this question. Should we decrease expenditures so that we may have a balanced budget, or is it desirable to have further stimulating action by the Federal Government, without going into the question as to whether this stimulating action should be a tax cut or public works?

How many subscribe to the predominant theory of 30 years ago, that we should balance the budget, and since income is falling, by reducing expenditures? How many feel that there should be stimulating action by the Federal Government either in the form of an increase in public expenditures or a tax cut which would involve increasing the Federal deficit?

Representative CURTIS. Would the gentleman yield for a third alternative.

Senator DOUGLAS. Yes, certainly.

Representative CURTIS. The third alternative is maybe the Federal Government has been messing around too much in the economy and not using more tax reduction but tax revision which would remove impediments to economic growth might be a third alternative.

Senator DOUGLAS. Mr. Bassie.

Mr. BASSIE. I would say definitely that we cannot afford to move toward a balanced budget at this time. It has been pointed out we are going to incur deficits even on the basis of present expenditures and tax rates. However, any increase in the deficit derived from falling taxes at fixed rates does us no good in this situation. It is built into the multiplier and merely reflects one aspect of the normal processes of the economy. It has a moderating effect, true, but that effect is already taken account of in our usual analytical procedures.

So I say we need additional stimulus.

Senator DOUGLAS. Mr. Butler.

Mr. BUTLER. Well, as I indicated in my paper, I think that Government expenditures will increase this year and probably increase next year again.

Senator DOUGLAS. Well now, you say "will increase." You accept this as a force of nature. But the Congress has the power to appropriate and if we put in a rigid program of economy we could reduce expenditures.

Mr. BUTLER. I think that there are things that Government needs to do which will produce an increase in Government expenditures in this period. I think that as a result we will have an increasing deficit and in a period of recession I think it is proper that Government run a deficit.

Senator DOUGLAS. You think we should blunder into the deficit or that we should have a planned deficit?

Mr. BUTLER. I am generally in favor of planning.

Senator DOUGLAS. Mr. Friend.

Mr. FRIEND. I think we should do two things. First we ought to have a big increase at this time in Government income-stimulating measures. Secondly we should adopt those measures which are as readily reversible as possible.

Senator DOUGLAS. Mr. Gainsbrugh.

Mr. GAINSBRUGH. I would endorse a countercyclical policy by Government which would lead it to build up surpluses in periods of prosperity so that it might resort to deficit financing in periods of recession.

Senator DOUGLAS. That is very difficult to do.

Mr. FRIEND. Very desirable, however.

Mr. GOLDFINGER. I would agree with what Mr. Gainsbrugh just said, but the problem at the moment is to get off dead center. We are not even at dead center. We are going down.

The problem is to get up and to get some kind of basis for a quick recovery. In that sense, I think we need tax cuts and we need additional Government expenditures and not blundering into a Government deficit as we have done in the past few months, because incomes have been going down and tax receipts have been going down.

I think the Congress and the administration should move in this direction, of a deficit finance policy at present, to get us into a quick recovery.

Senator DOUGLAS. Mr. Newcomb.

Mr. NEWCOMB. I hope the Federal Government will move quickly and definitely and once and for all.

In other words, end the uncertainty which is, I suspect, causing some hesitancy in making purchases today.

Senator DOUGLAS. Well, we could end uncertainty by saying we are going to balance the budget.

Mr. NEWCOMB. I would hope you would increase the Federal contribution; increase it promptly and definitely.

Senator DOUGLAS. Mr. Samuelson?

Mr. SAMUELSON. I think that both from the long-run and short-run point of view prudence does require the Federal Government to have an unbalanced budget when the private economy is weak. An attempt to reduce expenditure to the level of falling tax revenues would not even be a neutral act, because it would undo all the built-in stabilizers of our system and we would have a much worse situation than that mentioned by Mr. Bassie.

Senator DOUGLAS. Mr. Silbert.

Mr. SILBERT. Mr. Chairman, I think it is part of enlightened governmental approach to take effective steps to counteract the recession, even though it may result in an unbalanced budget.

There is one effect of those measures, that they help ultimately increase governmental income. I think that these measures, however, should be aimed at effectiveness rather than excess. And there is an opportunity for both the Congress and the Executive to develop a well designed program to counteract this recession.

Senator DOUGLAS. This is very interesting. Recently I reread the testimony of the eminent financiers and economic authorities who testified before the Senate Finance Committee in the months of January and February 1933 when the depression had been going on for over 3 years. With one exception their recommendations were that we should have a balanced budget; that we should reduce expenditures.

The only exception was an unknown banker by the name of Mr. Eccles.

In 1930 I advocated an unbalanced budget and a public works program of something like $4 billion. I was nearly read out of the economics profession.

I was almost regarded as insane by my brother economists. So now it is interesting to me, and reassuring, that after the passage of 25 years, we get almost a complete reversal.

Thank you very much.

(Whereupon, at 12:15 p. m., the subcommittee was adjourned to reconvene at 10:05 a. m., Tuesday, April 29, 1958.)

FISCAL POLICY IMPLICATIONS OF THE CURRENT ECONOMIC OUTLOOK

TUESDAY, APRIL 29, 1958

Congress of the United States,
Subcommittee on Fiscal Policy of the
Joint Economic Committee,
Washington, D. C.

The subcommittee met at 10:05 a. m., pursuant to adjournment, in room 212, the Senate Office Building, Hon. Paul H. Douglas (chairman of the subcommittee) presiding.

Present: Senator Paul H. Douglas and Representative Thomas B. Curtis.

Also present: Norman B. Ture, staff economist, and Roderick H. Riley, executive director.

Senator Douglas. This is the second day of the Fiscal Policy Subcommittee's hearings on the Fiscal Policy Implications of the Current Economic Outlook. As indicated yesterday, the purpose of these hearings is to bring out the facts about the Nation's current economic situation and to develop a careful appraisal of the economy's prospects for the remainder of this year and for 1959. These facts and analyses, we hope, will provide the basis for formulating realistic and constructive policies to end the recession and to restore the conditions in which economic growth may be resumed.

Yesterday, a panel of distinguished economists from business, labor, and the universities discussed with us the economic outlook for the remainder of this year and into 1959. Today, another group of eminent economists will concentrate on the comparative merits and limitations in the use of tax, expenditure, and monetary actions in arresting the recession and contributing to economic expansion.

We will hear the opening statements of each panelist before proceeding with a general discussion. Each of the panelists may submit for the record any prepared materials which he does not include in his opening statement.

I want to thank all of you most sincerely for the trouble which you have taken to come down here and testify. We appreciate it very much.

Our first witness is Dr. Gerhard Colm, chief economist of the National Planning Association. We are very happy to have you with us again, Dr. Colm.

Mr. Colm. Thank you.

STATEMENT OF GERHARD COLM, CHIEF ECONOMIST, NATIONAL PLANNING ASSOCIATION

Mr. COLM. Mr. Chairman, I will try to relate a discussion of various antirecession policies to the findings of yesterday's panel on the economic outlook. There was unanimity that economic activities in March–April were still contracting. With respect to the future, there seemed to be agreement that business investments in plant and equipment are likely to continue their decline well into 1959; that inventory liquidation is likely to slow down or come to a halt; and that Government expenditures are rising. There was no definite opinion expressed about the future course of consumer spending. Depending on the weights various panel members placed on these components, some concluded that the contraction is likely to come to an early halt and, possibly, would give way to a revival beginning later in the year. Others were uncertain about this prospect, and considered a further deterioration as a possibility.

Even the possibility that economic activity would continue at the present level for another year would give us a very unsatisfactory result. Economic activity at the present level would mean that we would be running at the first quarter 1959 at least $40 billion below a reasonably full employment level. Part-and full-time unemployment equivalent could rise to 8 million to 9 million workers by that time.

The belief in an early upturn is largely based on the assumption that Federal expenditures will show a very substantial early increase. Under legislation actually adopted or in advanced process of adoption, I would expect an increase in Federal expenditures of about $3 billion during the coming year. Larger figures which were mentioned at yesterday's hearing are likely only if additional programs are adopted and implemented with extraordinary speed. Estimates have been made that Federal expenditures might be up by a rate of $5 billion in the fourth quarter, 1958. These estimates are on the minds of people who believe that no further Federal action is needed. It should not be forgotten, however, that these estimates predicate substantial further action; this cannot, therefore, be an argument against action.

After having listened to yesterday's panel, it appears to me that it would be hazardous to base present policy deliberations on the assumption of an early and substantial upturn by forces of the market and present Government programs.

Under the Employment Act of 1946, the Government has the responsibility to "utilize all its plans, functions, and resources * * * to promote maximum employment, production, and purchasing power"—unless such policy would be inconsistent with "other essential considerations of national policy." These "plans, functions, and resources" include both fiscal and monetary policy. Monetary policy, however, cannot be expected to exert a significant immediate impact in a period of advanced recession. Business will avail itself of easier credit only if it expects that markets are about to expand again. Therefore, in the absence of an early upturn of market forces, a further increase in Government expenditure programs or a cut in taxes or some combination of the two are more effective policies for promoting market expansion.

What, then, are the respective merits of an increase in expenditures or a reduction in taxes? Regarding an increase in Government expenditure programs, it should first be noted that serious deficiencies exist in a number of the vital defense and nondefense functions of Government; for instance, education, research, health, water resources, urban redevelopment. From the viewpoint of providing for continued long-range economic growth and development, improvements in these areas deserve higher national priority than tax reduction. However, an increase in these programs requires considerable time for legislation and executive implementation, particularly for those programs which involve Federal, State, and local government cooperation. For this reason, increases in expenditure programs might not be initiated promptly enough to be immediately effective in countering the present recession. Nevertheless, some programs in these areas could be started promptly if legislative authorization were available. I feel it would be desirable, for example, to consider a program whereby the Government could assist State or local authorities in replacing the overaged school buses which are in use all over the country. Other such programs, once adopted, could exert an immediate and significant antirecession impact. An increase in well-timed and well-placed expenditures would, probably, be the most effective contribution to recovery.

It must be acknowledged, however, that the programs on which advance preparation has already been done and which could be implemented promptly are of limited magnitude and would, probably, not be sufficient for turning the current downswing or a continued sidewise movement into renewed economic expansion within a short period of time.

Tax reduction, in contrast to an increase in expenditures, can be adopted promptly and can be implemented promptly. Although we do not know exactly what portion of a dollar of tax reduction will be spent, whatever the effect, it will occur promptly. That is the great advantage of tax reduction.

In the past, I believed that a decision regarding the size of any tax reduction should be made when it is possible to estimate what action is likely to be taken on the Government's expenditure program. The expenditure outlook now appears approximately clear; therefore, the time for considering prompt tax reduction has come. Under present circumstances, I would favor an economic-recovery program which combines some further increase in truly meritorious expenditure programs, even though their economic impact may be felt primarily in the future, and some prompt tax reduction which could have an immediate effect.

The tax reduction that I would recommend would be 2-pronged, involving a reduction in the personal income tax on the first $1,000 taxable income from 20 percent to 15 or 16 percent, and a reduction or elimination of the excise taxes which were adopted during the war as an anti-inflationary measure. A $7 billion to $8 billion reduction in taxes might lead to additional consumer spending of $4 billion to $5 billion. These are not exact figures, just "guesstimates." This, plus the expected increase in Government expenditures by about $3 billion to $4 billion, and some increase in residential construction, would have a substantial stimulating effect on the slackening economy.

Although the expenditure element in such an antirecession program requires time for development and implementation, a recession—such as the present one—which is caused primarily by a contraction in business investments is not likely to be overcome in a short time. Moreover, some continued increase in essential Government programs will be necessary on its own merits for a period of years as well as justified in support of balanced and sustained economic growth.

One criticism of general tax reduction is that it does not give greatest benefit directly to those who are the victims of the recession, be they individuals or industries. Tax reduction is particularly suitable for counteracting the secondary effects of a recession, namely the general decline in consumer buying and in business confidence. By creating more favorable market conditions, tax reduction would assist business management in making the needed adjustments in investments, production, and pricing policies.

Some people further suggest that additional expenditure programs and tax cuts may reduce unemployment only at the price of leading to renewed inflation. Price stabilization, it is true, has not been achieved even during the recession. Nevertheless, maintaining mass unemployment is neither an effective nor a desirable remedy for the price rise. There are, I believe, other methods for dealing with the problem of inflation. Moreover, the problem of price stability will have to be dealt with whether or not we adopt an enlarged antirecession program.

With present levels of expenditure programs and assuming no tax cut, the budget deficit for the fiscal year 1959 may well be $8 to $10 billion. In the face of such a large impending deficit is it responsible fiscal policy to recommend a further increase in expenditures and a cut in taxes? The answer lies in the fact that a further drop in economic activity makes for a further drop in tax revenue and leads to an even larger deficit. If the Government cuts taxes, the deficit may grow larger for a period of time; but with the expected increase in economic activity tax revenues will begin rising. Seen over a period of 2 or 3 years, the budget is likely to have a substantially smaller deficit if an effective antirecession program is adopted than it would have without such a program and with the recession lingering on. Moreover, a budget deficit and a consequent increase in the debt resulting from a recession can at best mitigate the downswing. A deficit and a rise in the debt resulting from an antirecession program would—besides reducing the hardship and frustration arising from unemployment—create valuable assets in terms of much needed public works, consumer welfare, added capacity to produce, and a greatly enhanced international position.

A decision on economic policy must be taken in the face of economic uncertainties. We must recognize the possibility that we are proceeding on an erroneous appraisal of the outlook. In that instance it is necessary to decide whether greater harm would result from doing too little or from doing too much. I submit that in our present domestic and particularly international situation, the risk of acting with too little and too late is infinitely greater than the risk of acting too boldly.

(Dr. Colm submitted the following supplementary material:)

NATIONAL PLANNING ASSOCIATION,
Washington, D. C., April 7, 1958.

Note to Editors:

The National Planning Association is releasing herewith two statements pinpointing strong measures for checking the recession.

One deals with a long-range program for using idle productive resources and supporting continued economic development; the other suggests tax cuts which would be immediately effective.

NPA Chairman H. Christian Sonne, in releasing the statements, noted that even if the longer range program were put into operation immediately, its effect might not be felt for some time. The tax cuts, therefore, are needed as a quick-acting prop for the economy.

Approved by representatives of NPA's board of trustees and standing committees on agriculture, business, labor, and international policy present at a joint meeting this week, the statements recommend:

1. Government and private programs to put the unemployed portion of the labor force back to work.
2. Tax reductions which would at the same time expand purchasing power and improve the Nation's tax system.

A statement on the cost of unemployment points out that: "If production should remain at the level of the first quarter of 1958, a year from now it would run at $40 billion below the potential national output, as the size of the labor force and productivity per man continue to increase. At present, national production is running about $25 billion below the economic potential. This potential would increase by another $15 billion over a year's period."

All of this increased output capacity, the statement points out, would not be immediately available for expansion of defense, internal development, or foreign economic development programs. "For example, a $10 billion increase in Government programs, built up over a few years, would stimulate perhaps a 15 to 20 billion dollar increase in private consumption and business investment." Since these increases in Government expenditures would not materialize immediately, a rise in national programs of great urgency by approximately $10 billion would leave enough productive capacity to take care of the expected increase in consumer and business demand, the statement adds.

The statement suggests several possible programs the Government could initiate to help curb the recession, stimulate private spending, and make improvements in such fields as education, development of resources, and foreign economic development.

Mr. Sonne emphasized that: "These programs should be selected and timed so that they do not put excessive or conflicting claims on manpower and other resources, but rather contribute to the best possible use and development of the country's economic potential."

The second statement, on priorities in tax reduction as an antirecession measure, proposes tax reduction in two major areas:

1. Elimination of certain excise taxes—those imposed during World War II to limit consumption and lessen the pressure of inflation on scarce items, which are now no longer necessary. These would amount to about $4.5 billion, consisting of excise taxes on passenger cars, communication, transportation, and a variety of such items as electric light bulbs, photographic equipment, jewelry, toilet preparations, sporting goods, etc.
2. Reduction of individual income taxes, especially in the lower brackets. "The magnitude of the tax reduction which is needed as a recovery measure depends on the other recovery measures which may be adopted, particularly increases in expenditure and loan programs," the statement notes.

These two cuts in taxes, combined in a comprehensive antirecession program with longer range efforts to realize the Nation's potential productive capacity, should "achieve the broadest possible impact on purchasing power," the statement concludes.

Pointing up the necessity for action, Mr. Sonne stated, "A recession will unavoidably bring us deficits in the Government budget even if the Government would not increase expenditure programs and reduce tax rates. A deficit resulting from a deliberate increase in expenditures and/or a reduction in tax rates is preferable because it renders effective aid in overcoming the recession."

NPA JOINT STATEMENT ON THE COST OF UNEMPLOYMENT

In a dynamic economy in which some industries and companies and areas may be contracting while others are expanding, some unemployment of limited size and duration is unavoidable. Continually increasing and spreading unemployment, however, indicates that the market forces are failing to bring about the increases in some sectors of the economy which could compensate for contractions in other sectors. In that situation an antirecession program in which the Government plays a stimulating role is needed to halt a downward spiral and to stimulate recovery. In this statement we do not discuss a complete antirecession program. Rather we are concerned with certain less emphasized aspects of the costs of unemployment to the Nation.

Prolonged economic inactivity creates hardship, frustration, and despair for the unemployed; businessmen and farmers suffer losses, and communities experience financial difficulties. These direct personal and indirect economic costs of unemployment are heavy and widely distributed. While unemployment benefit payments and other social insurance income serve as a cushion to help maintain a minimum of purchasing power for those covered, even the best social security system can only mitigate the disruptive influences and the feeling of insecurity created by prolonged idleness. Experience during the recessions of 1948–49 and 1953–54 and during the current recession has demonstrated that our Federal-State unemployment insurance systems are inadequate. There is need to improve State laws in three major areas: (1) Coverage of a greater number of workers not now eligible for benefits, (2) increased benefits relative to current wages, (3) longer and more uniform duration of the period of benefit payments. Two decades of experience with a uniform national old age and survivors law, and the variable State unemployment compensation laws, demonstrate the desirability to make the unemployment compensation laws more nearly uniform through Federal standards. It is important that urgent steps be taken through appropriate executive and legislative action to cope with this critical situation.

Unemployment of people and facilities not only causes hardship at home; it also injures our allies and friends abroad and thus weakens the international position of the United States. We believe that these cost aspects are serious at this juncture of world events, and that they are not sufficiently recognized. While we are painfully aware of the personal stresses and strains which unemployment causes and the urgent need for the actions stressed above, this statement is concerned primarily with the losses which prolonged unemployment inflict upon the United States as a whole and upon the rest of the free world. These losses are especially serious at a time when the American economic system is challenged in a test with international communism. This tests puts an additional heavy penalty on the failure to do what needs to be done anyway. Long-lasting substantial unemployment could mean a serious loss in the competitive world struggle.

Many countries are critically dependent upon their trade with the United States, which is both the world's largest exporter and its largest importer. In particular, many of the raw material exporting countries that are striving for greater economic development find that in a period of declining economic activity they cannot buy all they need from the United States and possibly from other industrialized countries as well because of reduced markets or lowered prices for their exports. Thus, a severe and prolonged economic decline in the United States would spread to other countries, slowing down their economic development and increasing the unemployment and underemployment from which many of them already suffer.

The political and morale consequences abroad are fully as important as the economic effects. The Soviets have made important advances in recent years, which they never cease to attribute to the alleged superiority of communism. An economic setback of serious proportions in the free world would breed discouragement and disillusionment and thereby greatly ease the work of Soviet penetration and subversion. Economic difficulties in the United States would inevitably lower American prestige abroad, weaken our system of mutual defense alliances, and break down the resistance of the uncommitted and wavering nations to drift into the Soviet orbit. The consequences abroad of an economic depression in the United States are in themselves so serious that for this reason alone positive action is called for.

These social and international considerations, however, are not the only reasons for making an effective antirecession policy a matter of high national priority. The current levels of unemployment, production, income, and consumption leave a substantial amount of economic resources unutilized. This inactivity of men and machines is depriving the Nation of the opportunity for greater progress in economic growth and higher living standards. It represents a loss of income and production. It reduces economic opportunities for employment on the farm and in the factory. There are, for example, the loss of steel output of close to half of total steel capacity, the drop in overall industrial production of 11 percent over the past year and the substantial rise in the number of idle workers in a growing number of cities and towns throughout the country. Substantial unemployment means that we are foregoing the possibility not only of improving our national well-being but also of strengthening our position throughout the free world.

At the same time recent statements by experts both within and without the Government have suggested that we are devoting insufficient resources to many national priority programs: Our present military defense efforts are said to be inadequate; recommendations have been made for an expanded foreign economic development program, and serious deficiencies have also been pointed out in development programs in such fields as education, research, health, urban renewal, resource improvement, and conservation. Also, in many parts of the country the problems of water use and pollution control are becoming increasingly more critical. If deficiencies in these areas are permitted to continue, economic growth and development would be impaired. In the light of the present decline in investments, increases in these programs are not only feasible and desirable in themselves but would also promote economic recovery.

The National Planning Association believes that this is an opportune time to present a statement of some of the national priority requirements which could be undertaken through a fuller utilization of our production potential. There is a need to identify existing national deficiencies and to indicate where increases in private and public programs are urgent. Our Nation can ill afford the paradox of unfulfilled social and economic needs, on the one hand, and at the same time substantial amounts of unemployed production resources, on the other.

If production should remain at the level of the first quarter of 1958, a year from now it would run at $40 billion below the potential national output as the size of the labor force and productivity per man continue to increase. At present national production is running about $25 billion below the economic potential. This potential would increase by another $15 billion over a year's period. Not all of this increased output capacity would be immediately available for expanding programs such as for internal development and foreign economic development. For example, a $10 billion increase in Government programs, built up over a few years would stimulate perhaps a $15 to $20 billion increase in private consumption and business investment. Since it would probably take some time before these increases in Government expenditures could materialize, a rise in national priority programs by approximately $10 billion would leave sufficient productive capacity available to provide for the expected increases in consumer and business demand.

Increases in consumer and business demand both in the manufacturing industries and in services and on the farms would also contribute to putting the economy back on the road to economic recovery. Toward this end, agriculture, consumer, and industrial consumption could be stimulated through better marketing and distribution planning.

Properly timed an increase in Government programs could be undertaken without creating excess demand pressures or overstraining production capacity. Too great an increase in new and expanded programs, however, would involve the danger of solving the problem of recession by creating a problem of inflation. This could be avoided by proper management of the size, timing, and kind of programs to be initiated. Different types of programs stimulate different sectors of the economy and require different amounts and kinds of labor and capital. Methods would be needed which not only establish national priorities but also consider the availability of resources required to meet them.

Programs in some of these vital areas have been woefully neglected in recent decades. Improvements in these programs were limited during the periods of the Second World War, the postwar rearmament and inflation. The current decline in investment in plant and equipment presents an opportune time for bringing these programs up to needed levels. Moreover, an increase in Government expenditures over the next several years could take place without making it necessary to raise taxes. At higher levels of economic activity tax yields would increase even with no change in existing rates. With a $25 billion rise in gross national product, Federal tax revenues could increase by close to $5 billion under present rates. However, since Government expenditures in the initial period would probably increase faster than tax revenues, a temporary Government budget deficit could be expected. If the recession were allowed to grow, however, much greater and prolonged deficits might have to be faced.

The list of possible programs which could be initiated in a period of recession is numerous. These programs encompass the broad field of education including both basic and applied research as well as schools, colleges, and teachers; the field of resource development and conservation, including water supply; flood control; urban redevelopment and highway construction; and the field of international economic development and of our economic relationships with other countries. The need for improvements in some of these areas is urgent and pressing. We present here only a few examples of programs which could be undertaken or expanded.

Education: As a result of overcrowded classrooms and obsolete and substandard school buildings, there is projected for the fall of 1958 a shortage of an estimated 128,000 classrooms in the public elementary and secondary schools in the country. To overcome this deficiency would require approximately $6 billion of additional expenditures. Nor would this program provide for obsolescence and possible loss, through fire and other hazards, of school buildings, nor for the expected increase in student enrollment in the years ahead.

In addition to these public school needs at the elementary and secondary school level are the shortages in facilities at the college and university level. The construction needs in these areas are large and can be expected to increase significantly with expanding population and as more people seek advanced education and training.

Coincident with the need for more classrooms is the need for more teachers. States and local communities have estimated that an additional 135,000 qualified teachers are required in the primary and secondary schools. With total enrollment in schools and colleges expected to increase each year by close to 2 million students, the need for teachers will grow. To attract and retain sufficient qualified personnel, salary scales in many States and local communities will have to be raised substantially.

Development of resources: With the increase in industrialization, more extensive irrigation, greater population and higher living standards, has come a rapid rise in water utilization and consumption. As a result, the problem of providing an adequate water supply has become widespread and in many areas has forced curtailment in the use of water. The misuse of water resources through water pollution further restricts the use and possible reuse of water without undergoing purification. The Department of Commerce has estimated that an increase in construction expenditures of almost $10 billion is needed to provide adequate water works, purification plants, and sewage systems.

Also, urgent programs are needed to correct the deterioration which plagues our cities and to provide for the rapid increase in public services required by our rapidly expanding metropolitan areas. The problems of urban redevelopment, housing, transportation, recreation facilities, air-pollution control, and the problems of depressed economic areas underline the importance of adopting bold measures for urban redevelopment and metropolitan planning. Spread over the coming decade, highly useful and necessary redevelopment projects would require an additional $7.5 to $10 billion annually.

Foreign economic development: Many countries of the world are currently striving to achieve major economic as well as social and political transformations. In most instances, their own resources must be supplemented by those of other countries if they are to succeed. A number of studies have indicated that these lesser developed nations are in need of development assistance in excess of what they now receive from the more industrialized nations. These studies have led to suggestions that the United States foreign economic development program make available additional funds—of the order of $2 billion—principally for extending development loans abroad. It is in the national interest of the United States that an adequate degree of economic development be promoteed in these countries. Supplying funds for economic development abroad increases exports of American products, thereby providing additional employment at home while aiding other countries.

In the present situation the need for greater progress in these areas is so urgent that some of the available resources of men and machines should be used for making up these deficiencies. Coupled with prompt tax reduction, which we discuss in a separate statement, these programs would contribute to economic recovery and the resumption of economic growth.

MEMBERS OF THE NATIONAL PLANNING ASSOCIATION BOARD OF TRUSTEES AND STANDING COMMITTEES SIGNING THE STATEMENT, "THE COST OF UNEMPLOYMENT"

H. Christian Sonne, chairman-president, South Ridge Corp.
Stanley Andrews, executive director, national project in agricultural communications, Michigan State College
John A. Baker, legislative secretary, National Farmers Union
Solomon Barkin, director of research, Textile Workers Union of America, AFL–CIO
William L. Batt, Philadelphia, Pa.
Murray R. Benedict, professor of agricultural economics, College of Agriculture, University of California
John D. Black, professor of agricultural economics, University of Minnesota, Harvard University
Otis Brubaker, director, research department, United Steelworkers of America, AFL–CIO.
John F. Chapman, associate editor, Harvard Business Review
Myron Cowen, Washington, D. C.
August Dahme, Aberdeen, S. Dak.
Clinton S. Golden, Bucks County, Pa.
Marion H. Hedges, Washington, D. C.
Oscar Heline, Marcus, Iowa
Kenneth Holland, president, Institute of International Education
D. M. Levitt, president, D. C. A. Food Industries, Inc.
Helen Hill Miller, journalist, Washington, D. C.
Lowry Nelson, Institute of Agriculture, University of Minnesota
Miles Pennybacker, president, Voltarc Tubes, Inc.
Eric Peterson, general secretary-treasurer, International Association of Machinists, AFL–CIO
Clarence E. Pickett, honorary secretary, American Friends Service Committee
Beardsley Ruml, New York City
Stanley H. Ruttenberg, director, department of research, AFL–CIO
James S. Schramm, executive vice president, J. S. Schramm Co.
Boris Shishkin, director, civil rights department, AFL–CIO
Ted F. Silvey, national AFL–CIO education department
Lauren K. Soth, editor of the editorial pages, The Des Moines Register & Tribune
Herman W. Steinkraus, president, Bridgeport Brass Co.
Wayne Chatfield Taylor, Heathsville, Va.
Howard Tolley, Alexandria, Va.
Ralph J. Watkins, director of economic studies, The Brookings Institution
Robert A. Whitney, president, Marketing Audits Institute
Arnold S. Zander, international president, American Federation of State, County & Municipal Employees, AFL–CIO.

NPA JOINT STATEMENT ON PRIORITIES IN TAX REDUCTION AS AN ANTIRECESSION MEASURE

A good antirecession program should not only be effective in stimulating business activity, but at the same time it should also be of lasting national benefit. Thus an increase in Government expenditures should not only create jobs and incomes; it should also contribute to making up deficiencies in Government programs.

In a similar way, tax reduction should be so arranged that it contributes to economic recovery and at the same time leaves us with a better tax system than we had before. We believe that because of the urgency of certain national requirements selective increases in expenditure programs should be part of the program to fight against the recession. This refers to truly high priority pro-

25780—58——5

grams. However, prompt tax reduction is also needed to support purchasing power. Tax reduction can play an effective role in an antirecession program because it can be adopted without delay and would have widely dispersed effects on the economy. Also by adopting a carefully selected program of tax reduction our tax structure can be greatly improved.

In this statement we are not proposing a tax-reduction program by specified dollars and cents. The magnitude of the tax reduction which is needed as a recovery measure depends on the other recovery measures which may be adopted, particularly increases in expenditure and loan programs. Instead, we address ourselves to the type of tax reductions which should be included in a tax-reduction program.

High priority should be given to the elimination of miscellaneous excise taxes, particularly on passenger cars, communication, transportation, and a variety of such items as electric light bulbs, jewelry, leather goods, toilet preparations, sport goods, and so on, but excluding the taxes on alcohol and tobacco, and on motor fuel and related items most of which are allocated to the highway trust fund. The revenue of these miscellaneous taxes has been running at an annual rate of $4.5 billion. If they were removed some part of the revenue loss would be recovered by increases in revenue from other tax sources. These excise taxes which we propose for elimination were imposed during the war years for the purpose of restricting consumption. There is no reason for continuing these taxes under present conditions. Their removal would help in stimulating consumption and reducing costs of transportation and communication.

A comprehensive antirecession tax program would be most effective if it includes the elimination of certain excise taxes with a reduction in the individual income tax in order to achieve the broadest possible impact on purchasing power.

For a reducton of income taxes, particularly in the lower brackets, two main proposals deserve consideration. Both have similar effects on mass purchasing power. One proposal provides for an increase in the tax-exempt limit; the other provides for a splitting of the first $2,000 taxable income bracket and would lower the standard tax on the first $1,000 taxable income.

An increase in personal exemptions by, let us say, $100 would take about 4 million taxpayers off the income-tax rolls and would result in a revenue reduction of $2.8 billion. Of the total reduction in taxes, 40 percent would favor taxpayers with incomes of less than $5,000; 47 percent would go to taxpayers with incomes between $5,000 and $10,000; 13 percent would benefit taxpayers with incomes over $10,000.

A proposal to reduce the present tax on the first $1,000 taxable income from 20 percent to 16 percent would likewise result in a revenue loss of $2.8 billion. The decrease in taxes would be distributed by 40 percent, 50 percent, and 10 percent, respectively, among the income brackets of below $5,000, $5,000 to $10,000, and over $10,000.

The tax reduction through splitting the first bracket would not reduce the number of income-tax payers. To that extent it would leave a broader tax base. Both methods could be made effective within a short time through the payroll deduction mechanism.

Promptly eliminating miscellaneous excise taxes and reducing personal income taxes for the lower income brackets would effectively contribute to recovery and at the same time leave us with a greatly improved tax structure.

We hasten to add, however, that these measures would not exhaust the list of highly needed tax revisions. The combination of the highly fictitious top bracket rates in the income tax plus the tendency of gradually widening loopholes calls for a thorough revision of the tax structure. Also, the treatment of dividends in the individual income tax and the relationship between individual and corporate income taxes call for reexamination. Such revisions, however, require longer deliberation and, therefore, are not suitable elements for the current antirecession program.

In this statement we have confined the discussion to those proposals which offer the most desirable combination of recovery measures and tax improvement. These measures could be adopted promptly.

MEMBERS OF THE NATIONAL PLANNING ASSOCIATION BOARD OF TRUSTEES AND STANDING COMMITTEES SIGNING THE STATEMENT, "PRIORITIES IN TAX REDUCTION AS AN ANTIRECESSION MEASURE"

H. Christian Sonne, chairman of the board, president, South Ridge Corp.

Stanley Andrews, executive director, national project in agricultural communications, Michigan State College

John A. Baker, legislative secretary, National Farmers Union
William L. Batt, Philadelphia, Pa.
Murray R. Benedict, professor of agricultural economics, University of California
Otis Brubaker, director, research department, United Steelworkers of America, AFL–CIO
Myron M. Cowen, Washington, D. C.
August Dahme, Aberdeen, S. Dak.
Clinton S. Golden, Solebury, Pa.
Oscar Heline, Marcus, Iowa
Marion H. Hedges, Washington, D. C.
Kenneth Holland, president, Institute of International Education
Albrecht M. Lederer, A. M. Lederer & Co., Inc.
D. M. Levitt, president, D. C. A. Food Industries, Inc.
James G. Maddox, Washington, D. C.
Helen Hill Miller, journalist, Washington, D. C.
Lowry Nelson, institute of agriculture, University of Minnesota
Miles Pennybacker, president, Voltarc Tubes, Inc.
Eric Peterson, general secretary-treasurer, International Asssociation of Machinists, AFL–CIO
Clarence Pickett, honorary secretary, American Friends Service Committee
Beardsley Ruml, New York City
Stanley H. Ruttenberg, director, department of research, AFL–CIO
James S. Schramm, executive vice president, J. S. Schramm Co.
Ted F. Silvey, national AFL–CIO education department
Lauren K. Soth, editor of the editorial pages, the Des Moines Register & Tribune
Herman W. Steinkraus, president, Bridgeport Brass Co.
Wayne Chatfield Taylor, Heathsville, Va.
Howard R. Tolley, Alexandria, Va.
Ralph J. Watkins, director of economic studies, the Brookings Institution
Robert A. Whitney, president, Marketing Audits Institute
Obed A. Wyum, farm program consultant, Farmers Union
Arnold S. Zander, international president, American Federation of State, County & Municipal Employees, AFL–CIO

Senator Douglas. Thank you very much, Dr. Colm. Our next panelist is Prof. James Duesenberry of Harvard. Mr. Duesenberry, we are very happy to have you with us.

STATEMENT BY JAMES DUESENBERRY, DEPARTMENT OF ECONOMICS, HARVARD UNIVERSITY

Mr. Duesenberry. Mr. Chairman, in my statement I will discuss the outlook under present legislation very briefly and then consider the changes which would be brought about by tax reduction.

We have probably reached or nearly reached the end of the reduction in income. The best guess is that income will remain fairly constant for some months and begin to turn up before the end of the year.

Business investment will probably decline for the rest of the year, but it now appears likely that the reduction in business investment will be somewhat more than offset by increasing expenditures of $2.5 to $3 billions by the Federal Government and a similar amount by State and local governments. It is very unlikely that the rate of disinvestment in inventories will become any greater. Housing investment is not likely to decline further and may rise a little. Consumer expenditures have already declined about as much as one would expect for the reduction in disposable income which has taken place, assuming that some action to prevent large scale exhaustion of unemployment benefits will be taken.

Aside from the possibility of further decline in the foreign balance there is no strong net factor working for a further decline in income.

It is much more difficult to say when income will begin to rise. The big factor is inventories. Outside of inventories there is no very strong positive factor in the situation. But inventories declined at a rate of $7.5 billions per year during the first quarter. At worst that rate might continue for the rest of calendar 1958 which would bring inventories down in proportion to the reduction in final purchases of goods.

But inventories in durable manufacturing respond to changes in orders as well as in sales. Orders for capital goods have already declined while orders connected with increased Government expenditures did not rise until March. There is some hope then for an improvement in inventory investment before the end of the year, but the timing is very uncertain.

When inventories do turn around there should be a fairly strong recovery. By mid-1959 gross national product should have reached the neighborhood of $440 billions even if business investment remains at the levels forecast for the end of 1958. The rise in income should bring about positive inventory investment and a recovery of plant and equipment investment. Income should be rising rapidly in 1959, but in my view demand is not likely to outstrip productive capacity with present Government policies.

Thus present Government policies look fairly adequate to bring about some recovery in 1959 but will probably leave us with substantial unemployment for the rest of this year and at least part of next.

That brings us to the question of tax reduction as a remedy for the short run problem. I shall first discuss the short run effects of a tax reduction and then return to the longer run problem.

A tax cut given to the low- and middle-income groups would, I believe, have a substantial and fairly immediate effect on consumer expenditures. On the average a $1 change in disposable income results in a change in consumer expenditures of about 95 percent. But in the first quarter of the change consumer expenditures rise only about 40 percent. Further increases in expenditures would take place in later quarters but it takes at least a year before the change in income has had its full effect on consumption. An increase in consumer expenditures will, of course, cause a further rise in disposable income and consumption. In the short run, however, those secondary effects would be very small because so much of the increased income would go into increased profits, taxes and reductions in transfer payments. Under ordinary circumstances then, an increase in disposable income at an annual rate of $5 billions effective July 1 would not increase the annual rate of expenditures by more than $3 billion by the end of calendar 1958.

The statement above is based on the average relation between changes in disposable income and changes in consumption. But consumer expenditure at given levels of disposal income is subject to variations which, though small as percentages of income, are fairly large by comparison with quarter to quarter changes in disposable income.

It sometimes happens, therefore, that income goes up while consumption remains unchanged or occasionally even goes down. At other times consumption rises much more than disposable income. That is so because other factors which are difficult to measure influence consumer expenditures.

It is by no means certain then that a $5 billion tax cut will be followed by a $3 billion increase in consumer expenditures. The nonincome factors working on consumption will be at work whether there is a tax cut or not so that we have a better right to say that a tax cut will make consumer expenditures $3 billion larger than they would be without the tax cut.

However, one systematic factor must be noted. When disposable income declines consumption usually declines by a smaller amount and that is what has happened in the last few months. The reverse is true when income rises. We may therefore expect consumption to rise by rather less than $3 billion in the first 6 months after a tax reduction of $5 billion a year. I hesitate to say how much less because the distribution of gains on disposable income from a tax cut is not the same as the distribution of losses in income from unemployment.

Nonetheless the short-run effects of a tax reduction would be substantial. Unfortunately a large part of the effects would be in the wrong place. A large proportion of the decline in manufacturing employment is in the durable goods sector.

Only a fraction of the additional consumer expenditures generated by a tax cut will go to durable goods industries. On the average durable goods account for only about 15 percent of consumer expenditures. But variations in durable goods purchases make up a much larger fraction of the consumer response to short run changes in income. Because of the variability of durable goods expenditures it is difficult to make a reliable estimate of the effect of a tax cut. But it would not be wise to count on an increase in durable goods expenditures of more than, say, $1.5 billion within 6 months after a $5 billion tax cut.

Thus the short-run effects of a tax cut of the order of $5 billion will do an appreciable amount of good in the places where it counts but will not by itself solve the unemployment problem of the next 6 months.

Long-run effects of a tax reduction: Given a recovery of income from other sources and given time for adaptation the effects of a tax cut on consumer expenditures will be much larger than those indicated above. Ultimately a tax cut of $5 billion given to low- and middle-income groups will lead to a direct increase in expenditures of almost the same amount. The resulting additions to income will probably generate a further increase in consumer expenditures of another $5 billion. Private investment will also be favorably affected.

When we add the effects of a tax reduction to the rise in income which is likely to take place in 1959 anyway we can see that there is at least some possibility of touching off a boom in which demand will tend to exceed productive capacity.

It is not certain that a tax cut would generate excess demand and excess demand is by no means the sole cause of inflation, but if we make a permanent tax cut we do run the risk of feeding the inflationary spiral. Moreover we run the risk that in an effort to check the inflation desirable Government expenditures will be cut back.

If it is necessary to choose between permanent tax reduction and no tax reduction we face a choice between present benefit to the unemployment and future costs in terms of possible inflation and a restrictive expenditure policy.

A temporary tax reduction if it is feasible would get us out of the dilemma by giving a stimulus now without adding too much to demand a year from now.

Most types of Government expenditures which could be undertaken now would have only a small effect during the next 6 months. However, if we do not make a tax reduction, the economy could probably stand another couple of billions of Government expenditure during 1959. Appropriations now which would increase Government expenditures during 1959 by, say, $2 billion per year, would have some short-run effects, particularly through the effects of placement of orders in the inventory situation. In addition, there are, probably, still some categories of defense expenditures which could be speeded up with fairly immediate effects.

As to monetary policy, it should, of course, be pressed with vigor. If the Federal Reserve can bring down long-term rates a little further, they may have an appreciable effect on the mortgage market.

Senator Douglas. Thank you very much, Mr. Duesenberry.

The next witness is Prof. William Fellner, of Yale University.

Mr. Fellner. Thank you very much, Mr. Chairman.

STATEMENT OF WILLIAM FELLNER, YALE UNIVERSITY

Mr. Fellner. I believe the best guess concerning the duration of the present recession is that it is nearing its end. The main reason for making this guess is that the rate of contraction seems to be slowing. Very frequently, this means that the economy is in an advanced stage of the contraction; say, in its second half.

Such a forecast is, however, not a safe one. In some past cases, a forecast based on the slowing of the rate of contraction would have proved misleading. It is preferable, I believe, to base policy on where we stand now, and to use one's forecast merely to avoid with particular care those long-run commitments which will cause trouble in the future if the best guess comes out right.

The present degree of employment is below any reasonable long-run target by a margin that suggests the desirability of a temporary tax reduction. In the United States, balancing full-employment objectives with the objective of a reasonably stable price level might require not pushing the degree of employment beyond about 95 percent, on the average. From past experience, we may derive reasonable hope that most of the unemployment corresponding to a 5-percent rate would be made up of persons who are unemployed for no more than a short time. Only future experience can answer the question whether we can get vigorous growth rates at a degree of employment at which wage-push inflation does not yet become significant. At any rate, this is worth trying. However, the present 7-percent unemployment rate exceeds any target which might be set as a compromise. To me, the margin seems just about sufficient to call for a temporary tax reduction.

I think there is good reason to believe that the degree of employment compatible with an approximately constant price level is higher in the long run that it appears to be in the short run while an adjustment is being made to a noninflationary level of activity. To be sure, very recently the price level has been rising at an appreciably depressed level of activity. However, I would draw no conclusions from these recent increases, which started in January 1958 after a 4-month period of approximate constancy. These recent increases have resulted almost exclusively from farm products, and they may be explained by special circumstances of merely temporary significance.

I would suggest a prompt, 20-percent, across-the-board reduction of personal and corporate income taxes, at first for a 3-month period, with a possibility of extending the reduction for subsequent 3-month periods. My reason for not suggesting reductions in excises is that contemplating excise reductions is apt to result in the postponement of consumer purchases, now and in future recessions.

In practice, a 3-month reduction would, presumably, mean to reduce the pay-as-you-go withholdings by 20 percent actually for a 3-month period, and at the end of the year to allow 5 percent of the tax liability for 1958.

I do not believe that, by adopting the measure I suggest, we would run a serious risk of overshooting the mark, even if business should turn up in the near future. However, some of the recent additions to our future spending commitments to involve the risk of overshooting, because these plans may prove ill timed from a cyclical point of view. This danger exists, regardless of whether we do or do not reduce taxes now for a short period. In the later course of fiscal 1959, it might become desirable to slow down the rate of spending. I would like to suggest paying a good deal of attention ahead of time to the best methods available for achieving this result.

Senator DOUGLAS. Thank you, very much, Professor Fellner.

The next consultant is the well-known financial writer, Mr. Joseph A. Livingston, of the Philadelphia Bulletin. His writings are syndicated widely over the country. Mr. Livingston.

STATEMENT OF J. A. LIVINGSTON, FINANCIAL EDITOR OF PHILADELPHIA BULLETIN AND WRITER OF SYNDICATED COLUMN, BUSINESS OUTLOOK

Mr. LIVINGSTON. Senator, in trying to treat this recession, we ought not to be panicked by similarities to 1929. It is true that this decline has started 12 years after a major war; the 1929 decline came 11 years after. It is also true that housing, which was a premonitory symptom of the end of prosperity in the late twenties, has turned down this time. It is, likewise, true that capital expenditures of corporations and railroads have started to decline, even as in the late twenties. Those are important similarities.

But there is a fundamental structural difference. Government has become big business in the United States, a $110-billion-a-year business. It is a social force, an economic force, and, in the current recession, a stabilizing force.

Federal, State, and local government outlays constitute more than a quarter of the gross national product. One person out of four, directly or indirectly, derives his job, his income, from government. And the proportion will be even higher this year, because of increased government outlays and a drop in private outlays.

Federal expenditures are scheduled to rise from $73 billion in the current fiscal year to $78 billion in the 1959 fiscal year; an increase of about $5 billion. Receipts, on the other hand, are expected to fall from $70 billion to $68 billion. So, from a $2.6 billion deficit in the 1958 fiscal year, we will go up to a $10 billion deficit. Actual Federal outlays might rise from a current monthly rate of $73 billion a year to $77½ billion by December, and $79 billion by June 1959. That's a strong uptow.

As yet, there is no positive evidence that the business recession has reached a bottom. The best we can say is that the rate of decline has diminished. But it is not unreasonable to think that total expenditures for defense, for public works, and for housing will act as a holding force, and gradually start an upturn.

If this rate of outlays by the Federal Government is to be achieved it would be wise for Congress to raise the debt limit. It would be an inexcusable fiscal oversight to permit a ceiling on debt to repress anti-recession activities. We could have a repetition of what happened last year. As the Treasury approached its debt limit, defense payments to contractors were held up, contributing to the downturn then developing. I recommend a rise in the debt limit from the current level of $280 billion to at least $285 billion. I might say, parenthetically, that I question the advisability of a debt limit. If Congress appropriates money for expenditures and does not correspondingly provide taxes, why should not that be interpreted as an authorization for an increase in the debt?

I know 5 million persons are out of work. I know that nothing is so distressing, so humiliating, as wanting work and not finding it. I, personally, went through that experience during the great depression. A jobless man loses faith in himself. He wonders if he's no good. He becomes discontented with the social order. Therefore, we cannot permit unemployment to climb much higher, or to last for a long time.

Meanwhile, we ought to use the recession for what recessions are—for house cleaning. I'm not suggesting hairshirtism for hairshirtism's sake. But recessions have a function. They force people to adjust to changed conditions. The automobile industry is finding out that people are not interested in chrome, and size, and functionless design in cars. This is hard on autoworkers, on steelworkers, on auto dealers, and even I suppose on my friend, Ted Yntema. Some people have to find jobs in other industries as a result of this changing market. Some dealers may have to go out of business. The recession forces adjustments, some of which are socially necessary.

In a recession, businessmen are forced to cut down on extravagances and waste. Labor leaders who had been operating on the theory that the market place would justify all of their demands for higher wages discover that the market place is not a perpetual support for higher and higher wages. That's what Walter Reuther, of the United Auto Workers, is up against in his current negotiations with the auto companies. And the UAW officers are cutting their own pay.

In the prosperity boom, businessmen and even the Federal Government were willing to pay any price for labor peace. Charles E. Wilson, of General Motors, introduced cost-of-living, long-term contracts into the auto industry. These have spread through a large sector of industry. These contracts constitute built-in inflation. They're also built-in trouble.

In the steel negotiations of 1956, the Federal Government intervened to stop a strike. The result, so it has been said, was that the steel companies granted a luscious contract to the United Steel Workers. It was an election year.

The United Steel Workers of America has a contract which calls for wage and fringe benefits which will raise wage costs in July an estimated 20 cents an hour. This will squeeze the profits or add to losses of steel companies. It will tempt the companies to try to raise prices. This wage increase comes at a most inopportune time. David J. McDonald, president of the United Steel Workers, has said that his union has something new to offer society—the "mutual trusteeship" of labor leaders and corporate executives in which "everyone must give full consideration to the others' needs." It would be well for McDonald to show some trusteeship, some fiduciary responsibility, to the public needs now.

In 1948, the steel companies voluntarily reopened a wage contract with Philip Murray when wages of steelworkers fell behind the wages of other workers. Later, during the Korean war, Walter Reuther, arguing that long-term wage contracts ought to be "living documents," managed to get a cost-of-living adjustment under his contract with the auto companies.

This is a period which calls for living documents—wage and price restraint. A wage boost will help those steelworkers who are still on the job. It won't help those steelworkers who have been laid off; it won't help steelworkers who are drawing unemployment benefits; it won't help other workers who will, ultimately, have to pay higher prices for things made out of steel—automobiles, refrigerators, washing machines, nails.

This is a period for cost reduction, for price reduction. Mr. McDonald can't be expected, unilaterally, to shoulder the entire burden of high costs. But he could forgo part of the forthcoming increase if the steel companies cut prices.

Most steel companies have been operating at a profit at 50 percent of capacity. They can afford to make a contribution to recovery along with the union, and so help all consumers. The Government should use all its powers of persuasion to bring about an adjustment in the steel-wage contract and steel prices. This would be poetic retribution for its part in the steel-wage negotiations of 1956.

Finally, it seems to me the Consumers Price Index ought to get an overhaul. The last major revision was in 1951–52—more than 6 years ago. Consumption habits have changed and new influences have come into marketing. Bureau of Labor statistics and economists are aware of these influences but cannot always make suitable adjustments.

For example, the quality of service and of product tends to improve. In autos, we have automatic transmissions, power brakes, hillholders. The BLS tries to factor out such improvements from price, but cannot always do so. Similarly, in supermarkets, fresh vegetables are packed in plastic wrappers and are cleaned. The housewife gets a fresher product, a cleaner product. She can shop more quickly and spends less time in the kitchen. She gets built-in maid service. Does the food part of the index adequately take into consideration the improved quality and service? Long-distance telephone service has been speeded up by intercity dialing. How much of the increase in the telephone bill is better service and how much the higher price of living or telephone? Or take the repair and maintenance of TV sets, automobiles. They've become more complex. A mechanic who deals with a power transmission has to be more highly skilled than one who deals with an ordinary shift. He gets a higher price per hour—deservedly. So repair costs go up. Why? Because of more complex service—and not entirely because of higher prices.

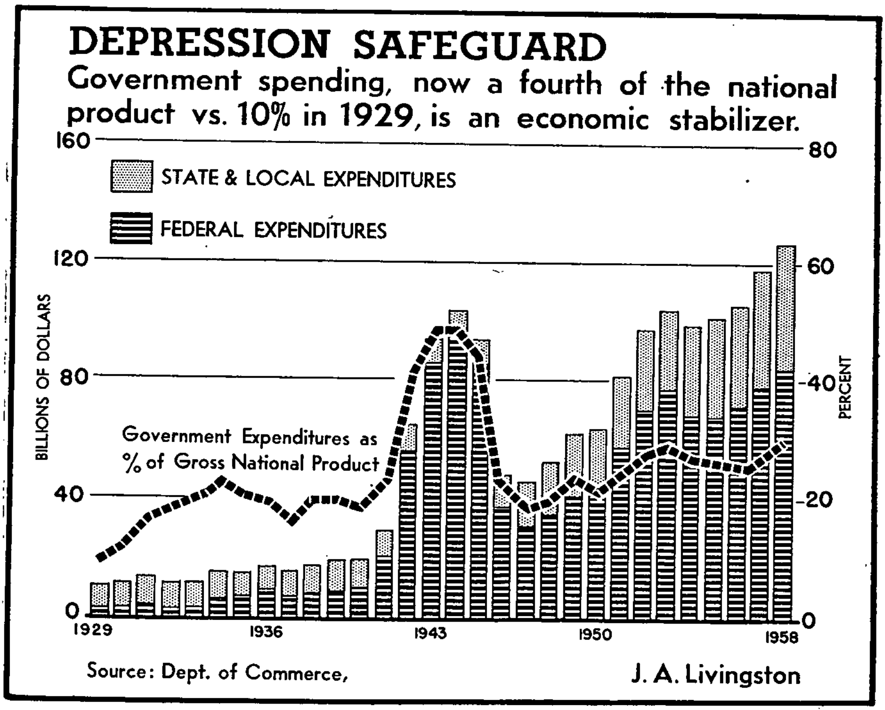
Finally, the market basket has changed. We eat TV-precooked dinners. Six years ago said dinners didn't exist. We have shifted, perhaps, from higher to lower cost foods—from meat to fish as meat prices rise. We need to know what people consume now, not what they consumed 6 years ago.

Part of the rise in wages under escalation contracts in the last 5 years has been due to a built-in upward bias in the BLS index—to improvement in quality. Workers have benefited in wage gains from a hidden uptrend. An improved index would improve our yardstick for measuring wage increases.

To sum up, I have these recommendations:

1. Raise the United States debt ceiling.
2. Extend unemployment compensation payments.
3. Use the Government's powers of persuasion to modify the forthcoming rise in steel wages.
4. Reexamine the Consumers Price Index.
5. Hold in reserve a tax cut. It may be required to prop purchasing power, but in view of the prospective large increase in the Federal deficit, I'd use it as a last resort.

(The chart accompanying Mr. Livingston's proposal statement follows:)



Senator DOUGLAS. Thank you very much.

It is a great pleasure for me to introduce the final discussant, an old personal friend and former colleague, Mr. Theodore O. Yntema, vice president, Ford Motor Co.

STATEMENT OF THEODORE O. YNTEMA, VICE PRESIDENT, FORD MOTOR CO.

Mr. YNTEMA. Mr. Chairman, in these hearings I should like to speak, not as a representative of Ford Motor Co. or of the automobile industry, but as a citizen, a businessman, and an economist.

In discussing monetary and fiscal policy today two important factors must be kept in mind.

1. Unless major economies in Government operations are achieved, Federal expenditures, especially for defense, will increase in the years immediately ahead. We shall need all the revenue from our present tax system to meet these expenditures. Permanent tax reductions now will lead to deficits in near future years. Such deficits will cause inflation. Permanent tax reductions are, therefore, contrary to the public interest now and should not be made until it is clear expenditures can be reduced.

