JANUARY 1962 ECONOMIC REPORT OF THE PRESIDENT

HEARINGS

BEFORE THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

EIGHTY-SEVENTH CONGRESS

SECOND SESSION

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JANUARY 1962 ECONOMIC REPORT OF THE PRESIDENT

THURSDAY, JANUARY 25, 1962

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

The Joint Economic Committee met, pursuant to notice, at 10 a.m., in room 1202, New Senate Office Building, Representative Wright Patman (chairman) presiding.

Present: Representative Wright Patman (chairman), and Senator Paul H. Douglas (vice chairman), Senators Sparkman, Proxmire, Pell, Bush, and Javits; and Representatives Bolling, Griffiths, Curtis, Kilburn, and Widnall.

Chairman PATMAN. The committee will come to order.

This morning we begin hearings on the Economic Report of the President for 1962. The first page of President Kennedy's report gives an excellent statement of the purposes of the Employment Act of 1946, as well as the history leading up to the passage of that act, which I will not repeat.

We have with us this morning the Council of Economic Advisers: Dr. Heller, Dr. Gordon, and Dr. Tobin. Gentlemen, I believe you are to be congratulated on your report. It seems to me a very exhaustive analysis. It not only shows an understanding of the purpose of the Employment Act of 1946, the purpose of setting goals for the economy, but it also sets goals and purposes and means for achieving those goals.

This is not to say, of course, that the committee will agree with everything you have proposed, but I think that you are to be congratulated for pointing out matters that need improvement and in making proposals aimed at achieving those improvements.

I believe that congratulations are also due for the high degree of accuracy of your forecast of last year. When you were here last year I believe you predicted that unemployment would not be reduced below 6 percent of the labor force by the beginning of this year, and it has not been. There were also some happier forecasts in your report of last year which also turned out to be approximately correct.

Gentlemen, you may proceed in your own way. Dr. Heller, would you like to begin?

STATEMENTS OF DR. WALTER W. HELLER, CHAIRMAN OF THE COUNCIL OF ECONOMIC ADVISERS; AND DR. KERMIT GORDON AND DR. JAMES TOBIN, MEMBERS OF THE COUNCIL OF ECONOMIC ADVISERS

Dr. HELLER. Thank you very much for your kind comments about the report. If I may, I should like to open with a prepared statement which tries to highlight a few of the points made in the President's report and in our report.

Chairman PATMAN. You may proceed as you desire.

Dr. HELLER. Mr. Chairman and members of the committee, in testifying on the administration's first annual economic report, I should perhaps open with a few words on its approach and composition—what the President's report and the Council's report are trying to do and say. You will have noted that the report has been split into two separate parts. This follows essentially the practice of the early 1950's in contrast with the single Presidential report in recent years. The two parts are:

1. The President's report: This is a broadsweep statement of economic policy, performance, prospects, potential, and program—a report by President Kennedy to the Congress in compliance with the requirements of section 3 of the Employment Act of 1946. In it, the President spells out in considerable detail his legislative recommendations in the field of economic policy.

2. The Council's report: This is a searching—but we hope not forbidding—examination of the rationale of this administration's economic policy—its factual, philosophical, and analytical foundations, its accomplishments to date, its expectations, and its complex challenges for the future.

My brief opening statement is designed, not to summarize the two reports, but, as I mentioned, to focus the committee's attention on a few of the principal facts and issues which shape economic prospects and policies in 1962.

RECOVERY IN 1961

A year ago, the economy was still in the grip of its second recession in 3 years. Nearly 7 percent of our labor force and 20 percent of our industrial capacity were idle. Actual output was running about $50 billion—or 10 percent—short of the economy's potential. The case for expansionary policy measures was clear and compelling.

To provide stimulus and substance for the recovery, the administration early in 1961 took four steps: (1) successfully sought the cooperation of Congress in enacting legislation to expand purchasing power and create jobs; (2) accelerated Federal orders and payments on a wide front; (3) pursued policies to ease money and credit; and (4) followed generally an expansionary budget policy.

With this well-timed and forceful support from Government policy, the U.S. economy again demonstrated its resiliency in a vigorous recovery. By the end of the year, new records were set in production and income—all figures at annual rates:

1. From a recession low of $501 billion in the first quarter, gross national product rose to $542 billion in the fourth quarter. Inventories, Government purchases, and fixed investment, including resi-

dential construction, each rose by $8 billion; consumer expenditures rose by $18 billion; only net exports fell—by $1 billion. That was not because gross exports fell, but because imports rose faster than exports.

2. The industrial production index—1957 equals 100—rose from 102.1 in February to 115.2 in December.

3. Per capita disposable income rose from $1,940 in the first quarter to $2,032 in the fourth, crossing the $2,000 mark for the first time.

4. Wages and salaries and other labor income increased from $281 billion in the first quarter to just over $300 billion in the fourth.

5. Profits before taxes increased from $39.6 billion in the first quarter to an estimated $50 billion plus in the fourth.

6. Farm income—operators' net income from farming—increased from $12 billion in 1960 to $13.1 billion in 1961, an average rise of nearly $350 in net income per farm.

Over this same period, the seasonally adjusted rate of unemployment fell from 6.8 percent in February to 6.1 percent in December, and the number of areas of substantial labor surplus, from 101 in March to 60 in December, out of a total of 150.

Prices, overall, remained remarkably stable for a period of vigorous recovery. For the first time in any postwar recovery wholesale prices fell, by 0.7 percent, in the first 10 months of recovery. The consumer price index rose only 0.6 percent from February to November. Perhaps the word "only" should never be used when the consumer's price index rises at all, but by comparison with past periods this was a modest rise and in considerable part generated from the service side of the cost of living sector.

Finally, confidence in the dollar was restored. In 1961, the overall deficit in our international accounts was cut by about one-third from 1960's level of $3.9 billion, and the deficit in basic international transactions was cut by about two-thirds. Gold losses of $1.7 billion in 1960 were cut in half in 1961.

THE UNFINISHED BUSINESS OF ECONOMIC POLICY

Yet, satisfaction with our progress to date is tempered with concern over the important unfinished business of economic policy.

First, recovery has carried the economy only part of the way to the Employment Act's goal of "maximum production, employment, and purchasing power." Even at $542 billion, production is still 5 percent below the economy's potential; unemployment is intolerably high; and the Nation's purchasing power, or real income, falls correspondingly short. A recovery that carries the economy to full employment and cuts deeply into the bitter core of depressed areas and displaced workers—at the same time continuing to maintain reasonable price stability—is the first order of business of economic policy. Indeed, it is the indispensable first step toward our other economic objectives.

Second, beyond full recovery lies the recurrent risk of recession. The uncomfortable facts of economic history bear witness: our postwar record—though incomparably better than that of the 1930's—has been marred by four recessions, three of them in the brief span of 7 years. More than $200 billion of potential output has been lost in our four postwar recessions. To avoid such losses in the 1960's and beyond—to keep recessions short and shallow if they occur—the President has called for standby programs of accelerated capital improvements and temporary income tax cuts and a strengthened unemployment compensation system.

Third, while moving toward full and sustained use of the economy's present productive capacity, we must also take other steps to expand its future potential. The rate of growth of the U.S. economy in recent years has lagged not only behind its early postwar pace but behind the growth of the world's other major industrial countries. We must make the 1960's a decade of faster economic growth so that we may improve the quality of life at home and meet our responsibilities of leadership abroad. A growth rate exceeding 4 percent will be needed in the 1960's merely to absorb into effective employment the net additions to our labor force. A rate of 4½ percent lies within the reach of private and public policy in this decade.

Fourth, persistent international payments deficits and gold outflows have brought the balance of payments to the forefront of economic policy. We must attain a balance in our international transactions which enables us to meet our heavy obligations abroad without continued depletion of our gold reserves. Simultaneously, we must continue to reduce barriers to international trade and increase the flow of resources from developed to developing countries.

Full recovery without inflation, stronger defenses against future recession, faster growth, balance-of-payments equilibrium, and further trade liberalization—achieved with equity and "in a manner calculated to foster and promote free competitive enterprise and the general welfare," as the Employment Act wisely requires—these are the guideposts of economic policy for 1962.

THE PROSPECT FOR 1962

We look for a further strong economic advance in 1962. Expansion in the first half of the year, supported by inventory accumulation and rising Government expenditures, should be sustained after the middle of the year by a quickening pace of business plant and equipment investment. Unemployment will fall, and profits and labor incomes will rise, as the economy narrows the gap of unused capacity. The year 1962 should see a gross national product of $570 billion—a $50 billion gain over 1961.

POLICY AND PROGRAM IN 1962

Economic recovery to date has been strong, and the outlook is favorable. But to achieve the goals of full recovery, growth, and balance in international payments, the U.S. economy needs (1) more demand now and more stable demand in the years ahead, (2) more investment, and (3) continued price stability. In the rest of my statement, I shall examine the broad outlines of economic policy and program for 1962 in terms of these three requirements. Specific recommendations to carry out this policy and program are listed in the attached summary: "Legislative Proposals in the Economic Report of the President."

1. The U.S. economy needs more demand now and more stable demand in the years ahead. Today business needs more orders, and workers need more job opportunities. Both plant capacity and labor are available to produce more goods and services if only there were

customers willing and able to buy them. As you know, unemployment is currently at the unacceptable level of 6.1 percent. One should also note that the various measures of capacity and operating rates suggest that we are using only about 85 to 86 percent of our industrial capacity today. The preferred operating rate is about 95 percent. This means that a 10-percent growth in industrial output is possible before we reach even the preferred limits of our present capacity. Overall, as we have indicated, there is approximately a 5-percent gap between our present output and potential throughout all sectors of the economy.

In the next 18 months, an expansion of about 10 percent in total demand will be needed if we are to close today's gap in our economic performance and catch up with the economy's ever-growing capacity to produce. Our capacity has been growing at about 3½ percent a year. That means just to stand still, so to speak. The economy has to increase in real terms by something around $20 billion a year.

For this expansion we can and must, of course, rely principally on consumers and business firms. But it is the task of Government fiscal and monetary policy to support and facilitate the expansion of private demand. Federal expenditures will increase moderately, though at a slower pace than in the early phases of recovery. This is appropriate because the very momentum of the upswing now gives private demand greater strength. Since the stimulus of rising Government expenditure will be moderate and declining—it will still be a stimulus, but it will be a falling stimulus—Government monetary and credit policies can appropriately maintain conditions favorable to private borrowing and spending.

Expansion of production beyond the current recovery requires more than the expansion of demand. The economy's capacity to produce must be enlarged, by investment and other measures, to increase productivity. Yet demand must grow too, roughly keeping in step with the growth of potential output—neither outpacing it to cause inflation nor lagging behind it to cause recession and unemployment. This is the long-run task of public policy for economic stabilization. In our view, it is in present circumstances consistent with this criterion to aim at a moderate surplus in the Federal budget when the economy is operating at full potential.

It is not easy to steer the middle course of stability between too rapid and too slow expansion of demand. In our free economy fluctuations in private spending are bound to occur. To offset these swings, or even to arrest and reverse them before they become cumulative, fiscal and monetary policy must be prompt and flexible. The President has made three proposals of the greatest importance to the future stability of the economy: (1) A standby program of public capital improvements to combat unemployment, (2) a procedure for temporary partial suspension of income taxes to buttress private purchasing power when recession threatens, and (3) permanent strengthening of unemployment insurance. (See items I–1, I–2, and I–3 of the attached summary: "Legislative Proposals in the Economic Report of the President.")

The gains from greater stability of the economy are not simply the production and employment which would otherwise be lost in recessions, great as these losses are. Instability also deters future growth by dulling incentives for investing in new and more efficient capacity.

2. The U.S. economy needs more investment. Private investment in plant and equipment in 1962 is a key element in the economic outlook—for full recovery, for economic growth, for improvement in the balance of payments. That is why major policies and proposals of the administration are designed to stimulate investment: enactment of the proposed tax credit for new investment in equipment with an effective date of January 1, 1962 (item IV–1 of the Legislative Proposals); revision of the Treasury's guidelines for depreciation for tax purposes; and maintenance of monetary and credit conditions favorable to the financing of investment.

I would like to refer briefly to the importance of these provisions to recovery, growth, and balance-of-payments equilibrium.

(*a*) Full recovery: To the saving of individuals from higher personal incomes and of corporations from increased profits, the Federal Government in fiscal 1963 will add a surplus of $4½ billion in its budget on national income account. At full employment this surplus would be doubled. Expansion in 1962 toward full employment in mid-1963 will require sufficient strength in investment demand to use the saving which higher personal, business, and Government incomes will generate.

Of the $50 billion increase in GNP projected for calendar year 1962 over 1961, about half will be purchased by consumers and another fifth by Federal, State, and local governments. The remaining 30 percent will be available for increased investment in inventories, housing, plant and equipment, and the like. An expansion of fixed investment outlays will be particularly important in the second half of 1962, when inventory building and Federal expenditure are expected to be contributing less to growth of demand than in the first half of the year.

Recovery itself will powerfully increase incentives for investment, by whittling away at excess capacity and by demonstrating the profitability of new capacity in a fully operating economy. At the same time, positive policy is essential to assure that the high potential saving of the economy is used in productive investment, not wasted in incomplete recovery and prolonged unemployment. If such policy is successfully adopted, the current recovery will pave the way for a higher trend rate of economic growth over the years ahead.

(*b*) Economic growth: Once our idle manpower, machinery, and plant are drawn fully into productive use, growth of production will depend upon growth in our capacity to produce. We will need an expanding stock of plant and equipment to give a rapidly growing labor force the tools to do their jobs. Indeed we will need more than that. Faster growth in per capita income requires faster growth in the productivity of labor. This requires not only more, but better, machinery and equipment to embody in industrial practice the fruits of research and development. And it demands that we provide the improved general education and specific training of our youth, and of many adults, which will equip them for the jobs that technological advance makes available. (Items III–1, III–2, and V–3 of the Legislative Proposals.) Without investment in human talent, investments in technological progress and physical facilities cannot yield their full potential return to the Nation.

(c) Improvement in the balance of payments: The United States must pay its way in the world by earning in international competition a large enough trade surplus to meet our oversea commitments and capital investments. We can earn the required trade surplus only if our products are competitive in price and in quality. By the way, I would like to interpolate that it isn't that our products have not been competitive in the past. We are, after all, exporting something like $20 million a year, about $5 million more than we are importing. We haven't priced ourselves out of world markets, but we need to price ourselves further into them.

To this end, rapid advance in productivity is the ultimate key. Research and investment can keep our products in the vanguard of the technological race, and keep our costs at levels which enable our firms to compete while real wages in the United States steadily advance. But our balance-of-payments position will be damaged if our productivity lags, or if the competitive advantage which gains in productivity might yield is dissipated in excessive increases of money costs.

At present the balance between investment overseas and investment at home is tipped too heavily in favor of foreign investment. One source of this imbalance has been the contrast between excess capacity and correspondingly low profits at home and sustained rapid economic growth abroad. Full recovery in the United States will go far to correct this source of imbalance. The administration's tax proposals and the new trade program are designed to overcome other handicaps which investment at home has been suffering in relation to investment in Europe. (Items IV–7 and V–2 of the Legislative Proposals.)

3. The U.S. economy needs continued price stability. The price record of the current recovery is so far excellent. Demand and production are increasing at a rate which is narrowing the gap of unused potential, without giving rise to bottlenecks, specific shortages, and upward pressures on prices and costs. The budget is appropriately paced for an orderly expansion, with time for the economy's reserves of industrial capacity and manpower to respond to the pattern of rising demands. If private demands should, contrary to expectation, threaten to outrun the capacity of the economy to meet them, monetary and fiscal policies can and will hold the expansion within reasonable speed limits. The administration's programs of area redevelopment, manpower training and development, and youth employment opportunities will help us to avert specific bottlenecks and shortages, by trying to provide in advance plant capacity and skilled labor to do the jobs which an expanding economy will require. (Items III–1 and III–2 of the Legislative Proposals.)

In a free economy, the course of the price level depends not only on Government policy but also on the decisions and negotiations of business firms and labor unions. The President has repeatedly asked that these decisions and negotiations give full weight to the national interest in price stability. Success in stepping up productivity and maintaining price stability can clear the path for solving our balance-of-payments problem in the framework of an expanding economy and capitalizing on the great opportunities and benefits of full recovery and economic growth.

(The proposals referred to are as follows:)

Legislative Proposals in the Economic Report of the President

I. STRENGTHENING OUR DEFENSES AGAINST RECESSION

(1) Provide standby authority for the President to make temporary (6 months) reductions of up to a maximum of 5 percentage points in all individual income tax rates, subject to congressional veto.

(2) Provide standby authority for the President to initiate and accelerate up to $2 billion of spending on capital improvements—Federal, State, and local—such authority to be "triggered" by persistent and substantial increases in the unemployment rate.

(3) Strengthen the unemployment insurance system by providing for an extended benefit period for experienced workers at all times and for all workers in times of high unemployment, by providing incentives to States to increase benefits, by extending coverage to 3 million additional workers, and other measures.

II. STRENGTHENING THE FINANCIAL SYSTEM

(1) Revise the terms of the officers and members of the Board of Governors of the Federal Reserve System, so that the 4-year term of the Chairman will coincide with that of the President, so that the terms of members begin and end in odd years instead of even years.

(2) Raise salaries of members of the Board of Governors of the Federal Reserve System.

(3) Repeal the acts relating to silver of June 19, 1934, July 6, 1939, and July 31, 1946, thus freeing the Treasury from any obligation to support the price of silver.

(4) Repeal the 50-percent tax on transfers of interest in silver, thus fostering orderly price movements by encouraging the establishment of a future market in silver.

(5) Authorize the Federal Reserve System to issue Federal Reserve notes in denominations of $1, thus making possible the gradual withdrawal of silver certificates in the denominations of $1 and $2 and the use for coinage purposes of the silver thereby released.

III. STRENGTHENING OUR MANPOWER BASE

(1) Provide Federal aid for training and retraining of unemployed workers. (Passage of proposed Manpower Development and Training Act.)

(2) Establish pilot programs to expand employment opportunities for young people, including training, employment in public service jobs, and employment in a newly established Youth Conservation Corps. (Passage of proposed Youth Employment Opportunities Act).

(3) Increase appropriation for the U.S. Employment Service, to enable that agency to better fulfill its function of matching available jobs and workers.

(4) Amend the Welfare and Pension Plans Disclosure Act so as (*a*) to provide adequate penalties for embezzlement and (*b*) to vest authority in a responsible Federal agency to enforce the statute by issuing binding regulations, prescribing uniform reporting forms, and investigating violations.

IV. STRENGTHENING OUR TAX SYSTEM

(1) Provide a tax credit equal to 8 percent of gross investment in eligible machinery and equipment, thus stimulating investment in capacity expansion and modernization by reducing the net cost of acquiring new equipment.

(2) Make dividend and interest income subject to withholding.

(3) Repeal the $50 dividend exclusion and the 4-percent dividend credit.

(4) Revise tax treatment of business deductions for entertainment, gifts, and other expenses, to stop abuses of "expense-account living."

(5) Eliminate the special tax preference for capital gains from the sale of depreciable property, real and personal.

(6) Remove unwarranted tax preferences to (*a*) cooperatives, (*b*) mutual fire and casualty insurance companies, and (*c*) mutual savings banks and savings and loan associations.

(7) Revise tax treatment of foreign income, to remove unwarranted incentives to the export of capital.

(8) Extend the corporate income tax and certain excise taxes for another year beyond June 30, 1962, except that certain taxes and charges related to the use of airways and waterways should be revised so that users of these facilities carry a larger share of the costs.

V. OTHER LEGISLATIVE ACTION URGED IN THE ECONOMIC REPORT

(1) Enact enabling legislation for U.S. participation in the recent agreement among 10 major industrial countries to lend specified amounts of their currencies to the International Monetary Fund when necessary to cope with or forestall pressures which may impair the international monetary system.

(2) Enact new trade legislation to facilitate negotiation of reciprocal tariff reductions with the European Common Market.

(3) Provide Federal aid to education, including assistance to States for provision of more adequate public school facilities and higher teachers' salaries and—at the higher education level—loans for construction of facilities and for scholarships to able students who need help.

Chairman PATMAN. Senator Douglas.

Senator DOUGLAS. Mr. Chairman, I have a question. Mr. Heller, you are expecting in your estimates, as I understand it, an increase in the gross national product from an average of $520 billion for calendar 1961, to an average of $570 billion for calendar 1962; is that correct?

Dr. HELLER. That is correct.

Senator DOUGLAS. That is an increase of $50 billion or between 9 and 10 percent?

Dr. HELLER. Yes, sir.

Senator DOUGLAS. And what would the figure be for the last quarter of 1962?

Dr. HELLER. The last quarter would run between $585 to $590 billion.

Senator DOUGLAS. As compared to $540 billion for the last quarter of 1961?

Dr. HELLER. $542 billion for the fourth quarter of 1961.

Senator DOUGLAS. Do you think this is too optimistic an estimate?

Dr. HELLER. We don't believe so, Senator, or we wouldn't have made it.

Senator DOUGLAS. I understand. I think the country wants a justification for it.

Dr. HELLER. As we have pointed out in the report, we look forward to about a half of the total $50 billion increase in GNP taking the form of increased consumption as consumer spending keeps pace with disposable income.

About one-fifth of the $50 billion total is made up of increases in Government purchases at all levels of government, and another fifth, private fixed investment. The remainder would be found very largely in expansion in inventory. There will be some expansion during the coming year in residential construction and plant and equipment investment which may taper off beyond midyear.

Senator DOUGLAS. Dr. Heller, how does this percentage increase in gross national product which you estimate for the calendar year 1962 compare with the increase for calendar years 1955 and 1959? This is a fair comparison as they were recession recovery years, just as you expect calendar 1962 to be a recovery year from the recession year of calendar 1961. Proportionately, what were the increases in this year?

Dr. HELLER. The figures on that, Senator, show that, in the calendar year 1955, gross national product grew 9½ percent over 1954. In 1959, it grew 8.6 percent over 1958. Our estimate for 1962 is a growth of 9.4 percent over 1961.

Senator DOUGLAS. But you had a rapid increase in the last quarter of 1961; isn't that true?

Dr. HELLER. Yes, sir; it is.

Senator DOUGLAS. So that from quarter to quarter, from the last quarter of 1961 to the last quarter of 1962, your estimate of the increase is slightly less than occurred in the previous recovery periods, isn't that right?

Dr. HELLER. I believe that is correct.

Senator DOUGLAS. So that you have left yourself some margin of safety, not a large one, but some margin of safety.

Dr. HELLER. I might say also that in spite of the very substantial expansion in profits that is forecast for this year, that, too, is a smaller percentage increase from one year to the next than previously.

During the last two recoveries, profits in the first full expansion year increased by 32 percent and 25 percent, and our estimate for this year is 22 percent.

Senator DOUGLAS. Well now, Mr. Heller, I noticed in your report, and I was very glad to see you take this position, that you are concerned with the fact that the relative volume of unemployment still remains high in spite of the fact that we are in a period of revival.

The unemployment percentages issued by the Department of Labor in cooperation with the Census Bureau have been over 6 percent for 15 months during this period of revival. If you take into consideration the full-time equivalent of part-time unemployment, that raises the figure almost 2 percent more. If you use as your denominator, not the total working force, but exclude the self-employed, the numbers who seek wage and salaried labor, and I think that is the best denominator, would be up another percent or more, and the figure is somewhere between 9 and 10 percent.

Now, this is a tremendous amount of involuntary lost time. I wonder what you think the country can do about it?

Dr. HELLER. As you noted, we have expressed, and the President has repeatedly expressed, deep concern over the continuation of these high levels of unemployment. It is part of our projection for 1962 that these levels will in the normal course of recovery diminish considerably.

Senator DOUGLAS. Would you say 5 percent at the end of this year?

Dr. HELLER. By the middle of 1962, somewhere between 5½ and 5 percent, and further improvement by the end of 1962.

Senator DOUGLAS. Do you estimate a 4-percent figure, if the revival continues to the midpoint of 1963?

Dr. HELLER. If the revival continues at roughly the same pace, or even at a slightly diminished pace as it usually does in the advanced stages of recovery, on into mid-1963, this would bring us to the interim objective of 4-percent unemployment by mid-1963.

Senator DOUGLAS. I suppose if you allow for full-time equivalent of involuntary part-time work, and use as the denominator those seeking wage and salary labor rather than the total working force, this would still be somewhere between 6 and 7 percent?

Dr. HELLER. About 6 percent, Senator, according to these figures.

Senator DOUGLAS. Suppose you don't reach these goals? One must always have plans ready in case the program of attack doesn't succeed.

Dr. HELLER. That is correct.

Senator DOUGLAS. Do you have any plans that you want to reveal or do you think it is wise not to discuss them?

Dr. HELLER. I don't want to suggest, Senator, that we have some hidden weapons or secret weapons that are in reserve for this purpose. Weapons are available that I think are familiar to this commitee and to all of us. For example, monetary ease: If the recovery is not as vigorous throughout 1962 and 1963 as anticipated, one of the weapons would be monetary ease.

Senator DOUGLAS. That involves Federal Reserve policy to increase the lending capacity of the banking system, to be effected either by open market purchase of Government securities or by lowering the reserve ratios.

I hope the former would be used rather than the latter. Has the Federal Reserve Board contributed to monetary ease during the last calendar year?

Dr. HELLER. Yes; it did.

Senator DOUGLAS. In what way?

Dr. HELLER. It did so primarily by holding the level of free reserves at approximately half a billion dollars throughout the period, even in the latter part of the year when there were very substantial demands on funds.

It also moved into a broad spectrum of purchases from not only the short end but the longer end of the Government securities market.

Senator DOUGLAS. It has abandoned its historic policy of purchasing bills only and is now purchasing securities in excess of 15 months' duration?

Dr. HELLER. Yes; it is doing that, according to what the current economic situation requires.

Senator DOUGLAS. And have the total holdings of the Federal Reserve System in Government bonds increased during this time?

Dr. HELLER. May I refer that question to Dr. Tobin, who has been studying these data?

Dr. TOBIN. Over the full year 1961, the Federal Reserve purchased $2.6 billion of securities with maturities of more than 1 year. They sold $1.1 billion of securities with maturities of less than 1 year, so their net purchases over the year were $1.5 billion.

Senator DOUGLAS. And assuming that there is a 6-to-1 ratio, that is of the lending capacity of the banks as compared to Federal Reserve purchases of bonds, this would increase the lending capacity of the banks by around $9 billions.

Dr. TOBIN. There are offsetting determinants of the reserves of the banks, but the net increase in reserves, if you take other things into account, was about $1 billion.

Senator DOUGLAS. Now my time is about up, but let me ask you this question: It has been said by some in the past that an increase in the lending capacity of the banks would lead to an increase in the price level, because the total quantity of the monetary medium would rise. Of course, this is not necessarily true. Has there been any increase in the price level during this past year?

Dr. TOBIN. Not appreciably.

Senator DOUGLAS. I mean wholesale prices.

Dr. TOBIN. Wholesale prices have actually fallen during the year.

Senator DOUGLAS. What about consumer prices?

Dr. TOBIN. Consumer prices have risen by a very modest amount, less than 1 percent.

Senator DOUGLAS. About one-half of 1 percent?

Dr. TOBIN. About seven-tenths of 1 percent.

Senator DOUGLAS. And this could be accounted for by an improvement in quality, could it not?

Dr. TOBIN. Well, it is very difficult to make an assessment.

Senator DOUGLAS. But the increase is almost entirely in the field of services, is it not, rather than in the field of commodities?

Dr. TOBIN. That is correct.

Senator DOUGLAS. So you feel that you have gone through the year with price stability?

Dr. TOBIN. Senator, you referred to the theory that increasing the volume of money would necessarily lead to an increase in prices, but generally one would expect that to occur only if the economy were fully employed and fully utilized, and where there is idle labor——

Senator DOUGLAS. What has happened is that the economy has moved upward as the total amounts of goods and services have increased.

Dr. TOBIN. The expansion has been an increase of production rather than an increase of price.

Senator DOUGLAS. I have always felt that people afraid of monetary expansion do not consider this factor, that you can also get an increase of production to take care of this.

Chairman PATMAN. Senator Bush is recognized.

Senator BUSH. Mr. Chairman and gentlemen of the Council, I want to congratulate you and congratulate the President on the excellent statement which you have made, with respect to the Nation's economic goals, in your Economic Report of the President.

I wish to emphasize agreement with the President's statement on pages 7 and 8 of this report and the unfinished business of the economic policy including first the achievement of full employment, and secondly prosperity without inflation. Then there is the acceleration of economic growth and the extension of equality of opportunity and the restoration of the balance-of-payments equilibrium.

We may find some disagreement over the methods of achieving these goals and undoubtedly there will be some but I agree with the importance of achieving these goals.

I am glad to note the emphasis which you place on price stability throughout both the President's report and the Council's report. The President said on page 8 of his report—

> We must seek full recovery without endangering the price stability of the last 4 years.

And the Council said on page 38:

> The necessity of moving toward balance in U.S. international accounts has given price stability new and compelling importance as a requirement of economic policy for recovery and growth.

In view of these very forceful statements, is the administration or the Council prepared to recommend enactment of Senate bill 144, which is designed to amend the Employment Act to make the maintenance of reasonably stable price levels an explicit aim of the Federal economic policy?

I might say that I introduced that bill on several occasions and it is pending now before the Senate at some level. I am not quite sure why, but it is not getting much attention. In view of the great stress that you lay on this point, and I agree with you, I ask you, would it not fortify you if the Congress were to make this an explicit aim of our economic policy by law, just as the Employment Act of 1946 is designed?

It seems to me that it fits in exactly with the purposes of that act and it seems to me from what you have said that that is so. Would you endorse or would you recommend to the Congress that it adopt that?

Dr. HELLER. Senator Bush, I would say first of all that we think the Employment Act of 1946 is by and large a very effective "constitution," so to speak, in the field of employment policy, and that the price stability objective seems to us to be clearly implicit in the 1946 Employment Act. If we are going to maintain maximum production and employment and purchasing power, I should think that price stability is one of the prime requisites, as indeed we have said on many occasions.

Senator BUSH. Are you afraid that putting this in the law would inhibit the administration in connection with implementing this policy which you state so firmly and correctly is most important?

Dr. HELLER. No, sir; I don't think it would inhibit the policy at all. I just think that this is a provision which really would be an interpretation of something that is already very clearly implicit in the act. Therefore it is not a necessary addition to the "constitution" in the field of economic policy.

Senator BUSH. I can't agree with you that it is so clearly implicit in the act. I think that is an interpretation. But you keep emphasizing it and I congratulate you on it. I think you correctly emphasize the importance of it.

Don't you think it would have a good psychological effect on the whole country if the Congress were to fortify you in your position on this matter by adopting that amendment to the Employment Act?

Dr. HELLER. I think that there might be some psychological advantage in reemphasizing it in that way. On the other hand, the process of amendment of an act is a serious one. It is one that I think should be undertaken primarily if there is a basic defect in the act. I don't believe that the act is basically defective in leaving out explicit mention of price stability.

Senator BUSH. Well, in other words, you do not choose to endorse that bill, that amendment to the act?

Dr. HELLER. I would say, without opposing it, that I do not endorse it.

Senator BUSH. Now turning to another subject, I certainly congratulate you in the thorough analysis of the balance-of-payments problem and the importance which you attach to it. I fully concur that it is an overridingly important matter affecting all of these matters.

I want to ask you just one or two questions. I don't have very much time but I want to ask you this question. This seems to be implicit in the President's approach to this problem. He seems to feel as though supporting his trade plan—which, incidentally as it is about to be published, is a great improvement over what we were given last autumn to believe was to be the plan and I certainly welcome the modifications of it that I have seen in a statement which I believe is to be released shortly—assumes, I believe, that a mutual lowering of tariff barriers with the Common Market will sufficiently expand U.S. exports to make a significant contribution to the closing of the balance-of-payments deficit.

We have just concluded a 20-percent reduction with the Common Market. What effect do you think that this is likely to have in 1962?

Before you answer, I would like to call your attention to a comment on this point which I saw in yesterday's paper by the National Foreign Trade Council. I will just read briefly from that statement.

They say that the council, a leading organization in the foreign field, forecast yesterday U.S. commercial exports would set a new record of $20,500 million in 1962. A continuing deficit in this country's balance of international payments this year at almost $3 billion, unless tripled by special developments, also was predicted by the trade group.

Among the council's forecasts, which are made each year by a committee of experts, was one for a sharp rise in imports to about $16,300 million for 1962.

In other words, they suggest a larger rise over 1961 in imports as against exports. This would seem, if these figures are at all reliable, not to be of any assistance in closing the balance-of-payments deficit but would seem to suggest an increase.

This same danger point, so to speak, was pointed out in the hearings of the Boggs' subcommittee of this committee last December 4, 5, and 6.

It was pointed out that in the growing economy which you so confidently predict—and I hope you are right—our imports are likely to rise more than our exports, thus narrowing the trade balance and aggravating the total balance-of-payments problem.

Would you comment on that, sir?

Dr. HELLER. Senator, I would like to make a separate comment and then ask my colleague, Mr. Gordon, to comment further.

As you correctly point out, recovery typically worsens the trade balance in the sense of narrowing the gap between our imports and our exports. We have already had a rise in our annual rate of exports from $19.8 billion early in this year, to something over $20 billion, and there will be some further rise as recovery quickens the pace of activity and draws in more imports.

Probably the largest part of the rise in imports of this recovery has already taken place, as inventory restocking and other similar adjustments have already occurred.

At the same time, however, we have had a continued increase in exports. The question is what the new agreement and the prospective agreements with the Common Market under the legislation that the President is spelling out today will do to the longrun picture. There the assumption—and I think it is one which can be thoroughly documented—is that exports will increase in the long run. These agreements have every likelihood of increasing our exports more than our imports because we would be pulling down the tariff barrier around a growing Common Market, within which there is increasingly free trade.

In effect, we have to disentangle the shortrun recovery effects, not all of which are bad, from the longer run trend which we think will be improved by both the current and future agreements.

When I say not all of the short-run effects are bad, I refer to the fact that the attractiveness of investment in the United States compared to abroad, will, of course, increase as our level of profits before taxes rises from this year's level in the midforties to next year's level in the midfifties—around $56 billion.

I would like to ask Mr. Gordon to comment further on this.

Dr. Gordon. Specifically, Senator, on the relationship between the President's trade program and the balance of payments, I don't think that, as you say, the trade program in itself constitutes a full solution to our balance-of-payments problem.

Senator Bush. I wasn't suggesting that. But it is a very important element.

Dr. Gordon. It is precisely for that reason, I think, that the President's statements with respect to balance of payments have stressed such a wide range of measures that have to be taken to deal with the problem.

But specifically on the relationships to the trade program, I think we have to bear in mind that if we do nothing with respect to the Common Market situation, the discrimination against U.S. exports to Western Europe will steadily increase as the external tariff remains unchanged and as the internal tariff diminishes. As the internal tariff goes down, the German competitive position in the French market will become steadily more favorable relative to the U.S. position in the French market. So it does seem to me imperative that we push ahead with an effort to lower very substantially the external tariff of the Common Market.

This, of course, also has implications for capital movement, for direct investment. In the absence of an effective program to reduce the level of European external tariffs, the temptation for U.S. manufacturers who are attracted by the growing market of Western Europe to enter this market through direct investment in Western Europe will remain undiminished.

In other words, the choice between exporting to meet this demand and investing in Europe to meet the demand will be heavily in favor of investing, whereas the steady lowering of the external tariff in the Common Market will favor U.S. exports to Western Europe as opposed to U.S. direct investment in Western Europe.

I think it ought to be said that other measures with respect to our trade position are important, although perhaps not quite as important as the President's trade proposals. We are continuing to seek steady reduction in such discrimination against U.S. imports as remains in Western Europe and other parts of the world. The export campaign, reinforced by such things as the new program of export credit insurance, attributes to this.

And I think that although the trade program itself is central, these other measures which have been proposed, which are underway, are contributing to the same effect.

Chairman PATMAN. Without objection, we will stand in recess for 5 minutes.

(A brief recess was taken.)

Chairman PATMAN. The committee will please come to order.

Congressman Bolling is recognized.

Representative BOLLING. Thank you, Mr. Chairman.

Mr. Heller, I would like to follow up a little bit on the colloquy that you had with Senator Douglas involving your estimates of unemployment through the end of this year and to the middle of 1963. If I remember correctly, you suggested that we would be down to about 5 percent unemployment at the end of this year and perhaps reach 4, was it, in mid-1963?

Dr. HELLER. That is with the very substantial proviso that the rate of expansion in the economy continues into the first half of 1963 at about the rate of the second half of 1962.

Representative BOLLING. The point that I would like to get at is that at some point in that colloquy Senator Douglas raised a question as to what weapons you had, or were thinking about, if the estimate proved overly optimistic. I would like to inquire of you as to how effective and how important you feel some of the items listed in the legislative program of the President would be in this case, in the event that your estimate proved overly optimistic.

There are a variety of proposals in the President's program, such as standby authority for reductions up to 5 percentage points in all individual income tax rates, the standby public works, the improvement in unemployment compensation, Federal training and retraining, and a whole variety of things.

What I am curious to know is whether you feel that if these things were in law they would very much strengthen your hand, or the hand of the administration, in the event that your estimates were overly optimistic.

Dr. HELLER. Congressman Bolling, I appreciate the opportunity to expand the answer to Senator Douglas' question, because we really only talked about the first part of possible policy for expansion in case the estimates for this coming year are not realized.

Before addressing myself specifically to this program, I should note two things: First of all, the President has pledged that if the recovery was not satisfactory, he was prepared to take additional measures to stimulate a full recovery; secondly, the budget is set to balance on an administrative basis at a level of $570 billion. If there should be a substantial shortfall from that figure, the budget itself would, of course, have a more expansionary effect than it is presently planned to have because revenues would fall short of expenditures and a deficit would automatically be generated. On the other hand, if expansion were more vigorous than we have anticipated, it might generate some inflationary pressures and the budget would go into larger surplus and have a restraining effect.

Such budgetary flexibility is part and parcel of the stabilization policy of this administration. As far as the specific legislative proposals are concerned, if the economy should actually turn downward—which, although we do not anticipate it, is always a possibility that policy has to take into account—economic policy has to be flexible and to be prepared for the unexpected—then in precisely that kind of situation the three types of special antirecession authority the President is requesting would be most helpful.

If he had the strengthened unemployment compensation system, which would automatically go into effect, rather than waiting upon temporary unemployment compensation legislation by the Congress; if he had standby authority for a quick, partial suspension of income tax rates; if he had standby authority for well-timed and well-placed public capital improvements, which could be invoked upon the development of a recession—in that event we would certainly be much better buttressed against adverse economic developments.

Representative BOLLING. Then, in effect, the answer to the question Senator Douglas originally posed as to what weapons you have will depends a great deal upon what Congress does with the President's program?

Dr. HELLER. Yes, indeed. Our weapons against recession are heavily dependent upon congressional action on this program. The moment you get beyond monetary policy, where the Federal Reserve does have discretionary powers, the effectiveness of Government policy to combat recession is always very dependent on the Congress.