2. Since 1955 we have had wage inflation, a persistent cost-push inflation brought about by the monopoly power of the unions. Even during this recession wage inflation is apparently going to continue. Cost-of-living escalators are raising wage rates. The steelworkers are due to get an additional 20 cents an hour. Mr. Reuther is asking for a wage and fringe increase of some 70 cents an hour plus a share of the profits. (Yet Mr. Reuther says his demands are not inflationary.) After recovery from this recession, the monopoly power of the unions will certainly drive up wages faster than productivity and will cause prices to rise.

We cannot let this recession run on just to slow down the inflationary rise in wages. Nevertheless, the monopoly power of unions to raise wages should give us pause. We cannot act as boldly and freely on the monetary and fiscal front as we would like when every opportunity will be seized by organized labor to drive up wages and, hence, prices.

The No. 1 economic problem of this country is wage inflation, rooted in the excessive monopoly power of unions. If it were not for the threat of wage inflation, we could act boldly and safely to end this recession and get back to prosperity in short order.

MONETARY POLICY

First, I want to pay tribute to the Federal Reserve for its courageous anti-inflationary actions in 1955 to 1957. We are fortunate to have a Board of such integrity and ability. My suggestions are minor compared with the praise the Board deserves.

With hindsight, it is apparent that restrictive monetary measures were continued too long in 1957 and that the increase in the rediscount rate in August 1957 was inadvisable. I am inclined to think, too, that the steps in recent months to ease credit might well have been taken more quickly.

At present, loans are obtainable by good credit risks, but interest rates to borrowers are high. Bank loan rates and long-term bond rates are considerably above the levels prevailing prior to 1955. Perhaps I have the bias of the borrower, but it seems to me that it would be in the public interest to increase the reserves of commercial banks and/or reduce their reserve requirements further in order to exert more downward pressure on sluggish interest rates.

Monetary actions of the magnitude thus far taken or likely to be taken will not end this recession quickly. Although monetary action to ease credit is a good deal more effective than the proverbial "pushing on a string," some of the expansionary effects of easier credit develop slowly.

GOVERNMENT EXPENDITURES

Government spending is a popular panacea for depressions. While there are some opportunities to accelerate needed Government expenditures in depression and restrict them in good times, these opportunities are rather limited.

In general, it takes a long time to start a program of public spending and a long time to stop it. The inflationary effects of the spending come too late in the depression and then intensify the inflationary pressures in the ensuing prosperity.

Public spending for its own sake is certain to be wasteful in its objectives and in its operations. Once started, a public spending program is difficult to stop. Economy and efficiency in Government are hard enough to achieve without having to cope with large expansions and contractions in the business cycle and without contamination from Government spending just to get the dollars out.

If additional spending is required, the taxpayers can spend their own money to far better advantage than the Government can.

To the extent that additional Government spending meets the tests of good timing, public need, and efficiency, it is an appropriate means of combatting depressions. The trouble is that Government spending, by and large, cannot meet these tests.

TAX REDUCTION

Here I shall deal first with excises and then with income taxes.

The excise taxes on passenger cars and trucks and on a number of other consumer goods were increased, some in 1941, some in 1944, and some in 1951. These increases were levied partly to obtain revenue and partly to curtail demand. In the 1954 recession many of the excises were lowered but, since the automobile market was strong, the taxes on autos and trucks were not reduced.

The excises on autos and trucks are clearly discriminatory and repressive. There is no reason or excuse for continuing them at present 10 percent rates. These rates should be reduced or eliminated at once, with retroactive coverage to the present so potential buyers will not defer purchases in the interim. The automobile industry today is severely depressed, as is to be expected in the case of major durable goods bought largely on long installment credit terms. The industry also is suffering seriously as a result of public talk of excise tax reduction and suggestions of lower prices to consumers.

Earlier I pointed out that permanent tax reduction now will probably mean future deficits and inflation. This does not rule out tax reform. The high, discriminatory excises on autos and trucks should be reduced, or preferably eliminated temporarily, and be replaced by a lower excise tax with a much broader base, effective January 1, 1959. This action would increase production and employment in the automobile industry substantially, but the industry, of course, cannot recover fully until the economy does.

I wish it were possible now to cut excises without any countervailing increases and I wish it were possible now to make permanent reductions in income and profits taxes. If we take such action, however, we shall be short of revenue to meet rising expenditures in good times when the budget should be balanced.

There is one advantage, however, in a temporary tax cut. It can be of large enough proportions to end the recession quickly and decisively. Moreover, if the cut is sizeable enough, it will be recognized that it must be temporary.

A temporary abatement or forgiveness of taxes withheld (and their equivalent on other income) would end this recession quickly. The increase of $2½ billion a month in disposable personal income—a 10 percent increase—would expand demand and call forth more production and employment. The downward economic trend would be reversed almost immediately. We would be back to a high level of employment and production in a matter of months.

Some may prefer a less powerful remedy. Thus half, instead of all, the withheld taxes might be forgiven.

My own preference would be to stop the collection of withheld taxes entirely for 2 or 3 months and then go to a 50 percent forgiveness until December 31, 1958, or until the seasonally corrected index of unemployment dropped below 5 percent, whichever occurred first.

During the period of tax reduction the Government would run a large deficit. This is not too serious in view of the fact that the ratio of Government debt to national income has fallen about 50 percent since the war.

The deficit also would increase the money supply—a result to be desired in view of the low ratio of cash balances to transactions and to national income as compared with the ratios prevailing from 1935 to 1954.

It is possible that we may get a recovery before long without further fiscal action to bring it about—but this is uncertain. If we take effective action to end the depression there will, I am sure, be a swift acceleration of wage inflation. If we do more than is necessary in tax reduction, we shall have correspondingly more inflation. Moreover, once the public discovers how effective massive tax reduction is, there will be a temptation to use it whenever unemployment rises to 3 percent or 4 percent instead of when it reaches 7 percent. If we use such measures when unemployment is only 3 percent or 4 percent we shall reap the whirlwind of inflation.

My own judgment is that we should use temporary tax reduction such as I have described to end this recession and at the same time face up to the problem that makes it dangerous to use such remedial measures—the problem of wage inflation.

Until we have reduced the monopoly of power of unions to drive up wage rates we shall continue to live in fear of inflation and unemployment.

Senator DOUGLAS. Thank you.

Are there any questions?

Mr. CURTIS. Mr. Chairman, in posing my general questions, I am somewhat at a disadvantage because the papers were directed to a certain subject which does not include, at least in terminology, the area I would like to explore. These papers had to do with the relative usefulness of Federal tax reductions, increase in Federal outlays, and expansionary monetary policies for promptly arresting further economic decline. The area I am interested in exploring is tax revision as opposed to tax reduction.

Now, that can involve us in a question of semantics, but I will try to point out the distinction I make, at any rate, between tax reduction and tax revision, or perhaps the words "tax reform" could be used in place of a reduction.

As I see a tax cut or a tax reduction, it is actually transferring, in effect, the purchasing power from the governmental sector to the private sector. That is a tax reduction.

A tax revision, as I see it, does not necessarily transfer ultimately any basic purchasing power between the governmental and the private sector, but rather alters the relationship in the private sector itself, or actually could result in no loss of revenue to the Federal Government, if the revision is removing an impediment to economic growth, because with the impediment to growth removed the growth will occur and the tax revenues will not be affected because we will gain revenue through the tax growth.

Or a third alternative in the tax revision, there might be a shift in this fashion: There is a decline in governmental expenditures because the Government has gone out of that particular operation and returned that operation to the private sector making it part of the tax base, and, therefore, there is a recoupment of any immediate loss in tax revision.

Now, I really need to write a paper on this, I guess, in order to get my question, but it seems to me that we should go back to some studies that this committee conducted back in December 1955. These hearings on the economic effects of our Federal tax structure produced several proper conclusions. One of these was that many business decisions nowadays are being made not on the basis of economics, but on the basis of tax considerations, and that being so and occurring over a period of time, we are getting a lot of uneconomic business decisions made which have not promoted economic stability or economic growth.

To deviate a little bit, tax take comes from tax base times tax rate times what I put in, a ratio of collectability. As the tax rate increases, I think we have lowered ratio of collectability; in other words, it is more difficult to collect the tax.

Also, under our Federal tax structure, as the tax rate is high, the tax base tends to shrink, because there is such an incentive to get away from paying any tax at all that many things are resorted to to avoid the taxes.

Now, to get to some specifics: we have an excise tax on transportation, which was imposed in World War II for the deliberate purpose of impeding the use of our transportation system. Now, that was put in as an economic impediment. My idea of a tax revision, for example, would be a removal of that tax, which is an impediment to growth on the theory if we did get the growth, we would not be altering our tax take. We might even be bettering it.

Take the cabaret tax, which is a misnomer as so many of these titles are. It is really a tax on any eating establishment that employs musicians. We are getting very little revenue from that, I might say. If we removed that tax, I would regard that as a revision, because we would actually get a bigger tax take since we would be getting income taxes from the musicians who would be employed, at least.

I am trying to illustrate these basic laws. I felt, for example, that the excess profits tax was a typical example of a tax that impeded economic growth. On analysis it was a tax on any new or growth business, and I predicted that its complete removal would bring in more Federal revenue, not less, within a period of 18 months.

Now, some people said that when it was removed and the fact that we did gain more revenue through the normal corporate tax than we were getting through the combination of the excess profits and the normal corporate tax did not necessarily prove the theory. All I can say is that its removal did not result in loss of Federal revenues.

I have tried to illustrate what I am talking about, and the fact that there is such a thing as diminishing returns in tax take. I would like to ask the panel whether or not they think that maybe some thorough tax revision along these lines might not be the very best thing that could happen to assist us in overcoming the recession.

I have made a little analysis, being an amateur economist, which leads me to conclude that to a large degree this recession is a Federal tax structure recession, brought about by these impediments to economic growth that are built into our tax system and that, therefore, if we remove those impediments, if we could select them, we might be doing the necessary job.

Having expressed this, I would like to get some comment from the panel, if I may.

Mr. Colm?

Mr. COLM. Congressman Curtis, I agree with you about the desirability of tax reform. I do not believe that tax reform of the kind you indicate is a feasible device for an antirecession program, because I think it would take too long a time. It requires very careful consideration by the committees in Congress and probably could not be enacted promptly enough.

Mr. CURTIS. May I impose, there is a big tax reform bill, 2 of them sitting over in the Senate right now, the result of 2 or 3 years of study, the Forand excise bill, some 300 pages, and the Mills' reform bill on corporate and individual income tax. Both of them were a result of 2 years' study.

There have been completed studies and hearings held by the Ways and Means Committee this year in just exactly these areas, one of them being my small-business tax bill that passed for municipal and school bonds, which would provide, we feel, a new market for those, and increase expenditures in the school area. There are a number of measures along these lines that have already been studied, so the timelag, I suggest, is not there. The United States Senate, Mr. Senator, should go to work on the Forand bill and the Mills bill—the Forand bill has been sitting over there since July, gathering dust. It contains in it many of these features that we have felt, those of us who have studied it, that would remove impediments to economic growth. Therefore, I think your timelag is not involved here.

Mr. COLM. I thought of some other additional tax reforms and as you know, I testified before the Ways and Means Committee on certain tax reforms and proposed a study which I think would take several months.

Furthermore, I do not believe that the causes of this recession have very much to do with our tax structure. I agree that we could have a tax structure which would promote more economic growth and I think such a tax revision is highly desirable. But, the most basic cause of the recession is the fact that we had some disproportion between the rate of increase in capacity and the rate of increase in real demand. I do not think that this disparity can be attributed to tax methods. There were contributing factors such as the contraction in the defense program to which reference was made. This had something to do with the debt limit. But by and large, I think tax reform is needed from a long-term point of view. In my judgment, it would not contribute to the immediate situation.

Mr. CURTIS. Could I ask one question there, Dr. Colm. Many of the economists who have testified before us say that one of the basic factors in this decline is the decline in capital goods expenditure; would you agree?

Mr. COLM. I do agree.

Mr. CURTIS. Now I feel this way, that the decline has mainly occurred in your growth companies, your smaller companies. From spot checking, I can tell you many companies who have put on their shelves their plans for expansion and growth primarily because they did not have the capital to finance the plans. That was the tight-money situation, and they usually rely on plowed-back earnings for that purpose. That is one reason I have suggested the tax structure which has created that situation lies at the base of this present recession. I say that for your comment.

Mr. COLM. Well, my comment would be that I share your view that investments of small firms probably have been declining severely. Our statistical information is very poor—our best estimates of capital expenditures are concentrated on the large companies. But, I share your view that the tight-money policy has been harder on the smaller corporations than on the larger ones. But I do think that what makes the big difference in this recession are the large billion dollar figures of business investments, and in our economic structure these are largely the investment programs of the larger companies.

By that I do not mean to say that we should not make every effort to create conditions which are more conducive to investment also in the smaller companies, and I note that certain bills are pending designed to promote small-business financing.

Mr. CURTIS. Don't the smaller companies though make up—there are thousands of them—a larger percentage of the total capital-goods expenditure than the smaller number of very large companies or what is that ratio, do you know?

Mr. COLM. I do not have the estimates at hand, but I believe that the small firms are probably 98 percent of all firms in number. In assets, however, the large proportion belongs to the large companies. If we relate investment in proportion to the assets, I would say large companies make the biggest impact.

(The following was later supplied for the record:)

In 1954–55 the small firms (corporations with assets of less than $1 million and partnerships) accounted for 97 percent of all tax returns but only 17 percent of depreciable assets.

	All corporations and partnerships	Corporations with assets of under $1 million and partnerships	Corporations with assets of $1 million and over
Number of returns (thousands)	1,627	1,577	50
Depreciable assets (in billions of dollars)	$278	$47	$231
Percent of all corporations and partnerships:			
Number of returns	100	97	3
Depreciable assets	100	17	83

Source: Statistics of income. Partnership returns for income years ending July 1953–June 1954; corporation income-tax returns for tax years ended July 1954–June 1955.

But, I would like to make a second comment on your point. I agree entirely with you, Mr. Curtis, that many business decisions are influenced by tax consideration, but tax considerations are not all in the direction of impeding growth or wasteful decision. We have also tax incentives which work the other way.

I believe that the very high expenditures for research and development of business have something to do with the fact that they can be treated as expenses; they are really capital outlays, outlays for intangible capital which can be deducted as expenses. The Treasury in a way gives them a 50-percent subsidy for these purposes.

Mr. Curtis. Exactly and that is one of the reforms we put in in 1954 which produced that economic result, which is an example of the other areas I am talking about.

Mr. Colm. The second fact is the capital-gains tax. The preferential rate for capital gains induces many people to invest in growth companies which do not have very high assured return now but give a better chance of realizing advances in the form of capital gains rather than——

Mr. Curtis. And yet we have a very dangerous situation in my judgment and have underlying economic phenomena resulting from the tax of inflation, where we have locked in investment of these very growth companies, because people that sell have to pay a tax, but if they hold, they pass it on to their heirs, get a zero percent income tax on it.

Mr. Colm. All I am trying to say, Mr. Curtis, the effects are not all to one side.

Mr. Curtis. Yes, sir.

Mr. Colm. That is why I believe this is a very complex problem. I would be tempted in response to your question to repeat the specific proposals on tax reform I made before the Ways and Means Committee, but I will refrain from doing that. I share your view of the necessity for tax reform and tax revision. I do not believe

25780—58——6

that taxes have caused this recession and I believe that fast action is needed.

Even the specific tax proposals I make—namely, splitting the first $2,000—in a way I regard as a tax improvement. I regard it as a tax improvement if we get rid of some of these excise taxes which have no logical place under present conditions as other panel members said.

So there might be a tax reform element in those proposals, but they could be done in a hurry.

Mr. CURTIS. Thank you.

Mr. Duesenberry?

Mr. DUESENBERRY. I do not think I can improve on Mr. Colm's statement. I associate myself with him.

Mr. CURTIS. In other words, you disagree with my observation, that the tax structure is an underlying cause, major underlying cause of this present recession?

Mr. DUESENBERRY. I think so; yes.

Mr. CURTIS. And, therefore, you do not think that in the area of tax reform we could seek remedies to the present?

Mr. DUESENBERRY. It is possible there are some things that might do some good in the short run, but it would be, I think, unwise to try to pick out a few spots for immediate action, because I think this would then probably foul up the total tax bill, and I think tax reform is in itself desirable, but I do not think that it is going to make a major contribution to recovery.

If Congress wants to——

Mr. CURTIS. Inasmuch as two major bills, though, have been studied and already passed the House of Representatives, which include many of these reforms, you certainly would think it would be advantageous to get that finished and out of the way.

Mr. DUESENBERRY. I will agree there, that it would be desirable to pass those bills, but not I think expecting that those bills in themselves will solve the recession problem. They are good for other purposes; they are a little good for that purpose. One should not expect to get the 2 for the price of 1.

Mr. CURTIS. It would be interesting to see them passed, just to see if my theory would not be proved.

Mr. DUESENBERRY. I am willing to give you your chance.

Mr. CURTIS. Mr. Fellner?

Mr. FELLNER. Mr. Curtis, may I just also say quite briefly, I think the problem of tax reform should be kept apart from the problem of antirecession measures, as far as possible, because these are measures that should be put into effect very promptly, and should be as noncontroversial as possible with respect to whom they favor and how they favor various parts of the population. I do not think these are really noncontroversial measures, these measures of tax reform, and I think there exists perhaps no really neutral way of reducing taxes. But I would be in favor of approximating neutrality in this regard, so far as possible, and that would mean some sort of general across-the-board reduction, temporary reduction.

Mr. CURTIS. So I take from that that you, too, join your colleagues in feeling that underlying this recession, one of the major factors is not these impediments to economic growth that exist in our tax structure?

Mr. FELLNER. Oh, they may contribute to what we have been experiencing. I don't know what their contribution is. I also would not interpret the recession primarily in those terms. But even if they have contributed, I think that the problem now is to find what one might call a neutral way of doing this, relatively noncontroversial way of reducing taxes temporarily for the time being.

And I don't think that a tax reform can be neutral or noncontroversial in the sense in which perhaps a general across-the-board tax reduction would be.

Mr. CURTIS. Mr. Livingston?

Mr. LIVINGSTON. Well, Mr. Congressman, I think the burden of proof is on you. I think that we have had an expansion in our economy since 1929. We have had a terrific growth since the war, and the economy has grown despite all of these so-called inequities that you suggest, and I would think that the evidence is that growth has not been impeded by taxes.

Mr. CURTIS. We are talking about continued growth, are we not?

Mr. LIVINGSTON. We are going to have continued growth. Just give growth a little time.

Mr. CURTIS. In other words, you do not view this present recession with too much alarm?

Mr. LIVINGSTON. I certainly do not view it as a tax recession, no.

Mr. CURTIS. But you think the underlying economy is sound and that we will bounce back under the present structure we have?

Mr. LIVINGSTON. Yes. The only economic axiom I know is that the sun always rises and so does the economy.

Senator DOUGLAS. I believe Mr. Hemingway proved that.

Mr. CURTIS. Mr. Yntema?

Mr. YNTEMA. Congressman Curtis, I think the facts bear out a good deal of what Mr. Livingston has said. As a matter of fact, from 1946 to 1957, we did have unparalleled expansion in our economy. That was not prevented by the tax system. Probably it was attributable to the dearth of durable goods built up from 1930 to 1946. First, we had a decade of mass unemployment, and then we had the war. We came out of the war in 1945 with a great deficit in——

Mr. CURTIS. During the war, we expanded our capital plant considerably, did we not?

Mr. YNTEMA. Not necessarily capital plant required for civilian production. Some of it was useful for civilian production and some of it was not. In our own industry we had a great shortage of capacity immediately after the war. Consumers, as well, had a serious shortage in the inventory of durable goods desired at a high level of employment.

In the last 12 years, we have been doing 2 things, making up that deficit in inventory of durable goods, both producers and consumers, and we have been producing durable goods for the growth that has taken place. The tax system has not changed very much in the last few years, and it is a little hard to pin this depression on the tax system when it existed also during the period of prosperity.

Mr. CURTIS. Certain things do accumulate though.

Mr. YNTEMA. Yes, sir. What I am saying is that I do not see how we can pin this recession on the tax system. On the other hand, there are certain tax situations to which I think we ought to take exception. There are some taxes in this system which were designed to repress consumption. I do not think it makes any sense to keep taxes like that. And, to some extent, the taxes to which you refer—the transportation taxes are of that sort; the excises on automobiles, trucks and parts are clearly of that sort. I do not think removal of the excise on automobiles will have a tremendous effect on demand in the long long run. I want to make clear the difference between the long and short run, in the reaction of demand for automobiles to the cut in excises.

Failure to act on the excise taxes in the near future may be almost catastrophic. At present there is talk of excise tax cuts and people are beginning to hold off purchasing cars. This may snowball and have very serious effects.

This is a case of hardship and an inequity, and I think there ought to be reform in these cases where the effects are clearly depressing.

Mr. CURTIS. Let me conclude with one other little illustration. The freight tax is producing this economic result where a vertical operation like the Ford Motor Co. can buy their own trucks and transport their own goods and avoid the excise tax, which has been a deterrent effect on the private or public carrier. Now, that is a matter of an economic result.

I suggest that possibly an equalization of the tax, whether it is removal or equalization, will produce some economic growth that we are not presently experiencing.

Mr. YNTEMA. I think in the long run we ought to evolve a tax system that will yield revenue with as little repressive effect as possible, and that would give us as dynamic an economy as possible. In a sense, all taxes are bad taxes. It would be better if we did not have such high income taxes and did not have corporate and did not have high——

Senator DOUGLAS. Or did not have any taxes at all, Mr. Yntema?

Mr. YNTEMA. I am not saying that. I am saying this, that every possible effort ought to be put forth to achieve economy in Government. I know this is an old speech and it is very hard to get economy in Government without profit and loss incentives. But it is one of my hopes that we will really go to work on economy in the Government.

Nevertheless, I am not in favor of large scale permanent tax reductions at this time. I am afraid that next year and the year after we shall have rising Government expenditures.

Mr. CURTIS. May I make one concluding observation. Then I would judge from this, the panel's general views are if tax reduction is used, it is to be used to bolster consuming power. That is what I gather from all of this.

Mr. YNTEMA. May I speak to that?

Mr. CURTIS. Yes.

Mr. YNTEMA. I would not say that. I think in the long run you do not want taxes that are going to bear any more heavily than necessary upon the incentives to expand and to produce. In the short run, I do not think anything that you are going to do with the tax system at this time in the way of reform is going to have a profound effect upon incentives.

You might, however, do something in the way of depreciation allowances.

If you want to use the tax system as a means for countering a depression, the easiest way to do it is temporary tax reduction on a fairly massive scale.

Mr. CURTIS. The only point I have been making, of course, if the Federal Government through the tax system has been having a repressive effect on the economy, it isn't helping the Federal Government to do more but less by performing in the manner in which it has been affecting the private economy.

Senator DOUGLAS. The first question that I should like to direct to the panel is based on the size and speed of the multiplier. Mr. Duesenberry said that approximately 95 percent of disposable personal income is spent on consumption and I presume this is based on a correct figure and that approximately 5 percent is saved.

Mr. DUESENBERRY. Actually, I spoke of a low- and middle-income tax, so I give myself the extra couple percentage points.

Senator DOUGLAS. Lower and middle income would be higher.

Mr. DUESENBERRY. I give myself the other couple of percentage points for changing distribution.

Senator DOUGLAS. Now, if this is fully carried out, it leads to a tremendous multiplier because, of course, the initial increase in expenditures is 95 percent of the increase in disposable income, and in the second stage, 95 percent of the 95 percent, and in the third stage, 95 percent of the 95 percent of the 95 percent, and so on, so that you get a multiplier of 20 out of this.

Mr. DUESENBERRY. Well, I am sorry, sir, I do not think that is a fair conclusion from this because in this first round, you get 95 percent, but in all——

Senator DOUGLAS. What happens in the second round?

Mr. DUESENBERRY. In the first round you are giving money directly to consumers. In the second round, you are giving to them the income—it is easier to start out with the full effect in the short run. You will have to deduct from the amount that goes to the consumers the excise taxes, the corporate profits, the personal taxes, the reduction in transfer of payments in case anybody gets employed and goes off the unemployment compensation on this, so that actually, a long-run multiplier of somewhere of the order of magnitude of two and one-half, I think, is appropriate, after you take account of all those considerations and, in fact, of course, this does not go quarter by quarter with anything like the speed you have indicated. There is some lag in the adjustment of consumers to their expenditures.

Senator DOUGLAS. That comes later. Have you worked out the mathematics of the multiplier and loss of some successive stages?

Mr. DUESENBERRY. Taking account of taxes, transfers, corporate profits, and so on, I think given time for all of the adjustments to take place, you get somewhere probably between 2½ and 3, but with a—well, anyway, that much margin of error. I do not think anyone ought to put it any more precisely than that and that is giving time for full adaptation all around and it will be a little bit lower in coming out of a recession because to the extent that consumers have cut their saving on the way down, they will tend to save a little bit more on the way up, so that for the period when you are recovering at least the previous levels of income, you would expect to get somewhat smaller—well, I do not think we have enough of a record to make anything out of it. That is why I put in my paper at about two for the full final effect, let's say, a year or year and one-half from now.

Senator DOUGLAS. Mr. Colm said that a seven to eight billion dollar tax cut would produce a three to four billion dollar stimulation in that current year. I suppose he was referring to the fact that if the tax cut were evenly distributed over the year, the net average effect would be approximately only half the amount of the cut; is that right?

Mr. COLM. First, I intended to say four to five. Second, I am a little skeptical about using the 95 percent of average spending as the basis for estimating the initial effect of a tax reduction. Third, we should consider that 60 percent of the benefits of either of the two proposals—namely, the increase of tax exemption by $100 or splitting the first bracket—would accrue to people with taxable income above $5,000.

Another tax reduction—namely, the across-the-board percentage reduction proposed by another panel member—gives 80 percent of the benefit to the people with taxable income of about $5,000.

Senator DOUGLAS. Doesn't it follow, from consumer budget studies, that the percentage of savings is very much less in the case of those with small incomes than those with large incomes, or to put it another way, that the income elasticity of savings is very high and the marginal rate of savings diminishes very rapidly as you go down the income scale and, therefore, tax cuts concentrated on middle and lower income groups will have a large multiplier than a tax cut for the upper income groups. Is that not true?

Mr. COLM. That is why I thought the 95 percent was too high as a point of departure for the calculation.

Mr. YNTEMA. May I ask a question? Isn't the unspent savings only a part of what is included in savings? What we ought to be concerned with is the increase in cash balances.

Senator DOUGLAS. What is saved will be invested.

Mr. YNTEMA. Yes, sir.

Senator DOUGLAS. Is that true in a recession, granted that it is, perhaps, true or more than true in an upswing; isn't one of the accumulated factors in a recession the fact that investment falls off more rapidly than savings, so that you have an accumulation of idle monetary purchasing power in the banks?

Mr. YNTEMA. If you look at what has happened in the third quarter of 1958, you find that gross domestic investment is off about $13 billion. Of that decline $10½ billion is inventory liquidation. The decline outside of inventory is only about $2½ billion.

Now, to come back to your question, there may be some tendency, for a while, to hold off investment. I do not think it is at all clear that the cash that will go to the higher income people will stay in the form of cash. It may or may not. But in any case, I think we ought to talk about the amount that is retained in cash balances rather than the amount not spent on consumers goods.

Senator DOUGLAS. That is the problem.

Mr. YNTEMA. That is right.

Senator DOUGLAS. I did examine figures on savings and figures on investment, and they seem to indicate that, for the last 20 years, in periods of upswing investment exceeded savings, probably financed by bank credit which, presumably, should not be used for that purpose, but that during periods of recession savings exceeded investment and, therefore, that you had, presumably, some idle purchasing power.

These factors have made me, personally, feel that the tax reduction, so far as class distribution is concerned, should be concentrated primarily on the middle and lower income groups—then certain ideas of equity there—and, also, to counterbalance the regressive tendency of State and local taxes.

Mr. LIVINGSTON. I would like to ask Mr. Yntema a question. Why would the pileup of bank balances in the hands of persons in the upper middle and upper income groups, if it were not spent for consumption goods, have any effect on investment except to supply money which the manufacturers would not want, if they do not except to sell their goods?

Mr. YNTEMA. There is a theoretical point to get clear. It is not what we spend in consumption, but what we spend on goods, either producer or consumer goods, that has an effect in employment and production. We do not know precisely what happens. There may be some tendency for those with higher incomes to build up their cash balances, but I do not think we ought to write off everything that isn't spent for consumption.

Mr. DUESENBERRY. Mr. Chairman, on that point, I think there may be those higher income people who are in business that might induce some more investments is one thing, but as far as financing investments is concerned, we certainly do not want to use the tax policy as a substitute for monetary policy. If we need more credit we want to get lower interest rates and that can be done otherwise than by tax reduction. But whatever effect you do have on investment is going to be relatively slow. It is not true that private investment takes as long to turn on and turn off as public expenditures, but it is true that there is a quite substantial lag between decision making and the actual expenditure effects for private investment; so, if we are dealing with the very short-run problem, not with the problem of a year from now, but with a problem of the next few months, then, whatever effects a policy may have on private investment, it is going to have an effect on private-investment decisions now which is going to result in expenditures only some time later.

Senator DOUGLAS. Now, there is another point I would like to raise, and that is, if you have a tax cut, should it be diffused over time or concentrated? Now, Mr. Yntema, as I remember it, urged very strongly that you should have a tax cut which was concentrated so far as possible rather than diffused. Do you want to develop that, Mr. Yntema?

Mr. YNTEMA. Well, in the first place, I am not sure we should have a tax cut now. This is a question on which there may be honest differences of opinion.

Senator DOUGLAS. I understand.

Mr. YNTEMA. But if we are going to have a tax cut, then I would favor one that is massive and one that can be made quickly and can be cut off in a fairly short period of time after unemployment gets down to 5 percent. There will be some lag effects, as was pointed out a few moments ago. All the additional money will not be spent immediately. There will be some carryover in spending later on.

Senator DOUGLAS. I am particularly concerned that the carryover effects will not come when we get down to a relatively low level of unemployment. That will spell more inflation than we otherwise would have. Removal of the 20-percent withholding tax on the first thousand dollars of taxable income for the year as a whole would reduce income by about $12 billion to $15 billion. If that were concentrated for 1 quarter, that would be a total loss of $3 billion to $3¾ billion, which would be, roughly, the same as a cut from 20 to 15 percent for the year as a whole. Now, what you are saying is make the cut as concentrated as possible; is that right, if you have it?

Mr. YNTEMA. Well, as concentrated as reasonably possible. I would make a large cut. I think that would improve the psychology of the country.

Senator DOUGLAS. The best way to get concentrated effect would be to give a refund to those who paid taxes last year, so that, instead of tax reduction diffused over a 3-month period, it would come all at once. If concentration is what you want, why not a tax dividend of $50 for each of the 60 million income-tax payers of last year? That will give you approximately the same amount. Instead of being diffused over a year or diffused over 3 months, it would come through the mails in one fell swoop.

Mr. YNTEMA. Mr. Chairman, I did not mean it should be as concentrated as possible, but I think it ought to be large enough to take effect quickly.

Senator DOUGLAS. This would be quick. If speed is what you want, this is it.

Mr. YNTEMA. I would rather have it large enough to take effect quickly, and then I would continue it until there is evidence it has taken effect, say, until unemployment drops to 5 percent.

Senator DOUGLAS. I thought I would stir up the lions with this proposal, but this is the logical conclusion.

Mr. YNTEMA. That is not my generalization, Mr. Chairman. I did not say, or mean to say, we should have as much concentration as possible.

Senator DOUGLAS. I read your testimony some weeks ago and was much impressed with it—which encouraged remitting the 20-percent withholding tax for 3 months, and that has been moving around in my mind ever since. Now, do you disavow your own child?

Mr. YNTEMA. No, I didn't say that. I did not mean to imply that you should have as much concentration as possible but merely that you would have enough so that the action would take effect quickly. I didn't say it should be a one-shot deal. I would rather start this on a fairly massive scale if it is to be done at all. I would taper it after 2 or 3 months, stop it after the end of the year or before year end if unemployment drops off to 5 percent.

Senator DOUGLAS. Does anybody else want to make any comments on the relative concentration or diffusion of the medicine?

Mr. DUESENBERRY. Let me say one word, Mr. Chairman. I think we know a little bit about how consumers react to changes in their income which come in more or less ordinary ways. It seems to me that the more gimmicks we put into it the less we know. We have a little bit of experience with lump-sum payments; if you look at the record on the various veterans deals, the bonus in the thirties and the terminal leave at the end of this war which is true, came in terms of bonds, the record is very mixed. I think it is true it is very hard to find the soldier's bonus if you go back and look at the quarterly figures on consumption. If you didn't know the date of the soldier's bonus you wouldn't identify it by looking at the figures on consumption.

Now, the thing is that there is a problem here of how people react to the thing, one-shot payments may result simply, people say, "Well, I never had any money before for a rainy day; now I have got it I'll put it away." You cannot tell how people are going to react. You might get a bigger reaction with a tax cut, you might get a smaller one. I don't think anybody is in the position to guess what the effect would be of any lump-sum payment. We are bad enough at guessing what are the effects of things which appear in more or less normal form.

Senator DOUGLAS. Anybody want to add anything?

Let me ask you another question.

If we assume for the sake of argument a multiplier of 3, a $6 billion tax cut should generate increase in gross national product of approximately $18 billion; should it not?

Mr. DUESENBERRY. Yes.

Senator DOUGLAS. Now, about $1 out of every $5 increase in gross national product goes to Government in the form of taxes, does it not? So that, by raising the level of gross national product and of national income, you will raise the level of receipts by about $3.6 billion. The net loss of revenue, therefore, would only be $2.4 billion; then the question comes is that too big a price to pay for the increase of $18 billion in gross national product?

Let me throw that out for you. You may quarrel with the multiplier or you may quarrel with my arithmetic.

Mr. Fellner, do you have anything?

Mr. LIVINGSTON. It all depends, Senator Douglas, on what you are trying to do. It seems to me if the purpose is to maintain full employment at all times, get your employment immediately up, it may be some such method as Ted suggests is good, but if we are to do anything about developing a kind of an awareness of the problem that strong labor and strong business negotiations have done and impress upon the heads of the automobile companies and the heads of the steel companies and the heads of the unions that they cannot rely all the time upon beneficent Government to make a market for them or to provide jobs, then it seems to me it would be desirable not to do anything too hurriedly.

I think when Mr. Yntema pleads for an excise tax he ought to have to mention something about cutting prices and I think that the steel companies ought to do something about cutting prices.

Senator DOUGLAS. I do not wish to inject myself too much into this discussion, but the other day I made a proposal that we have a 7½ percentage point cut in the excise tax, reducing it from 10 to 2½, which on a car which sells to the distributor for $2,000 would be a tax cut of $150, on the condition the automobile companies made a cut of 6 percent roughly in their price of $120 which would mean that the price to the distributor would be reduced by $270.

Now, we have invited Mr. Yntema here in his capacity as an economist and not as vice president of Ford, and I think it would be unfair to put him on the spot on this and you raised this issue without any prior conference with me.

I merely mentioned it to say that I am sure many of us would like to join tax policy with some price-reducing policy and I also suggested to the UAW that they also should moderate some of their demands as part of a three-way bargain.

Now, I do not know that a similar offer could be made to steel because there is no excise tax on steel, so that there is no possibility of a direct offer being made to them. There is a limit to the number of specific bargains that you can strike in this connection.

It so happens that the automobile industry is unique, it has few producers, it has an excise tax and it is almost completely unionized.

Mr. Yntema, you don't have to reply to this at all. You are here as an economist and not even by implication did I want to put you on the spot.

Mr. YNTEMA. I would like to say something.

There is so much myth recited about the automobile industry that I think there ought to be some disabusing of our minds, and I would like to start on my friend Joe Livingston, if I might.

He says this:

> The automobile industry is finding out that people are not interested in chrome and size and functional design in cars.

Well, there is something very interesting that has happened in the last 10 years and I do not think that people understand it. The basic thing that has happened is that the incomes of consumers have gone up and we in the automobile industry have had to run to keep pace with them. The bulk line car has had to get bigger because consumers want a bigger car. We have had to make the car bigger in order to get volume. If we don't, we find our competitors take the business away from us.

Mr. CURTIS. Could I interrupt a minute to ask you to explain this. I understand you have to be on the waiting list a long time before you can purchase a Volkswagen or a Rambler.

Mr. YNTEMA. That is right. I will try to explain why that is so.

The basic phenomenon has been a rise in consumer income, plus some stretching out of credit. As a result, the bulk-line car has gone up in size and price. That has left a market underneath for the small car.

You say, why don't the automobile companies produce a small car? Well, the difficulty is that you cannot get a premium price for a smaller car.

Now, medium and high-priced lines of cars command a premium price. You pay more for these bigger cars than they are worth intrinsically in terms of the material that goes into them. The Ford and Chevrolet and Plymouth, the big-volume cars, give you more for your money intrinsically because there are big economies of scale in their production, resulting in a lower cost of production and a lower price.

Below the Ford, Chevrolet, and Plymouth the market is not large enough now to make possible the economies of larger-scale production needed for a low price. In the volume the people buy the smaller cars we cannot produce them economically.

Mr. CURTIS. Can I pose a question? I have heard that the real reason, and I was told by a top auto man off the record that the real reason you have them is because the auto companies are so much in the used-car market and they want the housewife to buy the—wait; let me finish and you can answer—they want the housewife to buy the used car rather than the small car and if you made small cars you would be competing with your own used-car market.

Mr. YNTEMA. We would be competing with used cars, but that would not keep Chrysler or General Motors or Ford out 1 minute if we could produce and sell the small car at a profit.

One other point. If you will look at the car lines that have done the best, they are not the cars devoid of chrome. It is a myth that we are not making the kinds of cars most people want.

With respect to the price-cost-wage situation, I should like to offer a few comments. The Government did something that was appropriate in a seller's market: It kept the excise tax high during the seller's market. Now the responsibility devolves on the Government to recognize that the basic demand situation has changed and to reduce automobile excises. It would be nice if there were room to reduce prices, too, but the plain fact is that most of the automobile production, at least half of it, is not being produced at a profit today.

Senator DOUGLAS. If you get volume you might get profit.

Mr. YNTEMA. If you reduce the excise tax there will be some increase in demand. This increase will be bigger in the short run than in the long run. Part of this depression in the automobile business is due to the fact that people think maybe excises will be reduced and prices reduced soon. In the long run the increase in volume resulting from excise-tax reduction is not going to be very great.

With respect to the proposition made by Mr. Reuther we ought to be realistic. Reuther came out yesterday with a offer to defer the settlement of the contract for 3 months, until September, and the reason is a very simple one. He would be relatively more powerful 3 months from now and the automobile companies would be less powerful. Mr. Reuther has been asking for a 70-cents-an-hour increase and also for a share of the profits; and there is no indication whatsoever that at the end of the 3 months he intends to let up on any of those demands. Those are some of the facts of life with which we have to cope.

Senator DOUGLAS. May I say I do not want to concentrate attention too much on this proposal of mine. Frequently steps which would not be profitable for one party to take alone will be profitable if all parties move together through the increased volume and the increased production which will come and as an old student of Marshall, Mr. Yntema, I am sure you are well aware of that.

Mr. YNTEMA. I do not see, Mr. Chairman, how that could apply to reducing prices. The elasticity of demand tends to be greater for the individual firm than for the industry.

Mr. FELLNER. May I just raise one question in connection with these excises.

I am a little bit afraid if we cut excises now, in each further recession the public will start speculating on when the next excise reduction comes. I do not think that excises are good means of countercyclical policy for this reason. And to come back to a question which you originally raised, Senator Douglas, I really think it would be unreasonable to feel that the revenue loss which we have been contemplating here is more harmful than the continuation of this recession. I think the real problem there is not a revenue loss in this order of magnitude. The real problem is whether we get any delayed inflationary effects when this can harm us and I do not see that a tax reduction on the scale on which we have been contemplating it would have these consequences if we do it in 3-month periods so that we can decide 3 months from now whether we want to continue it.

Senator DOUGLAS. May I suggest another line of thought.

Chairman Martin of the Federal Reserve Board has urged against tax reduction that would expand the amount of bank credit, which it would, and this could lead to later inflation. I would like to ask couldn't this be offset by Federal Reserve policy, its selling bonds and thus decreasing the reserves of the member banks in the Federal Reserve System and thereby contracting their loan capacity? In other words, it would only be inflation if the Federal Reserve Board permitted it, is that not true?

Mr. FELLNER. Except we do not want to make it more difficult.

Senator DOUGLAS. Their intelligence would not be up to the problem?

Mr. Yntema?

Mr. YNTEMA. May I speak to this point that Dr. Fellner just mentioned?

Senator DOUGLAS. Certainly.

Mr. YNTEMA. The excise tax on automobiles is scheduled to go down on July 1. Either do 1 of 2 things, I beg you, either cut the excise tax now or otherwise extend it now. Just don't defer action on it. Inaction could have a very serious effect on demand in June.

Mr. FELLNER. I fully agree with that.

Mr. YNTEMA. The most important thing is to do something one way or the other.

The next most important thing is to do what I suggest. [Laughter.]

Senator DOUGLAS. Now, I would like to raise one final question if I may.

Every time we make a proposal either for public works or for a sizable tax cut we are met with this objection from the Treasury, from Chairman Martin and from certain Members of the House and Senate. Namely, that there will be an appreciable shrinkage in revenue anyway and even if we do not increase expenditures there will be a large governmental deficit for the fiscal year 1958–59 which is variously estimated from 7 to 10 billions of dollars. If Congress either increases expenditures or reduced the total volume of taxes, it will be adding to this deficit which will be improper and therefore, we should confine countercyclical effort to the natural shrinkage of revenues in comparison with ordinary expenditures and to monetary policy.

I would like to have the panel discuss this because this is what we face continuously up to date from the Treasury and from the Federal Reserve Board and from influential Members of Congress itself.

Mr. Colm?

Mr. COLM. Senator, I think it is true that we are facing a large deficit which is mostly the result of shrinking incomes and particularly profits. If we have an $8 billion deficit under present programs I estimate that $5 billion will be shrinkage of revenue and $3 billion the result of an increase in expenditure.

(The following was later received for the record:)

On request I am submitting some estimates which show the distribution of the possible $3 billion increase in budget expenditures.

Budget expenditures outlook, fiscal year 1959

[In billions]

	Administrative budget	Cash budget
January expenditures, budget estimate	$73.9	$86.7
Effect of action taken or likely to be taken:		
Military defense	+.7	+.7
Housing	+.8	+.8
Pay raise (military and civilian)	+.5	+.5
Extension of unemployment benefits	+.5	+.5
Public works	+.3	+.3
Agriculture (acreage reserve)	+.2	+.2
Miscellaneous expenditure programs	+.1	+.1
Total	+3.1	+3.1
Trust account transaction: [1]		
Unemployment benefits		+1.0
Old-age and survivors' insurance		+.2
Total		+1.2
Expenditures outlook, fiscal year 1959	77.0	91.0

[1] No allowance is made for an increase in highway expenditures over and above the January budget estimate assuming that under recently enacted legislation, it will be possible to reach the level of expenditures estimated in the budget.

To the extent that the deficit is due to shrinkage of incomes, it is a mitigating factor but not a factor which will reverse the tide and support an upswing. I think that further, legislation which could well be enacted would increase expenditures during the rest of the fiscal year 1958 and fiscal year 1959 only within narrow limits.

Let us assume expenditures in fiscal 1959 could be increased by another billion dollars due to further legislation, in addition to the $3 billion increase which now appears likely. Let us also assume that taxes could be cut by $7 billion. That would give us a combined additional action directly affecting the budget by $8 billion. Under current legislation the fiscal 1959 budget deficit was estimated at $8 to $10 billion. As a result of the new legislation the deficit for the fiscal year 1959 would be larger than the $8 to $10 billion because the effect, the multiplier effect which you demonstrated by your example, will not take place so fast.

Senator Douglas. But it will compensate for part of the loss.

Mr. Colm. It will compensate for part of the loss and particularly I am concerned not only about 1959 but also about fiscal year 1960 and thereafter. This all goes back to yesterday's discussion, how soon could we expect a revival due to the market forces?

I am particularly impressed by the McGraw Hill survey which tells us for the large corporations that business investments in 1959 will be 10 percent below those in 1958 which means 25 percent below those of 1957. There are even indications that this may be an optimistic estimate.

So, I would say that if we look at 2 or 3 years we may have a larger deficit which I call a recession deficit than the antirecession deficit which would be the result of a further program and which would include this compensating factor which you, Senator, demonstrated.

This whole discussion which got around to the automobile industry, I think, started with the question of the multiplier.

Because of the lack of knowledge and being on the cautious side, I have always figured with a multiplier of 2 rather than 3. But still a $10 billion increase in gross national product gives us under present tax rates a little better than $2 billion additional taxes. And with the economy operating at $40 billion below a satisfactory level of employment, we could expect a considerable rise in tax revenues, if we accomplish the purpose, namely, a real recovery.

Senator DOUGLAS. Mr. Duesenberry?

Mr. DUESENBERRY. Well, on your question as to how much we should worry about the deficits I think there are two things to be said.

The first is that we should not worry very much about them anyhow. The deficits, per se, are not a major consideration. There are some problems about how much liquidity there is in the economy and such things, but these are on the whole secondary considerations and to some extent they can be compensated for by other aspects of monetary policy.

The second thing is that I agree with Mr. Colm that if you wanted to figure out how to have the biggest deficit the way to do it would be to let income drop a good deal and keep income—run a policy of maintaining Government expenditures at about the present level and just let things take their course in a long depression and you might get a bigger deficit than you would get if you took some action——

Senator DOUGLAS. We are not cutting Government expenditures as incomes go down, the policy which most economists favored from 1929 to 1933.

Mr. DUESENBERRY. I am sure you would be hard put to find one that favors that today.

Senator DOUGLAS. Mr. Baruch favors that and as I understand it ex-President Hoover does. They are both able gentleman. They demonstrated their ability to make millions in the competition of the market.

Mr. DUESENBERRY. I think the ball we should keep our eye on is the effect of the policy on the economy and we should let the deficit fall where it is after we have decided what is the best policy with respect to expenditures and tax cuts, not givê major consideration to deficit, per se.

Now, I think our real problem is to decide how much action we want to take now and in particular what kind of a choice to make between speeding up the trend of Government expenditures. Let me put it this way. It is my view that there are a great many socially desirable expenditures which need to be made over the next 8 or 10 years and we ought to look forward to an upward trend in Government expenditures.

Now, if it were not for the problem let us say of the next 12 months during which time or at least the next 6 months during which time increased Government expenditures won't do much good, it seems to me that we should try to do, two things. First, to raise the level of Government expenditures now to give some further support to the situation in 1959, being presumably a little bit cautious, that is, making the increase in expenditures somewhat short of enough to guarantee that we will drive the system to full employment because the margin of error in our calculations is pretty big. If we try to hit the target we run about as much risk of going over as going short.

Secondly, it seems to me trying to arrange our planning in both directions. That is try to get some better scheduling of all of these programs so that we have some idea how quickly we can taper off new appropriations, if we do too much, as well as how quickly we can step them up.

Now, myself, I would give great weight to the desirability of increasing expenditures slowly and steadily rather than making tax reductions and no increase in expenditures. But, I recognize that this leaves us in somewhat of a box for the next few months and there is a hard choice to make, I think, between long run socially desirable expenditures and tax cuts now and whether we will be able to do it by temporary tax cut. One difficulty with a temporary tax cut is that it really is likely to shut us off from undertaking and getting going on an upward trend in Government expenditures because I don't think we are going to be able to make the calculation so delicately as to have a tax cut go in now, go out then, expenditures come out at the right time. That is getting too tricky.

I would like to see a steady upward trend in expenditures with somewhat larger appropriations now which will do some good next year and insure a reasonably strong recovery.

Mr. Colm says we don't know how good the situation is going to be.

My own feelings on this are very mixed. It is very hard to tell a man that is unemployed that he ought to be unemployed for another 6 months because it is really desirable to build some schools and have a better defense program a year from now. It is very hard lines to tell him that, and I have to confess that I spent all week mulling over this without reaching a very nice conclusion about it.

Senator DOUGLAS. Sometimes the roll is called, you know. When the roll is called you have to answer "aye" or "no," you can't——

Mr. DUESENBERRY. That is one of the privileges of academics.

Senator DOUGLAS. Mr. Fellner.

Mr. FELLNER. I agree with what Mr. Colm and Mr. Duesenberry have said. May I put it somewhat differently, although the idea is the same.

If the business situation will be worse, then the deficit looks frightening, but I don't think that the conclusion really is that it is frightening. It looks frightening because revenue for fiscal 1959 would be 70 billions or less, I take it. Government expenditures, Federal expenditures, might reach 78 billions or more.

If we reduce taxes, and I am in favor of a temporary tax cut, then the deficit might approximate 20 billions, and this is a frightening figure. But I think that the answer to that is that we have now defined assumptions, set our assumptions in such a way that we need a large deficit or to put it differently, that this situation will not be valid because of the fact that in that situation, we would have this 20 billion deficit. That situation would not be valid——

Senator DOUGLAS. Income would rise and tax receipts would rise.

Mr. FELLNER. That is right. Therefore, the deficit would be smaller. If you start with this assumption that the business situation is going to get worse, then the outcome is apparently frightening, but I think the outcome at the end points to its being desirable to proceed in this fashion, that is to say, to have a potential very large deficit for a potential situation which we would like to avoid and which we, therefore, can avoid by this method. The calculation comes out a little less favorably, however, if we assume that we get a vigorous expansion beginning, say, this summer, because in that event the revenue of the Federal Government will perhaps be in the order of 74 billions, the figure originally estimated for fiscal 1959, or am I wrong in this, Senator?

Senator DOUGLAS. That is right.

Mr. FELLNER. The expenditures now, however, might be higher because we are committed to additional expenditures, might be 4 or 5 billions higher, and this deficit which now arises in a potentially very favorable state of the economy would be inflationary. Therefore, I think that the net outcome of this reasoning is that we should try to develop a plan by which we can slow down on our expenditures on the basis of given appropriations, say in the second half of fiscal 1959, provided that at that time we are in an inflationary or near-inflationary situation and this, I think takes planning, because if it is going to be done in a haphazard fashion, then the defense program is going to suffer from it.

We should have some plan by which we can slow down in the second half of fiscal 1959 provided at that time we are in inflationary or near-inflationary situation, we should have some list of priorities. I don't know whether it is possible to make some of these contracts in such a way that a slowdown or a suspension is provided even if somewhat more has got to be paid for it. But that, I think, would be worthwhile to try to somehow make contracts which enable the Federal Government to go slow on this in fiscal 1959 provided that the business situation then calls for slowing down the expenditure program.

Senator DOUGLAS. Thank you, very much.

Mr. Livingston, how do you feel on this danger of an existing deficit being increased still further by a program either of increasing expenditures or reducing tax rates?

Mr. LIVINGSTON. Well, I am not terribly concerned about the deficit. I think I indicated that when I suggested that the debt limit be increased so that we do have more flexibility in our operation.

Senator DOUGLAS. You said $285 billion.

Mr. LIVINGSTON. Maybe it ought to be higher. Actually I said I thought we ought to get rid of the debt limit entirely.

The problem, it seems to me, is how you reach this deficit. I feel a little bit like Polonius in Hamlet who always said Hamlet was still harping on his daughter. I feel I am still harping on the necessity of using this recession to advantage for the consumer.

Now, we have large Government expenditures and our Government expenditures are going to get bigger and bigger. I don't think that there is any question that big Government is not only here to stay but is going to grow and we will eventually approach the day when we have a hundred billion dollars a year in Federal expenditures instead of $70 billion, that is, provided there in no letup in defense.

Now, if that is the case, as taxpayers, as consumers of Government services, of defense items, we have got to get the most for our money and if we permit labor unions and corporations just to raise wages and prices in the market that we as consumers are creating by our purchases as taxpayers, then we don't get good value for our money.

This hurts the particular group that does not produce the kind of goods that the Government wants, military goods and durable goods, and maybe eventually research facilities.

So, I think that I would like to go easy during this period on a tax cut and I would like to see if some pressure could not be brought upon the steel union to forego at least part of this coming wage increase. And much as I agree with Mr. Yntema's idea that excise tax was a sumptuary measure and, therefore, ought to be eliminated (and I agree it should be cut in part), I would like to see the automobile companies do something to warrant my cheers when the excise tax is cut.

Senator DOUGLAS. In other words, what you are saying is reduce prices and costs to the level of incomes rather than raising incomes through ultimate injection of bank credit to the level of prices of cars?

Mr. LIVINGSTON. I would certainly like to think that this is a period when prices and costs ought to come down. If we don't use this period for reduction in prices and costs, all we are going to do is accumulate inefficiencies which essentially will lead to another recession which may become bigger and bigger, because how do we define a depression?—simply an accumulation of imbalances of one sort or another.

Senator DOUGLAS. Mr. Yntema?

Mr. YNTEMA. I have some of the same comments Mr. Livingston has made. The deficit, per se, is not what concerns me. It might be just as well to have a bigger deficit now and a smaller one later on. Furthermore, as I pointed out, the ratio of Federal debt to national income is down by half of what it used to be. But what bothers me is what might happen if we take action to create a deficit.

This point may have been brought out yesterday. It is important. In the change of gross national product from the third quarter of last year to the first quarter of 1958, expenditures on services increased, expenditures on nondurable goods were down one-half of 1 percent, expenditures on consumer durables were down substantially, and expenditures on plant and equipment are down some $3 billion. Outside of inventory liquidation, the reduction in gross national product has been something like 5, 6, or 7 billion dollars, not 15 or 20 billion.

My concern is we may do too much. If we do too much, I predict that we will have further inflation, wage inflation, and you will find the price level driven up. I don't think you will cure our difficulties by monetary and fiscal policy alone. I think we have a fundamental problem in the structure of unions and the structure of industry.

Senator DOUGLAS. In a free society, it is almost impossible for Government, except in special cases, to force business and labor to reduce costs and prices.

Mr. YNTEMA. I don't think it is, sir.

Senator DOUGLAS. You might be able to do that in a totalitarian state, but it is very hard to do in a free society. I have been trying to, in a sense, induce automobile labor and automobile management to go along, but there is not much more than that that the Government can do to maintain the principles of freedom of contract.

Mr. YNTEMA. May I speak to that?