Of course, we were addressing ourselves primarily to a potential recession, which, as I say, we do not foresee within the 1963 fiscal year.

At the same time, there are other Government policies which we feel would be aiding the expansion during that period, some of them involve strengthening the manpower base; some of them involve taxes—particularly the passage of the investment credit which, if enacted promptly and made retroactive to January 1, might have a stimulative effect that could add as much as $2 or $3 billion to the gross national product in 1962.

Representative BOLLING. Thank you.

Mr. Heller, on page 77 of the report, you have a very interesting discussion of the budget. I find that in talking with my constituents there seems to be a tremendous amount of oversimplification in the public mind, at least, in dealing with this problem. I want to compliment you on that section of the report because it brings out very clearly that there are a variety of budgets and that the budget is a great deal more than the symbol it has become in, let's say, political terms. I have been extremely disturbed by the general public's acceptance of the notion that there is something almost sanctified in a balanced budget, and I have also been very much disturbed by the general view that our public debt is in a dangerous situation.

My own view is that the budget basically involves a very complicated set of tools and that the public debt is no great threat to our economy at its present level.

I wonder if you would agree that the notion of the public debt as a problem that may destroy our economy is not accurate.

Dr. HELLER. I would agree entirely that put in those terms it is a misstatement of the problem of the public debt. The public debt as a proportion of our gross national product, or of our national income, has been shrinking steadily since the end of the war. The public debt in relationship to national income has dropped from 1½ times the year's national income in 1946 to less than three-quarters of the year's national income today. What this means is that by the growth of the economy and, indeed, to some extent in the earlier postwar years by increases in the price level, the public debt has been cut down to size.

It does not mean that there are no problems associated with the debt. All it means is that it is a problem which is manageable and that it is a diminishing problem in relationship to the tremendous and growing strength of the economy.

Representative BOLLING. A much smaller debt today than we had in the immediate post-World War II period, relative to other economic facts of life.

Dr. HELLER. Less than half the size in relation to GNP.

Representative BOLLING. One more question, Mr. Heller, on an entirely different subject.

I have always been very much concerned about the general problem of economic growth, and at one time considered the possibility of proposing an amendment to the Employment Act to make that explicit. It is a very curious fact that although there was a great deal of discussion of growth in the consideration and early drafting of the Employment Act, it doesn't appear: That is, the idea of economic growth does not appear specifically in the Employment Act.

I have restrained myself and have not proposed an amendment to the act to include growth specifically, because it is included very clearly by implication. Would you agree that in view of this, it would probably not be worthwhile to include that phrase specifically?

Dr. HELLER. I would agree entirely. In the same way that I responded to Senator Bush's question about price stability, I feel that economic growth is thoroughly implicit in the phrase "maximum employment, production, and purchasing power."

Representative BOLLING. Thank you, Mr. Heller. My time is up.

Chairman PATMAN. Congressman Curtis of Missouri.

Representative CURTIS. First, Mr. Chairman, I want to compliment the Council for an overall very good job in this report.

I find that it is sufficiently clear so that we can point up differences. There is, however, one point about which I would raise serious question and that is the claims of the administration for their actions relating to the recovery.

The Council very properly points out that February of 1961 was the bottom of this recession and we began climbing out from that point. This is obviously long before any action taken by the administration could have had any impact upon it.

I regard that portion of the report as political and not justified by the economic facts.

There is one thing that I want to direct primary attention to, because it is one of great concern. It is this problem of employment and unemployment. The thing that I regret is not in the report, and I regret it is not in our economic statistics, is an attempt to estimate the number of jobs that are going begging. There is always emphasis on the unemployment sector, but we all know that anyone can just read the Sunday papers and look through the want ads and begin to get some concept of the tremendous number of jobs that people are just not there to fill. We have talked about the lack of teachers, nurses, doctors, and technicians of various sorts. It seems to me in the study of our economics we ought to be trying to evaluate just how much there is in this area of the skills that is going begging. I wonder if you would comment on that.

Dr. HELLER. I would be glad to, Congressman Curtis.

If I may, may I just, however, comment first on your opening remarks?

Representative CURTIS. Certainly.

Dr. HELLER. I would like first of all to thank you for your compliments about the report, and secondly, to state that our treatment of the relationship between the administration's programs and the recovery was, in our view, a strictly economic one, not a political one. There is no claim made, Congressman Curtis, that the economy would not have turned up in any event. The claim is made, however, that the strength of the recovery was very substantially affected by the measures that the administration took.

Representative CURTIS. Dr. Heller, if I may say, in your report, later on in the full report, I agree that there is that modest language, which I commend. But I regret to say that I think anyone who reads the front part of the report would not find that modest a claim at all.

Dr. HELLER. Turning to your question about the unfilled vacancies and the problem of fitting the available labor force to the jobs that are open in the economy, I would like to point out, first of all, that the relationship between unfilled vacancies and employment and unemployment seems to be a relatively stable one over time. In other words, there are always unfilled vacancies.

Representative CURTIS. But, Doctor, this is what I was referring to, if I may interrupt to clarify it: Why don't we attempt to make estimates of how many of these job vacancies there are? We know about it in a general way. Granted, it is more difficult to find where these jobs are than it is to look for the person who is unemployed, because that is attached to the human being.

All of these unfilled jobs are not attached to the human being, so they are not called to our attention so much. But the real question is: Why, in our economic statistics, don't we make an attempt to evaluate how big is this area of unfilled jobs?

Dr. HELLER. You are raising both a statistical and a substantive question.

Representative CURTIS. That is correct; yes.

Dr. HELLER. The statistical question you are raising is a very relevant one. Many of the European countries do collect information on unfilled vacancies. Indeed the Presidential Committee to Appraise Employment and Unemployment Statistics, which is headed up by Prof. R. A. Gordon of the University of California, is looking into the feasibility of collecting more effective statistics—more than just from the want ads of newspapers—on this problem.

It is a good deal more difficult to do this in this country because of the way we keep our statistics and do our reporting than it is in some of the European countries which have been doing it in this fashion for many decades.

Secondly, on the substantive side, of course a good part of the President's program on strengthening the manpower base is designed precisely to get a better fit of our working population to the job vacancies. That applies both at the youth education level and in the training and retraining programs. These are designed to improve the mobility and the skill structure of the labor force so that there will be a better fit to the available jobs.

Representative CURTIS. That part of his program I highly commend. As a matter of fact, I have been trying to get our attention directed to this area for many years. I am happy to see it.

Now let us direct further attention to another matter.

I was very disappointed to see claims of credit for the decrease of the unemployment rate from 6.6 to 6.1. Actually it was 6.6 in January, and it dropped to 6.1. This is what I want to call attention to, but I will refer first to some testimony last year by Dr. Clague, who suggested that if our economy was going to grow properly we would have 1 million more jobs in the year 1961.

Supplement A to your statement last year before this committee refers to that and suggests, I think I am reading accurately from last year's supplemental report, that—

> This shortfall is attributable to the disappointing performance of the economy. Many people stayed out of the labor market although they would take employment if jobs were available.

Now, let me direct attention to the employment figures: the civilian labor force of December 1960 was 70,549,000 and December 1961, 70,559,000.

Let me throw another fact into consideration, which, to me, is even more disconcerting. Taking the economic indicators on unemployment for January, we find that in October of 1961 the military force was 2.5 million. In November and December, when you show this drop from 6.8 to 6.1, the military went up to 2.8.

In other words, 300,000 people went into the military force. As many people commented, it looked like that was one way of opening up jobs in the civilian sector.

All I want to call attention to is that I think we must relate the employment factor to our defense and our military posture. There has been no reference at all to that factor in here.

One other thing for your further comment is this: I don't have the exact figures of the increase in Federal employment since January 1961, but I think the figure is around 75,000. No reference is made to that.

What I am pointing up is that I don't think that the recent little drop in unemployment in the month of November and the month of December, in the light of these other factors, is anything that we can be too happy about, the main factor being that the number in the civilian labor force is almost exactly what it was in December 1960.

Dr. HELLER. Well, again, Mr. Curtis, you are putting your finger on a problem that is disturbing to us all. That is, in pointing to the improvement from 6.8 percent in February, the trough of the recession, to 6.1 percent in December, in the seasonally adjusted unemployment rate, we have at the same time indicated that this is still an intolerable and unsatisfactory level of unemployment.

Representative CURTIS. Do you think that is the case in light of the military increase, because it occurred just in that month, the month when the decrease occurred, when you had the callup of some 300,000 people?

Dr. HELLER. I am sure there was a combination of factors that improved the figure so suddenly, some of which are the improvement in the business situation, some which are the military callup, and I am sure, seasonal developments.

Representative CURTIS. But the military callup is just a bald figure. That is the dramatic thing. Your figures all through the year have run, incidentally, 6.6, in January, 6.8, and then it goes up to 6.9, then 6.8, then 6.9, 6.8, 6.9, 6.9, 6.8, 6.8, and then you call up the Reserves of 300,000 and it becomes 6.1. I just think that your report, in claiming all this credit, and it is claimed throughout the report on this just recent drop, without a reference to the biggest factor—and maybe there were other factors, too—is not correct.

The other comment is that I do think some attention should be directed to the increase of the Federal Government employment; I think I am right in saying that it was around 75,000. That, too, is not too encouraging from this employment-unemployment picture. But, above all, you haven't increased the labor force and yet our population has continued to increase.

Dr. HELLER. You have raised a whole series of issues. I think two or three comments are in order. One is that, of course, there has been, along with the $40 billion increase in gross national product, a consistent rise in nonagricultural payroll jobs during the year. There has been a rise of 1 million jobs in the civilian nonagricultural economy.

Representative CURTIS. But not overall.

Dr. HELLER. In terms of the nonagricultural sector, yes.

Representative CURTIS. In our whole economy you have lost them. I would like us to get into the components of the work force. We are talking about total work force. These figures are gross figures. But you have lost the million men in the other sector.

Dr. HELLER. Mr. Congressman, we have to distinguish between the number of people at work and the number of people in the labor force. I was going to make a second comment.

The number of people at work in the nonagricultural sector of the economy has increased by a million. At the same time, you are quite right that the labor force has not expanded either to our anticipations or to any other projections that have been made of the labor force.

I don't pretend that we have a pat explanation of that very slow growth. A yearly increase of only 10,000 workers is statistically insignificant. There are some special factors that do enter in, however. Part of this small increase stems from the military callup, which I think withdrew about 300,000 net from the labor force during the year. Another part is that about 500,000 in the agricultural sector have dropped out of the labor force, which accounts for 800,000 withdrawals from the labor force. But the full explanation, I think, won't be known for some time to come.

We assume that as employment opportunities continue to improve there will be a dual movement, one into additional employment and the other into the labor force as some of the wives in the economy come back into the labor market actively because of better employment opportunities.

Representative CURTIS. This is the area to which, in my judgment, most attention needs to be directed. To my own thinking, in this dynamic economy automation actually creates more jobs than it displaces and, therefore, our emphasis must be on locating these jobs that are created and giving our people training for them. We still don't have them in our national statistics nor are we gathering this kind of information so that we can evaluate this affirmative aspect.

Our concentration has all been on the area of unemployment. I would like to direct our attention to this area of skills that we need, which are going begging. That will direct our attention to an area which will expand our economy, I think, and also open up jobs for the people who have lost their jobs.

I have one other comment. The unemployed are largely concentrated in the unskilled and semiskilled areas. The high school dropouts are not the ones that will take the jobs that require the higher skills. It is a process of upgrading someone with a job to train for a higher job, thus leaving a job open for someone down the ladder. Would you not agree that that is our particular problem?

Dr. HELLER. I agree thoroughly. I don't think we should close this phase of the discussion, however, without saying perhaps two things: One, that we agree with you entirely, that we should accentuate the positive in employment policy; and, secondly, accentuation of the positive means accentuating the creation of sufficient demand in the economy, sufficient jobs so that you will draw into productive employment the people who are available for employment.

Representative CURTIS. That is true. There is a big demand already there. That is the point I am directing attention to, and we haven't even identified the demand that exists for these skilled jobs. That is why I have dwelled upon this point.

The other thing, and I will conclude as I see my time is up, is that an undue concentration on what the Federal Government does at the sacrifice of what goes on in the private sector is, in my judgment, a grievous error. That is why I called attention to what I thought was a political observation in the report when it was really our great economy that moved out of this recession. Certainly the Federal Government can assist, but it can, in my judgment, never do more, really, than be of assistance.

Chairman PATMAN. Senator Sparkman is recognized.

Senator SPARKMAN. Thank you, Mr. Chairman.

Dr. Heller, I shall be very brief in my questioning. I want to join with the others who have commended you and your associates for a very fine report, a very clear report, and I think, a very encouraging report and one that you well substantiate with the facts that you bring forth.

Let me ask you just this one thing to see if I understand correctly: You do predict a continuing uprise in the economy, and you predict also that you will be able to have that uprise while maintaining price stability. In other words, you do not feel that we are in any great danger of inflationary pressures?

I am correct in that?

Dr. HELLER. That is correct, Senator. We feel that on both counts—that is, what is normally thought of as "demand-pull" inflation and what is termed "cost-push" inflation—we have a favorable setting for a continued price stability.

What is on one hand a vexing economic problem of unemployment and of unused industrial capacity, and of the gap between our actual performance and our potential performance is, on the other hand, of course, a very considerable built-in protection against price inflation.

As demand increases the response can be one of higher production, higher income, and higher employment, rather than higher prices.

Secondly, on the side of price increases induced through market power, either by management or labor, there is every indication of a moderating in price and wage advances. Advances in wages have been staying within the bounds of productivity increase, and consequently, given a continuation of the basic trend—to which there are exceptions, obviously—which the overall figures for manufacturing show for the past 4 or 5 years, the prospects from the cost-push side are also favorable.

Finally, the fact that wholesale prices, the prices that foreshadow the future, have been declining this year rather than rising also suggests that conditions are favorable to continued price stability.

Senator SPARKMAN. Doctor, I just heard some mention over the radio of a comment by the President at his press conference yesterday afternoon in response to a question relating to the labor settlement in New York involving, I believe, the electricians for a 25-hour week. As I understood over the radio, the President was referring to his views on productivity being a necessary factor in wage settlements and so forth.

If that kind of a move became general throughout the country, do you believe it would be inflationary?

Dr. HELLER. Indeed it would. The President expressed his regret, both at the shortening of the hours, and, in effect, at the fact that the wage increase was excessive in terms of productivity and price stability. The answer to your question is implicit in that regret, namely, that if this became general throughout the economy, we could expect very substantial upward pressure on our price level.

Senator SPARKMAN. Doctor, I would like to turn to another subject very briefly, and that is the recent action on the part of the Federal Reserve in authorizing commercial banks to increase their interest on savings accounts to 4 percent. Right after that happened, we saw quite a wave of increases by the savings and loan associations. I notice savings and loan associations out in California are advertising in the New York Times and in the Washington papers, asking for deposits at 4.6 percent dividend rates.

It seems to me that that would inevitably have the result of pushing up interest rates in those fields in which savings are used, particularly in the homebuilding field. Do you see any danger in that?

Dr. HELLER. Senator, there are mixed trends here. Of course, raising the ceilings on interest rates on savings deposits was designed to improve the competition for savings, and, in general, such competition is a part of our economic system and, therefore, such an action is in harmony with our basic policies.

Whether, however, this will result in higher mortgage rates, which I think is the specific point to which your question is directed, is a mixed question. On one hand, it might be that if the savings and loan associations have to pay higher rates, then eventually they would have to raise their charges to the homeowner. But on the other hand, it has been very interesting that the payment of higher interest rates by the commercial banks has led them to move further into the mortgage markets, and as a result has increased the flow of funds into the mortgage markets. Of course, with an ordinary demand-supply relationship, this would tend to hold down the interest rates on mortgage funds rather than increase them.

I don't think the final chapter of this book has yet been written, but for the moment it seems to have increased, rather than diminished, the flow of mortgage funds.

Senator SPARKMAN. I hope you are right, that it will cause the different institutions taking in savings to step up their tempo in the mortgage field. People who are connected with the savings and loan business have told me that they simply cannot operate on as narrow a margin as 0.4 percent, making mortgages at 6 percent, that they would be compelled to increase their mortgage rates.

The fear that I have is that the interest rates will go up and as interest rates go up we know that more and more people are priced out of the housing market. Therefore, it would seem to me that the inevitable result would be a curtailment in the production of homes.

By the way, that is one of the strong factors in the recovery, isn't it?

Dr. HELLER. Yes. As a matter of fact, it exceeded our expectations. We have had about a 16-percent rise in the rate of housing starts from the beginning to the end of 1961. That, of course, was in considerable part a response to the Housing Act of 1961.

Senator SPARKMAN. We got down to the low annual production at one time, about a year ago, in fact, in December of 1960, I believe, down to 900,000. We ended the year at 1,300,000, I believe.

Dr. HELLER. Just about at that level; yes, sir.

Senator SPARKMAN. I simply express this concern, and I do hope it will have the very careful watching from the members of the Advisory Council and all of those who are concerned with these problems. Thank you very much.

Dr. HELLER. Indeed, this is something we will watch with concern. Economic policy involves hard choices. Of course, one of the reasons for the increases in the savings deposit interest rates was to increase our international competitive position for funds that can either be deposited here or abroad. To date, there has been a harmony between that goal and the mortgage field. We hope this harmony will continue.

Senator SPARKMAN. Well, I join with you in expressing that wish. I understood that the increase was largely made in order to create that competition for funds that have heretofore been going abroad. But it seems to me that the competition has been very sharp between commercial banks and savings and loan institutions.

I think it will bear the most careful watching.

Chairman PATMAN. Congressman Kilburn, of New York, is recognized.

Representative KILBURN. Thank you, Mr. Chairman.

I would just like to say, Dr. Heller, it is always a pleasure and a privilege to have you testify. I learn a great deal.

Dr. HELLER. Thank you.

Representative KILBURN. Since Senator Javits has another meeting to attend, I ask unanimous consent to pass my time to him.

Chairman PATMAN. Is there objection?

The Chair hears none.

Senator Javits from New York.

Senator JAVITS. Thank you, Mr. Chairman.

I want to express my gratitude to my distinguished colleague and friend from New York in allowing me to use this time. I shall confine myself to one member's time, Mr. Chairman.

Dr. Heller, I am very interested in one title of this report headed "Our Goal of Equal Opportunity."

I notice that you intend to press for equal opportunity. This is at page 9 of the President's statement. That would be by trying to wipe out poverty and by getting health insurance for the aged, by Federal retraining programs, by strengthening our unemployment compensation system, by revising public welfare and assistance programs, by public education, by reducing adult illiteracy, but I see nothing whatever there about discrimination in jobs on grounds of race and color, which seems to be a pretty serious matter, and which one of our Secretaries of Health, Education, and Welfare estimated to cost the country $30 billion in productive power.

Could you tell us what are the intentions of the administration on that score?

Dr. HELLER. Senator Javits, if this was left out of that section by specific mention it was not for lack of interest or dedication to the elimination of racial discrimination. On page 121 of the Council's report, which, as I indicated in the opening of my statement, is really an examination of the rationale of this administration's economic policy, it says the following, which bears directly on your question:

> Racial discrimination is a national disgrace. In this respect, above all others, practice in the United States is a standing affront to professions of democratic principle. Discrimination inflicts immeasurable human and social costs on a large number of our citizens. In addition—and this is why it deserves particular mention in this Report—it inflicts an economic loss on the country.

Senator JAVITS. Can you give us an estimate of that economic loss?

Dr. HELLER. We present some figures, Senator, on the differences in median money income of white and nonwhite groups, for example. Among those figures you will note in the middle of page 122 in 1960, 11 percent of the white families but 31.7 percent of the nonwhite families had money incomes of less than $2,000. Roughly 37 percent of the white families but only 13.6 percent of nonwhite families had money incomes of $7,000 and over. That is not a direct measurement of the losses, but it is an indication of what we are losing by not making full use of our entire population.

Senator JAVITS. Dr. Heller, would you have any objection on the grounds of the President's prerogative to giving us an estimate to supplement your report, giving the committee an estimate of the economic losses? I have given you the precedent of a previous Secretary of HEW. I refer to the losses suffered by the country because of discrimination in employment.

Dr. HELLER. We would be glad to make our best attempt in cooperation with Secretary Ribicoff, and present that for the record.

Senator JAVITS. I thank you, Doctor. I shall repeat the request, if the Chair will allow me to, to the Secretary.

Chairman PATMAN. Without objection it is so ordered. (Dr. Heller later stated that the supplement requested was not available at this time.)

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Senator JAVITS. Is there any significance in your mind in the omission of this proposition from the President's report in view of the fact that the President seems to be avoiding the Congress when it comes to seeking legislation on civil rights at this session?

Dr. HELLER. No, sir; I do not believe there was any significance in its omission here.

Senator JAVITS. Does the Council of Economic Advisers expect to approach the President further and urge him to seek legislative action on discrimination in private employment? I know the President is proceeding in respect of employment by the United States and by contractors for the United States. You say that in your report.

Dr. HELLER. Insofar as our economic jurisdiction is involved. And, of course, the question of losses of resources through any form of discrimination, unemployment, and so forth, is a matter of concern to us. We shall certainly make recommendations designed to make full use of the country's human resources.

Senator JAVITS. Turning to another matter, and there were only two matters that I wanted to question you about, looking at page 66 of the advisers' report, we find that you make an estimate under the heading "Prospects for Full Employment"—an estimate of an unemployment rate of 5 percent or lower at the end of 1962 but not as low as 4 percent. Then you go on to make an estimate that the 4 percent unemployment rate, the so-called optimum rate—not that you would want any unemployment, we all understand that, but the point at which you feel that it ceases to be a major national problem—would not be reached, as you estimate it, until mid-1963, and even then only if we double, and I think it is more than double—an 11-percent increase in the gross national product—if we double what you gentlemen call economic growth. Is that correct? Is that your prediction?

Dr. HELLER. We have to distinguish, Senator, between the shortrun recovery and the longrun growth. In other words, for the past year, for example, we have been having an annual rate of growth in our real output of 10 percent per year. How much of that is trend-growth, which has been running at about 3½ percent, and how much of it is recovery rate, of course, can't be told immediately.

You are quite right that we need a rate of growth of output per year considerably in excess of 3½ percent in order to reach the interim full employment target by the middle of 1963. We need a rate of growth of about between 7 and 8 percent, about double that. But that is part of our cyclical recovery rate rather than just the longrun trend rate of growth.

Senator JAVITS. Have you made any estimate of what unemployment will be in mid-1963 if we just go on as we are going, in terms of growth rate? Whatever may be our present situation, if we just continue it, where will we stand in mid-1963 on unemployment?

Dr. HELLER. If we were to project the growth rate of gross national product that we had in 1961, we would readily achieve the 4-percent unemployment target by mid-1963.

Senator JAVITS. Do you gentlemen, as economists, expect it will be projected?

Dr. HELLER. We think that the estimate of $570 billion of gross national product for 1962 is entirely consistent with a growth path of output and employment which could bring us to the 4-percent target by mid-1963.

Senator JAVITS. If it continues at that rate?

Dr. HELLER. If it continues at that rate for the first half of 1963.

May I just say that throughout these discussions of projections and predictions and estimates and forecasts we have at heart a good deal more modesty about our statistics than we may express in response to these direct questions. These projections are hazardous. We have felt that since the Employment Act requires us explicitly to put forward current and foreseeable trends in the economy and since we have to do this for economic policy and for budget policy, we ought to make our estimates available both to public and private policy-makers.

This is living dangerously, and we are quite aware of it. So far our record, as the chairman was good enough to point out, has been a good one on forecasts. But we do not assume that we can always come as close to $542 billion as we did in July when we forecast $541.8 billion. Please don't hold us to that kind of a standard.

Senator JAVITS. I notice a rather important emphasis in your own statement upon the question of productivity as distinguished from growth rate. I am speaking now of the statement you made before us this morning, not of your report, particularly. But it is so noticeable here that under practically every heading you speak of your insistence upon the fact. For example, you say—

> A faster growth in per capita income requires faster growth in the productivity of labor.

This characterizes practically every one of the items which you refer to in your whole statement. Many of us have been rather disappointed because of the paucity of recommendation for increasing the productivity of labor. I would like to ask you, if I may, one or two questions upon that score.

Is the main reliance of the administration for increasing the productivity of labor upon the investment—the tax benefits for capital investments—which have been put forward?

Is that the main plank in the administration's platform upon that subject?

Dr. HELLER. Senator, this is one of several planks in the platform. It has so much prominence perhaps because of the fact that it yields quick benefits. That is to say, the 8-percent credit, if enacted, would, in our view, stimulate immediately an increase in investments, and through that investment an increase in output per unit of input, which is what we mean, of course, by an increase in productivity. But it is only one of a whole range of measures to increase productivity. There are also other tax measures, including the depreciation schedule revision, which are part and parcel of the same approach.

Beyond that, however, maintaining relatively easy monetary conditions to make the investment process cheaper is part of the program.

Then, on the intangible side, from which a good half of our growth comes, the President's programs in the fields of advances in research, technology, training, education, are a very important part of the economic growth program of this administration.

The manpower development and training program, Federal aid to education, special aids in the field of higher education, support of research and technology—these are all part of that program.

Senator JAVITS. Dr. Heller, my time is up, but if the Chair will allow me 30 seconds more, I would like to make one point with you and then to conclude. That is that it is my deep conviction that exhortation on this subject of stability of wage rates, and so forth, is not going to work. The administration is going to have to have some more concrete ideas, as to how to develop maximum productivity, especially in view of the trend which we have now seen in New York toward this extraordinarily short-hour period for work, and a continuance of the pressure on wage scales, and so forth, instead of any real effort to move in a sideways direction for profit-sharing or similar plans. I make that point. We will go into it at another time.

I would like to conclude, if I may, by saying that as a member of the opposition, I think it is going to be our duty to come up with some feasible alternatives for all these things that we think are left out, at least that I do, and I think other Republicans feel the same as I do. I think that will prove to be.

Much as I join with Senator Bush in approving the President's objectives, I feel that there is a lot to be desired on the measures to implement those objectives.

I think it would be our duty to come forward with feasible means for doing what we think needs to be done and what he thinks needs to be done.

Thank you very much, Mr. Chairman.

Chairman PATMAN. Congresswoman Griffiths, of Michigan, who has recently been made a member of the Committee on Ways and Means in the House of Representatives, is recognized.

Representative GRIFFITHS. Thank you, Mr. Chairman.

I, too, would like to congratulate you, Dr. Heller, on your very interesting, informative, and most readable report.

Dr. HELLER. Thank you.

Representative GRIFFITHS. I observe that you have picked up the suggestion of the Commission on Money and Credit that the President be given the power, over a brief period, to lower taxes.

As I recall, they suggested that the President also be given the power to increase taxes. May I ask what prompted the dropping of this request?

Dr. HELLER. Congresswoman Griffiths, concentration on the reduction side and dropping of the standby authority to increase taxes—which had, as you know, been recommended by the Commission on Money and Credit, and has been suggested by others, including the Committee for Economic Development—was prompted in large part by the consideration of the congressional power to tax. That is to say, that a temporary, partial suspension of the regular income tax rates seemed to be more consistent with the congressional powers and prerogatives in the field of fiscal matters, specificially in the field of taxation. In delegating some part of this power, which has constitutional precedence, of course, it was felt that the delegation would be much more consistent with congressional prerogatives if it involved only temporary suspensions of the rates determined by the Congress rather than increases in those rates.

Representative GRIFFITHS. In researching this suggestion, did you find that any President had ever asked Congress to reduce taxes, supplemented his case, and Congress had refused to do it?

Dr. HELLER. That is a very good question and one I can't answer offhand. I doubt that there is such a case, but I do not have a ready answer to it.

Representative GRIFFITHS. I would assume that if the President asked Congress to reduce taxes even for a brief period, and if he augmented his case with facts and figures, such a request would go through this Congress faster than a declaration of war.

Dr. HELLER. That is a very impressive prediction, Mrs. Griffiths.

Representative GRIFFITHS. I would also like to ask you this question: In determining that the President could reduce taxes during the period that Congress was not here, and that such a reduction would stay in force until 30 days after Congress returned, is there anything to suggest, historically, that the automatic indicators would be more apt to come into effect during the months of October and November than in any other months? Or is the reverse true?

Dr. HELLER. I don't think there is any clear historical trend in this respect, though it is perfectly true that the 1957–58 recession began in July of 1957, when, of course, Congress was in session, and this last time the peak month, that is, in 1960, was in May, when Congress was in session, and would have been in session for a number of months. I take it that in both of these cases, had the power been invoked, it would have been invoked during the time that Congress was sitting.

Representative GRIFFITHS. I think it is a commendable suggestion to fight recession, but before the power is given to the President alone I think he should try Congress. I think Congress would act.

Dr. HELLER. May I comment on just one or two other aspects of that, Mrs. Griffiths? The power is not given to the President alone under the form of proposal that has been made here. It is definitely subject to congressional veto.

Representative GRIFFITHS. But what a dubious pleasure that would be. He reduces them and I insist that they stay up.

That would be an illusory retention of power, in my opinion.

Dr. HELLER. The second comment is that the speed of congressional action in tax matters, to which you were referring initially, has not been, shall we say, proved by experience. That is to say there have been one or two relatively fast actions, but in general, with the controversy over tax structure, the form of the reduction, and so forth.

Representative GRIFFITHS. But, of course, nobody ever asked for exactly that reduciton, a straight reduction in income tax.

Dr. HELLER. I doubt that any reduction that the President has ever asked for has come through the Congress in precisely the form in which he has asked for it. In the process of debating it, a good deal of delay, which would be very costly in the fighting of an oncoming recession, would occur, and part of the rationale of this proposal is to move fast.

Representative GRIFFITHS. I think if you suggested that a resolution pass the Houses, that should such a request come from the President to reduce taxes that they would resolve to give it precedence over all other legislative matters. You might prepare a way now for such a reduction.

You could have all the arguments put forth now as to why it should be done. I think it would be helpful.

Dr. HELLER. Like all other Presidential proposals, I am sure this one is subject to congressional improvements.

Representative GRIFFITHS. But this would be the greatest one ever made.

Thank you, Mr. Chairman.

Chairman PATMAN. Congressman Widnall.

Representative WIDNALL. Professor Heller, I, too, would like to express my commendation at this time to you and the other members of the Council on the fine report you have submitted.

You said, I believe, a little bit earlier, that because of the growth rate, by mid-1963 unemployment should be down to around 4 percent. Are you counting on employing 1 million in the Youth Conservation Corps or the Federal payroll in order to produce that figure?

Dr. HELLER. No, we are not.

Representative WIDNALL. Would that reduce the rate further, to 3 percent, if that passes?

Dr. HELLER. I have heard no figures as high as 1 million in terms of the President's proposals on the Youth Employment Opportunities Act. The highest official figure is 150,000, recommended by the Senate committee.

Representative WIDNALL. I have seen figures of 900,000 to 1 million, according to the press, I believe. This certainly would have a material effect. I was very interested to see whether you had included this in your own figures, inasmuch as the budgetary message presupposes certain things are going to be done by the Congress in order to balance the budget.

Dr. HELLER. Insofar as the President's program is embodied in the budget, the budgetary provision, which is, of course, for a very modest beginning in this field, would be taken into account in our projections.

But by mid-1963, the numbers that would be involved in this program under the budgetary provision would, I am sure, not be that high. I am sorry I can't quote them offhand. But this was taken into account in our thinking.

Representative WIDNALL. Isn't it true that in that 18- to 21-age group, with which there is so much concern, there is a limiting factor in their employment because of their uncertain position with respect to the draft, and also in that, if they are employed, they are liable to be taken in the draft and then the employer has to take them back for a period of time into his company and put them on the payroll again?

Dr. HELLER. It is factually true as a general matter that, for whatever reason, the level of unemployment in our youth group is very substantially above that of the general level of unemployment in the economy. I suppose that may be one factor.

I am sure there are others which play a very great role.

Representative WIDNALL. With regard to this recent increase in interest rates by the commercial banks and also by the savings and loan associations, does it mean that there will be an increasingly unfavorable market for the sale of Government bonds, unless at much higher interest rates?

Dr. HELLER. In the competition for funds, commercial savings accounts have become relatively more important and more attractive.

Representative WIDNALL. I understood that within recent years attacks have been made on Government because interest rates were going up. It seems to me that approval of these developments in the commercial field will inevitably lead to higher interest being paid out by the Government to borrow funds for governmental purposes. Is that true?

Dr. HELLER. This is not inevitably the case. I think that here is a case of "leveling up" the interest rates in the commercial banks on savings deposits toward the levels in savings and loan associations and mutual savings banks. This is not likely to result in a substantial overall increase.

For example, the 4.6-percent rate that I believe Senator Sparkman mentioned as now being paid and advertised by the savings and loan associations out in California, is a rise from 4.5 percent before regulation Q was issued.

Representative WIDNALL. Of course, there have been substantial increases in rates on the lower level by other institutions.

Dr. HELLER. Yes, in the savings accounts of commercial banks.

Representative WIDNALL. Earlier, I believe in your colloquy with Representative Bolling, there was some talk about the debt being sanctified in some way, and that there shouldn't be too much concern over the size of our national debt. Shouldn't there be a lot of concern about the amount of interest we are forced to pay each year, the amount of interest taking more and more of our budgetary dollar?

I believe that in the projection you have in 1963, the interest on the debt will be about $9 billion. Ten cents out of every taxpayer's dollar will be going to pay interest, and not actually buying anything by way of goods, services, and the like.

Dr. HELLER. Sir, I tried to suggest in responding to the earlier question that while the debt management problem and the size of the debt have been substantially reduced through the growth of the economy, the public debt is, of course, always a problem that we have to deal with. Indeed, the interest cost of the public debt involves a very substantial transfer of funds from one group to another group in the economy. There is a lot of overlap, of course, between the taxpayers and the recipients of the interest.

Nonetheless, it is a very large claim on the budget and something that we should attempt to reduce. I might say that as a proportion of the gross national product, the interest on the debt has also been shrinking, although not as much as the debt itself, because interest rates have been rising.

Representative WIDNALL. To turn to another field, if the administration proposals for tax credit for new investments and depreciation allowances were enacted, would the amounts allowed put us in a competitive position with those nations in Europe and in Japan who have far greater opportunities? Don't they allow much more by way of depreciation?

Dr. HELLER. On this point, I am sure Secretary Dillon will be in better position to give you the details. But I can tell you that a direct tax credit, an offset against taxes, is essentially a more generous treatment than most of these countries give under their depreciation provisions.

A recent calculation by the Machinery and Allied Products Institute indicates that this 8-percent tax credit is the equivalent of a 40-percent initial allowance under the tax laws and that this compares very favorably indeed with the treatment of plant and equipment investment overseas.

Representative WIDNALL. Would it be possible to have a comparison between some of the leading nations and the United States before and after the enactment of this type of legislation?

Dr. HELLER. Yes, Mr. Congressman. The Treasury Department has prepared a document, dated January 11, 1962, entitled "Depreciation Practices in Foreign Countries." I am certain that this can be made available to the committee.

In addition, I would like to insert in the record at this point part of the testimony of Secretary of the Treasury Dillon given before the Joint Committee on Internal Revenue Taxation on January 18, 1962.

(The document referred to follows:)

EXCERPT FROM STATEMENT OF THE HONORABLE DOUGLAS DILLON, SECRETARY OF THE TREASURY, BEFORE THE JOINT COMMITTEE ON INTERNAL REVENUE TAXATION, JANUARY 18, 1962

DEPRECIATION ABROAD

Because American industry does not operate in a setting entirely of our own making, but is actively in competition at home and abroad with foreign producers, our practices with respect to depreciation policy need to be examined in the light of foreign experience. Thus the Treasury has gathered a substantial amount of information on depreciation practices in leading foreign industrial nations from a wide variety of published and unpublished sources, including our Embassy personnel and officials of foreign governments.

In today's highly competitive world we find widespread use of initial allowances and incentive allowances supplementing depreciation charges. Thus for the major industrialized nations of the free world—Belgium, Canada, France, West Germany, Italy, Japan, the Netherlands, Sweden, and the United Kingdom—we have assembled reliable information with respect not only to depreciation practices, but also regarding initial and incentive allowances.

The information presented in the first column of table 1 shows that the typical or representative tax life permitted with respect to production machinery and equipment in each of these countries, except Japan and the United Kingdom, is substantially lower than it is in the United States. Moreover, in addition to ordinary depreciation, Belgium, the Netherlands, the United Kingdom, and under certain conditions, Sweden, permit the deduction from income of incentive allowances. Initial allowances, which add very appreciably to the deduction that may be taken in the year of acquisition of a depreciable asset, are permitted in Canada, Italy, Japan, the Netherlands, Sweden, and the United Kingdom.

The impact of ordinary depreciation plus initial and incentive allowances on the amounts that may be deducted in the year in which a new asset is acquired is shown in the second column of the table. Here it may be seen that the percentage of the cost of an asset that may be deducted in the first year ranges from 20 percent in West Germany to 43.4 percent in Japan, compared with as low as 10.5 percent in the United States.

Columns 3 and 4 of table 1 show the percentage of the cost of the asset that may be deducted during the first 2 and first 5 years of its life. Here, again, it may be seen that the deductions permitted in each of the nine industrialized foreign countries comprise a far higher proportion of the cost of industrial machinery and equipment than is permitted under current law and practices in the United States. For the first 5 years of the life of the asset, the relevant proportion falls within the range of 60 to 70 percent for West Germany, Japan, and the United Kingdom, between 70 and 80 percent for Canada and France, and 85 to as much as 100 percent for Belgium, Italy, the Netherlands, and Sweden. In sharp contrast, the applicable percentage in the United States is 42.7 under the present average Bulletin F life and 51.1 percent for the commonly used 15-year life.

TABLE 1.—*Comparison of depreciation deductions, initial and incentive allowances*[1] *for industrial equipment in leading industrial countries with similar deductions and allowances in the United States under actual and various proposed plans*[2]

	Representative tax lives	Depreciation deductions, initial and incentive allowances (percentage of cost of asset)		
		1st year	1st 2 years	1st 5 years
	Years			
Belgium	8	22.5	45.0	92.5
Canada	10	30.0	44.0	71.4
France	10	25.0	43.8	76.3
West Germany	10	20.0	36.0	67.2
Italy	10	25.0	50.0	100.0
Japan	16	43.4	51.0	68.2
Netherlands	10	26.2	49.6	85.6
Sweden	5	30.0	51.0	100.0
United Kingdom	27	39.0	46.3	64.0
United States:				
Without investment credit and lives equal to current Bulletin "F" weighted average of 19 years		10.5	19.9	42.7
With lives of—				
15 years		13.3	24.9	51.1
14 years		14.3	26.5	53.7
13 years		15.4	28.4	56.6
12 years		16.7	30.6	59.8
11 years		18.2	33.1	63.0
10 years		20.0	36.0	67.2
With investment credit and lives equal to current Bulletin "F" weighted average of 19 years		26.5	35.9	58.7
With lives—				
15 years		29.3	40.9	67.1
14 years		30.3	42.5	69.7
13 years		31.4	44.4	72.6
12 years		32.7	46.6	75.8
11 years		34.2	49.1	79.0
10 years		36.0	52.0	83.2

[1] The deductions and allowances for each of the foreign countries have been computed on the basis that the investment qualifies fully for any special allowances or deductions permitted. The deductions in the United States have been determined under the double declining balance depreciation method, without regard to the limited 1st-year allowances for small business.

[2] For purposes of this table, the proposed 8-percent investment credit has been considered as equivalent to a 16-percent investment allowance. For corporations subject only to the 30-percent normal tax it is equivalent to an incentive allowance of 27 percent. The initial allowance of 20 percent of each year's investment, up to $10,000, is not taken into account because of its relatively small impact.

Source: Treasury Department, Office of Tax Analysis, Jan. 18, 1962.

This picture changes dramatically, however, when the proposed investment credit enters. In terms of its effect on current liability, the 8-percent investment tax credit is equivalent to an incentive allowance of approximately 16 percent for corporations subject to the 52-percent corporate income tax rate and about 27 percent for corporations subject only to the normal tax rate of 30 percent.[1] The bottom seven rows of table 1 indicate the effect on comparable allowances for new depreciable assets that would be achieved if the 8-percent investment tax credit were currently in force. Assuming the existing weighted average Bulletin F life of about 19 years, the equivalent first-year deductions would be 26.5 percent. In combination with a somewhat shorter life of 15 years, we find that the first year's equivalent deductions in the United States would be equal to 29.3 percent of the cost of new depreciable assets. This proportion is higher than that which obtains in Belgium, France, West Germany, Italy, and the Netherlands. First-year deductions or their equivalents would remain substantially higher than those permitted in the United States only in Japan and the United Kingdom. For the first 5 years of the life of the asset, permissible deductions would still exceed appreciably those allowed in the United States and in Belgium, France, Italy, the Netherlands, and Sweden. But allowances in the United States would be approximately the same as those allowed in Canada, West Germany, Japan, and the United Kingdom.

[1] Both the investment credit and the incentive allowance have greater overall effects than a similar initial allowance because they do not reduce the amount of depreciation that may be taken over the life of an asset.

The data presented in the bottom portion of table 1 demonstrate clearly that, especially within the first 2 years of the life of an asset, even a revision to provide realistic tax lives will not, by itself, place the United States in a position comparable to that of its most immediate foreign competitors. The achievement of this objective, rather, requires both the investment tax credit and the faster writeoffs that would be permitted under depreciation policies, which, in broader recognition of the increasing importance of obsolescence in the postwar world, would permit American firms to assume shorter tax lives for depreciable property.

Reviewing this summary and analysis, three important conclusions emerge: (1) Shorter tax lives alone will not do the job of bringing American industry abreast of its foreign competitors with respect to tax allowances for investment. (2) The investment credit will make a major contribution toward achieving that goal. (3) The combination of the credit and the forthcoming revision of depreciation guidelines will place the United States on substantially equal footing with other major industrial nations. These conclusions underscore the necessity for the Treasury's two-pronged program of revised, realistic depreciation and the investment credit.

Representative WIDNALL. I am just concerned with whether or not it goes far enough.

I have one other matter. In your statement, you say gold losses of $1.7 billion in 1960 were cut in half in 1961. Have you the figures for all four quarters of 1961?

Dr. HELLER. May I ask Mr. Tobin to respond to that?

Representative WIDNALL. What were the figures quarter by quarter in 1961?

Dr. TOBIN. The figures for gold losses?

Representative WINDALL. I understood that in the first half of the year it was in a much more favorable position and then deteriorated in the last half of the year.

Dr. HELLER. I think we can divide the year into three rather unequal parts. First of all, in January 1961, there was a continued very strong outflow that was really a continuation of the outflow of late 1960. Then there was a period of relative stability, indeed some net inflow, for some months. Finally, you are quite right, in the last 3 or 4 months there has been a stepping up of the rate of outflow, including one very large drawing by the United Kingdom related to the credits that it was given by the International Monetary Fund.

Representative WIDNALL. And this fact is something that should be of the deepest concern to the Congress, isn't it so?

Dr. HELLER. We have constantly stressed the problem of our balance-of-payments and the related problem of gold outflow as one which looks over the shoulder of all economic policy.

Representative WIDNALL. All the economic panaceas that we might impose upon our economy will be of no avail if this continues over a period of years, isn't that so?

Dr. HELLER. There has to be a proper balance struck between measures for domestic economic recovery and growth and measures for protecting and improving our balance-of-payments situation. Indeed, again, this is where the point that Senator Javits was emphasizing, namely the increase in productivity, tends to harmonize our various objectives—price stability, an internationally more competitive position, and stimulation of economic growth.

Representative WIDNALL. I am thinking that there could be an increasing lack of confidence in the dollar, and greater withdrawals overseas, if they felt that we weren't stabilizing our economy in times of prosperity and that we weren't concerned with the national debt, because many other nations look at a national debt in a different way.

Dr. HELLER. These are sources of concern to us in economic policy-making constantly, but what we are trying to emphasize is that they should be put in proper perspective in the full range of economic policy.

Mr. Tobin has just handed me the figures on the gold losses for the year, insofar as we have them.

In January and February we lost almost $400 million of gold. In other words, that was about half of the total gold losses for the year, in those first 2 months.

Then for the following 4 months we had a net gold inflow, and in the months of July through November there was a resumption of the gold outflow.

Representative WIDNALL. To what extent?

Dr. HELLER. The total for those five months was about $580 million.

Representative WIDNALL. That is all. Thank you very much.

Chairman PATMAN. Without objection, we will be in recess until 2 o'clock this afternoon.

(Whereupon, at 12:30 p.m., a recess was taken until 2 p.m. the same day.)

AFTERNOON SESSION

Chairman PATMAN. The committee will please come to order.

Senator Proxmire is recognized to interrogate.

STATEMENTS OF DR. WALTER W. HELLER, CHAIRMAN, COUNCIL OF ECONOMIC ADVISERS; DR. KERMIT GORDON AND DR. JAMES TOBIN, MEMBERS, COUNCIL OF ECONOMIC ADVISERS—Resumed

Senator PROXMIRE. Thank you, Mr. Chairman.

I want to congratulate the Council of Economic Advisers on the report. I think it is an extraordinarily useful report in many, many respects. I particularly like the way you discuss and define unemployment and show its difficulties and problems.

I would like to call your attention in this regard to page 43 in your report, where you have a chart entitled "Measures of Unemployment," and the accompanying pages, 42 through 44, discussing the various measures of unemployment you have here.

This is the first time that I have seen set forth the five measures of unemployment, including full time equivalent, experienced wage and salary workers, total civilian—I guess that is the big usual measure, is that correct?—married men, and longtime unemployment.

I would like to ask you, Dr. Heller, what the problems would be in making this part of the Economic Indicators. It would be very useful to me to have this kind of thing and I think it would be an excellent policymaking tool for the Congress.

Dr. HELLER. I am not entirely sure whether the detail on the basis of which these alternative measures are plotted, becomes available quite as quickly as the overall figure, but it would be technically possible to follow this series quite regularly. Of course, together with your staff and the membership of the committee, we are always examining Economic Indicators, for possible changes. This is one that we could take under consideration for future revision.

Senator PROXMIRE. From the standpoint of policy, what is your feeling on incorporating this as part of the Economic Indicators? Do you think it would be useful?

I understand that there are several other members of the committee who have other figures they would like to also include in the Economic Indicators.

We have to keep this limited, I know, or we destroy the whole benefit of a concise and simple report.

Dr. HELLER. You have essentially given the answer I was about to give. That is, from the standpoint of policy, these are all important measures which should be taken into account. But there are a lot of things competing for inclusion in the Indicators, and I think these would have to be set up against the other proposed changes or additions to the Indicators in making a final decision. In general, I would be very favorable toward the inclusion of this series if space permits.

Senator PROXMIRE. I would like to refer briefly to questioning by Congressman Curtis. The figures I have indicate, seasonally adjusted, that in the big drop, to which Congressman Curtis called attention, in unemployment in October and November, the increase in military was from 2,586,000 to 2,757,000 or 171,000 increase. The increase in total civilian employment was from 66.6 million, roughly, to 67.2, or an increase of 525,000, and unemployment dropped 486,000.

The point I am trying to establish or have refuted is whether or not it is not true that most of this drop in unemployment, therefore, seems to be the result of increased civilian employment, at least the two-thirds or three-quarters of it, rather than because of the callup of Reserves or because of any military action.

Dr. HELLER. Yes. I am very grateful for the opportunity to speak a little further to that point.

Meanwhile, we have pulled these figures together also.

What you were just giving were the seasonally adjusted figures. We went strongly against the seasonal trend in civilian employment. You are quite right, there was a total rise of 525,000 in civilian employment on the seasonally adjusted basis, as against the 171,000, I believe you said, increase in the Armed Forces.

Representative CURTIS. What month was that?

Senator PROXMIRE. October to November 1961. That was the crucial month in which we got the big and substantial drop in unemployment.

Also, in connection with Congressman Curtis' interrogation, I agree with him wholeheartedly it would be very useful for us to have reliable, regular statistics available on job vacancies and job openings.

I understand we now have available an index of classified ads for jobs and the number of jobs available for interstate transfer. These, of course, are of limited value. You can get a trend from them that might indicate the availability of jobs, but you cannot get any absolute figures that are very satisfactory.

I call your attention to something which may or may not ever be released, though I hope it will be.

Our Subcommittee on Statistics, of which I am chairman, says the following in our unpublished report:

> Research should be undertaken and directed toward the development of a regular monthly survey of job opportunities or vacancies to eliminate the demand side of the labor market in the way the present series measures the supply. Experience here and abroad indicates that substantial difficulties must be overcome before statistical series on vacant jobs become operational. The past success in using survey techniques resolves some other data-gathering problems and suggests another program may be practical. In any event, it would be so useful in analyzing labor markets, operating employment services, and developing practical worker training and retraining programs that expenditure of some funds on research into this problem should be warranted.

I think this reflects a unanimous feeling on the part of the subcommittee.

Other parts of the report are rather controversial. But we agree that this would be something well worth looking into.

We would at least like to explore it to find out how much it would cost to in turn determine these figures.

Dr. HELLER. As I mentioned earlier, I am sure that the President's Committee To Appraise the Employment and Unemployment Statistics, headed by Professor Gordon, will be examining this.

As you point out, in the last analysis, it is going to come down to a matter not only of technical feasibility but of congressional appropriation of funds to make this possible on the part of the Bureau of Labor Statistics.

Senator PROXMIRE. Early in your statement, you say:

> To provide stimulus and substance for the recovery, the administration early in 1961: (1) successfully sought the cooperation of Congress in enacting legislation to expand purchasing power and create jobs.

On page 101 of your report, you list the legislative recommendations on which action was either secured or on which the administration attempted to secure action.

Is it your position that this really had a substantial impact in 1961 on the economy, that the gross national product actually was increased significantly as a result of this legislation?

Dr. HELLER. Yes, sir; that is our position. We have made, with the usual qualifications about the inexactness of economic science, some calculations concerning the direct and indirect effects of these programs; that is, of both the direct expenditure and the multiplier effects of the expenditures of the various programs that were put into effect both by congressional action and by Executive action in the first part of 1961.

According to those calculations, leaving aside intangible psychological factors that may have been a further contributing factor to recovery, our calculation showed approximately $15 billion of increase in gross national product in the fiscal year 1962 to be attributable to these programs.

Senator PROXMIRE. To the legislative recommendations? Not the executive but the legislative, to begin with.

Dr. HELLER. This is the combination of all legislative and executive actions, not just those directed and originated as a matter of anti-recession action, but including the programs for expansion of the space and military programs, and so forth, the total impact of these.

Senator PROXMIRE. That is the reason I wanted to break it down from the way you present it.

It seems to me that a great deal of this was certainly the result of the increased military efforts.

I am sure that neither the President nor any adviser to the President suggested that we engage in expanding the Armed Forces for the purpose of reducing unemployment.

Dr. HELLER. No, of course not, we are talking about the employment-creating byproducts of the necessary expansion in the military and space side of the budget.

But adding those to the programs which are summarized in our annual report, beginning on page 97, accounts for, I would say, at least a third of the expansion in gross national product during 1961.

Senator PROXMIRE. A very substantial part of this improvement is a result of the military response to the international situation, and much less of it would be as a result of the programs such as temporary extension of unemployment compensation, aid to dependent children, and so forth.

Of course, these other actions, social security, for instance, took no effect until late in the year and then I presume their effect was fairly moderate.

As I go over these, it is hard for me to see where any direct and substantial and significant increase can be attributable to action by Congress as a result of administration requests.

Dr. HELLER. I would like to comment on a couple of aspects of what you have just said.

One is, of course, that had the President asked for matching tax increases with the military expenditure increases the consequent stimulating effect of those increases would have been in considerable part offset.

As he said in his statement, on page 6:

> In a fully employed economy, these increases—

increases for space and military programs—

> would have required new tax revenues to match. But I did not recommend tax increases at this point because they would have cut into private purchasing power and retarded recovery.

So, while the expenditures were not part of the recovery program, the decision not to match them with taxes was part of the budgetary policy for recovery in 1961.

Likewise, in the temporary unemployment compensation, the aid to dependent children of these unemployed, and in the other social security programs, a good deal of expenditure was actually incurred in 1961 and has made a contribution to purchasing power and to output and to creation of jobs.

Senator PROXMIRE. Disregarding the military for the moment, is it true or not that in most of these programs, if not perhaps all of these programs, any increase in the gross national product was borrowed from the future and perhaps borrowed from the fairly near future? In other words, it was borrowed from 1962 for 1961, to some extent, or, as in the case of unemployment compensation and social security, there will be an increase in taxes which will have a compensating effect in slowing down the progress during 1962 and 1963 as compared to what it would have been if there had been no action whatsoever?

Dr. HELLER. I think that if you take the actual expenditures under these programs I just mentioned in the fiscal years 1961 and 1962, which come to $800 million for social security and old-age and survivors insurance, $900 million for temporary unemployment compensation, $100 million for aid to dependent children of the unemployed, you have a combined total of nearly $2 billion of expenditures that would not have taken place except for the action of Congress as recommended by the President.

Senator PROXMIRE. If we might pause right there. On January 1, 1962, just begun, there will be a half-billion-dollar increase in the social security tax.

On January 1, 1963, there will be a $2 billion additional increase in social security.

The unemployment compensation will increase by half a billion dollars on January 1, 1962, or just did increase, I should say.

On July 1 of this year, there will be another billion-dollar increase.

So, looking at this in terms of economic aggregates and net effects, does this not tend to wash out?

Dr. HELLER. Well, I would say that——

Senator PROXMIRE. Well, it has speeded up the recovery, perhaps.

Dr. HELLER. We have unquestionably enjoyed an increase in gross national product and a speedup in recovery, as you suggest, as a result of these measures taken and these transfer payments made during 1961 and continuing into the 1962 period.

At the same time it is true, Senator, that taxes that were already scheduled, that were not part of the tax increase accompanying the liberalization of the social security program this past year, are going into effect. Temporary unemployment compensation under the 1958 program, as I understand it, however, is not repayable until 1963. Nevertheless, all of these revenue measures must be weighed in devising stabilization policy.

But I do not think this adds up to saying that we have, in effect, borrowed this recovery or borrowed this production from the future. We, in effect, took resources that would have gone to waste and put them into productive use.

I think that is a gain.

Senator PROXMIRE. My time has expired, but I want to add that I heartily approved the increase in social security and voted for it.

Unless you can show that you are picking up money that otherwise would be saved, and putting it into the pockets of people who will spend it, it is hard to to show an effect on the economy except to increase the gross national product in 1961 and part of 1962 at the expense of later on.

Chairman PATMAN. Senator Pell?

Senator PELL. Mr. Heller, I have three questions. The first is in connection with the gross national product increase: Would it not be correct to say that the important point is not the increase in GNP but the percentage of the GNP that is being reinvested in capital goods?

In this connection I was wondering if you would compare our rate of reinvestment of the GNP in capital goods with that of European countries. Also is the percentage which we have reinvested going up or going down?

Dr. HELLER. I would first of all say that both the absolute increase in gross national product and the proportion of it going into investment are extremely important magnitudes.

I am sure that you would agree that our first job from the standpoint of reemploying idle resources and manpower is to get the gross national product up to full employment levels.

At the same time, however, as we have stressed again and again, it is important that we increase the proportion that goes into the building up of future productivity and future capacity, through investment both in plant capacity and in trained capacity.

Our level of investment has definitely been low, as a proportion of GNP. Most of the European countries, countries that have had rates of economic growth of 4, 5, and 6 percent on the average for 1953–60 against our realized rate of growth have been just over 2 percent, and our growth potential of about 3½ percent. We are very much concerned about this.

Senator PELL. Is there another technologically advanced nation that has a lower rate of reinvestment than we do?

Dr. HELLER. May I ask Mr. Tobin to comment on that?

Dr. TOBIN. I do not have the exact figures here, but I believe it to be true that the United Kingdom and the United States have shared the dubious distinction that you are referring to. Certainly in the United Kingdom there is also an awareness that for accelerating economic growth they need to do more for investment in the long-term capacity of their economy to produce.

I might say that the really important thing for economic growth, as far as investment is concerned, is the share that investment is of our potential GNP, because it is the growth in the potential which, in the longrun, will determine how fast we grow and how fast our actual production will increase if we are sensible enough to use the potential as it moves along. So, there are really two reasons, then, why our recent growth has been low: The investment has been low relative to actual GNP and actual GNP has been below what it should be if we were using our resources fully.

Senator PELL. Has the percentage of reinvestment increased or decreased, over the last 12 months?

Dr. TOBIN. From the first quarter to the last in 1961, the percentage of business fixed investment relative to GNP remained about constant.

Senator PELL. The percentage of investments?

Dr. TOBIN. Yes. But, as we move to full employment, the percentage of investment in our GNP will increase further.

Senator PELL. That is, in capital production?

Dr. TOBIN. Yes, sir, because the structure of our system is that as corporate profits increase and there are more corporate retained earnings available for investment, there are more savings from personal incomes. There will be more savings from Government also, through the Government in the form of surplus.

There are two sides of it.

We will be able to increase our GNP and get to full employment only if we do have enough demand for investment to use that savings, and if that does come about, then our share of investment in GNP will increase as we move to full employment and that will be good.

Senator PELL. In essence, the situation has improved, the percentage is increasing as the recovery goes along?

Dr. TOBIN. Yes.

Senator PELL. I noticed, Dr. Heller, in your legislative proposals, you suggest amendment of the Welfare and Pension Plans Disclosure Act to have the authority vested in a responsible Federal agency to enforce the statute.

Do you have any opinion as to which agency should be the responsible Federal agency?

Dr. HELLER. I do not.

Senator PELL. You purposely worded it this way?

Dr. HELLER. I purposely worded it this way, because this is something that will be, I am sure, taken up by the Secretary of Labor and others who are more directly involved in this matter. This is something on which we just do not have an opinion.

Senator PELL. And finally, I noticed in your presentation, in the legislative section, that there is no reference to trade adjustment legislation. There is quite a bit of reference to expanded trade. Even in the full Economic Report, there is only a passing reference.

I was wondering if you thought that the importance of trade adjustment legislation might be underestimated, might there not be more emphasis on trade adjustment?

Dr. HELLER. Essentially, Senator Pell, we rely upon the trade message, which the President is transmitting today, to cover this subject. It is true that we brought it in because of its enormous importance to the general balance-of-payments picture, and, indeed, to efficient and full recovery in our economy. But the matter of adjustments and so forth was not gone into in detail here only because it will be gone into exhaustively elsewhere. This does not imply any judgment on our part that it is not important. It is a central part of the Trade Expansion Act proposal.

Senator PELL. I have no further questions, Mr. Chairman.

Chairman PATMAN. Dr. Heller, I wanted to ask you two or three questions.

Am I correct in assuming that the administration considers the savings and loan associations in competition with the commercial banks, in asking for equality of taxation?

Dr. HELLER. I think that there are bound to be points of competition; both competition for savings of people who have money on deposit with these institutions, and competition on the lending side, in housing in particular, since that is the special savings and loan area.

Chairman PATMAN. If you consider that the savings and loans are in the banking business, then you must assume that they are required to have 100 percent reserves, whereas the commercial banks only have a small percentage of required reserves, down to 5 percent on time and savings deposits. The savings and loan associations may lend only their investors' money; that is all they can lend. And they are dependent for their income on the difference between the rates they pay for their funds and the rates at which they lend them. In contrast, the banks create their money.

There is no doubt in your mind about that, is there?

Dr. HELLER. In terms of the reserve?

Chairman PATMAN. In terms of the money they lend or invest, they manufacture it themselves. You admit that, do you not?

Dr. HELLER. The commercial banking system creates credit, Yes.

Chairman PATMAN. Even for savings they do.

You see, they do not make any distinction between reserves against demand deposits and reserves against time and savings deposits. They do not separate these reserves; they compute their total required reserves as the weighted average of their requirements against demand deposits and time deposits.

I had a bill one time to separate the commercial banks, to get them out of the investment business. I did not think they should be in the investment business.

Forty years ago there were 31,000 commercial banks; and the banks at that time had the privilege of electing as to whether or not they would just take the lucrative part of the business, in short-term loans, manufacturing their lending funds, or whether they would have vision and meet the needs of the people in their communities. But they preferred the former. They have moved toward fewer and fewer banks, and tremendous power, and they have a fine business which is profitable. They did not ask Congress for any additional powers. The 31,000 banks have been reduced down to 13,000.

We have 43 banks now where we used to have 100 banks 40 years ago, although these years have seen the greatest growth in our history.

If the banks had had the vision that I think they should have had, they would have gotten into the farm loan business and we would not have any Federal land banks. They would have gotten into taking care of the cattlemen and the farmers and we would not have the Production Credit Administration. If they had taken care of the savings and loan business, we would not have had the savings and loan association.

If they had taken care of the short-term loans of poor people in the towns and cities, we would not have credit unions.

Instead, the commercial banks abandoned those fields entirely.

After abandoning those fields, they now find themselves where they consider they are in competition with the savings and loan associations. It looks as though they are now trying to get into that business, and in a way that will disrupt our economy.

The amount of money they now have in home loans is comparatively small. How much is it now, Doctor?

Dr. HELLER. I do not have that figure offhand. If we have time to look at the Federal Reserve Bulletin, we can probably find it.

Chairman PATMAN. Anyway, I cannot understand your reasoning on this—that the savings and loans are in equal competition with the banks, when the banks create their money, they manufacture it.

The savings and loans have grown up by providing a service that the banks were not providing in a satisfactory way. It now seems that the banks are trying to muscle in and cause a little trouble.

I just do not see the reasoning for it.

It is as when installment buying started and automobiles were being sold on time. People were making more money on installment paper than the franchised dealer made on the sale of he car. The banks would not have anything to do with this business for about 20 years. All at once they decided, "That is our business. We ought to have it."

I agree with them, even if they were a little bit late. They should have had it in the beginning.

Now I think they are too late in coming in here asking for taxes and laws to muscle in on the savings and loan associations. I think they are doing the country a great disservice. The banks have a lot of privileges and opportunities that no other business has in this country. Except for the Federal Reserve, they are the only institutions that can create money. They do this on books, with just a flick of the pen, upon the credit of the Nation.

I think, having that power, they ought to stay in the banking business and stay out of the savings and loan business.

I hope you look into this question and evaluate the question whether you think the banks should stay out of the savings business, the investment business. Would it not be better to let the savings and loan associations and the other institutions which have been built up to provide services which the commercial banks neglected go ahead and do the good job they are doing.

I think the administration, and I hate to take issue with the administration, but if they are taking the position that they have to tax the savings and loan associations to make them comparable with the banks, I think the administration is absolutely and clearly wrong. These are not comparable institutions at all.

What do you think about that, Dr. Heller?

Dr. HELLER. On a general point, I would like to say that we would surely agree that savings and loan associations have been an extremely important source, indeed the most important source, of funds for the housing industry and will, I am sure, continue to play that role.

At the same time, I suppose it is more or less natural in the American competitive system that if one part of the productive mechanism, and that is true whether it is in the industrial sphere or in the financial sphere, discovers a good thing by meeting a need, that he will soon find himself faced with competitors.

I think this is the situation that we have here, and that inherently, in spite of the kudos that the savings and loan industry deserves for the job it has done in the past, I do not think we should shield them from this competition.

I think this is something with which you would agree as a general principle.

I would like to have Mr. Tobin comment, if I may, on some of this.

Chairman PATMAN. I would like to know if he has the figure he was looking up a moment ago, about the amount of business that I referred to.

Dr. TOBIN. Real estate loans of commercial banks are in the neighborhood of $30 billion.

Chairman PATMAN. That is about half of what they hold in Government bonds? They are pretty small in that, are they not?

Senator BUSH. What is the comparable figure for the savings and loans?

Dr. TOBIN. I would like to comment on some of the differences or similarities that you mentioned between the two institutions.

Chairman PATMAN. I wish you would.

Dr. TOBIN. I do not think I understand how you could describe a savings and loan as being a 100-percent-reserve institution.

Chairman PATMAN. I say if you consider them in the banking business, you would have to consider them on a 100-percent-reserve basis.

Dr. TOBIN. The reserves, namely, their assets, are altogether earning assets, with the exception of the cash that they hold and are required to hold for safety purposes by the regulatory authorities.

Chairman PATMAN. I am not arguing that they have no reserve, but if you consider that they are in the banking business and on a reserve basis, then they are on a 100-percent-reserve basis. They can lend only the dollars that have been invested with them. That is correct, is it not?

Dr. TOBIN. That is also true of any individual bank, Congressman Patman, that they can only lend the dollars which the depositors have left with that particular bank.

The banking system, as a whole, as you pointed out, creates money on the reserve base which the Federal Reserve provides for it. But any individual bank is faced with a competitive necessity, just like a savings and loan institution, of attracting deposits away from other banks, away from savings and loan institutions, in order to have resources which it can lend.

The banks are subject to the requirement that they hold a certain amount of their assets in non-interest-bearing form, on which they get no yield.

Chairman PATMAN. If you want to get into a position of asking for equality, you know there is a law that the American Bankers Association quietly got through during the depression, when we were all concerned about the banks, and we were doing anything to help get out of the depression. It was intended to be temporary, but it became a permanent law, making it unlawful for banks to pay interest on demand deposits. Of course, bankers do not like regimentation. But that kind of regimentation they seem to like, because they have never asked for the repeal of that law.

If you are going to have equality between these institutions, do you not think you should ask that the banks be allowed to pay interest on demand deposits?

Federal savings and loans have to pay dividends on every dollar that they get.

Dr. TOBIN. I think there would be merit to reviewing whether that particular law—this is a personal opinion—any longer serves its original purpose.

Chairman PATMAN. On the reserve requirements, the exact ratios have gotten away from me in the last year or two since they brought in the vault cash, which is a kind of a pseudobusiness, the way I see it, and I cannot keep up with it too well.

But let us suppose a bank has a reserve of 15 percent which I assume is about the highest now, 15 percent on demand deposits, and they have 5 percent on time and savings deposits. If they have half savings and half demand, that is equal to a 10 percent reserve, because they lump them together. They do not separate them. That is correct, is it not?

Dr. TOBIN. That is right—16½ percent to be exact.

Chairman PATMAN. Did you want to comment further, Dr. Heller?

Dr. HELLER. Just to bring forward the figures that you requested, savings and loan associations have about $67 billion in mortgages, as against the figure of roughly $30 billion in real estate loans on the part of commercial banks.

Chairman PATMAN. Commercial banks?

Dr. HELLER. Commercial banks have a little under $30 billion and the savings and loan about $67 billion.

Chairman PATMAN. Let us break that down. How much of that is Government guaranteed paper?

Dr. HELLER. That I am unable to answer from my sources.

Chairman PATMAN. My time is up. Now we will have to start all over again. Senator Douglas?

Senator DOUGLAS. I have no questions.

Chairman PATMAN. Senator Bush?

Senator BUSH. I would just like to ask a question apropos of the chairman's question that banks create money.

Of course, if they make loans and credit the account with the amount of the loan, that does create money. On the other hand, if that loan is paid off in 6 months or a year, that has the opposite effect, has it not? The creation of money in the banking system, and I would like to be corrected if this is not true, results from, really, financing Government deficits through the banking system that are not paid off but which become a part of the Government debt. In that way, it really is the Government that creates the increase in the money supply when it does the financing on a deficit basis through the banking system. Is that not a correct observation?

Dr. HELLER. Again, may I ask Mr. Tobin to comment on that?

Senator BUSH. Yes, sir.

Dr. TOBIN. Sir, whenever the commercial banks—the banking system as a whole, adds to its assets, either by making commercial loans or by buying Government bonds, and equivalent deposits are thereby created, they are creating money, whether the assets are commercial loans or Government bonds. But they can only do this to the extent that the Federal Reserve provides the reserve base which enables them to do so in line with the reserve requirements to which they are subject. And the reserve base of the banking system depends on the assets of the Federal Reserve System which does, of course, acquire Government debt.

Senator BUSH. Therefore, the increase in the money supply which the banks may create is really controlled by the Government. In other words, if the Government does not do any financing through the banking system, then they cannot create any permanent increase in the money supply; is that not true?

Dr. TOBIN. I would not put it quite that way.

The money supply which the banks can create, no matter whether they create it by buying Government bonds or by making commercial loans, is subject to the control of the Federal Reserve, because the Federal Reserve controls the reserve base of the banking system.

Senator BUSH. Of course, the Federal Reserve—I appreciate that. I look upon the Federal Reserve as an agency of the Government, which it is, is it not?

Dr. TOBIN. Yes, sir.

Senator BUSH. So it is, in effect, only with the blessing of the Government, so to speak, that the money supply is increased through bank loans.

Dr. TOBIN. It is only with the blessing of the Government that the money supply is increased in any way.

The Government might be running a deficit and increasing——

Senator BUSH. Well, I wanted to make that point because I think, with all due respect to the chairman, he has created the opposite impression, that the banks seem to have, to him, unlimited power to increase the money supply. I do not believe that they do. I think when they make a permanent increase in the money supply it has been due to action by the Government.

If you forbid the banks from financing the Government through the banking system, by buying bonds or short term obligations, which is usually the case, if you forbid that, this would be a serious embarrassment to the Government, would it not?

Dr. TOBIN. Not necessarily. It would be possible to market the Federal debt outside the banks if it was an occasion on which you needed to market Federal debt, and at the same time it was not wise to have an increase in the money supply.

In the opposite case, you might want to have an increase in the money supply at a time when there was no need for financing Federal debt. That also can happen.

Senator BUSH. I think it would be helpful if the Government did try to finance a larger part of its needs in the market exclusive of the banks. It would be less inflationary if they could sell long-term obligations and get away from the banking system. I would agree with that point.

But I cannot get away from the conclusion that it is because the Government does, of necessity, apparently of necessity—and I think it is of necessity, myself—use the banking field for financing especially its deficits, this is what causes increases in the money supply. Is that not true?

Dr. TOBIN. I cannot go along with that, Senator, because we have had, over the years, increases in the money supply long before we had a Federal debt of any magnitude at all, and when we were not having any Federal debt that was increasing. We would have to have an increasing money supply during those years.

Senator BUSH. I do not mean to say that the money supply cannot be increased otherwise. But where banks are involved, what I say is true; is that not true?

Dr. TOBIN. I do not know to what period you are referring to. Certainly, during the war and immediately after the war——

Senator BUSH. Say in the last 25 years or 20-odd years.

Dr. TOBIN. During the war there was a good deal of bank financing of the public debt, and it would have been difficult to finance the war had reserves not been provided so that the banks could absorb a good part of the tremendous increase in the Federal debt that was occurring at that time.

Senator BUSH. I think in the last 10 years there has been a lot of it, too, since Korea or during Korea.

Dr. TOBIN. I do not think that the increase in the money supply during the last 10 years has been any different because of the Government's financing problems from what it would have been in any case.

Senator BUSH. Than what?

Dr. TOBIN. During the last 10 years I do not think the increase in the money supply has been different because of Federal financing than it would have been anyway because we needed an increase in the money supply to finance increasing volumes of trade, and we would have needed this regardless of Federal financing.

Senator BUSH. As I see it, you are not really differing with what I say, you are simply saying that there are other ways of creating money without using the banks, and that I cannot deny.

Chairman PATMAN. There is only one other way, Senator, and that is through the Federal Reserve.

Senator BUSH. They can do it, I will agree.

Well, I will not pursue that further, Mr. Chairman, unless you wish to. I have spoken to your point.

Chairman PATMAN. About the banks having to buy the Government debt, I think it should be unlawful for them to just create money to buy the Government debt. That is a privilege that no one should have.

If new money has to be created, the Federal Reserve can do that and buy these bonds. They have over $25 billion worth of bonds now. They could buy a lot more, and when the interest is paid, it would be turned back to the Treasury and returned to the taxpayers.

There is no reason why the commercial banks should buy these bonds or be permitted to buy them.

I would not object to them buying them up to a reasonable extent, but not to the extent they have.

Senator BUSH. I do not think they are required to buy them, but I think when it comes to buying them through the banking system, it does indicate Government approval of what they are doing.

Chairman PATMAN. I am sure of that.

Senator BUSH. Now, Dr. Heller and members of the Council, if I seem to dwell too much on this balance-of-payments problem it is not in an effort to embarrass anybody, but because I think all of you know that I have thought for a long time that this is an overriding issue of the gratest importance. I think it is more important than balancing the budget, myself, although balancing the budget is very important.

I wanted to address a few questions to this point of the balance-of-payments deficit.

Can you give me your estimate or thought pertaining to the balance-of-payments deficit in the last quarter of 1961? At what rate was the balance of payments running at the end of the year?

Dr. HELLER. Senator, as you know, the official figures on the fourth quarter are not yet available. They become available in about a month. Some preliminary indications have been given in the press that suggest something in the order of $5 billion at an annual rate as the fourth quarter overall balance-of-payments deficit. I cannot give any final valuation of that figure, but I suppose the figures that will become available a month from now will be of this order of magnitude.

Senator BUSH. I think I saw that figure mentioned in the press, but it rather astonished me, and I asked you to comment on it for that reason.

Can you give us any estimate which you have made of the balance-of-payments deficit for 1962, on the year?

Dr. HELLER. No; I do not have an estimate for the current year.

Senator BUSH. You do not have any estimate of what is likely to happen in the calendar year?

Dr. HELLER. No; this is something we are working on in cooperation with the Treasury Department and Commerce and other departments of Government, but we do not have one available at the present time.

Senator BUSH. You would not be able to give us an estimate of how much can be saved to military outlays, on Government loans and grants overseas, and the question of private long-term investment, and then the item of services? Are you attempting to break down those different categories and make estimates?

Dr. HELLER. This effort is currently being made and I think it is addressed to exactly the kind of question that you are raising; namely, what the various magnitudes are that are likely to develop and to what extent Government policy can operate on these magnitudes to improve our balance-of-payments situation.

As you know, Secretary McNamara has been working through the entire oversea military expenditures to try to minimize the foreign currency cost.

Senator BUSH. I was very much pleased with what he told our committee on this just this week.

Dr. HELLER. I think he has found some very impressive possibilities of cutting the foreign exchange costs without in any way undermining our overseas military strength.

Likewise, of course, there are the negotiations with Germany to try to get some offsetting procurement in the United States for military costs in Germany.

Senator BUSH. That is a big item.

Dr. HELLER. Yes; a big item. And further efforts to get a larger sharing of foreign aid by the other advanced nations, particularly the surplus nations. By this I mean balance-of-payments-surplus nations. These are among the efforts that are being made to minimize our foreign exchange costs of aid and military expenditures.

Senator BUSH. Mr. Chairman, my time is up.

Thank you.

Chairman PATMAN. Mr. Curtis?

Representative CURTIS. Our Subcommittee on Economic Statistics has gone into various price indexes, and I thought they were quite good, and just recently on the employment statistics with some of that brought out by Senator Proxmire, the chairman.

The third big inquiry that I think we need to go into quite thoroughly is—well, we don't have the indicator—for economic growth. I was sorry to again hear reference to growth figures through gross national product as an estimation of what is real economic growth. This is where I would direct my questions.

First, I think one of the basic concerns is our economic potential, which breaks down into labor force by numbers and by skill. Second, our capital plant. Third, our business organization, whatever that might be, and, fourth, I would add the state of research and development.

Maybe there is something else to be added. But now moving over into our yearly estimates of growth, of course gross national product is one of the best factors to help measure, but it measures economic mistakes. It actually measures sterile production, which the military largely is.

That sort of production is not meaningful in our actual potential. But there are other factors that suggest themselves to me that would throw light on real growth.

One of them is productivity increase. This should be related, in my judgment, to an estimation of whether we have grown.

Next would be new goods and services on the shelf. I have heard a figure that 30 percent of the goods and services on our shelf today weren't there 5 years ago. These are hard to measure, perhaps, but there ought to be some series of statistics by which we could gain insight into this.

Next is the shift in employment. When we see the constant shift from agriculture and out of agriculture into nonagricultural employment, that, to me, is an indication of real growth.

Then there is the shift from manufacturing employment to services and distribution which indicates to me a more flexible and, therefore, a stronger economy, an indication of real growth. Within the manufacturing sector and all sectors, there is the shift from blue collar to white collar, the lowering of the percentage of unskilled and semiskilled labor as part of the work force.

Next would be a measure of leisure time.

Next is the greater lengths of time per capita that our people spend in education.

All of these are suggestions of what I think would give us a real picture of meaningful economic growth instead of an almost stupid reference to those economic products that I have heard year by year and I quetsion whether that is giving us a good indication of whether we are growing or not growing.

My questions will be directed along that line. However, you might want to make a preliminary comment.

Dr. HELLER. I have just a brief comment to say, that I agree with you that our measurement of economic progress is imperfect. Certainly there are factors in, let us say, air pollution and stream pollution and so forth which you would want to subtract from our index of well-being if you had a perfect measure. But to date, the overall advance in real gross national product, that is, with price changes squeezed out of it, is the best comparative measure that we have been able to find.

Representative CURTIS. It is so inadequate when you stop to analyze what is in it that I just hate to see us using it without a reference to other things that are more meaningful.

Just take this in relation to economic potential. For instance, for military reasons, if we had to mobilize we are more interested not in what we did last year in the way of production, but what we would be capable of doing because of the plant that we have. Take advancements in communications and transportation which actually, I would think, would tend to decline the GNP, because it would show more efficient ways of getting around and communicating. Yet for a mobilization or to perform a greater economic achievement, that would be a tremendous plus item, like the investment in our highways. That is what I mean. I think there has been much misleading of our people going on and misleading also in our national policy by not being more analytical in what real economic growth is. That is the reason I raise the point and say, "Sure, I think gross national product is one of the best indicators that we have, and probably, as you say, the best thing we do have, if we want to talk about a single thing. But it is so inadequate to measure meaningful economic growth." I think we are making a grievous mistake to refer to it constantly as if if were giving us a meaningful result.