Senator DOUGLAS. Surely.

25780—58——7

Mr. YNTEMA. I think there is a great deal more, Mr. Chairman, that can be done. There was a time when we allowed businesses to get together, when we didn't have an antitrust law. The area over which labor is permitted to organize is far greater than the area over which business is permitted to organize and combine. My feeling is, that this problem of inflation and unemployment will not be solved until we do something about the structural organization of the labor unions and keep on doing it in the structural organization of business.

Mr. LIVINGSTON. May I say something on that, Mr. Chairman?

Senator DOUGLAS. Surely.

Mr. LIVINGSTON. Aside from this structural organization of labor, the structural organization of industry, we also have the structural organization of the economy. Now, there are only certain times when you can do things like this. In a free society the Government can't order what shall be done; but there are forces at work now, and one of the forces at work is that you have a depression in the automobile industry and that depression has alerted Mr. Reuther to the fact that he ought to take a wage reduction in his own organization. It has also suggested to him that he postpone any immediate wage increase. He is willing to prolong the present contract.

Now, I think it makes a lot of sense, as Mr. Yntema said, that the automobile companies don't accept a 3-month prolongation, because all it does is to take them into the new model period, but the mere fact that Mr. Reuther has made that statement indicates that he is bowing to events.

Now, if the automobile companies were to suggest a price cut in order to get an excise tax cut and were to go to the steel companies and say, "Now, look, we think that we need a price cut," that would help.

The steel companies may not be receptive to the Congress but they are awfully receptive to the automobile industry.

And if the steel companies were then to go to work on Mr. McDonald something might be done and I think you have got a conjuncture at the moment which could result in major and basic price cuts, if we do not act too fast on taxes. And I think it is about time that industry and labor began helping itself instead of rushing always to Government.

Mr. YNTEMA. We have not rushed to the Government. The excise tax problem is before us, whether we like it or not, because of the reduction scheduled July 1.

And, incidentally, we have offered Mr. Reuther a 2-year extension and not just a 3-months' extension.

Mr. FELLNER. May I make one very brief comment?

Senator DOUGLAS. Yes.

Mr. FELLNER. This problem of wage-push inflation is really a very complex one and conceivably one that cannot be solved at just minor costs to society. But some English and some Swedish investigators feel that the rate of inflation is very sensitive to minor changes in the degree of employment, to relatively minor changes in the degree of employment; in other words, it depends a great deal on just how full that so-called full-employment is.

Now, I think that this isn't a definitive answer to the question, but some investigators feel that a good case can be made for this hypothesis that the sensitiivty of the rate of inflation to relatively minor changes in the degree of employment is very great.

Senator DOUGLAS. This raises some very profound questions.

Mr. FELLNER. Yes.

Senator DOUGLAS. The question of wage-price problems will be gone into by the full committee next week.

Mr. Curtis, do you have a question?

Mr. CURTIS. Yes, sir; just one thing. I am not going to pursue my original line. I am afraid I am going to have to write a book on that.

This may be a trick question, but previous panels have suggested one of the reasons behind their suggestions of possible tax reduction as a way of assisting in this present recession comes from their statements that we experienced in the 1954 recession that that was one of the factors that was very helpful.

Does this panel—I again emphasize this was a trick question—does this panel believe that that previous so-called experience is one of the reasons you think it might be helpful now if there is a 10 percent——

Mr. LIVINGSTON. In 1953 to 1954 you mean?

Mr. CURTIS. That is right.

Mr. LIVINGSTON. I think the conditions were quite different, Mr. Congressman, in 1953–54. Then you were having a decline in Government outlays and now you are having a rise. The tax cut offset the decline in Government expenditures.

Mr. CURTIS. The reason I said it is a trick question——

Mr. LIVINGSTON. I didn't say it is a trick question. I don't think it is.

Mr. CURTIS. The reason I say it is a trick, there really wasn't a tax cut that most people think because at the same time we reduced income taxes 10 percent we increased social security tax so the net result to the bulk of the consumer was about washed out and yet I find that economists have pointed to that as a factor in the elimination of the previous recession.

I personally analyzed it differently. That is the reason I said it was trick in the nature of a trick question. Because I don't think that that is anything we can go on in judging this even if this recession were regarded as a similar basis for it.

I would like to suggest that in the experience of analyzing the 1949–50 recession some economists have pointed out that it was the massive Federal expenditures coming about as a result of the Korean war that corrected that. I wonder if it was actually the massive expenditures as much as it was the employment of men which the war brought on, many at sweatshop wages because those that went into the Military Establishment didn't get too much in wages, and the employment that came through the new products that you had, you can say it is expenditures, but it seems to me more employment and conversely the 1954 recession came when the war was over and we had the similar number of men returned to the private section of the economy seeking employment.

It seemed to me that those were the elements, economic elements in the 1949–50 and the 1954 recession, and the one factor that I can see in the 1954 recession that changed things was the elimination of the excess-profits tax.

The only reason I point it out or pose that is it seems to me we can gain some knowledge from previous economic experiences, but in order to gain it it is necessary to properly analyze it and I am afraid at least the analyses that I have read of those two economic phenomena leave much to be desired.

If there is any comment——

Mr. LIVINGSTON. Mr. Yntema was just pointing out to me that the high unemployment occurred in February of 1950 and that was my recollection, and that was immediately before Korea which was in June of 1950. We were beginning to come out of it when the Korean war really made it, certified it.

Mr. CURTIS. I think that is a fair observation. Any other observations?

Senator DOUGLAS. I want to thank the panel. The two final comments that I should like to make, if I may be permitted to do so, are, first, the implicit feeling of members of the panel that by 1959 we are likely to get into what is termed "relatively full employment." We have the staff making some computations on what the gross national product would have to be, and assuming now the 4 percent unemployment which was roughly the figure of last summer, and providing for the growth in population and the normal growth in productivity, 1958 would require a gross national product of $460 billion, 1959 a gross product of $475 billion, and 1960 a gross product of $490 billion.

The current gross national product is approximately at the rate of $425 billion and, indeed, since one must go on a monthly and not a quarterly basis, it might be below $425 billion.

Now, to get up to these levels requires a tremendous increase in employment and productivity, and I confess that I am not as suffused with optimism at this point as perhaps some of the members may be. I think it is going to be a harder job to get back than some people think.

Mr. LIVINGSTON. This is 4 percent unemployment, sir?

Senator DOUGLAS. That is 4 percent.

Now, the second comment I would like to make is really a question of values.

Granted, of course, that you have seasonal unemployment and granted that you have transitional unemployment and that the rates for both of these are much higher in the United States than in England, and that therefore, Beveridge's level of 3 percent should not be applied in the United States. I myself find that I reject the view that you must maintain a considerable pool of unemployed in excess of the frictional unemployment in order to exercise a depressing influence upon inflationary movements on wages and prices, because I think then you are treating human beings as instruments really and human beings should be ends and not means. I would say this is a challenge which the Employment Act gives to America, namely, that we so devise our financial, our monetary, our tax, business, and labor policies that we can get substantial full employment without inflation.

I do not want to throw in the sponge myself, and, therefore, I do not want to accept the idea of a permanent pool of the unemployed to restrain inflation. I would say let us restrain inflation by other means and that this is a great responsibility upon the Reserve Board, upon the Congress, upon public opinion, upon management, upon labor, and I do not want to go over to this idea of a permanent pool.

Mr. LIVINGSTON. I certainly subscribe to that, Senator, despite my suggestions for the time being.

Senator DOUGLAS. Well, I want to thank you again. This has been a most interesting and productive morning.

We meet in room 457, Senate Office Building tomorrow morning to discuss alternative methods of reducing taxes.

(Thereupon, at 12:25 p. m., the Joint Committee was adjourned to reconvene at 10 a. m., Wednesday, April 30, 1958, in room 457, Senate Office Building.)

FISCAL POLICY IMPLICATIONS OF THE CURRENT ECONOMIC OUTLOOK

WEDNESDAY, APRIL 30, 1958

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON FISCAL POLICY, OF THE
JOINT ECONOMIC COMMITTEE,
Washington, D. C.

The subcommittee met at 10 a. m., pursuant to recess, in Room 457, Senate Office Building, Hon. Thomas B. Curtis presiding.

Present: Senators Paul H. Douglas and Hoblitzell; Representatives Thomas B. Curtis and Henry S. Reuss.

Also present: Norman B. Ture, staff economist, and Roderick H. Riley, executive director.

Representative CURTIS. The subcommittee will please come to order. Senator Douglas is going to be delayed for a few minutes. He has to testify before another committee.

This is the third day of the Fiscal Policy Subcommittee hearings on the Fiscal Policy Implications of the Current Economic Outlook. The purpose of these hearings, as previously indicated, is to bring out the facts about the Nation's current and prospective economic situation in order to provide the basis for formulating realistic and constructive policies to end the recession and to promote economic growth. We have met so far with two panels of distinguished economists. On Monday we examined the economic outlook for the remainder of this year and for 1959, and yesterday we had a discussion of the relative advantages in the use of tax, expenditure, and monetary actions in arresting the current decline and contributing to economic expansion.

Today we have another distinguished group with us to explore alternative approaches to tax reduction should this be necessary as a stabilization device.

We will hear the opening statement of each panelist before proceeding with a general discussion. Each panelist may submit for the record any prepared materials which he does not include in his opening statement.

Our first witness this morning is Prof.Roy Blough, Graduate School of Business, Columbia University. Professor Blough, we are happy to have you with us.

STATEMENT OF PROF. ROY BLOUGH, GRADUATE SCHOOL OF BUSINESS, COLUMBIA UNIVERSITY

Mr. BLOUGH. Thank you, Mr. Chairman.

In my appearance before the full Joint Economic Committee in February I expressed the view that if the economic situation worsened or did not show improvement by the time Congress was approaching adjournment, a temporary tax reduction should be promptly passed, the amount to depend on the estimated increase in Government spending. This continues to be my view, and every passing week has brought new support to the probability that economic conditions will call for such action. In view of the considerable time involved in passing even noncontroversial tax legislation, it is by no means too soon for both the House Committee on Ways and Means and the Senate Finance Committee to be actively engaged in work on a temporary tax reduction measure.

I have seen various statements in the press to the effect that Congress has cooled to a tax reduction because the public is not demanding it. What the public view may be in this situation should be considered largely irrelevant. Of course public opinion must control the goals of policy in a democracy, and with respect to this question it has done so, in the Employment Act of 1946. The application of policy is quite another matter, for it involves more technical knowledge and understanding than the public can be expected to acquire. This is pretty generally recognized with respect to monetary policy, the application of which has been delegated by Congress to the Federal Reserve System. It is equally important in the case of fiscal policy, which Congress has not delegated. If the Congress is to manage fiscal policy wisely, it must base its action on the economics of the situation, and lead public opinion, not merely follow it.

The purpose here today is to consider the kind of tax reduction that should be made, assuming there is to be one. Should it be temporary or designed for permanence? Which taxes or parts of taxes should be reduced? As I shall point out, the intended duration makes a vital difference in the kinds of taxes to be reduced.

While I would greatly welcome conditions that made possible a permanent tax reduction, I do not think we have such conditions now, in view of the expanding programs for defense and other purposes. To make substantial "permanent" tax reductions now would mislead the public and threaten to promote future inflation, since tax increases would not be easy to secure when needed. It is precisely the temporary character of a tax reduction that makes it a good instrument for promoting economic stability. The date when the rates would be automatically restored to their higher level should be stated in the tax reduction law. Precisely what that date should be may not be important, although it might be risky to set it later than December 31, 1959. Congress can extend the legislation if this turns out to be needed.

I am not impressed with the argument that unless the tax cut is permanent people will not spend the extra money. True, they might not enter heavily into installment debt on the basis of temporary tax reductions, but as to spending the money itself, I fail to see what the duration has to do with it, since after all, the money would be theirs—

they would not have to pay it back. Nor am I much moved by the related argument that people are fearful of the future and therefore will not spend but will save the amounts involved in any tax reduction. There is, of course, always likely to be some leakage into saving, but experience strongly suggests that a very large part of money added to the worker's pay envelope from whatever source is likely to be spent. At the very least, it would speed the day when spending was resumed.

I have recommended limiting a temporary tax reduction to personal income taxes. Why not make temporary reductions in excise taxes and corporation profits taxes, which are the other major source of Federal tax revenues? In the case of the excise tax, the reason is to be found primarily in effects of anticipated tax changes on consumer behavior. Excise taxes usually are added more or less in full to the prices of taxed commodities. At first glance, raising excise taxes and therefore prices during booms and lowering them during recessions appear to make such taxes an effective stabilization measure. Actually, such excise tax rates changes would almost certainly be more disturbing than helpful. Expectation of a decline in the tax would cause postponement in purchases in the early stages of recession before the decline took place, thus accentuating the downward movement. Expectation of an increase in rates in a boom would stimulate a bunching of orders to beat the tax. Orderly marketing would thus be seriously disturbed.

The considerations with respect to the corporation income tax are somewhat different. It is argued that a reduction in corporate taxes would stimulate corporate investment. A temporary reduction, however, would seem unlikely to have much effect of this kind. The central reason for decline in actual and planned expenditures for productive plant and equipment is not the lack of corporate funds but overexpansion of facilities combined with poor market prospects for products. A temporary corporate tax cut provides some funds but no promise either of greater sales or of higher future net return on investment.

The central need in the recession that tax reduction could help to fill is the need to sustain and promote consumer buying in order to prevent a downward spiral and lay the basis for recovery in production of both consumer goods and capital goods. A reduction in the personal income tax, although no certain cure for recession, is the quickest and most easily controlled method of filling this need that is available to the Government.

There are various patterns of income-tax reduction that might be followed. It has been urged, for example, that personal exemptions should be raised. Such a step would put money where it was most likely to be spent, but the proposal suffers from a major defect as a temporary tax reduction measure. It would mean taking millions of taxpayers off the tax rolls and then putting them back on again in perhaps a few months. This could result in misunderstanding and confusion, and might lead to unfortunate taxpayer relations and political action to make the reduction permanent.

I would suggest that the tax cut be fairly uniform across the board with not more than two brackets, because this is a simple and easily understood approach and because it minimizes the danger that tax reduction will raise a major controversy over tax reform. Care should be taken to make a clear distinction in the public mind between stabilization policy and tax reform. It is difficult at best to achieve public understanding of the use of tax changes for the purpose of economic stabilization and it may prove to be impossible if the revision of tax burden distribution is added to the picture.

The kinds of tax reduction that would be appropriate for a permanent law do not necessarily bear any close or positive relation to the kinds appropriate to meet the recession. When permanent reductions can be undertaken, excise taxes, corporation income taxes, personal exemptions, rates in the higher brackets, and many other features will deserve very careful consideration in order that the reductions may do the most to promote tax justice and long-run growth. If Congress were to see its way clear to make permanent tax reductions, there would be several directions in which it might move and pressed to be moved, and the debate would be long and vigorous, jeopardizing the quick action that tax reduction to meet the recession may well require.

Representative CURTIS. Thank you, Professor Blough.

The next witness will be Mr. Ralph E. Burgess, economist, American Cyanamid Co.

STATEMENT OF RALPH E. BURGESS, ECONOMIST, AMERICAN CYANAMID CO.

ALTERNATIVE APPROACHES TO TAX REDUCTION

Mr. BURGESS. Mr. Chairman and members of the committee, it is indeed a pleasure once again to participate in the vitally important work of this committee.

THE BACKGROUND CONTROVERSY

As the members of the committee undoubtedly know, there exists considerable difference of opinion as to the advisability of tax cuts during a period when prices are continuing to advance, month after month, to record levels. Some persons argue that, in view of the inflationary potential implicit in such widespread release of purchasing power, the corrective forces at work in the economy should be given free rein in an effort to bring about recovery in a natural manner. It is further argued, that a natural recovery of this type would occur as the inflationary excesses of the preceding boom were mitigated and would be essentially devoid of inflationary overtones.

STATEMENT OF PURPOSE

Although much can be said in favor of this view, I am convinced that such a course of action would not be effective in bringing early recovery. In the light of my conclusion, it seems fruitless for me to debate here the issue of whether or not we should reduce taxes this year in an effort to stem the recession, bearing in mind the international situation and the prescriptions placed upon the Joint Economic Committee by the Employment Act of 1946. In this connection, however, I would be remiss in my duty if I did not remind the committee that the human suffering occasioned by a more lengthy natural recovery would be insignificant when compared to the tragedy of a runaway inflation; a possibility which, in the present situation, is not as remote as it may seem. The economic world seldom permits us the luxury of a simple choice between good and evil, white and black. More often than not it is a gray world in which we are forced to choose between degrees of evil. However, operating on the assumption that for one reason or another tax cuts are in the making, I shall direct my remarks to an assessment of those principles upon which a sound policy of tax reduction, and one that minimizes inflation dangers, should be based.

CYCLICAL AND SECULAR REQUIREMENTS: A UNIFIED APPROACH

At the outset, I feel that a sharp distinction should be made between tax reduction as an element of compensatory fiscal policy and tax reform as a long-term objective. The former is usually viewed as a temporary phenomenon, a stratagem resorted to only in periods of crisis or near crisis with the objective in mind of restoring previous levels of economic activity primarily through increased consumption. As such, its objective is often dangerously restricted and its means often ill conceived in terms of the longer range requirements of economic growth and stability.

The attempts at basic reform of our tax system, on the other hand, although long recognized as a requisite to secular growth and equally appropriate during both recession and boom, are often innocent of short-term cyclical realities. In my opinion, neither of the two approaches can be economically sound in the absence of the other. Approaches to improvement of the tax structure must be cognizant of cyclical requirements; and tax reduction, as part of compensatory fiscal policy, should never be undertaken without reference to the longer range needs of the economy. It is my desire to convey to you, briefly, suggestions which, it is hoped, will exemplify just such a unified approach to the problem before us.

There is a need for encouraging both consumption and investment, considerations which, in my opinion, are vitally important both from the cyclical and secular points of view. Thus, while we deliberate on alternative forms of tax reduction as a means to stimulate the economy through increased consumption, in the short run, we should do so with the full realization of the depressive effect which our current tax structure has upon the savings and investment so essential to economic growth, in the long run. Proposals for tax reduction as a stimulant to recovery, therefore, should not only incorporate consumption generating features, but must be designed to fulfill the secular requirements of increased savings and investment, as but the first step in a long-term program of tax reform.

Such a program, in my opinion, to be effective in removing the existing deterrents to further investment should concentrate personal income-tax rate reductions in the middle and upper income brackets. As an ultimate goal, the gradual reduction of the maximum rate to a figure approximating one-half the present level would seem indicated. In consonance with this revision of middle and upper personal income-tax rates, the corporate tax rate should be reduced to a level no greater than the maximum individual income-tax rate. Such action with respect to the corporate tax rate would be desirable to avoid discriminating against the particular form in which one chooses to do business.

PRESENT INCOME-TAX CUTS

At the present time a comprehensive approach to tax reduction in line with the above principle would necessitate a broadly based personal income-tax cut affecting all taxpayers, lower, middle, and high income groups, without favoring any special interests and without eliminating any present taxpayers from liability. Thus, regardless of the income bracket of the individual, his purchasing power will be augmented; whether he spends, or saves and invests his tax saving, will depend upon his personal circumstances and desires; but in either event the economy will be stimulated. Further, I should like to add my voice to the growing chorus who recommend that such reductions be of a permanent nature. This is an important point affecting both the propensity to consume and the incentive to invest. It is well known, of course, that rates can and do move up and down as succeeding Congresses strive to meet expenditure requirements.

Tax cuts for those in the lower income brackets, who are characterized by the highest propensity to consume, would tend to bolster falling sales, further reduce inventories and generally stimulate production through increased consumption. In large measure, the same effect could be anticipated in the middle income brackets. However, a certain amount of additional savings could also be expected to result from reduction of levies applied to those in the upper middle income group.

With respect to taxpayers in the higher income brackets, the same percentage reduction in rates would, of course, release larger absolute amounts of income. Normally, we should expect that such increases in income after taxes would tend to be saved and invested, thus materially affecting the flow of funds to capital markets. An interesting side effect, however, might very well be a stimulation of the depressed consumer durables sector. Since these taxpayers, as well as many in the upper middle brackets, realize relatively large absolute gains from such a program, they are the very people who are in a position to make the more substantial outlays necessary for durable goods. This potential related effect could have rather significant repercussions in the sagging automobile industry for example.

CORPORATE INCOME TAX REDUCTION

It is strongly recommended that the tax rate on corporate income be reduced by at least 2 percentage points, as a part of the short-term program. This action should also be permanent in nature.

The intention here is obvious. By lowering this rather unrealistic tax rate, the profit expectations of businessmen would be materially improved. This, of course, should lead ultimately to an increase in income generating investment throughout the economy. While additional plant capacity may not be needed at this time, there are many opportunities for modernization and replacement that would be helped by a cut in the corporate rate. Since, for the purposes of short term corrective action, all business—both large and small—is essentially indivisible, preferential treatment for small business would not be crucial at this juncture. In terms of long range consideration, however, a continued differential in tax rates favoring the smaller businessman is definitely indicated.

EFFECT ON LONG- AND SHORT-TERM OBJECTIVES

Let us consider briefly the effect such a program as this might have upon the long- and short-term objectives of economic policy.

With respect to the short-term, the entire gamut of tax cuts would, of course, have an immediate effect upon the disposable income of potential consumers and investors. Further, these effects would be widespread with respect to geographic location, income groups and potential impact on various types of market. The permanent character imparted to such action would greatly affect the expectations of both consumers and investors and thus increase the magnitude of consumption and investment. Also, potential investment made possible by reductions in the higher brackets would, in large part, be actualized by cuts in corporate income taxes which improve the marginal efficiency of capital.

Such balanced and permanent action in pursuit of short-term goals would essentially fulfill many of the requirements of long-term economic growth and stability. Thus, not only would consumption be stimulated, but as we emerge from the trough, the flow of funds to capital markets would be increased, investment demand would be stimulated and the process of capital formation would be greatly enhanced. The lasting character of this action should be, as I have pointed out, but the first step toward a thorough reform of our present tax structure; reform which would insure a rate of capital formation more in line with the anticipated growth in population and the universally desired end of rising living standards for all.

Representative CURTIS. Thank you very much, Mr. Burgess.

At this time I have to announce with regret that Prof. Walter W. Heller was unexpectedly called back to Minnesota and cannot be here.

Representative CURTIS. Unless there is objection, one of our panelists yesterday, Mr. Colm, had intended to request the committee to place in the record an additional statement that he had and without objection that will be placed in the record at the time of his remarks.

Our next witness is Mr. Everett M. Kassalow, industrial union department, American Federation of Labor-CIO.

Mr. Kassalow, we are glad to hear you.

STATEMENT OF EVERETT M. KASSALOW, INDUSTRIAL UNION DEPARTMENT, AFL-CIO

Mr. KASSALOW. Thank you, Mr. Chairman. Let me say that my statement was prepared with the thought in view that we are here concerned with the question of alternative approaches to tax reduction in the light of the current economic outlook. I did not try to consider permanent tax reforms which may or may not be needed.

An immediate tax cut on individual incomes—a tax cut which will give substantial relief to low- and middle-income families—is the single most important thing Congress can do to halt the present recession.

This tax cut should preferably take the form of an increase in the present $600 personal exemption to $800. Additional tax cuts in the form of reduction in excise taxes and assistance to hard-pressed small business are also in order as part of a well-conceived program to restore employment and production.

Any reasonable analysis of present domestic difficulties points to the need for enactment of this type of tax program.

There is virtually unanimous agreement among economists that a major cause of the current recession as well as the boom which preceded it has been the ebb and flow of business investment.

For the 2- to 3-year period preceding the fourth quarter of 1957, the country was undergoing the effects of a record investment boom. By mid-1957 these effects took the form of excess industrial capacity in almost every line of industry. The growing gap between capacity to produce and ability to consume made for a sharp and inevitable downturn.

A few figures show these trends more graphically: Business investment in new plant and equipment which had already reached an all-time high in 1955 went up over 20 percent more in 1956. Business investment spurted again in 1957, and by the fall had reached an annual rate of $38 billion.

Looked at another way, during the 1955–57 period, the investment in producers' durable equipment and nonresidential construction grew at an annual rate of 5.5 percent.

Total gross national product over this period grew at less than half this rate while personal consumption went up only 2.6 percent per year.

This rate of investment obviously could not be sustained without a corresponding increase in consumption. To put it another way, a healthier pattern of growth would have combined a more modest rate of increase in business investment with a more substantial rate of increase in personal consumption.

By mid-1957 the sharp discrepancies were beginning to take their toll of the Nation's economic health. As early as July 13, 1957, Business Week magazine, in an article entitled, "Output Lags as Capacity Grows," took note of the widening gap between expanding capacity and lagging production.

This growing gap was already reflected in low levels of operations in autos, appliances, many soft goods, and even in steel. By September of 1957, Business Week estimated that manufacturing industry as a whole was operating at only 82 percent of capacity with serious effects on new business investment.

Editorially, the magazine commented, "The prime reason for this setback is that capacity has outrun demand."

More recently, viewing the downturn in hindsight, the National Industrial Conference Board, a business research organization, noted:

> It is becoming increasingly clear that America's capacity to produce manufactured goods has temporarily outrun its capacity to consume.

There are doubtless several reasons for these uneven patterns of development which have brought on this imbalance between ability to produce and ability to consume. However, one of the basic influences in this period was the ill-chosen series of tax changes passed in 1954.

This committee will recall that tax amendments enacted that year were designed primarily to encourage investment and investors. Judging by the economic trends of the past few years, they succeeded all too well.

In 1954 Congress revised the depreciation regulations so that business could write off two-thirds of the cost of new plant and equipment in the first half of equipment's life expectancy in contrast to the old method under which only one-half could be written off in the same period.

By 1956 it was estimated this meant a revenue loss to the Government and an immediate increased cash flow to business of $1,050 million. Additional tax changes in the treatment of research and development funds gave further encouragement to business to step up the rate of investment to what was really an unsustainable level. The 4 percent tax credit for dividend recipients was also the kind of tax change calculated to feed the investment boom.

Please do not misunderstand me. I know full well that the only economy that suits America is an expanding one in which business investment and productivity rise along with all other elements.

Clearly, however, there must be a working balance between these factors and in the period immediately behind us we failed to give adequate encouragement to consumption.

In making tax reductions to help pull us out of the recession, the only real choice open to us is to give top priority to tax cuts which will stimulate consumer buying. We must strengthen consumer demand to help clear the market of the tremendous potential product built into our great new industrial capacity. An immediate and substantial cut in individual income taxes, particularly on the low- and middle-income groups whose propensity to spend will naturally be highest, is necessary.

Talk of tax cuts to stimulate business spending is nonsense at a time when we are only using about 70 percent of our existing plant and equipment. To quote the National Industrial Conference Board again:

> The next business investment boom is not expected for several years to come. Probably not until the population rise in the 1960's.

The most rapid and effective tax cut to help the economy would be to raise the personal income tax exemption from $600 to $800. I am not impressed with the argument that this would drop several million taxpayers off the rolls.

When the Federal income tax was passed in 1913, it was recognized that sufficient income tax exemptions should be provided—

> to leave free and untaxed as part of the income of every American citizen a sufficient amount to rear and support his family according to the American standard and to educate his children in the best manner which the educational system of the country afford.

Measured against this standard, as well as the great increase in the cost of living in the past decade, the present income tax exemption of $600 has become completely outmoded.

Based on the United States Department of Labor minimum decent standard of living budget, it is now estimated that a worker with a family of only 2 children needs an annual gross income of at least $4,472. Setting the income tax exemption at $800 would bring us closer to the original objective of the Income Tax Act.

My own preference is for this type of income-tax relief, i. e., raising the personal exemption. I do not think it is wise to open up the question of individual income-tax rates when we are seeking quick action on economic measures to check and reverse a downturn.

For those, however, who insist on the rate approach, I commend to your attention that income-tax plan which would split the first $2,000 taxable income class into two classes of $1,000 each, provide a rate of 10 percent on the first $1,000 and leave the present 20 percent rate on the next $1,000.

Either of these two alternatives of income-tax plans, raising the exemption to $800 or reducing the rate on the first $1,000 of taxable income, would put $5 billion or $6 billion into the hands of consumers, with the great bulk of it going to the low- and middle-income brackets. This could not but strongly stimulate consumer spending.

To those who assert that giving the average family an additional $3 or so a week would not have any spending effect, I can only say that our experience in the labor movement argues to the contrary.

It is precisely because the amount is so modest that the fear that most of this would flow into savings seems groundless to me. Past experience indicates that when an average worker gets a 5- to 10-cents-an-hour wage increase, his standard of living is so modest to begin with that inevitably the great bulk of this increase is spent on a current basis. This is the magnitude of the tax cut we are talking about, an average equivalent of 5 or 10 cents per hour.

Some of the very people who argue that a tax cut now would be inflationary are also heard on the side of the argument that most people would save this money rather than spend it.

The argument ought to go one way or the other, because if it is saved, it is not inflationary. In any event, it is only someone who has had little contact with the average worker who thinks he will be in a position to save any such modest increase in his net income.

While it is hard to assess all the figures precisely, the 1954 experience, when income-tax cuts automatically took place as a result of the end of the Korean war, supports the position that increases in disposable income lead to increases in spending.

In that year, despite the recession and some decreases in personal income, cuts in personal taxes led to an increase in disposable income which sustained personal consumption expenditures and helped pull us out of that recession.

The detailed figures on income, taxes and spending in the 1953–54 recession are quite interesting. As the recession moved in, personal income fell from an annual rate of $287.3 billion in the fourth quarter of 1953 to $285.1 and $285.7 in the first and second quarters of 1954. Taxes were reduced, however, and disposable income actually went up more than $1 billion in the first half of 1954 as against the last quarter of 1953.

Personal consumption expenditures which had fallen between the third and fourth quarter of 1953, as a result of the downturn, turned up sharply in the first and second quarters of 1954, and the country began to move out of the recession.

Income taxes: Personal consumption, 1953–54—Seasonally adjusted annual rates

[In billions]

	Personal income	Less personal taxes	Disposable income	Personal consumption expenditures
3d quarter 1953	$287.5	$36.3	$251.2	$231.2
4th quarter 1953	287.3	36.1	251.2	229.7
1st quarter 1954	285.1	32.8	252.3	230.5
2d quarter 1954	285.7	32.9	252.9	233.1

Source: Economic Report to the President, January 1955, pp. 137, 148.

The positive influence of tax cuts in the 1953–54 period seems undeniable. There seems to be no reason why an income-tax cut today will not have a similar effect, provided we cut promptly and thereby reassure the Nation of our determination to restore full employment in the shortest possible time.

I also find little substance in the contention that there is plenty of money around in savings, and that all we need is "old-fashioned salesmanship." The best surveys we have of personal liquid assets holdings, those that are made annually by the Federal Reserve Board, simply do not support this contention of widespread holdings of savings.

The Federal Reserve Board surveys have consistently shown a very high degree of concentration of liquid assets, over four-fifths of personal liquid savings in the hands of only one-fifth of America's consumer spending units.

Moreover, the latest survey of the Board reveals that the median holdings of liquid assets early in 1958 were $500 as against median holdings of $580 early in 1957. If anything, one must anticipate that the economy's support from this quarter will be less this year than last.

Alleged or real savings are no substitute for income tax relief so far as propping consumer demand is concerned.

To help consumer demand, I also believe certain excise-tax cuts are in order. We have long since passed the period when the original purpose of these excise taxes was valid, namely, the desire to restrict consumption.

I think we should take steps to reduce or eliminate the excises on automobiles, tires, appliances, transportation, and all of the non-luxury goods.

Finally, in view of the special difficulties of small business in the downturn, it would be well to provide some relief here by adjusting the 30 percent normal rate on corporate income below $50,000 to 25 percent.

But we must not lose sight of the basic tax need at the present time. We must move swiftly to give relief to low- and middle-income taxpayers to shore up consumer demand and help reverse the present downswing.

The spectacle of steel at 48 percent of capacity, autos at even less, and appliances and other items similarly down is not a happy one.

This enormous waste at a time when there are still great unfilled needs on the part of ourselves and the entire free world is intolerable. A decisive income-tax cut is called for.

Representative CURTIS. Thank you very much, Mr. Kassalow.

Our next witness will be Prof. Richard Musgrave, department of economics, University of Michigan.

STATEMENT OF PROF. RICHARD MUSGRAVE, DEPARTMENT OF ECONOMICS, UNIVERSITY OF MICHIGAN

Mr. MUSGRAVE. Mr. Chairman, when I appeared before your committee just a year ago, the economy was still going strong, and I opposed early tax reduction. However, I added that I would favor reduction if a severe recession should develop, and that I would like to see increased flexibility in tax policy to secure prompt action. I now feel that the time for a tax cut has come, and that there has been an unfortunate hesitancy to act.

At the same time, I am not convinced that we are in for a long and outright depression. If tax rates are cut promptly now, and the decline is stopped, it may well be that some renewed increase in rates would be in order before the end of fiscal year 1959. Assuming an increase in budget expenditures of $3 billion above 1958 levels, and a decline in yield of $2 billion below 1958 levels, the estimated deficit for 1959 will be about $9 billion. Adding to this a loss of yield from rate reductions of say $6 billion, we arrive at a deficit for fiscal year 1959 of $15 billion. While I am all in favor of such a deficit if economic stability requires it, the economy may be sufficiently recovered early next year to permit at least a partial closing of this gap.

For these reasons, I should like to see the current tax reduction made in line with the following considerations:

1. The best approach may well be that which gets us the quickest action.
2. Those changes should be made which will be most effective in raising private expenditures promptly.
3. The cut should be such as to facilitate rather than hinder a later return to higher rates if and when needed.
4. Tax reduction should improve, or, in any case, not damage the long run equity of the tax structure.

Quick action: The need for quick action is my most important point. This is not the time to revive old controversies about loopholes or other defects in the tax structure. Let us agree on what is most feasible—be it a cut in income-tax rates, an increase in exemptions, or some package, including income and excise tax reduction—and get moving.

PROMPT EFFECTIVENESS

A good deal has been said about what tax cuts are most effective in the longer run, in meeting depression, and what taxes are most effective in checking inflation. This is not my major concern now. Assuming that we deal with a fairly short run decline rather than a secular condition, my major concern is with the speed at which the tax reduction wil be reflected in increased spending.

In this connection it is interesting to note a recent suggestion by Professor Katona, to reduce retroactively liabilities on 1957 taxes, with prompt payment of refunds, rather than to reduce rates on 1958 income. This might be difficult to implement, but it points in the right direction. Even if the reduction applies to 1958 taxes, it might be better to reduce the withholding rate and payments on estimated tax more sharply for a shorter period, say a quarter, than to reduce it lightly for the year as a whole.

Apart from this, I would place primary emphasis on personal income tax reduction with excise cuts second, and a reduction in corporation tax a late third. This is based on the thought that the primary need is for stimulating consumption; that, in the present setting of excess capacity, the best way to raise investment is to use fully the capacity we now have; and that investment incentives can be raised more effectively by reducing personal rather than corporation income tax rates.

I note here an interesting difference of opinion with Mr. Burgess' point.

In choosing excise cuts, we should note that the recession is concentrated in the durable goods and, in particular, in the automobile industry. A removal of the excise on automobiles might reduce the price by $150 for a low priced car, provided, of course, that we can be assured that the full benefit is passed on to the consumer. This may stimulate car sales; and even if it does not, the purchasers of cars will be able to spend more on other things.

REGARD FOR FUTURE REVENUE POTENTIAL

Chances are that expenditure requirements in the Federal budget will remain high and growing for many years to come, and tax reductions must be seen in the context of these requirements. I am as yet sufficiently optimistic about the longer run outlook to believe that, before too long, we may again be faced by a situation in which expenditures should be matched, or more than matched, by receipts. Therefore, the current cut should be made in a way which will facilitate the resumption of higher tax rates later on if needed. Unless this is done, I fear that political obstacles to necessary expansion and future expenditures of Government will be increased by current tax reduction and/or that we may run a future deficit when perhaps we should have a surplus.

One way of doing this might be to limit the tax cut to a short period, say a year. However, our experience with such provisions has not been good, and I am hesitant to clutter up the statutes with further requirements of this sort, requirements which may not be met anyhow, and which only serve to reduce the freedom of future action.

We shall have to find a way of making changes in tax rates which can be undertaken as a part of stabilization policy, up or down as conditions require, without interfering with the basic rate level and structure of the tax system. In line with this thought, I recently suggested to the Ways and Means Committee that the Congress should delegate to the executive authority to raise or lower first bracket rates under the income tax. These adjustments would be within limits prescribed and annually reviewed by Congress, and the President would be authorized to make such changes when needed to meet his responsibilities under the Employment Act. This, it seems to me, is the only way in which short-run adjustments in the tax structure can be made a working tool of stabilization policy, and in which such adjustments may be isolated from the basic problems of tax structure and level of rates.

I am aware, of course, that such a plan could not be introduced in time to meet the needs of the present situation, but it may well strengthen our ability to meet similar difficulties in the future.

REGARD FOR EQUITY OF FUTURE REVENUE STRUCTURE

Since I assume that revenue requirements will remain high for a good number of years, the present tax reduction should be made in a way which will do least damage to the longer run ability of our revenue structure to provide a large yield in an equitable fashion.

This is the reason why I would prefer to reduce income-tax rates at the lower end of the scale rather than to raise exemptions. The rate reduction will maintain the large tax base which we now have. It will enable us in future years to obtain the required revenue from the lower income groups in the more equitable form of income taxation, thus making it unnecessary to resort to the less equitable sales taxation. Similarly, I am against adjustments in the corporation income tax which, though perhaps helpful in the short run, would threaten to remain as loopholes in the longer run tax structure, even after higher levels of rates are resumed. All these considerations point to the imperative need of finding a way to adjust rate levels in a counter-cyclical fashion, while insulating the basic tax structure from such short-run changes.

In concluding, I would like to add a more general thought, which may well be more important than these considerations relating to detailed aspects of tax reduction. One of the disheartening aspects of the present situation is the tendency, found widely around Washington and elsewhere, to look upon tax reduction as a means of last resort, something to be undertaken only as an alternative to economic disaster. This, I believe, is a mistaken view. We ought to look upon changes in tax rates—and resulting states of deficit and surplus—as a more or less routine means of stabilizing the economy. We ought to accept the fact that the market economy by its very nature requires stabilizing action by Government; that built-in flexibility and monetary policy (which has been of very little help in recent months) cannot do the job alone, especially when it comes to checking a downturn; that the essence of fiscal adjustment is in securing a deficit or surplus; and that neither undue additions to the level of public expenditures in the depression nor undue restriction in the boom are required to accomplish this.

All this should be familiar by now and well understood, but recent developments make one wonder. Thus we find an elder statesman recommending a tax increase in the midst of a deepening recession, and a Secretary of the Treasury urging more and bigger savings, while retailers do their best to get consumers to spend. We find people responsible for stabilization policy arguing that a tax cut cannot be afforded, because yield has declined already due to depressed conditions; and that a deficit now will make for inflation later, as if there could be no subsequent adjustment in monetary policy. We find political leaders cool to a tax reduction, rather than explaining to the public why the principles of government finance must differ from those of private finance. In addition, we find a general tendency to rely on raising expenditure programs which will become effective only with a long lag, while tax reduction is shied away from because it is related too nakedly to the objective of creating a deficit. In view of all this, one wonders how depression-proof the economy has really become, and how well the lesson of past experience has been learned.

Representative CURTIS. Thank you, Professor Musgrave.

Our next witness will be Mr. Sidney Rolfe, C. I. T. Financial Corp.

STATEMENT OF SIDNEY ROLFE, ECONOMIST FOR C. I. T. FINANCIAL CORP., NEW YORK CITY

Mr. ROLFE. Mr. Chairman, my name is Sidney Rolfe. I am economist for the C. I. T. Financial Corp., New York City, and a lecturer in economics at Columbia University.

I wish first to express my gratitude to the committee for this opportunity to present my views in this distinguished company, on this important platform. In the course of my remarks, prepared and other, I am speaking as an individual.

I. The facts of the current recession hardly demand repetition. For purposes of discussion, however, these facts may be regrouped to reveal some meaningful trends, and by implication some remedies.

This is, I think, a classic capital expenditure recession, in its inception, following an expansion which overshot the mark in terms of capacity to current demand. A free-enterprise economy, while its growth curves may look smooth in retrospect, usually works in fits and starts, and some overshots of the mark or some lapse from total demand is to be expected. No employment policy can guarantee absolute precision in the use of resources at all times in a free society.

The question we face, however, is one of tolerable limits of excess or underutilization, and the related question of timing with respect to contracyclical policy.

The cutback in capital expenditures, starting in late 1957, was initially estimated to be a decline of 13 percent below the 1957 level. It has triggered an inventory reduction which amounted to some $7.5 billion in annual rates in the first quarter of 1958. In consequence, gross national product has fallen by $16 billion in annual rates from the peak of 1957 to March 30, 1958, or by $21.2 billion in annual rates, if constant 1957 dollars are used. The bulk of this decline results from inventory decumulation.

With respect to consumer expenditures, and unemployment, the greatest burden of recession has fallen on the consumer durable goods industry. Thus, comparing the first quarter of 1958 to the same period in 1957, durable goods expenditures have fallen 12.3 percent, while total consumer expenditures rose 1.6 percent. Nondurables rose 3.1 percent and service expenditures rose 4.4 percent in current dollars.

The impact of recession has reduced automobile production in the first quarter of 1958 by 31 percent from first quarter 1957, and new auto sales some 29 percent. It is hardly necessary to detail the dolorous story of employment in this industry. Spreading to related industries, steel output of 6.3 million tons in March 1958 may be compared to 10.6 million tons a year earlier (and parenthetically but perhaps not irrelevantly to 5.1 million tons in the Soviet Union).

All of these items of national accounts are well known. Some time ago, the Cleveland Federal Reserve Bank prepared an analytic, rather than merely descriptive, regrouping of national accounts which I think useful.

In this analysis, two basic divisions are used for classification. The stable, or secular-growth, sector has gone rolling along, like Old Man River. This includes nondurable and service expenditures in the consumer sector, and State and local expenditures in the Government sector. The volatile sectors, however, determine cyclical direction, and bear watching. These include capital investment by industry, and "consumer investment", including the volatile areas of housing and durable goods expenditures or in short, consumers' capital formation. Federal expenditures need be neither inherently stable nor volatile, but can provide, within the margins determined by defense and welfare programs, the swing element. The following graph illustrates the past postwar relations between the two volatile sectors, business and consumer investment.

(Graph referred to appears on p. 115.)

Mr. ROLFE. This recession is proving deeper than others because it is, at the moment a conjuncture of downturn in both these elements, the down force added to, at least in late 1957, by a decline in Federal expenditures.

It might be added that first quarter 1958 Federal expenditures of $49.7 billions was still 1.2 percent below first quarter 1957 in current dollars, and considerably further below in constant dollars.

The investment trend chart shows that at least since 1948, excluding the Korean war period, the relationship has been such that consumer investment has preceded capital investment in direction, and even indicated magnitude. This is not surprising since in an economy as highly oriented to consumption as this one, much industrial capacity building necessarily is for consumption.

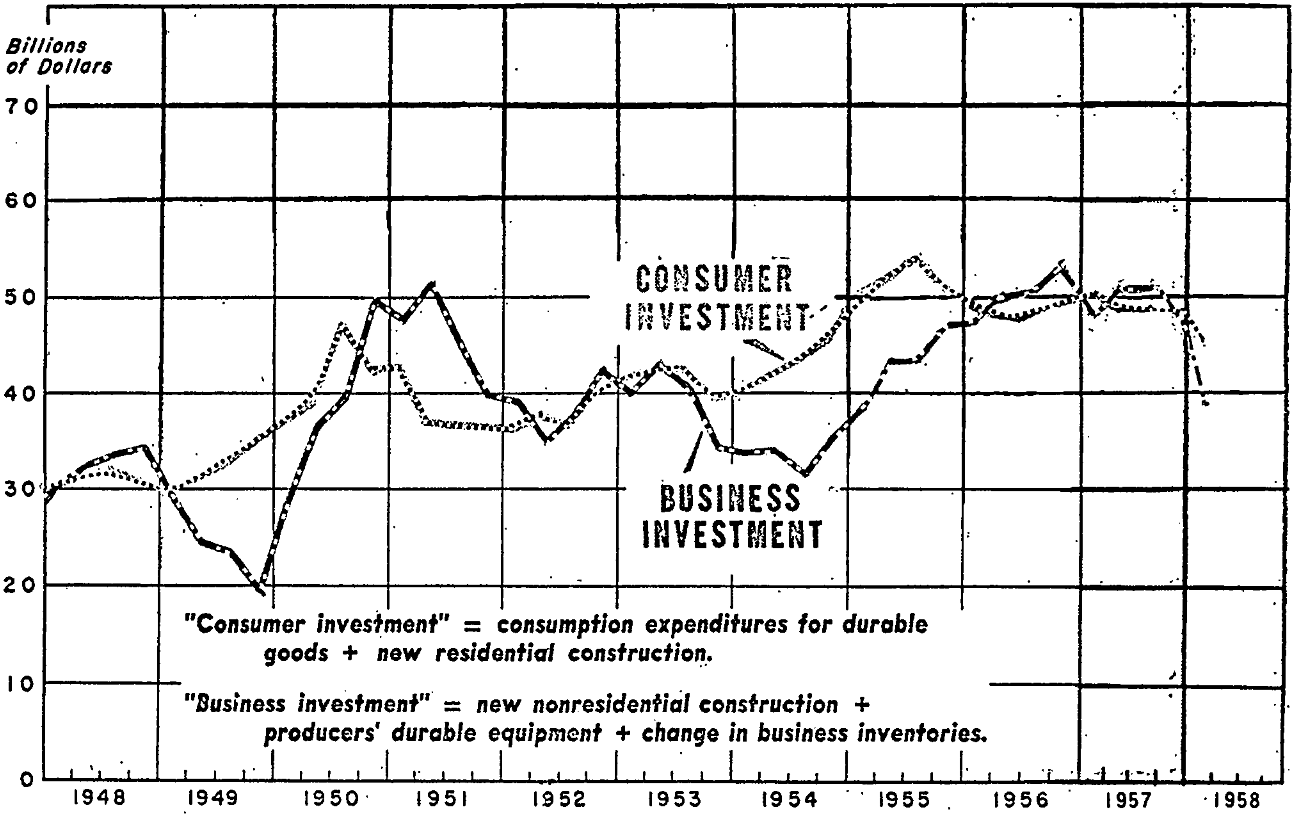
With an excess of plant capacity, it is quite clear that an upturn of the volatile sectors will have to await a return of increased consumer investment, and by the latter I mean mainly automobiles—show no very considerable signs of pickup at least for the bulk of 1958. Automobile sales were running, through April 20, at an annual rate of about 4.6 millions—seasonally adjusted. Actual sales January 1 through April 20, 1,300,300 new units of United States-produced cars.

The second 10 days of April had an average daily selling rate of 14,250, not much better than the year-to-date. Moreover, the forecasts now in the works, to which production schedules are being geared, do not look for much improvement.

The Federal Government has taken some steps to overcome this decline in consumer investment. We all know the Federal Reserve's easier money policies have resulted in reductions in interest rates and, most significantly, in an inflow of funds to the mortgage markets. Financial intermediaries are picking up mortgages heavily, and even buying many of the outstanding FNMA issues.

The change in VA policy has apparently had some effect, although whether it affects the total demand for housing or merely indicates a pickup in the VA sector at the expense of the more conventional sectors remains yet to be seen.

(Information referred to follows:)



Seasonally adjusted annual rates, plotted quarterly.

C.I.T. FINANCIAL CORP., ECONOMICS DEPT.

There is no easy Federal action available to shore up consumer investment in the durable goods sector. However, it is obviously to this end that many of the suggestions regarding a tax cut have been made.

Reading the various accounts of tax-cut proposals, ranging from Dr. Arthur F. Burns' proposal of an immediate $5 billion tax cut—A. F. Burns, The Business Recession, the Commercial and Financial Chronicle, New York, March 27, 1958—to the more hypothetical statements by Mr. Nixon, Mr. Martin, and the Federal Reserve bank presidents, there is unanimity with respect to the means to be used, but not with respect to the timing.

On the general subject of a tax cut, I do not have anything to offer other than what has been said by the various statements which have been issued. However, it seems to me that a reduction in the excise tax on automobiles, or preferably its elimination, would be a stimulus to automobile sales, a very much-needed step at the moment. Elimination of the excise tax on automobiles would, in my opinion, increase auto sales some 300,000 to 400,000 new units over current estimates for this year. This not only gives needed relief to the auto industry and its employees, but would also serve to increase workers' income and corporate profits, enabling the Government to recoup from these sources some part of the revenue lost from excises.

I have prepared some more extended remarks and data on the excise tax and the automobile industry generally, to which I will turn, if there is time in the ensuing discussion. In this preliminary discussion, I would like to state, however, what may be my bias, but I think are supportable economic hypotheses.

First, that it is virtually impossible to restore economic health to this Nation without a healthy auto industry, because of the very size and importance of that industry.

Secondly, that excise tax repeal is one of the cheapest, as well as one of the most effective, antirecession measures which can be taken.

Third, that talk of excise tax reduction by the Congress now without corresponding action is hampering auto sales now since many consumers are awaiting this reduction.

I might add parenthetically that many dealers are promising to pay the consumers the reduction when it comes. Even a decision not to eliminate excise taxes would be clarifying and in a weak way helpful.

Elimination of the full 10 percent excise tax on autos would mean a price reduction of about 6.6 percent at the retail level, as the tax is imposed on the manufacturer's price. I have no doubt that an excise tax cut now would be passed on to consumers by overstocked dealers. For that two-thirds of the new-car-buying public who use installment credit, a 6.6-percent price reduction would mean monthly payments reduced from about $87 currently to some $82 per month on the average. This is a very significant reduction. It is equal to nearly the entire increase in monthly installment payments since late 1956. That one-third of the new-car buyers who do not use credit of course obtain a direct price reduction.

The question may be asked why not further lengthen terms to attain the same type of monthly payment reduction for the credit buyer. A general lengthening of terms is virtually impossible now, and it would not be desirable. Installment terms are at their limit with respect to collateralized auto values.

Longer terms now would be a disservice to consumers, in that they would diminish equity, and to the economy as well as they would invite greater credit losses in the short run, and consequent credit stringency as a result.

A mere reduction in monthly payments will not, of itself, induce greater sales. Installment credit is like all credit; its absence hinders sales, but its presence does not assure sales. There is excess capacity, or, more accurately "excess reserves," in the installment industry now, which is not being used, because the initial decision to buy durables is lacking. Once durable sales rise, however, I think the lower monthly payments will be an added stimulus to pickup.

In advocating a reduction or elimination of automobile excise taxes, I am in effect advocating what is commonly called the rifle approach; that is, a specific tax remedy for a specific ill.

On the subject of more general tax reductions, I have said I have little to add to the general argument. However, my bias leads me to believe that a general tax reduction now would be wise. I base this admittedly tentative conclusion on my own estimation of the immediate future, that is, that inventory reduction at the rate of $7½ billion will go on into the second quarter, and that even with a tax cut, this decumulation could be at the rate of about $3 billion in the third quarter, rising to zero at the end of the year.

While I am fully aware of the steps which have been taken by Congress and others, and of the impact implicit in these steps, I regard it preferable to take a calculated risk now to place recovery ahead of inflation as a short-run goal. We have tools to combat inflation. The tools we have to combat deflation are not as proven, particularly as we have no tools to combat mounting fear and what Mr. Erhard has called our psychological short circuit.

The London Economist has dubbed this the "confident recession." We all know that confidence can be lost, however, and that it is most difficult to rebuild. I would, to repeat, rather risk more inflation than further loss of confidence, but the Congress obviously must judge the relative strength of forces on the basis of its more complete knowledge than I have.

II. Since the rise of Federal deficits in the late 1930's and particularly in the 1940's, this Nation has been confronted with a new magnitude in the area of taxes and fiscal policy. We have one way or another used taxation and fiscal policy as contracyclical devices, and indeed we set great store by such use.

Without exploring the subject fully in this brief statement, I am impressed with the fact that deliberations such as these should, in my opinion, focus on the question of tax reform as well as tax manipulation.

This is, of course, a most important subject in itself, and I would like only to raise 2 or 3 issues which I think relevant.

First, our thinking about tax policy has been developed in terms of short-term expedients, imposed in the present period by the cold war and the need for large defense budgets.

I think we all assumed at one point that these would be temporary and thus certain elements of our tax program such as high corporate and high individual surtax rates were appropriate as expedients. However, if we make another assumption, namely, that we will have not only a long-run defense program to cope with, but also a longer-run need for a high capital expenditure program to reach the $600 billion GNP implicit in the full employment estimates a decade ahead, as well as larger private investments abroad, particularly as common market and the free trade are grow, the high tax rates of the past may prove limiting factors in our growth.

Second, while plant and equipment are certainly important elements of American strength, it is by now apparent that we face a gargantuan task in the expansion and improvement of the quality of our intellectual resources as well, which also demands consideration under a long-term fiscal program.

Third, the importance of flexibility, as well as the relative impact of taxes on various sectors of our economy, is a concern to all of us as citizens.

In conclusion, I would like to state the opinion that fiscal policy, because of its vast importance now and because of its relative newness, may occupy the same position in national thinking as monetary policy did at the turn of the century. The time may well be at hand for something similar to the Aldrich Commission for fiscal policy, to study further the unknown question of incidence of taxation, and the related questions of timing, flexibility and the relationship to the several goals of national life which this Nation will be called upon to meet in the period ahead.

Certainly the Congress and its staffs have dealt with these complex problems exceedingly well in the past. But the future deliberations of Congress may well be benefitted by a comprehensive study of the bearing of fiscal, as well as monetary, policy on the longer-term goals we as a people have developed and those which have been thrust upon us.

Representative CURTIS. Thank you very much, Mr. Rolfe.

Our next witness is Mr. William W. Tongue, economist of the Jewel Tea Co., Inc.

STATEMENT OF WILLIAM W. TONGUE, ECONOMIST, JEWEL TEA CO., INC.

Mr. TONGUE. Thank you, Mr. Chairman, members of the committee, I appreciate very much the opportunity to be here this morning.