Dr. HELLER. I have just one additional comment, that in our chapter 2 on economic growth we have acknowledged a number of the points you are making and have discussed some of the factors involved in measuring economic progress and growth. This is not a problem which we have ignored by any means, though a great deal more work needs to be done on it.

Representative CURTIS. It is just a matter of emphasis, but I think a very important one. I have two points, one picking up Senator Proxmire's references to my references in regard to unemployment figures and the military. I don't know where he got the figures, or where you got them, in regard to the increase in November for the military. I will tell you where I got mine. It was by subtracting the total labor force, including Armed Forces, from the civilian labor force to give me the 2.5, and then in November I did the same thing which gave me the 2.8.

I think he produced a figure of 176, or something. Can you clear up that discrepancy?

I am referring to the first two lines on page 9 of the January 1962 Economic Indicators, where we have our unemployment, employment, and wages. The first column is total labor force, including Armed Forces. The second column is civilian labor force. I subtracted the two, thinking that gave me the correct figure on the military, which I assumed it would, in October, which is 2.5. November would be 2.8 and December would be 2.8.

Dr. HELLER. I think what we should do is provide for the record, if we may, a reconciliation of the two sets of figures. The figures we were using a moment ago in the exchange with Senator Proxmire were BLS figures. There is, of course, always some rounding problem when we are dealing with economic indicators, and I imagine that is part of our problem here.

That is, I notice in the BLS figures that September to October has 39,000 increase in the Armed Forces; October to November, 171,000; November to December, 56,000. So we had a September to December increase of 266,000, and an October to December increase of 277,000.

(The following was later received for the record:)

Reconciliation of labor force data from economic report and economic indicators

[Millions of persons]

	Total labor force		Armed Forces		Civilian labor force	
	Report [1]	Indicators [2]	Report [1]	Indicators [2]	Report [1]	Indicators [2]
1961:						
September	73.670	73.7	2.547	2.6	71.123	71.1
October	74.345	74.3	2.586	2.5	71.759	71.8
November	74.096	74.1	2.757	2.8	71.339	71.3
December	73.372	73.4	2.813	2.8	70.559	70.6
Change:						
September–October	.675	.6	.039	−.1	.636	.7
October–November	−.249	−.2	.171	.3	−.420	−.5
November–December	−.724	−.7	.056	0	−.780	−.7

[1] P. 231.
[2] P. 9.

Representative CURTIS. The other comment on the long-range figures is the fact that you mention in November the increase of 500,000 from October to November, but then from November to December there is a decrease of 300,000. I still think the point that I tried to make is well taken, that this 300,000, as it looks to be from what I gather, of the shift in the military, occurring as it did at this time, looked like it was the primary factor.

I didn't suggest it was the sole factor.

Now, I have a question which is a general policy one that has disturbed me very much. The President's message on trade liberalization reached us today on the floor of the House. His previous message, and we are working it over in the Ways and Means Committee, was on his tax proposal. The tax proposal is restricting and imposing a greater burden on our private investment abroad. Regardless of the reasons for it, the net result is going to be that the trade policy is on the theory to liberalize and to encourage. It just strikes me that the two are going in completely opposite directions.

The trade and investment are tied very much together. To damage investment is going to damage trade, willy-nilly. It strikes me as being a different emphasis on approach.

Dr. HELLER. I think, Congressman Curtis, we have to distinguish between short-run and long-run effects and distinguish between the stimulus to investment that comes from high tariff walls around the Common Market and other stimulants to investments.

Taking the first point, to the extent that our investment overseas takes many years to pay off, so to speak, in return of earnings, it worsens the balance of payments at the present time, when we put long-term funds into Europe. The two measures are consistent in this respect, that the reciprocal liberalization of tariffs with the Common Market is designed to lower the tariff wall around the Common Market, to lower the barrier for the goods that go from our plants over that wall, and therefore make it less necessary for American industry to pole-vault the wall and put investments in Europe.

It is consistent with this for the tax proposals to suggest that special inducements for investments in Europe be reduced or removed, because they again, tend to attract investments to Europe instead of having us invest at home.

Representative CURTIS. Of course, you used the word "investment." There is a question as to whether that is an inducement or whether it is simply a fair treatment. But getting beyond that, on our investment abroad, sure, the tariff has some relation to it, but a great deal of it is just the economics involved of building a plant closer to the market.

I suggest that is the basic reason for our investments abroad, not the tariff. I think that you interfere very markedly with that process in the particular areas where the tax recommendations are, the so-called tax saving as we have analyzed.

In Switzerland, it isn't a tax saving against the U.S. taxes as much as it is a U.S. corporation going to Switzerland along with the British, who avoid the impact of British taxes. It is just like a West German company going into Switzerland. Then the treatment of the individual employees abroad which the companies send is going to be somewhat restrictive on our companies following this procedure. So even apart from the long-term investment angle which you have raised, which I think is a legitimate one, it is something that I would criticize in its essence to say, what a very foolish policy to destroy our long-range picture, in light of trying to meet a temporary situation, unless, indeed, we are that badly off.

There is one other idea I might express. I think this so-called liberalizing of trade, talking in terms of just tariff, is certainly distracting. It has distracted my attention, but I will no longer be distracted, from what the real thing is. These so-called free trade talks in terms of tariff result in taking off a tariff and substituting a quota or a subsidy or a license in its stead.

And that ends up in more restrictive trade. Western Europe never used a tariff as their primary method of impeding or regulating trade. They have used quotas, licenses, subsidies, monetary exchanges, state trading, cartels, and so on. Instead of only talking in terms of tariff reductions, if you are going to replace tariffs with quotas and licenses, you are going to end up, in my judgment, with more restrictive trade.

Dr. HELLER. I would fully agree that one has to look at the whole range of restrictions—tariffs and all others.

May I ask Mr. Gordon to comment on this point?

Dr. GORDON. I would agree that it is virtually impossible to get the tariff reductions by using other types of restrictions, such as quotas. But I think this recent history of Western Europe has been a history of steady movements toward the elimination of quantitative restrictions, reductions, at least, of quantitative restrictions, on imports, particularly as they affect us. It is quite true that there remain in Western Europe fairly substantial quantitative restrictions, some of them of a discriminatory sort, which affect the trade of Japan, Latin America, and so forth. But the general picture, I think, is one of declining use of quantitative restrictions and heavier and heavier reliance on tariff as the principal means of protection.

I would be virtually certain that when negotiations occur with the Common Market under the legislation with respect to trade policy, which it is hoped will pass the Congress, that safeguards will be incorporated in such an agreement to assure that tariff reductions are not frustrated by the imposition of other kinds of trade-reducing limitations.

Representative CURTIS. I would have felt a lot better about that if the President, in his state of the Union message that came down today, had made reference to it. But it very carefully says tariff reduction in regard to Western Europe. I would feel a lot better if people in our own country who have been advocating this so-called free trade know about this. When our textile people, for example, brought up their traiff case through the escape clause, they then went over and got voluntary quotas from the Japanese, so quotas were supplanted by tariffs. The same thing was done on residual oil, by getting our oil companies to agree to quotas in lieu of tariffs. In lead and zinc they supported a subsidy program. So the people who have been doing a lot of squawking for freeing up trade in our country seem to be perfectly content to supplant a tariff with what I regard as a much more aggressive trade barrier, a quota, a license, or a subsidy. I like your answer; but, without the President having made this clear after Senator Bush's statement which I know was brought to his attention and pointed these things up, I am not sure that the Executive, the President, feels that way.

Dr. HELLER. I think another final point that could be made, Mr. Curtis, is the very basic point that we are adherents to GATT, as are all the members of the Common Market.

The rules of GATT are quite restrictive with respect to the use of quantitative restrictions on trade, and any negotiations conducted through the machinery of GATT for the reduction of tariffs will automatically erect a barrier to the substitution of quotas to take the place of tariffs.

In other words, the rules of GATT, which are very relevant here, would, I think, offer us considerable assurance that tariff reductions would not simply be frustrated by the imposition of quotas.

Representative CURTIS. Thank you. I have consumed my time, but I must make a last observation, that in spite of GATT, Western Europe, through import and quantitative restrictions, has been a very restrictive trader over recent years, and I think it is due to the United States having been the freest of traders, relatively.

Dr. HELLER. But I think it is also true, Mr. Curtis, that if you look at the recent history of commercial policy in Western Europe you do find a steady movement for the elimination of quantitative controls on imports.

Chairman PATMAN. Senator Proxmire.

Senator PROXMIRE. I want to take a minute, to begin with, on the point that Congressman Curtis referred to.

The figures to which I referred are on page 231 of your report. This is what shows the increase in the Armed Forces from 2,586,000 to 2,757,000, between October and November, and it was the subtraction that gave me 171,000. It is my understanding from talking with the staff of the committee that the rounding figure is what provides the distortion in the statistics which seems to give a figure almost as large as 300,000 for the increase.

As a result of this, I still maintain that substantially more than half, close to two-thirds or more, of the increased unemployment seems not to be accountable on the basis of military action.

To get back to the figures that we were talking about, or, rather, to get back to the part of your statement I was talking about, it seems to me that if we take your subsection 1 in the actions of Congress; 2, the accelerated Federal orders and payments on a wide front and subsection 4, an expansionary budgetary policy—which I take it is the increase in military activity uncompensated by tax increase—as I calculated it as quickly as I can about two-thirds of this total overall increase is military, about one-third transfer payment increase, and other transfer payment increase. Well, because they are transfer payment increases there is going to be an automatic increase in taxes which will result in a net effect on the economy that will be pretty much of a washout over a period of a couple of years.

Dr. HELLER. Of course, on the matter of washout, one would hope that the expansionary part of it came when we needed it and that the somewhat more restrictionist part will come when we need that, or can at least stand it in the face of the strength of demand in the private sector of the economy.

Senator PROXMIRE. I wonder about this: I would feel that the estimates of the Council are fairly optimistic on feeling we can get down to 4 percent unemployment rate by mid-1963. Perhaps not, but in view of the tendency of the work force to expand as we move toward full employment, it would seem to me that that is the situation.

Therefore, it may well be that the borrowing from the future, so to speak, will come at a time when we are still struggling to get to a lower unemployment figure while unemployment is still a serious problem.

Dr. HELLER. I would not rule out this possibility, that some of this effect of increase would come before it would be ideally desired in the expansion phase of our business recovery. At the same time, given the prospects for increase in demand from the various sectors of the economy, given the fact that the Federal budget is increasing rather than decreasing in overall expenditures by about $3.5 billion, there will be, of course, a continued contribution from the Federal Government, and, indeed, as usual, from the State and local governments, to the continuation of recovery.

Senator PROXMIRE. The third figure which I skipped, that is subsection 3, pursued policies to ease money and credit, this was something that you developed to some extent in reply to a question from Senator Douglas.

As I calculate it, the increase in the money supply between December of 1960 and the most recent figure, December of 1961, was an increase of 3½ percent, about 140 billion to about 145 billion. At the same time, the increase in the gross national product was 8 percent.

In view of the fact that the gross national product measures the increase in value added, and involves all dollars—comparing it on a dollar basis, the gross national product—therefore, it seems to me that this was not an eased credit situation; on the contrary, the credit situation seems to have been tightened somewhat.

Furthermore, the ratio between the money supply and the gross national product is now as low as it has been, or lower than it has been for more than 30 years. It is now something like 26.5 percent, the money supply, that is, as a ratio of gross national product.

So how can you argue that this was a contributing factor to the expansion in view of the fact that it failed to keep pace with the expansion in the gross national product?

Dr. HELLER. I would like to make a general comment on this and then ask Mr. Tobin to comment further.

We are, of course, concerned about the adequacy of the money supply, both for recovery purposes and for accommodating longer run expansion. I am sure you will find in your discussions with Chairman Martin of the Federal Reserve System that he, too, is concerned with this problem. In making these measurements it is also true that the ratio has been dropping. Essentially we have been making our available supply of money work harder.

In other words, the velocity of circulation measured in terms of national income has been increasing, in effect, if you will, through more efficient use of the money.

Senator PROXMIRE. If you will yield at that point, this always happens whenever you contract the money supply or whenever the money supply fails to expand as the gross national product expands. You automatically by definition have an increase in velocity. There is no other possibility. You are bound to have it. It would seem to me that you can't very well justify the failure of the money supply to keep pace with the gross national product on the grounds that you have greater velocity. Of course, you do. You couldn't have anything else.

Dr. HELLER. I think whereas part of this is, as you say, necessity being the mother of invention, at the same time our monetary institutions have increased in their efficiency over this period.

But abstracted from that, and addressing myself to your points about the 8-percent increase in the rate of the gross national product and the slower increase in the money supply that, again, is a case, in part, of matching a cyclical figure, that is a recovery figure, and a longer term trend figure in the money supply. That is to say we had a falling off in gross national product, and you are measuring from the trough of that period to the fourth quarter which had a rise of $40 million.

In the first quarter there was certainly a considerable part of the money supply that wasn't even working very hard.

Senator PROXMIRE. If you want to take any longer figure at all, you can take almost any figure or any time period since 1945. I argue that you would get the same kind of a contraction of the money supply with regard to gross national product. I have figures here from December 1955 to November 1961. In the actual money supply, seasonally adjusted, it goes from $134 billion to $144 billion. On the other hand, if it had kept pace with the GNP, it would have gone from 134 to 165 billion.

What I am saying is that there has been a steady tendency on the part of the Federal Reserve to contract the money supply in relationship to the job it has to do.

They always say, "But it is more efficient now," or "they are doing a better job," or "there is greater velocity." When you look at the statistics, it seems that the statistics are very strong. Furthermore, you have the best evidence of this, the high interest rates, which we still have. I am not trying to make an academic point, but I am arguing that this has a real tendency to discourage home construction and homebuilding because interest is such an enormously important element in the monthly payments and the cost of building homes.

I argue that this has been retarding the expansion and has been keeping us from moving ahead as fast as we ought to move. If we followed a policy simply of neutrality with regard to the money supply, let the money supply keep pace with the gross national product, as some in Congress have advocated, some very conservative in Congress, as you know, we would have had a lower interest rate, we would have had a greater money supply than we have at the present time.

Dr. HELLER. I will make just one further comment and then ask Mr. Tobin to comment in addition. As you will see on page 26 of the Indicators, the money supply has been rising since about April of 1960. In other words, during the period that the gross national product was falling in the recession, the money supply was rising, and it has continued to rise with the exception of a very short break just after midyear since that time. So it has now been rising for better than a year and a half.

Let me put it this way: The current situation does fit in with the concern that I think we share. It fits into an expansion designed to accommodate the growth in gross national product.

I would like to ask Mr. Tobin to comment further on it.

Senator PROXMIRE. I might say at this point it seems to me what is happening is that in the last few months at least you might argue that the money supply has been fairly neutral. It has expanded about at the same rate as the gross national product on a long-term basis. It has had a restrictionlike effect if you look at it on the short-term basis and recognize how rapidly the GNP has expanded in the cycle. But it would seem to me that it is hard to make a case that there has been a positive and effective action on the part of the Federal Reserve Board to expand the money supply at a more rapid rate of growth than the cyclical rate of growth in the gross national product.

Dr. TOBIN. I think you are quite right to call attention to the ratio of money supply and GNP and to the necessity in the long run for having a growth of the money supply along with GNP. At the same time, I think it is worth recognizing that there are assets which are close to money, which are good substitutes for money, and which have expanded in the last year at a faster rate than the money supply proper. Total bank deposits and currency, including time deposits as well as demand deposits in banks, have expanded 7 percent in the last year.

Take a total measure of the liquid assets held by the public, including not only bank deposits and currently but savings deposits and shares in other savings institutions, and U.S. savings bonds and short-term Government securities held by the public—this has grown also by 7 percent during the last year.

The public has shown a preference for holding the liquidity in these alternative forms in the last year.

The second point I would make is that the money supply could have expanded faster during the last year had there been, on the one hand, preference for demand deposits by the public, and on the other hand a greater demand for business loans and other loans than did develop. The reason it could have expanded faster is that the Federal Reserve was following a policy of providing free reserves of roughly $500 million throughout the year.

Presumably, if required reserves had increased, the Federal Reserve would have, under this policy, provided the necessary addition to reserves to provide what was needed by the banks in the way of reserves. This policy is in considerable contrast to what they did in the previous upswings. We are now a year, almost a year, from the trough of the recession. We still have free reserves in the neighborhood of $500 million, whereas in the previous upswing, and in the one before that, free reserves fell permanently below $500 million and as early as 4 months after the trough of the recession.

So, there has been a change in the way they have handled this recovery on the monetary side in comparison with the way they handled those previous recoveries.

The final point I would like to make, or a semifinal one, is that in regard to your point about velocity, naturally by definition velocity increases when GNP expands faster than the money supply. There are two causes that one might distinguish for such an increase in velocity.

One is the kind of longrun economy in management of liquidity which Mr. Heller referred to a minute ago, and the second is the incentive of higher interest rates for business firms and individuals to get along with smaller cash balances, less deposits, less liquidity. We haven't had the second phenomenon to any marked extent during the past year. On the contrary, interest rates have been, on the whole, stable throughout the year in contrast to the previous upswing.

Finally, to indicate that we are also very much concerned with having a sufficient expansion of money, and liquidity in general, to handle an expanding economy, could I refer to the last part of our discussion on monetary matters in the report on page 92?

Senator Proxmire. Again, you have your very convincing and appropriate set of statistics. I still think that mine have some validity. I call your attention to your charts on page 87, the three charts, which show that it is true that the interest rates have been more stable, regardless of what you choose, the FHA mortgage yields, Treasury yields, or corporate bonds.

But this also indicates to me that there was no constructive part played by monetary policy to get us out of the trough, out of the recession. Interest rates remained in the prerecession period, high. They didn't come down. They didn't play a constructive part. I know that there are balance-of-payments problems involved here. I think there is an answer there, too.

Dr. Heller. On that point, of course, the question is what would they have been in the face of a different Federal Reserve policy, and I think we have reason to believe in comparing them, as Mr. Tobin did, with previous recoveries, that monetary conditions have been kept easier longer in this recovery than in any of the previous postwar recoveries.

This, of course, is as it should be in the light of the continued slack in the economy. Also, some of the Treasury debt handling, and trust account operations, there has been a contribution to the maintenance of the flow of investment funds in the economy.

Finally, in the housing credit field, as a matter of fact in all the credit operations of the Government, there has been a further contribution to making investment funds available.

Senator Proxmire. Except that I call your attention again to the chart on page 87.

Corporate bond interest rates are higher now than they were in 1953–55, higher for FHA mortgage yields. They are about the same for Treasury bill rates in 1960–61, on the one hand, and 1957–59, on the other. So as far as results are concerned and as far as most people—and I think with a great deal of sense—regard the best measure of whether a monetary policy has been tight or easy, as to whether interest rates are high or low, this is what they have to pay, and this seems to indicate that interest rates are higher now than they have been before at a comparable period. It is true that the trend may have been more stable. It is true that there may not have been a tendency on the monetary policy to have a restrictive effect. But, nevertheless, it is also true that interest rates still remain high.

Dr. Heller. To that we would say, "Amen." We wish they were lower, too. But we do feel that policy has accomplished something at holding them through these levels through 9 or 10 months of brisk recovery.

Senator PROXMIRE. The reason I labor this is because I feel this is one area where there has been traditional Government policy.

I have to be shown that by reducing taxes and increasing spending we can move out of a recession period. Monetary policy for economic stabilization has been practiced for many years. We have all kinds of precedent for it. There is relatively less resistance to it; therefore, it seems to me that we should do the best we can with tools that have been proven, that have been used before, that are acceptable, and show that we have made a real effort in this area before we move into this more controversial and unproven area.

What relationship does your Council, Dr. Heller, have with the Organization for Economic Co-operation and Development?

Dr. HELLER. Senator, we attend the meetings of a number of the organs of the OECD. The Council Chairman serves as chairman of the delegation to the meetings of the Economic Policy Committee which meets several times a year. We also are represented on the working parties on economic growth and on the balance of payments of the EPC.

Senator PROXMIRE. In the report that came out, which was released in November 1961, on the United States—I am sure you are familiar with it—what part did your Council play in this report?

Dr. HELLER. I think that this relationship should be made clear. This is not a report that can be controlled in any way by the government of the country which is under examination. This is a report made by the staff and the organization of the OECD. Now, it is true that they send it in an early draft for comment and review by various agencies of the country in question, but primarily for factual accuracy. What they say on policy is something that is of their own determination and not under the control of the country in question.

Senator PROXMIRE. In other words, the policy discussed in a story on the front page of the New York Times which disturbed me very much seems to be a fairly radical departure from what I have been given to understand before. I would like your viewpoint on it, because I think the basic argument is if you have a big enough budget, if you tax enough and spend enough both, regardless of whether you have deficits or surpluses, this alone tends to promote growth, and this alone is, per se, beneficial to the economy.

Let me read you the section on page 40 of the report. It says:

> It has been pointed out above that there has already been a significant change in the impact of the Federal budget, which operated as a counterexpansionary force in the second half of the 1950's. It may well be, however, that the achievement of the Government's objectives in employment and growth will entail in the years to come greater reliance on the Federal budget as a means to insure an adequate level of final demand.
>
> This need not imply a continuous accumulation of budgetary deficits; a regular increase in the absolute dimension of the budget can equally lead to the desired result. Indeed, the experience of the second part of the 1950's suggests that, in the absence of a sufficiently strong autonomous expansion of other components of final demand, the stagnation of the Federal demand for goods and services has contributed to the emergence of the slack in the U.S. economy.

Do you subscribe generally to the feeling that the growth of the budget, disregarding whether you have deficits or surpluses, this, by itself, will tend to encourage growth in the economy, and do so significantly and substantially?

Dr. HELLER. I think as a part of departure I should say "No." That is, we feel that the size of the Federal budget, the proportion of our total resources that is used in Government expenditures, should be determined by the comparative advantage of a dollar spent publicly, and that of a dollar spent privately.

In some years, perhaps most years, that will mean a rise in the Federal budget as the economy expands, even though the Federal budget remains the same proportion of GNP as it has over the past 7 years, right around 15 or 16 percent.

Senator PROXMIRE. I think there are things that were left out that we can include.

Dr. HELLER. At the same time, one of the sources of increased demand in the economy at such time when Government expenditures can efficiently expand would be rising Federal expenditures. This, however, would not be something that should be pushed through thick and thin as a guarantor, as it were, of economic growth, for economic growth involves action on a great many fronts. Whether Government expenditure increases in a particular year are appropriate or not depends on the situation and the stated preferences of citizens.

Senator PROXMIRE. For example, on the basis of this, what would happen if we could have, it is very hard to imagine but conceivable, an armistice in the cold war that would work, conceivably, a reduction in armaments that would cut our military budget from what we expect, $52 billion down to, say, $30 billion, reduce it by $22 billion.

Would this mean that the economy would necessarily contract or that the Government would have to spend an additional $22 billion in other areas in order to avoid contraction?

Dr. HELLER. No, Senator, it would not. After all, we have the tax-reducing machinery readily at hand. We find that by and large the private consumer tends to spend about 93 percent of his disposable income. If we increase his disposable income by tax reduction, I think both economic theory and past experience tell us that we can adjust quite readily, not without some pain in particular industries and areas, but we can adjust quite readily to the overall impact in the large reduction in armaments. Surely the post-World War II experience lent impressive evidence, as did the post-Korean wind down of expenditures on the military lends impressive evidence on just this score.

Senator PROXMIRE. I see my time is up, but it seems to me that in a statement as important as that, and it was the statement picked up by the newspapers as the principle news out of this report, that the position of the United States being in opposition to it should have been registered somehow, or it should be known in view of the fact that it is an important part in the OECD.

Dr. HELLER. I think the statement has to be read very carefully in terms of its particular framework. You will note that it is put in a conditional fashion, that if you don't do it one way you do it another. The way it was reported I must say did suggest a stronger interpretation, a positive recommendation that we increase our Government expenditures constantly as a source of economic growth. I think this interpretation is a good deal stronger than the statement itself meant to be. Put very carefully in the context, I don't believe it comes out quite as strongly as it did the way it was generally reported.

Senator PROXMIRE. My time is up.

Chairman PATMAN. Senator Pell.

Senator PELL. Dr. Heller, do you conceive of the discouragement of the flow of American capital abroad for investments in the advanced countries as being a permanent or a temporary measure until our balance of payments comes back into line?

Dr. HELLER. If you are referring to the tax proposal——

Senator PELL. The taxable dividends of corporate income abroad, and earnings.

Dr. HELLER. Let's put it this way: In the immediate postwar period, at the time we were trying to contribute to the reconstruction of Europe, to the time of the Marshall plan, provisions of the tax laws which tended to have a favorable effect on oversea investment were wholly consonant with our policy, shortrun and longrun.

At the present time, as I pointed out in response to an earlier question, oversea investments give us an additional problem with respect to our balance of payments. In the longer run they would, of course, return funds to us in the form of dividends. If we were to change from a period of dollar glut back to a period of dollar shortage, one might take a somewhat different view on whether there should be special tax incentives for investing abroad.

The proposal that has been made has been primarily directed to the withdrawal of the inequities involving the tax havens and the neutrality of treatment between investments at home and investments in advanced economies abroad.

Senator PELL. Pursuing the question of Mr. Curtis, earlier, do you not see a certain incompatibility with this proposal and the amount of trade abroad?

Dr. HELLER. Not really, Senator, because both of the measures are designed to make investment in the United States more attractive relative to investment abroad. I think it is fair to say that the tax proposal is not designed as a discouragement or as a penalty of some kind on investment abroad, but the withdrawal of what is now a differential favoring such investment. This is a differential which has been in the law for a long time. It is simply being proposed that the treatment be neutralized between investment here and investment in advanced economies abroad.

(A supplementary statement follows:)

The question was raised in the hearings whether the administration's proposals in respect to taxation of foreign subsidiaries of U.S. corporations are consistent with the spirit of liberalization of international economic transactions which animates other administration proposals, notably the new trade expansion program. In our view, the tax proposal and the trade proposal reflect the same liberal spirit. Both are designed to reduce artificial barriers and incentives which now affect the pattern of trade and investment. Both are designed to permit and to encourage trade and investment decisions which respond to basic economic factors, market opportunities, and competitive advantages. The proposed trade legislation will reduce tariff barriers which distort the pattern of trade and investment. The proposed tax legislation will help to eliminate tax differentials which distort the pattern of trade and investment.

At present, tax rates on corporate profits are lower in many other countries than they are in the United States. Maximum tax rates on corporate profits are 50 percent in France, 47 percent in the Netherlands, 40 percent in Sweden, 31 percent in Italy, 28½ percent in Belgium, and less than 20 percent in Switzerland. Moreover, because of more liberal writeoff provisions, investment tax incentives, and other favorable tax treatment, the effective tax rates are frequently substantially lower in other industrial countries than they are in the

United States. One study, for example, shows the effective tax rate, on a basis comparable to the 52-percent U.S. rate, to be about 40 percent for France, 20–22 percent for Belgium, and about 25 percent for Sweden. In addition, for those corporations which choose to locate their head offices in foreign "tax havens" even when operations occur elsewhere, the corporate tax rate can generally be reduced to less than two-thirds of the rate in the United States.

These differences in taxes have two effects of great concern to us: First, they aggravate our present imbalance in international payments. American capital is attracted overseas, and earnings of U.S. subsidiaries abroad are frequently reinvested abroad instead of being repatriated to the United States. American firms tend to reinvest abroad 55 percent of all foreign earnings after taxes; the figure for domestic reinvestment of domestic earnings is 47 percent.

Second, the differences in tax treatment encourage U.S. firms to invest for production abroad instead of investing in the United States for production of goods to export. Even in the case of a product which could be produced in the United States and landed in Europe cheaper than it could be produced abroad, an American firm might find it advantageous to invest for production abroad because of the tax difference. Such distortion of investment incentives hinders the achievement of a full employment economy at home and results in a less efficient use of world resources.

The existing provisions for tax deferral on earnings not repatriated to the United States provide an artificial inducement to foreign investment as compared with domestic investment. There is, in effect, an interest-free loan of the difference between the foreign tax bill and the tax which would have to be paid if all earnings were returned to the United States. We believe that investment in other advanced countries should not be favored over investment in the United States.

At the same time, liberal tax treatment on investment by other countries may encourage foreign firms to expand and modernize their plan and equipment. Such incentives undoubtedly place some U.S. firms at a competitive disadvantage in world markets. Through the proposed investment tax credit of 8 percent on new machinery and equipment, and through a revision of our depreciation guidelines, the administration hopes to place American firms on a basis more comparable to that of their foreign competitors.

Even with parity of tax treatment and reduced tariff barriers, there will continue to be many market opportunities which American firms can best serve from foreign plants. Foreign investment to respond to these opportunities can and should take place. Nothing in the administration's program would in any way interfere with such investment.

Senator PELL. What is the custom of other countries, Western European countries?

Dr. HELLER. I am not certain that I can give you a useful answer on that. I know that some of them provide special incentives to their investments abroad and some do not.

Senator PELL. I was wondering, because I understood the same thing, that the majority of them did give incentives to nationals to invest outside.

Dr. HELLER. I think quite a few of them do. In fact, the majority also have direct controls over investment abroad, which we did not have and do not intend to have, because there is where the real interference with the market freedom in this field would occur. It is pointed out to me that only Canada, Germany, and Switzerland allow the free flow of capital among the advanced countries of the world.

Senator PELL. What were those countries?

Dr. HELLER. Canada, Germany, and Switzerland.

Senator PELL. I have one other question. What do you feel would be the difference in revenue to the Federal Government if a tax was put into effect on dividends and interest? What is the estimate?

Dr. HELLER. I am sorry, I don't have the estimates available. I am sure that Secretary Dillon would have those when he appears before you.

Senator PELL. That is all right. Thank you.

Chairman PATMAN. Dr. Heller, I wanted to ask you two or three questions. I would like to ask each one of you gentlemen this question about interest rates. Are interest rates generally determined by supply and demand for money?

Dr. HELLER. Given the U.S. Government as one of the suppliers and demanders, yes.

Chairman PATMAN. Do you other gentlemen agree with that?

Dr. TOBIN. I would amend it slightly to say that the whole structures of interest rates, because there are a lot of different rates, are determined by the supply and demand for different kinds of assets and debts and for real property.

Chairman PATMAN. Do you believe in a free market in Government bonds?

Dr. TOBIN. There is a market in Government bonds in which the Government, both the Treasury and the Federal Reserve, is in various ways a large factor.

Chairman PATMAN. Would you say, though, that there is a free market in Government bonds?

Dr. TOBIN. There is a free market in the sense that the price is determined by the trading of people on both sides of the market. But the Government is certainly the major factor in the market and could make the market one way or the other as it pleased.

Chairman PATMAN. Would you tell me if I am correct in this: Looking at table B-47 of your report, this indicates that last year the interest yield on corporate bonds, triple A, was never below 4.22 percent. That was in March of last year. Then, throughout the rest of the year, the rate rose to 4.42 percent in December. On the other hand, we go back to 1953, and we find that the average for that year is 3.20 percent. In 1955, the average yield on high-grade corporate bonds was 3.60 percent. In 1957, the yield was 3.89 percent.

Yet, in all of these earlier years I have mentioned 1955, 1953, and 1957, the Federal Reserve had what was admittedly a tight money policy for the purpose they said of putting a damper on the economy.

You know one of the committees of which I am a member held hearings in December of 1957, with members of the Federal Reserve Board, and a number of the Federal Reserve bank presidents. They told us that what they had been trying to do in 1957 was to put a damper on the investment boom, because they felt that business capacity was expanding too fast; that was with the rate of 3.89 percent.

Yet, in 1961, you had an average rate on high-grade corporate bonds of 4.35. What puzzles me is this: If interest rates are a reflection of the demand and supply of bonds, how is it that your report repeatedly refers to monetary policies last year and monetary policies now, as being an easy money policy? The Federal Reserve called its policy in 1953 and 1955 and 1957, as a tight money policy.

I would like to have your comments on that.

Dr. HELLER. May I ask Mr. Tobin to comment on that, Mr. Chairman?

Dr. TOBIN. Well, I think the easiness or tightness of monetary policy can be measured by a number of things, of which the level of interest rates is one, and in those terms, looking back as you did over the past decade, you have to say that in the long-run trend it has been toward a tighter policy over the past decade since the pegging of interest rates by the Federal Reserve was ended in 1951.

Easiness or tightness can also refer to the availability of bank reserves and the changes in interest rates that are going on in relation to the general changes in the economy. In that sense, you could say that during the past year, things were relatively easy.

I think another factor to consider is that there is a good deal of stickiness and persistence in interest rates. That is why it took them some time to rise from the levels that they were in the early part of the postwar period. One of the major factors in the markets for these securities and loans is the expectations of people as to what interest rates are going to be. Those expectations are greatly colored by what has happened in the recent past. One of the factors that has been at work in the past year has been expectations on the part of many people in the market, that interest rates were not going to fall, and in fact, that they were most likely to rise, as they did in the previous upswings.

Also, I think that possibly during the last decade, interest rates have more and more acquired some premium for expectations of inflation, and part of the reason for the change in the relationship between interest rates on bonds and other debt instruments and the ratio of dividends or earnings on stocks to stock prices, is a change in expectations about the price level.

We would anticipate—and certainly hope—now that these expectations would change to expectations of stable prices. This would mean that gradually we may get the inflation premium shaken out of interest rates over the next few years.

Chairman PATMAN. I wonder if there has ever been a time in history when there wasn't plenty of money available at a price.

Dr. TOBIN. That is a broad sweep, Mr. Chairman, but generally, I agree, money is available at a price.

Chairman PATMAN. Well, without objection, each member will be allowed to extend his own remarks in connection with anything that he considers germane in connection with this hearing, and that will apply to the whole hearing.

I will insert at this point, a table about the material distribution of U.S. Government securities held by Federal Reserve banks in millions of dollars, and also the rates of long-term Government bonds and 91-day Treasury bills.

Senator Bush, would you like to ask any questions?

(The material referred to follows:)

Rates on long-term Government bonds and 91-day Treasury bills

	Long-term bonds	U.S. bills		Long-term bonds	U.S. bills
Yearly average:			Monthly, 1961—Cont.		
1950	2.32	1.218	May	3.73	2.288
1953	2.94	1.931	June	3.88	2.359
1955	2.84	1.753	July	3.90	2.268
1957	3.47	3.267	August	4.00	2.402
Monthly, 1961:			September	4.02	2.304
January	3.89	2.302	October	3.98	2.350
February [1]	3.81	2.408	November	3.98	2.458
March	3.78	2.420	December	4.07	2.594
April	3.80	2.327			

[1] Fed announced abandonment of "bills only" and a program of open-market operation in long-term securities to reduce long-term interest rates without also reducing short-term rates.

Maturity distribution of U.S. Government securities held by Federal Reserve banks

[In millions of dollars]

	Feb. 28, 1961 [1]	Percent of total	Jan. 17, 1962	Percent of total
Under 5 years	25,207	94.5	25,948	91.2
Over 5 years to 10 years	1,189	4.5	2,227	7.9
Over 10 years	271	1.0	266	.9
Total	26,667	100	28,441	100

[1] Fed announced abandonment of "bills only" and a program of open-market operation in long-term securities to reduce long-term interest rates without also reducing short-term rates.

Senator BUSH. In our previous colloquy, Mr. Heller——

Chairman PATMAN. Just a moment, Dr. Heller. Would you please get me the information I asked for a while ago, about the commercial banks holding mortgages? That will be broken down to where it will include homebuilding mortgages, and then the ones that are risk mortgages, and those that we will consider riskless, guaranteed by FHA or the Government in different ways and so forth.

Dr. HELLER. We will be happy to get that for you for the record.

[The information referred to follows:]

Commercial bank holdings of mortgages as of September 1961

		Billion
Total		$29.9
Residential		21.0
Federally underwritten	8.6	
Conventional	12.4	
Other nonfarm		7.2
Farm		1.7

Senator BUSH. Going back to our previous colloquy, Dr. Heller, I believe that you said that the Council was in the process of trying to estimate in 1962 the balance-of-payments situation. You don't know whether you have that ready, do you?

Dr. HELLER. No. This is a joint effort with other Government agencies to try to assess the various factors. As you know, there are some that are a little more difficult than others. There is the short-term flows and so forth. We are trying to get the best assessment possible.

Senator BUSH. You are trying to reach some conclusion, that is, some estimates, is that right?

Dr. HELLER. Yes, we are.

Senator BUSH. Well, I would ask, Mr. Chairman, that as soon as that is available, and you have that estimate, that you make it available to this committee.

Dr. HELLER. I think that this is something that is going to be going on for a considerable period of time, in order to try to nail down the various pieces. This isn't something that we are going to have ready today or tomorrow or this week or next week.

Senator BUSH. You are going to be advising us throughout the year?

Dr. HELLER. This is in the nature of things, that given the difficulty of predicting the developments, once the basic estimate is made, it will have to be under a process of continuous revision. We would be very hesitant to put even as much faith in a balance-of-payments projection as we do in our projections of the overall gross national product, because it is inevitably a residual of so many factors.

Senator BUSH. Have you made any attempt to estimate a balance, a forecast of balance of trade figures for 1962? Do you estimate the spread between our exports and imports will increase favorably to exports, or how have you estimated that balance-of-trade figure might come out in 1962?

Dr. HELLER. I don't have a specific estimate of that, Senator, but we have looked at the relationships between the gross national product and imports and exports over the years. In terms of those relationships, I made my earlier comment that we felt that there had been a faster upswing in imports over the long run than we have seen in recoveries in the past.

This suggests that a good part of the total upswing in imports that will take place during this recovery process has already taken place. We do not look for a very large addition to imports over and above the current rate of about $15.5 billion. It might rise to $16 billion or $16.5 billion, but if it did so, it would be achieving approximately its historical relationship to gross national product by the end of the year.

Senator BUSH. You don't expect that the export-import spread will broaden this year, then?

Dr. HELLER. It is very hard to forecast this. I will ask whether any of my colleagues have worked through this any further than I recall at the moment.

I think Mr. Gordon's main contribution would be to explain why it is so difficult to forecast exports.

Senator BUSH. The reason I am raising this, is this: I think that I mentioned this morning this news dispatch in the New York Times, giving the estimate of the national foreign trade council, I think it was, which indicated that the imports would likely increase rather more substantially than the exports in 1962. This causes a narrowing of the trade balance. I mentioned that, and I think my time is up, and we didn't get a chance to pursue it, but perhaps Mr. Gordon would want to comment on that.

Dr. HELLER. I am sorry, I do not mean to divert from the basic point that a recovery tends to narrow this balance, and indeed, that has been going on through 1961 and there is a fair chance that it will go on through a good part of 1962.

Senator BUSH. If it does, this tends to aggravate our balance-of-payment problem, doesn't it?

Dr. HELLER. Yes; but at the same time that that might be going on for cyclical reasons, in response to economic recovery, we are confident that the measures that have been taken by the administration and are being taken on various fronts, are improving our cyclical relationship between inpayments and outpayments on the international accounts.

Also, let us come back for just a moment to the fourth quarter of 1961 which as we mentioned earlier, seemed to be in considerable deficit. Although there was a substantial overall deficit we have indications that the basic deficit reflecting trade, Government commitments, and long-term investments was definitely smaller in the fourth quarter than in the third, and our trade figures for October and November indicate an improvement in the export surplus over that period. That may just be a temporary improvement, but it does suggest that my earlier statement about a lot of the upsurge in imports having come early in the recovery is valid.

There were no signs in the fourth quarter of speculative movements of short-term currency, and the deficit seems to have been related to commercial financing.

Mr. Gordon wants to comment further.

Dr. GORDON. Senator, forecasting exports is a very speculative undertaking because, obviously, it depends on a level of economic activity in a large number of countries abroad and it is even more difficult to forecast that than it is to forecast our own. All I would like to do, I think, is to mention one fundamental force which seems to me to be strengthening our export position and will strengthen it further if this force is sustained.

That is the very healthy recent price behavior we have been having. I think that in the period 1955–58 we lost ground in the behavior of our prices relative to the prices of our principal foreign competitors. I think since 1958 we have made up some of that ground and perhaps not all of it, but our wholesale price level has been stable since 1958, and some of our principal foreign competitors have had slowly rising wholesale prices.

I think to the extent that we can continue to recapture some of this price advantage or rather to offset some of the damage to our competitive position which may have been done in the 1955–58 period, I think, to that extent, our basic longrun export position will be strengthened. I think that our recent behavior of prices and the outlook for prices next year would suggest the basis for some degree of optimism, at least as it related to prices on our export potential.

Senator BUSH. My recollection in reading the report was that the Council had estimated that the proposed new trade policy would result in a more rapid expansion of exports than imports, and I wanted to see if you had any estimates ready on that basis.

Dr. GORDON. I think that the basic statement is correct, Senator, but we were talking about the outlook for the year ahead. I would doubt very much whether the trade policy program is likely to move ahead fast enough so that the negotiations occur in time to affect the 1962 picture and I think it is a longrun matter.

Senator BUSH. Mr. Chairman, I received a letter here from a man who is president of the Union Pin Co. up in Winsted, Conn., and it is a very facetious letter, but the point of it is that recently in Europe our State Department agreed to a deal by which American chickens would always cost 7 cents a pound more than whatever the common market chickens would cost.

He thought that was very good and he asked me to see if it wouldn't be possible for them to arrange a deal whereby pins could be sold in this country, by import, at a constant 7-percent premium over domestic prices. I am not going to propose any bill to implement this.

Chairman PATMAN. Is he correct about the chickens?

Senator BUSH. If the New York Times is correct about it, because I read it in the New York Times and I think it was in a dispatch which came out the other day.

He is correct about that. But I would like to insert this in the record.

Chairman PATMAN. Without objection, it is so ordered.

(The letter referred to follows:)

THE UNION PIN CO.,
Winsted, Conn., January 22, 1962.

Hon. PRESCOTT BUSH,
Senate Office Building,
Washington, D.C.

DEAR SENATOR BUSH: I was glad to notice in the Connecticut Manufacturers Association bulletin that you objected to the conclusions of the joint congressional Economic Subcommittee in reference to the extreme demands of the President for tariff.

We have been taught that the most efficient place should produce the product. A very interesting illustration of this came from the New York Times on Sunday, January 21, in reference to U.S.-produced chickens, which apparently are produced here cheaper than anywhere else, and $30 million of them went into the Common Market. The State Department is triumphant of its own success in negotiating the chicken situation, for the Europeans don't want the most efficiently produced chickens. However, we escaped a European tariff; we escaped a European quota; our State Department proudly agreed that American chickens should always cost 7 cents per pound more than whatever a European chicken costs. I think that is just plain wonderful. In our own industry we have tariffs on pins. Would it be possible to eliminate the tariff, eliminate a quota, and just agree that all imported pins would sell in the United States at a price 7 cents per pound higher than our domestic prices? I think that is just a wonderful demonstration of the right way to do things. How about having it for the United States?

Senator BUSH. Mr. Chairman, I want to compliment the gentlemen on their patience and their efforts to be very detailed and explicit in their answers to our questions and it has been a very interesting day.

Dr. HELLER. Thank you, Senator.

Senator PROXMIRE. I have a few more questions. First, I would like to put into the record, if I could, and also call the attention of the Council, to some figures that seem to contradict an earlier position that was taken with regard to the tendency of the Government to shift their purchases of Government securities from short term to long term.

My quarrel with these statistics that were given was that they were confined to 1-year obligations and less. If we take 5-year obligations, which I think are more appropriate, then we find that as of January 3, 1962, the Federal Reserve Board portfolio had $26 billion, roughly, in short-term obligations and only $2.227 billion in 4, 5, or 10 years and only $266 million in over-10-year obligations, and the changes had been under 5 years in the past year, an increase of $12 billion. Over 5 years, it was an increase of a little less than that, $1.043 billion. The point is that there hasn't been an apparent policy that I can see, on the part of the Federal Reserve Board to meet the balance-of-payments problem and the monetary ease problem by attempting to keep interest rates on short-term obligations high, which they have to be to forestall capital movements abroad, while trying to push interest rates on long-term obligations as low as possible, which it seems to me is desirable in terms of economic expansion and growth.

Dr. HELLER. On these objectives, of course, we are agreed that the policy should try to prevent the withdrawal or outflow of short-term funds seeking higher interest rates abroad, at the same time that it makes available a flow of long-term funds to stimulate investment at home.

On the data, Mr. Tobin has some specific figures that may be of interest to you.

Dr. TOBIN. First, just to comment on your figures, Senator, the distribution of the Federal Reserve portfolio by maturities reflects not only their open-market operations during the year, but also their participation in any refunding operations of the Treasury. Also, it reflects the mere passing of time, which makes something that was a 6-year maturity a year ago, a 5-year maturity now. You cannot infer directly from a comparison of the Federal Reserve portfolios on two different dates what operations they undertook.

Senator PROXMIRE. I think my statistics would establish that there hasn't been a very ambitious or decisive effort to get into obligations of a longer term than 5 years. There have been some, and it hasn't been as emphatically done, and it seems to me you can't make a case that they have gone all out to follow the policy that some members of this committee have advocated and others have advocated, of trying to have most monetary ease possible consistent with a balance of international payments.

Dr. TOBIN. I think that is a fair statement, and I agree that that is a correct inference from the figures.

I have some figures which show the distribution of the public debt held outside of the Treasury and the Federal Reserve, that is held outside of the Government altogether, at the end of 1960, and the end of 1961. I can put these in the record at this point.

(The following was later received for the record:)

Public debt held outside Federal Reserve and Treasury

[Billions of dollars; end of year]

	1960	1961
Marketable securities: [1]		
Maturing within 1 year	58.6	67.0
1 to 5 years	57.7	54.3
5 to 10 years	15.9	16.0
10 years and over	21.3	21.3
Nonmarketable securities	54.3	54.3
Average maturity (months) of marketable securities	58.0	56.0

[1] Including guaranteed securities.

What they indicate, in general, is that there has been some reduction in the average maturity of the debt outside the Treasury and the Federal Reserve together, from an average of 58 months to an average of 56 months, reflecting in the main, an increase of some $8 billion in the short-term securities outstanding. As you mentioned, the main decrease in the public's holdings is in the 1- to 5-year category, rather than in the categories longer than that.

Senator PROXMIRE. That is on the average.

Dr. TOBIN. This is the debt held outside the Government in general. It is not the total marketable debt of the Government, which has not changed in average maturity. It takes account of the fact that the Federal Reserve and the Government trust accounts have absorbed certain amounts of the debt.

Senator PROXMIRE. Now, the reason I raised the questions I have raised throughout my interrogation on your statements is that it would seem to me that any assessment of economic activities of the Government in this year, in 1961, should be fairly modest in the achievements that have been made outside of the impact of the military achievement which is, we all agree, not designed for economic purposes. Therefore, it is hard for me to see any justification on the basis of the experience so far, of the administration or for that matter, of past administrations, that we should put reliance, or great reliance, on fiscal policy of the kind you advocate—a standby program of public capital improvements and a procedure for suspending income taxes.

You said earlier in reply to Mrs. Griffiths, that there were constitutional precedents for these requests. What are the precedents?

Dr. HELLER. I am thinking particularly of the tariff negotiating powers, which is a fiscal power of a type, in which the President has been given a good deal of discretion over the past years in the reciprocal trade acts to negotiate on behalf of Congress changes in the tariffs with other countries.

Senator PROXMIRE. But there has been no precedent for the President in changing the income tax power.

Dr. HELLER. No; there is no precedent for this.

Senator PROXMIRE. Now I have heard people argue that in England they have done this, and I understand they only do this in England with regard to excise taxes and not with regard to the income tax.

Dr. HELLER. Excise taxes and employment taxes. They have powers to do both.

Senator PROXMIRE. Is there any international precedent, any other countries that have ever done this kind of thing that you know of?

Dr. HELLER. I believe not in the income tax field. But under the Cabinet systems the recommendations of the Prime Minister become law unless the Government is overturned. In such a system, the executive recommendation has more thrust, and is a bit of a precedent for this kind of proposal—that is, a proposal that unless it is "vetoed" by the Parliament becomes law.

Senator PROXMIRE. I have read the justification in the report for this and I am wondering if there are any specific estimates on how much a $5 billion increase in income this way in a 6-month period—what estimate there is of the impact it would have on employment.

Dr. HELLER. Well, we have done a good bit of thinking and some calculating as to the reflection of this in consumer purchasing power, that is the part of it that would be spent and part of it that would be saved. One could carry those calculations further, speculative though they have to be because we don't have any sure way of translating a temporary tax reduction into purchasing power, and they could presumably be carried into the question of employment opportunities. But we do not have specific calculations available on them.

Senator PROXMIRE. It would seem to me that there might be considerable loss here, as I understand this is quite different than the proposal that has been made that you simply give a cut in the bottom bracket income tax.

Dr. HELLER. Of course, the cut in the bottom bracket would be a cut in the lowest bracket for all taxpayers, regardless of the height their income might be. Out of our total income tax base of about $200 billion, close to two-thirds is in the first bracket. That would bring us to around $135 billion, so that there the cut per pound would be about $1⅓ billion on an annual basis instead of $2 billion.

Senator PROXMIRE. Is it not true that a great deal of the remainder that would be cut under your proposal would be for people who would not have it withheld, and who would be in a position where they would not be constrained to spend what they earned, and therefore would save quite a bit?

Dr. HELLER. I believe that our calculations show that three-quarters of the cut would be reflected immediately in lower withholding.

Senator PROXMIRE. One-quarter would not be.

Dr. HELLER. One-quarter would not be, that is right. Again I hope that you will give me the privilege of correcting this for the record in case I don't have it in exactly the same proportions, but it is at least three-quarters that would immediately be reflected in lower withholding.

Senator PROXMIRE. For the typical taxpayer, this would mean $6, $8, $10 more per week, of which I would presume in a recession period over a little would be spent on consumer durables. The trend in recession for those who have income, particularly when they are signaled by the President of the United States that we are in trouble enough, might be to save it or at least not to commit themselves to a long-term purchase of a new car or a new home or something of that kind that would have its maximum effect on employment.

Dr. HELLER. This works two ways: You have the effect as it were of recognizing a recession, in case it had not already been recognized in the private economic lives of the citizens involved. Certainly the recognition of the recession in very direct and sharp terms last January and February did not seem to in any way shape or manner interfere with the direction of that downward movement, and the upturn.

Senator PROXMIRE. That was a little different because that recognition was by an increase in the unemployment compensation. I am talking about the reaction to a specific tax cut that was itself related to the economic situation, and it would be a windfall and it would be of limited duration—6 months. It might be a somewhat different attitude.

Dr. HELLER. There might be some differences, although they are generally related as increases in the disposable income, the take-home pay, so to speak, of individual citizens. Beyond that I wanted to say that the assurance that the Government would take effective, fast, and substantial action to counter the recession might be a confidence-creating factor which would cause people to continue their spending patterns rather than to restrict their outlays and hold back as you suggest.

On the basis of the best evidence available, and it is not too good, we would think that out of a $5 billion or 6 months' reduction, as much as three-quarters of it would be reflected in consumer spending.

If you applied a multiplier of 2 to that, as the funds are respent and I don't think that is unreasonable under these circumstances, and again looking at past experience, this would mean that the economy in the space of 6 months might get a stimulus of something like $7½ billion. It would be very substantial as a factor in preventing a recession and turning it around.

Senator PROXMIRE. Is it not true that there is a tendency over time through a recession period or expansion period and so on, that it would be a fairly steady trend in nondurable expenditure?

It varies far less than durable spending, which tends to rise sharply and drop sharply. The argument I am trying to make is that if the impact of this extra $5 and $10 a week is not going to be in buying cars and buying homes and that kind of thing, that a great deal might be saved or spent on nondurables the actual effect on the economy in terms of providing additional employment might not be very great.

Dr. HELLER. Well, the impact on durable goods consumption is of course a very complex one. If you provide this tax reduction there are more funds available for payment of installment debt, and after all most durables now are bought on an installment plan. This means in some cases you would permit faster payment, but in other cases you would provide the wherewithal to undertake new installment debt.

Senator PROXMIRE. This is the kind of additional compensation that discourages any prudent person from making an installment commitment. If it ends in 6 months, and if he knows his income is going to go back to what it was before 6 months, why would he commit himself to buy something over 12 months or 18 months or a year or 10 years or 20 years? I think that he would be very ill advised to make an additional commitment so that he could buy something over time.

Dr. HELLER. Well, the interesting observation on that is that such evidence as we have on past temporary incomes indicates that they have a particularly strong impact on the undertaking of commitments with respect to durable goods consumption. A good part of the final effect would depend on the conviction of consumers that the Government was dead serious in trying to limit any recessionary movements to just very short and shallow interruptions in the economic development and growth of the country.

Senator PROXMIRE. Is it not possible that you might get business decisions that would compensate for that, recognizing that you are tending to borrow from the future, and you are lowering taxes temporarily, and going to increase them later, and therefore the spending that is going on now is something that you cannot rely on?

It would be an argument for not increasing inventories, and not engaging in the kind of business expansion that you would want if this were a permanent tax cut.

Dr. HELLER. We are talking about filling in dips in what has been historically a substantial upward movement in total consumption and total production. This is not a case of having lower rates now and higher rates later. It is a case of taking a dip in the tax rates themselves, and then restoring them to what they were before.

In other words, this is a net gain to the taxpayer, and I have difficulty seeing how it would have a discouraging effect, relative to just holding the tax rate steady.

Senator PROXMIRE. Do you have any estimates on what effect this would have net on the national debt? I take it that you have a multiplier there of $7.5 billion. Some of this would be recovered in higher revenues, and I am sure you wouldn't bring it up to a washout. You would lose something, I am sure.

Dr. HELLER. It would in and of itself increase the national debt to some extent, but one would hope that its impact in keeping the economy closer to full employment levels over a larger proportion of the time would mean that in the long run you would find that the debt would fall both relatively and absolutely.

Senator PROXMIRE. Now, I just have a couple of quick questions.

You discuss the budget on national income account, and you talk about the surplus of $4.5 billion, which you say will be added in fiscal 1963, would you explain this concept of a budget on the national income account?

Dr. HELLER. As compared with the conventional or administrative budget, the budget on national income account includes all Government expenditures, including the trust accounts. Secondly, it counts taxes in particular, and expenditures to some extent, on an accrual basis rather than a cash basis. This is best illustrated by the corporate tax: it counts as a corporate tax receipt, the liability when it is accrued, when it shows up in the national income accounts, rather than the date when the cash happens to be paid into the Treasury account of that liability.

And, third, the income and product account, or national income account, of the Federal budget omits Federal credit transactions. The difference therefore between roughly half a billion surplus on the administrative account and $4.5 billion surplus account on the national income account, consists of these three factors—one, that the trust accounts which are not included in the administrative budget will be running a slight surplus, and, two, that credit transactions as a whole will involve a net outflow which shows up in the administrative budget but not in the income and product budget, and, third, the fact that corporate taxes because of the recovery and the rise in profits will be accruing during 1963 faster than they will be paid into the Treasury.

Those are the three factors that account for it.

Senator PROXMIRE. As I understand it, then, this would include all of the trust fund transactions, such as the social security income and outgo, and the unemployment compensation income and outgo, but it would not include the gross transactions of the Post Office Department, is that correct—TVA and of the Commodity Credit Corporation?

Dr. HELLER. That is correct, Senator.

Senator PROXMIRE. Now this is why I would question——

Dr. HELLER. It does include the net cost to the Government or the net intake but not the gross intake and outgo.

Senator PROXMIRE. This is why I would question your statement in the first place, that there was about 17 percent of the budget of the gross national product, and there was this proportionate involvement of the Government in the economy and it was perhaps declining and available rather than increasing. The most rapidly increasing element in personal income, as you know, has been transfer payments. It has gone up 150 percent since 1950 or 1952 and it has gone up 3 times as fast as wages, and it has gone up 10 times as fast as prices, and if we include that factor in the budget you get a far different picture than you do with a conventional budget, and you get something like 23 percent or 22 percent rather than 17 percent, as the relationship between the budget and the gross national product.

Now, if we go on, and I can see no reason why you shouldn't include it, but if you go on to include the Post Office, TVA, and the Commodity Corporation in full, it is something like $140 billion, to my calculations which is something like 26 percent as the relationship between government activity and the gross national product. Is this correct?

Dr. HELLER. Well, those statistics of $140 billion are surely correct, but I think it is only fair and accurate to note that the calculations of the gross national product is on a value-added basis and not a gross-flow basis. In other words, we net out the value added and eliminate duplications. We don't take the gross sale of United States Steel and then the gross sales of General Motors and of all the fabricators in between and add those together. That would be the comparable action to counting the gross receipts of the Government.

Senator PROXMIRE. You do not take the net profit of General Motors or the net profit of United States Steel. What you are doing with the Post Office is to take the net surplus or net deficit and counting it in, and you are doing the same with the Commodity Credit Corporation and you are not necessarily taking the value added and you are not taking the value of it, when you argue that the deficit measures the value of the commodity or service.

Dr. HELLER. No, there is certainly not a direct relationship between the two. On the other hand, to take the gross would involve very substantial double-counting.

Senator PROXMIRE. Now let me just conclude by saying that on page 82 of your report you have a chart showing the surplus or deficit and in 1962 that amounts to about $2.5 or $2 billion, and in the first quarter or first half of 1963 it is at an annual rate of over $6 billion. I don't want to be arguing on both sides of everything, but I am wondering as a question, won't this have a deflationary discouraging effect on economic expansion during a period when you testified to us that we will be short of the 4 percent goal?

In other words, is this a wise thing? This is the real impact and not the conventional budget. This is the real impact on the economy.

Dr. HELLER. Well, Senator, as you point out, in the fiscal year 1963, we will have substantial overall surplus as compared with a deficit in the fiscal year 1962. And yet, I think it is fair also to point out that there are two or three factors bearing on the relationship of the Federal budget, to the prospects of economic recovery that should be added to this picture.

First, as I mentioned earlier, and particularly in contrast with the last recovery period, the overall level of Federal expenditures will be rising by about $3.5 billion in fiscal 1963 over 1962, in contrast with the shrinkage of about $3.5 billion for 1959 and 1960. Second, the swing——

Senator PROXMIRE. You are going back to the OECD theory, that it does not matter if you have a deficit or a surplus, provided the budget is big enough?

Dr. HELLER. No; I am talking about a recovery period and not an assertion that you have to do this year in and year out, for longtime growth. I think there is that distinction.

The second point is that on an income and product account basis we will be swinging from perhaps a maximum quarterly rate of deficit of about \$5.5 billion to approximately \$5 or \$5.5 billion surplus. It is about an \$11 billion swing and in the last recovery it was an \$18 billion swing, from about 11 minus to about 6½ plus.

This budget balance is predicated on a prosperity level of gross national product, that is, on a very substantial rise in the total employment and income and output in the economy. If that fails to materialize, of course the budget would tend to run into a deficit situation, and would be a source of stimulus to the economy. I think those points are relevant in looking at the absolute size, whether deficit or surplus, for 1963. We think that there is a strong future recovery in prospect which would make this kind of a budgetary development consistent with continuation of expansion of the economy toward the full employment goal. We can't be sure that we are right, but this is where the best bets have been placed.

Senator PROXMIRE. I want to thank you very much, and I want to thank you, Mr. Chairman, for your patience, and I want to say this has been a very enlightening and educational day for me.

Chairman PATMAN. We want to thank you for the information we have received while you have been on the witness stand—over 5 hours, which is very unusual. You have certainly been patient and considerate and we appreciate it very much. We appreciate your testimony, and it will be helpful.

Dr. HELLER. Thank you very much.

Chairman PATMAN. Without objection, the committee will stand in recess until 10 o'clock in the morning, when we meet in the old Supreme Court room, in the Senate wing of the Capitol.

(Whereupon, at 4:20 p.m. the committee was recessed, to be reconvened at 10 a.m. the following day.)

JANUARY 1962 ECONOMIC REPORT OF THE PRESIDENT

FRIDAY, JANUARY 26, 1962

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

The Joint Economic Committee met, pursuant to notice, at 10 a.m., in room P–63, the Capitol, Representative Wright Patman (chairman) presiding.

Present: Representative Wright Patman (chairman) and Senator Paul H. Douglas (vice chairman), Senators Sparkman, Proxmire, and Bush, and Representative Griffiths.

Chairman PATMAN. The committee will please come to order.

This morning we continue hearings on the Economic Report of the President for 1962. Our witness this morning is the Honorable David Bell.

Mr. Bell, I believe that you are to be warmly congratulated for the new form in which you have presented your first budget. I know this has taken a great deal of hard work, and I feel the results are an important forward step. For the first time, a Member of Congress can readily find information on any subject he may be interested in. As you know, Mr. Bell, they say that the late Gov. Al Smith had a unique talent in being able to talk about any subject and make it interesting. They say he used to go down to the Bowery in New York and make speeches about what would seem a dry subject, the budget for the State of New York, but he would make it very interesting. Of course, those of us in Congress already are interested in the subject of the budget, but you have made it even more interesting and I expect that you will continue to do so.

Thank you for coming, and you may proceed in your own way, sir.

STATEMENT OF DAVID E. BELL, DIRECTOR OF THE BUREAU OF THE BUDGET; ACCOMPANIED BY ELMER B. STAATS, DEPUTY DIRECTOR, ROBERT C. TURNER, ASSISTANT DIRECTOR; SAMUEL M. COHN, DEPUTY FOR FISCAL ANALYSIS; AND RAYMOND T. BOWMAN, ASSISTANT DIRECTOR FOR STATISTICAL STANDARDS, BUREAU OF THE BUDGET

Mr. BELL. Thank you very much, Mr. Chairman. I am very pleased to hear your favorable words about the new budget format. We were stimulated in this direction by this committee and members of its staff, and I hope that it does, indeed, prove to be a more effective way of presenting what is necessarily a highly complicated and very large subject.

If I may, I should like to start with a fairly brief formal statement.

Chairman PATMAN. You may proceed in your own way.

Mr. BELL. I think members of the committee have copies.

It is a pleasure to appear before you today to discuss with you the budget recently transmitted by the President for fiscal 1963.

Economic basis for the budget: The balanced budget transmitted for 1963 accords with our expectations with respect to the state of the economy. Specifically, we expect that the expansion which has already lifted the rate of gross national product by over $40 billion since the first quarter of calendar 1961 will continue through the current year and beyond, carrying the gross national product during calendar 1962 to a record of $570 billion.

Personal incomes are expected to reach $448 billion in calendar 1962, up $30 billion from a year earlier, and corporate profits $56½ billion, an increase of $10½ billion.

The increase in the gross national product from the first to the fourth quarter of 1961 averaged well over 2½ percent per quarter. Our assumptions for 1962 will be realized even if the expansion slows down to an average quarter-to-quarter increase of 2 percent. Steady expansion at a rate of 2 percent per quarter should bring the rate of unemployment down from its present rate of over 6 percent to about 4 percent by the end of fiscal 1963.

The current budget outlook: Under the President's recommendations, budget expenditures for fiscal 1963 will increase by $3.4 billion over the level estimated for the present fiscal year, to $92.5 billion.

We have a table which is summarized from the budget document.

Chairman PATMAN. You may insert anything you desire which you consider germane.

Mr. BELL. Thank you, sir.

(The table is as follows:)

TABLE 1.—*Budget summary*

[Fiscal years. In billions of dollars]

Description	1961 actual	1962 estimate	1963 estimate
Budget expenditures:			
National defense	47.5	51.2	52.7
International affairs and finance	2.5	2.9	3.0
Space research and technology	.7	1.3	2.4
Subtotal	50.7	55.4	58.1
Interest	9.0	9.0	9.4
Domestic civil functions:			
Agriculture and agricultural resources	5.2	6.3	5.8
Natural resources	2.0	2.1	2.3
Commerce and transportation	2.6	2.9	2.5
Housing and community development	.3	.5	.8
Health, labor, and welfare	4.2	4.7	5.1
Education	.9	1.1	1.5
Veterans benefits and services	5.4	5.6	5.3
General government	1.7	1.9	2.0
Subtotal, domestic civil functions	22.4	25.3	25.4
Civilian pay reform			.2
Allowance for contingencies		.1	.2
Deduct interfund transactions	.7	.7	.7
Total	81.5	89.1	92.5
Budget receipts, total	77.7	82.1	93.0
Budget surplus (+) or deficit (−)	−3.9	−7.0	+.5
Public debt, end of year	289.0	295.4	294.9

Mr. BELL. More than three-quarters of the increase in budget expenditures, or approximately $2.7 billion, is accounted for by national security and space activities. Most of the remainder will be required for interest charges on the public debt. In total, budget expenditures for civilian programs for fiscal 1963 are virtually unchanged from fiscal 1962.

The President is recommending increases in a number of areas, such as education and health, that will be valuable in terms of productivity of our human resources and longrun growth of the economy. This is made possible, with almost no increase in total civilian expenditures, by holding down or cutting back on some less urgent outlays.

Budget receipts in fiscal 1963 are estimated to total $93 billion, an increase of $10.9 billion over the recession-affected level of the present fiscal year. These receipts estimates assume extension of corporation income taxes and most excise taxes at present rates as well as the economic expansion described above.

The administrative budget for 1963 thus shows a modest surplus of about $500 million. As a result, the public debt on June 30, 1963, is expected to be $294.9 billion compared with $295.4 billion at the end of the current year, furthering the decline of the outstanding debt relative to the gross national product, which has been going on since the end of World War II. The public debt, far from being an increasing burden on our economy, has declined steadily from the equivalent of about 130 percent of the GNP at the end of the fiscal year 1946 to a little over half the GNP at present.

Outside the administrative budget, trust fund expenditures are estimated to increase by about $1 billion in fiscal 1963.

We have a table we would like to insert showing the details on that. (The table is as follows:)

TABLE 2.—*Trust fund summary*

[Fiscal years. In billions of dollars]

Description	1961 actual	1962 estimate	1963 estimate
Trust fund receipts:			
Federal old-age and survivors' insurance trust fund	11.9	12.3	14.2
Federal disability insurance trust fund	1.1	1.1	1.2
Unemployment trust fund	3.8	3.6	4.2
Railroad retirement account	1.1	1.1	1.2
Federal employees' retirement funds	2.0	2.1	2.1
Highway trust fund	2.9	3.1	3.4
Veterans life insurance funds	.7	.7	.7
Other trust funds	.8	1.0	1.0
Subtotal	24.3	25.0	28.0
Deduct interfund transactions	.5	.5	.5
Total, trust fund receipts	23.8	24.5	27.5
Trust fund expenditures:			
Federal old-age and survivors' insurance trust fund	11.8	13.3	14.3
Federal disability insurance trust fund	.8	1.1	1.2
Unemployment trust fund	4.7	3.8	3.9
Railroad retirement account	1.1	1.1	1.1
Federal employees' retirement funds	.9	1.0	1.1
Highway trust fund	2.7	3.2	3.4
Veterans life insurance funds	.8	.7	.7
Federal National Mortgage Association trust fund, net	−.1	.9	.5
Deposit funds and all other trust funds	1.0	.9	1.0
Subtotal	23.8	26.0	27.1
Deduct interfund transactions	.5	.5	.5
Total, trust fund expenditures	23.2	25.6	26.6
Net accumulation	.6	−1.0	.9

Mr. BELL. The largest increase is for benefit payments under old-age and survivors' insurance, up about $1 billion. Proposed legislation for medical care for the aged through the social security system is not estimated to take effect in time to affect 1963 expenditures. Regular unemployment insurance benefits from the trust fund will decline with economic recovery, and budget expenditures for temporary extended unemployment compensation are terminating. Outlays under proposed legislation for permanent improvements in unemployment compensation, however, are estimated to begin in 1963.

Trust fund receipts for fiscal 1963 are estimated at $27.5 billion, or approximately $3 billion more than in fiscal 1962. About two-thirds of this increase will be accounted for by the higher collections anticipated from higher payrolls and increased tax rates for Federal old-age and survivors' insurance.

Federal accounts on the basis of the consolidated cash statement—combining the administrative budget and trust fund programs along with certain other Federal transactions, and eliminating intragovernmental transactions—show an estimated increase in expenditures of $3.7 billion and a $14 billion increase in receipts, with an excess of receipts from the public of $1.8 billion over payments to the public in 1963. This compares to an excess of payments over receipts of $8.5 billion in fiscal 1962.

We have a table again to show the details on this:

(The table is as follows:)

TABLE 3.—*Receipts from and payments to the public*

[Fiscal years. In billions of dollars]

Description	1961 actual	1962 estimate	1963 estimate
Receipts from the public:			
Budget receipts	77.7	82.1	93.0
Trust fund receipts	23.8	24.5	27.5
Less:			
Intragovernmental transactions	4.2	4.0	3.9
Receipts from the exercise of monetary authority	.1	.1	(1)
Total receipts from the public	97.2	102.6	116.6
Payments to the public:			
Budget expenditures	81.5	89.1	92.5
Trust fund expenditures	23.2	25.6	26.6
Government-sponsored enterprise expenditures (net)	−.2	.5	.3
Less:			
Intragovernmental transactions	4.2	4.0	3.9
Accrued interest and other noncash adjustments (net)	.8	.1	.8
Total payments to the public	99.5	111.1	114.8
Excess of receipts (+) or payments (−)	−2.3	−8.5	+1.8

1 Less than $50,000,000.

Mr. BELL. Fiscal policy considerations: Federal receipts and expenditures on a national income account basis are summarized in a table which we would like to insert in the record and describe a little more fully.

This is the first time, as you know, Mr. Chairman, that the administration has given much emphasis to Federal receipts and expenditures on a national income account basis. We consider this an important innovation.

(The table is as follows:)

TABLE 4.—*Federal receipts and expenditures in the national income accounts*

[In billions of dollars]

Fiscal year	Expenditures			Receipts	Surplus (+) or deficit (−)
	Purchases of goods and services	Other	Total		
1953	56.8	19.6	76.2	69.9	−6.3
1954	53.9	20.6	74.5	65.9	−8.6
1955	45.0	23.0	68.1	67.0	−1.1
1956	45.2	24.3	69.5	76.3	+6.8
1957	48.3	28.3	76.5	80.9	+4.4
1958	50.5	32.2	82.8	77.8	−4.9
1959	53.8	36.5	90.2	85.4	−4.8
1960	52.9	39.0	91.9	94.1	+2.2
1961	54.6	42.3	97.0	94.8	−2.2
1962 estimate	60.2	45.9	106.1	105.6	−.5
1963 estimate	64.2	47.7	111.9	116.3	+4.4

Mr. BELL. Looking at the expenditure side first, several points might be made in assessing the impact of the 1963 budget on the economy.

First, the projected increase in total spending of just under $6 billion in fiscal 1963 follows on the increase of $9 billion expected for the current fiscal year. Only a part of the latter increase has so far taken place. The $15 billion increase for the 2 fiscal years combined, for which expanded defense and space programs are in large part responsible, represents half-again as rapid a rate of growth in Government spending as we have had on the average over the 6 years preceding.

Second, Federal purchases of goods and services are scheduled to rise more rapidly than total spending, reflecting the proposed reductions in postal and farm subsidies on the one hand and the increase in goods bought for defense and space activities on the other.

The increase in purchase of goods and services as a percent of total Federal spending reverses a steady downtrend that has characterized the Federal budget ever since the end of the Korean conflict as shown in the following table:

(The table is as follows:)

TABLE 5.—*Relation of purchases of goods and services to total Federal expenditures (national income accounts basis), by fiscal year*

[Purchases of goods and services as percent of total]

1953	74.5	1959	59.6
1954	72.3	1960	57.6
1955	66.1	1961	56.3
1956	65.0	1962 estimate	56.7
1957	63.1	1963 estimate	57.4
1958	61.0		

Mr. BELL. While this change in the composition of Federal expenditures is the net result of individual program decisions rather than any deliberate effort to increase the fraction of the budget going into the purchases of goods and services as such, it does have significance for the economy. Other things being equal, purchases of goods and services probably have a more direct impact on aggregate demand and a larger total economic impact per dollar of Federal outlay than other categories of spending.

However, a greater economic impact per dollar does not necessarily mean that the purchase of goods is the most appropriate kind of expenditure for an antirecession program. For such periods, as was the case in 1961, certain categories of transfer payments, such as unemployment compensation benefits, may be easier to start quickly, may make their economic impacts more promptly, and relieve hardship more directly and equitably.

Turning to the other side of the ledger, Federal receipts in the national income accounts, since they are recorded on an accrual basis, respond more promptly than receipts in the administrative budget or consolidated cash statement to changing levels of income in the private sector. Thus, the rise in corporate profits tax accruals since the first quarter of 1961 has already wiped out most of the Federal deficit on a national income basis that was occurring at the trough of the recession.

In national income terms, we estimate a Federal deficit of only $0.5 billion in 1962, compared to deficits of $7 and $8.5 billion in the administrative budget and consolidated cash statement, respectively. For fiscal 1963, the estimated national income surplus of $4.4 billion compares with much smaller surpluses of $0.5 billion and $1.8 billion on the administrative budget and consolidated cash basis.

I have been asked from time to time whether the switch from Federal deficit to surplus with economic recovery will not "pinch-off" the recovery short of full employment, as is generally agreed among economists of a variety of persuasions to have happened on the road to recovery from the 1958 recession. We do not believe this will happen this time, and there are two points I would like to make in this connection.

First, the turnaround in fiscal policy will not be as sharp as in the last recovery. The "pinch-off" in 1959 and 1960 was not wholly a matter of automatic built-in stabilizers. It also involved a cutback in defense and other Federal spending, and increased tax rates for gasoline and for social security payroll taxes. Administrative budget outlays fell by almost $4 billion in fiscal 1960.

By contrast, fiscal 1963 budget expenditures will be $3.4 billion higher than in fiscal 1962. The consolidated cash statement swung from a deficit of $13.1 billion in fiscal 1959 to a surplus of $0.8 billion in fiscal 1960—a net change of just under $14 billion. This time, the total swing from deficit in 1962 to surplus in 1963 is estimated at $10.3 billion on a consolidated cash basis.

Second, there is no reason to expect the sharp change towards a tight money policy that took place in the last expansion. With the good record on price stability so far in this recovery, and with the absence of any indication of an early resumption of inflationary pressure, the monetary authorities, within the constraints imposed by balance-of-payments considerations, should be in a better position to continue their policy of monetary ease than they have been in previous postwar recoveries.

With both fiscal and monetary actions expected to be less restrictive on the economy in the coming year than they were during the previous economic recovery, the 1963 budget can be characterized as expansionary without being inflationary. An increase in Federal spending is in prospect, but the annual budget figures do imply a slowdown in the rate of increase sometime in calendar 1962. In addition, the payroll tax rates under the old-age and survivors insurance program will be increased under present law by an annual rate of approximately $2 billion on January 1, 1963, and this will have a restraining effect on private demand.

Although the administration is rather confident about the economic outlook and the economic assumptions underlying the budget, we cannot be dogmatic about such matters. The possibility of a more vigorous or a less vigorous expansion cannot be ruled out. Perhaps the most important factor in our confidence about the performance of the economy in the long run is the fact that the present administration remains alert to developing economic trends, and stands ready to change its policies when the evidence shows this is appropriate.

As you know, the President has requested three major steps to increase the built-in stability of our economy—strengthening of the unemployment insurance system, standby authority to initiate a temporary expansion of public works, and standby authority to cut personal tax rates for recession periods. We do not expect a recession in the period covered by this budget that would call for the use of these weapons. But as the President stated, "the time to repair the roof is when the sun is shining." I hope this committee will give its wholehearted support in setting up this new policy machinery.

In closing may I say a few more words about the budget document itself?

We have received and are studying with interest the very recent staff report of this committee on the Federal budget as an economic document. It is an excellent report on the data economists need to analyze issues of public finance, and should prove helpful to us in making future improvements in the budget document. Some of its recommendations follow similar ideas of our own that are already incorporated in the new document for 1963.

This administration is certainly sympathetic to the general philosophy underlying your staff report, that the budget process must be useful for purposes of economic analysis, as well as for budgeting in the traditional and most important sense of assessing the proper level of Federal expenditures to meet defense, international, and other national needs, and of calculating revenue requirements and availability.

There is increasing recognition of what economists have long held—that the Federal budget can and should be used for economic stabilization, and to promote economic growth, equilibrium in our balance of international payments, and efficient allocation of resources. The budget document should be a vehicle for promoting intelligent public discussion of these and other economic questions.

In the new budget document for fiscal 1963, our new small-size or book-size volume, we have taken a number of steps along these lines.

For one thing, the budget contains a more comprehensive and explicit discussion of the economic assumptions underlying the revenue estimates.

Second, we have included in the budget document a translation of Federal fiscal activities into the national income terms more familiar to economists—an alternative presentation of the budget totals more indicative of the direct impact of Federal activity on current incomes and output in the national economy. The very recent statement of the Committee for Economic Development, "Fiscal and Monetary Policy for High Employment," has, as I am sure you all know, recommended the national income basis as the most useful single way to express budget totals for the purpose of evaluating fiscal policy.

Third, we have incorporated in the document new tables, including summaries of obligations incurred, of Federal civilian employment, and the investment character of Federal budget expenditures.

Fourth, we have put back into the document itself certain special analyses that are particularly useful for analyzing the economic character of the budget, such as those on public works, Federal credit programs, research and development programs, and Federal aid to State and local governments.

Finally, the new format (and I might add, the lower price) of the budget should promote wider public use and understanding.

In considering further improvements in the budget document, we will, of course, continue to welcome suggestions. However, I believe we must agree that much more than a modification of the budget is involved in improving the flow of data on the economic aspects of Federal activities. Reports and documents prepared by various Federal agencies, including those directly involved in carrying out important Federal programs, must also share this responsibility.