I might say before I start that I have been impressed as Mr. Rolfe has with the tendency for action taken to meet a particular situation to become built into our political structure as time has gone on; therefore, I would agree that we should take this opportunity to give more consideration to long-term factors.

We cannot afford to continue for long to have over 5 million people unemployed, with needless human suffering here at home and possibly abroad. Also, continued recession injures our cause in the ideological struggle for men's minds in the uncommitted areas of the world. More than that, from a practical standpoint, we have a very real need to keep increasing our material resources to offset the ever-growing strength of the Communist bloc. For example, steel production in the United States currently is barely above that in the Soviet Union.

Any tax reduction decided upon should, therefore, be for the dual purpose of restoring full employment and also of promoting long-run growth to advance our position in the world.

The need to stimulate growth and innovation in our economy would seem clear. We are beginning to recognize this in the physical sciences and generally in education. Attention is increasingly centered on ways to stimulate the exceptional student to greater effort and attainment in the interest of society as a whole.

This apparently is also being recognized in the Armed Forces in the new pay scales. But in the field of Federal taxation, we continue with a structure designed during World War II and the Korean war for the purpose of holding down private economic activity and discouraging spending on goods, particularly those requiring steel and other metals.

Surely then, if tax revision is feasible at present, the first order of business should be to rescale the present rate structure of the individual income tax to stimulate and channel individual effort into productive activity. An enormous waste of effort by talented individuals currently goes into finding ways to divert income into areas where it avoids the clutches of the tax collector. I know of no studies on the extent of this waste, but that such efforts are practiced widely, and successfully, is attested to by the Tax Foundation revelation that in 1953 taxable income in excess of $100,000 per return was less than half the amount of such income reported in 1916.

This last statistic suggests that a substantial reduction in the progressiveness of the individual income tax might cost very little in terms of reduced tax collections and might even raise revenues over a period of time as income is channeled back into taxable areas. In any case, even without a substantial increase in reported income in the upper brackets, the cost of a cut in rates would not be large since nearly 85 percent of the present individual income tax liability is attributable to the first-bracket 20 percent rates.

A reduction in the progressiveness of the individual income tax would not only be sound from the practical standpoint of stimulating constructive individual effort; it also appears to accord with the public's notions of equity. According to a Gallup poll conducted approximately 2 years ago, people think taxes on the income brackets from $10,000 up should be about half what they are now.

A second tax that clearly seems out of step with the need to stimulate growth is the tax on corporate income. The rate should be reduced to a maximum of 50 percent and preferably lower in the interest of promoting economy in corporate expenditures.

One cannot be certain how stimulating a reduction in the corporate rate might be to the economy, but I would note that in the 1954 recession, when there was a substantial cut in corporate incomes taxes, there was only a 10 percent decline in the rate of business capital expenditures from peak to trough compared with double this in 1949 and probably again now.

Reduction of the high-bracket individual rates and the corporate rate would have some tendency to increase saving, as well as spending, though it is impossible to say with accuracy how much. In the long run, increased saving will be necessary to permit the buildup of our Nation's capital assets. The tax reductions suggested would be particularly helpful to the growth of small business ventures which are so dependent for equity capital on plowed-back earnings.

I strongly believe that these long overdue steps should be taken now, and that the cuts should be permanent. The revenue loss, if any, would not be of the order of magnitude which would seriously add to possible inflationary pressures in the future.

Another area where taxes were deliberately imposed to discourage sales as well as to raise revenue is the general area of excise taxes, with particular reference to automobiles, other consumer durable goods, and freight and passenger transportation, industries which currently seem to be suffering about all of the discouragement they can stand. It would appear that such taxes have lost their original reason for being and they should be reduced or eliminated at the first opportunity.

Reduction of excise taxes would be reflected in lowered prices to consumers. This would benefit those unemployed directly as well as indirectly through stimulating the general recovery of the economy. Also, this is an area where a temporary reduction in rates can be at least as stimulating to the economy as a permanent reduction, and perhaps susbtantially more so.

Thus, if it appears that Federal expenditures will rise in the future to a point where a lowered tax structure could not reasonably be expected to produce a balanced cash budget at full employment, a temporary reduction in excise rates now would serve to stimulate consumer expenditures, while the restoration of rates later would tend to discourage consumption if that should be thought desirable. In general, however, I believe we should concentrate tax relief as much as possible in areas where permanent changes can be made now, in order to avoid capricious results which may not be lasting and may result in uncertainty about long-run market potentials, thus causing unwise investment to serve those markets.

Finally, if the economic situation permits a further cut in taxes, I believe we should reduce the basic rates of the individual income tax. This would release substantial amounts of income now flowing to the Federal Treasury and make it available for spending. In the present monetary environment of declining interest rates and greater availability of funds, past experience suggests that consumers will respond to a tax cut with greater expenditures.

For example, in the 1954 recession, spending on housing and other consumer goods and services rose from an annual rate of $242 billion in the fourth quarter of 1953 to a rate of $275 billion in the third quarter of 1955. The rise of $33 billion was actually $10 billion greater than the increase in disposable personal income over the period and amounted to approximately 85 percent of the total rise in gross national product.

Such was the power of tax reductions reinforced by easing credit terms in the 1954 recession. So vigorous a response in the present situation seems unlikely since consumers have larger debts in relation to incomes than was true in 1954. Consequently, they are not in a position to take on as large an amount of added debt if a part of their future income is freed of tax. Also, it seems unlikely that credit terms would show a pronounced an easing as in 1954.

Finally, a temporary tax cut could be expected to be less stimulating than one considered to be permanent. Nevertheless, the experience of 1954 offers grounds for believing that a tax cut will lead to greater consumer spending.

In summary, our present tax system carries forward a rate structure and types of taxes which were designed to raise revenue and discourage the use of scarce resources under wartime conditions. The present, therefore, offers an opportunity not only to make tax reductions in the short-run interest of stimulating recover of the economy, but also in the long-run interest of promoting growth and savings to build up the capacity and strength of our country.

Representative CURTIS. Thank you very much, Mr. Tongue.

That completes the papers of the panel.

I should have announced before that it has been our custom to permit the panel to interrogate each other in the event they want to do that, too. You might bear that in mind if any of the panelists do want to interrogate their own members within the committee proceedings.

Before we go to that, I will ask Senator Hoblitzell if he has any questions.

Senator HOBLITZELL. I believe, Mr. Rolfe, you mentioned about a commission to study our tax policy. Would you want to elaborate further on that?

Because of the uncertainty in the public understanding of these matters, I think we need some clarification. Have you any suggestions regarding that?

Mr. ROLFE. I don't know that I have any terribly concrete suggestions. I quite agree with you that public understanding of the nature, the effect, and the difficulties of what might be called tax engineering as opposed to tax policy should certainly be increased.

At the same time, those who make tax policy and change the rates, I think should have something akin to a longer term goal.

I think we as a country have almost willy-nilly ended up with certain long-term goals. We talk about full employment, we talk about the gross national product necessary to get there. If we accept this as a desirable end, and it is in the full employment Act of 1946, it seems to me that many of the facets which led to that should be integrated with this long-term goal.

One hears about roadbuilding and one hears about education and plant and equipment; but somehow one does not hear about them all in a very integrated fashion. This is what I am driving at.

Senator HOBLITZELL. The opposition to tax reduction more or less hardened when Mr. Baruch made his statement, and of course, is given impetus by economists and political leaders who make contradictory statements which confuse the public. One man said something about savings in his paper this morning. The report on savings indicated a substantial increase all over the country.

I know in my own bank, our time deposits were up 11 percent in January and the overall employment is declining. When I take the desk as a lending officer on occasions when I get home, I find people are scared and feel they are not getting value received for the things they do buy, particularly the automobiles. There is a buyer strike of new automobiles because they are too high. They are also thinking in terms that the excise tax will be reduced, and if I wait 3 or 4 months, I can save $150.

Mr. ROLFE. Exactly.

Representative CURTIS. We are happy to have with us a member of our full committee, Mr. Reuss, who, although not a member of the subcommittee, may ask any questions he wishes.

Would you rather do that now or would you rather have me go ahead?

Mr. REUSS. Would you go ahead, Mr. Chairman?

Representative CURTIS. Before I go ahead, maybe the panelists are bursting with questions they would like to ask fellow panelists. Maybe we can have that now.

Does any panelist wish to question any of his colleagues?

If not, then I will ask a few questions, if I may.

As I gather the testimony of the full panel, the theory behind tax reduction which would go into the consumer area to bolster consumption is based on the assumption that that in the long run will create more jobs. Am I right in that assumption?

After all, I do make a distinction between the taxpayer and the jobless. I think we all agree that the consuming power would be best utilized in the hands of the jobless and the jobless is not a taxpayer. So all this talk of tax reduction will not help the jobless unless it produces the economic effect of somehow creating jobs. That is why I posed the question.

The real question I am getting to is, How much of a lag do you think would be involved in that process?

Mr. ROLFE. I would like to try to answer that, sir, or at least give my opinion.

It seems to me that the unemployment figures which we have indicate a rather frightening concentration of unemployment in certain types of industries and those related to them. I refer specifically to automobiles and steel and related industries. That is why I think that if one wants to think in terms, as a short-run goal, of increasing employment, whether it is absorbing the unemployed or lengthening the working week for those who are partially employed, one ought to shoot for the specific areas in which the unemployment is most severe.

A relatively small tax cut could very well increase the amount of services that people are buying, and the amount of nondurable goods they are buying, without increasing terribly much the durable goods they are buying and not doing very much for the jobless situation we have. The estimates which have been made indicate—I advocated repeal of the excise tax for the timing—that excise tax elimination will produce about 330,000 more sales; if true, this results in 125,500-odd jobs, that is, man-years of employment in the auto industry.

These won't necessarily be 125,000 new employees, but it will be lengthening of workweek, a lot of new employment, and so forth.

It seems to me if one wants to shoot for a specific target, that is the one to shoot at.

Representative CURTIS. Yours is the rifle approach and it seems that the other would be the shotgun approach.

I would ask this added question: How can you be sure that the consuming power would be spent in durables as opposed to soft goods and services where consumption is still up?

Mr. KASSALOW. Mr. Chairman, I think there are several factors in this situation. I think one factor is the problem of delay that Mr. Rolfe mentioned. The London Economist called this the confident recession. I think if we go along another 6 months, perhaps even a shorter period of time, and then attempt some modest tax cuts, the chances are the effects will be much less than if we move swiftly.

It is true that probably most of the population still retains a good deal of confidence in the economic future, 6 months or 1 year ahead; if, however, we persist with a period of 5 or 6 million unemployed for an additional 5 or 6 months, I am afraid the measure of confidence still left can be undermined and any tax cuts at that point will have very little effect. People will begin to try to hold onto whatever resources they had.

The first point I make is that for any of these tax cuts to have maximum effectiveness, I think they should be put into effect fairly soon, within 1 or 2 months. Under those circumstances, if people are still confident, I think there is a very good possibility we will get a great deal of spending as a result of those tax cuts.

On the second point, I think we should probably have a combination of tax cuts involving both income tax and excises.

I think our economy is really too complicated, however, to say if you get a general income tax cut and people only spend generally that additional $2 or $3 a week, this will not help durables. I am not sure that is the case. The money will flow into the corner grocery store or perhaps textiles.

Maybe the textile manager will find his income up and he may buy the durable goods.

Mr. ROLFE. Isn't that the very timelag you are afraid of?

Mr. KASSALOW. I don't see how, if you get an immediate increase of $3 or $4 in the paycheck of the average worker.

Representative CURTIS. I want to make one other comment if I may there.

I noticed in your paper, and I think Mr. Tongue referred to it, too, and others, the experience we had in the 1954 recession in utilizing the 10 percent cut in income tax that occurred that time. It ignores at the same time there was that 10 percent decrease there was an increase in social-security taxes, which for the lower income groups practically wiped out any tax benefits.

I wonder if you can refer to that as an example where the economy was stimulated. Perhaps there are other economic factors that underlay the recovery from the 1954 recession.

Professor Musgrave, I believe you were going to comment.

Mr. MUSGRAVE. Yes. I would also like to say a word about the matter of speed.

Mr. Kassalow is very correct in urging the point that what might be done by a $1 billion tax cut now might cost a $5 billion tax cut if we wait 6 months, simply because the public response would be much better now than after the business outlook deteriorated further.

As to the immediate speed with which we can expect a response in spending—I am thinking here primarily on the part of consumers—the consumer will spend more when his real income increases.

If you cut excises, he pays less for a car, he has more income left for other things, and he will spend more. If you cut income taxes—

let us say if you cut income taxes at an annual rate of seven billion—spread over the year, this will mean that this month there may be an increase of six hundred million or so in disposable income, and you get only one-twelfth of the effect to begin with. The rest is spread over a year.

Therefore, if more of the income-tax cut could be concentrated in the earlier period, it would be more potent. The advantage of the excise cut is that it would concentrate more in the earlier period.

Now to Mr. Rolfe's more general point of the rifle approach versus the shotgun approach. This is similar to approaching the problem by having WPA-type of public works, where you go to the area, where you go to Detroit and put the unemployed automobile workers to work. Or you can say you have a tax cut on automobile excises so as to increase specifically the automobile demand. In a sense this rifle approach is more effective.

But, as Mr. Kassalow pointed out, this also involves a cost. It tells consumer demand where it has to pick up and it may be that there is something to be said for using a more general approach, even though it might involve a somewhat larger deficit. Who cares about minimizing the deficit? In so many cases this is a tacit assumption, that we ought to economize on the deficit. We ought to have that deficit which raises income in an efficient way. This may not be the minimum deficit.

It may be better to have a larger deficit, cut taxes more generally, have this involve a change in relative prices and let the consumer spend wherever he wants to spend and raise the economy in that way, rather than subsidize the automobile industry which maybe ought to take a beating because it produces these awful cars nobody wants.

Representative CURTIS. Mr. Blough.

Mr. BLOUGH. Mr. Chairman, I assume it is always understood in hearings that silence does not give consent to what everyone else says. So without commenting on some points with which I might not agree, I would like to speak directly to your question.

If what you are after is an immediate impact on the automobile industry, the excise-tax reduction, in my opinion, would have a more rapid effect than anything else involving comparable revenue. If such a reduction is seriously contemplated, there should be an announcement by everyone involved that the excise-tax cut will be made retroactive to the date on which consideration was announced by the Committee on Ways and Means, since otherwise sales would be substantially discouraged during the waiting period.

I am in some doubt that the modest decrease in the price of automobiles resulting from an excise-tax cut would have a large effect on the sale of automobiles although of course there should be some increase. There are other factors than price in the automobile situation, including the fact that in the heavy competition of a couple of years ago automobiles were sold at a rate that quite clearly could not be sustained.

I would not object to a cut in the automobile excise tax. I would hope that we might get helpful results from it. But I do not view it as a very important antirecession measure.

Turning to the question of a general tax reduction, its immediate effect would not be on consumer durables. Its very important function would be to prevent us from sliding, down and down and down. The general economy has not yet been greatly affected by the recession, but economists live in continuing fear every day that the downward spiral will begin in earnest. The bolstering of general consumer spending through tax reduction would, I think, be a very powerful force to prevent that downward spiral from getting underway and to give a general stimulus to rising spending. This, together with the wearing out of old cars and the paying off of old installment debt would help change psychological attitudes and lead to a recovery in the durable-goods industry as well.

Representative CURTIS. Thank you.

Mr. Burgess.

Mr. BURGESS. Mr. Chairman, it may have been noted that I did not recommend a cut in excise taxes in my statement. I prefer the general approach. I am less optimistic than Mr. Rolfe with respect to the possible effect of a cut in excise taxes in stimulating sales of automobiles.

Further, I fear that setting a precedent for selective reduction of excise taxes as a part of compensatory fiscal policy may very well plague us in the future, if not at present, when manufacturers of appliances, TV's, and other hard goods may insist that the taxes on their articles be reduced also.

Further, and perhaps most important, is my belief that we have a limited opportunity now and always to achieve much needed tax reform, which I emphasized in my statement. I believe that some measure of reform can be achieved while we are reducing taxes to stimulate the economy.

I would be reluctant to use these limited tax-reduction tickets in lowering certain selective excise taxes where the final impact on the economy is apt to be small.

Representative CURTIS. Thank you.

I will go on to one other general question and then turn it over to Mr. Reuss.

I cannot help to comment that as a member of the Ways and Means Committee, to notice that whenever an industry is declining or is sick, they also look at taxes, and I might add tariffs, as a possible source of their woes, when it seems to me there are other basic economic factors lying at the base.

Your point of tax reform, or as I term a tax revision, brings up the question that I have been asking. So much emphasis has been made on tax reduction, which I distinguished—and I know this is semantics to a degree, but I think there is a real economic distinction—between tax reduction and tax revision. For the purposes of my question, the distinction I seek to make is this: The tax reduction is trying to take purchasing power out of the Government sector and put it back into the private sector. Tax revision might do that, but its essential purpose is to remove an impediment to economic growth and possibly would create a different balance in the private sector of the economy. It actually might reduce the tax take to the Government for a short time, but there would be a recoupment, if the theory were right, through the growth that would ensue if the impediment were removed.

25780—58——9

To illustrate it specifically, I think some mention has been made of the taxes during the Korean war, or World War II, really. The transportation tax was imposed to impede the use of our transportation system. That was the economic effect it sought to achieve. If that tax did achieve that economic result, if it were removed it would create a stimulation of economic growth in that area.

. The cabaret tax, which to me on economic analysis is a tax on any eating establishment that employs musicians—we get very little revenue from that particular tax. That is another illustration that would remove it if it were an impediment of growth in that sector.

You can go down the list of the small-business tax bill which I have put in, which seeks to permit to retain a certain amount of plowback. I want to emphasize that 85 percent of the small business does not operate under the corporate form. We have a great tendency to talk of small business as if it were doing business under the corporate form. That is only about 15 percent.

Particularly I want to direct attention to this panel, and I wish the country were more aware of it, to the fact that there are 2 very tremendous tax revisions or tax-reform bills sitting over in the Senate right now, which have been the results of 2 years of study. One is the excise bill of some 300 pages, which includes what we thought in the Ways and Means Committee, removals of impediments of economic growth.

The Mills bill does the same thing in the corporate and personal income tax.

The first bill went in 1957 and the Mills bill went over there early in January of this year. Normally it would have gone over in July except that we ran into a minor difficulty on a specific issue. I wish more attention were paid to this early tax reform. I know some of the panelists' papers have suggested that would not immediately affect the present recession.

I think Professor Musgrave made that suggestion, if I interpreted it right. If that study had already been made, do you not think immediate movement in that area could be beneficial, depending on what happens to be in the specific bills?

Mr. Musgrave. If I may briefly reply to this, your distinction between tax reduction on the one side and tax revision on the other side is a very sound one. As I see it, the problem of tax revision is always with us, if we define this to relate to matters other than stabilization considerations. This involves not only growth; it might be other things, such as equity and so forth. A sound governmental mechanism should somehow provide for the possibility to conduct this stabilizing function of adjustments in the level of rates, a reduction now and perhaps increase a year from now, without interfering too much with other aspects of tax policy.

We should conduct this as a matter of continuous operations similar to the open-market operations of the Federal Reserve. It could not be a day-to-day operation because the mechanics of changing tax rates differ from the mechanics of selling and buying bonds. But in principle, it ought to be the same. Maybe quarter to quarter, maybe half year to half year, we could have adjustments in tax rates, with the view, as a matter of course, to stabilize the economy. These adjustments should be taken as routine matters and be entirely noncontroversial.

The public does not worry about open-market operations, but it worries about changes in the level of tax rates. They are the same thing.

In addition, of course, you have these problems of tax revision. In the long run, they are just as important. It may be that right now we are in a situation where your revision objective would fit in very well with the stabilization objective. But it may be that another time the two might not move together, as for instance in a short-run inflationary situation.

Thus, I agree that we should always think about the revision problem, and that maybe in the long run it is the more important thing. Yet, I feel that there ought to be a distinction, and that we ought to make some arrangement whereby the stabilizing type of changes in the level of rates ought to be done as a routine matter. I would even go so far as to say that this ought not to be the business of the Ways and Means Committee. The function of the Ways and Means Committee, as one might interpret its spirit in terms of the constitutional provisions, is to assure that the Congress has control of the Government's purse strings, and the way in which the money should be raised.

This is very sound and certainly ought not to be impaired. But this is something very different from short-run adjustment in stabilization policy. We would not really maintain that the Banking and Currency Committee should every week decide what ought to be done about open-market operations. It ought to set the Federal Reserve Act, and the statutes and the short-term operations should be left to the Federal Reserve. We should do the same thing in dealing with tax policy with regard to stabilization, but not with regard to basic level of tax structures.

Representative CURTIS. The comment I would like to make there is this: There are some of us, certainly myself—in fact, I go so far as to say that our present recession to a large degree is the economic result of an uneconomic tax structure—if we were to remove these uneconomic features to a degree, we could probably solve some of the underlying causes. That is a very difficult thing to establish.

I might say to Mr. Rolfe in that connection—suggest that an Aldrich-type commission for fiscal policy would fit in that. I would call attention to the fact that this fiscal policy subcommittee conducted some rather extensive hearings in December 1955, had some excellent papers prepared, on the subject of the economic effects of our tax structure.

To a large degree, the philosophy I am expressing here is derived from those studies where it looked like to me that if we did not do something about reforming or revising our tax structure, we were going to have exactly the type of thing that has occurred. If we do not revise our tax structure, we are going to continue to be in the soup, even though we may be able to put in some temporary palliatives.

Mr. Tongue.

Mr. TONGUE. Mr. Chairman, I think your point is extremely well taken from a practical standpoint. With our present tax structure, tax reform almost inevitably means tax reduction on balance, particularly if you get into the excise field. Conversely, tax reduction, though it be called temporary, will probably wind up as a more or less permanent tax reform, as so many other "temporary" taxes have.

Representative CURTIS. May I interrupt you a minute to get on the same thought. I do not believe that would be so. For instance, if you believe that an excise or a tariff can get beyond the point of diminishing returns, a reduction in rate can bring in more revenue. Likewise, I call attention to a proven fact, I think, that the removal of the excess-profits tax was really a tax on growth and new industry produced more revenue through the normal corporate tax after its removal than the combination of the returns from excess profits and the corporate tax. That is why I tried to make the distinction that tax reduction actually economically is transferring purchasing power from the Government sector to the private sector. My definition for the sake of this discussion, at any rate, was where you actually did not have a loss of Federal revenue. You gained it through the growth you gained from removing an impediment.

Mr. TONGUE. I think that could be quite true, especially for reducing the "progressiveness" of the personal income tax.

Mr. KASSALOW. The excess profits tax was a temporary measure. It is not fair to judge it.

Representative CURTIS. From the tax standpoint, the things that are temporary, like the communications and transportation taxes, what is temporary?

Mr. MUSGRAVE. In the thirties you had a big depression with no tax structure to speak of. There is much in favor of what you say, I am sure. Yet there is a question of just how far these things would go in increasing investment at a time when you have excess capacity, in the short run.

Mr. BURGESS. Mr. Chairman, I should like to express a different point of view than some of the panelists have with respect to the need for stimulating investment in the short run and at the immediate time. In this connection I am happy to note a similarity between my paper and Mr. Tongue's, although I assure you there was no collusion between us in advance.

I point out that business expenditures on plant and equipment, although the total is expected to decline by some 12 percent this year from last year, will still amount to more than $30 billion, or 7 or 8 percent of our gross national product, and still represents a most important contributing factor to our well being and to the health of the economy. A great portion of that $30 billion goes for modernization and replacement of facilities that are obsolescent in an effort to reduce costs, to improve production. Although expansion of facilities may not be immediately required, this continuing investment to improve our facilities, to reduce costs, is very badly needed.

There are serious deterrents in the tax structure to that type of savings and investment. Those deterrents ought to be removed not only for the long-term but to aid the immediate situation.

Mr. ROLFE. I would like to answer 2 or 3 points or comment on 2 or 3 points that have been raised, which I think tie together.

The first has to do with this business of subsidizing the automobile industry. I am not proposing an excise-tax reduction to subsidize the automobile industry. I am saying that if you want the consumer capital sector of these volatile curves to turn around, something has got to be done in this area. It may happen of its own accord, but it is going to be a long time.

Combining the long and short run of this, it seems to me it is quite obvious that the Government in one of its branches, not through taxes, but through monetary policy, has done this, namely, the change in interest rates, the change in veterans' business and housing, is aimed precisely at increasing consumers' expenditures in the consumer investment area. This is precisely the point that Mr. Musgrave made and you were driving at and I mentioned earlier in terms of an Aldrich Commission. It seems to me that we have pieces often going off on tangents or randoms, and we don't have a long-run pattern or goal at which to shoot. I am not trying to demean the work of the various committees. I am aware of some of them. I think they have been excellently done. I do feel in the current case, for example, I am not at all sure that further growth of the automobile industry should be stimulated. Perhaps the same amount of effort should be put into university growth, and if we want to focus in one area, Mr. Musgrave's university would be the ideal candidate.

But the point is, it seems to me, that not having a pattern of the relative merits of growth in one area as opposed to another, we face each short-run situation as though it were a de novo situation, and we don't know how to integrate the long and short.

I never agreed with Lord Keynes when he said in the long run we will be dead, but it does seem to me that the long run is nothing but a series of short runs. Unless we give ourselves a good idea, I don't see how we can go through. The only part of the Aldrich Commission is that after a great many of these year-to-year manipulations in the monetary area, was put in the administrative hands where it could be coped with on this level with some long-run goals in mind which should remain the province of the people of the United States through their Congress to delineate. Unless we have something like that, it seems to me that every time we come to a place like this, everybody puts his oar in the water, pitches for something or other, and the Congressmen in their deliberations must be to some extent impressed at any rate by the very special pleas that are made.

Representative CURTIS. I certainly appreciate that. I could not agree with the gentleman more of the need for something of this nature. Mr. Blough.

Mr. BLOUGH. Mr. Curtis, the problem I see with trying to achieve tax reform as part of an antirecession measure is that different people have conflicting ideas of what would be good for the economy in the long run. If you could get real agreement on that, and get a bill through Congress in a reasonable time, then I would agree that a time when we can give up some revenue is the best time to achieve tax reform. But it is a very big "if."

Representative CURTIS. May I comment that is what I was just saying. We have two bills. One is 300 pages long and there is a lot of stuff in it. The excise bill was the result of 2 years of study and passed the House. The Mills resulted from 2 years of study in this area. They are spelled out. No one apparently studied those to find out what the economic results of those reforms would be. I can point out lots of little things in there that would be tremendous in their stimulating effect. The cumulative effect, I think, would come very close to giving us the shot in the arm we need, and we wouldn't have to do all this talking.

Mr. KASSALOW. Mr. Chairman, while I appreciate as everyone else does the need for a better long-term framework for the tax structure, it seems to me that some of the comments that have been made here today are somewhat distressing to me. I could take, for example, the positions that Mr. Tongue and Mr. Burgess made about reform of tax structure to stimulate investment spending and perhaps make a contrary set of arguments. What bothers me is that we are confronted really with an immediate economic situation. I think if we begin to open up the whole tax structure to this kind of debate, we will be 6 months from now still looking for some tax measure to help us in the present period. For this reason I think it is well to remember that in the first place the Congress will be confronted with certain tax decisions by June. There will be certain automatic changes taking place in the corporate tax rate and excises. So it seems to me the Congress will have to have a tax policy geared especially to the present situation before that time or else it will have a tax policy thrust upon it.

Representative CURTIS. I might say that I have seen some of these extensions come about and the practical way it happens, the Ways and Means Committee will meet for about 5 minutes and we vote to extend it, and it goes through the House and Senate the same way. So because there is a deadline on there really does not mean it will be restudied, I regret to say.

Mr. KASSALOW. If we did not have the current recession, if we did not have general agreement that general industrial capacity appears to exceed our ability to consume at the present time, I am not talking about the long-term problem, perhaps we could let the thing slide or deal with this in the long-term manner. Confronted with the basic economic problem at the present time I don't see how we can get around some serious consideration of some help to low and middle income groups to stimulate consumer spending.

In this it is hard to give specific instruction, but we have an immediate economic situation to deal with.

Representative CURTIS. I hate to cut this off, but I would like to have Mr. Reuss ask his questions now.

Representative REUSS. Thank you, Mr. Chairman.

I am really going to continue this subject. Let me ask Mr. Rolfe on this question of the rifle approach as opposed to the shotgun approach you advocated I think the rifle approach, saying that heavy industry, particularly the automobile industry, was having it so much worse that is where it should be concentrated. Is that not true?

Mr. ROLFE. Yes, sir, that is the first part.

Representative REUSS. I would like to raise a couple of questions in connection with that. First, according to the March Census Bureau employment figures, while unemployment among experienced workers in durable-goods manufacturing was alarming—it came to 11.6 percent—unemployment among experienced workers in nondurable manufacturing was also quite alarming and came to 8 percent. Isn't there something really to be said for the shotgun stimulating consumer purchasing power across-the-board approach?

Mr. ROLFE. There is something to be said for it, but I am still very much impressed with this fantastic concentration of unemployment and difficulty in specifically these durable-goods areas. I can't argue with the figures. I wouldn't argue with them anyway. I am not sufficiently familiar with them. It does seem that when you get unemployment approaching 16 percent in cities like Detroit and Pittsburgh in the related areas that something specifically has got to be done there.

My argument is, Mr. Reuss, not only related to the current employment situation. If I may take a moment, I would like to look at the 1954 business that was raised before. What is the sequence of events actually in the period subsequent to 1954? I think it shows up in this chart the Cleveland bank developed, and I think it might be analyzed a little further.

The upturn in consumer spending and particularly in consumer investment started late in 1953, According to this chart, and the increase in capital expenditure was subsequent to the increase in consumer expenditure at that time. That has been the history in this cycle we have had since the war.

What conditions were present in 1954 which are not present today? It seems to me in the first place in 1954 the stock market was still rising, which gave a lot of confidence to people who had some stock. Second, and I think this is very important, with respect to durable-goods purchases, and particularly automobiles, installment terms were lengthening at that time, and that added a certain amount of purchasing power to the economy in specifically that sector. Neither of those conditions is present today. Therefore, if we want to turn this consumer investment program around, and we are trying to do it in housing, it seems to me we have got to do it in the other durable-goods areas. I believe if we do this, then the income generated and the increase would work through the economy and work into the nondurable goods sector as well.

Representative REUSS. Mr. Chairman, I was an interloper from the full committee asking that question so I will yield happily. I will just ask this question of Mr. Blough. I rather liked what you said about the relative irrelevance of the public reaction to tax cuts, and whether there should really be one at the present time. I am interested in that. I conducted a questionnaire sent out to some 130,000 of my constituents, in which I ask the question, as I recall it, as a means of combating the current recession, do you favor (*a*) a prompt tax reduction to stimulate consumer expenditures, (*b*) public-works programs.

I have not fully tabulated these yet, but the results are somewhat curious and bear out what you say; namely, an overwhelming majority of those who replied are for New Deal-type public-works programs. They use a lot of white space on my questionnaire to say why. However, only some 46 or 47 percent are for a tax reduction, and they explain with great patriotism and virtue that they do not want to do any inflationary things.

I think this bears out the observation you were making, but I would ask you this question: Is an understanding of the nature of compensatory tax reductions or increases really beyond the grasp of the public? I would not think so. I think people in this country have a more practical economic education and the public shows a greater grasp of this particular economic problem, even though I agree that open-market operations are not only beyond the reach of the many in the public, but beyond the reach of many of us here in the Legislature.

Mr. BLOUGH. Mr. Reuss, I have very great faith in the American public's ability to grasp the important facts of life and to make important policy positions. I had hoped they had achieved somewhat greater understanding than they apparently have in connection with this problem of recessions. They are not altogether to blame—a lot has been said that confuses them. Someone with a reputation of being an extremely good economist comes up and says that this is the time to raise taxes and not lower them. One little thing like this can do as much to tear down public understanding of this problem as you might do to build it up in a year of patient discussion of the question.

So it will take time. It is coming, I think. If you will examine the attitudes of Government officials and Congress and bankers and businessmen and the public generally in the latter years of the twenties and the early years of the thirties in comparison with the last few years, you cannot help being optimistic. A very great deal has been done in improving public understanding. I am hopeful of the future. But there are limits. In the application of policy you are often dealing with matters which are abstruse and technical. If the Congress decides, as it has in the past, that it wants to keep fiscal policy in its own hands, then it will have to act in an intelligent and technically informed manner, just as it would expect of someone to whom it delegated fiscal policy.

Representative REUSS. Thank you very much.

Mr. MUSGRAVE. May I add a word to this, Mr. Reuss, because I feel very strongly about it. As Mr. Blough pointed out, there has been a good deal of gain in understanding of these problems. If you look at the statement of the CED, at the statement of the Rockefeller group, many of these statements have been very enlightened about all this. This is certainly a very great step forward. On the whole, I feel that the less enlightened statements about it in many cases come from Washington. This includes the administrative as well as the legislative branch. It seems to me tremendously important, as Mr. Blough points out, to be consistent, and whatever the situation is, explain what should be done on the basis of a sound compensatory principle. Every time when we have an inflationary situation, and we sell the need for keeping taxes high, not by arguing properly as we should, but by saying that an unbalanced budget is immoral, we go 10 years back in dealing with the next recession.

We are now suffering for the sins of recent years, when under conditions of inflation we used the wrong arguments to defend the then proper objective of keeping taxes high and of having a surplus. The educational process is one that is continuous. Every time it goes wrong, you go 10 years back.

I would add, however, that it would help Congress if there were institutional arrangements by which they could tell the public, their constituents, I am in favor of stabilizing the economy with tax adjustments as required in the short run, but I am also in favor of the long-run principle that we should make public expenditures only if they are worth their money, and if the people who pay the cost really want them. I think we need an institutional arrangement whereby the Congressman can consistently take both of these positions vis-a-vis his constituents.

My previous proposal of delegating part of the tax adjustment goes along these lines. I would add that this problem is not too difficult to explain. At the same time, it is not really simpler than the problem of open market operations. It is just that the bankers and people concerned with central banking have built up such a mythology and anthropology and structure around this thing that everybody thinks he can't understand it. They just got away with this. Banking policy is not any more difficult, and it should be just as open to the public as tax policy.

Senator DOUGLAS (presiding). I must apologize to my colleagues for being absent so long a period of time. I had to testify this morning before the Senate Interior Committee on another matter, so I have been delayed until now in coming. I will try to read the morning testimony to find out what has been going on here. I would like to ask a general question, if I may.

As you know, I have been an advocate for some months now of a tax cut. Every time the tax cut is proposed, objections are offered that this will mean inflation and a rise in prices. Of course, it is true that a tax cut with the normal expenditures of Government continuing or with increased expenditures will require borrowings by the Federal Government, borrowings in large part from the banks which will create the monetary purchasing power to purchase the Government securities. Therefore, there will be an increase in the effective money supply.

The reason behind this fear of inflation is that if you increase the money supply in relation to goods, the price level will rise. I do not want to foist my own views on anyone here, but I should like to express my own feeling in relation to this matter, and ask you very frankly whether or not you agree. If you disagree, I want you to say that, too.

It has been my own feeling that a tax cut or an increased program of public works, although I favor the former more fully than the latter, will through the operation of the multiplier principle result in an appreciable increase in the gross national product. That is, it will cause people to buy more, which will lead to more production, which will lead to more employment, which will lead to more purchases, which will lead to more production, and so on. Just what this multiplier is, we do not know fully. Our own computations are roughly that it will be around three. It may be less and it may be slightly more. If this is true, and only if this is true, a tax cut of $6 billion should lead ultimately, although not immediately, to an increase of some $18 billion in gross national product. That will be not merely a money figure; it will be goods and services which otherwise would not be produced and which should result in idle labor being put to work with otherwise idle capital producing goods and services which otherwise would not be produced, and which should raise the gross national product which at the present is $20 billion less than it was last October, and should be growing.

If this is true, am I correct, or am I wrong in thinking that this increase in gross national product will largely help to offset the increase in the money supply? The money supply as I remember at the present is about $120 billion. The gross national product is $425 billion. The ratio of gross national product to the money supply is about $3\frac{1}{2}$ to 1.

In other words, is this a situation in which we merely increase the quantity of money, M in this formula, or is it a situation in which we also increase quantity of goods and services on the other side of the equation and thus help to counterbalance or possibly even completely negate the increased prices which would come if you merely increased the money supply but the quantity of goods remained unaltered?

Therefore, it seemed to me that the immediate increase in prices would be far less than people assumed. While I don't have the benefit of your discussion, it seems to me that any pressure for an increase in prices would be largely offset by selling bonds in the open market and restricting the policy at a later time if that is necessary. Am I off on the wrong track?

Mr. BURGESS. Senator Douglas, I would be happy to have the privilege of commenting on your statement.

Senator DOUGLAS. I would appreciate it.

Mr. BURGESS. In my opinion, under present circumstances of large numbers of unemployed and some excess capacity in industry, your statement is essentially correct. I think if there is any flaw in that contention it lies more in the fact that fiscal policy cannot be quickly turned off and on. While under present conditions the quantity of goods available may increase as rapidly as the monetary supply, we might very quickly reach a point where there was danger of inflation, that is, where we could not turn off the fiscal policy which had initiated it, and where monetary policy might not be adequate to handle the situation. I do believe there is risk in enacting a major reduction in taxes at this time—a risk of that nature.

Senator DOUGLAS. What about the possibility that if inflation comes later it could be offset by open market policy of Federal Reserve Board selling governments, thereby diminishing the reserves of the member banks, and decreasing their lending capacity?

Mr. BURGESS. That, too, would be available to the monetary authorities and presumably they would employ it. Perhaps it would be as effective as it was in 1955, 1956, and 1957. Nevertheless, there is no assurance that it would be adequate nor that it could stem the inflationary tide.

Mr. TONGUE. Senator Douglas, I think there is some distinction to be made here between the effects on the money supply and the effects on income. I think most people would agree that the Federal Reserve, for example, is in a position to influence the money supply in either direction irrespective of the deficit situation of the Federal Government, within certain limits. As a matter of fact, the money supply is now rising very rapidly as a result of the substantial easing of Federal Reserve policy in the past few months. This does not directly influence spending, however. The creation of a deficit, on the other hand, permits a direct increase in total spending in the economy. It does nothing to curtail the Federal Government's expenditures while it does permit private individuals and others, depending on where the tax cut is made, to increase their spending. So you do get a net increase. Whether that is inflationary depends, I think, as Mr. Burgess mentioned, on whether you have unemployed resources which can be drawn in.

Senator DOUGLAS. We have those now, Mr. Tongue. You have at least 5,200,000 unemployed, 3,500,000 working less than full time, and probably 30 percent of the manufacturing capacity of the country lying idle.

Mr. TONGUE. Today I believe we have the resources to meet an increased demand without inflationary consequences. The only question is whether a year from now this combination in addition to large Government expenditure will create too much pressure on the economy. I agree at that time the Federal Reserve can reverse its present policy if that should be necessary.

Mr. MUSGRAVE. I agree with your general analysis, Senator Douglas. I would just emphasize the point that while we may look at what happens to the M and and what happens to the T, the real crux in the equation is always what happens to V. In dealing with a depression we start out with a premise that any measure which will increase the money expenditures will increase prices. This will be so, whether the increase of money expenditures results from an increase in the money supply or results through the multiplier operation on the income side. Suppose we compare two policies to meet the present situation. In the one case we finance a deficit by new money. In the other case, we finance a deficit by borrowing. I would say under the present setting, we might expect that the debt would be sold largely to people who have idle balances on the second case, and that the increase in the money supply under present conditions would not lead to increase spending in the first case. In the short run the effects would be more or less the same whether the deficit is financed by debt creation or money creation.

It may be a bit more expansionary with money creation, in which case we could do with a smaller deficit, which might make some people happy. If we take a longer run view it might make a difference if we create debt or money now. If we create debt in competition with private debt, this may make for a less buoyant situation later on, and require less restrictive Federal Reserve action than would be the case if we now create money.

Let us start out with the premise that you have to have a deficit or surplus to meet economic imbalance with the fiscal mechanism. If you have a deficit you have to create claims, money, or debt. If you do this, this has implications for monetary policy later on. If we assume that monetary policy cannot handle these when they result, then we are driven to the conclusion that monetary policy is impotent, and that the only way you can secure stabilization is by lowering or increasing the balanced budget.

My conclusion is that we ought to forget about these later implications of claim creation which results now. If people want to worry about it, let us finance by debt rather than money creation.

Senator DOUGLAS. The creation of debt would lead to creation of added bank credit.

Mr. MUSGRAVE. Not if you sell it to the nonbank public.

Mr. BLOUGH. I do not want to go into this interesting argument about the source of funds and so on, because I think it has been very well handled. I would like to speak more generally in support of the position you have presented. Any economic growth requires the various sectors of the economy in total to spend more in each succeeding period than was received in income in the previous period. Speaking broadly, deficit spending, whether by the consumer, by business, or by government—perhaps by all three—is a necessary condition for growth. It is not all that is required for economic growth, but it is one of the necessary conditions. The deficit you would create through a tax cut in a period such as the present would, it seems to me, result chiefly in the expansion of production and only to a minor degree in rising prices. Whether it would mean rising prices eventually would depend to a considerable extent on the growth potential of the economy and how it responds to increased demand. You might not have any inflationary problem at all. However, I am a little worried on that score for the future, and that is the reason I have put emphasis on the temporary character of a tax reduction so that Congress would be obliged to take another look in a year or so to see whether the reduction should be continued.

Senator DOUGLAS. I may say I have had the staff prepare some estimates of what the gross national product would have to be in terms of current price levels to provide what we may term "full employment," say, 4 percent unemployment. They estimate that it would have to be $460 billion this year and $475 billion in calendar 1959, $490 billion in calendar 1960. Again I want to say this is on the assumption of stable prices, 4 percent unemployment, but a normal growth factor of around 3 percent. Against this we have a current annual rate of gross national product of not more than $420 billion. So it seems before we got up to full employment, we would have to rise by $40 billion this year and by $55 billion next year. Therefore, is there not latent capacity within the economic system to provide for an increase without any substantial rise in the price level?

Mr. BLOUGH. I certainly think so; there is the latent capacity. It is not inevitable that it will work out that way, because you may not get balanced demand or balanced production.

Senator DOUGLAS. I agree.

Mr. BLOUGH. There is the potential for it, certainly.

Mr. KASSALOW. I am in general agreement with the position you outlined, Senator. I think you stated it well in emphasizing that we could not ignore the future inflationary problem as it might occur. The thing that bothers me all through this period is that it seems so easy to arouse such great moral fervor about this future inflationary problem, and even the problem we have had, and there does not seem to be enough concern about the enormous waste of over 5 million people unemployed, and the figures in gross national product which you yourself cited.

Mr. TONGUE. Senator Douglas, I certainly agree. Incidentally, I made some calculations of the full employment level of gross national product and I came up with the same figures. I agree there is plenty of room for expansion without inflation. I would like to emphasize that I think we should not continue with the current level of unemployment any longer without taking some action. I believe we should face whatever inflationary problem may come in a future year when that problem arises, and do what we need to do now to treat the problem we have today.

On the other hand, I have in my testimony placed considerable emphasis on long-run considerations in suggesting the type of taxes that should be cut. I would like to clear up one point. Mr. Kassalow suggested that I was emphasizing reduction in the progressiveness of the personal income tax, and cutting the corporate tax below 50 percent, as a means of stimulating investment. I think it would have that effect, but I would say that my major concern is to promote the economical use of the resources we have and having people work in desirable directions as determined by consumer preferences. Also, these reforms would not cost anything to speak of in lost revenue and would not complicate future action in fiscal matters.

Secondly, where we could get a considerable addition to purchasing power would be in the removal of the artificial restraints to purchasing in the durable goods field that were imposed for another reason at an earlier time. This would apply to automobiles but I think others, too; the transportation agencies and other durable goods and some nondurable goods, too, as far as that goes.

Then if it is the judgment that we need additional stimulus to purchasing power, then we should consider cutting the basic personal income-tax rate, temporarly or preferably permanently.

Senator DOUGLAS. I would call on Mr. Rolfe. I know he is in an embarrassing position, because he was at one time a student of mine, and students are always reluctant to take issue with their former teachers. I might say he is now a free man and may express himself.

Mr. ROLFE. Thank you, Senator Douglas. I may say for the record that I suffered not one whit because of this experience. I have stated in my testimony, Senator Douglas, that I think we should take in the current short run more or less crisis situation we face a kind of rifle approach to the question of tax reduction and advocating reduction in the excise tax on automobiles because I think the consumer durable sector which has been very hard hit has interplayed in the past with the capital investments sector. This economy will not turn around until the consumer investment sector rises.

The step that the Congress and the Government have taken in the housing area is part of the effort and more is needed.

I further said that I think in my opinion, and I said it may be my bias, that a general tax cut is needed, if one wants to take today a calculated risk to look for full employment now rather than possible inflation later because the tools we have for inflation are much better. Therefore, I quite agree with your statement.

With respect to the long run, and again this is in my testimony, I do feel that we need some integrated and some well-thought-out long-run goals with respect to the competing claims which arise from time to time on fiscal policy and on taxation policy and that not only economic growth in the sense of capital investment is necessary, but also less tangible types of growth in the form of improving our intellectual resources, our universities, and so forth. However, at the current juncture to make it a more or less unanimous panel I agree with your basic position.

Senator DOUGLAS. We all know the wisecrack which is told at the expense of the economics profession. If you would lay all the economists of the country end to end you would not reach a conclusion. I do not want to force this panel to any premature conclusion. There is great value in keeping an open mind, presenting various facets of thought, and not jumping prematurely. We in political life have to move sometimes without all the facts, and thus conclude wrongly. So I am not going to put this question unless the group feels it is a fair question.

I would like to find out how many feel that the possible danger of future inflation should prevent major governmental stimulus now? If the group feels that is not a fair question, or do not wish to be polled this should be stricken from the record.

Mr. BLOUGH. As a point of clarification, Senator, further means, further than has yet been done, not further than has been talked about here.

Senator DOUGLAS. Further than has now been done.

Mr. TONGUE. In clarification could you say something further about the term "major"?

Senator DOUGLAS. No. Say further, and then if you want me to continue this exposition, I will come to definite figures. First whether anything more should be done than is being done, or whether the danger of future inflation should prevent action. Is that a fair question?

Mr. TONGUE. Yes.

Mr. BLOUGH. Yes.

Mr. BURGESS. In view of the international situation, the Employment Act, and the desire to alleviate suffering, I think it is a fair question.

Senator DOUGLAS. That seems to cover the waterfront. Let me ask you, how many feel that the possible danger of future inflation should prevent further major Government stimulative action now? If you say "Yes," that means you feel nothing more should be done than is now being done. How many feel that? Raise your hands. We won't have a record of how you vote. I see no hands raised. I trust no one has been stricken with paralysis and this indicates how you feel. How many feel that the Government should carry out major stimulating action now?

Mr. TONGUE. At this point, Senator, would you be willing to go into "major" a little more?

Senator DOUGLAS. Let us say how many favor a tax cut of $5 billion.

Mr. BLOUGH. Would you identify "now"?

Senator DOUGLAS. Before Congress adjourns sine die or as much earlier as possible.

(Four voting.)

Mr. BLOUGH. I would like to explain my vote, Senator.

Senator DOUGLAS. The record will show that 4, as I understand it, said "Yes," and 2 did not.

Mr. BLOUGH. I am one who did not raise my hand in response to that question, because of the emphasis on the immediacy of action. What I suggested in my earlier testimony before this committee and in my testimony today is that the committees ought to go ahead and get a tax-reduction bill worked up and very well along. It is my fear that we will be needing this. I would be glad to see the work done toward it with the possibility of withdrawing if things seem to be considerably better in another month.

Senator DOUGLAS. That is, you are for it as of now, but reserve the right to change if conditions improve.

Mr. BLOUGH. Yes. I know Congress does not usually move this fast, and I think I would like to have that reservation.

Mr. BURGESS. Senator, I should like to aline myself with the view expressed by Mr. Blough, as well.

Mr. TONGUE. I would like to emphasize my affirmative response to your question, Senator. I admit that there is a long-run inflationary problem that will undoubtedly be with us when the economy recovers again. I also think the economy will recover without a tax cut, and that the turn will probably come within a matter of months. However, the recession has already gone further than either of the other two that we have had since the war. We have very definite indications from many areas that it would be unlikely that we would have a near term revival in the capital expenditure boom, and for that reason we can probably live with a substantial Federal deficit for some time into the future, by which time even with a tax cut the higher level of income might well produce sufficient revenues to balance the budget. So again, I say, let us take care of the problem we have to today. The problem we may face a year or a year and a half or 2 years from now is at this point vague and uncertain; but let us deal with that at that time.

Mr. ROLFE. May I ask Professor Blough a question on his hypothetical position here? I should add for the record Professor Blough was also a professor of mine from whom I suffered not one whit, but on the contrary enjoyed very much. If the index of production in the month or 2 months ahead falls to the vicinity of 120, 123, or 125, something in that area, and if other aggregate measures move accordingly with it, would you then say that is sufficient stimulus to precipitate this tax cut which you said should be in preparation?

Mr. BLOUGH. Yes. I am afraid that the necessity for this is almost completely demonstrated even now, but I don't want to say this without any reservations, because people have made mistakes about recessions and they may be mistaken about this one.

Mr. ROLFE. Given the choice of making a mistake?

Mr. BLOUGH. It should be in the direction of a tax cut, especially if it is temporary.

Mr. MUSGRAVE. May I ask Mr. Blough another question? On the hypothetical assumption that Congress had already undertaken this preparation which you think should be undertaken, and that this tax-reduction bill was ready right now, would you advise to move now or to wait a month; and if so, why?

Mr. BLOUGH. I don't see the value in answering a hypothetical question like that.

Mr. MUSGRAVE. I disagree. I think this is precisely the answer which we owe the committee. I think not to answer this question is begging the issue.

Mr. ROLFE. We have to make some forecast.

Mr. KASSALOW. Otherwise Senator Douglas could say to us what would be the position of this committee a month from now. He could say if recovery were clearly under way a month from now, what would your position be and we would perhaps have to say no tax cut.

Mr. BLOUGH. Senator, if I may answer this, if I had to decide now, I would say, cut taxes; but to me the real timing problem is geared to the adjournment of Congress. Once Congress goes home, it is not coming back and can't do anything about the problem. The decision must be made soon enough so that action can be taken before Congress adjourns. If the action is to be taken before Congress adjourns, it must be gotten underway at least 6 weeks ahead of time because even a very simple tax reduction bill, on the basis of past experience, will hardly go through faster than that. The time left for decision is short, but it seems to me that whether we make it this month or not until next month is not so important. The important thing is that what needs to be done, be done before Congress adjourns.

Senator DOUGLAS. Mr. Blough was a very efficient economist for the Department of the Treasury who had a very intimate part in drafting bills. I would say that you tried to get Congress to pass better tax bills than they were willing to pass. As you well know, the corporate tax expires on the 30th of June and some of the excise taxes expire on that date. So in all probability we will have to deal with this issue before the 1st of July. Therefore, the time is even less than you think it is. We are right up against the gun, really. It is now in effect the 1st of May.

Mr. BLOUGH. I think Mr. Curtis pointed out in your absence, Senator, when it comes to extending these taxes, sometimes what happens is that Congress waits until the very last minute and then rushes the extension through without much thought.

Senator DOUGLAS. Exactly, sir.

Mr. KASSALOW. That is precisely the function of these types of inquiring panels, to evaluate is this automatic type of tax cut which we are apt to get the thing most desirable in the light of the present economic situation.

Mr. TONGUE. Or conversely, an automatic extension of the present rates.

Senator DOUGLAS. Thank you very much for coming. We are greatly in your debt. We know how much this disturbs the ordinary tenor of your lives and activities. I know it is a real drain upon your energy. I assure you we appreciate this very much, indeed, and it has its effect both upon the Senate and upon public opinion which has some influence upon the Senate.

Tomorrow morning we will meet in room 212, Senate Office Building, with recommendations of various interested research groups.

(At 12:40 p. m., a recess was taken until Thursday, May 1, 1958.)

FISCAL POLICY IMPLICATIONS OF THE CURRENT ECONOMIC OUTLOOK

THURSDAY, MAY 1, 1958

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON FISCAL POLICY OF THE
JOINT ECONOMIC COMMITTEE,
Washington, D. C.

The subcommittee met at 10 a. m., pursuant to recess in room 212, Senate Office Building, Senator Paul H. Douglas (chairman of the subcommittee) presiding.

President: Senators Paul H. Douglas and John D. Hoblitzell; Representative Thomas B. Curtis.

Also present: Norman B. Ture, staff economist, and Roderick H. Riley, executive director.

Senator DOUGLAS. The subcommittee will please come to order.

This is the final day of the Fiscal Policy Subcommittee hearings on fiscal policy implications of the current economic outlook. We have sought in these hearings to bring out the facts about our current and prospective economic situation and to establish the major considerations which should be taken into account in formulating fiscal policy at this time. Our policy objectives, of course, are to bring the present recession to a prompt end—or to as prompt an end as we can bring it—and to provide the conditions under which economic growth will be promptly resumed.

In the preceding days' hearings we have considered major economic trends observable at this time, the merits and limitations in alternative stabilization policies, and various broad approaches to tax reduction should this be desirable in the interest of economic stabilization.

Today we are to hear from a number of the major economic interest and research groups concerned with public economic policy. We hope that those appearing on behalf of these organizations will feel free to address themselves to any or all of the topics covered in the preceding hearings.

We will hear the opening statement of each panelist before proceeding with a general discussion. Each panelist may submit for the record any prepared materials which he does not include in his opening statement.

Our first witness this morning is Mr. John C. Lynn, legislative director of the American Farm Bureau Federation. Mr. Lynn, we are happy to have you with us.

25780—58——10

STATEMENT OF JOHN C. LYNN, LEGISLATIVE DIRECTOR, AMERICAN FARM BUREAU FEDERATION

Mr. LYNN. Mr. Chairman, I would like to file for the record, if I may, this statement, and make a few very brief comments.

Senator DOUGLAS. Thank you.

(The statement referred to is as follows:)

STATEMENT OF THE AMERICAN FARM BUREAU FEDERATION PRESENTED BY JOHN C. LYNN, LEGISLATIVE DIRECTOR

We appreciate the opportunity to present our views on the fiscal policy implications of the current economic outlook.

Farmers have a very direct interest in employment and the general economic situation, and the American Farm Bureau Federation has long emphasized the importance of sound monetary and fiscal policies. While it has been demonstrated that a high level of employment does not automatically guarantee farm prosperity, it certainly can be said that the opportunity for farmers to prosper will be greater when employment and productivity are rising than when the reverse is true.

Our interest in employment is twofold: (1) Employment creates the purchasing power that is essential to a good demand for farm products, and (2) a rising level of employment creates opportunity for underemployed farm people to obtain nonfarm jobs on either a part-time or a full-time basis. In many cases the underemployed farmworker who gets a nonfarm job not only improves his own situation, but also improves agricultural conditions—by releasing land to someone who needs it, and by becoming a cash customer for farm products.

From the standpoint of agriculture the most serious aspect of the present economic situation probably is to be found in reduced opportunity for underemployed rural people to obtain off-farm work. As of now, there is no evidence that the current economic situation is having any seriously adverse effects on the demand for farm products. As a matter of fact, the farm products such as hogs, cattle, and eggs, which are free of the surplus problems that have developed in some other commodities under Government price support and production controls programs, have been bringing good prices. We, of course, recognize that rising unemployment constitutes a threat to present farm price levels, and we want to make it clear that we share with other groups a desire for an early improvement in the general economic situation.

In our opinion the following broad lines of Government policy are fundamental to the creation of a proper climate for high employment, rising productivity, and general prosperity.

(1) Monetary and fiscal policies which will contribute to the maintenance of a relatively stable general price level must be used effectively.

(2) The restraint of trade or the exercise of monopolistic power by any group—Government, industry, labor, or agriculture—must be prevented.

(3) Policies which encourage rather than strangle foreign trade and investment must be followed.

(4) Policies that encourage the creation of private capital and its proper use throughout the world must be maintained.

Some of these policies, of course, are more directly the concern of other congressional committees. We believe, however, that our current policy resolutions on price level stability, current budget policy, and long-range tax policy are pertinent to this hearing. These resolutions are attached to this statement for your information.

In our opinion, the Government can make a greater contribution to the achievement of a high level of employment through general policies which contribute to the development of a favorable climate for competition, enterprise, and individual initiative, than it can make through direct action to create jobs.

Unemployment is, of course, a serious problem—particularly for those who lose their jobs. But, in deciding to do something about unemployment we must consider not only the problems of the unemployed but also the interest that all of our people have in avoiding policies which will lead first to an artificial boom, and then to an ultimate financial collapse.

In a period of recession, such as the present, when unemployment has been rising many people are tempted to advocate inflationary actions. Unfortunately such actions often have their major effect after the apparent need for stimulating the economy has long since passed. While inflation brings temporary prosperity to some people, it creates great hardships for many others, and makes the economy more vulnerable to future depressions.

Even a gradual inflation can have serious consequences. For example, a price rise of only 2 percent per year would cut the real value of the dollar in half every 35 years. Furthermore, if people at large became convinced that it was the policy of the Government to foster a gradual inflation, they would be encouraged to act in such a way as to cause the inflation to proceed at a more rapid rate and this would increase the danger of an eventual crash.

In dealing with the problem of cyclical unemployment, we need to realize that it is unreasonable to expect a free choice, market economy to move upward at all times. When business is good and profits are rising, production is stimulated with the inevitable result that some industries oversupply the market. Our economy has been moving upward with relatively minor interruptions ever since the end of World War II. In the months immediately preceding the present recession a capital-goods boom resulted in a great expansion of productive capacity. At the same time that productive capacity has been increasing prices have been rising in response to rising wages and other costs. Under these circumstances it is not surprising that we have run into a period of readjustment with an attendant increase in unemployment.

The basic things that we need to do to terminate the recession are (1) to avoid rushing into unsound programs which could set the stage for a serious inflation later, and (2) to allow some time for economic forces to work out adjustments and set the forces of recovery in motion.

As a matter of general policy, we prefer tax reduction to large increases in public works, in cases where major Federal action appears to be indicated to counteract a downturn in the economy.

While we believe that it is desirable to accelerate the construction of sound, well-planned public works that would be undertaken anyway in the normal course of time, when there is a slack in the civilian economy, we do not believe that a downturn in business activities should be used as an excuse for make-work projects or other public works which are unsound from an economic standpoint. Tax reduction can be put into effect much more rapidly; and terminated more promptly than a public-works program; it is more in keeping with a free choice system; and we believe that it would be more effective than pump priming.

Under present circumstances, when there is no evidence that the economy is undergoing anything more than a somewhat painful readjustment, we see no justification for major Federal action. It would take months and perhaps years to increase public-works expenditures sufficiently to have much effect on the economy. By that time, our pressing problem may well be inflation than recession. Furthermore, a major expansion of public works would constitute a very round-about way to solving the problem of the workers who have lost their jobs in automobile factories and other plants that produce consumer durables. We, therefore, can see no justification for a major expansion of public works.

We also doubt that a reduction in income taxes would be warranted at this time at the expense of a large Federal deficit. Under our present tax structure, Federal revenues decline automatically whenever there is a reduction in business activity and personal income. The reduction in Federal tax receipts to be expected from reduced employment and production, together with the increased Federal spending now being programed, has already raised the prospect of substantial deficits. To increase these prospective deficits by substantial tax cuts would be inflationary and unwise. It would, however, be desirable to explore the possibilities of reducing Federal spending and simultaneously making a corresponding reduction in Federal taxes.

If taxes are to be reduced under present circumstances, the emphasis should be on the reduction or elimination of taxes which increase costs and prices, or otherwise interfere with the efficient working of our economic system. For example, this would be a good time to eliminate the excise taxes on freight transportation, as these taxes not only increase costs throughout the economy but also discriminate between private and for hire transportation. Consideration might also be given to the reduction of other excise taxes which increase the cost of goods to consumers; however, the inflationary aspects of further unbalancing the Federal Budget should be given careful consideration.

One of the things that is needed under present conditions is nongovernmental action to encourage increased consumer and business spending. To this end it would be most helpful if business and labor would cooperate in programs to reduce costs and prices.

When prices and wages are maintained or increased in the face of falling demand and rising unemployment, the result is almost certain to be greater unemployment and a longer period of recession than otherwise would occur.

For this reason, among others, we believe that Government policies should be directed toward preventing concentrations of economic power which make it possible for private groups to exercise undue influence over wages and prices. In the business field this means that we must have effective programs to prevent the exercise of monopoly power. In the case of labor it means that unions should be subject to prohibitions against actions to restrain trade comparable to the prohibitions imposed on other groups. It also means that compulsory unionism should be prohibited by law.

ATTACHMENT I

Current Farm Bureau policies with regard to—

PRICE LEVEL STABILITY

We reaffirm our belief in the importance of measures to bring about a more stable general price level as a means of providing a favorable climate for economic growth and a rising standard of living. This is essential if we are to avoid a far-reaching expansion of Government controls over individual decisions and actions.

We continue to oppose direct price and wage controls.

Government policies which affect the supply of money and credit should be directed toward promoting a relatively stable general price level together with high employment and rising productivity. The Government also has a responsibility to so conduct its affairs as to inspire confidence that everything possible is being done to protect the economy from the extremes of inflation and deflation.

In periods of relatively high employment and business activity, the Federal Government should not only balance its budget and keep it balanced to eliminate the need for deficit financing but also reduce the total national debt. If the budget is unbalanced in such a period, the Government should borrow necessary funds from nonbank lenders to the maximum extent possible to avoid the creation of new money. The existing national debt should be managed to prevent nonbank-held securities from being shifted to the commercial banks, as such a shift creates new money just as the sale of new securities to banks.

In periods of declining employment and falling prices, these policies can be reversed to combat deflation. In such a period, for example, it may be desirable to reduce taxes to leave more purchasing power in the hands of the public even though this results in a deficit.

If the budget is to be unbalanced to counteract a deflationary trend, emphasis should be on reduced taxes rather than increased Government spending.

The Federal Reserve System can help to stabilize the price level by relating its policies to the country's needs for money and credit rather than to other considerations. The independent status of the Federal Reserve Board must be maintained. It should restrain the expansion of bank credit in inflationary periods and make it easier for the banks to extend credit if deflation threatens.

The policies of Government agencies which make or guarantee loans should be coordinated with overall credit policies.

In order to be effective in checking deflation, the Federal Reserve System must recognize the danger of a downturn and act before deflation has gone so far that public confidence in the outlook is undermined. In such a situation, prompt tax rate reductions, especially in the lower income brackets, can be a valuable supplement to Federal Reserve action.

It is generally recognized that it is more difficult to combat deflation than inflation with monetary and fiscal policies. It should be remembered, however, that our worst deflations have followed periods of inflation and that effective action to prevent inflation will go a long way toward preventing subsequent serious depressions.

We urge that the American Farm Bureau Federation board of directors continue to sponsor periodic conferences on monetary and fiscal policy.

CURRENT BUDGET POLICY

It is apparent that current events in the realm of atomic weapons and space experimentation will be used as an excuse for extravagant appropriations and wasteful methods in Government.

Congress should take effective measures to regain control of Federal expenditures.

The times require that Government exercise strict economy, eliminate duplication of effort, and promote efficient operations. We urge that budget requests be scrutinized carefully and that Government operations be cut to the minimum needed to carry on proper governmental functions. Necessary increases should be offset by reductions in other items.

We are opposed to increasing the national debt limit unless absolutely necessary to meet a national emergency.

LONG-RANGE TAX POLICY

A sound national tax policy is necessary to maintain the private enterprise system, which is the foundation of our form of government. Tax programs should be designed not only to bring about fair and equitable distribution of the tax burden but also with due regard to their effects on the national economy.

As a long-time tax policy, we favor the following principles and urge their adoption as rapidly as conditions permit:

(1) Long-range plans should be made for the gradual reduction of the national debt; however, debt retirement should be handled so as to contribute to the stability of the general price level and an expanding economy. Debt reduction should be given priority over tax reduction except in periods of threatened depression.

(2) A Federal tax policy should be adopted which will contribute to a stable price level in an expanding economy. This means that tax revenues should rise relative to Government expenditures in inflation and fall in depression.

(3) The individual income tax should be the major source of revenues for the Federal Government. All self-supporting persons should make a direct contribution to the support of Government. When conditions warrant a reduction in personal income taxes, rate reductions—particularly in the lower brackets—should have priority over proposals which would take substantial numbers of taxpayers off the rolls.

(4) Personal exemptions and progressive features of the income tax are designed to adjust tax liabilities to the individual's ability to pay. In the interest of equity, additional deductions and exclusions should be limited in order to broaden the base for the income tax and thereby permit lower rates for everyone.

(5) We favor gradual reduction and eventual elimination of hidden taxes.

(6) Taxes levied to increase revenues in an emergency should be terminated when the emergency has passed.

(7) Orderly plans should be developed for a general reduction in income tax rates.

(8) In order that State and local governments may be able to support Government services which they properly should supply, it is imperative that certain areas of taxation now preempted by the Federal Government be systematically restored to State and local governments.

FEDERAL EXCISE AND SALES TAXES

We oppose a general Federal sales tax. Such a tax would create inequities and increase the overlapping of Federal and local State tax systems. The retail sales tax field should be reserved to the States.

Taxes on transportation, farm tractor and implement tires, and other excise taxes which affect production and distribution costs should be eliminated. Federal excise taxation should be limited largely to taxes on nonessential and luxury goods. All purchasers of items on which an excise has been paid should be informed of the amount of such taxes.

Mr. LYNN. May I say in the beginning that Mr. Charles Shuman, our president, regrets very much his inability to be here.

As farmers, certainly we are interested in the present situation, because when we have unemployed people they do not usually buy as much food and fiber as they do when they are employed. Certainly we recognize that we do have an unemployment situation on our hands that needs attention.

We would simply want to make this point, that we hope in this period of recession we will not adopt policies that perhaps will be inflationary in character and maybe over a long pull do the economy more harm than good.

It has been said many times that the United States economy is a very delicate instrument. It has also been said that we should at this time perhaps not use sledgehammers and jackhammers, but use the delicate tools that are necessary in this very intricately balanced economy of ours.

On page 2 of our statement, we list four points that we think are important as you consider this problem:

1. Monetary and fiscal policies which will contribute to the maintenance of a relatively stable general price level must be used effectively.
2. The restraint of trade or the exercise of monopolistic power by any group—Government, industry, labor, or agriculture—must be prevented.
3. Policies which encourage rather than strangle foreign trade and investment must be followed.

There are a lot of groups who say, for example, that we should be very careful in extending the Reciprocal Trade Agreements Act, because we have some unemployment in the United States. The American Farm Bureau would like to say that we completely disagree with that philosophy. We are for the extension of the Reciprocal Trade Agreements Act, because we think it will contribute to rather than deter the United States economy in this situation.

4. Policies which encourage the creation of private capital and its proper use throughout the world must be maintained.

We have been coming before this committee and other committees of Congress for a number of years, particularly during these years of very high employment and high prosperity, recommending monetary and fiscal policies that would cause us to pay off some of the public debt so that we would be in a better position to meet the kind of situation we now have. Certainly all of us had in mind a period such as we are going through now, where it might be necessary to have some deficit financing.

Unfortunately, we have not been able to accomplish this objective, which we think would have been a good thing during these years, and now it may be necessary to unbalance the budget to an even greater extent than we think may be good in the long-term interest of the United States economy.

On the bottom of page 3 of our statement, there is a little paragraph that I think is very significant:

> The basic things that we need to do to terminate the recession are (1) to avoid rushing into unsound programs which could set the stage for a serious inflation later; and (2) to allow some time for economic forces to work out adjustments and set the forces of recovery in motion.

We have great confidence that we will come out of this recession in good shape soon if we act wisely. We will do it by all of us working to establish, with all our might, confidence in this system, confidence that we will again have rising employment and continued prosperity. We must not talk ourselves into a worse situation.

Mr. Chairman, we have attached to our statement our policies with regard to taxes, monetary, and fiscal policies. We would simply make this statement with regard to taxes, that certainly consideration should be given to a tax rate reduction, rather than work projects, or what have been referred to as the "leaf-raking type of projects." We would emphasize that the principal tax reform that we are recommending here is the repeal of the transportation tax and, some consideration of the elimination or reducing some of the excise taxes.

If consideration is given to income tax reductions, we hope that the major consideration will be placed on the rates rather than on raising the exemption, because we firmly believe the tax base should be kept very broad.

Mr. Chairman, this concludes a brief summary of our statement. We hope to participate later in the discussion.

Senator DOUGLAS. Thank you very much, Mr. Lynn.

I am going to ask Mr. George G. Hagedorn, associate director of research of the National Association of Manufacturers, to take up the discussion.

STATEMENT OF GEORGE G. HAGEDORN, ASSOCIATE DIRECTOR OF RESEARCH, NATIONAL ASSOCIATION OF MANUFACTURERS

Mr. HAGEDORN. Thank you, Senator.

The announced purpose of these hearings is to inquire into the fiscal policy implications of the current economic outlook. It is a source of satisfaction that the subcommittee used general language of this kind, rather than specifically asking for suggestions on "how to cure the recession," or "how to stop inflation." Our current economic situation is far too complex to be described by any one word, whether that word be recession, inflation, unemployment, or whatever.

The use of the word "outlook" in your title suggests that you may be looking for predictions of economic developments in the short-range future, or for recommendations based on such predictions. However, you have already heard from experts and I will not attempt to criticize or supplement what they have told you. Frankly, I would hesitate to offer recommendations which depend on my own, or anyone else's, answers to such questions as: Have we already bottomed out? When will the upturn begin? What will the trend of prices be during the rest of this year?

Still, a physician can diagnose an ailment and discuss possible treatments, even if he is unable to predict with confidence the erratic day-to-day fluctuations in the patient's fever chart. The American economy suffers from certain underlying chronic difficulties which have been with us for some years. The recession which began last year is one phase in the working-out of those chronic underlying difficulties, and it can be correctly understood only in that context.

There are two chief economic problems, to which most of our other economic problems can be referred. These are:

1. The tendency for unit labor costs to increase continuously. This puts us in perpetual danger of inflation, recession, or a combination of both.

2. A tax system which impairs both the incentives for capital formation and the sources out of which capital formation can be financed.

This has serious consequences in regard to our prospects for economic growth.

These two problems, and their implications for fiscal policy, will be the focal points of the discussion which follows.

RISING LABOR COSTS

The basic cause of the tendency for wages to rise faster than productivity, and hence for labor costs to increase, is the power position organized labor has attained in our society. Since that problem is not the subject of these hearings, I will pass over it, but it must always be recognized in the background of current economic developments.

In and of itself, the effect of any increase in costs is to restrict markets. It is an elementary principle that if your product or service becomes more costly you are very likely to sell less of it.

Of course, the restrictive effect of increased costs can be offset in various ways, and that is where fiscal and monetary policy comes in. The net effect of relying upon these offsets is inflation.

You might view our economic history during the years since 1940 as a race between the restrictive effects of rising labor costs and the ability of fiscal and monetary measures to offset them. By the end of World War II, the fiscal and monetary measures had attained a long lead in this race. There was enough money in circulation, and sufficient credit was available, to insure that there would be little resistance in the market place to increased costs, and inflation thus went its merry way.

We have now reached a situation where rising cost levels have not only caught up with the money supply, but evidently forged somewhat ahead.

A year ago, economists were disputing as to whether the inflation, which had then been going on for about a year, was due to the "push of costs" or the "pull of demand." This controversy should be resolved by now, by the fact that price rises are still continuing. Rising prices with rising volume might be due to either cost-push or demand-pull. But rising prices with falling volume must obviously be ascribed to the pressure of costs.

We have two choices in dealing with this situation. First, we can do something to reduce the excessive economic power of organized labor, in which case we can have some hope for prosperity without inflation. Alternatively, we can use budget deficits and easy money to offset the job-destroying effect of uneconomic cost increases, in which case the best we can hope for is prosperity with inflation.

In the long run, it is doubtful that we can have even that. Reverting to the analogy of the race, monetary expansion can move ahead, but labor costs can move ahead even faster. It seems likely that if this is the course we choose, the pace of the whole process must continuously accelerate. Once it becomes clear that fiscal and monetary policy will be used "to whatever extent is necessary," there will be very little incentive to resist whatever cost increases are demanded. The end of this accelerating process must be some form of economic chaos that no one can predict in detail.

The revenue effects of the present recession are creating substantial budgetary deficits, even without any deliberate decision to adopt such deficits as a weapon against the recession. This should be further cause for hesitation in taking action, the primary purpose of which is to enlarge those deficits.

GOVERNMENT SPENDING AS A CURE FOR RECESSION

There is no doubt that, if our only objective were to put the unemployed back on a payroll, one way it could be accomplished would be by a program of Government spending—provided we used enough Government spending. The trouble is that we don't know how much "enough" would be, and experience warns us that, if this is our sole reliance, the amount required might be astronomical.

In 1930, the spending side of the Federal budget amounted to slightly over \$3 billion. By 1939, it had risen to almost \$9 billion, and there were still 9 million unemployed. In other words, tripling the expenditure rate was not enough. It wasn't until 1942, when annual expenditures had risen to \$34 billion, 10 times the predepression level, that excess unemployment disappeared.

This is an indication of what we might be letting ourselves in for if we placed our major reliance on Government spending as our way out of our present difficulties. And remember, we are starting from a base of over \$70 billion in Government spending instead of the \$3 billion we started from in 1930. The lengths to which we might be driven are so fantastic, and the prospects of success so poor, that only the utmost desperation could justify seeking a solution down this road.

TAX REDUCTION AS AN ANTIRECESSION WEAPON

Various schemes of tax reduction have been proposed as an antidote to this recession. Probably almost any one of them would be effective, to some degree, as a temporary palliative. But, surely, in making changes in our tax system, we will want to have a broader objective than that.

The National Association of Manufacturers has long advocated a thoroughgoing reform of our income-tax-rate system. This would involve reductions of corporate and individual rates in every bracket. It would also involve a compression in the spread of rates along the income scale. Our reasons for recommending this action will be explained more fully in the later discussion of restrictions on economic growth.

We believe that such a reform of the tax-rate structure would give a tremendous and permanent lift to the economy. It will leave us in better condition to face whatever other problems may exist.

At the same time, frankness compels me to state that we had better not rely on this as a complete cure for the ailments which afflict us. The upward pressure on labor costs seems to be relentless, and we can't expect that tax-rate reform will solve this problem.

INFLATIONARY EFFECTS OF FISCAL MEASURES

There is a widespread illusion that we can use fiscal measures—increased spending or reduced taxes—to restore full employment, and then abandon or reverse these measures before they start to cause inflation. But this is a misunderstanding of the problem. Even if our knowledge and our timing were perfect, this neat solution would be impossible, since inflation and recession are simply different aspects of the same condition.

Perhaps we have put too much emphasis on the tendency for cost increases to be passed on to customers. In some cases, the problem is that market conditions will not permit them to be passed on, and they have to be absorbed in the form of reductions in profit margins. The evidence that this has been going on extensively is the fact that the dollar total of corporate profits did not increase at all between 1948 and 1956, while the dollar total of corporate sales increased by 60 percent.

This squeeze between costs and prices is one of the factors which is depressing business at present. Since fiscal policy does not deal with the cost side of the squeeze, it can relieve the pressure, and thereby improve business conditions, only by raising prices. It is impossible to separate the inflationary from the antirecessionary effects of fiscal measures.

THE PROBLEM OF ECONOMIC GROWTH

The inflationary-recessionary race brought about by rising costs is not the only major problem we face now. There is also the danger that we may be falling far below attainable rates of economic growth.

Much current economic discussion seems to assume that, if we simply avoid depressions and recessions, economic growth will be assured. But this is not so. Even if we keep our manpower and other productive resources at a level reasonably close to full employment, the rate of growth still depends on how economic forces allocate our output as between current uses and capital formation. Our current tax system seems almost designed to insure that very little will be allocated to capital formation.

It may come as a shock to hear the suggestion that we haven't been devoting enough of our energies to the formation of business capital. There has been much talk of our capital-goods boom in the period since World War II, and especially in 1955 and 1956. Some feel that the current reduction in capital-goods outlays is a reflection of previous excesses in such outlays.

It is true that a part of our productive facilities is now lying idle. But this is no more an indication that we have more capital than we should have than unemployment is an indication that we have too many people. Unemployed facilities and unemployed manpower are both the result of the impairment of markets by cost rises.

The statistics on gross outlays for new business capital can give a very false impression. The $35 billion to $40 billion totals of recent years make it seem as though we are building up our facilities at a tremendous rate. What few bother to recall is that, in our huge economy, capital facilities are also being used up at a rapid rate. A careful study by the National Association of Manufacturers research department indicates that the current rate of capital consumption is about $35 billion a year, so that the net gain in our available capital is now a very narrow margin.

STANDARDS FOR ECONOMIC GROWTH

One of the problems in trying to devise policies to promote economic growth, and to balance them against other objectives, is that we have no realistic standards by which a growth objective may be set. Merely equaling past rates of growth cannot be considered satisfactory when potential enemies may be doing much better. The only conclusion is that no rate of growth is satisfactory below the maximum attainable within our free-enterprise system.

The Russians devote a substantially larger part of their national income to capital formation than we do. They do so by a program of austerity forcibly imposed on their consumers. This is a method we wouldn't want to use, and it probably wouldn't work here, anyway. We prefer to rely on individuals and businesses to devote a part of their incomes, by their own choice, to saving and investment. Still, we had better strive to eliminate any condition which impedes or deters them from making such a choice. The present structure of income-tax rates most assuredly has this effect.

RECOMMENDATIONS

The foregoing discussion is intended to explain the basic thinking which lies behind the recommendations of the National Association of Manufacturers. Due consideration has been given to the aspects of the situation which are peculiar to the present moment. These have been related to the underlying problems of which they are the current reflection. As a result of this analysis, the National Association of Manufacturers sees no reason for modifying the position it has maintained in the past.

Fiscal policy should not be regarded as a balance wheel or regulator for the economy, nor as a means of redistributing income. The function of fiscal policy should be simply to provide revenue for necessary Government expenditures. For providing economic balance, we should rely on the forces of free competitive markets, supported by a noninflationary monetary policy. For growth, we must rely on private capital formation.

It should also be clear that this attitude does not reflect a belief that all is well and there are no problems. On the contrary, free competitive markets cannot do an adequate job at present because of the monopolistic condition of the one market which pervades all others—the labor market. Private capital formation is seriously impeded in its task of providing the basis for economic growth, by a tax system which confiscates the sources of capital and reduces the incentives for saving.

Our association, therefore, urges the following measures:

1. Strict Government economy—expenditures limited to those necessary for ordinary Government functions.
2. Curbing of labor monopoly—impose the same restrictions as are imposed on industrial or commercial monopoly.
3. Reform of the income-tax-rate system—the Sadlak-Herlong bill embodies the methods we believe should be followed. Its reduction goals should be considered as a minimum program of rate reform.

These recommendations deal with the underlying ailments, rather than their currnet symptoms. It is the only program which offers the hope of more than temporary success.

Thank you.

Senator DOUGLAS. Thank you very much.

The discussion will be continued by Mr. Stanley H. Ruttenberg, director of research for the AFL–CIO. Mr. Ruttenberg.

STATEMENT OF STANLEY H. RUTTENBERG, DIRECTOR OF RESEARCH, AFL–CIO

Mr. RUTTENBERG. Thank you, Mr. Chairman.

If I might have my longer statement incorporated into the record, I will attempt to summarize it in a few minutes.

Senator DOUGLAS. Very well.

Mr. RUTTENBERG. I will not take time from my direct presentation to comment upon the views just expressed by Mr. Hagedorn, but I do hope I will have an opportunity to do that later.

Senator DOUGLAS. I anticipate that there may be some difference of opinion.

Mr. HAGEDORN. I would not be surprised, sir.

Mr. RUTTENBERG. Just a slight difference.

(The statement referred to above is as follows:)

STATEMENT OF STANLEY H. RUTTENBERG, DIRECTOR OF RESEARCH, AFL–CIO

President Eisenhower and other administration leaders have been trying America's patience with a dangerous wait-and-see philosophy. As the downturn began last summer, cheerful statements about a "rolling readjustment" emanated from the administration. In January, as unemployment figures climbed higher, the pat reassurance became "Wait and see what happens in March." But the rolling readjustment lurched downward. Joblessness shot up 1.1 million in January and another 700,000 in February. As March failed to produce an upturn, more patience was requested, with the explanation that only April figures could show what happened in March.

We have waited. We have seen.

We have seen unemployment rise more than 50 percent since December.

Now that April is here, the administration has struggled to find a false ray of hope in the statistics. The March rise of 25,000 in unemployment and increase of 320,000 in employment has been proclaimed evidence of an upturn. The April rise of 600,000 in employment and 78,000 drop in unemployment will also be hailed as a reversal in the downward drift of the economy. But this slackening in the unemployment rise and the upturn in employment are less than normal for this time of year. Nonetheless, these figures have been, and will continue to be, used to justify further delay in taking steps to stop the recession—a recession now hovering on the brink of a depression.

It seems incredible that the administration and even certain segments of Congress can continue to slough off the seriousness of current evidence:

Five million one hundred thousand unemployed workers, with an additional number of part-time unemployed equivalent to 1.3 million full-time jobless, represent 9½ percent—or, seasonally adjusted—almost 9 percent of the labor force. Can these people afford to "wait and see?" Can the Congress afford to let America "wait and see?"

Almost one-half of the currently unemployed have been out of work for more than 10 weeks. In the recession of 1954, only one-third were out of work that long, and in 1949, only one-quarter.

Personal income—particularly wage and salary payments—has dropped. Less than one-quarter of this decline is offset by unemployment benefits and public assistance.

Personal consumption expenditures have dropped in each of the last two quarters (for 6 months).

None of these important economic factors shows signs of changing the downward direction. Yet America is told to "wait and see."

During this "patient" period, a few actions have been taken:

1. The Federal Reserve Board, which waited too long to find out what would happen with tight money, has adopted an easy money policy by reducing the rediscount rate 4 times in the last 6 months—to a current level of 1¾ percent.

2. Government contract placements, housing, roads, and Government purchases of supplies have been accelerated.

Can these actions reverse the downward trend and with some sleight-of-hand put America back on the road to recovery? We in the labor movement think they definitely cannot. We know that businessmen borrow money to expand their inventories, improve their plant, and meet their markets. They don't borrow just for the sake of borrowing cheaper money. With productive capacity 30 percent idle, with sales down, easy money will not encourage inventory building or investment in new plant and equipment. Easy money will help in the future when sales improve enough to justify rebuilding inventories. Easy money will help when American consumers (both public and private) are able to buy the products the industrial potential of this Nation can produce. But easy-money policy will not help until then.

The housing program enacted into law will encourage, at best, only 50,000 additional housing starts in 1958 over what was already anticipated—not a great advance over an already too-low level of housing.

Government contract placements will not affect production for a few months and then not to any great extent.

The accelerated road program, reluctantly signed by the President, will not have much effect for 6 to 9 months.

Government civil and military construction projects can be stepped up only after many more months, and the accelerated purchases of Government supplies may add only 100 to 200 million dollars to expenditures in 1958.

The total of Government programs may add some 3 to 4 billion dollars to Government expenditures between the low-point of the fourth-quarter last year and the fourth-quarter this year. Surely no one expects this to offset the loss of more than $25 billion in gross national product over the same period. Surely these planned programs are inadequate to meet the needs of a continuing decline in the economy.

Unemployment will remain very high—in relation to any period in the last 15 years. Personal incomes are falling and personal consumption expenditures are declining. These problems are here right now. They call for immediate action, a quick stimulus with an immediate effect.

The right kind of tax cuts can provide that rapid stimulating effect on the economy. A broad-based tax cut will expand purchasing power and consumption, concentrating the bulk of the reduction among those people with less than $5,000 of taxable income. A cut in excise taxes on key commodities and services, such as automobiles, electrical appliances, as well as telephones, and railroad transportation of freight and passengers, can be effective. A reduction of corporate taxes for those companies with less than $25,000 in gross income would be effective. By reversing the 30 percent and 22 percent normal and surtax rates to 22 percent and 30 percent, companies with limited earnings would benefit substantially.

The total cost of such a package must be between 6 and 8 billion dollars to give effective stimulus to the economy. Between 5 and 5½ billion dollars should go to individuals in the form of personal income tax cuts. An additional 1½ to 2 billion dollars in excise reductions and about $¼ billion for small business should be provided.

In addition, immediate action must be taken to help the unemployed workers. Workers are exhausting unemployment compensation benefits at a rate of 50,000 a week. This means the number of exhaustions has reached a total of almost one-half million.

Duration of benefits must be extended to help those who will be exhausting or who have already exhausted their benefits. Extension of this duration alone is not enough. Present benefits, which average about one-third of weekly wages, must be increased. The suffering and hardship caused by inadequate benefits is obvious to all. Workers who are jobless today through no fault of their own should not be forced to subsist on these low levels of unemployment compensation benefits.

Increased benefits for unemployed workers and tax cuts for workers still employed will bolster incomes and consumer expenditures.

This stimulus is needed right now; not next month or next June or July. If a tax cut will help in June or July—as some administration spokesmen think their watchful waiting may show—it will be even better today. As a matter of fact, it would have been better months ago. The longer we wait, the greater the problem. A tax cut of $3 to $4 billion 3 months ago might have been enough to give necessary push to the economy. Now we need at least $6 to $8 billion. In another few months, even a greater tax cut may be necessary to produce the desired effect.

Neither tax cuts nor improved unemployment compensation benefits will in themselves be enough to solve the problem of the recession. The challenge of a growing and expanding population require initiation and expansion of programs for our total social needs. This country must provide more and better schools, hospitals, homes, roads, airports, as well as assistance to distressed communities, to depressed farmers, and to the blight in urban centers. These programs must be started or increased now. Though it will take 6 months to a year even to begin many of these projects, Congress should authorize them now.

Only by combining such a long-range public works program with tax cuts and improved unemployment compensation, can the Congress and the administration meet their responsibility to the American people, so clearly stated in the Employment Act of 1946: "It is the continuing policy and responsibility of the Federal Government to seek all practical means consistent with its needs and obligations * * * to promote maximum employment, production, and purchasing power."

For those who argue that an unbalanced budget and future inflationary trends threaten our economy, I must point out that the far greater threat is 30 percent idle productive capacity and almost 9 percent of the labor force unemployed. Surely the threat of rapid expansion of Soviet output while our production declines has disturbed the leaders of all free nations. It is appalling that the Sino-Soviet bloc should have been able to surpass United States steel production for the first time in the first quarter of this year, that in 3 months the U. S. S. R. produced over 75 percent of the steel tonnage of the United States.

In quoting these figures on April 29, Allen Dulles stated the worldwide threat: "A recession is an expensive luxury. Its effects are not confined to our own shores. Soviet propagandists have had a field day in recent months, pounding away at American free enterprise."

Surely an unbalanced budget this year with prosperity and full employment next year outweighs the prospect of a balanced budget today and joblessness and further lost production next year.

As for inflation, it is curious to note that the President, who last August was so concerned about "fanning the flames of inflation," should now find himself exhorting the American people to buy more. It seems almost too obvious that buying is not something that can be turned off and on like a faucet. People need jobs and incomes to buy.

Perhaps the best answer to the inflationary threat argument was given by Arthur Burns, president of the National Bureau of Economic Research and the first Chairman of President Eisenhower's Council of Economic Advisers.

"As long as the Government is prepared to take more decisive steps to combat recession than to resist inflation, our economy is likely to be biased in an inflationary direction. However, the proper remedy for this bias is not to diminish our efforts to curb recession, but rather to deal vigorously with inflation in times of economic exuberance.

"Much good can come from recognizing our mistaken tolerance of inflation in the past. But it will come by taking resolute steps for dealing with inflation in the future, not by reducing our willingness to curb recession today."

What better advice could be found? First things first. This is not the time to fight inflation or an unbalanced budget, but the time to fight a recession. The longer we dilly and dally, the more drastic the necessary action will become.

We cannot afford to wait much longer. We cannot afford the "luxury" of "wait and see." Further inaction must not be tolerated. The American labor movement sincerely hopes that whatever leadership is lacking from the administration will be supplied by the Congress.

Mr. RUTTENBERG. The present "wait and see" philosophy of the administration and of many Members of Congress is a very disheartening kind of situation. We had an announcement from the Secretary of Commerce about 2 weeks ago that we had about bottomed out; and now he is commenting that we might not have a bottom to the present depression until midsummer or early fall. They keep postponing the date when action might be taken.

We have waited, and we have really seen that unemployment has increased by 60 percent since December. The duration of unemployment has considerably increased. It is true presently about one-half of the total number of workers unemployed are unemployed for 10 weeks or more, as against in the 1954 recession, when there were only a third out of work that long, and in 1949, when only a quarter of the total labor was out of work.

Senator DOUGLAS. At a comparable point?

Mr. RUTTENBERG. Yes; 7 months after the decline.

The current statistics released the other day about employment and unemployment are not heartening at all. Even though unemployment dropped slightly and employment rose by about 600,000 between March and April, we ought not to interpret this to mean that we have gotten to the bottom of the recession or that we have slowed down the rate of the decline. The only thing that can be said is that the economic situation is probably worsening at a slower rate.

But when we move from 7 to 7.5 percent of the total labor force unemployed, seasonally adjusted, this is something we ought to be concerned about. Further wait and see will not be the solution. Immediate action ought to be taken.

But during this period of wait and see, we have had two kinds of action taken by the Government. One has been a decline in the interest rate policy, an easing of the money policy by the Federal Reserve Board, and the other has been an attempt to speed up Government contract placements, a housing bill from the Congress, a road bill, and the acceleration of Government purchases.

In relation to these two programs, little can be said favorably in terms of their effect upon the economy. Certainly the easy-money policy is not going to produce much added significance to the economy in the face of 30 percent of productive capacity lying idle and 7.5 percent of our labor force unemployed. Easy money will help only when the American consumers are able to buy, not when money is cheap.

In terms of the accelerated expenditure program, the housing program enacted by the Congress and signed by the President, at best, will add only 50,000 units to what was anticipated in terms of housing starts in the year 1958. This is relatively insignificant. The Government contract placements will take a few months, if not longer, before they have any effect. The accelerated road program will not take effect for another 6 or 9 months, and the same can be said for the other programs.

In total, Government expenditures in the fourth quarter of 1958 may be $3 billion to $3.5 billion higher than they were in the fourth quarter of 1957. And this is in relation to a decline in gross national product and a rise in needed growth of about $25 billion.

The present situation needs an immediate kind of action, an immediate stimulant. Such a stimulant ought to be a tax cut, a broad-based tax cut that will expand purchasing power and consumption, and that will concentrate the bulk of that tax cut among the people least able to buy—those with less than $5,000 of taxable income. In addition, there ought to be a cut in certain excise taxes, such as those on automobiles, electrical applicances, telephones, and railroad transportation of freight and passengers. In addition, there should be some adjustment of the corporate rate, but only for small business, not a reduction of the total 52 percent rate, but a reversal of the normal and surtax rates. In this way, a very slight loss in revenue will substantially aid and assist the small corporations with gross incomes of less than $25,000.

The total cost of such a tax cut ought to be in the neighborhood of $6 to $8 billion. This is the sort of thing which ought to effect purchasing power immediately and stimulate people's ability to consume and to buy.

I might say that all the current talk about tax cuts by the President and by the administration, in which they say, "Let's wait until June or July," means to me that if a tax cut is good in June or July, it is even better today. And the kind of a tax cut we might need in June or July may have to be even considerably greater than what is now anticipated, because the economy will continue to sag during the coming months.

Let us not lose sight of the fact that come May and June, when the children get out of school, unemployment will rise, and we may, with no change in the economic situation, be faced with 6 million or more unemployed.

In addition to the tax cuts, we need immediate action in the unemployment compensation area. We are exhausting benefits at 50,000 a week minimum. It may be going higher, according to current reports.

Senator DOUGLAS. Subject to correction, I believe there was an article in the New York Times on page 15 this morning, which I have sent out for, by Mr. A. H. Raskin. As I remember it, he fixed the total number who had exhausted their benefits in the current recession at approximately 700,000. Of course, some of those have found employment since then.

Mr. RUTTENBERG. As of about 10 days ago, the Secretary of Labor stated that there were about half a million who had already exhausted their benefits. It is unquestionably true that if we are exhausting it at 50,000 a week, we are very close to the 600,000 or 700,000 that Senator Douglas refers to.

I think the unemployment compensation program ought to be not only an extension of duration, but there ought to be an increase in the level of benefits.

And as a third program, we suggest a combined long-range public-works program, not of the leaf-raking type that has been referred to by Mr. Hagedorn, but of a design to meet the problems of a growing population: increased numbers of schools, hospitals, homes, roads, and the eliminatiton of slums and blighted areas in urban centers.

With this summary of the three specific points—tax cuts, unemployment-compensation extensions, and a program of schools, hospitals, roads, houses, et cetera—I should just like to conclude with a few comments about the arguments which are used against the kind of program we have just suggested.

It has been said, for example, that an unbalanced budget brought about by tax cuts will be very dangerous to the economy.

I can only say that an unbalanced budget this year, with prosperity and full employment next year, far outweighs the prospects of a balanced budget today and joblessness and further loss of production next year.

Even if no tax cuts are enacted, it is currently estimated that the current budget is unbalanced by about $8 billion in fiscal 1959, anyway. You can reverse the present trend by a tax cut and still end up with a budget that might not be unbalanced by much more than it would be unbalanced, if we take no positive action.

As for the argument of inflation, it is curious to note that the President, who last August was so concerned about fanning the flames of inflation, should now find himself exhorting the American people to buy, and to buy more. Perhaps the best answer to inflationary arguments was given by Arthur Burns, president of the National Bureau of Economic Research, and the first chairman of President Eisenhower's Council of Economic Advisers. I would like to read two paragraphs from a recent speech delivered by him:

> As long as the Government is prepared to take more decisive steps to combat recession than to resist inflation, our economy is likely to be biased in an inflationary direction. However, the proper remedy for this bias is not to diminish our efforts to curb recession, but rather to deal vigorously with inflation in times of economic exuberance.
>
> Much good can come from recognizing our mistaken tolerance of inflation in the past. But it will come by taking resolute steps for dealing with inflation in the future, not by reducing our willingness to curb recession today.

What better advice could be found than this which Arthur Burns gives? First things first. Let us fight recession when we are confronted with one. Let us fight inflation if inflation develops in the future. But at the present moment, when 30 percent of our productive facilities are lying idle, when 7.5 percent of our labor force is fully unemployed and an additional 1.5 to 2 percent are partially unemployed, or the full-time equivalent of partially unemployed, it is necessary that immediate action be taken.

The American labor movement sincerely hopes that whatever leadership is lacking from the administration on the other side of Pennsylvania Avenue will be supplied by the Congress on this side of Pennsylvania Avenue.

Senator DOUGLAS. Thank you.

The discussion will be continued by Mr. Herschel D. Newsom, master of the National Grange.

STATEMENT OF HERSCHEL D. NEWSOM, MASTER, THE NATIONAL GRANGE

Mr. NEWSOM. Mr. Chairman and members of the committee, if I may, I would like to file my statement and make some brief oral comments.

Senator DOUGLAS. Very well.

(The statement is as follows:)

STATEMENT BY HERSCHEL D. NEWSOM, MASTER, THE NATIONAL GRANGE

The National Grange is grateful for the opportunity afforded by this subcommittee to present its views and recommendations concerning the current economic recession and to participate in this panel discussion.

Because this economic adjustment is more deep seated and more far reaching than either the recession of 1949 or the one in 1953-54; and because it has brought more unemployment and the trend toward greater numbers of unemployed has been more rapid than in either of the previous recent economic setbacks, the Grange has given much consideration to means of reversing the trend. Since gross national product has also slipped more, and industrial production is off to a greater degree and has dropped faster than in either 1949 or 4 years ago, we feel that the situation poses a real threat to the only relatively good factor in current agricultural income status.

It is also apparent that whether or not we have reached the bottom of this period or whether the bottom is ahead of us, recovery may be very slow. It is this assumption that forms a substantial portion of the basis for today's Grange recommendations.

Specifically, we have wondered how the Nation escaped as long as it did a general recession of serious proportions when agriculture has suffered from major economic ills for several years. A lack of rural buying power has sapped heavily at our national economy.

The National Grange urges, then, that Congress place heavy emphasis at this session upon passage of the sort of an omnibus farm bill that will enable farmers to be a positive bolstering force within the economy. Our recommendations as to the sort of measures this bill should contain are currently before the appropriate congressional committees. Because of the tremendous buying power contribution that a prosperous agriculture makes to the total that is America we should not delay this action. This is in the interest of helping to pull us out of the present recession—but more specifically and of even more immediate concern, to prevent rural America from pulling us into another one.

The National Grange also believes that a tax cut at this time would serve a very useful purpose in stimulating a more rapid recovery. It is true that this economic medicine carries with it some danger—not the least of which is the possibility of spiraling inflation following the recession. This is a delicate matter, however, and a danger that we will have to meet realistically when the time comes. As it is, however, we cannot afford to wait and see any longer. Our view is that a quick upward thrust, even though modest in terms of increased economic activity, could be generated by a wise tax cut at this time.

The tax cut that we propose involves three areas:

1. We would favor reducing the rate on taxable personal income from 20 percent to 16 percent for the first $1,000.

2. The Grange urges immediate termination of the passenger and freight transportation excise tax enacted during the war as a temporary measure. This would tend to lower retail prices, stimulate sales, increase shipments, and carry with it certain psychological values since transportation costs have risen more than other basic costs in recent years.

3. The third tax cut recommended by the Grange involves farm machinery. This is food and fiber production machinery. We advocate removing the excise tax on farm machinery as a means of lowering prices on these essential machines. Farmers must have them to increase their efficiency. Paying for them is now often a difficult task.

We have another recommendation to the Congress. This is in the field of public works. We call for the moving up of those public construction and development programs that provide improvements of lasting value and which meet established national needs.

We believe that present conditions and trends dictate these actions in terms of total American well being.

We further believe that a decline in consumer demand for agriculture's livestock products would now be serious. The probability of avoiding that decline would be much improved by the action that we recommend.

Mr. NEWSOM. Mr. Chairman, we are of course grateful for the opportunity to contribute to this meeting, but we have some misgivings. We admit that our point of view is probably prejudiced from a strictly rural point of view. We feel very firmly, however, that the very fact that this adjustment is more deep seated and more far reaching than either the one in 1949 or the one in 1953–54, and because it has brought more unemployment than either of those, we need to take a harder and more realistic look at the situation.

As we read the figures—and we do not pretend to be qualified to pass final judgment—our very definite impression is that the gross national product has slipped more and industrial production is off to a greater degree than either of these other recessions. This prompts us to be very much concerned about the possible impact upon the only relatively satisfactory phase of agriculture that we have now, and that is the livestock economy.

Senator DOUGLAS. What about vegetables and fruits, Mr. Newsom?

Mr. NEWSOM. Some of the vegetables and fruits that are having price rises now reflect the freeze in the southern area, and have a price structure that is relatively satisfactory. But the income structure for those segments of agriculture is not satisfactory.

What we are attempting to say is that we have no patience with a few people that seem to proceed on the assumption that we can have continued national prosperity in the face of agricultural recession. We think that the prolonged decline in the farm income has had a relatively important impact on this present situation.

We therefore feel that it is imperative that this session of the Congress do something constructive in respect to farm income. But we recognize that this is a little late to rely on even this kind of action in terms of the total national economic structure, and even though we may succeed in getting what we would consider sound legislative action on the farm income front, we still think that there are some other factors that need to be considered now.

We find much basis for agreement with some of our colleagues around the table here. We notice quite a difference in emphasis.

I should like to say that in light of all this situation, the National Grange is prepared to say that we believe there should be a reduction in personal income taxation. We believe that this reduction should take the form of a lowering of the rate on the first $1,000 of taxable income rather than an increase in exemption.

We have discussed this increase in the exemption to some extent, but we are philosophically, more than anything else, opposed to removing 4, 5, or 6 million Americans from the tax rolls entirely, because we believe that all of us as Americans ought to help, even though in a limited way, to support the Federal Government. We all must be made to realize that we have an interest in it.

Our proposal, then, of lowering the rate on the first $1,000 from 20 to 16 percent, we believe, would pump an important $2.8 billion or approximately $3.0 billion into the economy, as a time when we think it might find its way into a sustaining of the livestock section of the agricultural economy here for a relatively short period of time, and thus buy us some more time for adjustment.

We believe, as we have long believed, that transportation excise taxes should be terminated and the excise taxes on communication facilities should be terminated. We believe that the excise taxes on farm-equipment tires, running up as high as $25 to even $35, on a rear tractor tire, should be terminated at this time. This kind of excise tax is not terribly important in the overall, but it is important to the individual. We think there are certain so-called regressive effects, in this kind of a tax structure that need to be examined very carefully now.

Mr. Chairman, that is about the extent of our recommendations. We have had some disagreements and some certain discussions on this, and this is a reflection of a majority considered judgment.

But we do believe firmly that this is a situation that we should confront squarely, even though temperately, perhaps.

Senator DOUGLAS. I appreciate that very much.

The discussion will be continued by Mr. Frazar B. Wilde, chairman of the research policy committee of the Committee for Economic Development.

STATEMENT OF FRAZAR B. WILDE, CHAIRMAN, RESEARCH AND POLICY COMMITTEE, COMMITTEE FOR ECONOMIC DEVELOPMENT

Mr. WILDE. Mr. Chairman and gentlemen, as early as 1954, the Committee for Economic Development was conscious of this possible problem and prepared a policy statement setting forth the principles that we believed should be followed if the economy ran into a recession. We were in one then, but it was not regarded as sufficiently serious to turn our policy recommendation into a specific program.

This fall, it seemed to some in CED that we ought to study our own prescription and see if we had a specific recommendation to make. We met in the fall and winter, and prepared a release which was put out about a month ago, and which revolved around the application of our policy. This is a paper which attempts to repeat that the basic problem in dealing with the recession is the problem of uncertainty. We know that the economic decline will come to an end, but we do not known when, or how far the economy will fall before the end comes. We know that there will be recovery, but we do not know when it will start or how fast it will proceed.

That is based, again, on the basic philosophy of CED that we think this is a dynamic economy. It is going to have periods of halt and readjustment, but will go forward. It will go forward better if we are wise in our readjustments. But we do not think we can avoid some of these ups and downs.

This uncertainty creates risks. If we do nothing, on the assumption that the economy will soon automatically and quickly recover, we run the risk that, if we are wrong, unemployment will continue to rise and production to fall. This may sap confidence to a point where only quite heroic measures can restore the economy to prosperous operation. On the other hand, there are risks in jumping in with massive and long-continuing recovery measures on the assumption that the recession will be deep and protracted. The most serious of these risks is that, if the assumption is wrong, we will add to the already grave, long-run problem of inflation.

There is no way to avoid these risks entirely. They are inherent in the situation. Certainly, we must not think that the risks can be avoided by inaction.

But the risks can be reduced if we choose the timing and character of action that is most suitable both to the best appraisal of the outlook and to the fact that even the best appraisal can be wrong. In a statement issued a month ago, the program committee of CED suggested a course of action intended to avoid the twin evils of too little, too late or too much, too long continued. I shall outline our main recommendations.

1. Do not take strong antirecession action unless the economy declines for 2 months below the February level, with no clear current improvement in sight. Be prepared to act quickly and vigorously if that happens, unless there is unmistakable evidence of quickly forth-

coming improvement. By February, the economy had declined somewhat more than in the recessions of 1949 and 1954. The economy recovered from both of those recessions without extraordinary Government action. We felt that the balance of risks would be against strong action unless the recession was clearly more serious than in 1949 or 1954. On the other hand, a continued decline below the February level, long enough not to be accidental, would shift the balance of risks to the other side, in the absence of clear evidence of prompt recovery. Even though quick, natural recovery would still be a possibility, policy could no longer be controlled by this possibility. We recommended then, and recommend now, that advance preparation be made for quick action to be taken if the decline continues.

We base our wait-and-see policy strictly on reliance on the record and not because we desire to procrastinate or guess one way or the other.

2. If strong action is necessary, a large, temporary tax cut should be made. A tax cut has the great advantage that it can come into effect quickly, certainly more quickly than the chief alternative, which is a spending program of similar size. A tax cut enacted in June or even July is prompter action than a large expenditure program enacted in April. This is so because the tax cut will start raising production and employment sooner. Reliance on the tax cut enables us to wait to get a clearer view of the economic picture and still reduce the danger of being too late if strong action is needed.

3. The tax cut should have a terminal date specified in advance. Any strong antirecession action contains the danger that it will be continued too long, into a period when it causes inflation. This danger is especially great in public-works projects, which cannot be stopped in midstream without serious waste. This particular difficulty does not arise in the case of a tax cut. But, even here, there is a real obstacle to undoing antirecession action when the need for it is past. The obstacle is political. We all dislike taxes, and it takes a great deal of political courage and responsibility to raise taxes, even when the need is clear. Setting a terminal date in advance will not, by itself, solve this problem. There are no mechanical substitutes for maturity and understanding. But a terminal date will help. While the tax cut could still be continued beyond the date set, affirmative action by the Congress and the approval of the President would be required.

4. The tax cut should be simple. This conclusion follows from what I have already said about the timing of the tax cut. We need something that can be quickly adopted and that has a good chance of being temporary. Obviously, a tax measure as complicated as, say, the Revenue Act of 1954, could not be enacted without long study, and we would not want to undo it once it had been done. Also, it would be difficult to get quick agreement on a major shift in the distribution of the tax, such as would be involved in raising exemptions or substantially reducing the progressiveness of the rate structure. We have the tax structure and distribution, we have, despite repeated proposals for change over the past 10 years.

We have been unable to agree on any other program, even though a large majority opinion is strictly of the belief that the present tax structure is inefficient and thoroughly bad from the standpoint of a dynamic economy. I see no likelihood that we could get agreement on a change in the structure now. Moreover, if one or the other viewpoint on how the tax structure should be changed did win out in an antirecession tax cut, this would only reduce the likelihood that the tax cut could, later, be promptly terminated.

The CED has persistently urged reform of the Federal tax system since its first study of this subject in 1944. If this were the occasion for permanent tax reform, we would recommend, as we have in the past, many changes. We would support a reduction in corporate tax rates and further correction of the double taxation of dividends. We would urge a substantial cut in the highest rates of individual income tax, together with measures to make the tax rates apply without special privileges to incomes from all sources. We would recommend correction of our present discriminatory system of excise taxation.

We shall continue to recommend such changes as steps in the permanent improvement of the Federal fiscal system. But we do not include them as part of a temporary antirecession package because we do not believe they could be quickly adopted. We hope that others will refrain from using the recession as an occasion for pressing tax reforms of an isolated character.

A good illustration is the agitation for changing certain excise taxes. This would be wrong, because excise taxes should only be changed as part of a full reform determination.

We need a truce in the contentions over the structure of our tax system, and agreement on a simple, neutral kind of tax cut that can be used as a temporary, antirecession instrument only.

On the basis of these considerations, our committee came to the following conclusion:

If the economy declined for 2 months with no recovery in sight below the February level, there should be a tax cut. The tax-cut legislation should contain provision for its automatic termination on March 31, 1959, although it could, of course, be terminated sooner or continued by act of Congress. The reduction should take the form of a 20-percent, across-the-board, equal reduction of all individual income-tax rates. This would affect withholding immediately upon enactment and other income-tax payments when they are normally made.

The economy has already declined—in March—for 1 month below the February level. We do not yet have sufficiently comprehensive figures to tell reliably what happened in April. Even the April figures would not be conclusive if in May there was clear evidence of an upturn. But Congress should be at work now preparing the kind of tax cut that could be promptly enacted if the April figures on production, sales, incomes, employment, and unemployment show continuation of the economic decline and if clear signs of an upturn do not emerge.

The idea that a tax cut should be the main instrument of Federal policy in a recession is fairly new, having only come into prominence in the postwar period. The reasons for a tax cut are not adequately understood. Much public thinking on these matters still reflects what we now know to be rather primitive notions that emerged in the 1930's. This thinking has not advanced much beyond the idea that the Government can increase employment by putting men to work directly on public projects.

But what counts is not merely the jobs the Government directly creates by its expenditures, but the effect of its entire fiscal policy on the total number of jobs. This means that we must look both at Government receipts and Government outlays. The net effect of Government fiscal policy on employment is the difference between the jobs the Government creates by its spending and the jobs the Government prevents from being created by its taxes.