Moreover, a large part of the economic analysis of individual Federal programs must continue to be a part of the budget review process within the executive branch and in testimony of responsible agency officials before the committees of the Congress.

Mr. Bell. Might I, Mr. Chairman, add one additional point that is not in my prepared statement but which I would like to call to the committee's attention, if I may. The budget document, after a lapse of a few years, again contains a special analysis, identified as "Special Analysis I," which summarizes the obligations recommended in the 1963 budget for the Federal statistical program. I know the interest this committee has also had in the statistical programs of the various Government agencies and, therefore, if I may, I would like to supply for the record a copy of "Special Analysis I" and a more detailed statement of the subject matter content of the new statistical projects proposed in the 1963 budget.

Chairman Patman. Thank you, sir. We have an understanding here that any member of the committee may extend his remarks on any matter which he believes germane to what we are discussing, and that will apply to the witness, too. So you will be allowed to do that.

(The documents are as follows:)

SPECIAL ANALYSIS I

PRINCIPAL FEDERAL STATISTICAL PROGRAMS

(Reprint of pp. 348 to 351 from the Budget of the United States Government for the fiscal year ending June 30, 1963. Detail will not necessarily add to totals because of rounding).

The principal programs in the 1963 budget designed to collect statistical information for the use of the Government and the public are summarized in two categories: current and periodic. Recommendations for the current programs, reflecting the continuing year-to-year statistical activity of the various agencies, total $61.9 million in 1963, an increase of $9.1 million over 1962. The periodic statistical programs—the large-scale census-type surveys characteristically undertaken once or twice a decade—total $11.5 million for 1963, $1.3 million less than the amount available in 1962.

The functions of collection, processing, and publication of current general purpose statistical information are often closely related to other agency objectives. To indicate the interrelationships of the statistical programs carried out by different agencies and to aid in evaluating the Government's overall statistical system, the significant components of current Federal statistical activity are brought together and classified by broad subject areas in this special analysis. These areas and the amounts involved are summarized in table I–1.

TABLE I–1.—*Direct obligations for principal current statistical programs, by broad subject areas*

[In millions of dollars]

Program	1961 actual	1962 estimate	1963 estimate
Labor statistics (Department of Labor and Agriculture)	10.3	11.8	14.3
Demographic and social statistics (Departments of Commerce, Agriculture, and Health, Education, and Welfare)	6.4	7.0	8.5
Prices and price indexes (Departments of Labor and Agriculture)	4.3	4.4	5.1
Production and distribution statistics (Departments of Agriculture and Commerce)	20.2	22.0	24.9
Construction and housing statistics (Department of Commerce)	1.3	1.5	1.7
National income and business financial accounts (Departments of Commerce, Treasury, and Agriculture; Federal Trade Commission, and Securities and Exchange Commission)	5.8	6.1	7.3
Total, principal current programs	48.4	52.8	61.9

The current statistical programs included in this analysis represent a substantial part of the collection and processing activities of the Federal Government. Since it is not always possible to separate the production or use of data from other aspects of agency administrative responsibility, some statistical activity is not included. Nor has any attempt been made to include resources used in applications of statistical methodology to other than data collection and use. That portion of the work of the Bureau of Employment Security in the Department of Labor resulting in current statistical data of general use is included in the 1963 analysis for the first time. Comparability with data shown in previous analyses is also affected by organizational changes relating to statistical work within the Department of Agriculture.

Recommendations for the periodic programs for 1963 reflect the completion of the Eighteenth Decennial Census and include funds needed to complete the 1962 Census of Governments and to start operational work on the 1963 Censuses of Business, Transportation, Manufactures, and Mineral Industries. In addition, funds are recommended to provide for modernizing the present electronic equipment in the Bureau of the Census. Funds are also included for the fourth year of the 5-year project to revise the Consumer Price Index.

The agencies included in the analysis of both current and periodic programs and the sums involved are shown in table I–2.

TABLE I-2.—*Direct obligations for principal statistical programs, by agency*

[In millions of dollars]

Agency	1961 actual	1962 estimate	1963 estimate
CURRENT PROGRAMS			
Department of Agriculture:			
Economic Research Service (except foreign economic analyses)	8.3	8.5	9.3
Statistical Reporting Service	8.1	8.8	9.7
Department of Commerce:			
Bureau of the Census	9.6	10.8	13.0
Office of Business Economics	1.5	1.6	1.9
Department of Health, Education, and Welfare:			
Office of Education: Educational statistics	.9	1.0	1.3
Public Health Service: National health statistics	4.0	4.5	5.2
Department of Labor:			
Bureau of Employment Security: Statistical activities	1.3	1.5	1.8
Bureau of Labor Statistics	11.1	12.4	15.3
Treasury Department: Internal Revenue Service: Statistical reporting	3.1	3.2	3.9
Federal Trade Commission: Financial statistics	.3	.3	.3
Securities and Exchange Commission: Operational and business statistics	.2	.2	.3
Total, current programs	48.4	52.8	61.9
PERIODIC PROGRAMS			
Department of Commerce: Bureau of the Census:			
1962 Census of Governments	.1	1.1	1.4
1963 economic censuses	----------	1.0	3.2
1964 Census of Agriculture	----------	----------	.7
Modernization of computing equipment	----------	----------	3.7
Eighteenth Decennial Census	18.0	8.4	1.1
1958 economic censuses	2.0	.2	----------
Department of Labor: Bureau of Labor Statistics: Revision of Consumer Price Index	1.3	2.1	1.3
Total, periodic programs	21.4	12.8	11.5
Total, principal statistical programs	69.9	65.5	73.4

NOTE.—Detail will not necessarily add to totals because of rounding.

OBJECTIVES OF THE FEDERAL STATISTICAL SYSTEM

The continuing objectives of the Federal statistical system are to provide accurate, comprehensive, and timely data needed for the operations of the Government, to insure the efficient utilization of Government resources with minimum burden on respondents, and to furnish the public with information about the functioning of the economy and the welfare of the people. The data produced are used in the study of social and economic problems, in the formulation of Government and business programs, and in the evaluation of basic trends and activities.

The attainment of these objectives requires continuous consideration of the balance between competing purposes so as to achieve maximum benefit to the Government and the public. The rate at which needed improvements in statistics are carried out is limited not only by available funds, but by the supply of skilled personnel and other resources. The 1963 budget recommendations provide for acceleration of efforts to achieve a better balanced, more adequate current statistical program for the Government as a whole.

CURRENT PROGRAMS

Labor statistics.—Almost half of the increase of $2.5 million over the 1962 level recommended in this broad area is for extension and improvement of manpower and employment data. Emphasis will be placed on studying the effects of technological change, the determinants of labor force growth, the factors affecting worker mobility, the problems of selected groups with high unemployment rates, and similar problems.

Other subjects on which improved data are sought include wages and industrial relations, measurement of productivity, industrial hazards, foreign labor conditions, and social security programs.

Demographic and social statistics.—In this area an increase of $1.5 million is provided for three agencies. An increment of $0.7 million over 1962 for the National Center for Health Statistics in the Public Health Service will permit full scale operation of the National Health Survey and will provide for studies of vital statistics in relation to data from the 1960 Census of Population. The increase of $0.5 million recommended for the Bureau of the Census in this area provides for improvements in population estimates and projections and for exploration of problems involved in developing a national register of dwelling units. An increase is also included for the Office of Education to further strengthen its program of basic statistics on the educational system.

Prices and price indexes.—The increase in this area ($0.8 million) will enable work to be started on specific improvements which are recognized as urgently needed. In addition to increasing the number of items priced and the number of price quotations per city for the Consumer Price Index, provision is made for research on concepts and on the measurement of quality and for the improvement of various types of price indexes, including farm prices.

Production and distribution statistics.—This broad area, the largest shown here, involves a recommended increase of $2.9 million over 1962. About half of this increase is for improving agricultural statistics in the Department of Agriculture, including a planned expansion of the enumerative survey designed to improve crop and livestock estimates, and various studies on farm economic problems. The balance of the increase is for improvements in Bureau of the Census series covering data on retail, wholesale, and service trade; industry; foreign trade; the consumer anticipations survey; and other subjects.

Construction and housing statistics.—The increase ($0.2 million) in this area is equally divided between Bureau of the Census projects for the development of a price index for residential construction and for collecting information on construction expenditures of State and local governments.

National income and business financial accounts.—Over half of the total increase of $1.2 million in this area is for the improvement and extension of the use of existing records of the Internal Revenue Service to get more information on capital gains, depletion, depreciation, and other topics of economic importance ($0.7 million). Most of the balance of the increase is for programs within the Department of Commerce and covers such projects as improving data for measuring the balance of payments and initiating annual estimates of national income for the larger metropolitan areas.

PERIODIC PROGRAMS

The periodic statistical programs for 1963 include (1) the major censuses scheduled by law at 5- or 10-year intervals; (2) the revision of the Consumer Price Index; and (3) the Census Bureau's program to modernize its data processing systems equipment.

The funds shown are for the completion of processing and publication for the 1960 decennial censuses and include the amount needed to complete the 1962 Census of Governments. The amounts for the 1963 economic censuses cover the second year of a planned 5-year program. Preparatory funds for the 1964 Census of Agriculture, to be taken in October 1964, are for the first year of a 4-year program. Funds in the 1963 budget also cover the fourth year of a 5-year program to revise the Consumer Price Index ($1.3 million). A request for $4.1 million would provide funds to be expended over 2 years for modernizing the present electronic equipment in the Bureau of the Census.

EXECUTIVE OFFICE OF THE PRESIDENT

BUREAU OF THE BUDGET

Washington 25, D.C.

JANUARY 18, 1962.

SUPPLEMENT TO SPECIAL ANALYSIS I

PRINCIPAL FEDERAL STATISTICAL PROGRAMS IN THE 1963 BUDGET

This statement describes in greater detail than was possible in special analysis I of the 1963 budget the subject matter content of the new projects included in the principal statistical programs recommended for 1963.

The principal programs in the 1963 budget designed to collect statistical information for the use of the Government and the public are summarized in two categories: current and periodic. Recommendations for the current programs, reflecting the continuing year-to-year statistical activity of the various agencies, total $61.9 million in 1963, an increase of $9.1 million over 1962. The periodic statistical programs—the large-scale census-type surveys characteristically undertaken once or twice a decade—total $11.5 million for 1963, $1.3 million less than the amount available in 1962.

A summary description of the new projects included in the principal current statistical programs and the activities proposed under the periodic programs in 1963 follows.

RAYMOND T. BOWMAN,
Assistant Director for Statistical Standards.

SUPPLEMENT TO SPECIAL ANALYSIS I

PRINCIPAL FEDERAL STATISTICAL PROGRAMS IN THE 1963 BUDGET

CURRENT PROGRAMS

LABOR STATISTICS

This area includes the statistics compiled by the Bureau of Labor Statistics on employment, hours, and earnings, by industry; number and characteristics of persons in the labor force, including employment and unemployment status; labor turnover; wage rates; industrial relations; industrial hazards; foreign labor conditions; and productivity. It also includes the statistical work of the Department of Agriculture on farm labor, supply, and requirements. Included in this area for the first time are the activities of the Bureau of Employment Security, Department of Labor, which result in statistics of general public interest. Part of the BES programs included here are based on administrative byproduct statistics which serve the dual purpose of administrative and general-purpose statistics; the remainder represents the BES and State employment security agency share of the joint BLS-BES-State agency current employment and labor turnover statistics programs.

Almost half of the increases recommended for this area in 1963 are for the extension and improvement of manpower and employment data. The major program changes are identified below. In addition, increases for administrative costs and other adjustments have been included in the $2.5 million increase.

Manpower and employment data

The 1963 budget provides $200,000 to enable BLS to develop annual estimates of the hours and earnings of all employees in nonagricultural industries. Present monthly figures are limited to production workers in manufacturing and nonsupervisory workers in most other industries. Added data on nonproduction workers will provide measures of labor input for use in productivity estimates.

BLS obtained $300,000 this year to engage in a series of studies of the unemployed, most extensive being a survey in depth of the characteristics of the unemployed, their employment and job-hunting experience over several years, the impact of their unemployment on the labor force participation of other family members and on family income, and other factors affecting unemployment status. An equal amount of funds is being continued in 1963 for carrying on similar studies of the unemployed. An additional amount of $600,000 is also being provided to obtain further information on the labor force, particularly concentrating on occupational information, factors affecting worker mobility, especially occupational mobility, the determinants of labor force growth, and the problems of selected groups, such as youths and minority groups, with high unemployment rates.

Some $300,000 is also included in the 1963 budget to meet increased costs, primarily in programs carried out cooperatively with the State employment security agencies, and to complete the extension of the labor turnover statistics program (in manufacturing industries) to all States.

Wages and industrial relations

One hundred thousand dollars is provided BLS to obtain further data on employer expenditures for fringe benefits and the composition of payroll hours. For manufacturing, the additional information will permit publication of seprate data for some 60 industries at the 3- and 4-digit levels for which productivity estimates are contemplated. An additional $50,000 will permit (1) starting a continuous study of labor-management relations at the plant level and (2) supplementing the analysis of major collective bargaining agreements by examination of those agreements dealing with small establishments. Another $100,000 will be allocated to studies of union and management organizations and to providing technical assistance and services in labor disputes, and about $50,000 is provided for collection of additional data in the survey of professional, administrative, and technical salaries.

Measurement of productivity

An important step in minimizing the adverse effects of technological change is the development of objective information about emerging trends in various industries and in the kinds of labor problems that might be anticipated. Three hundred thousand dollars is included in the BLS budget for studies of (1) individual selected industries and (2) of major innovations that affect a number of industries.

Industrial hazards

Fifty thousand dollars has been provided to strengthen the present BLS program of cooperation with State labor departments in developing work injury-rate statistics. An additional $50,000 is allocated to sponsoring State agency programs for the development of meaningful and comparable workmen's compensation statistics.

Foreign labor conditions

One hundred thousand dollars is included in the 1963 budget for (1) a reports program in the Bureau of Labor Statistics which would provide summaries on labor developments in countries of the free world important to the United States; and (2) to expand the pilot program for developing international comparisons of unit labor costs and other labor conditions.

Employment security activities

An increase of $245,000 is recommended for the extension and improvement of statistical programs on characteristics of insured unemployed, labor market information, benefit adequacy, and postexhaustion studies.

DEMOGRAPHIC AND SOCIAL STATISTICS

The programs in this area are those which involve the number, distribution, and well-being of the people of the United States, acting as individuals or as groups. The principal statistical programs included here are the activities of the National Center for Health Statistics, the program for current population studies in the Bureau of the Census, the educational statistics program of the Office of Education, and the studies of farm population by the Economic Research Service of the Department of Agriculture.

Much basic data in this area result from the census of population taken in 1960, included under periodic programs later in this report. The availability of detailed data from this census makes possible related analysis in all the fields included in this group.

Center for health statistics

An increase of approximately $700,000 is recommended for the National Center of Health Statistics, including about $500,000 for the national health survey and $200,000 for vital statistics programs and other statistical activities.

The national health survey program comprises three major activities: The health interview survey, the health examination survey, and the health record survey. The survey covers a wide range of health and health-related topics including various important demographic, social, and economic factors. The program recommended provides for continued full-scale operation of the health interview survey with more adequate provision for methodological and developmental studies and quality controls. The health examination survey will also continue full-scale operation. The 1963 program includes the processing and publication of the data on a national sample of adults aged 18–79 gathered during the first completed cycle of examinations. Provision is also made for methodological and developmental studies to prepare for the second cycle of this survey emphasizing pediatric examinations. The necessary work basic to the health record survey is included, covering the planning, pretesting of questionnaires and schedules, and selection of a sample of all institutions providing hospital and medical services to individuals.

The recommended increase for the vital statistics program provides for (1) a continuation of census-related studies such as the construction of National, State, and geographic divisional life tables and related actuarial tables; (2) the development of more adequate statistics on marriages and divorces; (3) assistance to States in improving registration methods; and (4) acceleration of the processing and publication of basic vital statistics reports.

The increase recommended for other activities of the National Center includes provision for an expansion of activities in conducting analytical studies on the health problems and health status of the population and on the impact of health programs and activities on the Nation's health.

Population estimates and projections

In the Bureau of the Census, an increase of $100,000 is recommended to improve and expand its program of population estimates and projections. Research will be undertaken to make the annual estimates of total population by States more accurate, to develop better methods for making current population estimates for local areas, and to improve population projections for the United States, as a whole. With local cooperation it is expected that a consistent set of population estimates for individual metropolitan areas will be developed.

Register of residential addresses

The sum of $400,000 is recommended to finance exploration of the problems involved in developing a national register of residential addresses. Such a register would involve transcribing the addresses from the 1960 census enumeration listing books on to magnetic tape. The listings would be kept up to date by incorporating data from building permits and other sources. If the developmental work and testing of an address register demonstrates the effectiveness of this approach, its use will help improve completeness of coverage and achieve lower costs in future censuses and provide a more efficient method for drawing samples for current population and housing data.

Education statistics

The increase of $200,00 for the Office of Education, Department of Health, Education, and Welfare, will make possible needed improvements in the statistics for this important area. This increase will permit the strengthening of the planning and technical staff and the exploration of more efficient methods of collecting and processing data to improve their quality and timeliness.

PRICES AND PRICE INDEXES

Four major price index series are compiled in this program area. The Bureau of Labor Statistics prepares the Consumer Price Index and the wholesale price index. The Statistical Reporting Service of the Department of Agriculture computes the index of prices paid by farmers and the index of prices received by farmers. The index of prices of new houses, for which data will be collected as an integral part of the construction statistics program of the Bureau of the Census, is discussed under that subject matter area.

Consumer Price Index

The major portion of the increase in funds in the Bureau of Labor Statistics 1963 budget for price statistics is to expand and improve the collection of price data for the Consumer Price Index as follows: (*a*) The boundaries of the local areas in which are located the stores from which price data are collected have been limited to the central city or, in some instances, the downtown section of the city. These are to be extended to include suburbs so that the stores selected will be representative of the entire metropolitan areas; (*b*) the use of scientific probability-based methods will be extended in the sampling of stores from which prices are collected and items to be priced; (*c*) the number of stores and items and the number of price quotations from items other than food will be increased. These steps will improve the accuracy of the index and will permit the calculation of the approximate sampling error in it—one of the high priority recommendations of the Price Statistics Review Committee.

In addition to these extensions of the pricing program for the Consumer Price Index, this budget includes funds, also urgently recommended by the committee, to provide for price and index number research related to problems of changes in quality of items priced, introduction of new items, handling seasonal items and making seasonal adjustments and other technical problems.

Wholesale price index

The wholesale price index reflects the movement of all types of commodities, from raw materials to fabricated products, sold on primary markets. Additional funds are included in the 1963 budget to permit improvement of the index and the price data collection program on which it is based. A system of indexes classified and computed by industry sectors will be initiated. This will make the various components of the index more directly comparable to other types of data which are grouped in accordance with the standard industrial classification and will make them more useful in analyzing economic changes, such as productivity, for example. Work next year will be directed to output price measures and will involve the development of weighting structures for the industry sectors, classification of commodities priced according to their producing sector, beginning the computation of indexes for sectors or combinations of sectors for which present coverage is adequate, and determination of those sectors which require expanded data collections. Development of a system of indexes classified according to industry sectors in which the commodities represent inputs is deferred for later years. Some beginning will also be made in extending the program to cover industrial services. The present limitation to commodities represents a serious deficiency in the use of the index as a measure of industrial costs and nonretail prices.

Standard budget studies

Finally, additional funds are provided to enable the Bureau of Labor Statistics to reexamine concepts and techniques for deriving standard budgets, such as the city worker's family budget and the retired couple's budget on which the Senate Special Committee on Aging requested testimony last year. This developmental work will provide the basis for later computations of various standard budgets utilizing data from the surveys of consumer expenditures being conducted as part of the revision of the Consumer Price Index.

Prices received and paid by farmers

No additional funds are provided in the budget for the Statistical Reporting Service of the Department of Agriculture for price statistics. However, research which that agency has been doing in methodology and the study of data collection problems peculiar to areas of prices paid and received by farmers will be directed toward the development of plans for an improvement program which can be implemented in subsequent years.

PRODUCTION AND DISTRIBUTION STATISTICS

An increase of $2.9 million over 1962 is proposed for production and distribution statistics. About half of this increase is for improving agricultural statistics in the Department of Agriculture, including a planned expansion of the enumerative survey designed to improve crop and livestock estimates and various studies on farm economic problems. The balance of the increase is for improvements in Bureau of the Census series covering data on retail, wholesale, and service trades; industry; foreign trade; consumer anticipation; and other subjects.

Statistical reporting for agriculture

A $750,000 increment is provided to continue the planned expansion of the enumerative survey which collects crop and livestock data on a probability sample basis. This increment represents the third year of the expansion of this survey technique to additional States in a program to improve crop and livestock estimates and forecasts.

The additional funds provided for this purpose in the 1963 budget will be used (1) to expand the program to an operating basis in 4 additional States (Virginia, Michigan, North Dakota, and South Dakota) and (2) to initiate pilot survey in 11 Western States. The program will then be on a fully operational basis in 24 States which account for most of the cotton and corn crops. In the pilot survey States, the sample will be augmented in the wheat producing areas to provide national estimates on a probability basis for that crop also.

An additional $175,000 is provided for (1) the development of new or improved systems and programing techniques for automatic data processing and (2) expanding research and development work on statistical techniques and methods. The data processing studies are designed to develop methods that are superior to those now used in accuracy, timeliness, and operating efficiency and to provide ways and means of obtaining significant data not otherwise obtainable. Intensive analysis and review of systems and programing techniques will insure that within the capacity of the equipment, maximum service is provided to economic and statistical programs.

Reseach and development work on statistical techniques and methods must proceed along with the expansion of the long-range enumerative program into new geographic and community areas in order to insure maximum speed, efficiency, and accuracy. The work to be initiated or strengthened includes (1) research on sampling frames and development of methodology for using area and list frames in combination; (2) development and construction of new sampling materials which will make possible more efficient sample designs; (3) design and analysis of general purpose and special purpose enumerative and mail surveys at National, regional, and State levels; and (4) development of objective yield forecasts for sorghum, rice, and tobacco.

Agricultural economic research

Increases for this activity (excluding foreign economic analysis) amount to $780,000. Of this, $190,000 is for expanding economic studies on rural development. Persistent low incomes of large numbers of rural families in many areas call for studies to develop recommendations for adjustments of resource allocations both within and outside of agriculture for potential economic development of rural areas. The problems in the Appalachian region are especially acute. Two hundred and eighty thousand dollars is for expanding studies on land and water development and conservation so that these basic resources can be better managed. One hundred and twenty-five thousand dollars is for intensifying research on the size and structure of farms that would be most efficient under alternative conditions. It is clear, for example, that mechanization has increased, and will continue to increase, the inevestment and acreage requirements for efficient low-cost production. One hundred and eighty-five thousand dollars is for strengthening the economic and statistical analysis work in the Department. This work is basic to providing an improved outlook service for farmers. Also, the development of effective farm programs calls for the evaluation of alternative programs as to impacts on farm output, prices, cost, and income. Likewise, policy decisions by the Congress and the administration require that the factual basis for such actions be accurate and comprehensive.

Business statistics

One hundred and eight thousand dollars is recommended to inaugurate a program to measure the physical and dollar volume of retail inventories of large consumer durables. This proposal grows in part out of recommendations of the Federal Reserve Board's Consultant Committee on Inventory Statistics which emphasized the gap in our data on physical volume of inventories. It also reflects an increasing reliance on knowledge about consumer behavior; in addition, the proposed data would supplement existing data on retail trade activity. Initially the program aims at monthly measures covering all large consumer durable goods in the aggregate in terms of both physical volume and value. After 2 or 3 years of development, the program is expected to expand to produce data individually for such separate classes of merchandise as furniture, appliances, automobiles and equipment, etc.

An additional $65,000 is recommended for a monthly survey to produce estimates of selected service trades receipts. These data will provide a measure of an increasingly important share of consumer expenditures and better source data for current estimates of personal consumption expenditures in the national accounts.

Manufacturing and industrial statistics

Gaps have developed in the Bureau of the Census program of monthly, quarterly, and annual commodity surveys, as a result of the growing economic importance of new products and new industries. The amount of $150,000 is recommended for 1963 for expansion of this program. New surveys would be selected for 1963 from such fields as electronic components, industrial control devices, drugs, medicines and other finished chemicals. Most of the surveys would be on an annual basis covering shipments or production data, in terms of both dollar value and physical quantity. For selected products additional items such as inventories, receipts, consumption, or equipment in use would be covered. Some of the commodities with significance as economic indicators would be obtained on a monthly or quarterly basis. Some existing commodity surveys would be expanded to cover inventory data for key products.

The current proposal provides for the inclusion in the Census Bureau's budget of a group of textile industry surveys heretofore carried out by the Bureau with funds transferred from the Business and Defense Services Administration. The amount of $100,000 is provided to maintain these surveys which were initiated in fiscal year 1960 in recognition of the expressed needs of numerous trade and governmental organizations. The survey program covers (*a*) monthly inventories and unfilled orders for textile piece goods, finished and unfinished, (*b*) production of sales yarn (monthly) and of all yarn (annually, (*c*) production of other items such as sheets and towels (annually) as well as fabric blends and mixtures.

The sum of $100,000 is provided to initiate a program of weekly industrial economic indicators which will assist in rapid recognition of suspected business cycle turning points and in guiding courses of action to be taken. Where existing weekly series under private sponsorship exist and meet appropriate tests of reliability and usefulness, they will be incorporated in the composite of series; where available only in terms of physical quantities they will be converted to a dollar basis by means of appropriate unit values. In most industrial areas, however, Census will be obliged to collect weekly orders and sales data through new surveys. While the aim will be to cover all major manufacturing areas, emphasis will be placed on durable goods industries, especially machinery and equipment. The weekly series will be closely integrated with existing monthly data for the same area.

Foreign trade

Export statistics have for many years been compiled in terms of a special export commodity classification (schedule B) the class structure of which was designed to reflect patterns of international trade. There has been a growing recognition in recent years of the advantage of being able to analyze export data in relation to corresponding production data, as compiled in terms of the product classes related to the standard industrial classification. A sum of $48,000 is included in the budget of the Census Bureau to begin the task, expected to extend over two or more fiscal years, of effecting a conversion of the schedule B code to the standard industrial classification product classes. This involves careful analysis of product classes which do not lend themselves to easy conversion; consultation with industry groups; decisions as to the optimum degree of product detail for export statistics and as to the basis for summary groupings; preparation of detail coding specifications and an educational program directed at shippers; and, for a transition period, the publication of statistics on both new and old basis.

U.S. foreign trade statistics have until the middle 1940's appeared in final, official form in an annual set of volumes entitled "Foreign Commerce and Navigation of the United States." These volumes have presented the final corrected figures, both in full detail and in various useful summary arrangements together with a full technical explanation of the statistics. This volume has not appeared since the one covering data for 1946, although an expectation of resumption of publication has persisted from year to year. The current proposal is to allocate $100,000 for a resumption of this yearbook as a normal and essential feature of the foreign trade statistics program of a leading trading nation. One benefit of resumption will be to make possible the publication of a body of shipping statistics which, again for economy reasons, have been published in recent years only in token form.

The Census Bureau's 1963 budget for the foreign trade program includes also an item of $62,000 to anticipate a normal increase in workload with the expansion of trade—this being a program where workload is related in a direct way to the volume of activity being measured.

Statistical abstract program

An increase of $48,000 to strengthen the program of supplements to the "Statistical Abstract of the United States" is provided for in the Census Bureau's 1963 program. In the past, work on supplements has been sporadic, as limited funds permitted, with publication and tabulation usually handled as a byproduct of a major census. The additional funds proposed would permit a stronger and more regularly planned program of supplements and intensified work on data sources.

Census emergency planning program

The Bureau of the Census will expand its program to provide data on human and economic resources for the National Resources Evaluation Center and the Office of Emergency Planning regional offices. An additional $217,000 is included in the 1963 budget for this purpose.

Consumer anticipations survey

A $200,000 increase in the Census Bureau's budget proposal will permit the compilation of data on consumer inventories, purchases, and plans to buy for selected important consumer durable goods. These data are of significant use in the analysis and prediction of economic fluctuations. During the developmental period this survey was financed by the Board of Governors of the Federal Reserve System and the continued collection as part of the Government's regular statistical program is considered highly desirable.

CONSTRUCTION AND HOUSING STATISTICS

Since consolidation of this program in the Department of Commerce in 1960, the Bureau of the Census has made significant progress. This is evidenced by the complete overhauling of the housing starts series to improve both its accuracy and timing, the initiation of a completely new quarterly series on expenditures for residential additions, alterations, repairs, and maintenance and by the introduction of methods and procedures which should ultimately lead to better measurement of construction activity. The proposed increase of $200,000 for 1963 represents another step in perfecting and extending the construction and housing statisics programs to meet current requirements.

Half of the increase would be used to develop quarterly measures of construction expenditures by State and local governments. It is estimated that such expenditures account for over one-fifth of the amount spent on all new construction. The importance of this segement requires more accurate and more frequent measurement than is now available. The balance of the increase is to start development in 1963 of a price index of new single family residences. This is the first phase to be completed in a comprehensive program for the development of price or construction cost indexes for major construction types, both residential and nonresidential.

NATIONAL INCOME AND BUSINESS FINANCIAL ACCOUNTS

The statistical programs included here are concerned primarily with the analysis of the national economy. The area includes all the work of the Office of Business Economics—preparing estimates of national income and product, measuring and analyzing business trends, and computing the balance of international payments. It also includes the preparation by the Internal Revenue Service of financial statistics from income tax returns filed by individuals, sole proprietorships, partnerships and corporations; estimates of farm income by the Economic Research Service; statistics on the financial and other operations of State and local governments compiled by the Bureau of the Census; the quarterly financial reports program, presenting income and balance sheet data for manufacturing corporations, conducted jointly by the Federal Trade Commission and the Securities and Exchange Commission; and other economic statistical serious compiled by the Securities and Exchange Commission. Increases for improvements in our national income and business financial accounts aggregate approximately $1.2 million.

The largest single increase ($700,000) represents provision for both an increased workload in the regular statistical program of the Internal Revenue Service and for extended use of the existing records of the Internal Revenue Service to obtain more information on capital gains, depreciation, depletion, source of interest received by individuals, analysis of foreign tax credit and ownership of foreign subsidiaries, and other subjects of economic importance that are significant in tax policy formulation.

Three new projects are planned for the Office of Business Economics: (*a*) $100,000 for the initiation of annual estimates of income for about 100 metropolitan areas, showing the industrial sources of income and back-year estimates for 1929 and 1950, which would provide a new source of data for marketing research and for studying patterns of regional growth; our present regional income estimates do not go below the State level; (*b*) $60,000 for the study of the role of Government in economic activity, to explore various aspects of the influence of both Government expenditures and receipts on the economy. The statistical basis of this project would be an elaboratiton of the Government sector date of the national income and products accounts; (*c*) $100,000 for additional basic data research and analysis in the area of the balance of payments. Recent attention directed to the Nation's balance-of-payments position has intensified demands for special research and compilation of balance-of-payments data, pointed up limitations in the existing data and the need for analysis of the interaction between our economy and the rest of the world.

The sum of $100,000 is also included within the overall increase for a quarterly survey, in the Bureau of the Census, to provide national estimates of State and local government revenue, expenditures, indebtedness and financial assets. These data would help to measure the impact of current economic trends upon State and local government finances and would also supply a much firmer basis for the Government component of statistics on national income and product.

Periodic Programs

The periodic programs include: (1) The major censuses scheduled by law at 5- or 10-year intervals; (2) the 5-year program to revise the Consumer Price Index; and (3) the Census Bureau's program to modernize its computing equipment.

MAJOR CENSUSES

Census of governments, 1962

The sum of $1.4 million is provided in 1963 to complete this quinquennial census of over 90,000 State and local governments. Four broad subject fields are covered—governmental organization, public employment, taxable property values, and governmental finances (revenue, expenditures, debt, cash, and security holdings). The total cost of this census, over 3 fiscal years, is approximately $2.6 million. Data collection and processing will be completed in 1963 and final reports published.

Economic censuses, 1963

The sum of $3.2 million is provided for preparatory work on the 1963 censuses of business, manufactures, and mineral industries and transportation. This includes provision for general administrative costs allocable to this program.

Census of business.—The preparatory work for the forthcoming census of business is estimated at $1.5 million and includes: Development, review, and printing of data collection forms in time for them to be available for the information of respondents at the beginning of calendar year 1963; a precanvass of large multiunit companies to insure proper coverage and reporting arrangements; a field listing needed for producing shopping area data within metropolitan areas; completion of a test census (begun in 1962) designed to evaluate the feasibility of collecting and processing reliable merchandise line and other new data; testing plans to extend the census to additional kinds of business; and development of necessary plans and specifications, for all phases of the census.

Censuses of manufactures and minerals.—The preparatory work for these two censuses is estimated at $1.2 million and includes all aspects of form development and plans and specifications for all phases of the census. Preparatory tasks include the review of products shipped and materials consumed categories for individual industries; the preparation of some 250 report forms for printing, and a canvass of large firms to determine the specific reports to be filed. In addition, the collection and partial tabulation of 1962 data for manufacturers on fuel consumption and on installed prime movers and generators are planned.

Census of transportation.—Special studies conducted for other Federal agencies and private organizations over the past several years afforded the opportunity to test the concepts and methodology planned for the three major surveys that will constitute the census of transportation and thus decreased the need for preparaory funds. The three surveys are: (*a*) A survey of the volume of goods shipped by selected classes of shippers, showing broad area movements by means of transport employed; (*b*) a survey of passenger travel; and (*c*) a truck and bus delivery. The funds for fiscal year 1963 ($175,000) provide for residual preparatory work, development and review of forms, and some data collection and processing for the passenger travel survey.

Census of agriculture, 1964

The sum of $700,000 is provided in the 1963 budget for preparatory work in connection with the 1964 census of agriculture which will be taken in the fall of 1964. These funds will be used for: (1) Geographic work, such as delineating enumeration districts, consulting local officials, and preparing maps; (2) reviewing questionnaires in consultation with Government and non-Government groups; (3) updating lists of large and special farms so as to prevent omission or duplication of these units; (4) preparing plans for field enumeration, including recruitment, training, and providing supervision; and (5) preparing tabulation programs so that maximum use can be made of the data processing equipment.

Eighteenth decennial census

No new funds are requested for the eighteenth decennial censuses in 1963. The 1962 appropriation will remain available until December 1962. An amount of $1.1 million will be carried over from 1962 funds to complete the processing and publication of reports for the 1960 censuses of population and housing.

REVISION OF CONSUMER PRICE INDEX

The Bureau of Labor Statistics budget includes $1.3 million to finance the fourth year of a 5-year program to revise the Consumer Price Index. Tabulation and analysis of consumer expenditures data collected in fiscal years 1961 and 1962 will be nearing completion this year, as will the determination of the market basket and the weighting factors for the revised index.

Upon completion of this work early in fiscal 1963 full scale collection of price and rent data for the revised index will be initiated and test indexes will be computed. This program will be completed with the publication of the Consumer Price Index on the revised basis in January 1964.

Funds in the 1963 budget also provide for tabulation of consumer expenditures data for rural nonfarm and farm families being collected in fiscal 1962 in cooperation with the Department of Agriculture.

MODERNIZATION OF COMPUTING EQUIPMENT

The 1963 budget includes $4.1 million to be expended over 2 years in modernizing and increasing the capacity of the present electronic equipment of the Bureau of the Census. Present plans call for the obligation of $3.7 million in fiscal 1963 for this purpose.

Chairman PATMAN. I notice in your statement you have stated:

The present administration remains alert to the developing economic trends, and stands ready to change its policies when the evidence shows this is appropriate.

Therefore, I am encouraged, not for the purpose of controversy, but I hope constructive criticism, to bring to your attention some matters that I think worthy of consideration.

On page 40 of the budget you have estimated that the public debt will decrease slightly from 1962 to 1963. Yet on page 99 you estimate that the interest on the national debt will rise slightly.

What rate or what bill rate and what long-term rate have you used for computing the effect of interest costs on the Federal debt in 1962 and 1963?

Mr. BELL. As I am sure you know, Mr. Chairman, the Treasury Department prepares the estimates of interest costs which are reflected in the budget. Their practice, if I understand it correctly, is to assume, and they certainly did this in the present case, to assume, that present rates will continue through the period covered by the estimates.

Chairman PATMAN. With no increase contemplated?

Mr. BELL. No increase is contemplated, sir.

Chairman PATMAN. In your statement, Mr. Bell, you state this:

> Second, there is no reason to expect a sharp change toward tight-money policy that took place in the last expansion.

It seems to me that one of the reasons why you can expect there will be no sharp change toward a tight-money policy is that you have already got a tight-money policy.

You know, I was sometimes critical of the tight-money policy of the Eisenhower administration because I thought that was a very bad policy. On at least three occasions that tight-money policy was used for the purpose of dampening down the economy, and on three occasions that policy was very largely responsible for bringing about recessions.

I must observe, however, with some reluctance, that we have had a tighter money policy under President Kennedy's administration than we ever had under President Eisenhower's administration. If interest rates are a reliable barometer of the supply and demand for funds, then it is obvious that this is so because we have had a short-term rate about twice as high as the Eisenhower administration ever had in a period of recession, and you have a long-term rate which is even higher than the Eisenhower administration had in 1953 and 1955, and which is about the same as the Eisenhower administration had in 1957 when the Federal Reserve was deliberately trying to dampen the economy.

I just wonder if you would like to comment on that.

Mr. BELL. Well, Mr. Chairman, I believe you will have on the stand on next Tuesday, Secretary of the Treasury Dillon and Mr. Martin, Chairman of the Federal Reserve Board, who are certainly following these matters much more closely than I. I would not want to go into this matter in any detail. There is one comment that I should make immediately, and then let them follow up this matter more thoroughly.

I would respectfully differ with your conclusion that the policy which has been followed is tighter or has been tighter in these recent months than that which was followed under the previous administration. I entirely agree that interest rates are higher now than they have been in some previous years. There has been an upward trend in interest rates for perhaps 10 or 15 years. But in shorter run terms, considering the period of the swing of the economic cycle over the last year and a half, certainly the policy has been markedly different from the policy followed in 1958 and 1959. At the present stage of the cycle, economic recovery having been moving strongly forward now for some months, I think it is rather noteworthy that the monetary policy continues to be one of relative ease.

As is indicated in my statement, I do not see any reason to expect soon any change in that policy of relative monetary ease. I repeat, I recognize, of course, that interest rates are higher today than they were some years ago, and that is a subject for additional discussion, and perhaps we hade better leave that for Tuesday.

Chairman PATMAN. If it is not too much trouble, Mr. Bell, I wonder if you will do this: For the record, make a computation of what the interest costs on the Federal debt would be in 1963 if instead of paying the average interest rates you expect to pay, you paid the average interest which was paid during President Truman's administration, and also during the first term of the Eisenhower administration.

Mr. BELL. That could be done.