Individuals and businesses cannot spend money the Government takes from them in taxes. Indeed, the main function of taxation is to keep the individuals and businesses from spending. But private spending creates jobs. Consequently, when we need more employment it is only logical to reduce the employment-restricting effect of taxation.

A government that is already collecting over $70 billion a year in taxes to restrain private spending does not need to add more expenditures of its own to stimulate spending. All it needs to do is to stop restricting private spending so hard. In fact, this is the only thing it can effectively do on a large scale. For a large expenditure program will almost certainly combine the evils of too little and too much. Because of the time required to get it underway, it will help little in the near future when we need it. But it will be reaching its maximum impact in 18 months or 2 years, when their effect is likely to be inflationary.

In conclusion, may I comment about the responsibilities and opportunities of your Joint Economic Committee in the present recession. This is, in my opinion, the kind of problem which the Joint Economic Committee was created to help solve 12 years ago.

Congress is being flooded with proposals for doing something about the recession. Recognizing that some items are heavily tinged with politics and local issues, they nevertheless represent the point of view of many groups, and deserve review. Most of these proposals are spending programs, others involve Federal lending or a combination of Federal lending and spending in combination with State and local bodies. Some involve tax changes. Accelerated defense spending is a favorite proposal. None of these proposals is being carefully analyzed in a broad and relative sense as part of a total program.

What would its effects be? How would its effects be distributed over time, which is one of the vital questions. Nobody is comparing the total with any estimate of what might be sound. Nobody is trying to establish priorities among the various courses of action. These are all functions that the Joint Economic Committee could perform in its capacity as a general staff charged with the duty to make plans for action against recession. The Congress as a body cannot perform this duty. Your committee can, and it would be an exceptionally valuable contribution and in the best interests of the public as a whole.

While in a vague way the country thinks this is your responsibility, there is apparently no specific recognition of the approach I am trying to outline, which would lead to this committee's being the initiator of a comprehensive, rational, balanced plan of attack.

Another observation, which is relevant and important, is to remind the country that the overwhelming bulk of economic activity in this country is and must continue to be performed by individual citizens, individual businesses, and individual communities, unless we intend to abandon our free economy. More than 75 percent of the activities of our country are generated in the private sector. Things that Congress does or proposes must instill confidence in that sector and not discourage or alarm it.

I must say that I am amazed, and somewhat amused, to see the ideas of our self-designated "modern" and "liberal" thinkers in this recession. The proposals of those who consider themselves devotees of Government planning turn out to be unsystematic and planless. The wornout phrase used by the so-called liberals that "a positive approach is needed by Government" ends up as a demand to do something—anything—everything—and do it now.

Your Joint Economic Committee is in the best position to introduce, through thoughtful staff work, recommendations that produce order and reason for consideration by the legislative bodies. You would greatly aid the Congress and the country by undertaking the task.

I would like to add this comment in connection with the CED's recommendation for a tax cut. I was a member of the program committee, which debated the CED recommendation this winter. The committee assumed, as we have strongly urged here, that there be a minimum increase in public expenditures if a substantial antirecession tax cut were to be adopted. It is a pretty bold thing to recommend a tax cut of the magnitude of some $600 million a month, which, if continued for the full period, would run into very large figures. If as a result of massive spending programs, we are to run into a deficit of $15 billion to $20 billion in the next 2 fiscal years, as the papers have reported Senator Byrd as prophesying, our recommendations might change. CED would hesitate to add a large tax cut if the Congress decides on expenditure programs of the aggregate amount being discussed.

Senator DOUGLAS. Thank you very much.

Mr. Wilde, do you desire to have the material appended to your prepared statement incorporated in the record at this point?

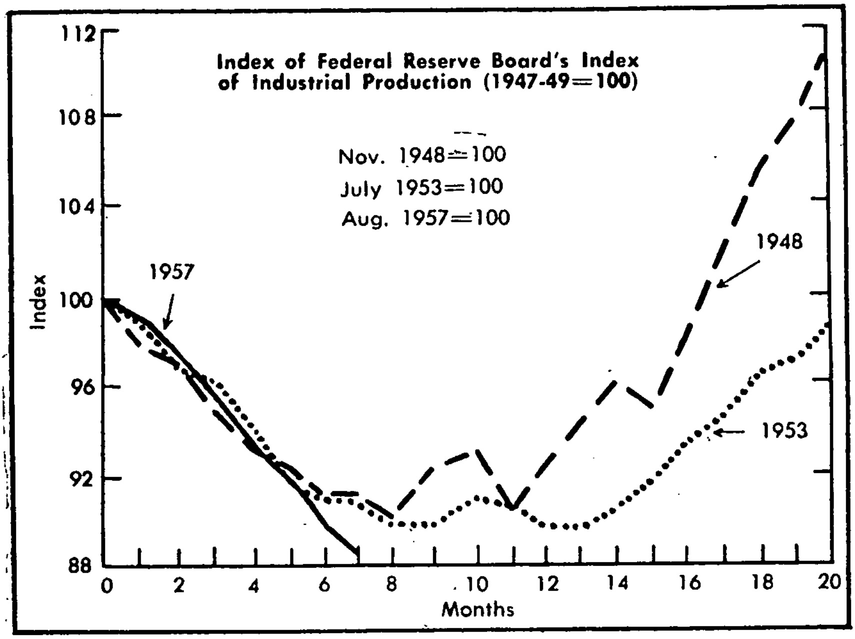
Mr. WILDE. If you please, sir.

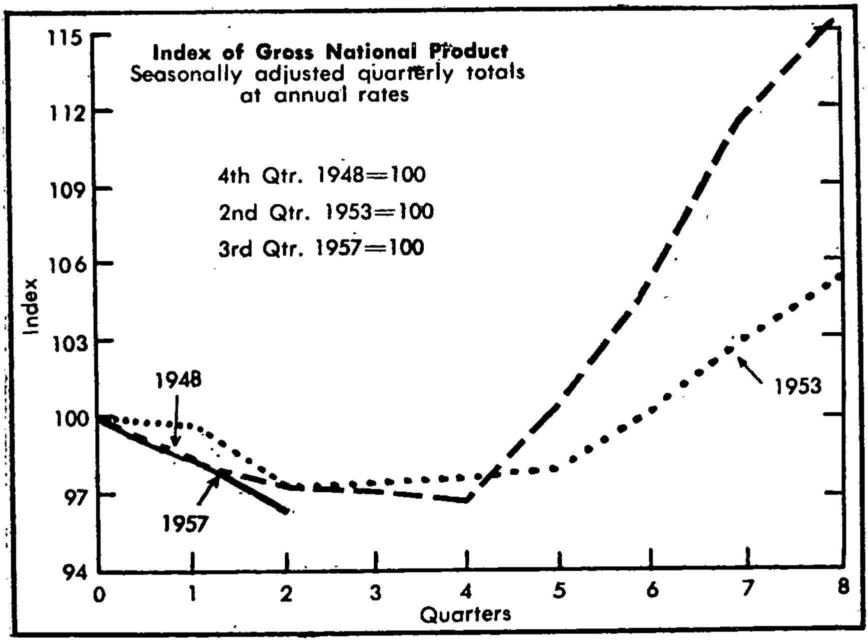
Senator DOUGLAS. Without objection, that will be done.

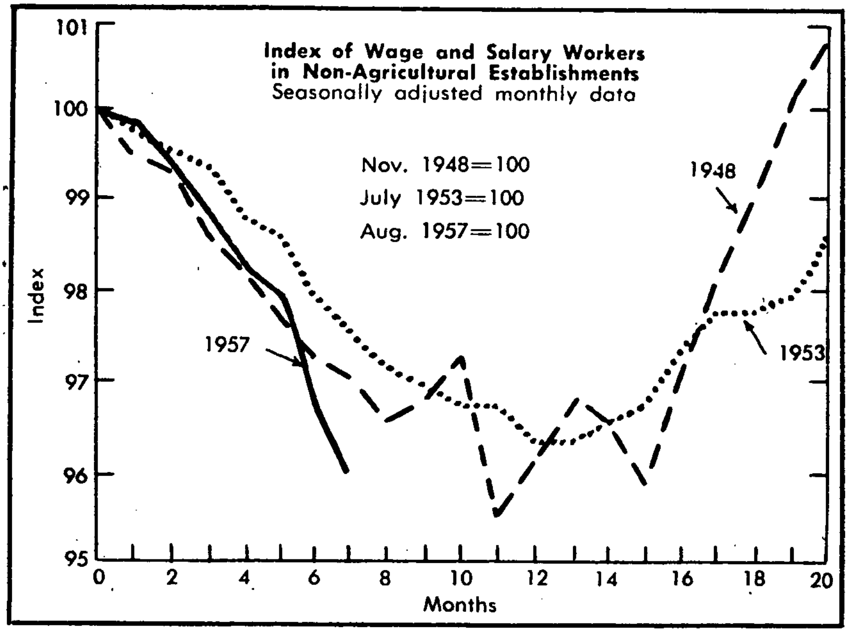
(The material is as follows:)

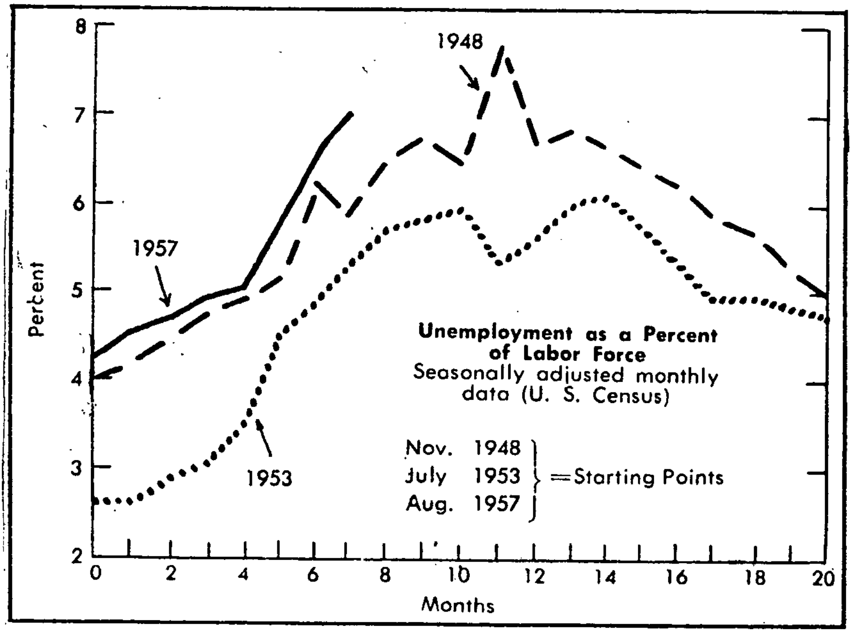
SCOREBOARD IN THE THREE RECESSIONS: 1948–49, 1953–54, 1957–58

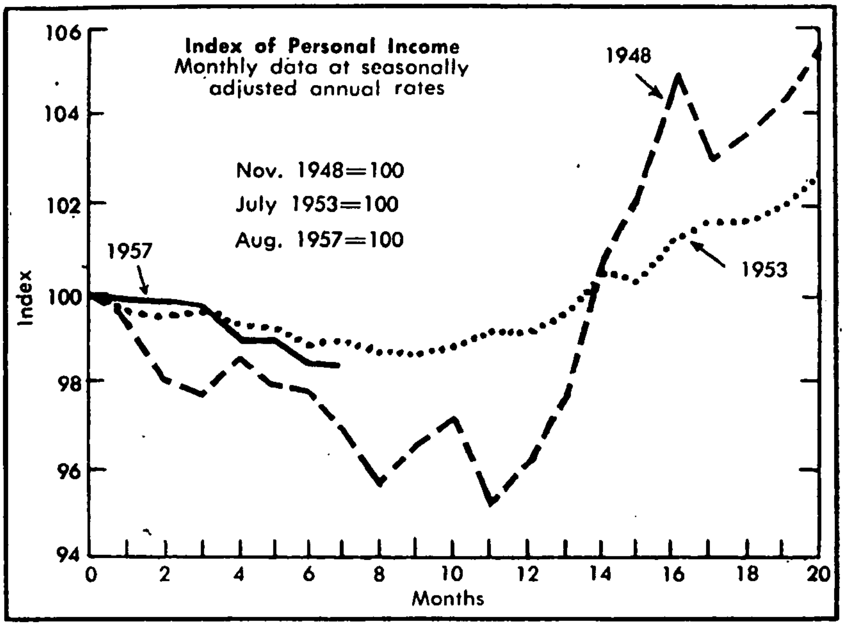
Charts prepared by the Research Division, Committee for Economic Development, April 1958

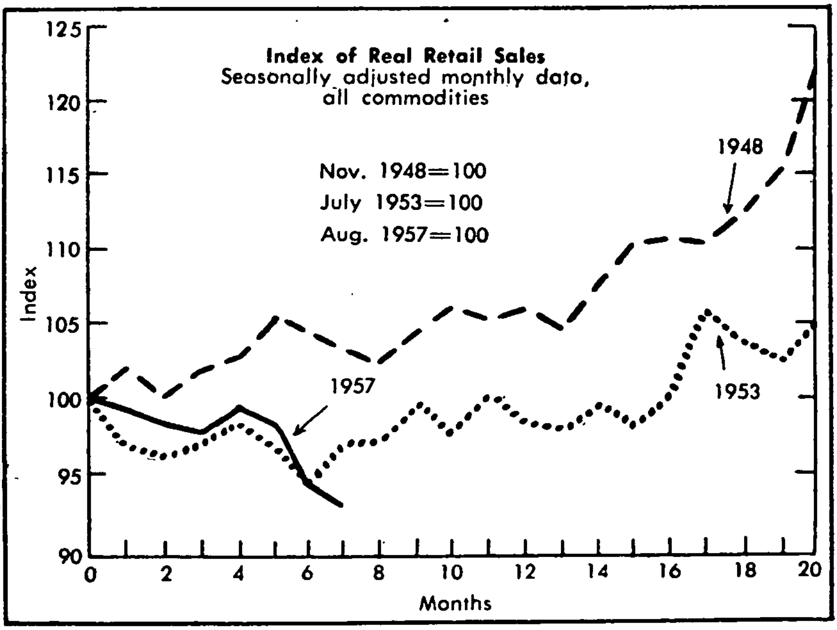


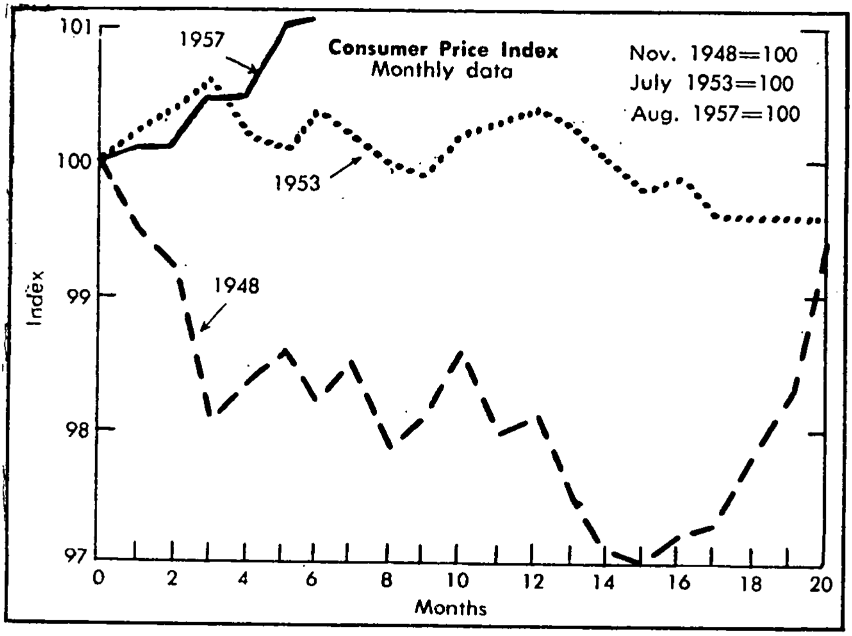


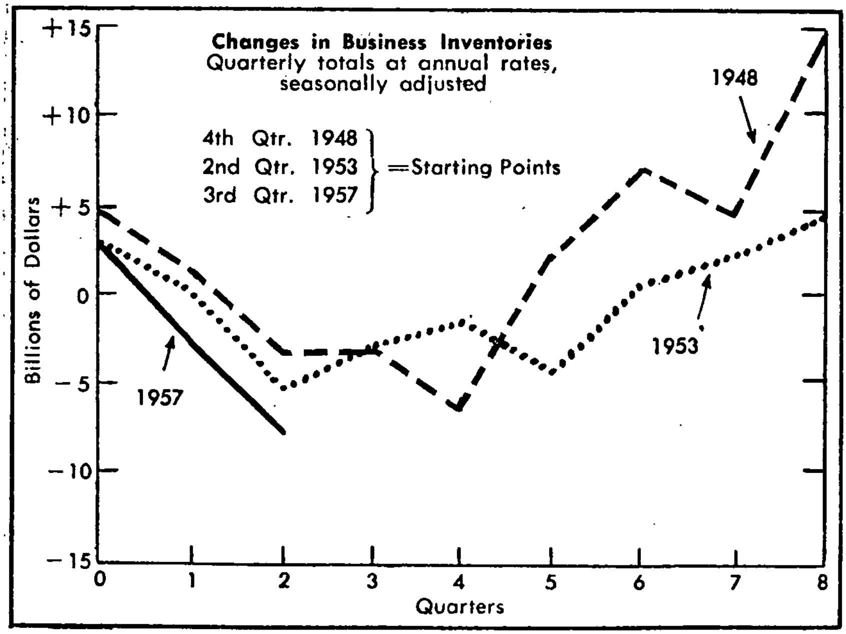

Index of Wage and Salary Workers
in Non-Agricultural Establishments
Seasonally adjusted monthly data
Nov. 1948=100
July 1953=100
Aug. 1957=100
1948
1957
1953
Index
101
100
99
98
97
96
95
0 2 4 6 8 10 12 14 16 18 20
Months

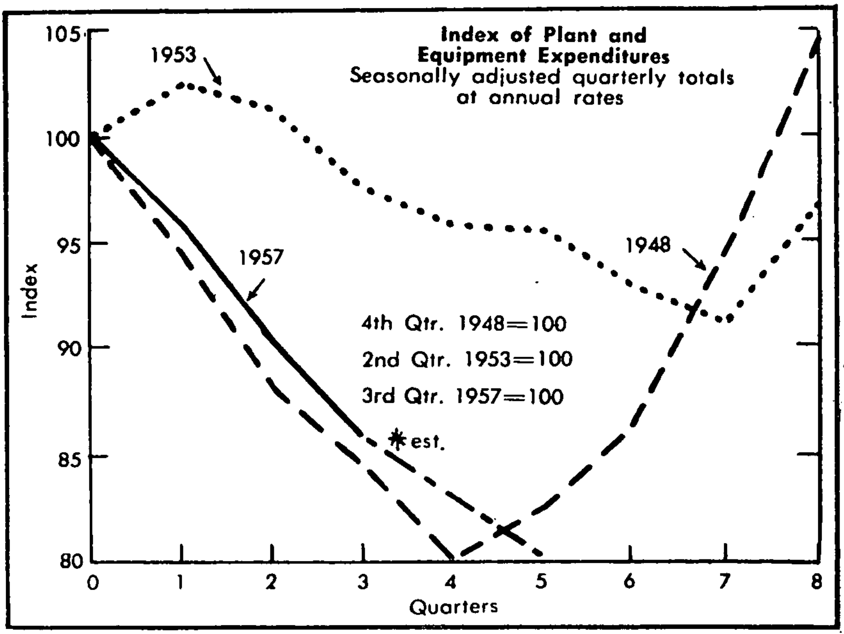

Unemployment as a Percent
of Labor Force
Seasonally adjusted monthly
data (U. S. Census)
Nov. 1948
July 1953
Aug. 1957
=Starting Points
1948
1957
1953
Percent
8
7
6
5
4
3
2
0 2 4 6 8 10 12 14 16 18 20
Months

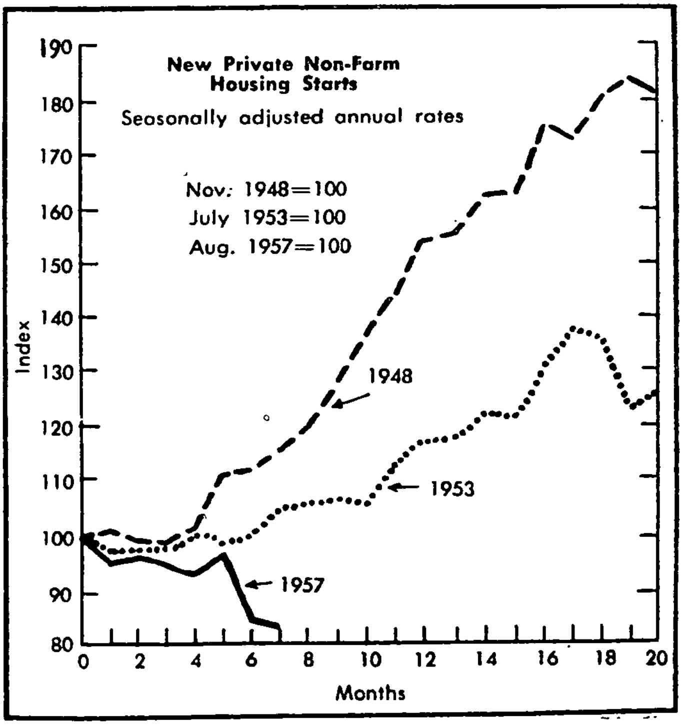

Index of Personal Income
Monthly data at seasonally adjusted annual rates
Nov. 1948=100
July 1953=100
Aug. 1957=100
1948
1953
1957
106
104
102
100
98
96
94
Index
0
2
4
6
8
10
12
14
16
18
20
Months

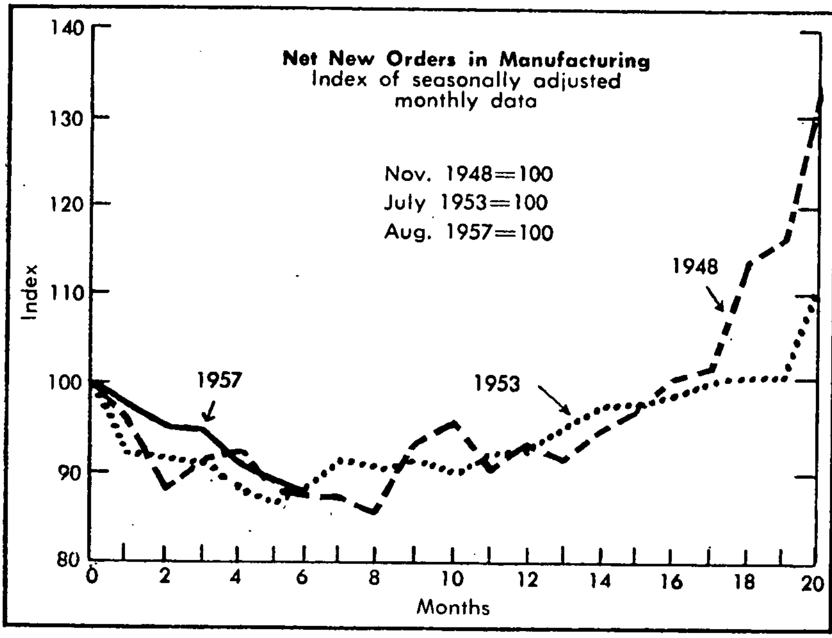

Index of Real Retail Sales
Seasonally adjusted monthly data, all commodities
Nov. 1948=100
July 1953=100
Aug. 1957=100
1948
1953
1957
125
120
115
110
105
100
95
90
Index
0
2
4
6
8
10
12
14
16
18
20
Months

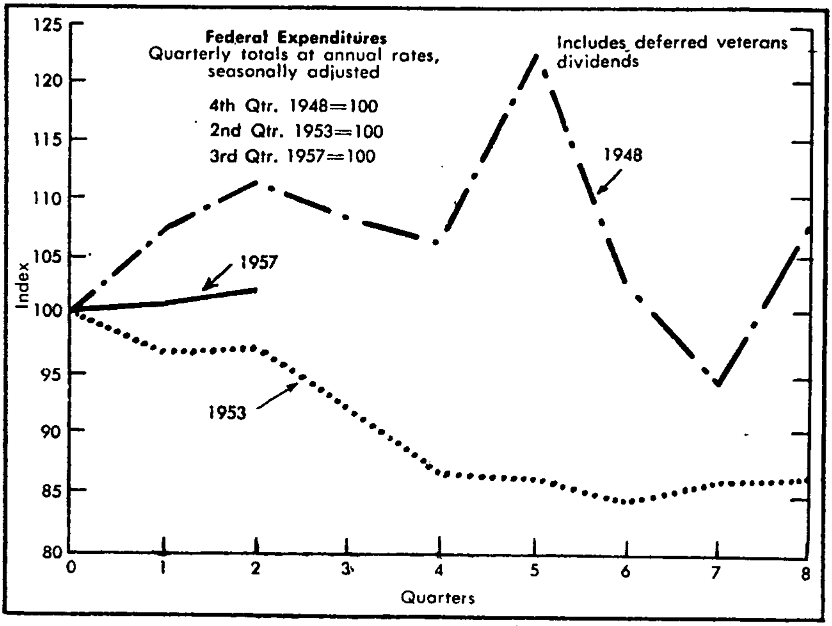

Consumer Price Index
Monthly data
Nov. 1948=100
July 1953=100
Aug. 1957=100
1957
1953
1948
Index
101
100
99
98
97
0
2
4
6
8
10
12
14
16
18
20
Months

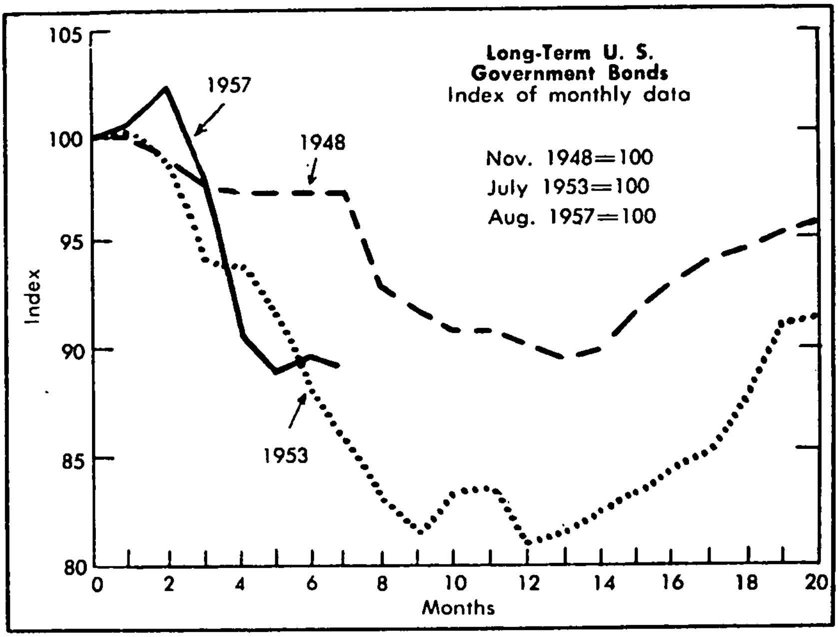

Changes in Business Inventories
Quarterly totals at annual rates,
seasonally adjusted
4th Qtr. 1948
2nd Qtr. 1953
3rd Qtr. 1957
=Starting Points
1948
1953
1957
Billions of Dollars
+15
+10
+5
0
−5
−10
−15
0
1
2
3
4
5
6
7
8
Quarters

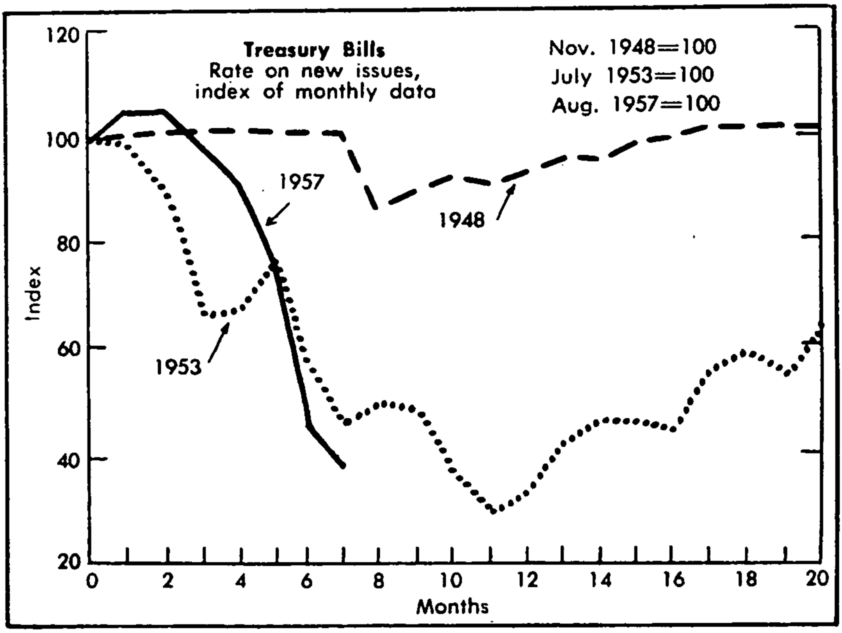

Index of Plant and
Equipment Expenditures
Seasonally adjusted quarterly totals
at annual rates
4th Qtr. 1948=100
2nd Qtr. 1953=100
3rd Qtr. 1957=100
*est.
1953
1957
1948
Index
105
100
95
90
85
80
0 1 2 3 4 5 6 7 8
Quarters


New Private Non-Farm
Housing Starts
Seasonally adjusted annual rates
Nov. 1948=100
July 1953=100
Aug. 1957=100
1948
1953
1957
Index
190
180
170
160
150
140
130
120
110
100
90
80
0 2 4 6 8 10 12 14 16 18 20
Months


Net New Orders in Manufacturing
Index of seasonally adjusted monthly data
Nov. 1948=100
July 1953=100
Aug. 1957=100
1948
1957
1953
Index
140
130
120
110
100
90
80
0
2
4
6
8
10
12
14
16
18
20
Months


Federal Expenditures
Quarterly totals at annual rates, seasonally adjusted
4th Qtr. 1948=100
2nd Qtr. 1953=100
3rd Qtr. 1957=100
Includes deferred veterans dividends
1948
1957
1953
Index
125
120
115
110
105
100
95
90
85
80
0
1
2
3
4
5
6
7
8
Quarters


Long-Term U. S.
Government Bonds
Index of monthly data
Nov. 1948=100
July 1953=100
Aug. 1957=100
1957
1948
1953
Index
105
100
95
90
85
80
0
2
4
6
8
10
12
14
16
18
20
Months


Treasury Bills
Rate on new issues,
index of monthly data
Nov. 1948=100
July 1953=100
Aug. 1957=100
1957
1948
1953
Index
120
100
80
60
40
20
0
2
4
6
8
10
12
14
16
18
20
Months

Data for Using These Charts

In all but 2 cases, we have given all 3 recessions a common starting level—an index of 100—in our charts to make the speed of change in the 3 periods easier to compare. In two cases—unemployment and inventories—comparison was only practical when actual, rather than index, starting levels were used.

Where data are by months, November 1948, July 1953, and August 1957 are the times when the activity charted equals 100. Where data are by quarters, the starting times are the fourth quarter of 1948, the second quarter of 1953, and the third quarter of 1957.

Numbers along the bottom of each chart indicate months, or quarters, from the time the recession began. Numbers along the side of the chart indicate change.

Antirecession Policy for 1958

A statement by the program committee of the Committee for Economic Development, March 1958

FOREWORD

This is a statement by the program committee of the research and policy committee of Committee for Economic Development. It is issued under the rule of the research and policy committee which authorizes the program committee to issue statements within the framework of policy previously stated by the research and policy committee. This statement is based on two statements by the research and policy committee: Monetary and Fiscal Policy for Greater Economic Stability, issued in 1948, and Defense Against Recession, issued in 1954.

Except for the members of the program committee of the research and policy committee, the recommendations presented in this program committee statement are not necessarily endorsed by other trustees or by the advisers, contributors, staff members, or others associated with CED.

THE PROGRAM COMMITTEE

Antirecession Policy for the Federal Government in 1958

PREFACE

This statement deals with the policies that the committee for Economic Development believes the Federal Government should follow in 1958 to aid economic recovery. The statement is confined to a discussion of Federal policies because, unlike private or local governmental actions, they require the collective decisions of the Nation as a whole as expressed by the Congress and the administration.

Production and marketing in the United States are conducted primarily by individual private business enterprises, and sales of their products are made mainly to private customers. In such a society, exercise of good sense and responsible behavior by private citizens is indispensable to economic growth and economic stability. Most American businessmen and consumers have a well-justified faith in the prospects for continued long-term expansion of the economy.[1] This provides a background of confidence for private decisions that are currently required. The Federal Government can do much to aid in establishing conditions conducive to recovery. By following policies that are helpful now, and by planning for stronger action if it should become necessary, it can assist in maintenance of confidence in the short-run future among private citizens, an essential

[1] See CED, Economic Growth in the United States: Its Past and Future, 1958.

for resumption of sound business expansion. Businessmen should welcome properly thought-out governmental steps for this purpose.

There is also a responsibility upon Government to avoid reacting to the present recession in ways that would impair business confidence, such as extravagant and wasteful spending schemes or new social experiments.

An earlier CED statement discussed the responsibilities of individual businessmen as well as of other groups in the community in the reduction of economic fluctuations.[3] One contribution would be to do even better the things they already do well—such as developing new products to satisfy new wants and applying improved production and distribution methods to reduce costs and prices and bring more products within the reach of more people. They can improve their inventory and investment policies, in comparison with what has been done in the past. Exaggerated pessimism and over-stressing of short-term sales developments are to be avoided. The wise plans for plant and equipment expenditures that many businesses have scheduled are no less wise now and should be carried out. Maintenance of sales effort also is important. In the past, the sales budgets of businesses have often been one of the first things cut when sales decline. This is partly because sales effort is easy to cut and partly because advertising budgets are commonly determined by a rule-of-thumb ratio to sales. It is true that the market for particular products may become so unresponsive to selling effort that the return per dollar of sales effort declines. But this is not commonly the case today, when income has continued to flow to consumers at a right rate.

While businesses, like others in the community, suffer a loss of income in periods of recession, the development of slack in the economy also offers frequent opportunities to get more for each dollar spent—to modernize and expand facilities with a smaller outlay, to tighten operations and improve efficiency generally, and thus to lay the basis for expanding markets by offering better values to customers. Alert businesses are taking advantage of these opportunities today, and by doing so contributing to economic stability.

Just as business has its responsibilities, so labor and its leaders have responsibilities for helping to maintain the conditions necessary for economic growth. Collaboration in working out ways and means for reducing costs so that consumer values may increase would be one important way of doing this.

CED does not claim that the program presented in this statement would immediately and exactly restore the economy to high employment and production. The time and pace of recovery will depend upon the decisions and actions of private consumers and producers. The influence of Government can stimulate and supplement private behavior but not displace it. How the private economy will respond, when and how fast, are difficult to predict. As CED's research and policy committee said in 1947:

"The picture of an allwise expert precisely manipulating the keys of the fiscal instrument to produce a perfect harmony of stable demand is sheer, and dangerous, fantasy."

What we would claim is that sensible, flexible, and well-timed Government policy—policy that we are prepared to moderate, terminate, or supplement as conditions change—can significantly reduce the range of fluctuations to which the economy might otherwise be exposed, and thereby encourage individuals and businesses to act with faith in the resumption of long-term economic growth.

Early 1958 finds the United States in a business recession—the third since the end of World War II. The country is determined that the present recession, like its predecessors, shall be followed by recovery without a long-extended or very severe intervening period of excessively low sales and production.

Our economic system has great inherent strengths and bright prospects for long-term growth that provide background conditions favorable to recovery. The monetary authorities have adopted a policy of making credit more readily available and cheaper, thus facilitating the financing of private purchases. The Government is allowing the built-in stabilizers in the Federal budget to operate, by permitting tax revenues to fall with the drop in taxable incomes, and Government outlays to rise as unemployment insurance benefits and other transfer payments increase, without trying to close the resulting budgetary gap by raising tax rates or cutting expenditures. If these measures should prove insufficient, the country has available in the Federal budget a powerful tool that can be used, not with precise effect, but nonetheless with sufficient strength to pre-

[3] See CED, Defense Against Recession: Policy for Greater Economic Stability, 1954.

25780—58——12

vent a long drawn-out depression. Use of this mechanism includes some readjustment of Government purchases, including well-considered public works, to increase private production and employment, but consists mainly of cutting taxes temporarily to allow private citizens to use more of their current income for spending.

CED believes that it would be prudent for the Nation to agree now both on the conditions under which such stronger action would be instituted and, in fairly definite terms, on how expenditures would be increased and taxes cut if these conditions occur. This recommendation implies no forecast that stronger action will in fact become necessary.[3] Definite plans to deal with this possibility would, however, provide business firms and consumers with even stronger grounds than now exist for continuing their normal spending rates and expenditure plans in the confident expectation that a serious depression does not lie ahead. It would also reassure the country that deterioration of the economic situation, if it should develop, would be met calmly with effective action to promote recovery. The decision to use stronger measures will then be viewed, properly, not as a sign that we are in a desperate situation, or that policy has failed, but as a contingency for which appropriate plans have been laid.

While we are in a recession today, we have behind us a long period of inflation. The Consumer Price Index was 7 percent higher in January 1958, than in January 1956, and almost one-third higher than in January 1947. The price index has not declined in the present period of business contraction, and in January 1958, the most recent month for which data are available, moved up.

We want to end the present recession and restore high production and employment. We also want to avoid a resumption of inflationary price increases. Since short-run policies for creation of more jobs are almost the exact opposite of those for restraining inflation, to achieve the dual objectives requires flexibility, discrimination, and determination. This imposes some genuine difficulties. We believe, however, that the Nation can avoid excessive waste of productive resources for a long period without adding greatly to subsequent inflationary danger if we act with sufficient responsibility and political maturity.

Our proposal for 1958 is simple, and we believe it will be effective in putting a floor under the decline and setting the stage for recovery. So long as the recession does not become deeper than in 1949 and 1954, we should utilize monetary policy vigorously, and adhere to a budget policy that permits a deficit to widen in automatic response to lower private employment and earnings. In addition, plans should be made now for stronger action to be taken if and when necessary.

If the economic situation becomes clearly worse than in 1949 and 1954, as would be the case if seasonally adjusted production and employment continue to drop as they have during the fall and winter, this should be taken as a signal for stronger action. Necessary Federal purchases and public works that would otherwise be undertaken at a later date should be advanced, but only in situations in which the major impact upon the economy would be felt within a year or so. Main reliance, however, should be upon a large temporary cut in personal income taxes to stimulate private spending. For the conditions in which a tax reduction would be necessary, we would recommend a cut of one-fifth in personal income tax rates effective until March 31, 1959. This would mean a tax reduction, computed at high-employment income levels, at a yearly rate of $7½ billion. At the end of the period, the cut would end unless the economic situation at that time demands its extension in whole or in part.

CED's Research and Policy Committee has repeatedly recommended reduction in the corporate profits tax and in selective excise taxes as part of the long-run reform of the Federal tax structure. We urge consideration of these and other desirable tax reforms at the earliest possible time. We omit them from the proposed antirecession tax program only because of our desire to concentrate on the simplest step, on which quick agreement would be most readily forthcoming. We believe that reduction of individual income taxes would be an effective way of stimulating an increase in private spending, with resulting increased employment, until expansionary forces within the private economy reassert themselves.

We cannot emphasize too strongly the importance of distinguishing clearly between temporary emergency measures to deal with the recession and permanent

[3] Footnote by Allan Sproul, in which Howard C. Petersen has asked to be associated: "While I agree in general with the measures recommended in this statement, I believe that we are closer to the time of decision on more vigorous antirecession measures than the statement seems to suggest."

changes in public policy. This distinction will make prompt and effective action both more feasible and less dangerous. The possibility of agreeing quickly on emergency measures will be greatly enhanced if there is also agreement that these measures are for the duration of the emergency only. In particular, it should be much easier to agree upon a generally acceptable tax cut to last for a short period than to agree upon a broad and permanent revision of Federal tax policy with all the complications that entails.

Moreover, the danger the emergency measures would persist into conditions when they would be inappropriate—when they would be inflationary, wasteful or inconsistent with a long-term growth—would also be reduced by prior understanding of their temporary character and by advance provision for their termination. One implication of this is that we must all resist the temptation to use the recession as an occasion for trying to fasten permanent changes upon Federal policy with respect to expenditures, taxes or anything else. Permanent changes should be considered in the light of the expected long-run condition of our economy, which is not a condition of recession.

We also wish to warn against the danger of basing policy primarily on forecasts of the future rather than on present facts. Forecasts of the short-term course of employment and business are guesses that cannot be continuously correct, so that any action based upon them may be wrong. Moreover, agreement can rarely be reached on forecasts of the future. Hence, if effective policy action depends upon forecasts, we may do the wrong thing or do things too soon or too late.

We do not wish to fire our heaviest antidepression artillery each time business activity slackens, simply because we fear future economic collapse. A practice of doing so in periods such as that we are in today would make inflation unavoidable, and also impair the flexibility that our economy requires to adapt to changing patterns of market demand. But in a serious situation we do not want to temporize and delay because of successive forecasts that an upturn is just ahead. When the existing situation is clear, we want vigorous action by the Federal Government to help restore high employment and production, and we need the confident action of the business community based on knowledge of our longer-term growth. It is always possible to find scraps of information, seasonal movements, and signs and portents to rationalize optimism or pessimism as to near-term future events. But they provide no basis for national policy.

THE PRESENT POSITION OF THE ECONOMY

The current decline in business activity is one of the long series in the wavelike movement that has been characteristic of our economic growth. Most previous business declines in our history have been moderate and brief, with the downward movement ending within a year, recovery substantially completed within 2 years, and the trough in the Nation's total output not more than a few percent below the previous peak. The recessions of 1949 and 1954 were of this character. We have had only a few depressions that were both very deep and prolonged; those beginning in 1837, 1873, 1893, and 1929 are the only ones that really qualify for this description. Their extreme character stemmed largely from the collapse of the financial system, and the wholesale destruction of confidence that such a collapse engendered. Institutional changes in the financial system since 1929 provide a guarantee against financial collapse and, along with other changes, warrant our belief that there will not be a future depression on the scale of the thirties. We have also had a certain number of depressions of intermediate character, such as those that started in 1920 and 1937. We have done a good deal to make such pronounced dips less likely, but we cannot be sure that we will not have to deal with them again.

The most recent peak in production, employment, and income was reached in August 1957, culminating a 3-year advance. At that time business expenditures for plant and equipment—mainly equipment—were leveling off after a long and sharp advance, and there was an actual decline in such expenditures in the fourth quarter. Moreover, business programs called for reduction of investment expenditures throughout 1958. With smaller investment programs, orders to equipment manufacturers fell off, and they reduced their production and employment as well as their orders to suppliers. At the same time that the rise in investment was ending, the Federal Government, noting that continuation of the existing uptrend of defense expenditures would carry outlays far above the budget estimate for the fiscal year 1957–58, and seeking to remain within the authorized debt limit, curtailed new contract placements, cancelled some existing contracts, and accomplished a small reduction in the actual rate of expenditures. Consumer buying of automobiles had slipped earlier in the year; later, consumer purchases of household equipment also declined. Meanwhile, there was a reduction in United States sales abroad.

The leveling and subsequent reduction of hard goods sales, accompanied by a much sharper reduction in new orders, made inventories of hard goods and materials entering into their production appear excessive, especially at the manufacturers' level. Inventory accumulation, which had been absorbing some of the current output of the economy, gave way to inventory liquidation in the last quarter of 1957, and has since continued. This shift from inventory accumulation to liquidation was the immediate source of most of the drop in the national product.

In February 1958, employment in nonagricultural establishments, seasonally adjusted, was 1.7 million, or 3.2 percent, lower than in the previous August. In the same period, the seasonally adjusted unemployment rate rose from 4.2 percent of the civilian labor force to 6.7 percent.[4] Short hours became more prevalent. The gross national product, seasonally adjusted at annual rates, dropped from $440 billion in the third quarter of 1957, when the economy was operating at high employment, to $432½ billion in the fourth. If allowance is made for both the subsequent decline and the fact that prices had risen, it is likely that by February the "real" gross national product, which measures the total production of the economy, was about 3½ percent below the 1957 third quarter. But with normal growth of the economy's productive capacity, we would now be able to produce about 1½ percent more than in the third quarter of 1957. This would indicate that in February the economy was operating at about 95 percent of the high-employment level, if gross national product in the third quarter of 1957 is taken as a standard. The decline in employment and production was not slackening.

This, in broad terms, is where we stand as this is written. Certain important characteristics of the decline thus far should also be pointed out. Consumer expenditures for nondurable goods and services, together, which in 1957 absorbed 56 percent of the entire gross national product, have held up well. This is significant, because an outstanding characteristic of the declining phase of major depressions is a general downward spiral of consumer income and consumer spending. Thus far in the present recession the decline in spending has not become general, and such a cumulative spiral is not in process. It should also be noted that purchasing by State and local governments is continuing to rise; Federal Government spending is scheduled to turn up a little; and the movement of residential construction activity continues irregular rather than clearly upward or downward.

The impact of the recession thus far has been principally upon employment and production in durable goods manufacturing. Employment in mining, construction, transportation, and nondurable goods manufacturing has been affected to a lesser extent. In other industrial divisions, employment has declined only slightly or increased.

Despite important differences in the forces initiating declines in 1948, 1953, and 1957, the magnitude and most general characteristics of the 1957–58 decline are similar to the patterns of the 1948–49 and 1953–54 recessions after they had been in process for the same length of time. However, they are also similar to the pattern we should expect in the early stages of a more serious decline if we make allowance for the support provided to consumer income by "automatic stabilizers," such as unemployment insurance, that have been introduced since we last experienced such a decline.

If the probabilities are that the amplitude and duration of the 1958 recession will be similar to those of its immediate predecessors, it is mainly because most recessions are of such a moderate character. That we do not know what will bring a reversal does not mean that it will not appear—any more than the outstanding sales success of the 1955 model automobiles, that accelerated recovery in late 1954, could be foreseen with assurance earlier in that year. But we must also reckon with the possibility that we are in the early stages of a more serious decline. The most likely cause would be the same as in many such periods in the past—a pronounced and prolonged slide in the rate of business investment in plant and equipment, without sufficiently strong offsets in other types of demand.

[4] Without seasonal adjustment, unemployment in February was 7.7 percent, or 5.2 million persons.

Reinforced by a further drop in foreign sales, and by a rise in the rate of business inventory liquidation, a sharp slide in business capital outlays could curtail consumer income enough to set in motion the characteristic downward spiral of consumer income and spending, the hallmark of depression.

Our purpose in this section has been to indicate in a general way where the economy now stands, and to warn of the difficulties of forecasting where it is going. The remaining sections of this staement will discuss, in order, the following questions: 1. What should be done now? 2. Under what conditions would stronger antirecession measures be appropriate? 3. What should be done if the recession deepens?

WHAT SHOULD BE DONE NOW

Federal policies in a period of recession such as that existing in early 1958 should—

Be adequate. The aim is effective help in supporting business activity now and reversing the forces making for contraction.

Be flexible. It must be possible to employ them quickly, and to reverse them quickly so that they will not contribute to inflationary pressures when recovery gets underway.

Be general. It is important to avoid interference with the adjustments in resource allocation, prices, and costs that are needed to keep the economy efficient; the way to avoid interference with the normal adjustment processes of the economy is to rely upon general measures to stimulate spending, production, and employment, rather than on attempts to increase demands for particular products.

Include definite plans for more vigorous action if the economic situation should seriously deteriorate, and specify the conditions under which such action would be taken.

In view of these considerations, we suggest the following program for the present situation:

1. *Monetary policy.*—A main reliance for support of the economy in the present situation should be monetary policy.

Monetary policy influences private spending through its effect on the supply of money and the cost and availability of credit. Individuals and businesses tend to spend more if they have easier access to credit, if the cost of borrowing declines, and if they find themeselves holding more cash and other liquid assets in relation to their needs.

All of these factors depend, to a great extent, on Federal Reserve policies, since the Reserve System can make credit more readily available at lower cost by increasing the reserves of the commercial-banking system. It can do this by buying Government securities in the open market or by reducing the reserves the member banks are required to hold against their deposits, and it can lower the interest rate at which banks can borrow reserves from the regional Federal Reserve banks. These actions increase the lending capacity of banks, and reduce the cost of borrowing and this, in turn, will tend to stimulate the banks to lend more readily to qualified borrowers at favorable interest rates and will thus help to increase private expenditure.[5]

Since last fall, the Federal Reserve has taken action along each of these lines, and also reduced the margin requirement for purchasing corporate stock. Its continuing action in this direction has our commendation.

The Federal Reserve System should move even more vigorously to provide the banks with abundant reserves. The reserve position of the banks should be adequate not only to permit them to meet all sound loan demands that come to them, but also to impel them to seek to make additional sound loans and acquire other assets. The small decline in the money supply (seasonally adjusted) that has occurred since mid-1957 should be halted and reversed. We believe that monetary policy is most effective when it is used wholeheartedly. Obviously, we cannot prescribe the precise timing of the necessary steps or the magnitude of reserves that should be supplied. Such decisions must be made by the Federal Reserve on the basis of day-to-day developments.

In deciding on the appropriate policies, some lessons can be learned from the experience during the 1953–54 recession and the succeeding expansion. It is clear that the policies pursued in that recession helped in the reversal of the

---

[5] For a detailed explanation of how monetary policy operates to stimulate expenditures, see our statement entitled "Flexible Monetary Policy: What It Is and How It Works," 1953.

business decline and the resumption of growth. But it now appears that once recovery began the reversal of monetary policy may have been delayed too long and was thus less effective than it might have been in moderating the credit expansion that was associated with the 1955 boom. This experience should not discourage more vigorous action now. The problem at hand is to arrest the decline, and monetary policy should play its full role in the antirecession program. When that has been done, the Federal Reserve should be prepared to reverse its policies at an early stage in the next expansion in order to restrain inflationary pressures.

When a Federal agency accepts loans for guaranty or insurance at lower rates of interest, lower downpayments, or longer maturities, those seeking credit are able to borrow more than they would otherwise be able to borrow. Obviously, there are limits beyond which terms of credit should not be liberalized, but terms on residential mortgages were restricted during the boom, and there is now some room for moving in the other direction.

2. *Federal budget policy.*—In a recession, Federal tax receipts tend to fall, and unemployment-compensation payments, social-security pensions, public-assistance payments, and other expenditures increase. These automatic responses to recession are stabilizing, because they cushion the decline in incomes that individuals and businesses have available to spend.[6]

The Federal budget should be permitted to exercise its normal, stabilizing effect on the economy—an effect that is far stronger than at any time prior to World War II. This means that if, as is to be expected, tax receipts drop below those estimated in the President's budget because of lower incomes, we should not try to make up the deficiency in receipts by raising tax rates or by lowering expenditures.

In addition, some acceleration of Government expenditures planned for the near future under existing authorized and necessary programs is appropriate.

To get the stabilizing effect of the budget principle we recommend, it is necessary that in a recession the budget be allowed to run a deficit as tax revenues drop and certain expenditures automatically rise. In the coming year—fiscal year 1959—tax receipts are very likely to fall below the budget estimate, mainly because individual and corporate incomes are likely to be lower than was assumed in the tax forecasts. If this happens, the debt limit should not force the Government to reduce its spending precisely when the economy needs the stimulating effect of a Government deficit and when provision for national security demands increasing defense outlays. To avoid these undesirable consequences, the debt limit should be raised by an amount that would allow not only for ordinary seasonal variation in receipts the coming year, but also for the possibility that expenditures for the entire year will substantially exceed receipts. In our view, the $5 billion temporary increase already enacted is too small, in view of the uncertainties on both the receipts and expenditures sides of the budget, even on the assumption that the recession will be moderate in extent and duration.

3. *Planning stronger action.*—Additional measures to be used if the recession deepens should be readied and agreed upon now. This is necessary so that action may be taken quickly if it is needed. It will also provide a solid basis for confidence on the part of the businessmen, investors, and consumers that there will be no deep depression. Hence, it will prevent fear and uncertainty from holding up investment and consumer spending, and make it more likely that recovery will be achieved by natural forces assisted by the measures suggested above.

CONDITIONS WARRANTING STRONGER ACTION

It would be unwise to set up a single rigid "signal" for strong antirecession action, but we believe such action would be appropriate if the economic decline passes the low points reached in 1949 and 1954.

Comparison of the present position with earlier experience may be illustrated by the unemployment data. In the 1949 recession, which began at the very end of 1948, seasonally adjusted unemployment exceeded 6 percent of the civilian

[6] In its 1954 statement, Defense Against Recession: Policy for Greater Economic Stability, the research and policy committee recommended that the States should raise their maximum unemployment-compensation benefits, raise the maximum duration of benefits where that is below 26 weeks, and extend the coverage of their unemployment-compensation systems. The committee also recommended that provision be made for Federal loans to States that are in danger of exhausting their reserves. The current recession emphasizes the importance of strengthening the unemployment-compensation system.

labor force continuously from July 1949 through March 1950, and rose above 7 percent in 1 month, October 1949. In the slightly milder 1954 recession, which began about August 1953, seasonally adjusted unemployment exceeded 5 percent of the civilian labor force from February through November 1954, and rose above 6 percent in 2 months, August and September. In the present recession, the seasonally adjusted unemployment rate reached 5 percent of the civilian labor force in December 1957, and in February 1958 had climbed to 6.7 percent.[7]

Changes in production, incomes, and employment indicate that by February we had experienced about as large a decline from the previous peak as occurred in 1949 and 1954. If the economic situation becomes clearly worse than in the earlier postwar recessions, strong action should be taken. We suggest that this would be the case if, after allowance for seasonal influences, business activity continues to contract for another 2 months, after February, unless there is unmistakable evidence of quickly forthcoming improvement.

If this happens, seasonally adjusted unemployment would probably stand at about 5 million. However, the burden of decision as to whether and when additional measures should be adopted should not be placed entirely upon the unemployment statistics. We use this measure to represent the entire economic situation with respect to employment, production, and incomes that would ordinarily be associated with about 5 million unemployed. If this position were reached in the spring of 1958, it would imply, for example, a decline from the August 1957 peak of nearly 2 million in seasonally adjusted employment in nonagricultural establishments. We would also stress the behavior of the gross national product, which measures the total output of goods and services, and, particularly for a month-to-month appraisal, of industrial production. The situation envisaged would imply a drop in the seasonally adjusted annual rate of gross national product of perhaps $20 billion from the third-quarter 1957 peak. Either an error in the unemployment estimate or some unusual development in entrances into or departures from the labor force could conceivably cause the unemployment figure to become unrepresentative of the entire economic situation, so these other measures must also be considered.

Thus far, the main comprehensive indicators of economic activity have yielded a broadly consistent picture of developments. They indicate that we are now close to the low points reached in 1949 and 1954. Hence, should the marked declines in seasonally adjusted production and employment, and the rise in seasonally adjusted unemployment, that have been underway, continue in the spring months, the conditions calling for strong action would be met.

Any significant decline in total consumer spending for nondurable goods and services, accompanying a pronounced drop in disposable personal income, would also suggest the need for strong counteraction, since, as indicated earlier, it would suggest the beginning of a downward spiral of income and spending generally that, if unchecked, could cause the decline to snowball.

WHAT SHOULD BE DONE IF THE RECESSION DEEPENS

Circumstances described in the previous section would call for an economic policy that has a good probability of stopping the business decline and turning activity upward; half measures that merely slow the downward movement would not then meet our national objective. Subject to this criterion, we should also continue to use measures that do not interfere with adjustments in resource allocation, relative prices, and costs through normal competitive processes, and that are quickly reversible. The latter criterion, however, may be interpreted somewhat more loosely, since we shall be starting with more idle resources and less immediate danger of reviving inflationary pressures.

RESCHEDULING GOVERNMENT EXPENDITURES

As we indicated at the beginning of this statement, our main reliance for Government help should be upon tax reduction. However, the expenditure side of the Federal budget can make a valuable contribution to recovery.

Under conditions calling for strong Federal action, the Federal Government should make every effort to accelerate necessary procurement and public works, but only when the major impact upon the economy of so doing will be felt

[7] Statements in this paragraph are based upon revisions of previously published Census Bureau data to bring them into conformity with the present census definition of unemployment.

within a year or so. This allows more scope for rescheduling than the narrower program we have suggested for the present situation, but is, nonetheless, a severe restriction. If it is not met, procurement and public-works acceleration will not only be ineffective in helping to check recession, but may later add to inflationary problems.

The increase of expenditures in order to fight recession can easily become wasteful unless discrimination is exercised. While a speedup of expenditures that would otherwise have to be made later is warranted, embarking upon unnecessary projects is both extravagant at the time and likely to lead to a continuing scale of Government expenditures larger than would be adopted were programs considered strictly on their merits. Acceleration of contract terms so much that costs are increased by overtime work at time-and-one-half or double time, or by wasteful production and buying practices, is also to be avoided. The Government should obtain more, not less, for its dollars in periods of slack business.

The size and character of the defense program should be determined solely by considerations of national security. It would not violate this principle, however, for procurement scheduled for a year or two ahead to be rescheduled to support incomes and employment when such support is needed. The danger of obsolescence and the long lead times required for many items limit the extent to which this can be done, but some significant support to the economy should be possible. Continued procurement of items that are no longer needed, merely because this is the easiest way to place contracts and obtain production quickly, must be guarded against.

Acceleration of activity on public works projects already underway, and moving up necessary new projects that have already been authorized, have had the necessary preliminary work completed, and are of short duration, should also be pressed. To consider the role of Federal public works expenditures, it is useful to have certain magnitudes in mind.

Federal expenditures for public works in fiscal year 1959 are estimated in the budget to include $3.8 billion for Federal construction ($2.3 billion for major national security public works and $1.5 billion for other projects) and $2.8 billion in grants and loans to State and local governments, a total of $6.7 billion.

Although as of June 30, 1958, there will be a reserve of authorized work on civil construction projects to be started after 1958 having an estimated total cost of $12.4 billion, only $1.6 billion of these projects will have been planned to the stage where a contract could be let. The bulk—$1.3 billion—of the projects on which planning has been completed consists of river-basin programs of the Corps of Engineers and the Bureau of Reclamation, and of TVA projects. Evidently, little of the $1.6 billion consists of projects on which expenditures would not be spread over several or many years. There is little point to moving up projects unless the work will be done mainly within a year or so of the date that it is decided that vigorous antirecession action is needed.

The roads program, which accounts for nearly all the grants and loans to State and local governments, is already being pressed. Even a sizable percentage stepup in Federal construction now scheduled for fiscal 1959 would not amount to a great sum; a 15-percent increase, for example, would amount to about $0.6 billion. New projects offering a suitable time schedule are apparently small. In all, it appears that rescheduling of public works projects can of themselves make only a limited contribution to quick reversal of a downward trend of the gross national product.

Acceleration of procurement and public works, together, can and should play a supporting role in bringing about recovery. State and local governments, by accelerating their programs in the manner suggested here for the Federal Government, could also make a contribution. But increases in Government expenditures should not be our chief reliance.

A large temporary tax cut

The major emphasis should be upon temporary and substantial reduction in Federal income taxes to raise private incomes and hence to increase consumer spending and business investment. The tax cut should have three principal characteristics:

1. The purpose of the tax cut is to help lift us out of a recession, not to change the burden of taxation or to reform the tax structure. Consequently, it should be neutral with respect to the distribution of the tax burden. A flat percentage reduction in the income-tax bills of individuals applied to the

amounts computed under existing law would meet this criterion sufficiently well.[8] Such a tax reduction would provide a quick spur to consumption expenditures. It should also help to restore opportunities for profitable investments, mainly by the improvement of business sales though also by directly increasing net yields to individual investors.

2. If the conditions we have assumed appear, the tax cut should be prompt. It should also be put into effect for a limited time only, with automatic provision for a return to the previous rates. This is essential to permit enough tax reduction to stimulate recovery and yet not run a pronounced risk of inflation in the ensuing business advance.

3. The size of the tax cut must be commensurate with the size of the problem. If the situation we describe should develop within the next few months, the real gross national product would have fallen something like 4½ percent from its previous peak. Over the intervening period estimated normal growth at a rate of 3 percent a year would have increased the productive capacity of the economy by more than 2 percent. Our gross national product, consequently, would probably be nearly 7 percent below a high-employment level. This amounts to an annual rate of about $30 billion in gross national product.

We suggest the tax cut should aim to provide a stimulus that would provide the basis for quickly eliminating the larger part of the gap between actual and potential production. The immediate effects would be mainly to raise private consumption and, as a result of the strengthening of business sales, to check inventory liquidation. Some additional stimulus would be provided by the temporarily higher rate of Federal purchases we urge above. Together, the effects of these actions should strengthen investment generally, and impart an upward impetus to the economy that would set us on the road back to high employment.

Although a precise calculation is impossible, we believe that this objective requires a personal income tax cut at a yearly rate of about $7½ billion, when yields are computed on the basis of income levels consistent with high employment and stable prices. Present personal income tax rates would yield about $38 billion a year under conditions of high employment and price stability, so this would mean a cut of one-fifth in these taxes. A much larger reduction would carry too great a risk of inflation; one much smaller would have an insufficiently high probability of success.[9]

The actual cost to the Treasury of such a temporary tax cut should be less than $7½ billion. First, because the actual income base to which it was applied would be below the high employment level; under the assumed conditions the tax loss initially would be at an annual rate of about $7 billion. Second, because we would expect the reduction to be in effect, at least in full, for less than a year. Third, because, under conditions of substantial unemployment, the stimulus of the tax reduction should raise the tax base well above what it would be in its absence—without the corresponding increase in Government costs resulting from inflation that would ensue from a similar policy under high-employment conditions.

We recommend that, if such a temporary tax cut becomes necessary, its original enactment should be for a period ending March 31, 1959. Tax withholdings, which account for the bulk of individual income tax collections, would be immediately reduced by one-fifth. Individuals making tax payments on current-year incomes would recompute their liabilities, and adjust their current payments. The tax liability on the final returns for the year would be computed in the usual fashion, but with the addition of a line for the "emergency antirecession tax reduction." This would be equal to the ordinary tax liability multiplied by one-fifth the fraction of the year for which the reduction was in

[8] We recognize that complete neutrality would call for a similar reduction in excise tax and corporate income tax rates. Moreover, we believe that in the long-run reform of the Federal tax structure these taxes should be reduced. However, we concentrate our recommendation on the individual income tax because this raises the least technical complications and disagreements that might impede quick action. Also we believe the reduction of the individual income tax to be the most important and useful step from the standpoint of promoting recovery.

[9] If the circumstances postulated actually develop, it will probably be because the combined decline in private domestic fixed investment in construction and producers durable equipment, together with the decline in net foreign investment, is large—probably heading, if not checked by Government action, toward a figure below the 1957 quarterly peak by an amount in the range of $10 billion, at annual rates, by the last quarter of 1958. This consideration has influenced us in concluding that, if a tax cut becomes necessary, it should be large.

effect. If, for example, the reduction were effective on July 1, 1958, and ended on March 31, 1959, the deduction on calendar-year returns for 1958 would be equal to 10 percent of the originally computed liability, and for 1959 to 5 percent.[10]

Shortly after Congress convenes in 1959, the President, on the basis of economic developments to that time, would recommend whether the tax reduction would be permitted to expire, be continued at a reduced rate for another limited period, or be continued in full for another limited period. If recovery were proceeding very well, the President might also recommend earlier termination, before March 31. A March 31 termination date would give Congress ample time to act if extension were necessary. If by then Congress has been able, consistent with long-run budget requirements, to enact any permanent tax reforms, the timing of these reforms could be adapted to the expiration date of the temporary tax cut.

To meet the objective of high employment without inflation—and to justify the use of taxation in any similar future situation—it is essential that the temporary tax cut be pared or eliminated as quickly as the recovery of the economy warrants.

If this more vigorous action becomes necessary and is taken boldly, there is reason for confidence that tax reduction on the scale we have recommended, supported by rescheduling of Federal expenditures and expansionary monetary policy, will succeed in turning the economy upward. Given the necessary determination, it should also be feasible to reverse action quickly enough to prevent the stage from being set for another round of inflation.

The performance of the American economy must depend in the final instance on the responsiveness of the private economy. As we have pointed out here, Government has a major responsibility toward the economy, in good times and in bad. But the role of Government is a limiting and conditioning role. Government's action can restrain expansion in boom times. In recession, Government can make available to the economy the means to expand. It is an important aspect of governmental action that the restraint, or the expansionary forces, it sets off apply very broadly throughout the economy, establishing general conditions from which individuals and businesses can take their cue. This general conditioning is what Government can do, and the private economy cannot do, if the private economy is to remain free and competitive.

But it is up to the private economy—businesses big and little, and consumers—to react responsibly to the limiting and conditioning policies of Government. Government can make credit less expensive and more easily available; enrich the economy's spending power by reducing taxation, if that becomes necessary; and initiate and speed up spending that is within the proper functions of Government. These actions and policies, however, cannot in themselves cure recession. The recession is only cured when the private economy is operating on a scale that makes employment and income high.

We have outlined here policies that will, in our judgment, establish the conditions in which our economic growth can be resumed. They can do no more than that. The private economy must do the rest.

RESEARCH ADVISORY BOARD

Theodore W. Schultz, chairman; professor of economics, University of Chicago
Arthur Smithies, vice chairman; department of economics, Harvard University
Richard M. Bissell, Jr., Central Intelligence Agency
Howard R. Bowen, president, Grinnell College
Douglass V. Brown, professor of industrial management, department of business and engineering administration, Massachusetts Institute of Technology
Robert D. B. Calkins, president, Brookings Institution
Solomon Fabricant, director of research, National Bureau of Economic Research, Inc.
Don K. Price, vice president, the Ford Foundation

---

[10] We have not referred to the possibility that Congress may not be in session when institution of a tax reduction becomes appropriate. This does not seem to us a real obstacle to the program, since it could be remedied either by temporary adjurnment of Congress or by agreement with the President that a special session would be called if necessary. Economic stability is, after all, second in urgency only to defense as a national problem this year.

Ralph W. Tyler, director, Center for Advanced Study in the Behavioral Sciences, Stanford, Calif.
Henry Wallich, department of economics, Yale University
W. Allen Wallis, dean, school of business, University of Chicago

RESEARCH STAFF

Research director: Herbert Stein
Secretary, research and policy committee: Robert F. Lenhart
Edward F. Denison
David Fand
Gardiner C. Means
Frank O'Brien
Addison Parris
Joseph A. Pechman

TRUSTEES OF THE COMMITTEE FOR ECONOMIC DEVELOPMENT

*Member of Research and Policy Committee.

George H. Coppers, president, National Biscuit Co.
H. H. Corey, chairman of the board, Geo. A. Hormel & Co.
Charles R. Cox, president, Kennecott Copper Co.
Charles E. Daniel, chairman, Daniel Construction Co.
Paul L. Davies, chairman of the board, Food Machinery & Chemical Corp.
*Nathanael V. Davis, president, Aluminium, Ltd., Inc.
Donald C. Dayton, president, Dayton's
William C. Decker, president, Corning Glass Works
John S. Dickey, president, Dartmouth College
George S. Dinwiddie, president, New Orleans Public Service, Inc.
Robert W. Dowling, president, City Investing Co.
Morris Edwards, vice president, Thomas E. Wood, Inc.
Fred J. Emmerich, Allied Chemical & Dye Corp.
Charles T. Fisher, Jr., president, National Bank of Detroit.
*Edmund Fitzgerald, president, the Northwestern Mutual Life Insurance Co.
Jewett T. Flagg, president, Flagg-Utica Corp.
Lamar Fleming, Jr., chairman of the board, Anderson, Clayton & Co.
Percival E. Foerderer, Philadelphia, Pa.
*William C. Foster, executive vice president, Olin Mathieson Chemical Corp.
John M. Fox, president, Minute Maid Corp.
Fred C. Foy, president, Koppers Co., Inc.
Alfred C. Fuller, chairman of the board, the Fuller Brush Co.
Walter D. Fuller, the Curtis Publishing Co.
Clark R. Gamble, president, Brown Shoe Co.
Arthur S. Genet, president, the Greyhound Corp.
Paul S. Gerot, president, Pillsbury Mills, Inc.
*Philip L. Graham, president and publisher, the Washington Post and Times Herald
H. J. Heinz II, president, H. J. Heinz Co.
*Robert Heller, president, Robert Heller & Associates, Inc.
J. V. Herd, chairman and president, America Fore Insurance Group
William A. Hewitt, president, Deere & Co.
Oveta Culp Hobby, president, the Houston Post
Paul G. Hoffman, Pasadena, Calif.
*T. V. Houser, chairman of the board, Sears, Roebuck & Co.
J. C. Hullett, president, Hartford Fire Insurance Co.
G. W. Humphrey, vice president, the M. A. Hanna Co.
Eric Johnston, president, Motion Picture Association of America, Inc.
Henry R. Johnston, New York, N. Y.
Ernest Kanzler, vice chairman of the board, Universal C. I. T. Credit Corp.
*Meyer Kestnbaum, president, Hart Schaffner & Marx
Robert J. Kleberg, Jr., president, King Ranch
Sigurd S. Larmon, president, Young & Rubicam, Inc.
Roy E. Larsen, president, Time, Inc.
*Fred Lazarus, Jr., chairman of the board, Federated Department Stores, Inc.
*Ralph Lazarus, president, Federated Department Stores, Inc.
Elmer L. Lindseth, president, the Cleveland Electric Illuminating Co.
Homer J. Livingston, president, the First National Bank of Chicago
George H. Love, chairman of the board, Pittsburgh Consolidation Coal Co.
J. Spencer Love, chairman of the board, Burlington Industries, Inc.
Franklin J. Lunding, chairman of the board, Jewel Tea Co., Inc.
L. F. McCollum, president, Continental Oil Co.
George C. McGhee, McGhee Production Co.
Ralph McGill, editor, the Atlanta Constitution
Stanley Marcus, president, Neiman-Marcus Co.
J. A. Martino, president, National Lead Co.
Fred Maytag, II, president, the Maytag Co.
*Don G. Mitchell, chairman of the board, Sylvania Electric Products, Inc.
C. G. Mortimer, president, General Foods Corp.
Malcolm Muir, president, Newsweek
*Alfred C. Neal, president, Committee for Economic Development
L. B. Neumiller, chairman of the board, Caterpillar Tractor Co.
Aksel Nielsen, president, the Title Guaranty Co.
Frank Pace, Jr., president, General Dynamics Corp.

*Member of Research and Policy Committee.

*Member of Research and Policy Committee.

ABOUT CED

The Committee for Economic Development is composed of leading businessmen and scholars who, working together, conduct research and formulate policy recommendations on major economic issues, and promote education on the operation of the American economy.

CED's objectives are to contribute to full employment, higher living standards, and increasing opportunities for all Americans, to promote economic growth and stability, and to strengthen the concepts and institutions essential to progress in a free society.

CED's bylaws emphasize that its work must be thoroughly objective in character and that each issue must be approached, not from the viewpoint of any particular economic or political group, but with regard for the general welfare.

Thus, CED unites scholarship with business judgment and experience in analyzing issues and developing recommendations to resolve the economic problems that arise constantly in a dynamic and democratic society.

CED is supported by voluntary contributions from business and industry. It is nonprofit, nonpartisan, and nonpolitical.

President: Alfred C. Neal
Secretary: Robert F. Lenhart
Research division: Herbert Stein, director
Area development division: Robert H. Ryan, director
Business-education division: Robert S. Donaldson, director
Finance division: Herbert Malley, director
Information division: Porter McKeever, director
John Crider
Karl Schriftgiesser

Senator Douglas. The discussion will be continued by Mr. Robert R. Nathan, national chairman of Americans for Democratic Action. Mr. Nathan.

STATEMENT OF ROBERT R. NATHAN, NATIONAL CHAIRMAN, AMERICANS FOR DEMOCRATIC ACTION

Mr. Nathan. Thank you, Mr. Chairman.

I would ask that the statement which I prepared and submitted be introduced in the record. I will just summarize a few points briefly.

Senator Douglas. Very well.

(The statement is as follows:)

STATEMENT OF ROBERT R. NATHAN, NATIONAL CHAIRMAN, AMERICANS FOR DEMOCRATIC ACTION

Mr. Chairman and members of the subcommittee, my name is Robert R. Nathan and I appear here as national chairman of Americans for Democratic Action. I appreciate very much the opportunity to participate in this discussion and to present ADA's views. ADA has consistently been on record in favor of action by the Government to prevent the recession from extending in severity and duration. Even before the end of 1957 we recognized signs of dislocations in the economy which if not corrected would tend to accentuate the decline. In any such situation there is the danger that the recession may feed upon itself and grow worse unless action is taken. As early as December or January it seemed likely that the economic situation did not contain the elements for correcting itself without further decline. Such a decline could have been avoided only by positive action which must come in the first instance from the Government.

At that time also we pointed out that the magnitude of the action required would increase as the recession deepened; that positive measures which might suffice in January would no longer be sufficient if the recession was allowed to deepen into May and June. This is exactly what has happened. The recession has been allowed to proceed to a point where it requires vigorous action on a rather large scale.

I should like to emphasize five points which we feel are essential to public policy for economic recovery.

(1) The administration's criterion of the need for Government action is all wrong. Action is needed in the absence of clear signs of a prompt and vigorous upturn. It is expensive folly to continue to wait to see whether or not there are signs of further deterioration—whether the recession will "bottom out" in May or June or July or later. Every month of recession costs the country billions of dollars in wasted productive capacity and manpower; prolongs the hardship on the millions of unemployed; and deepens the serious effects our recession is having on the international economy and the free world. What is absolutely essential is that recovery be as prompt and as fast as we can bring it about.

(2) Inflation cannot and must not be fought by recession or depression. It makes no sense to try to combat damaging inflation by deliberately tolerating a damaging recession. This is stupid and wasteful defeatism. No matter how or when we emerge from the recession, there will be the possibility, perhaps the threat, of inflation. Inflation must then be fought by means appropriate to the circumstances as they arise. We have at our disposal a wide range of economic policies for combating inflation, but we cannot do it by permitting resources to lie idle.

(3) This recession has now proceeded to a point where a variety of potent measures must be taken:

Certainly we need prompt and substantial increases in the amounts and duration of unemployment benefits—of the order of those proposed in the Kennedy-McCarthy bill and certainly far beyond those specified in the bill now pending in the House.

We need a substantial temporary cut in taxes. These cuts should be so designed to increase the levels of consumption which are so conspicuously lagging behind the productive capacity created by the investment boom of the past few years. The tax reductions should accrue principally to middle- and low-income consumers, through reductions in income taxes in the lower brackets and through cuts in excise taxes.

Prominent among the tax reductions we recommend a temporary suspension of the excise tax on automobiles, as a means of reducing the price of automobiles, conditioned, as a matter of policy, on action by the automobile manufacturers to make substantial reductions in their factory list prices. The automobile industry occupies a central position in this recession because of its size and because of the sharp decline in its sales. But price reductions should not be confined to automobiles. There are a number of industries, notably for example, steel, whose price structures are conspicuously out of line with today's markets and which should contribute substantially to stimulating demand by lowering prices.

(4) There is no need to wrestle over the false dilemma of choosing between public works and tax reductions as means of combating the recession. If we seriously want a quick recovery—and we must seek quick recovery—tax reductions have the advantage of being prompt and general. This should not preclude programs of essential public works which are useful in themselves and which must be carried forward under any circumstances short of total defense mobilization. The fact that both tax reductions and public-works spending will add to the immediate Federal deficit is no reason for choosing between them. A large Federal deficit arising out of the recession is inevitable. The size of the deficit should be scaled positively to the needs for a rapid return to full employment rather than resigning ourselves to an even bigger deficit through inaction and a longer period of recession.

(5) When we finally climb out of this recession and regain levels of full employment and economic growth, we will face two challenges: first, to prevent distortions which might bring on future recessions; and second, to prevent further inflation.

Preventing distortions requires that we must be on guard against overstimulated investment booms and adhere to economic policies which will keep the consumption base of the economy expanding in concert with the production base. We must particularly avoid overreliance on high interest rate and tight-money policies, of the kind we witnessed in 1955 to 1957, as a means of restraining and directing demand. Experience has shown that fiscal policies are more efficient and more equitable than monetary policies.

In preventing new inflation we should carefully study the anatomy of the 1955–58 inflation and its price distortions; we must not be blinded by the mythology of the well-heeled Madison Avenue campaign to blame the inflation entirely on wages. Administered and monopolistic pricing is truly our No. 1 inflation enemy.

Mr. Chairman, we can no longer afford inaction. What has been done up to now, both by the executive branch and by the Congress, has been much more of show than of substance. Nearly 6 months after the first signs of recession, we have yet to take the first really vigorous steps to combat it. We must now decide whether we are going to let this recession drag out its dreary course and resign ourselves to a slow and halting recovery, or whether we are going to take those steps which are necessary and would be effective. If we follow the first course we may find ourselves next winter at best in the course of a creeping recovery with several million still unemployed. If we take the second, we may be able to restore full employment within a few months. The difference will be measured in tens of billions of dollars of national income and in the suffering of millions of our citizens.

Mr. NATHAN. Mr. Chairman, I would like to state first—apologizing if it is necessary for calling this to the attention of the committee—that I believe it is important that we start out with a recognition of the fact that we have on the statute books of his counry legislation called the Employment Act of 1946, in which it is stated very clearly that it is the continuing policy and responsibility of the Federal Government to promote maximum employment, production, and purchasing power.

It seems to me, Mr. Chairman, that in line with the positive responsibility that this legislation imposes on the Congress and on the Government, there is some justification for the feeling on the part of some of the people that in a real sense the responsibilities under this legislation have not and are not being fully and effectively executed. I think it is within the framework of the provisions of that Employment Act of 1946 that we ought to orient and focus our discussion.

First, let me say with respect to the recession that I think the criterion for action has been largely wrong that positive action ought to be undertaken if the situation deteriorates materially from where it is or where it has been for the past month or two. It is our feeling that positive action ought to be undertaken short of any clear and unquestioned evidence of a speedy and prompt upturn in business activity. I think it is bad enough to resign ourselves to the present level, let alone to feel that we should not take action unless the situation deteriorates substantially from the present level. I think that our criterion for action ought to be based on whether or not there is very clear evidence of an immediate and substantial upturn in business activity.

I followed the hearings for the past 3 days, especially the Monday hearings, and it seems to me that the majority of people who testified before this committee—and I think properly—could find no overwhelming and important evidence of an immediate and major upturn in business activity which would get us away from this waste of tens of billions of dollars of production from which we are suffering, and the hardship on the individuals who are unemployed—and perhaps I should say, Mr. Chairman, most importantly, the fantastic damage being done to the American status and the status of free societies throughout the world as a result of our exporting this recession.

I am very optimistic about the long-range growth of the United States, and I think we do have prospects for a brilliant future. But I am afraid that if we resign ourselves to the "let nature take its course" philosophy, which has largely prevailed, the optimistic possibilities will not be achieved in the very near future, which is what we need.

One of the subjects for discussion today, it seems to me, is this question of inflation. I believe all of use who bear any sense of responsibility or feel any sense of responsibility for a prosperous American economy are against inflation. Certainly inflation is undesirable as an end objective, as a feature of our society. But I believe that the idea of fighting inflation by a recession is a most disturbing and negative and defeatist attitude. Yet, what seems to be the fundamental policy of those who say that we must not fight the recession and try to get out of it in a hurry by massive measures, because these measures might bring about inflation.

I think, Mr. Chairman, that we are going to be faced with a threat of inflation no matter when or how we get back to prosperity, and I believe that we must fight inflation just as we must fight recession, but we must not resign ourselves to recession as the only answer to inflation.

I do not think inflation is inevitable. I think, by the way, that our deficit financing at the present time is inevitable. We are running into deficit financing even without positive action.

As far as one other issue is concerned, there has been introduced into the whole discussion of the recession the thought that we have a choice between public works—Government spending—on the one hand, and tax reduction on the other hand. I believe, Mr. Chairman, this is an invalid set of alternatives. There are essential public works which we need under any circumstances. We are short of schools, we are short of hospitals, we are short of low-cost housing. There are many public works that are essential, and we ought to undertake them under any circumstances. But I think that we want to fight this recession in a very meaningful sense by trying to reverse the tide of economic activity promptly, and a tax cut is the only way we are going to get really speedy, prompt action and reverse this trend in a matter of weeks or a month or two, instead of 6 months, 9 months, or a year.

25780—58——13

So we are in favor of a positive program of tax reduction. Let me say that while I will yield to no one in my interest, enthusiasm, and support of the free enterprise system, I think it is utterly absurd at this stage of the game to emphasize tax cuts in terms of incentive for investment when we have idle capacity. What we need today is consumption so that American business can have a market for the goods it produces; that market will provide the maximum incentive for investment. What we need is a tax cut geared primarily to increase the buying power of the middle- and low-income groups, through reducing the rate on the first thousand dollars of taxable income.

I would agree that we should not raise the exemption but ought to keep the large coverage. I would suggest that there be a reduction of the rate, say, of the first $1,000 of taxable income from 20 percent to 10 percent, and a reduction in excise taxes.

I would also agree that the tax cut ought to be temporary, Mr. Chairman. I think that in the world situation in which we live, and with the essential needs we have in our society, it is quite likely that we will need to restore taxes a year from now or two years from now or six months from now, depending on the rate of recovery.

We also desperately need, and I think it is overdue, some improvement in our unemployment compensation in terms of duration and level of benefits. I do not see anything sacred about 26 weeks. If a man loses his job and is out of work for 26 weeks, through no fault of his own, and he cannot find a job, there is nothing sacred about cutting off his benefits at 26 weeks. The benefits ought to be extended for the period when a man cannot find a job despite desire and effort on his part.

I think the level of the benefits is too low, too. In an economy as prosperous and abundant and productive as ours, we should not allow the ratio of unemployment benefits to wage levels decline from the depression period of the midthirties to the tremendously productive economy of the midfifties.

One final point I would like to make, Mr. Chairman, is that in my judgment, the contribution of business to solving the recession through price cuts has been absolutely absent. I think that the steel industry especially, which is one which undertook an irresponsible type of pricing—inflationary and administered monopolistic pricing—raising its prices up by 26 percent from mid-1955 to mid-1957, now finds itself producing at less than 50 percent of capacity, and yet has made even no gesture at reducing prices.

I think that the profits of United States Steel, which will be announced this week, will reveal very sizable profits, at the level of 50 or 60 percent of capacity. Profits will not be what they were in 1957; but their contention that their break-even point was 70 percent is obviously going to be exploded. I think the steel industry, the automobile industry, and some of the others ought to reduce prices.

Just one final point, Mr. Chairman. I would like to say that as we get out of this recession, it would be my hope that we will concentrate our efforts then toward two ultimate objectives: one, how we can achieve and sustain our high levels of production and prosperity without the distortions that cause another recession; and secondly, how we can maintain our prosperity with reasonable price stabilization and without inflation.

But we cannot fight inflation by myths and hoaxes that the entire inflation of 1955–57 was due to wage increases alone, and that somehow labor is the dog in the manger for everything that has happened, when in large measure that is not true. I think we ought to be objective and intelligently seek to arrive at solutions to the problems of sustaining high levels of production and employment with price stability.

Thank you.

Senator DOUGLAS. Thank you very much, Mr. Nathan.

The discussion will be continued by Mr. John A. Baker, director of the legislative services division of the National Farmers Union, who is appearing, as I understand it, for Mr. James G. Patton, president of the National Farmers Union.

STATEMENT OF JOHN A. BAKER, DIRECTOR, LEGISLATIVE SERVICES DIVISION, NATIONAL FARMERS UNION

Mr. BAKER. Mr. Patton regrets he was unable to be here this morning, Mr. Chairman.

I would like to preface our statement by commending the work that the Joint Economic Committee has done in the 11 years since it was established. The hearings that you have planned, and these that you are holding now, are a continuation of the fine work you have done.

As you pointed out, I am honored this morning to read this statement for Mr. Patton to your subcommittee.

For over 5 years our national economy has been held back to a rate of economic growth well below our needs and far below our potentialities. Now our growth has been brought to a halt. Not only are we not progressing, we are actually going backward.

This development was not a blind accident of fate. It was planned that way. The current recession is an inevitable result of the totality of national economic policies followed by the executive branch of the Federal Government for the past 5 years. Those policies were designed to make the rich richer, to make stronger the economically already strong, and to reduce, eliminate, and whittle down the protections in our system for the economically weak.

The result has been that plant capacity owned by great concentrations of wealth and economic power expanded at a greater rate than consumers' expenditures were allowed to expand. In this situation, boards of directors of large corporations found that their most profitable rate of production would be considerably less than full capacity. Having the power to do so, they cut output, laid off workers, and idled the machine down to a recession level.

The dramatic example, of course, is that of the steel industry. With full knowledge of the implications of their decisions, steel management deliberately decided to raise the price of steel and cut output by half. This cut orders from suppliers by half. And it increased the cost prices for farmers and all other producers and consumers who must use products made of steel. At each step in the steel marketing chain, the increase in the price of steel was passed on, and a markup was added by every entreprenuer who operated under conditions monopolistic enough to protect himself from competition.

Let us reflect for a moment on the probable results of similar action on the part of farmers. If farmers had cut the 1957–58 supply of food by half, as steel has done, there would have been riots in Brooklyn long before now. And in Chicago and all over the Nation. Of course, it would be unthinkable to cut the food supply in half. Yet here we sit, more or less complacent, and quietly debate the proposition of steel operating at less than half of capacity as if it were an academic question.

What has been true in steel has been true to lesser degrees in other monopolistic industries. Administered price inflation and rising costs of production and cost of living have accompanied rising unemployment and a grinding to a halt of our national economic growth.

This situation was not brought on alone by faulty fiscal policies and it cannot be cured by changes in fiscal policy alone. However, there are changes and improvements in fiscal policy that can and should be made. Making them will help lift our economy out of the current slump.

Recognizing that changes in fiscal policy are not the only antirecession steps that should be taken, I submit for your consideration the following fiscal policy reforms:

1. Repeal of all excise taxes, except on alcohol.

2. Raise the personal income tax exemption by the degree required to make up the deflationary gap.

Close all personal and corporate income tax loopholes such as the depletion allowances, proprietary corporate dividend credits, and propaganda contribution deductions.

4. Tax capital gains at as high or higher rate than regular income.

5. Base Federal Government expenditure policies on justified need for national priority goals, such as unemployment compensation; school construction; teachers' salaries; airport modernization; highway construction; other public works; community facilities; resources and power development and conservation; hospital facilities; medical, nursing, and dental education; college scholarships; urban redevelopment and modernization; more nearly adequate pay for Federal employees; inauguration of a significant program of expanding economic opportunities in chronically depressed urban and rural areas; housing; expanded research; and national defense.

6. We should either greatly expand United States efforts to assist the economic expansion of the free world, which is much to be preferred, or else we should greatly expand domestic expenditures for vast projects of civilian defense against nuclear bombing.

In closing, let me say this: The current depression is not a new development for farmers. Our prices and income started down 7 years ago. The price parity ratio fell below 100 in 1953, and has not been above 90 percent since that time. Current predictions are that farm prices will drift downward for the remainder of 1958. As many Members of Congress have stated, "The farm depression has come to town."

We in Farmers Union have been urging that the downward trend in farm policy be reversed. We have pointed out that this wrong farm policy was part and parcel of wrong general economic policy. In the main, a majority of the Congress have agreed with us, and have tried to protect and improve the bargaining power of the weaker segments of our economy—education, farmers, Government service, labor, and small business.

I, therefore, again urge that improved farm-income protection programs be enacted as part of a broad general antirecession program of many phases. I hope that Congress will override the veto of Senate Joint Resolution 162, which would have been a start toward preventing further farm-income declines. Moreover, I urge the enactment of a comprehensive system of farm commodity income improvement programs that will enable farmers to earn and receive a parity of income in an expanding national economy. Such a program can be developed and operated upon the general outlines of the findings and recommendations published early this year by the Farm Policy Subcommittee of the Joint Economic Committee.

Senator DOUGLAS. Thank you very much, Mr. Baker.

Mr. BAKER. As a member of this subcommittee, I was a signer, and the chairman was a member of this committee.

Senator DOUGLAS. The first round of discussion will be concluded by Mr. George J. Burger, vice president, legislative activities, National Federation of Independent Business.

Mr. Burger.

STATEMENT OF GEORGE J. BURGER, VICE PRESIDENT, NATIONAL FEDERATION OF INDEPENDENT BUSINESS

Mr. BURGER. I am George J. Burger, vice president, legislative activities, National Federation of Independent Business.

We are the largest business organization in the Nation, from the standpoint of directly supporting business and professional people. Our membership is exclusively among small, independent enterprisers. These people, who are your constituents, and they alone, set our stand on bills and issues by direct, signed votes which they sent to their congressional representatives on the House side, in our mandate polls. I mention this only to emphasize the fact that what I say here reflects their collective thinking, just as though they were here to speak for themselves.

Naturally, they are concerned about their welfare. But I would make it clear that their concern centers exclusively around the achieving or broadening of the climate of free and fair opportunities. Let them have that, and they will do the rest themselves. And let me point out that this concern of theirs is not entirely selfish—for the facts show that what affects them clearly affects the entire national welfare.

Let me illustrate.

First, we've been hearing a lot about unemployment. Well, according to a recent staff report of the Federal Reserve Board, approximately 60 percent of all wage earners in the United States are employed by what might be termed small firms.

More than this; we've been hearing a lot about business activity. Well, according to Senate Small Business Committee's 1954 Annual Report, small firms accounted for about 70 percent of all sales made in the retail, wholesale, and service trades.

Expanding on the foregoing a bit, this same Senate Small Business Committee report makes the following pointed observations:

The small establishment is an extremely important outlet for the distribution of goods that are coming in increasing volume from the growing productive capacity of mines, factories, and farms. Without these small distributive units it is quite unlikely that sales volume would approach what it is today. These outlets have untold importance, not only to our national economic health, but to the producers whose goods are so distributed.

Moreover, from the standpoint of national purchasing power, the employment and income provided by small distributive establishments are of utmost significance. It is highly important that the efforts of these establishments to operate profitably and to increase efficiency be facilitated.

The same can be said of small manufacturers in their own fields, too.

This is entirely aside from the factor of competition which small business injects and keeps alive in many industries—from the factor of introduction of new products and processes many small firms account for—from the factor of property ownership they represent, which is one of the pillars of our very system of liberties.

Now, we've all been hearing a lot about the situation in small business today. Frankly, unlike Chicken Little, we're not going to say the sky has fallen. Nothing could be further from what we hear from the thousands of independents we contact daily. But we will say that something more than a pea has struck the heads of independent firms. Slowing sales are engendering sharper and, many times, unethical competition, which is putting a squeeze on profits at a time when overhead due to taxes, wages, and other costs, including the costs of goods they buy, is holding fast.

Of course, most independents would be the first to admit that much of the total needed correction can come only by and through themselves—by digging down to the sound bedrock of more efficient operations (the tremendous call we get for Small Business Administration management aids, in response to offers made in our mandate, proves this), and by the use of smarter and harder selling. But some of it must come from the Congress itself, by your own action on factors which you alone control, and which do have a material bearing on small-business opportunities.

What can you do? Well, there's need for tax relief to permit independents to retain more of the profits they earn, for expansions and modernizations, rainy-day reserves to help tide them over depressed periods—for some elimination of tax inequities which favor giant competitors at their expense—for stronger antitrust laws, and, particularly, stronger antitrust enforcement to assure them freer and fairer chances to earn a dollar—a stronger means for supplementing financing assistance available from private banks—for reduction in Federal paperwork burdens, to ease overhead pressures—for curtailment of Government competition to expand their sales areas—for continuing work to keep channels open to Government contracts.

But I'm not telling you anything. These are the very things which your parties, after long and serious study, promised to independent business in their 1956 platforms. I don't have to remind you that these pledges rang like sweet music in the ears of independents, the very ones who should know best the type of prescription needed for their ills. I don't have to remind you that your own Senate Small

Business Committee hailed these pledges as the strongest and soundest programs yet devised to promote small-business welfare. I can tell you that each and every time we have polled our members on these things, we have received overwhelmingly favorable response.

Unfortunately, the first 18 months of the current Congress have been more sound and fury than constructive accomplishment about moves toward sound small-business programs.

To date, the only steps (important as they are) have been those for some limited strengthening of Small Business Administration loan programs.

Now, I don't mean these 18 months have been a do-nothing period, for during them the administration has moved to ease the financing squeeze on independents who worked on Government contracts by permitting advance payments; its antitrust arms have scored a 20-percent increase in cases aimed to promote fair competition, and have brought the highest rate of antimonopoly merger actions ever; its Small Business Administration operations have improved to the extent of a 30-percent increase in the volume of loans to independents—more than this, congressional committees have blocked some proposed expansions in Government competition, by skillful investigation have prodded antitrusters into greater activities aimed to clear markets of monopoly roadblocks—and the Congress itself has gone halfway, or just about halfway, on measures to further strengthen the antitrust laws, to cut through redtape on small-firm stock offerings to $500,000 value, and to make the Government lending agency—which is also the agency that specialized in helping independents to secure Government orders—a permanent agency.

But I do mean that all signs show that Congress must roll up its sleeves and get to work, to finish up these projects before it closes down in July. More than this, it must go to bat on the most important tax-reduction measures now pending before its committees and hammer out the homers that will bring the 1956 platform pledges into the winning column by the time you go home.

Let me tell you that we keep our ears to the ground along the main streets of America. We're hearing definite rumbles from independent business and professional people. We can tell you that they are demanding that Congress stop dragging its heels on small-business programs, putting them off to the last minute as usual, when there's little time for them to get the attention they deserve.

"Talk about the need for greater employment; talk about the need to get the wheels of industry turning faster; well, what is Congress doing to clear the roadblocks in the path of independent business which plays such an important role on both of these?" These are samples of the questions being asked our representatives every day as they visit independent business and professional people the Nation over.

And this sentiment is reflected in the attached copy of an open letter to Members of Congress, which we published in the February 19, 1958, issue of Roll Call, and a copy of which was sent to every Member of Congress and all officials in the executive branch of Government. We urge you to study closely every line of this message.

Finally, you cast your bread upon the waters and small business will return to you, and the Nation, tenfold. All that independents want is a fair chance; they'll do the rest. Your action now on these

1956 platform pledges will help supply them this opportunity—and the benefits the Nation will reap, in more secure personal liberties, in more stable employment through greater distribution of the product of farm and factory, and in expanded purchasing power that accompanies all of this, will truly be tremendous.

Thank you, Mr. Chairman.

Senator DOUGLAS. Thank you.

(The open letter to Members of Congress follows:)

[Roll Call—the newspaper of Capitol Hill, February 19, 1958]

AN OPEN LETTER TO MEMBERS OF CONGRESS

You were home during the recent congressional recess. You heard directly what is foremost in the minds of your constituents. Your small-business friends are in trouble. Many of them are having to close their doors. Unemployment is growing. You know that small business hasn't been given the consideration by Congress that it rightfully deserves. If present trend continues there will be many questions asked this fall that will be hard to explain away. There is a solution to many of these problems and, bear in mind, without Congress having to run to the money till for any sizable amounts.

LET'S PUT FIRST THINGS FIRST

You found the health of American free enterprise first and foremost in their minds. Full employment demands it. After all, 7 out of 10 jobs in retailing, wholesaling, and service industries are in small, independent firms. Strength against communism demands it. Many in Government forever talk about dealing from strength. What greater strength to deal from for America, for the entire free world, than a strong independent business and economic system.

ACT NOW BEFORE YOU'RE BOGGED DOWN

It's understood the internationalists, free traders, socialist schemers now swarm around you like flies in Maytime. Take time to listen to them now, you'll be tied up through summer. They'll wait. They can afford to; after all, they want billions from you. Small business wants no handouts. In addition, much groundwork is already done. Small business only asks action from you now. Get it over in a couple of weeks, and then, if you like, you can take the rest of the season to listen to the high-level moochers.

NOT MORE SURVEYS BUT ACTION NOW

Don't let any group or groups sidetrack you by advising still further studies. Who would throw another shovelful of dirt on Mount Everest? And who would throw another report on the mass of data and testimony you have already taken showing the urgency of these measures? You now have studied enough facts. In addition, in your own files, personally signed by your business constituents, are the mandate ballots of the National Federation of Independent Business giving their sentiments.

ARE WE DOING AS ROME DID?

Ancient Rome's Senate contained men whose intellect and integrity are legendary even today. Yet because they concentrated all attention on foreign matters, they failed to keep Rome economically strong. And when the chips were down, free bread and circuses had failed to provide the citizens the spiritual strength to stem the barbarians from the north. Mighty legions, while most necessary, are not by themselves sufficient to guard against the 20th century savages of northern steppes.

WHO LAUGHS AT MEIN KAMPF NOW?

Once it was thought very funny that a madman named Hitler wrote down his plan of conquest. But after more than 20 million violent deaths, who laughs now? Neither should the published blueprints of communism be considered comical. Lenin wrote the greatest obstacle to American communism is the great number of independent enterprises. Karl Marx wrote that eventually the American system could be influenced to bankrupt itself into destruction. These are not the ravings of imbeciles.

RUSSIA IS WINNING THE STRUGGLE

Without firing a shot, Russia is winning. Face the facts. They are cunning. They look to the day when the American economy is concentrated in the hands of a few. Before communism there must be monopoly to sap individuals of hope, of opportunity. Remember the 1940 lesson of France. Discouragement at home is the prelude to defeat from without. Two blood baths in this century taught West Germany the necessity of antitrust laws. No nation with antitrust laws has succumbed to communism.

YOU CAN'T MAKE A GIFT OF EQUITY

You will be assailed by those who would have you believe that just tax relief measures for small business is favoritism. Yet many of these false prophets pleaded with you for relatively unknown, if not actually hidden, tax advantages for huge corporations in the form of fast writeoffs, other benefits, on the grounds such measures were necessary for expansion. Is it sound to only water the big trees to bear more fruit and let the young growing trees die of drought?

PROPAGANDA WINDS SCATTER FACTS

You in Congress may well have remarked at this session's opening "This is where I came in," for in recent years every session has been presented with a shiny new crisis accompanied by pleas for more billions for more bureaucracy. This course, it is claimed, is the will of the people. But the people can speak for themselves, and are doing so in the voted mandate ballots which they are sending to you, which are signed by the responsible, thinking people you know personally back home.

SMALL BUSINESS ASKS FOR NO DOLE

It costs little, or no money, to strengthen small business. For just a fraction of the money poured out into global boondoggling, small business can have the tax and other relief needed to expand. This expansion in turn will produce even more tax revenues in years ahead, eliminating constant need to increase the national debt limit. For literally peanuts now, you can avoid killing the goose that lays the golden eggs. And you can also look forward to bigger golden eggs in the future.

ACT NOW ON VITAL DOMESTIC ISSUES

Before becoming too occupied with matters of less importance, act on these vital issues now. The promotion of foreign gifts and bureaucracy will be with you, yea verily, until the end of your days. When home you found your constituents demanding action on small business problems and Government economy. What they want to know is this: are you going to take quick action to safeguard American independent business and the present and future jobs of this Nation? It is a temper of the times that party regularity will not serve as an excuse for failure.

C. W. Harder,
President, National Federation of Independent Business.

HERE'S HOW THE BOX SCORE STANDS ON SMALL-BUSINESS MEASURES

MEASURES ON THIRD BASE

1. Act making Small Business Administration permanent. Passed by House 392–2. Needs Senate action.
2. Act slashing redtape in small business stock offerings up to $500,000. Passed by Senate. Needs House action.

MEASURES ON SECOND BASE

1. Action strengthening Government's arm in blocking monopoly producing mergers. Has passed House committee. Needs final action on floor of House and Senate.

MEASURES ON FIRST BASE

1. Acts defining "good faith" interpretations of antitrust laws to protect small business against ruinous price cutting. Has gone through Senate hearings. Needs action on floor of Senate and House. House, in earlier Congress, voted overwhelmingly in favor.

MEASURES NEEDING TO GO TO BAT

1. Correct labor laws that are designed only to meet production requirements of large manufacturers, but under which small producers cannot operate efficiently, or compete effectively in the market place.
2. Reduce corporation taxes on first $25,000 of taxable income.
3. Reduce costly reporting burden by reducing number of withholding and social security forms businessmen must file.
4. Permit fast tax writeoffs on purchases of used property to $50,000 value per year.
5. Permit installment payments of estate taxes.
6. Permit corporations choice of paying taxes at lower partnership rates.

(NOTE.—There are other important small business bills that demand your attention and action now—but these are the basic measures).

Senator DOUGLAS. Senator Hoblitzell.

Senator HOBLITZELL. Sir, do you want me to ask questions?

Senator DOUGLAS. If you care to.

Senator HOBLITZELL. I did not get the gentleman's name from the Farmers' Union.

Mr. BAKER. Baker.

Senator HOBLITZELL. Mr. Baker, earlier in your item 4 you said:

Tax capital gains at as high or higher rate than regular income.

You feel they should be increased?

Mr. BAKER. To put capital gains of corporations on the same schedule as corporate profits and capital gains to individuals to be on the same tax rate schedule as personal income.

Senator HOBLITZELL. We operate on an incentive system, and we want people to take the risk, and this is true in small business. It is a problem to get capital invested in small business. You would be discouraging that by increasing the capital gains tax rate.

Mr. BAKER. No, sir. We would be handling the problem you mention by a progressive tax rate on the business so that the small business you are worried about would pay a lower rate than the 52 percent in existing law.

Senator HOBLITZELL. If someone comes to me as an investor and wants me to invest in something, and perhaps it is hazardous, yet it might have a potential of creating a lot more employment, if I cannot see that I can get some return on that investment, I am apt not to make the investment. If I take that risk and keep the gains on it I am more apt to make the investment.

That is the incentive I am given in terms of 3 or 4 or 5 years.

You want housing. You want real estate developments. You want this and that. You want to encourage people through an incentive tax system. You want the Government to do everything. It seems to me your program is more and more Government and less and less for the individual.

Mr. BAKER. No, sir, that is not true.

Senator HOBLITZELL. In reading this over that is my opinion.

Mr. BAKER. That is your opinion. You have a right to your opinion.

Senator HOBLITZELL. I do not have the Farmers' Union in my State voting for a program like this.

Mr. BAKER. What is your State?

Senator HOBLITZELL. This morning's paper stated that the farm prices are up five point something, which is over eighty-some percent parity over last year. In my State the farm prive levels for livestock and so forth, are the best prices they have had in 6 or 7 years. The farmers are happy and support Mr. Benson's program.

Mr. BAKER. Would you recommend the buying of cattle at this time, sir?

Senator HOBLITZELL. I am not a cattle buyer. All I am saying is that prices are better than they have been for a good many years in my State and the farmers are supporting Mr. Benson's program.

Mr. BAKER. What is your State, sir?

Senator HOBLITZELL. West Virginia.

Mr. BAKER. Which part of the State?

Senator HOBLITZELL. I live in the Ohio Valley. I am a good friend of the Farm Bureau and support the program.

Mr. BAKER. My reason for asking is that I wonder if you would recommend to your constituents that they add to the number of cattle they have in the feed lots.

Senator HOBLITZELL. All I am saying is that prices are better and they are happy. They say they want to support Mr. Benson's program.

Mr. BAKER. Cattle are at 95 percent of price parity at the moment. I wonder how long you think that will continue?

Senator HOBLITZELL. I am just saying what is happening right now and that is what the result is.

Mr. BAKER. I wonder if you consider that there was some 7 years of drought in Texas, Colorado, Kansas, and Oklahoma?

Senator HOBLITZELL. I understand.

Mr. BAKER. Where the breeding herds were very deeply diminished during that drought, both by sales and by failure to add to the breeding herds. Those herds are now being replenished to furnish stocker cattle.

Senator HOBLITZELL. Why have the stocker-dealers not wanted a price control?

Mr. BAKER. The most recently, I saw the Department of Agriculture——

Senator HOBLITZELL. You did not answer my question.

Mr. BAKER. You interrupted, sir. If you will let me continue my thought, then I will get to your question.

Senator HOBLITZELL. Yes, sir.

Mr. BAKER. As to the number of cattle on feed, the most recent report shows 13 percent more now than a year ago, which at the time it was building up there was a demand factor. By the time they sell the cattle there will be a supply factor.

The same report shows placement of cattle on feed for the first 3 months of this year was up 36 percent from last year. Cattle on feed are eligible to start being sold within 90 days after they go on feed.

If you are ready to make this long-term investment that you were talking about——

Senator HOBLITZELL. I was not talking in terms of the farmer, but business and industry was my question.

Mr. BAKER. I am not sure you would want to add further to the volume of cattle on feed at this time, based on this rosy feeling you have about the cattle market.

Senator HOBLITZELL. I am only saying what people say in my State. I am not a farmer. I am a banker and builder. I know my people feel that way about it. That is why I make the statement. The basic question was on capital gains tax. I would violently disagree with you.

Mr. BAKER. I understand that, you being in the building business.

Senator HOBLITZELL. In relating this back to other nations, our capital gains tax is higher than Canada's and England's. The capital gains tax was lower because you want to invite people to take more risk, invest, and create jobs.

I want to ask one more question. I have an appointment to keep at noon.

Mr. Nathan, I agree with many of your statements concerning the pricing policy of a lot of our major industries. I think in a competitive system we should lower prices and cut the fat off of business and I also think labor organizations should cut some of their fat out and be willing perhaps to forego some of the immediate benefits and wage increases they want. I think we have grown soft in business operations in America.

A man came up to my home Monday morning to see me. He had been turned down at my bank and he wanted to see if I would go along with him. In his statement he had listed a Cadillac car, a station wagon, and a $5,000 speedboat. He had taken money out of his business to have those personal luxuries. These are things that are not good. In a time like this he should be thinking about creating his own working capital and giving up a few things to make this work in our community. I think we are all guilty of that, the bankers, the farmers, and others.

Mr. BAKER. There are very few Cadillacs on the farms in America, even in West Virginia.

Mr. HOBLITZELL. There are some in Ohio. I have seen them. They are financed, though.

The point I want to make is that it seems we want to blame everyone else but ourselves about the ills in our Nation and economy. We have had cost-plus deals and everybody charging everything off. And the unions kept wages going up and up. Our productivity has not increased particularly in the automobile industry in the last 5 years, in terms of the wage increases. That is the cost-wage spiral.

You do not agree, Mr. Ruttenberg? It is a moot question?

Mr. RUTTENBERG. It is not moot that productivity in the auto industry increased more than wages.

Senator HOBLITZELL. In what?

Mr. RUTTENBERG. In the auto industry. The wage increase, based upon the productive advances in the auto industry have been far less than productivity. I think everybody agrees to that.

Mr. NATHAN. As a matter of fact, Senator, I think if you have free enterprise you have to have incentives for business.

Senator HOBLITZELL. You agree with the tax program. Capital gains taxes have been increased. You are an economist.

Mr. NATHAN. What disturbs me, Senator, about capital gains is this. I think too often normal income is diverted and becomes capital gains by some manipulation, and the taxpayer gets a tax advantage that he does not deserve.

On this matter of wage and prices, there is one thing that worries me; that is, if we are going to have a fully employed prosperous economy and more production it means we have more goods for consumption and therefore the goods and services for a high standard of living. We also need more demand to keep producing. I am not one who believes businessmen like a recession. I do not think they would like to lay off employees from work.

Senator HOBLITZELL. That statement made awhile ago that businessmen were deliberately doing this, you do not agree with.

Mr. NATHAN. I do not believe in that. On the other hand I believe a businessman will not produce when there is not a market for his goods. I think the problem is to get industry to cut prices substantially and then I think labor would forego wage increases.

Senator HOBLITZELL. On Monday when the feedstore officials spoke they maintained their sales for last year but they tried to sell and cut prices to get volume.