Chairman PATMAN. And I wish that you would carry that forward 10 years, and 20 years, so as to indicate what we will probably be paying as interest on the national debt in 10 and 20 years, after these 2½-percent bonds, most of them, are out of the way.

Mr. BELL. This would be on what assumption—that the size of the debt is the same?

Chairman PATMAN. Assuming it is the same, yes.

Mr. BELL. As its composition changes with the replacement of the old 2½-percent bonds, you mean?

Chairman PATMAN. Yes.

Mr. BELL. All right.

(The information referred to is as follows:)

On the basis of average interest rates paid on the outstanding public debt during the fiscal years 1946–53 the interest cost on the debt during fiscal 1963 would be about $6.6 billion. On the basis of average rates paid during fiscal years 1954–57 the 1963 interest cost would be about $7.1 billion.

The computed average interest rate on the public debt at the beginning of fiscal year 1946 was 1.936 percent; at the close of 1953 it was 2.438 percent; and at the close of 1957 it was 2.730 percent. At the present time the computed average interest rate is 3.135 percent.

A projection of interest costs forward 10 or 20 years would have to be based on a number of assumptions in addition to the size of the debt—among these are the levels of rates and the changing composition of the debt. The Treasury Department therefore advises that projections of interest rates or detailed debt composition changes can hardly be made in a meaningful way for a period so far into the future. However, since some of the public debt securities presently outstanding were originally issued at interest rates below current rates, it can be said that the refinancing of these securities, assuming no further change in present interest rates or in the composition or size of the public debt, would indeed cause an increase in interest expenditures in the future.

Chairman PATMAN. In your special analysis "E," beginning on page 304, you indicate that Government loan guarantees and insurance are to be increased considerably in fiscal 1963, from $26 billion to over $28 billion. Have you made any assessment of the economic impact of this increase, either on interest rates or on economic activity?

Mr. BELL. Well, sir, I do not believe it would be accurate to say that we have attempted to make any special assessment of the impact of this fact on the economy. It is obviously one of the elements which will contribute, or which we expect to contribute, to a continuing growth and expansion. These loans and loan guarantees, as you all know, affect the housing market, the condition of small businesses, farmers, and so on. An increase as projected here indicates that the Federal Government in these ways will be contributing to an expansion of economic activity in those various fields.

So far as the latter half of your question—the effect of this on interest rates—is concerned, I suppose it would be appropriate to say two things:

Firstly, it is the intent and purpose of many of these activities, whether they are direct loans or loan guarantees, to permit borrowers to obtain loans at rates which are lower than would otherwise be the case.

Consequently, the general effect of these loans and loan guarantee programs, most of them at least, is to permit the borrowers to obtain loans on better terms than would otherwise be the case, and I suppose it would be accurate to say that this is a force which tends to keep interest rates down, at least for those borrowers.

The second point, however, which I think is proper to note, is that as business activity recovers during a period of economic stimulation, growth, and recovery from recession periods, I think any economist would agree that one must assume that there will be continuing pressure on interest rates to move them upward. So far the rates are holding quite stable, and all of us have been watching the housing mortgage rate very closely and we have been taking such steps as seemed feasible to hold it where it has been for some time.

But as the months go by, and the economy expands strongly, there cannot help but be increasing pressure upward on interest rates.

Chairman PATMAN. Thank you, Mr. Bell. Senator Bush is recognized.

Senator BUSH. Thank you, Mr. Chairman. I would just like to observe on this question which the chairman calls tight-money policy, that I never have agreed that it was tight money policy that created any of the recessions in the postwar period. There has been a sound money policy, and it seems to me that this administration, as the previous one, has rather committed itself to that, and I am delighted that it has.

I do not think that anyone can prove that the recessions of the past 10 years were due to monetary policy. One was the result of the aftermath of the Korean war, and the other was the result of the aftermath of the great automobile splurge of 1957, and the overselling of automobiles, and the overextension of the public in buying them. As to the last one, I believe a case can be made that it was the aftermath of the steel strike.

I hope we will not have to have an aftermath of a steel strike in 1962, but I observe with some apprehension that a great deal of buying is being done in advance on account of the threat of a steel strike. This, I think, does impose somewhat of a hazard.

The interest rates, I believe, have been generally responsive to the needs of the country and to the laws of supply and demand, and to the extent monetary policy has been used in affecting interest rates this year, I believe they have been used wisely in response to the needs of the country, including the balance-of-payments problems.

As I have said yesterday, I regard this as the overriding and most important single consideration affecting our economy.

Mr. Bell, in your statement, you refer to trust funds. You have taken into account the possibility of a medicare bill being passed under the social security system.

Mr. BELL. Yes, sir; there is not expected to be any effect on the 1963 budget.

Senator BUSH. Can you speak a little louder, please.

Mr. BELL. I am sorry, sir. I thought the loudspeaker would take care of my soft speaking. The medicare bill, if enacted, is not expected to result in any increased trust fund expenditures during the fiscal year 1963, and I believe the same thing is true on the receipts side, is it not? My staff tells me that there would be a small trust fund revenue effect of the medicare bill of about $42 million only during fiscal year 1963. The bulk of the effect on both receipts and expenditures would take hold with the fiscal year 1964.

Senator BUSH. Would you expect that to continue to be the case if this bill became law?

Mr. BELL. I am not sure that I follow you.

Senator BUSH. In other words, is it your opinion that a medicare bill, under the social security system approach to insurance for the aged, would have no impact upon the Federal budget?

Mr. BELL. No, sir. That was not what I meant to say. I was talking only about the timing. The timing of the bill and the arrangements for getting the program underway would be such that it would not have a significant effect in the fiscal year 1963, but it would have a very significant effect beginning with fiscal year 1964 and each year thereafter.

Senator BUSH. Why would it, if the taxes are designed to carry the load?

Mr. BELL. Well, these are trust funds, receipts, and expenditures.

Senator BUSH. You are speaking of trust fund accounts rather than the administrative budget?

Mr. BELL. Yes, sir.

Senator BUSH. I am addressing my question, and I should have been more specific, to the administrative budget.

Mr. BELL. All right.

Senator BUSH. I now ask you to comment on that.

Mr. BELL. The effect on the administrative budget, so far as we can see, would be to reduce to some extent the budgetary outlays for welfare payments. The reduction would not be large, less than $100 million as I recall it. Elderly people would have their medical bills taken care of under the social security system, and some of them are now receiving their medical care through the welfare program in direct budgetary outlays—that would no longer be necessary.

Senator BUSH. Your conception is that this type of approach to the problem should be set up so that the taxes from the social security system would carry this?

Mr. BELL. That is right.

Senator BUSH. That is definitely the intention of the administration.

Mr. BELL. Yes, sir; it is.

Senator BUSH. You say—

> there is no reason to suspect a sharp change to a tight money policy that took place in the last expansion.

I have disavowed my affection for that expression, but we will go along—

> with the good record on price stability so far in this recovery, and with the absence of any indication of an early resumption of inflationary measures, the monetary authorities within the restraints imposed by the balance-of-payments consideration should be in a better position to continue their policy of monetary ease than they have been in previous postwar recoveries.

Will you kindly amplify on that language, so that I can understand better what you mean by the restraints imposed by the balance-of-payments consideration?

Mr. BELL. Yes, sir; I apologize for rather a complicated sentence structure there.

Senator BUSH. No, I think it is a perfectly valid approach, but I am interested in what is behind that language.

Mr. Bell. As you know, Senator, the President has been deeply concerned and continues to be deeply concerned over the problem of the U.S. balance of international payments. The policy which he has followed, including a number of steps which he has recommended to the Congress and which have been enacted, have resulted in an improvement in the balance-of-payments situation from 1960 to 1961.

In the calendar years 1959–60, the net deficit in the balance of payments was in the order of about $4 billion, and the deficit in 1961 was on the order of $2 billion. This is a substantial improvement. But, it is by no means an eradication of the difficulty. We still have a balance-of-payments problem which must be regarded in the longrun sense as very significant and very much to be concerned about. I believe I am saying only what you said a little earlier, that the balance of payments is a matter of serious policy concern to all of us.

One of the aspects of the balance of payments with which anyone concerned with that problem must deal is the relationship between the level of interest rates and the movement of capital. This is a fairly substantial and complicated subject and it must be looked at at least two different ways—first, the short-term problem of money flowing from the New York market to the European markets and back, depending on the changes in short-term rates and the temporary advantages that a holder of funds may obtain in one market as against the other.

It is necessary to be concerned about these matters; and at the same time, they do not represent the underlying difficulties with the balance-of-payments position. However, the possibility of substantial short-term movements of capital must always be in the minds of those who are establishing rates or interest rates. This is one of the important aspects of what is meant here by a constraint imposed by the balance-of-payments consideration.

Surely the Federal Reserve Board must consider in establishing a rediscount rate or making any change in it, the effect it might have on the short-term movements of capital between countries.

In the longer term sense there are also constraints—although they are probably much less urgent and perhaps much less significant—in the sense that long-term capital to some extent will probably go where there is a differential return.

But when a businessman or a backer is investing long-term capital there are, of course, many considerations which he must weigh, and I believe most economists would consider that interest rates are perhaps not the most important of those considerations. There is long-term safety of the capital, and return on the investment. These are probably more significant in making long-term capital decisions than the particular rate of interest at the time.

Nevertheless, it is still one significant factor, but, particularly, there is the short-term relationship between international capital movements and the interest rates. That is the major point which was referred to here in this comment.

It is a very hypothetical assumption, but if there were a large and striking and sudden movement of capital from the United States abroad, one of the steps that might make sense in the very short run might be a lifting of interest rates for that purpose. This is not something that any of us expects to happen, but clearly it must be in the back of our minds at all times.

Senator BUSH. My time is about up, but when I come around again, I would like to pursue this subject a little further, along this line: It seems to me in view of the balance-of-payments problem, which you recognize and the administration correctly recognized, and increasingly so as being of overriding importance, it would have been desirable to produce a budget with a substantial cushion in it.

In other words, as we are going ahead in national income, and prosperity and production and reducing unemployment, and so forth, and making very rosy forecasts, it seems to me that if we can't establish a valid dependable surplus under those conditions, it is hard for us to convince our friends abroad who have these $17 billion or $18 billion on deposit here, short term, that we ever will do it.

I will come back to that when my turn comes around.

Mr. BELL. Perhaps it might be sensible if I respond to that now.

Senator BUSH. I would be glad if we would.

Chairman PATMAN. You may proceed.

Mr. BELL. This is a very relevant question and put very precisely, and one of the most important which was faced in framing the policies which the President has expressed in his budget.

I think perhaps the shortest and simplest way to answer it is that while we anticipate a continuation of the very strong economic recovery which is now underway, it would not be our characterization that this is a very rosy economic outlook.

There is a large share of the labor forces still unemployed—still over 6 percent.

During the calendar year 1962, and the fiscal year 1963, we do not expect to achieve the reasonable level of unemployment—which has been established by the administration, as sort of an interim target—of 4 percent. We do not expect the economic conditions during the period covered by this budget to represent in any respect at all a boom or a runaway period of inflationary pressures.

We do not expect that the economic recovery will continue and it will be moving upward strongly. But under these circumstances, it would seem to us that it would be very risky indeed to plan for a large surplus in the administrative budget, much larger than is shown here. To do so would be to risk a depressing effect from the Federal budget on economic growth and recovery.

As I have indicated in this statement, we believe that there was some such depressing effect from the budget and fiscal policies which were followed in 1959–60. Obviously, the people who prepared and presented those policies did not expect that that would be the effect and they did not desire that that would be the effect, but looking back I think it was the effect. We are trying to learn from the experiences of that period and we are trying to do better this time. Consequently, it would seem to us to be a very firmly defensible point of view that the administrative budget surplus which is warranted as we look ahead to the fiscal year 1963, is a small one only and not a large one.

I recall, Senator Bush, that we had a brief exchange last year, a question and answer as to the attitude of the European bankers and other financial observers. I cannot claim to have learned a great deal during the meantime, but what little I have learned about their attitude, I think reinforces me in feeling as I did then that the main question which the European bankers and financial experts look at is not whether we have a large budget surplus or a small one, but whether we are following policies which can be expected to keep the U.S. economy in good condition—meaning moving toward high employment and maintaining reasonable price stability.

If we meet those standards, which I believe we are meeting with these plans, then I think that we can expect or we should expect the European observers to recognize the soundness of those plans and consider that the United States is doing as it should under the economic circumstances that we have at the time.

Chairman PATMAN. Senator Douglas is recognized.

Senator DOUGLAS. I want to commend you for the full statement you made here but I am glad that among other things you made a very minimum statement of the amounts that our budget contains in capital investments and that is in the $93 billion figure.

Am I correct in my impression, which I think is reinforced by Dr. Roy Moor's study, that most of the European countries do not include capital expenditures in their budgets, as a separate capital expenditures item?

Mr. BELL. That is my impression, too, Senator. I believe that there are differences among the European countries, but generally speaking they do draw this kind of a distinction.

Senator DOUGLAS. And is it not also true that if they were to follow the American practice and include capital expenditures in their ordinary budget, most of their budgets would be out of balance?

Mr. BELL. I assume that this is so, though I have made no study of it.

Senator DOUGLAS. Would you make a study on that subject?

Mr. BELL. We can, I believe, yes.

Senator DOUGLAS. I wish that you would. If that were known, might it not dispel some of the advice which the European bankers give to us about our budgetary practices?

Mr. BELL. Well, Senator, I suspect that most of the responsible observers, whether they are bankers or finance ministers or whoever they may be, are fairly sophisticated about our budget techniques.

Senator DOUGLAS. But the echo of those comments as they come back from across the Atlantic—those echoes are not sophisticated, because the comments of the European bankers are always quoted as saying or as indicating that we are following very bad budgetary practices in this country. So I think it would help on the echo, if you would clarify this point.

Mr. BELL. We will be glad to look at some of their budgets, sir.

(The Bureau of the Budget subsequently furnished the following information for the record:)

Bureau of the Budget staff was of some assistance to him, and therefore has been advised generally by Mr. Andrew H. Gantt of the preliminary results of a forthcoming study prepared by him for Harvard University. This study compares the Central Government budget results of England, France, and Western Germany with the United States. Adjusted to a basis comparable to the U.S. consolidated cash statement (Federal receipts from and payments to the public). the study shows that England ran deficits in 9 of the last 11 calendar years (1950 through 1960); France in every 1 of the last 10 calendar years (1951 through 1960); and Germany in 4 of the last 6 calendar years (1955 through 1960). In the 11 calendar years 1950 through 1960 inclusive, the United States ran surpluses in 5 years and deficits in 6 (see following table). Research on this project was made possible by the support of the National Committee on Government Finance of the Brookings Institution.

Central Government surpluses and/or deficits for recent years for four countries

Calendar year	England (millions of current £)	France (billions of current new francs)	Germany (millions of current DM)	United States (billions of current dollars)
1950	611	(1)	(1)	0.5
1951	−55	−2.40	(1)	1.2
1952	−464	−6.27	(1)	−.6
1953	−628	−7.94	(1)	−7.2
1954	−74	−7.56	(1)	−1.1
1955	−42	−8.32	2,221	−.7
1956	150	−11.72	1,331	5.5
1957	−175	−12.21	−2,926	1.2
1958	−101	−9.36	−1,755	−7.3
1959	−282	−5.48	−3,881	−8.0
1960	−453	−3.24	−200	3.5

[1] Figures not available at this time on the same basis.

NOTE.—The figures in this table differ from the usual "budget" deficit or surplus figures printed by these countries, which usually do not express adequately the surpluses or deficits for which their central governments are responsible. For instance, in the United States, the trust funds and other items are excluded from the budget figures. The figures in the table are on a basis analogous to the "Cash receipts from and payments to the public" of the United States, which encompass the entire operations of the central governments of these countries, including trust funds, government owned and sponsored enterprises, etc. It should be noted, however, that no attempt has been made to include exactly the same operations in each country. If the central government of the United Kingdom operates her radio stations and they run a deficit, this deficit is included above, even though the U.S. Government has nothing to do in an operational way with the radio stations here.

Senator DOUGLAS. Now, on the question of foreign trade and balances of payments, are the following facts approximately correct? That so far as commodities are concerned, we have an excess of exports over imports of approximately $4 billion.

Mr. BELL. I was carrying in my mind the figure of $5 billion, Senator Douglas.

Senator DOUGLAS. If you take so-called invisible items or other items, the deficit of balance of payments is between 3 and 5 billion, is that correct, approximately, within a billion dollars or so?

Mr. BELL. Well, the deficit, sir, they give it to us in annual figures and in quarterly rates. The quarterly rates have changed markedly over the last four quarters. During the early part of calendar year 1961, the quarterly rate was even, and there was no significant deficit, and in the last quarter there was quite a sharp deficit.

Senator DOUGLAS. You don't have the figures for the last quarter?

Mr. BELL. I believe Secretary Dillon said the other day that the quarterly rate in the last quarter for calendar year 1961 was up $4 or $5 billion, but this reflected a number of things.

Senator DOUGLAS. But, what I am trying to get at are the causes of the fact that although we have an excess of exports over imports of $4 or $5 billion, we have a deficit at a rate of from $3 to $5 billion on the balance of payments. Now, this deficit is caused, is it not, by foreign travel of American citizens or excess of foreign travel by American citizens over American travel by foreign citizens?

It is also caused by the cost of maintaining our troops abroad?

Mr. BELL. Yes, sir.

Senator DOUGLAS. Primarily in NATO?

Mr. BELL. That is right.

Senator DOUGLAS. And by the personal expenditures by troops and their dependents?

Mr. BELL. That is right.

Senator DOUGLAS. And foreign aid?

Mr. BELL. Yes, sir.

Senator DOUGLAS. And foreign investment?

Mr. BELL. That is correct.

Senator DOUGLAS. Now, do you think that our European allies are contributing their fair share to the defense of Europe and to foreign aid?

Mr. BELL. Well, "fair share," as I learned from you and other economists——

Senator DOUGLAS. Well, these are relative figures. Is this true, that last summer the force consisted of 17 NATO divisions, and there were 5 American divisions, 9 German divisions, and Great Britain and France contributed the magnificent total of 3 divisions between them?

Mr. BELL. I regret I do not carry those figures in my head.

Senator DOUGLAS. Is that approximately correct?

Mr. BELL. I thought there were more French and British divisions committed to NATO. My recollection was that their number was somewhat larger. Nevertheless, let me answer your question somewhat more directly. It has been the policy of this administration, which has been pursued vigorously and is now being pursued vigorously, to obtain a larger sharing by the NATO countries.

Senator DOUGLAS. Would you modify your language to "seek to obtain a larger share"? Now have you had much success in this?

Mr. BELL. We have had some success.

Senator DOUGLAS. How much success?

Mr. BELL. Well, the agreement that was reached about 6 weeks ago or 2 months ago between Secretary Gilpatric and the German Government——

Senator DOUGLAS. The Germans are going to add three more divisions. Is that not so?

Mr. BELL. Not only are they going to add three more divisions, but they are also going to purchase substantial quantities of military equipment from us.

Senator DOUGLAS. What success have you had with the French and the British?

Mr. BELL. At the last reading I knew about, Senator, we had less success with the French and the British.

Senator DOUGLAS. That is correct. And is it not true that according to the British press, they are actually thinking of diminishing their NATO forces and having what they term "a floating reserve," instead of a reserve in Western Europe?

Mr. BELL. I had not heard that, but you may very well be right.

Senator DOUGLAS. Now do you think that Germany, France, and Great Britain are contributing adequately in the field of foreign aid to underdeveloped countries?

Mr. BELL. This administration has been pressing them very strongly and continually to increase their contributions. We again would think there has been some progress in this direction, but not nearly enough.

Senator DOUGLAS. That is right. Now, then, do you not think that these foreign bankers, if they are really worried about the adverse balance of payments of the United States, can remedy this situation by seeing to it that their governments provide more adequately for the defense of Europe, and also bear a larger share of foreign aid?

Mr. BELL. This is an argument, Senator, which all of us make at the tops of our voices whenever we get a chance.

Senator DOUGLAS. Do you not think it is well to have this expressed not merely in the conference rooms, but publicly?

Mr. BELL. Yes. And, although perhaps not strongly enough, this point is made by the President in his budget message.

Senator DOUGLAS. And therefore when these international bankers gather together to wring their hands over the deficit of the United States, might it not be appropriate for you to say, both privately and publicly, "Physician, heal thyself"?

Mr. BELL. It would be appropriate, sir, and I believe that we have done so and will continue to do so. Perhaps this committee could contribute to the same objective.

Senator DOUGLAS. Senator Sparkman?

Senator SPARKMAN. The OECD was set up for the purpose of increasing help from these countries in the field of aid?

Mr. BELL. Yes, sir.

Senator SPARKMAN. Is that underway yet?

Mr. BELL. It is underway, Senator. It is a new organization, still weak in an administrative sense. They are just building their staff, and so on. And all of us hope to see them functioning soon.

It has, however, had a number of meetings, and we are trying to use it—the United States is trying to use it—as another forum for pressing the point of view which Senator Douglas has just outlined.

Senator SPARKMAN. In other words, a definite and positive approach has been taken to help out in that field?

Mr. BELL. Yes, sir. That is right.

Senator SPARKMAN. There is one item in your table 3 that I just cannot understand. I am going to ask you what it is—"Government-sponsored enterprise."

Mr. BELL. Yes, sir. This is an item which I had asked about, too. If I am correct—and I will ask my colleagues, here, to expand on this if necessary—this would include enterprises which are quasi-governmental in nature. The Farm Credit Administration is a good illustration; the Federal Deposit Insurance Corporation; the Federal home loan banks are other illustrations. These are organizations with many of which you are personally very familiar, Senator Sparkman.

Senator SPARKMAN. Does that represent administrative expenses that go into those organizations? I thought, as a matter of fact, those organizations paid for themselves and perhaps netted a profit to the Government.

Mr. BELL. They do, sir.

Senator SPARKMAN. And I notice there in fiscal 1961 you do have a profit.

Mr. BELL. As you recognize, this table is the cash consolidated statement.

Senator SPARKMAN. That is right. The payment would go into the Treasury and would not show, would it?

Mr. BELL. No, sir. This table is intended to reflect receipts from and payments to the public; so that when there is a net receipt of cash from the public during a year, this would show in this table. Or, as in this case, the payment of a small net amount by these enterprises as a whole. It is a very minor matter, so far as the total amount of money is concerned, as you can see from the table, and it will swing from year to year. In 1961, there was a small net receipt of cash. This has no bearing on whether they showed a profit or a loss during the year. That is a different set of accounts. This simply indicates whether there was a net receipt or payment of cash to or from the public.

Senator SPARKMAN. I realize it is a small item, but my curiosity got the better of me on that.

Mr. BELL. If you would like——

Senator SPARKMAN. No, I think I understand it quite well.

Now, in your statement, you referred to the public debt. You say:

> Far from being an increasing burden on our economy, it declined steadily from a total of about 130 percent of gross national product at the end of fiscal year 1946 to a little over half the gross national product at the present time.

I just want to make this comment: I think statements of that kind are sometimes a kind of palliative. I do not think we ought to resort to them. It seems to me there ought to be an effort made steadily to reduce the national debt and certainly to keep it from increasing, even though spread out over the population, on a capital basis, or even in relation to the gross national product, it may be improving. I think it would improve all of our feelings, when you get to the point of reducing it.

You do not intend anything to the contrary by that statement, do you?

Mr. BELL. I agree with you wholeheartedly, Mr. Sparkman, and so does the President, as I am sure you know.

Senator SPARKMAN. And, by the way, I think it shows itself up quite well in the amount of interest we pay each year; $9 billion and this steady increase year by year that becomes a big part of our budget.

Mr. BELL. The interest cost has been rising, of course, as interest rates have risen, primarily.

Senator SPARKMAN. As interest rates increase, and, of course, as the debt increases, too.

Mr. BELL. But the principal reason for the rising interest cost since the end of the war has been the increase in interest rates rather than the increase in total debt.

Senator SPARKMAN. That brings me to my next subject.

Mr. BELL. But to be sure my statement is clear, Senator, I wholly agree with you that our policy objective must be to minimize increases and if possible to decrease the public debt. Even though it is a declining burden in this special sense that economists would agree with, any debt is to be avoided if it can possibly be.

Senator SPARKMAN. Now with reference to interest rates, the prospective increase in interest rates, are you watching rather carefully the effect of the recent increase of interest on savings by commercial banks, to 4 percent?

Mr. BELL. Yes, sir; we are trying to. The Treasury and the Federal Reserve Board follow these matters most closely, and the Council of Economic Advisers have also been watching that with considerable interest.

Senator SPARKMAN. Have you taken note of the fact that savings and loan associations, particularly out in California, have gone up to 4.6 percent, compounded quarterly, I believe?

Mr. BELL. I had not heard that particular figure.

Senator SPARKMAN. You see them in ads in the New York Times.

Mr. BELL. I knew that the savings and loan associations felt that this change in the interest rates on time deposits in banks clearly increased the competitiveness of the banks in seeking savings funds.

Senator SPARKMAN. Well, I hope there is a healthy competition. I am quite certain that there is as a result of the ads. I mean judging from the ads that I have seen. But I am thinking of what the effect is going to be on interest on home mortgages. How can a savings and loan association pay 4.6 percent compounded quarterly and yet make loans at an interest rate of 6 percent? I just do not think they can do it. I think the inevitable result is going to be an increase in the interest rate in home mortgages, unless there is such competition, getting in sufficient savings that it will serve to hold it down; and as the interest rates go up on home mortgages, it seems to me that there is bound to be curtailed, the homebuilding rate, which, if it happened, will have a very serious effect on the economy, will it not?

Mr. BELL. This is the aspect of the effect of the increased rate on time deposits in banks which has concerned all of us the most, and which we are watching most closely. Thus far, it has been possible to hold the mortgage rate relatively stable, as you know.

Senator SPARKMAN. Yes, but this 4 percent increase is only a month old, is it not? Or 6 weeks?

Mr. BELL. A couple of months. Yes, sir. That is right. And I do not mean to say that the effects that you are speaking of are impossible or will not happen. Indeed, there is bound to be some tendency in the direction you speak of. We would hope that the basically good position of funds available for housing mortgage loans would continue to exert a downward pressure on housing interest rates, and we see no reason, in the short run, at least, why the housing interest rate cannot stay level.

Senator SPARKMAN. By the way, one statistic that I think it might be well for us to keep in mind, is the fact that savings and loan associations handle 44 percent of the home mortgages in the country. I saw that statistic just a few days ago.

I am bringing this up not because I predict these dire consequences, but simply to say that I think that some of these things bear most careful watching.

Mr. BELL. They certainly do, Senator. You are right.

Senator SPARKMAN. Now, there is just one other point about which I want to ask. I realize that the budget management of the business affairs of the Government can be used, and probably ought to be used, in order to help you stabilize conditions. But there is one thing that seems to me always to be true, and unfairly so, and that is the severity with which the smaller people that you mentioned a few minutes ago—the small business, housing, the farmers—I just want to express the hope that in management of Government affairs those groups will not be called upon to carry a disproportionate share.

I felt rather bad, for instance, after Congress last year had liberalized, with administration approval, the direct-loan program of veterans, for instance, veterans' housing, in order to take care of the backlog, the big backlog, that had accumulated, to see the pinch put on them, to see cut down the amount that could be loaned. And the same thing was true with small business, and the same thing was true with farm housing.

It just seems to me that elements such as these do bear a disproportionate share of any cutting down in order to help stabilize the economy.

I do not protest against it. I just hope that it certainly will not be too heavy.

Mr. BELL. I do not think that the President has had any intention, nor have we, that there should be a disproportionate effect on the kinds of spending that you speak of, Senator. As you will recall, after the end of the congressional session last fall, the President asked that there be a very close scrutiny given to all spending; not just these kinds but clear across the board; and that was done by the various Cabinet officers and agency heads.

Taking account of the actions following the President's request, there were still some very sharp increases, as I am sure you are aware, in the rate of lending of the Small Business Administration in this past period, as compared with the previous year, a sharp increase in lending under the farm programs that you speak of, as compared with the previous year. I do not think that the direct loans under the Veterans' Administration went up very much. Perhaps it stayed nearly level.

But these other programs, while they did not rise as much as they could have, did rise very sharply. We are, therefore, very conscious of the point you speak of, and this has always been in the President's mind as he has tried to make these difficult adjustments. And I am sure that neither he, nor we, have ever intended or have any intention of a disproportionate burden falling on this group of programs. If anything, we would all feel to the contrary.

These programs have been instituted by Government, by the Congress, to reflect a public interest in assisting groups of people who are especially disadvantaged in one way or another by the economic system; and to carry out the intent of Congress, obviously, therefore, calls for a strong use of these authorities. We are trying to do that.

I agree that in response to the President's instructions, these programs and others were not carried out with maximum all-out speed. It was felt that this was the correct policy under the circumstances. But there certainly was no intent of a disproportionate burden on this kind of activity.

Senator SPARKMAN. Thank you very much.

Thank you very much, Mr. Chairman.

Senator DOUGLAS. We will call on the lady member of the committee, now, Mrs. Griffiths.

Representative GRIFFITHS. Thank you, Mr. Chairman.

I would like to ask you, Mr. Bell: With reference to table 4, your estimated increases in receipts in 1962 and 1963 over 1961, how much of that is due to anticipated increases in rates, rather than increased economic activity?

Mr. BELL. Well, the great bulk of it, Mrs. Griffiths, is expected to flow from larger production and incomes in the economy and therefore increased receipts from existing tax rates.

However, there are significant changes in the old-age and survivors insurance tax rate, which go into effect, which are going into effect—some of them went into effect this January 1st and an additional change is scheduled for January 1, 1963—so that there would be a 1963 increase, I believe, of between $2 and $3 billion, which reflects increased rates.

Representative GRIFFITHS. And a possible postal rate? Is that reflected?

Mr. BELL. That would include the effects of the postal rate increase.

Representative GRIFFITHS. And a possible withholding of dividends, tax on dividends? Is that reflected in here?

Mr. BELL. Yes; although you will recall that the series of tax proposals which is now being considered by the Ways and Means Committee includes a substantial decrease which would result from the enactment of the investment tax credit, which would be approximately offset by the increases in withholding and various other kinds of loophole closing which have been recommended. Consequently, that particular combination of tax proposals is not expected to have any significant net effect.

The postal rate increase would have. There is no offset to that, so to speak, as shown here. And the old-age and survivors insurance tax rate increase certainly does show up here.

Representative GRIFFITHS. How do you reconcile—or is this necessary and relevant—concerning the sharp turnabout as compared to the surplus or deficit column on table 4, in which there obviously is no sharp turnabout?

Mr. BELL. I am not sure I follow your comment.

Representative GRIFFITHS I will point out first, the turnabout on fiscal policy will not be as sharp.

Mr. BELL. There is certainly a turnaround. The comment in my statement was meant to say that the turnaround was not as sharp a turnaround as in fiscal 1960.

The figures which we used to illustrate this point were the cash consolidated figures from table 3. Actually, they do not show on table 3, because that does not go back to the appropriate year. But on a cash consolidated basis, the swing was about $14 billion from 1959 to 1960, and it is only expected to be about $10 billion this time.

A similar point can be made if you look at table 4, where the receipts and expenditures in the national income accounts show a turnaround from 1959 to 1960 of about $7 billion, whereas the turnaround from 1962 to 1963 is about $5 billion.

So that I entirely agree that there is a turnaround, but it is not as sharp a one as took place in that previous period.

Representative GRIFFITHS. Thank you very much.

Thank you, Mr. Chairman.

Senator DOUGLAS. Senator Proxmire?

Senator PROXMIRE. I, too, want to compliment you on this budget. I think for many, many reasons it is a vast improvement. Just to compare the size, this I understand is the appendix, and this is the typical size of the previous budget, and this is the present one, which is in large print, readable, with lots of charts and graphs and tables.

Mr. BELL. And only a dollar, Senator.

Senator PROXMIRE. And only a dollar; yes.

That aspect is most encouraging: reading less and enjoying it more.

The logical organization, too, I think is an improvement.

Mr. BELL. Thank you very much, sir.

Senator PROXMIRE. And the inclusion and emphasis on the national income and product accounts. Then this special analysis, which we have for the first time, investment, operating, and other expenditures, the capital budget idea, Federal credit programs, Federal activities in public works, and other constructions that were not in before, Federal research and development programs, Federal aid to States and local governments, receipts from and payments to the public, which you present right here.

Mr. BELL. Some of these were available before if you applied to the Budget Bureau. We have now put them in print in the budget document itself.

Senator PROXMIRE. There's an entirely different reason why this budget is extraordinarily significant.

I am sure you are familiar with a recent column by Walter Lippmann who wrote:

> This 1963 budget is noteworthy because for the first time in our history it states that balancing of the budget—whether with a surplus, a deficit, or with neither—is a question of economic policy and of deliberate decision. It is not as so many regard it, a question of right and wrong.

And then he goes on to say:

> It used to be a heresy to ask whether a budget should or should not be balanced with a surplus or a deficit. In this generation to ask the question has become the new orthodoxy.
>
> Its [the new orthodoxy's] central theme is that in the business cycles of recession and recovery, the budget can be and should be used to make the down swing short and shallow and the recoveries long and noninflationary.

I think because this is a sharp departure from the past, because the economic profession seems to have accepted it overwhelmingly, and because the Congress has not accepted it with the same degree of unanimity—I, for instance, do not wholeheartedly accept it; Senator Sparkman has just given some interesting observations—will you give us your views?

Mr. BELL. I would be glad to comment on that, Senator.

I believe that the most important thing to say is that what is presented in this budget, what Mr. Lippmann is talking about, does not represent any sharp, radical new idea, insofar as those are concerned who have studied these matters in an academic or research capacity.

Dating back many years, the economists have now come to agree—economists of all descriptions and political faiths have now come to agree that an important aspect of budget policy must be the impact of the budget totals and the relationships between receipts and expenditures on the overall level of economic activity in the country.

Arthur Burns, who was President Eisenhower's first Chairman of the Council of Economic Advisers, would put this point, I am sure, in the identical terms that I would use or Walter Heller would use. This is not a matter any longer of dispute or controversy among economists who study these matters.

The particular judgment in any given year as to whether the budget should be in surplus or in deficit, and if so, the appropriate size of the surplus or deficit, is still a matter on which different individuals will and should inevitably reach different judgments.

But the conception that in planning a budget it is legitimate to consider planning a deficit, which is the basic conception that Mr. Lippmann was talking about—this is no longer a matter of issue among the research and academic economists who have studied these matters.

Furthermore, I would call your attention to the fact that for the last dozen years or more the Committee for Economic Development has recommended that the Federal Government, in preparing its budgets, should follow what they used to call a stabilizing budget policy; which means the same thing as what we are now talking about. That is, that the level of the budget and the relationship between receipts and expenditures should be planned to contribute to stability of employment and incomes over the business cycle.

The Committee for Economic Development, the CED, has just recently, last week, in fact, quite fortuitously as far as timing is concerned, issued a new policy statement, called "Fiscal and Monetary Policy for High Employment." They do not use, in this new statement, the same term that they used before, but their basic policy prescription is the same. It has been extended and understood in more detail than it was some years ago. And whereas then they recommended that the figures which were most useful in determining these policy decisions were the figures in the cash consolidated statement, they now suggest that the most relevant single set of figures are the Federal receipts and expenditures calculated in national income account terms.

This, however, does not alter their commitment to this basic policy notion that it is desirable for the Government to exercise judgment as to whether a deficit or a surplus is the relevant policy in a given set of economic circumstances.

Thus far, all I have said is that the authorities, the academic and research authorities, agree. Now, let me say a few words to lay out for you—I am sure this is no news; you could do it as well as I could—the basic logic, why they agree, what it is that they are talking about.

What they are saying is that the phenomenon of swings in the economy, of booms and recessions, is in part the result of variations in the demand from private sources for various kinds of goods and services. These variations in the private demand may stem from a number of different causes. They are always complicated and interrelated. They relate to inventory cycles. They relate to changes in consumer tastes, changes in the types of products that are available over a period of time, the basic changes in labor force and technology and so on.

The private economy moves not smoothly and evenly and continuously, but with ups and downs.

This is probably a characteristic of a free economy like ours. It would probably be very damaging for us to try to institute sufficiently severe restrictions and controls on private activity as to achieve a complete ironing out and leveling out of the rates of change of private activity so as to prevent business cycles altogether. It is probably much more to our advantage to accept the necessary fact of some degree of fluctuation, because it is related to the degree, the very high degree, of private initiative, and the centralization of economic responsibility throughout the economy, which makes our system as dynamic and energetic as it is.

Now, if there are these necessary and inevitable and desirable—in the sense I have just described it—swings in private activity, what should be the relevant Federal policy? Should it be that we should fix our budgets to adapt our expenditure levels simply to whatever is earned, whatever comes in, from a given tax structure, whatever we receive? That would mean that when the private economy goes into a downturn, incomes drop, and Federal receipts drop, then we should, if this were our policy, restrict our expenditures to the level of receipts that we happen to be anticipating during the coming period.

If we were to do that, we could strive toward a balanced budget every year. Most of us think that it would be impossible to obtain it, and that such a policy guide, if we tried to follow it, would be self-defeating; because as we try to cut down our expenditures to match an anticipated drop in revenues, that decline in Federal expenditures itself would have further depressing effects on the economy, which in turn would result in lower incomes and lower receipts, and we would be chasing a will-o'-the-wisp in trying to achieve actual balance in a recession year.

Furthermore, to attempt to do so would obviously pose some very severe choices. This budget is well over half a defense budget. It is not possible to trim expenditures in the short run very substantially without cutting defense. Most of us would argue, I think, that the basic level of our defense expenses——

Senator PROXMIRE. Raise taxes?

Mr. BELL. Well, it doesn't do you any good to raise taxes in a depression year very sharply.

Senator PROXMIRE. I am talking about this year.

Mr. BELL. The present year? Excuse me. I was talking in general terms, an we can come back and talk about this particular budget policy if you like in a minute.

Senator PROXMIRE. I did not want to interrupt, but you had talked about the big defense budget we have this year, which this year is more than half of our total budget. You say it is difficult to cut. And I say in this year if you wanted to follow the policy of assuring a balanced budget, you could increase taxes.

Mr. BELL. I quite agree. I was not trying in this specific discussion to defend the particular budget policy for this year. I was trying to explain why most economists agree, most students of the subject agree, that the Federal Government should follow a policy of determining whether a given set of economic circumstances can best be met by planning a budget surplus or a budget deficit.

I was saying that if we tried to follow a policy of balancing the budget every year, come what may, this would mean that in periods of recession the Federal budget would not only contribute to worsening the economic situation, but we would also, in the process, have to cut very deeply into important national purposes, such as defense.

Now, this is, therefore, in summary, to say that to attempt to balance the budget every year, recession or prosperity, would be a futile policy and a policy which would contribute to making the swings of the business cycle more extreme rather than less.