Mr. NATHAN. Look at steel and the auto industry. General Motors averaged in the last 10 years 50 percent return on their net worth before taxes, and over 25 percent on their net worth on the average over 10 years after taxes. That is on its net worth. When the automobile industry is operating at half capacity it is not indicating any real price cut. I do not see an incentive to competition in such price behavior.

Senator HOBLITZELL. They have had bad judgment in gaging the market and on their styling and so forth. They have priced themselves out of the market. I think the American public feels that way. When I am back of my desk I hear people say that automobiles are priced too high and that they are not going to buy them. That is the feeling.

Mr. HAGEDORN. May I get in this discussion, Senator?

Senator HOBLITZELL. Yes, sir; I am trying to find an answer.

Mr. HAGEDORN. Any generalizations we make in this very complex economy are subject to very many individual exceptions. I am not prepared to talk about any particular industry or what they have been doing, or whether what they have been doing is right. Still, when we look at the picture as a whole, we find from the statistics on profits, for example, profits essentially have gotten nowhere in the last 9 years.

The figures on corporate profits after taxes are just about the same in 1957 as they were in 1948, and a little bit lower, though I do not suppose these figures are accurate enough to make any point out of that small decrease. As they stand, the total of corporate profits after taxes was $20.3 billion in 1948, and $20 billion for 1957. Of course, it has been going lower since. There are clear indications of that, though these figures are not available for a later period.

That is in a period when the economy as a whole has been going up at a very rapid rate. That is the disposable income of the corporations.

If you take the disposable income of individuals you will find in that same period it went up, for a round figure, about 70 percent, I think, from about 1948 to 1957. I think when you look at that comparison you have to say that the bulk of the difficulty has been on the cost side rather than on the profit side.

If I may go to the point that Mr. Nathan introduced: Sure, to keep going in our economy we have to have an adequate level of demand. People do not produce goods to put them on the shelf. They produce them to sell them. There has to be an adequate level of final demand.

When we make that simple statement I think we are missing one big side of the whole problem. There is always an adequate level of demand if you can sell your goods cheaply enough. If you could sell Cadillacs in 5- and 10-cent stores, there would always be enough demand to sell more than we could ever produce.

So there has to be a balance between the cost level and the level at which you can profitably sell goods, which depends on your cost and the level of demand.

To assume in all econoic problems we must deal with them on the demand side, it seems to me is the great trouble in our economics now. We have put all our emphasis on the demand side, and the result is that all solutions that we propose are inflationary solutions.

Mr. BAKER. Could I expand on this comment? I notice from the President's Council of Economic Adviser's report, called the Economic Indicators, that the gentleman who just spoke picked 1948, the highest level of profits after taxes of any year until the last two.

I would further like to point out that there has been a 25-percent increase in corporate profits after taxes from $16 billion in 1952 to $20 billion in 1957.

Mr. HAGEDORN. 1952 was an excise profits tax year.

Senator HOBLITZELL. That is right.

Mr. BAKER. Dividends increased by a third, from $9 billion to $12.1 billion.

Representative CURTIS. What is that in relation to the amount of capital invested?

Senator HOBLITZELL. That is the thing that counts, the ratio.

Mr. BAKER. As I understand that figure, and I do not have it with me, Senator, but I understand the long range average for the last 10 years on return of corporate assets has been in the neighborhood of 12 percent. If the farmers had a 12-percent return on their capital assets, not covering any return to the operator and family labor and management at all, farm income would have been $5 billion higher last year than it was.

Senator HOBLITZELL. The farm is like the coal industry; it has had to adjust itself to many technological changes. We have had to spend millions of dollars to compete. To do that we had to mechanize. There has been a tremendous change. Your productivity per farmer has increased tremendously in the farm industry.

Mr. BAKER. I will also point out it has increased tremendously in the automobile industry.

Representative CURTIS. Will the gentleman yield for a comment on that?

One thing about the farming industry is that a great deal of the return seems to come in capital gains, just as it does in small business where it is plowed back. If you would try to evaluate or estimate the amount of farmer income that has come over a period of years from his increased equities in his investment you would have a very fine figure, I might state.

Mr. BURGER. Mr. Chairman, I would like to inject a thought here in this conference.

I have been in the business for a little over 50 years. In my youth I was with the Borden Milk Co. in the treasurer's office. Therefore, I had knowledge of the so-called depression, I think, in 1907. Then I was in my own business from 1909 up during the depression of 1919 and 1920. Then I noticed the falling off of business in my official position in the National Federation of Independent Business shortly before Korea. So I would think that what has taken place in these last 15 or 18 years is that our whole business economy has become weak, due largely to excessive expenditures of the Federal Government, which was not natural expenditures during preceding times, and I think industry, both in production and labor, must realize that we are getting down to the hard core of competition and we are getting down to a more stable situation.

I am well acquainted with the automobile industry, being a member of that industry beginning in 1909. Any man with commonsense knows that they could not put many more cars on the streets of the United States than are on there today. It was just overproduction, trying to force the market, and I think we better realize that situation if we are going to build on a sound economic condition in this Nation of ours, and that affects both small business and large business.

Senator HOBLITZELL. Mr. Chairman, I have a speaking engagement but I have one more statement to make before leaving.

I appreciate the very fine remarks made by all you gentlemen here this morning, and I subscribe to the idea that tax cuts are necessary. We have an incentive enterprise system. We have to give labor its incentive, we have to give the entrepreneur incentive, and also give incentive to management as well as the farmers.

We have gotten away from the basic thinking in terms of the free enterprise system. We have a lot of people today who have not had experience. They have been on a rising economy and have never had experience in declining markets. They do not understand that you have to put reserves aside and you have to protect yourself. They automatically make this deal and go to the bank and say, "I want the money."

In the ordinary situation you go to the bank and say, "Could I borrow the money to do this?"

I had many people in the last few years operate on that basis and never realized that things sometimes can go down and they do not prepare themselves accordingly. But this system of ours is the best in the world, and I think all of us getting together here and discussing our various views is good.

Thank you very much.

Senator DOUGLAS. Thank you.

I wonder if I might address a question to Mr. Wilde, which may waken some general discussion?

I would like to direct your attention primarily to the third paragraph on page 5, Mr. Wilde. C. E. D. recommends a tax cut if conditions decline from February. You say they declined from February to March. It is not yet certain what happened to April. You suggest that we watch the April or May figures on production, sales, incomes, employment and unemployment.

Now we have an estimate on unemployment issued by the Office of the Secretary of Commerce on April 29, which shows on the face of it a decrease in the probable numbers of the unemployed from 5,198,-

000 to 5,120,000 or a decrease of 78,000, but which when seasonally adjusted is from a rate of 7 percent to 7.5 percent. I wondered whether you would regard that as an improvement in the unemployment situation or a worsening of the unemployment situation.

Mr. WILDE. I would regard it as inconclusive, Senator. But I am not a statistician and I do not want to pretend to be one.

Are you familiar with this little chart we made up for ourselves? That is the type of thing we would use if we were in your position as a Senator.

Mr. RUTTENBERG. May I comment on the unemployment question he raised?

Senator DOUGLAS. Yes.

Mr. RUTTENBERG. Senator, when the normal decline in unemployment between February and March is normally 200,000, 300,000 to 400,000, which has been the experience year in and year out over the last 13 years or so, since the end of the war, how can one say that a decline of 78,000, the lowest decline in unemployment in any month in any year, February to March, in the post World War II period, is inconclusive?

Mr. NATHAN. No, it is the March unemployment figure we have out now.

Mr. RUTTENBERG. I am sorry. That is March to April figures. They confuse me. They put it out 10 days earlier than they should.

Senator DOUGLAS. Ten days earlier than usual.

Mr. RUTTENBERG. Yes.

We asked the Secretary of Commerce back in March to put out the figure for March in the end of March or early April, and you know what he said: "We do not put out employment statistics piecemeal. We will wait to put out a joint release with the Department of Labor."

He violated what he wrote us on April 3, 1958.

Representative CURTIS. He is following your suggestion now, perhaps.

Mr. RUTTENBERG. I am glad he is.

As a result of this decline of 78,000 in unemployment, with the normal seasonal pattern of 350,000, this is what causes the seasonal adjustment unemployment rate to jump from 7 to 7½ percent.

How can you say this is inconclusive? I do not understand that.

Mr. WILDE. I can only give you this much of an answer if it is worth anything. In times of stricter competition a great many factors come into play, for example, there may be more work with less people producing the same output. There is an efficiency step-up by management, technology, and the workmen themselves. I would not know what particular factor added to unemployment. It is also not clear how many women wanted to work or did not want to work. There are what I would call a great many short-term aberrations. That is all I meant. I do not think the figures look good. I agree with you they do not look good. I merely say to me they are not conclusive yet.

Representative CURTIS. Will the gentleman yield on this point?

It seems to me you have to take the other side of the coin, too.

Mr. RUTTENBERG. I wish you would and carefully analyze, Mr. Curtis, as you discuss it.

Representative CURTIS. I want to talk about the employed which shows over the same period of time an increase of almost 600,000.

Mr. RUTTENBERG. But where was it?

Representative CURTIS. Now, wait—an increase of almost 600,000, plus the fact that we have in the labor market, comparing 1957 to 1958, 1,100,000 more people in the same figures to find jobs for. You could look at it this way, that in handling the job of getting additional jobs as our economy grows, 1,100,000. You have gotten 600,000, roughly, of them jobs, although you have not been able to cut down as much on the unemployment as you like. That is the other side of the coin which bolsters, I would say, that these are inconclusive figures.

Mr. RUTTENBERG. But, Mr. Curtis, may I comment there? The increase was 500,000 plus in agriculture, 100,000, plus or minus 10,000 or so in outdoor activities.

Representative CURTIS. Sure. This is seasonal.

Mr. RUTTENBERG. In nonagriculture.

Do you realize between January and June every year the increase in agriculture employment is in the neighborhood of about 2 million and that this 500,000 rise on the farm is purely what happens at the springtime of the year when people go back to farming?

Representative CURTIS. But, Mr. Ruttenberg, you all want to regard the seasonal angle one time and at the other time disregard it.

Mr. RUTTENBERG. Oh, no.

Representative CURTIS. Where were your comments in regard to weather conditions? The unusually severe winter this winter, which was experienced all over this country, has had its effect on the construction industry and other industries. In fact, that has been a factor, but at that time you wanted to use absolute figures. I dare suggest when June comes around, when we know that the figures are going to jump because of the people out of high school and college, who under our system of counting unemployables, will increase it considerably, will you be ready then to want to adjust seasonally?

Mr. RUTTENBERG. When you and I discussed this problem before the Joint Economic Committee's hearings back, when was it, the first or second week of February, you and I discussed and let us look at the record, the seasonally adjusted rate of unemployment.

Representative CURTIS. Yes, because I brought it up.

Mr. RUTTENBERG. And I am prepared to discuss the seasonal adjusted rate at any time of the year if you want to do it. Do not say we discussed at one point seasonally adjusted figures and not at another point. That was not what you and I did in February.

Representative CURTIS. That is why I think your observation is perfectly proper, but I think it has to be taken in balance. I think the statement that it is inconclusive is a fair statement.

Mr. BAKER. Mr. Chairman, could I interpose a hillbilly comment at this time?

Senator DOUGLAS. It will be as sophisticated as most hillbilly comments are.

Mr. BAKER. If a fellow is unemployed and he has run out of his number of weeks of unemployment compensation he has a problem, whether he is seasonally adjusted or not.

Mr. WILDE. Could I add?

Representative CURTIS. Mr. Chairman, let us not interject that. There is not a person in this room that is not concerned about the unemployment. We are trying to talk about the underlying economics of this deal with the thing and not deal with demagoguery.

Senator DOUGLAS. Mr. Wilde?

Mr. WILDE. I want to add that from CED's point of view a massive tax cut is a pretty bold step. We did not want to rely on just one figure in too short time. That is why we spelled out our 1954 prescription in terms of a series indicator.

Senator DOUGLAS. What I want to find out is the number of series you are analyzing. Unemployment is one that is not conclusive. Employment is another. I take it that is not conclusive.

Mr. WILDE. Gross national product would be.

Senator DOUGLAS. What about production?

Mr. WILDE. Yes.

Senator DOUGLAS. The index last August was 145. The preliminary figures for March are 128. That was a decline of 17 points, or just short of 12 percent. Now, the statistics for April will probably be out sometime next week.

From the indexes of the New York Times, a weekly index, and the figures that we have on automobile and steel production, and so forth, carloadings, it looks as though there will be a further fall in the index of industrial production, and some people who are watching things closely expect an index not higher than 126. Suppose we get the 126, which would be a decline of 19 percent.

Mr. RUTTENBERG. Points.

Senator DOUGLAS. Nineteen points, pardon me; 19 points or 13 percent. Would you regard that as significant?

Mr. WILDE. Yes, I would.

Senator DOUGLAS. You would?

Mr. WILDE. I would.

Mr. NATHAN. Mr. Chairman, on this point and what you were asking Mr. Wilde, including Congressman Curtis' statement, I really believe we ought not just wait until we see an upturn, until we see evidence of further decline. I think our criterion ought to be whether it looks like there is a real upturn in prospects. Let us say we did level off at this level. Say unemployment did not go above 5¼ or 5½ million for the next 2 or 3 months. Does that mean we should not take any action at all? There is where I think the mistake is made. The criterion ought to be whether or not there is strong likelihood of a rather prompt upturn, because we are hurting now. That is the point I would like to make. We are hurting now in terms of loss of production, hardship of unemployment, and international impact.

Representative CURTIS. Will the gentleman yield?

I think that is a fair statement of position. I think what the CED is doing is setting out the indicators as to how you evaluate it when you should take it. It may be when you view the indicators——

Senator DOUGLAS. I do not see the upturn.

Mr. NATHAN. I do not see the upturn. That is what I was trying to say.

Representative CURTIS. I could not agree with you more. I think that is what we should be looking for. It is a matter of judgment to agree whether it is.

Mr. Ruttenberg may think, and I think it is some basis for his saying unemployment figures are a little more conclusive, perhaps, than I would say. But I think the CED position, if I may say it, Mr.

Wilde, and you correct me if I am wrong, is that you think that is one indicator, but there are other indicators that ought to come along before that is firmed up.

Senator DOUGLAS. That is a subject I would like to pursue.

Now, let us take the third test, incomes. You can follow this on pages 2 and 3 of the economic indicators that have been furnished.

Mr. WILDE. We have it in somewhat different form in our chart.

Senator DOUGLAS. There are no figures on national income for the third quarter of 1957, let alone the first quarter of 1958. So if you take pure national income as the test you will have to wait a good many months.

That is page 2 and page 3, Mr. Wilde. The national income is on page 3. That is the first column at the bottom of the page.

If we wait for national income figures, they are 6 months behind, we will have to wait on into the late summer.

Mr. WILDE. Do we not have any quarterly figures, Senator? I thought we did.

Senator DOUGLAS. These are, I assume, the most recent figures. These are issued as of April 21, I believe.

Mr. RUTTENBERG. You have monthly personal income figures.

Senator DOUGLAS. We have the total wages, which is down.

Mr. WILDE. We have the personal income, which of course can be distinguished from national income. We regard it as one of the very significant indicators.

Representative CURTIS. I would like to add that corporate income is on the slack.

Senator DOUGLAS. If you take personal income, then you substitute personal income for national income.

Mr. WILDE. It is a pretty significant figure. Would it not be?

Senator DOUGLAS. Yes, I think it is. If you take gross national product that is computed on a quarterly, not on a monthly basis, and we have an estimate for the first quarter of 1958. It is only an estimate. And this came out in April. I do not think we had it in March. So we will not get an estimate of the second quarter until July, by which time Congress may be adjourned.

So the point that I am trying to make is this: That if you ask that a policy wait until all of these symptoms become manifest, do we not have to wait pretty long?

Mr. HAGEDORN. Senator, may I comment?

Senator DOUGLAS. I will ask Mr. Wilde first, and then you.

Mr. WILDE. I think we gave ourselves a cutoff point where we cannot hedge any longer, probably by the end of May, by our own statement.

Senator DOUGLAS. Even if these figures are not available?

Mr. WILDE. Some of them may be available.

Senator DOUGLAS. I know. But if all of them are not available you would say that we should not postpone action merely because not all of them are available. We should move with such knowledge as we have.

Mr. WILDE. That is right. That is what we said.

Senator DOUGLAS. There is another point I think needs to be considered. That is the length of time it takes for a measure to go through Congress and the length of time it requires to get popular consent. We are very grateful for the CED, but after all it is only one element in public thinking. This is not Soviet Russia. It takes time for a tax bill to go through the process of hearings in the House, a report, action by the House, hearings in the Senate, action in the Senate, and so on. So if you would postpone starting this program until the end of May you have very little prospect of getting through before the 1st of July. As a matter of fact, with the corporate tax rate going down and the expiration and reduction of certain excise taxes we have a July 1 deadline to meet.

Is it not necessary for sane consideration that we start moving before the end of May, as it is now the 1st day of May? So can you reproach some of us if we start to move a little bit in advance of the CED?

Mr. WILDE. Senator, of course we will admit that there are practical difficulties, but we recommended a month ago that the staff work be speeded up, so that when sufficient evidence was accumulated for the House and Senate to determine what could be done they could move pretty fast.

Senator DOUGLAS. It is not merely staff work, as important as staff work is, but there is a problem of obtaining consensus in a democracy which is time consuming.

When I first proposed a tax cut in February, I was virtually hooted off the floor of the Senate and blasted in every newspaper of the United States, and blasted very severely by the business groups of this country. Now, in the process of three months public opinion has changed. I do not regret going out ahead of the CED or the other groups. If everyone waits until the last minute then you get action which tends to come too late.

Mr. WILDE. You understand it better than I do, I am sure. Maybe I am not making myself clear. A tax cut in substantial nature would be helpful. We believe it will. It does not seem to me it is vital whether it is taken one month, or another month, and it is important to be sure it is necessary before we do it.

Senator DOUGLAS. Here is the point. As you well recognize, a recession is an accumulating process and there is danger, in the popular phrase, of its feeding upon itself by the destruction of purchasing power, production, investment, and so forth, and so on, creating still further decreases. It is an impetuous process.

Mr. WILDE. It can do that way. But, Senator, are we all clear as to what the cause of this recession is? We might see the remedies clearer if we knew the cause.

Senator DOUGLAS. If we have to wait until the economists and businessmen agree on the causes, we shall wait for a long time. As an economist I studied this subject for years. I read books, and books and books upon it from all sources. I talked with economists from all over the world. And there were virtually as many theories as there were economists. And if you try to get at the initiating causes, the initiating causes of depressions, then you get a wide variety of choice. But there is some agreement on the cumulative factors.

Mr. BURGER. Senator Douglas?

Senator DOUGLAS. Yes, Mr. Burger.

Mr. BURGER. Do you not think that the overall economy is just closing their eyes to the contributing causes of the prosperity that existed within our Nation during the last 19 or 20 years? You do not have to be an economist when you figure we are supplying the world market with most everything and that could not go on indefinitely. Take one industry, the coal industry—bituminous coal. How many millions of tons of coal were supplied all over the world? And we used to say when we were boys "shipping coals to Newcastle." Those markets could not continue. It applied through our whole economy. We were supplying the world markets that were closed during the war periods and after the war periods. Industry and labor ought to know in our Nation that things could not go on indefinitely and we are back now to a hard core competition and if small business was to take this gloom picture that is emanating out of Washington continually, and I have been in small business all my life, 99 percent of small retailers would close their store and get out and liquidate their business. So I think we better get back to a normal national condition within our economy and build within our domestic economy and stop trying to reach for the moon that we have been doing for the last 10 or 15 years. That is my observation.

Mr. WILDE. I want to say, Senator, despite the 5 million that are unemployed and others that are on part time, which is awfully serious in human terms, we do have personal income of a magnitude of $340 billion. That is a lot of money if the people are in the mood to spend it. In broad economic terms we have a lot of buying power in this country if it were effectively used. Why some of it is not used, I do not know. I have certain personal notions. You all do. The whole economy is not in bad shape.

Mr. RUTTENBERG. But, Mr. Wilde——

Senator DOUGLAS. No one would say everything is in bad shape. No one would say that. But when there are significant drops in production and employment——

Mr. RUTTENBERG. Mr. Chairman.

Senator DOUGLAS. I recognize Mr. Hagedorn.

Mr. HAGEDORN. Thank you, Senator.

I appreciate fully the force of your remark a little earlier that we will have a difficult road if we try to get agreement among the economists on basic causes, but at the same time I think the discussion here this morning illustrates that we have a difficult road, too, if we try to base our actions on short term signals as to which way things are going. You never get agreement on that, either, Senator. I think the people I represent would look at the problem like this: All this discussion is in the context of your question. What are the current symptoms. And the answer I would give is that the current symptoms are very clear. The patient has been suffering from both chills and fever alternately, recession and inflation.

Senator DOUGLAS. I once had that and it is not a pleasant sensation.

Mr. HAGEDORN. The metaphor runs out. I do not know whether you can suffer chills and fever simultaneously.

Senator DOUGLAS. Yes, alternately.

Mr. HAGEDORN. If those are the symptoms in our economy, is it really to the point to try to decide exactly what the temperature of the patient is at this moment, or to try to say whether he will be having a chill or fever at 4 o'clock this afternoon? Doesn't the physician rather say, "All right, he has chills and fever, let's find out the basic cause of his ailment and then prescribe the cure."

Senator DOUGLAS. What is the fever? I can see the chills.

Mr. HAGEDORN. I do not know how valid this metaphor will turn out if we keep working on it. But recession and inflation——

Mr. NATHAN. Mr. Chairman, I think Mr. Hagedorn has performed a service for us by highlighting this fallacy that inflation and recession are inevitably part of the same thing. I think we have too much confusion in this country between inflation and prosperity, and they are not necessarily the same phenomenon.

Mr. HAGEDORN. I agree with that.

Mr. NATHAN. In 1955–57 we had good business in the country but unemployment was over 50 percent higher than 1952 or 1953. We had in 1952 and 1953 a million and a half unemployed, in 1956–57 it averaged about 2¾ million. That still was not serious. Certainly in 1956 and 1957 nobody would say in this country we had excess demand. We had idle automobile capacity and we had idle textile capacity. We could have produced a lot more. We had fairly good prosperity, although not full employment. Yet, we had inflation. The implication of what you say, Mr. Hagedorn, is that if you have inflation you have to cut down on total demand in order to fight inflation. Inflation and prosperity are not the same thing. You say the symptoms are the same.

We have today an ailment in that $20 billion or $30 billion of idle capacity of manpower, machinery, and income. We had underutilization of resources and hardship and waste. At the same time we have high and rising prices.

I feel what we have to do is attack this inflation as a serious phenomenon and not seek its solution by idle resources. We must not say the chill of unemployment and idle resources is a counterpart of the fever of inflation. We have to fight both of them, not one against the other. That is where I think the mistake is made.

Mr. HAGEDORN. Just for the record I do not say here that I think the recession should be used to fight inflation.

Senator DOUGLAS. I understand.

Mr. RUTTENBERG. Mr. Chairman, I would like to comment on Mr. Wilde's remarks a moment ago. He said we had high levels of personal income, $341 billion, and a lot of purchasing power. And everything looked fairly favorable in that regard. A careful look at these figures, though, on page 4 of the April indicators show the total personal income from the peak in August to March, the latest figure, has fallen almost $6 billion. That is to say, $5.9 billion. The drop has been even greater in the wage and salary sector where it has been almost $9 billion, about $8.7 billion. And it has continually dropped, and dropped steadily, as you can see, by looking at the figures. The April figures are not out yet, but if the April figures were to show this same kind of continual decline as I am certain they will, and with employment already showing that it has not recovered as much as it should seasonally, the same for unemployment, and with sales, as we can see, by looking at the economic indicators on page 21, the most recent figure we have is only retail sales for March, and it shows a decline again from the January and February levels. So, if you put together the things which you have, production, sales, income, employment, unemployment, which you list on the statement on page 5, do not all these show you moved into March with a downturn? We are moving into April and it looks like they are moving down also. Is it not about time they take some action?

Mr. WILDE. Well, Mr. Ruttenberg, I will say those are figures for the purpose of illustration that we put forth as significant and if they are all continuing as you say, and as they appear to be, we run off the page. We have to agree, because the burden is on us. If you are going to take what to us is a pretty bold and new step in trying to adjust the economy, we say that the evidence in May should be clear that the economy is not going up. We never had a deliberate tax cut in this country for anticyclical purposes.

Senator DOUGLAS. Here is the point. There is no danger that we will take any action before the end of May. Knowing the House Ways and Means Committee and the Senate Finance Committee as I do, there is no danger that we will be unduly precipitous in our action. The danger is quite the other way. Might it not be a good thing to start the ball rolling, and then if conditions reverse themselves we can call it off? We have to start, do you not think?

Mr. WILDE. I agree.

Senator DOUGLAS. So you would not throw any dead cats at us if we start this; would you?

Mr. LYNN. Why not start hearings? I think if the indexes and figures change we can call it off.

Senator DOUGLAS. The House Ways and Means Committee of course under the Constitution has the power of initiation. My colleague is a member of the House Ways and Means.

Representative CURTIS. It is hard for me to keep silent here, but I am waiting.

Mr. RUTTENBERG. There is no need for further tax hearings in the House; is there? I thought your chairman announced that the tax hearings you had are sufficient, that you can draft a bill.

Representative CURTIS. The thing that disturbs me from the standpoint of Senators, Congressmen, the press, businessmen, economists, is this: We have two tremendous tax bills sitting over in the Senate right now. True, too, they are dealing with details but every one of those details was the result of hearings and studies for over 2 years. One is the Forand excise bill, consisting of 300 pages. Almost everything in there is designed to remove impediments to economic growth and stability. The same thing is true of the Mills bill, Senator. Those things have passed the House. They are sitting over there, and let me add one other——

Senator DOUGLAS. All right. You frame your indictment and I will make my reply.

Mr. RUTTENBERG. What is the Mills bill?

Representative CURTIS. The Mills bill does the same thing on corporate and personal income taxes. Granted it is only 100 pages long, but it is a pretty long piece of legislation. We completed some 5 weeks of hearings in January on other bills that were designed for the same purpose to remove some of these impediments to economic growth and stability. So hearings have been completed on many of these areas. Even though you might say they will not have the economic effects that I see, nonetheless there is not the argument against tax reform because it takes too long, because work has already been done. That could be passed out last August, because the Forand bill went over there in July.

Senator DOUGLAS. May I reply?

Representative CURTIS. Yes, certainly.

Senator DOUGLAS. In the first place, may I say I do not make out the program for the Senate Finance Committee. Therefore I am not responsible for failure of the Finance Committee to act. I wish that we might have acted, but I think my colleague gives too much importance to these bills as antirecession measures. There is virtually no change in net governmental income contained in them. There are balancing considerations. So if you are thinking of overall fiscal policy, aside from this alleged stimulation of activity on which my colleague places great reliance, there will be no overall economic effect upon the system as a whole, to which the various witnesses have been addressing themselves.

Representative CURTIS. Will the Senator yield for a comment to clarify?

I agree. It does not shift purchasing power from the Federal sector to the private sector.

Senator DOUGLAS. That is all right.

Thirdly, I have tried to study those bills very carefully, and I would say that they may correct minor defects in the tax structure. But they assidiously avoid dealing with the major weaknesses of the tax structure. There is nothing about the depletion allowance, the most notorious scandal in our system. There is nothing about a whole variety of tax weaknesses.

Representative CURTIS. A lot of things are not in there that should be in there.

Senator DOUGLAS. And I think that by the time we get through it will be worse than when we started.

All I am trying to say is this is no substitute at all for a tax program designed for antidepression purposes. Therefore, whatever delinquencies the Senate Finance Committee may have, and I for the purposes of argument am not prepared to admit at this time that we have any, it is about time that we get busy on a general tax program. If conditions turn up we can call it off.

Representative CURTIS. Senator, would you not agree with me——

Senator DOUGLAS. And take up tax reform. There has to be tax reform. I will qualify that.

Representative CURTIS. Even though you might not agree with me on the effect of this, certainly to go about ordinary tax reform and continue it rather than hold it up is going to be helpful. You can not do any damage.

Senator DOUGLAS. I am all for tax reform and I would like to see real tax reform.

Representative CURTIS. I would, too. That does not mean I will hold up on the details.

I might state in these bills are many specifics. Let me illustrate one little one. I have illustrated it before. The cabaret tax. We get no revenue from the cabaret tax. It is a tax on any eating establishment that hires musicians. I do not know how many musicians would be employed if that tax would be repealed. It has been studied. It has been sitting over there for some time. There are other little but significant items contained in both bills.

Senator DOUGLAS. Let me say this. I am fast discovering points of agreement with my colleague from the State of Missouri. I am with him in an attempt to relieve the tax on music with your meals.

Representative CURTIS. Because there has been so little understanding on the part of people to study these two tax bills, I am prepared to take the floor next week, Senator, to bring out some of the details that it would do and cumulatively, I think it would have a tremendous effect.

Senator DOUGLAS. I only hope that at that time you discuss depletion allowances for oil and sulfur and for clamshells and oystershells.

Representative CURTIS. We are merely saying, Senator——

Mr. RUTTENBERG. And capital gains for apples.

Representative CURTIS. I wish you would read some of my statements. I made a statement on depletion allowance. They should be constantly reviewed. I do not think it is a scandal, but I certainly think the oil depletion allowance is too high and recommend that we study it and figure out where it should be.

So I am in accord with these other basic reforms.

Senator DOUGLAS. We are coming together more and more, Congressman.

Representative CURTIS. My only point, if I may go on——

Senator DOUGLAS. Sure.

Representative CURTIS. On this basic thing, it does seem to me that it is a shame when we are faced with an economic condition such as the present situation that these reforms that are needed and have been badly needed for some time, and not implemented by proper legislation, that we still do not go ahead with them and here we have these things well in the process, ready to move, and everyone is talking about something new. Why do we not start analyzing what we have done and see what it will produce? And that gets back to the statement, Mr. Wilde, that I think it is important to find out the symptoms of this recession.

I took the floor to point out why I thought this was really a tax structure recession, and I can point out many details, I think, that would indicate that what we have been doing through our tax structure is produce business decisions not based on economics but business decisions based upon tax considerations.

And let me illustrate one very important area, and that is the increased mergers and acquisitions of small growth businesses by their larger competitors, not for economic reasons, although they can have the merger and acquisition for economic reasons; but the increased growth or rate of these mergers and acquisitions seem to have been almost entirely on the basis of tax considerations.

Now, you would not lose any revenue. We would gain revenue, I submit, and we would strengthen our economy if we removed that impediment to economic growth and stability.

And there is the problem of locked-in investment, where you have practically frozen investment in certain areas because of the effect of inflation. We have this problem arising from the combination of inflation on capital gains because if you sell you have to pay a capital gains on something that is purely inflation and not an actual realized increase in your equity holdings.

Those are economic phenomena that lie under this whole situation and I can go on and list many, many others. That is why I want to see this thing analyzed a little more. We should not pass off lightly the work that has been done by many people in trying to figure out areas of tax reform, because sure, some of the things you want are not in there, Senator. There are a lot of things in there that should have been in there many years ago, and it would only get them passed. Then we could see where we are. I suspect you would find this thing would disappear in a hurry if we hit on some of these things.

Mr. BAKER. Mr. Chairman, I would support Congressman Curtis' position, to this extent: Having studied the legislative history of various tax changes, I am convinced the best time in the world, Congressman Curtis, to get a tax reform passed, is at the time you are making the cut in taxes, rather than when there is no change being made in the tax structure or at a time when you are trying to raise taxes.

Representative CURTIS. I think the gentleman made a good point. That is why I asked these people who are trying to make tax reform to get away from the idea that it is a tax cut. I think as far as Federal revenue is concerned you will gain rather than lose Federal revenue, if the theory is you are removing an impediment to economic growth. You will recoup any loss in Federal revenue.

And as Mr. Ruttenberg pointed out, if we have a decline in gross national product we lose Federal revenue because it has a negative growth. If these things are caused to any degree by our tax structure, then we would improve our revenue position by digging into these things.

Mr. RUTTENBERG. I am inclined to say the same thing is true of the tax gains Senator Douglas recommended in the Senate 2 or 3 months or so ago, that you actually would increase over a period of time Government revenues with reduction in personal income tax.

Representative CURTIS. I think that is a good argument.

Senator DOUGLAS. I never claimed that, for the sake of the record. I never said it would increase revenues. I merely said that the loss would not be anywhere near as great as you would assume from the reduction in tax rates, on the assumption that national income did not increase. My own belief is that the final loss would not be more than 40 percent of the initial loss from the reduction in tax rates——

Representative CURTIS. Perfectly logical.

Senator DOUGLAS. Used on the basis of the multiplier of 3.

Mr. BURGER. Mr. Curtis, you are a member of the House Ways and Means Committee and you were on the Forand committee, I believe.

Representative CURTIS. No; I was not on that. I was on the Tariff Subcommittee.

Mr. BURGER. Do you believe that if these inequities that exist in the tax structure today are corrected that would bring in more income to the Government?

Representative CURTIS. There is no question in my mind. Let me point out that every tax has a point of diminishing return.

Mr. BURGER. All right. For 15 or 17 years I have been appearing before the House Ways and Means Committee requesting an inequity that exists to be corrected. This gentleman over here, Mr. Newsom, I believe, brought up the fact that, on a farm tractor tire, I think he said the tax was around $25 somewhere.

Mr. NEWSOM. On a large one.

Mr. Burger. All right. Fine. Here is the inequity. The tire retailer in that area that is carrying that tire has already advanced that $25 to the Government that he will eventually collect, be reimbursed, after it is sold. But here are these large tire manufacturers, three or more, owning and operating retail stores. And those stocks of tires have been exempt.

Representative Curtis. That is right.

Mr. Burger. They have been exempt from the tax rate these past 17 years, whereas the 100,000 to 150,000 tire retailers of all descriptions have advanced that money to the Government and will have to wait 6 months, maybe a year, or never get the money back. Here are these 3 major rubber companies with retail outlets having that exemption for the past 16 or 17 years. There is the inequity.

Representative Curtis. I agree with you.

Mr. Burger. These are not for reduction of that tax, but are asking for adjustment, and nothing has been done on that.

Representative Curtis. I agree. That is the kind of thing I am talking about, and that, if you equalize it, you will remove an impediment to growth and strengthening of our economy.

Mr. Ruttenberg. I am sympathetic to tax reform. The problem which confronts us today is not revision in the tax structure; that will take a lot of time. Even if the Senate passes a bill, it will take time.

Senator Douglas. There is a very inadequate bill that was passed by the House. It shirks all the major problems.

Mr. Ruttenberg. I agree. The issue here is to reduce the trend of recession. Here is one point where I find myself in agreement with Mr. Wilde, I am happy to say.

Mr. Wilde. Thank you.

Mr. Ruttenberg. That is, we ought to now be taking an approach to the kind of tax cut that is necessary to stimulate consumption, to stimulate a return of full employment and full production opportunity, and leave to a future time a revision of the tax structure, because that is going to take too long. What can we do now to immediately enact the kind of tax cut that is essential to reverse the trend in the economy? I think that is the key question.

Representative Curtis. That is an argument, and a fair way of putting it. All I am saying is there should be an examination into what has already been done. Let us see if your group would urge the Senate to move ahead on some of these things, for example, and put the pressure on there and, at least, get that out of the way. Then we can pick up the next step. I could not agree more; that is what we are talking about.

Let me make a further suggestion. There is going to be a delay in this program of turning money into the hands of consumers, and there is no insurance, I might state, that it will actually go into consumer durables, and spent for that purpose. There will be some lag, and the only way you create more jobs is on the assumption that you actually will have consumption go up.

I would think a more direct way would be where you have the removal of an impediment, that is to say, like in the cabaret tax. The removal of that impediment would increase employment immediately, and I can give you at least 10 other examples in there where you would get immediate employment, sure, on a smaller scale, perhaps, but, nevertheless, on some scale.

Mr. RUTTENBERG. Maybe if people had more money to spend to go to restaurants that play music, the removal of the tax may employ more people, but they do not have the money. Then the removal of the cabaret tax will not help much.

Representative CURTIS. They did not do it in 1956 and 1957. They just do not employ musicians.

Mr. RUTTENBERG. That is right. It is worse now. They have less income to spend in these cabaret-type restaurants.

Representative CURTIS. All I am pleading is for an examination into this area, because I think it is very important. You are doing two things. One, you get into the symptoms, and maybe I am wrong on them, but at least let us examine them. Secondly, if those are the symptoms, and I should not say symptoms—I should say causes—if they are the causes, then the removal of them is going to help correct these things. It is a rifle approach as opposed to a shotgun approach.

Mr. BAKER. You are not urging the enactment of these already partially enacted reforms in lieu of——

Representative CURTIS. I did not say in lieu of. Otherwise, all this other talk about what you are going to do is so much talk.

Mr. RUTTENBERG. I am glad to hear you commit yourself to a tax cut. I hope you carry that view into the Ways and Means Committee.

Representative CURTIS. I am in favor. I think we have to do a lot of basic tax revision, which might include, and probably would include, what we call tax cuts. My distinction is this: The tax cut is where you deliberately change purchasing power from the Government sector to the private sector. The tax revision, as I define it, does not necessarily switch it one way or the other, but removes impediments to economic growth and stability.

Mr. WILDE. Congressman, as an officer of an institution that lends money, I see all kinds of weird schemes rigged up to walk around the tax law. So, I am sure we have money and brains exercising a lot of their skill to get around tax law. We have an awful lot of details that do not seem fair and right. But the reason CED, and I was not solely responsible, took this position was that there are so many problems and it would take, as we saw it, so much time for full consideration that you just could not cover them in time to enact an antirecession tax cut. We agree with you; there are all kinds of inequities and inefficiencies. There are two things, inequities and inefficiencies.

Representative CURTIS. This is my last comment on it. If CED had taken what is already in the mill, already studied, already in the bills over in the Senate, already what has been heard in the House and said, "Now, in this area this much, in our judgment, will be accomplished, but we think in addition this should be done," then I would feel better about it, but there has been a complete ignoring of the work that has already been done in the Congress. So let us have an evaluation of it.

Senator DOUGLAS. May I interject here, without continuing the argument, whether H. R. 7125 makes any substantial reform in the system or whether H. R. 8381 makes any substantial reform. The report of the House Ways and Means Committee, to which my good colleague belongs, states that the net revenue loss on H. R. 7125 is only $15 million; while no definite numerical estimate is made for H. R. 8381 by the House report, nevertheless a study of individual provisions indicates that there is not much change really.

Representative CURTIS. There is no change. I never made a claim that there was. That is what I said.

Senator DOUGLAS. So far as overall economic policy is concerned, these two measures really are beside the point.

Representative CURTIS. On your theory that the only way tax reform does any good is if you transfer purchasing power from the Government to the private sector, that is the only basis.

Senator DOUGLAS. It is not the transfer, it is the creation of purchasing power. That is what people find hard to understand. When you get a Government deficit in a period of recession you should finance it primarily by borrowing from the banks. Let the banks create the additional monetary purchasing power. They will get their cut out of it to satisfy them. What you do is get additional monetary purchasing power thrown in. In a period of prosperity when you want to check inflation I think any Government borrowing, and I hope there would be none, you understand, should come from nonbank investors.

Mr. RUTTENBERG. Like this administration has been unable to do.

Senator DOUGLAS. What you do not understand is that the quantity of monetary purchasing power is not a fixed amount, and what we are primarily trying to do is to increase the number of money counters so as to increase the monetary demand for goods so that more goods will be demanded, more goods will be produced, more people would be employed, who with more money in their pockets, will buy more, and you will get the multiplier effect and hitherto I have not thrown in the accelerator principle. Then you add the accelerator principle, namely, the increase in demand for consumer goods creates a still larger increase for demand for capital goods and then you have two potent combinations. I am ready to throw in the accelerator principle as well as the multiplier principle now, to really get some figures as to stimulating effect of the reduction in taxes when there is substantial unemployment of labor and unemployment of capital.

Representative CURTIS. I wish the world were that simple, Senator, and I just happen to feel that actually you are going to find your solution in taking little problems one at a time rather than these big, broad approaches.

Senator DOUGLAS. I would just throw this thought in and then I will stop. Reform is a long-range problem.

Representative CURTIS. It should be continued.

Senator DOUGLAS. It is a long-range problem of adjustment and growth. Tax reduction is a short-run stabilizer.

Mr. NATHAN. I would like to say one word. There is no question that the level of taxation in relation to the level of expenditures is important. But I think the composition and characteristics of taxes are also important.

Senator DOUGLAS. It is a problem of to what degree the tax cut does come should you try to amalgamate tax reform into it.

Mr. NATHAN. That is, I think, the real problem. I think we ought to continue toward tax reform. If we are to move quickly, Congressman Curtis, I think we will have to move now toward a cut. I think that is immediate. I am for reform and continued change. You raised the question of the cabaret tax, which I think is important, and in essence——

Senator DOUGLAS. He wants to remove it, not raise.

Mr. NATHAN. Congressman Curtis, what you are proposing in a sense is reduction in price.

Representative CURTIS. Sure. That is what happens.

Mr. NATHAN. And create greater demand. I think we ought to, and I think we ought to cut automobile excise taxes and cut them substantially. I think it would not be inappropriate to go to the automobile industry and say, "You join with the Government and you cut prices," and let the Government cut excises.

This little chart here that the C. E. D. presented shows the change in prices in the 1948 recession, the change in prices in the 1954 recession and the change in prices in 1957. It is about the sixth page or seventh page of this little chart book. It is a very, very revealing one in terms of what is happening now.

By the way, in 1948 we had as strong a labor movement as in 1954. I think what we have is far more monopolistic prices today than then. I think the continued rise in prices is a very disturbing element in this situation.

Mr. RUTTENBERG. I would like to comment on that if I might, Mr. Chairman.

The continual rise in Consumer Price Index during 1958 is in the main attributed to foods, and not because there is any conspiracies involved. The freeze in the Southeast, is responsible for higher fresh fruits and vegetables this year. The long-run drought and what is happening in terms of curtailment of production of beef cattle has produced the highest price for steers on the Chicago market in more than 5 years. These are the basic reasons that consumer prices moved up. It has no relationship to the economy or the unit labor costs which my good friend, Mr. Hagedorn referred to in his opening remarks. This is not the issue.

Senator DOUGLAS. Gentlemen, we can go on for some time but we all have engagements.

Mr. Newsom's eyes have been twinkling very merrily but he has not said a word. Mr. Newsom, do you have any comments you want to add?

Mr. NEWSOM. There was a point I wanted to make with respect to the remark of Congressman Curtis a moment ago, when I did not know how important it was to the immediate concern of this particular committee, and therefore I hesitated to interrupt the discussion, which I was enjoying a great deal.

But lest Congressman Curtis carry away a wrong concept of the situation which he described as a very good income situation in agriculture, "if we were to take inventories and equities into account," I want to respectfully urge you to reexamine your basis for that statement.

On page 7 of the Economic Indicators for April you will find that inventories have been taken into account, in assessing the income situation.

Representative CURTIS. I was mainly thinking of real estate, I might say.

Mr. NEWSOM. Do not be misled by some of these real-estate figures. Incidentally——

Representative CURTIS. How would I be misled by them?

Mr. NEWSOM. You can be misled because it is not farm real estate in all cases.

Representative CURTIS. I realize the suburbanization. If you take the suburbanization out and farm real estate just for farming has gone up tremendously.

Mr. NEWSOM. Mr. Chairman, this is obviously likely to get longer than is justifiable for the subject matter before this committee.

Representative CURTIS. It is very important.

Mr. NEWSOM. I just want to say just recently, 2½ miles out of Fayetteville, Ark., for example, I had pointed out and identified to me two separate plots of ground, each of them less than an acre, that had recently changed hands at a thousand dollars. You know the area as well as I—I expect you do. You know this is a fictitious figure insofar as agricultural equity or agricultural balance sheet is concerned. It does reflect increased costs, incidentally.

Representative CURTIS. Inflation is here.

Mr. NEWSOM. Especially in that we are having farm indebtedness at the highest figure since 1924.

Representative CURTIS. There is an example how crazy it is. Your farm indebtedness is a ratio to farm equity. It has declined from 19 percent to where it is around 8 percent.

Mr. NEWSOM. I would hasten to point out that I am not trying to say we are in as desperate a situation as we were in 1924.

Representative CURTIS. I am trying to say it is a reverse. You have an amazingly prosperous situation where your ratio of your debt to equity has gone from 19 percent to some 8 percent in some 20 years.

Mr. NEWSOM. My expectation is confirmed here. I do not want to give up, because I think that we can produce figures that clearly indicate the Congressman has drawn a totally erroneous conclusion. Obviously it is not too important in this particular meeting.

Representative CURTIS. I think it is very important. The farm economy is part of this. Actually, after listening to the prepared paper by the gentleman, let us say it was read in his behalf, Mr. Baker read it, completely ignoring what has been happening in the farm sector, the farm sector is definitely on the rise and if anyone wants to look at an indicator whether or not the total economy seems to be recovering, certainly there is a recovery in the farm sector. So it is important.

Mr. NEWSOM. I do not happen to have the Federal Reserve balance sheet with me but I do know, if you take the agricultural equity, even out of that figure, and relate it to the change in value of the dollar, your statement is just not true.

Represenative CURTIS. I regret to say, sir, when you deal in percentages you wash out the value of the dollar, because I am relating equity, which is an inflated figure, or deflated, whichever you want, to debt, which likewise reflects the value of the dollar. So your percentages have washed that out and 19 percent compared to 8 percent is a remarkable figure.

Mr. WILDE. I would like to make this observation, although perhaps I should not, because I may say the wrong thing. I just sat through one of these sessions on the Rockefeller report. I got the impression that agriculture was not one problem, but that it was several problems with a great many farmers doing very well relative to their investment and their risk and many millions doing poorly because they had a different situation. It is not one problem.

Representative CURTIS. Very true.

Mr. NEWSOM. It is a very involved problem. We talk of it as a problem, the agricultural problem.

Representative CURTIS. One of the subcommittees of this committee just completed studies on the economic situation in the farm sector and that was one of the very basic points brought out and the second point, which I think is equally important is that there is such a thing as commercial farming.

Mr. NEWSOM. Yes.

Representative CURTIS. And what we call people who live in rural areas who are below the level of commercial farming, and that there is the real problem. Commercial farming seems to be certainly on the upgrade. But we still have a real problem of these rural families.

Mr. NEWSOM. This is another point upon which we could discuss the thing for quite some while but with respect to the point that the Congressman originally made, having to do with inventories and equity, I would only remind him that just last week when I was at an international meeting in Ottawa, I found our Canadian friends are very hostile to us of course on many fronts, but one of their biggest concerns is that our people have been going up there and buying feeder cattle as high as 49 cents a pound, simply because we are desperate to try and take advantage of the low grade feed abundance situation. I am saying to you that this is another indication of how we fictitiously, though temporarily, run up inventory right substantially. Those cattle are reflected in this figure here.

Representative CURTIS. The figures I was giving you are from 1940 to 1947, the two comparisons there, so that washes out those.

Mr. NEWSOM. I just do not want decisions made on the basis of information that I think is totally erroneous. That is all.

Representative CURTIS. I would be very glad to get your figures because what I am quoting are the Department of Agriculture's statistics.

Senator DOUGLAS. If you think it is sufficiently important, Mr. Newsom, have someone prepare your figures for the record.

Mr. NEWSOM. Sure.

Senator DOUGLAS. Is there any further discussion? Mr. Lynn?

Mr. LYNN. No, nothing further. I thoroughly enjoyed this. Based on this discussion the farmer seems to be doing pretty good at the moment.

Senator DOUGLAS. Thank you very much, gentlemen, for coming.

(The following was subsequently received for the record:)

VOLTARC TUBES, INC.,
Norwalk, Conn., April 30, 1958.

HON. PAUL DOUGLAS,
Chairman, Subcommittee on Fiscal Policy of the Joint Economic Committee, Senate Office Building, Washington, D. C.

DEAR SENATOR DOUGLAS: Your invitation to appear at the hearings of the Subcommittee on Fiscal Policy of the Joint Economic Committee is greatly appreciated. Unfortunately, I cannot attend, and, due to the fact that the invitation was late in reaching us, I have been unable to arrange for any other member of the Small Business Coordinating Committee to attend.

However, I would like to submit a brief statement, to be read at the hearing if possible, and if not, to be inserted with this letter in the record. This statement is the one presented by me to subcommittee June 7, 1957. Not only have events since then borne out my warnings, but the statement is even more urgently appropriate today than it was then.

None of the action then recommended, which was so badly needed to prevent the current recession, was then taken. Such action is now vital. In fact, if such actions are longer delayed, the present recession will turn into perhaps the most serious and unnecessary depression in our history.

All of our built-in controls will be powerless to stem the tide if the present downward trends are not curbed by positive, prompt, and substantial Federal policy of the type we urged last June 7.

Very truly yours,

MILES PENNYBACKER.

STATEMENT OF MILES PENNYBACKER

Mr. Chairman, and members of the committee, I want to thank you for the invitation to appear here to discuss fiscal policy implications of the economic outlook and budget developments. I am here as a representative of the Independent and Small Business Coordinating Committee. I am also the president and owner of a small manufacturing company, Voltarc Tubes, Inc., of Norwalk, Conn. We manufacture fluorescent lamps, and products that are used in electric signs.

My statement may be summarized in outline form as follows:

I. Recent trends show some serious soft spots in the economy.

II. Moderate remedial fiscal action now is indicated:

(*a*) Modify the corporate income tax to shift some of the burden from small to large corporations.

(*b*) Reduce taxes on low-income individuals.

III. The possibility of further adverse trends should not be neglected in fiscal planning.

IV. Compensatory spending, and standby tax reductions:

(*a*) Projects that warrant large Government spending should be planned now.

(*b*) The Congress should grant to the President certain standby powers to lower taxes as warranted by economic conditions.

The following will supplement the above outline:

I. *Recent trends.*—Small businesses, and small manufacturers in particular, are now in a period of recession. During the past 4 years of prosperity for big business many thousands of small manufacturers have failed, and the total number of manufacturers has declined. Total failure liabilities in dollars were higher in 1956 than for many years past, they have averaged still higher in 1957. Average small-business profits as a percentage of sales continue to be very low, compared to those of big business. The inequitable results of credit tightening have further restricted small-business activity.

In spite of increases in consumer credit, consumers have by no means been able to increase their purchases to match the increases in our productive capacity. Housing, automobiles, appliances, textiles, and agriculture are some of the important suppliers to consumers that have slowed down.

Consumers have not yet felt the full brunt of the price increases that have in general started with big business and have been absorbed partially by small business. Consumer purchasing power must grow much faster than it has recently if we are to keep employed our growing labor force, with its increasing productivity, and if we are to utilize the enormous expansion of plant capacity that has taken place in 1955, 1956, and 1957. Big-business profits, based to a considerable extent on price increases in those fields of limited competition where administered prices are possible, have stimulated capital investment. This investment (in producers' equipment) grew eight times as fast as the increase in consumption from the fourth quarter of 1955 to the fourth quarter of 1956.

II. *Remedial action.*—A very substantial reduction in the tax on small corporate income, with a change for large corporate incomes from the present 52-percent maximum to a maximum rate of 53 percent, is recommended. This could be done with no decrease in Federal revenue. It would enable small business to compete more effectively and, hence, would tend to eliminate artificially high administered prices.

A reduction in individual income tax in the low brackets is a desirable step to correct the growing imbalance between consumption and production capacity. Any budget deficit this would bring about on paper would be largely offset by the revenue from increased business activity. And any budget deficit remaining could not cause inflationary pricing unless demand should outstrip our capacity, a remote contingency we could correct later if necessary. Some increase in Federal debt at this time is not so serious when it is realized that at the close of 1946 it amounted to 123 percent of our annual gross national product; at the close of 1956 it amounted to only 67 percent.

III. *The possibility of further adverse trends.*—No one has a crystal ball that works. Let's consider the possibility that we may not continue to have major sectors of the economy turning upward as others turn down. It is conceivable that during a period such as the present, when housing, automobiles, appliances, textiles, and agriculture are slowed down, other major sectors may react also. For example, it is an undeniable fact that the billions of added consumer purchasing power that resulted from augmented consumer credit during recent years would be lost if such debt merely stopped expanding. This consumer purchasing would be curtailed still more drastically if people paid off old debts faster than they incurred new ones.

Likewise, further curtailment of inventories, with the resultant loss of production, can certainly take place from the current economic level. Furthermore, there is no law that says capital investment will continue at its present rate, a rate that has already created productive capacity in most manufacturing industries beyond our present ability to buy. Even our spending on national security, considered by some as the most stable prop of our economy, may diminish if our international policies bring constructive results.

These are not predictions. They are possibilities, and it is these possibilities that pose our gravest problems, that deserve our most serious study. In such a study we must recognize what effects a turndown would have on the budget for the fiscal year ending in 1958. The Bureau of the Budget has based its guess on a continued increase in income and profits, an increase that would net about $3 billion of additional taxes. Hence, a leveling off, a plateau, would reduce anticipated revenues by 3 billion. Even a minor drop would mean a real budget deficit unless spending were curtailed. Obviously, a bigger drop in business would mean a bigger deficit.

IV. *Compensatory spending, and standby tax reductions.*—We should be prepared for the deficit mentioned above, and be willing to increase it temporarily by spending and by tax reductions, to increase consumer purchasing power, to provide employment, and to promote economic stabilization. Otherwise, the decline could snowball, leaving us with a much more serious problem.

The spending should be in stages as needed. We should have a series of projects planned and ready, some of which would utilize money and labor effectively at once, others that require more time could be brought along later as the need arose.

The tax reductions again should be for the low income individuals and small corporations. It is these that have the fewest savings, hence they are the ones that will first put tax reductions to use as either increased purchases of consumer goods or increased capital investment as needed. Because action may be needed on short notice, I recommend that carefully defined standby power for such tax reductions be delegated to the President by this Congress.

With advance planning and with a willingness to use our fiscal and budgetary tools as outlined above, the Federal Government can help on the many new schools that are so badly needed, we can build roads and other public works, we can devote more to medical research and to public health, we can give more aid to housing and to the redevelopment of our urban areas. We can help small business and the consumer. We can help make up the many other deficits in our economy, all of which in turn will aid in providing jobs, purchasing power, and economic progress.

(Whereupon, at 12:45 p. m., Thursday, May 1, 1958, the subcommittee recessed subject to the call of the Chair.)

☒