The contrary point of view, which we do espouse, and which Mr. Lippmann has set forth there, is that in a time when the private economy is temporarily in recession, this is a time in which it is legitimate and proper for the Federal Government, to some extent and to some degree—the extent and degree being certainly matters of judgment and debate during the year in question, but to some extent and to some degree—to contribute to stabilizing the economy, to holding up levels of income and production, to stimulating the private economy, helping to turn it around and urge it back toward recovery and economic growth; and that this is one of the elements which should be taken into consideration by the President and by the Congress in determining the budget policy in any given year.

Senator PROXMIRE. My time is up, but I just wanted to say when my chance comes again I want to ask you about two, I think, very big and powerful assumptions that are made, that underlie this budgeting for economic policy approach.

One assumption is that you can forecast with a fairly good degree of accuracy, and secondly, that there will not be the kind of pressure constantly on the Budget Director and on the President year after year that there is this year to make optimistic assumptions on the economy and program for a bare budget balance which will usually work out to be a deficit and often a big one.

Even in a year of expansion and prosperity, you have a bare budget balance if everything works out, and if everything doesn't work out quite so well, you have a deficit.

I know this is an enormously big question to discuss, but I want to come back to it a little later on.

Senator DOUGLAS. Senator Bush?

Senator BUSH. I have no questions at the moment.

Senator DOUGLAS. Mr. Bell, I would like to ask this question, to start off with: Am I correct in assuming that the increase in actual expenditures for fiscal 1962, as compared with fiscal 1961, was caused first by the Berlin crisis and the need to have greater national defense, and also by the demands of the recession so far as unemployment compensation and other things are concerned? The increase, as I remember, was from $81 to $89 billion, roughly.

Mr. BELL. Yes, sir. The increase was from $81½ billion to a little over $89 billion; of which close to $4 billion—that total increase is 7.6—of which 3.7 was in national defense, almost exactly half.

Senator DOUGLAS. The projected increase for fiscal 1963 over fiscal 1962 is a little over $3 billion?

Mr. BELL. $3.4 billion; yes, sir.

Senator DOUGLAS. And this is caused by what?

Mr. BELL. Well, three-quarters of it is national defense, international affairs, and space, of which a good chunk is the increase in space technology.

The bulk of the remainder of the increase between 1962 and 1963 is in the cost of interest on the public debt.

There is no substantial total increase between 1962 and 1963 in the anticipated outlays for what is grouped here as domestic civil functions; but within this total, this virtually stable total, there are considerable changes. There is expected to be a drop of about $500 million in the outlays for agriculture. There is expected to be a drop of about $600 million in the postal deficit.

Senator DOUGLAS. If the postal bill is passed.

Mr. BELL. Well, as it was passed by the House a couple of days ago, which looks very encouraging.

Senator DOUGLAS. It will still have some difficulties in the Senate, I am sorry to say.

Mr. BELL. I am sorry to hear that.

Senator DOUGLAS. Now may I ask this question: Is it true that while the total Federal expenditures have increased from year to year, for the last 10 years they have remained approximately constant as a percentage of gross national product?

Mr. BELL. Yes, sir. That is indeed true.

Senator DOUGLAS. At about between 16 and 17 percent of the gross national product?

Mr. BELL. That is right. If you would like me to provide it for the record, we have a table which shows this percentage calculated back to 1938.

Senator DOUGLAS. We will print that in the record at this point.

(Table referred to follows:)

Budget expenditures and gross national product, fiscal years 1938–63

[In billions of dollars[

Fiscal year	Gross national product	Budget expenditures	Budget expenditures as percent of GNP	Fiscal year	Gross national product	Budget expenditures	Budget expenditures as percent of GNP
1938	88.0	6.8	7.7	1952	338.8	65.3	19.3
1939	88.2	8.8	10.0	1953	359.7	74.1	20.6
1940	95.7	9.1	9.5	1954	362.0	67.5	18.6
1941	110.5	13.3	12.0	1955	377.0	64.4	17.1
1942	140.5	34.0	24.2	1956	408.5	66.2	16.2
1943	178.4	79.4	44.5	1957	433.0	69.0	15.9
1944	202.8	95.0	46.8	1958	440.2	71.4	16.2
1945	218.3	98.3	45.0	1959	466.7	80.3	17.2
1946	202.8	60.3	29.7	1960	494.8	76.5	15.5
1947	223.3	38.9	17.4	1961	506.6	81.5	16.1
1948	246.6	33.0	13.4	1962 estimate	545.0	89.1	16.3
1949	261.6	39.5	15.1		580.0		15.7
1950	263.8	39.5	15.0	1963 estimate	to	92.5	to
1951	310.8	44.0	14.2		590.0		15.9

Mr. BELL. But your point is quite correct. Since 1955, which is following the effects of the Korean war, the ratio of budget expenditures to gross national product, has varied between 17.2 and 15.5 percent. Those were the extremes in that whole 9-year period.

Senator SPARKMAN. May we have those figures again, the two extremes?

Mr. BELL. Yes. The two extremes in the years 1955 through 1963, inclusive: The variation has been that the high year was 1959, when it was 17.2 percent, when budget expenditures were 17.2 percent of gross national product. The low year was 1960, when it was 15.5 percent. And each of the other years was in between those levels. The anticipation for 1963 is about 15.8.

Senator BUSH. That is set forth on page 11 of the budget message that you were just looking at, is it not? Budget expenditures as a percentage of gross national product?

Mr. BELL. Yes, sir; that chart shows exactly the same thing. That is right.

Senator DOUGLAS. Now, may I ask some questions about the space program? If you could isolate the projected expenditures to divide the man-to-the-moon from the other items, would you be able to estimate what the estimated expense is of putting a man on the moon?

Mr. BELL. May I answer that question, sir, in two pieces? I am not trying to dodge it, but I would like to say that in one sense the phrase "putting a man on the moon" is misleading. That is symbolic of what we want to be able to do. What we want to be able to do is to handle ourselves, to make use of the space environment, to be able to put men out there, or instruments, at least as capably as any other country is able to do. And the notion of putting a man or a group of men on the moon is simply symbolic of mastery of space exploration and travel.

Senator DOUGLAS. Words are symbols, anyway, Mr. Bell, as you well know, so if you will permit me to use symbols: What is the estimated cost of the man-on-the-moon project, or the moon project, or the earth satellite project?

Senator SPARKMAN. Space inspiration?

Mr. BELL. We have divided the expenditures as shown in the budget—page 72 is the table I am looking at—between manned space flight, unmanned investigations in space, meteorology, and communications, and other research technology and supporting operations. This will show you the very high proportion, close to half, of the total outlays for 1963.

Senator DOUGLAS. Two and a quarter billions for manned space flight; is that right?

Mr. BELL. Yes; that is right.

Senator DOUGLAS. But that is simply for 1963. You are not going to put Mr. X on the moon in 1963. You hope to put him on in a certain year?

Mr. BELL. Yes, before the end of the decade.

Senator DOUGLAS. Projecting over a period of time, what will be the total cost of putting, first, instruments, I suppose, and then a man, on the moon? Is this classified?

Mr. BELL. No. I was going to go on to say that these are the figures which show in the budget for the particular years that are there.

Incidentally, we expect to put instruments on the moon today, I believe, do we not? That is one of the shots that is supposed to go up from Canaveral. I do not know whether it has actually gone, but that is the plan.

Senator SPARKMAN. It will take 2 days to get them there.

Mr. BELL. Yes. The firing takes place today.

Senator DOUGLAS. Have you an estimate of how much you think it will cost to get him there?

Mr. BELL. The last figures I recall are some months ago, and as with many other programs, the figures in this program change rapidly. At that time, if I am not mistaken, the estimated cost over a period of time, 6 to 8 years, was in the neighborhood of $20 billion.

Senator DOUGLAS. $20 billion?

Mr. BELL. I would be glad to check that for you.

Senator DOUGLAS. If it would be possible to furnish that for the record, I think that would be very important.

A great many people, you know, and I am one of them, who do not know very much about this program, wonder whether it is worth it. It may be that if we know more about it, we would think it was worth it. Some of us have doubts when we think what $20 billion could do in the form of schools, in the form of health, and in the form of education. If it is purely a stunt to get there before someone else, that raises a question whether we should spend as much money as that for such a project.

There may be military consequences, but certain physicists have said you can bombard any place on the earth more effectively from the earth than you can from some point in the heavens, where the margin of error is naturally greater.

Now, I do not know. But, the public has never really had a chance to consider this space program, and I suppose there are reasons why it cannot, but we are apparently committed to it.

I do not think there has been any thorough discussion on the floors of Congress on this matter, or really in the press. This is something that has just been considered and acted on quietly by the administration authorities.

Mr. BELL. May I say something about that, Senator?

First, as to the degree of public discussion, there is no security. There are no top-secret stamps of any kind on any of the space activities of the National Aeronautics and Space Administration.

Senator DOUGLAS. That is good.

Mr. BELL. Everything they do is an open book.

Senator DOUGLAS. You agree with me that there has not been much public discussion of the costs and of alternate possibilities and so forth, and relative advantages to be gained?

Mr. BELL. No, sir, I do not think I can agree with that. My impression—of course, I have necessarily been exposed to it more than most people.

Senator DOUGLAS. You have been on the inside, of course.

Mr. BELL. The President made a relatively significant and major statement and made major recommendations on this in his personal appearance before the Congress—wasn't it last May? It was on a nationwide TV hookup, and he described this and made his recommendation, and I cannot quote his words, but I was present and heard him say that he thought the Congress should face this issue and decide whether they agreed with him, or not, that we should undertake this very large and very costly effort to gain the capability of moving about in space.

Senator DOUGLAS. It may well be that we in Congress have been delinquent—that is quite possible—in not probing this further. And I am not trying to shift any blame on anyone. But it is certainly my impression—and I read something like 20 journals in this country—that there has not been a great deal of public weighing of alternatives.

I conducted a poll of the American Astronomical Society, and I found that about a third of the astronomers did not believe that a man landing on the moon was desirable; and I had thought that this group of people would be prejudiced in favor of this.

Mr. BELL. Does that mean that two-thirds of them were in favor?

Senator DOUGLAS. Some of the astronomers came to me and asked me not to make the results of the poll public. This was on the ground they did not think astronomers were competent to pass judgment. Now, if astronomers are not competent to pass judgment on it, who is?

Mr. BELL. You and I are. We have to be, sir. We are stewards of the public funds.

Senator DOUGLAS. As I say, I have the feeling that we in Congress have not been sufficiently alert to this matter. I feel a sense of personal guilt about it.

Mr. BELL. May I say a word or two about the merits, Senator?

Senator DOUGLAS. Yes.

Mr. BELL. I think the basic notion, here, about which there has been some misunderstanding, is that there is no stunt involved. This is not embarked on by the Government of the United States as a stunt. This is embarked on because it is the opinion of the responsible officers in the executive branch, headed by the President, endorsed by the Congress, after full hearings and debate——

Senator DOUGLAS. After very cursory debate—after very cursory debate.

Mr. BELL. Nevertheless endorsed by the Congress, that the United States should embark on this very costly and very major effort to achieve a capability of moving about in space, of being able to explore space, of using it as an environment, of being able to use it to the same extent that any other country can do so.

In this sense, it is, so far as I can see, legitimate to couple it with national defense and international activities in the broad setting of a national security program.

The military significance of space activities is, of course, much debated, as you have indicated. The Defense Department does not debate it. They will tell you strongly, and indeed, passionately, that there are very significant and very dangerous potential military meanings to the capabilities that the Russians have already acquired, and which we are trying to acquire, in space; and that consequently the Department of Defense has strongly supported the point of view that I have just summarized.

But I do not mean to rely on that. I think it is up to the Members of Congress, as it is certainly up to the executive branch, to decide whether this is a wise expenditure of national funds. The President certainly came down clearly in his recommendation of last May, and the Congress supported him in the sense of passing the legislation.

Senator DOUGLAS. We really signed a blank check. Full details are known only to the members of the Space Committee; not really shared with the Congress. I think that is correct to say.

Mr. BELL. They are not classified in any way; so that I am sure that any Member of the Congress who wants to know about it can learn as much as he wishes to.

Senator DOUGLAS. Would you prepare for the record, then, an estimate of what the man in the moon and instrument venture will cost in addition to the space program? That is, granted that you have an ordinary space program, how much will the addition of putting instruments on the moon or a man on the moon gain in added costs?

We want to get at the incremental costs.

Mr. BELL. We will try to do exactly what you say, Senator. My guess is that most scientists would say that instruments on the moon would be a part of anybody's space program.

I think the argument, as I understand it, when this administration came into office a year ago, revolved around the question of how important it was to put men out into space, to do various things, among which was landing one or more on the moon and bringing them back. The scientific community was, and I think still is, divided on this matter. A number of scientists have said that it is adequate, for the national interest, to have a space program which is built around the use of instruments only, sending all sorts of instruments out, landing them on the moon, if that will yield valuable and important information, but that it is not necessary to put a man out there.

Senator DOUGLAS. As I say, a third of the astronomers of the country specifically took this position in a questionnaire. We got the results, incidentally, too late for the congressional committee.

Mr. BELL. I suspect, therefore, that the most useful figure from your point of view, and to respond to the interest that you have, is to try to distinguish those parts of the expenditures which are made necessary because we are trying to put men out in space.

We will try to do that, Senator.

(The following statement was subsequently supplied for the record:)

It is very hard to establish the separate cost of manned lunar flight since many elements in our preparation for manned flight to the moon would undoubtedly be included in the space program for other purposes. It is currently estimated by the National Aeronautics and Space Administration that the cost of the manned space flight program through the first landing on the moon will be about $14 billion. This amount includes the development and operating costs of the launch vehicles and spacecraft required for all manned space flight between the Mercury program and the first lunar landing, even though many of the near-earth flight experiments would be desirable without adopting the goal of manned lunar landing. Examples are manned rendezvous in earth orbit and maneuverable reentry experiments.

In addition, the development of some large launch vehicles included in the total cost of manned flight programs would be needed for advanced unmanned lunar and planetary experiments. An example is the Saturn launch vehicle which would be required for large-scale robot exploration of the moon or probes of the surfaces of the near planets.

Senator SPARKMAN. Mr. Chairman, I will have to go. I dislike very much to find myself in disagreement with my friend from Illinois, but I am rather of the opinion that the American public has been greatly concerned with this matter of getting a man into space.

Don't you think so?

Mr. BELL. It seemed to me, sir, that there is a very strong feeling.

Senator SPARKMAN. I think that was the reason Congress acted so quickly on the President's recommendation. Congress usually reflects pretty well what the feeling of the people is.

I think you have been most helpful to us this morning. I appreciate you being here.

And I am going to have to leave, Mr. Chairman.

Thank you.

I just happened to think of this as I turned away. It may not be entirely relevant. But I wonder if perhaps the same budgetary question might not have been raised when the Congress raised funds to help Samuel B. Morse develop the telegraph.

Senator DOUGLAS. Well, the amounts involved were a little different.

Senator SPARKMAN. But the principle was just the same.

Senator DOUGLAS. I am sufficiently old fashioned to think that a matter of $20 billion is a matter of some moment.

Senator BUSH. Even now?

Senator DOUGLAS. Even now.

Senator PROXMIRE. I would like to carry on the questioning I engaged in before, but first let me say I wholly share Senator Douglas' concern about space expenditures, for two reasons.

In the first place, I think we should have a clear, comprehensive justification of this expenditure in terms of the national defense or any collateral health or research assistance which this program may give which would be justified.

One of the things Mr. Moore pointed out in his excellent study was that we should get some indication of returns in comparison with the costs of programs, so that we can assess whether or not to go ahead.

There is another point I wanted to make, and this is even more serious than the dollar cost. That is that a newspaper article indicated recently that NASA will require 13,000 scientists and engineers for their program alone. They will pull these valuable experts out of the economy at a time when we already suffer a serious shortage.

This is such a grave matter, this shortage of supply, that the President in his recent press conference put special emphasis on his deep concern over the shortage of engineers in science. It has been said that this would certainly tend to impede other scientific and engineering activity, and it might very well cripple our graduate science and engineering educational program, as we take people from the universities who are teaching scientists and engineers and pull them into NASA.

So that I think that this is an extremely serious aspect of this investment, too.

Mr. BELL. Yes, it is.

Senator PROXMIRE. And we should have really a full-scale debate on it.

Mr. BELL. The devotion of scientific talent to this program will be very large indeed, as Senator Proxime has said. If you talk to Jim Webb about this, you will find him extremely sensitive to this point and very much interested in making arrangements by which the net effect of the space program will be to augment our supply of scientists as well as of scientific information and technological growth, and not simply to drain scientists from other activities.

Senator PROXMIRE. We could very easily damage rather than assist our national defense effort, because, as the President indicated, one of the great Soviet advantages is that they are graduating so many more competent engineers and scientists than we are. And this could aggravate the situation seriously.

Now I would like to get back to my questioning on the budget.

In your statement, it seems to me that the assumptions are somewhat rosy. Considering the fact that World War II and the Korean war may well have been a part of the reason for pent-up demand in purchasing power and giving a push in previous expansions, this current boom may not have the same zing. Also, as Senator Bush pointed out, there is a situation now in steel which may have accounted for the improvement in the fourth quarter of 1961 and the current period. If there is, this could easily diminish in the second and third quarter.

What I am getting at is that you are expecting and predicting the biggest increase in gross national product that we have ever had in peacetime.

Is that not correct? In terms of absolute dollars?

Mr. BELL. I think that is correct in absolute terms. As to GNP growth, of course, everything is bigger in absolute terms than it ever was before. And the percentage growth, as you have indicated, that is anticipated here, is certainly not out of line at all with previous experience. Indeed, I think it is about the same as in 1958–59 and 1954–55.

Senator PROXMIRE. But as I say, that was closer to a period when there was a pent-up war demand.

Mr. BELL. Well, if your basic question is whether these are reasonable anticipations, of course, anyone can differ about it. The specialists in the executive branch, in the Treasury and the Council of Economic Advisers and their staff, the Federal Reserve Board staff, all regard these as very reasonable anticipations, looking ahead through this calendar year and on to the next one.

This is not to say this is a flat prediction. We obviously in this business have to base our budget figures on reasonable assumptions, and we have to consider what will happen if those assumptions do not turn out to be realized.

I think this is perhaps the most significant point that you are aiming toward, because if we do not have a GNP of $570 billion in calendar 1962, and we do not have $93 billion in receipts, then won't the budget be unbalanced? If the GNP this year is substantially less than $570 billion, we would not get $93 billion, and the budget would be unbalanced.

But the key question is whether that would not, under those circumstances, be desirable rather than undesirable?

Senator PROXMIRE. Very good. That is the important question; because it seems to me there may be a tendency, with this new economic policy, to project a surplus only if things worked out extremely well; and the surplus is so small that it does nothing to retire the debt. And you are projecting a situation in which, if you follow this policy, the logic of it would lead to continual deficits and continually higher national debt.

Mr. BELL. No, I certainly do not feel that that is what we are projecting here. The $570 billion figure is an estimate arrived at independently, not to achieve a particular figure, of what is a reasonable expectation if the economic recovery continues as it is now going.

This is in a perfectly legitimate sense a most reasonable anticipation.

Senator PROXMIRE. I think you are right, and you corrected me properly. But then let me put my question a little differently.

What you are assuming—and your predictions may be completely sound—is that we are going to have a continued excellent expansion.

Mr. BELL. Right.

Senator PROXMIRE. A continued excellent expansion, even. Even, still, with this fine expansion, we barely balance the budget. So my argument is that in this period, when we are expanding, and when we are moving into a greatly improved economic situation, shouldn't this be exactly the time, in peacetime, that we should run a surplus?

Mr. BELL. The basic reason why we differ on this is that while we expect a very steady and very encouraging, a very good, economic recovery and growth during this present year, it is not expected to be a period of high boom. We expect to have a continuation of substantial unemployment. It is 6 percent now. It should be diminishing through the year. But we do not expect to reach 4-percent unemployment until the middle of calendar year 1963.

Under those circumstances, this is not the kind of period under which it would make sense to run a sizable surplus and make significant payments toward retiring the national debt.

If calendar 1963, when we get to it, some months from now, toward the end of this year, when we have a better look at what the calendar year may turn out to be, looks to be a year in which economic conditions continue to move strongly forward, and it looks as though we can reach and pass the 4-percent unemployment rate, that would be the kind of a year in which the kind of fiscal policy I have been describing would call for a sizable surplus, as a contribution to preventing the economy from going on into an inflationary boom. And we would be able then to make a significant payment on the public debt.

Senator PROXMIRE. But when you look at our historical experience with employment and unemployment, one of the figures that struck me recently is that during the relatively prosperous period, from 1900 to 1913 and from 1919 to 1930, America averaged unemployment between 6 and 7 percent, as I understand it.

I feel very strongly that we should do all we can to reduce unemployment. I feel that we should use other means as well as fiscal means, however, and I think we are placing far too big a reliance on an unbalanced budget to achieve a reduction in unemployment.

Now, if, during this period, after the effect of the wars has diminished very greatly, the economic tendency, other things being equal, would be to have unemployment rates of 7 to 8 percent, and if we rely so exclusively on budget deficits, as I think we have been doing, we could easily dig ourselves into a very deep and heavy and burdensome national debt, without ever achieving this goal of 4 percent, on the assumptions that are made in this budget.

Mr. BELL. I am one of the loudest spokesmen within the administration for the point that you have just expressed, that it would be a mistake to rely too heavily on fiscal policy; that it should be regarded simply as one among many policy measures which are available to the Government to contribute to reducing unemployment and to encourage more rapid economic growth.

From many points of view, it is certainly not the most valuable or most important of the economic measures that are available to us. It does not discriminate among parts of the country. It does not contribute significantly to some places in the country—not the backward areas, but the depressed areas.

Senator DOUGLAS. The less developed areas.

Mr. BELL. Less developed? All right. Areas of exceptionally high unemployment, southern Illinois, West Virginia, and so on. Those areas obviously do need a series of economic measures of much more precisely tailored nature.

Some of those are underway, as you all well know, in the Area Redevelopment Administration. Others the President has pending before the Congress such as the training and retraining bill, which is a most important measure, in my judgment, which would be aimed at reducing the degree of chronic or long continuing unemployment and permitting also a much easier transition into the labor force by younger people, which is another of our current and continuing economic problems.

So that I strongly agree with you that fiscal policy is only one among a number of different kinds of tools which the Government, the President, and the Congress have available to try to affect the economic circumstances.

But this is not to say that it is not an important tool. I strongly feel that it is an important one.

So that the notions we have expressed here I think can have a considerable impact in contributing to high employment and continuing high employment over time.

Senator BUSH. Mr. Chairman, I certainly associate myself with the querulous point of view of the Senator from Wisconsin.

Senator DOUGLAS. The Senator from Wisconsin was not querulous.

Senator BUSH. Well, I meant one based on "query." He will not misunderstand me.

Senator DOUGLAS. But we want the record to be clear on this.

Senator BUSH. It will be clear if you will just be quiet for a minute.

Senator DOUGLAS. If the Senator will use words accurately, I will be very glad to be quiet.

Senator BUSH. I still stand on my language.

Mr. Chairman, I associate myself with the thinking of the gentleman from Wisconsin on this point, and the questions which he has raised.

I previously raised a similar one on the first round, here; and the point that seems to me to be involved is that there seems to be too great a tendency to depend too much on Government spending to correct all of our difficulties, and particularly the question of unemployment, which I agree is a grievous and important one, and I am very glad to see it improving; and I hope that the gentleman's forecast will be correct, and it will be greatly reduced this year.

But in support of my view on this, I recall in 1932 that when President Roosevelt came in there was an unemployment factor then of about 9 million unemployed, which was a much higher percentage.

Mr. BELL. About 25 percent, I believe.

Senator BUSH. Well, I would have thought it was less than that, but you may be correct.

But whatever the percentage was, it was a very high one. And at the end of 7 years, September 1939, when the war broke out, this figure still remained at 9 million unemployed. It had varied. But that is where it was when the war broke out, although during those years all kinds of efforts were made to increase Government spending, and all kinds of increased Government spending did take place.

And I did feel that there couldn't be too great emphasis placed on Government spending; that this is the only thing that can correct the unemployment factor.

Mr. BELL. I doubt if there is a difference between us, Senator.

Senator BUSH. There has been great emphasis laid on this all the time by Dr. Heller and other representatives of the administration.

Mr. BELL. One of the things that I have tried to emphasize in talking about this budget—and I would be delighted to do it right now—is the extent to which it includes measures and proposals which are intended to stimulate the private economy.

The investment tax credit, which is before the Ways and Means Committee, is an illustration of one kind of thing. The very heavy expenditures for scientific research and development, which will contribute to the possibilities for new products and new methods, and so on. The Federal Government is now financing about two-thirds of the scientific research and development of the Nation.

And incidentally, Senator Douglas, Mr. Webb, when you give him a chance, will make a very eloquent statement as to the scientific gains which we can expect to flow from the effort to achieve manned space flight. That is only one part, of course, of the Federal Government's expenditures on research and development.

The expenditures, the proposed expenditures, on education, of many kinds, and at many levels, are clearly intended to and will clearly have the effect of increasing the capability of the economy as a whole, the private economy, to move forward and to achieve greater economic growth and progress.

Senator BUSH. Do you feel that you have had a satisfactory reaction from the private sector, as you call it, on this question of the 8-percent tax credit? Has that been a satisfactory reaction?

Mr. BELL. Their first reaction was quite negative; but as more and more companies began to calculate what this would mean to them personally, to their own companies, the reaction has become increasingly strongly favorable, as I understand it. This is obviously not the field that I follow most closely. Therefore, at the present stage, I believe the sentiment in the business world is quite favorable toward it.

Senator BUSH. You believe it is favorable?

Mr. BELL. That is my impression. Do you have a different impression, sir?

Senator BUSH. Well, I have the impression that they are very lukewarm about it, and that they would much prefer to have larger freedom in establishing depreciation policies, and this would be a much more stimulating policy to plant expansion, which would increase employment, and so forth.

Mr. BELL. These are two devices aimed at the same objective, and I assume that they strongly support the objective, which is to encourage higher rates of investment and modernization of equipment.

Senator BUSH. I agree that they strongly support it. But as far as I have been able to ascertain, they have been unenthusiastic about that approach to it and wish the administration had taken the other approach. This would have been, they say, a much greater stimulant to plant expansion and the creation of new job opportunities.

Mr. BELL. You may wish to ask Secretary Dillon on Tuesday, but it is from him that I get the impression that more and more people in the business community feel that the investment tax credit is a pretty good approach.

Senator BUSH. Well, I am glad to feel that there is that feeling about it. I have not sensed that, myself. I think they have become resigned to the fact that that is about what they are going to get.

I thank my colleague for his patience and understanding.

Mr. BELL. May I say to Senator Bush that my colleague, Dr. Turner, here, has turned up, in the appendix to the Economic Report of the President, the figures on unemployment as a percent of the civilian labor force during the 1930's.

The figure in 1932 was 23.6 percent, and the figure in 1940 was 15 percent.

Senator BUSH. 1939?

Mr. BELL. 1939 was 17 percent.

Senator BUSH. It came down percentagewise?

Mr. BELL. It came down, but the rate was still very high. The total unemployment in absolute terms in 1932 was 12 million, and in 1939 was 9½ million.

Senator BUSH. I am not going to pursue my records to find out where I got my figures. It is a question of date. It may have been 1933. What is the figure in 1933, as long as you have it?

Mr. BELL. The absolute figure in 1933 was higher, was 12.8 million, and the percentage was 24.9. Those figures were the highest.

Senator BUSH. And the 1932 figure was 12 million?

Mr. BELL. 12,060,000, and 23.6 percent.

Senator BUSH. And the 1939 figure?

Mr. BELL. 9,480,000 people; 17.2 percent of the civilian labor force.

Senator BUSH. I stand corrected on that variance in my earlier figure of 9 million. But I do not think it changes very much the point that I am trying to make, which was that despite the 7-year period of intense efforts to cure by Government spending this very serious unemployment problem, it did not produce very effective results.

Senator DOUGLAS. It reduced it by approximately 3½ million.

Senator PROXMIRE. If the Senator will yield, I am inclined to feel as you know, that spending is not the best way to do it. There were many, many other things the New Deal did. We had a very expansionary monetary policy. We had, of course, the Wage-Hour Act, which was not effective until after 1938, but there was a tendency for the hours to drop. There was the Wagner Act, which had its effect on reducing the hours of labor, and so forth.

There were many, many other factors than Government spending that helped to hammer employment down; plus the fact that we were at the bottom of a cycle in 1933, and all of our experience, all American economic history, suggested that we should expect to tend to go up.

Mr. BELL. It was Senator Bush who raised that point, I think.

Senator PROXMIRE. You say:

> The very recent statement of the Committee for Economic Development, "Fiscal and Monetary Policy for High Employment," has, as I am sure you all know, recommended the national income basis as the most useful single way to express budget totals for the purpose of evaluating fiscal policy.

I agree wholeheartedly. Would you mind taking that up for the record and explaining what this is and why it is more useful?

Mr. BELL. Yes.

First of all, the administrative budget is regarded by most economists as inefficient for purposes of economic analysis, because it includes only a part of the Federal transactions which affect the economy. It omits entirely the trust fund expenditures. Consequently, the first major modification, which was made by economists some years ago, was to move, in most of their thinking, from the administrative budget to the consolidated cash statement, which includes both budget transactions and trust fund transactions.

Those were the figures that the Committee for Economic Development used some years ago and recommended as the best figures then available.

Since that time, the Department of Commerce and the other people who have worked on national income have arrived at a new set of figures, which, like the consolidated cash statement, do include both trust accounts and budget accounts; but these national income account figures have two advantages over the consolidated cash statement, for purposes of economic analysis.

The first is that the Federal receipts and expenditures and the national income accounts are based on accrual data and not on cash data; which means that the national income account figures attempt to take account of the effect of Federal activities as those activities accrue, as their impact is felt, and not when the taxes are actually collected or the checks are actually written for expenditures.

This is particularly significant on the receipts side, where, as you know, the corporation tax collections lag 6 or 7 months behind the time when they actually accrue to the Government.

The national income accounts figures will include the accrual of corporation taxes and other taxes as that has happened, and accordingly, they are a much more accurate and precise measure of the timing of the effect of Federal tax laws on private activity.

On the expenditure side, a second major difference, a major improvement, which shows up in the national income accounts figures, is that they are intended to reflect those activities which have a direct impact on production and income, and they omit, therefore, purely financial transactions.

They do not count as having a direct impact on production and income, the making of a Government loan, which is simply giving some money to a person. When he uses that money, it may indeed have a direct impact on production and income, but that is his action, and it may take place at some later time, and shows up in the national income accounts not as a Government action but as a private action.

Consequently, the Federal receipts and expenditures in the national income accounts omit this and a lot of other similar kinds of financial transactions; and for economists it is therefore a much cleaner indication of the direct effect of what the Federal Government is doing in influencing the production and incomes in the economy.

Now, those are the two principal advantages as economists see them, one, that these figures are on an accrual basis, and two, that they omit purely financial transactions.

Senator PROXMIRE. What prospect is there, would you say, of finding a wise policy of calling attention to this type of budget, which gives a far clearer picture of the impact of the budget on the economy, than the administrative budget?

The administrative budget, it seems to me, has so many weaknesses. The budget you have just been talking about has a substantial surplus.

Mr. BELL. $4.4 billion; that is right.

Senator PROXMIRE. For fiscal 1963, which will have a retarding effect on economic expansion. And this is the one we should have been talking about this morning, perhaps, at least when we were discussing the economic impact of the budget.

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

Senator PROXMIRE. Why can't we move into this field and away from the administrative budget?

Mr. BELL. Senator, I think probably the answer is that we can, but not all at once. You know, these are worlds in which there are substantial traditions. We have felt that we have indeed been rather bold in making the changes that we have in the last year.

The first time that the Federal receipts and expenditures in the national income accounts were ever published at all as a part of the Federal budget explanations and discussions was in the review of the 1962 budget that we published in October. This is the first budget message that any President has ever submitted in which the term even occurs, in which there is any reference to it. We have made a major innovation in bringing these figures into the realm of public discussion.

And we will continue to do so. When we are talking essentially around economic issues, as we are here this morning, I think most of us would incline to begin to use these figures as the center for the discussion.

This is not, however, to say that we should abandon the other kinds of figures, which are of use for other purposes. The Appropriations Committees of both houses, I am sure, would be most reluctant, and quite properly so, if there were a decline in the attention paid so far as the processes of congressional approval of appropriations are concerned if there were a decline in the attention paid to the administrative budget.

Senator PROXMIRE. May I interrupt at this point?

The action by the Congress with regard to social security, with regard to unemployment compensation, increasing benefits and increasing taxes, is an action which is enormously important to individual Americans, and vastly important to our economy. Why should this be entirely left out of the traditional budget?

Mr. BELL. Because the Appropriations Committee has nothing to do with it.

Senator PROXMIRE. That does not seem to me to be a very convincing reason.

Mr. BELL. Well, sir, for purposes of analysis and discussion, you are entirely correct. For purposes of congressional procedures, the activities, the range of responsibilities, of the different committees, while we may chafe at them now and then, is a fact of life as far as the executive branch is concerned, and we naturally have to adapt to it and adjust our presentation of data and so on to fit the circumstances.

This is not to say that those circumstances look to an outsider to be as rational as they could be; but these are areas in which any representative of the executive branch necessarily treads with some caution

Senator PROXMIRE. There is still—I cannot say an error, exactly, but an omission, in the national income basis; because you do not include the gross effect of, say, the Post Office, TVA, Commodity Credit Corporation, and other Government agencies.

At any rate, this net figure which is the figure you use, has little economic significance as I understand it.

Mr. BELL. This is in my opinion a very good point, indeed, and recently I have asked my staff, specifically Sam Cohn, here, who is our leading expert on these matters, to look into this precise point.

I am not at all satisfied that we should be netting out the things we do and grossing the things we do. The figures are mixed, now. Some are on a gross basis and some on a net basis. I do not understand the rationale for it.

I think what we have are figures that were sort of put together piecemeal, and for each specific decision there was a rationale at the time it was done; but whether it all adds up to an appropriate set of overall figures, I am not prepared to say today.

We are looking into it. We may very well be proposing some changes.

Senator PROXMIRE. Can you give any estimate, any figure, on what the relationship is between Government activity, total Government activity, and the gross national product?

This I recognize is a very difficult one, because I understand transfer figures are not included in the gross national product. I do not know whether we have extracted the figures you say we are working on for the various Government activities, such as the post office. Yet this would be extremely useful to us.

Mr. BELL. We have lots of exploration to do before we could give you a satisfactory response. However, even when we have explored it, we would have to give it to you not as a single figure but as a number of different figures; because there are a number of different kinds of relationships between the activities in the gross national product.

You can measure the share of goods and services purchased by the Government as part of the total goods and services.

Senator PROXMIRE. Why not use exactly the same concept you use with regard to private companies? In other words, the value added by Government, in terms of wages paid, services purchased, et cetera.

Mr. BELL. This is not possible, I think, in relation to Government, because the value added in manufacture is the difference between the value of the product as sold and the value of the inputs which are purchased by that company.

There is no such difference in Government. We do not have a separate valuation on the output of Government. All we can value is the services and goods that the Government buys.

So that that particular comparison I do not think offers us very much help.

But there are lots of questions here which we can pursue, and we should be able to shed more light on these as time goes by.

For example, and I think this is one of the points that Mr. Moore pointed out in his study, we do not have a very accurate or current set of figures which is sort of integrated with these other figures, on the significance of the guaranty type activities. The figure on the volume of mortgages that is insured by the FHA system is available; but what is the economic significance of the volume of mortgages that is insured by the FHA? What is the impact of that on the gross national product? This is not a Government expenditure, but it is something that the Federal Government does which obviously does have an impact on private activity.

That is the sort of thing that at the present time just sort of stands in the wings, and we do not know quite how to integrate it into our general thinking.

Senator PROXMIRE. There are certain possibilities, such as how to evaluate the cost to the Government and the taxpayer of providing this service, of guaranteeing, and so forth. I know it is very involved.

My time is up. I would like to just say one more thing. That is that I am delighted at this supplement, these statistics. I am chairman of the Statistics Subcommittee of this committee, and I am very pleased with the excellent job that has been done by this administration in the statistical field.

I would like to suggest to you, too, while Mr. Bowman is before the committee: In your supplement you refer to the $300,000 to be spent to secure manpower and employment data; and by the $300,000 I am referring to the BLS study in depth of unemployment.

I would like to get, and I am sure the committee would like to have, the questionnaires to be used, the study as it evolves and develops, so that we can be in a position to make suggestions and to consider it.

I am deeply interested in this. Other members of the subcommittee are, too. There is a great deal of information we do not have on unemployment, which can be exceedingly helpful to us policywise, and as we get this information, it will be very useful.

Mr. BELL. Dr. Bowman, who is head of our Division of Statistical Standards, and responsible for much of the good work here, is present today and will be glad to provide for you the various questionnaires, forms, plans, and so forth, that are related to this series of studies; and I will ask him to do so.

Senator PROXMIRE. Because it seems to me that one of our serious problems on unemployment is that we know so little about it, about the real problem of the unemployed person, his willingness to move to get other jobs, et cetera.

Senator DOUGLAS. Mr. Bell, I appreciate your being here. Sorry to detain you so long.

One or two comments and one or two questions.

I am informed that this committee has for 10 years obtained from the Department of Commerce the tables from the national income accounts, but never previously have these been adopted by the Budget Bureau.

Mr. BELL. That is correct.

Senator DOUGLAS. We are very happy to see this.

If you will turn to table 4 of the Federal receipts and expenditures and the national income accounts, that indicates that the surplus is not $500 million, as in the administrative budget, but $4.4 billion.

Mr. BELL. That is right.

Senator DOUGLAS. And if you compare this surplus with surpluses in previous years, there is only 1 year, since 1953, that the surplus has been greater.

Mr. BELL. That is correct.

Senator DOUGLAS. So that on a national income basis, this is about as restrictive a budget as we have had in the last 10 years.

Mr. BELL. If you measure the restrictive character of the budget by this particular figure, that would be the conclusion reached.

There are, sir, considerable variations in the timing of the peaks and valleys of economic activity, which would affect this particular figure. Nevertheless, I accept the point. It is correct.

And as Senator Proxmire was saying earlier, this gives a somewhat different picture from the $500 million surplus in the administrative budget; and in economic terms this is unquestionably a more significant figure.

Senator DOUGLAS. I am just going to throw this question out, then: If we could consider these issues on their merits, without regard to the idols of the marketplace, and if we were concerned about the volume of unemployment, might not this be too restrictive a budget in terms of the high rate of unemployment which exists?

Mr. BELL. It has been my experience, in the past few months, in talking with a large number of the economists who specialize in these problems, of differing political ideas, that this is the question they ask. Their question is: Is the budget surplus calculated this way too much? Is it too high? Is this going to contribute to pinching out the economic recovery?

For the reasons I gave in my earlier statement, we are persuaded that this is not the case. However, I personally would feel that if one had to lean in one direction or the other, in judging the economic impact of this budget, it certainly leans a little bit that way, rather than being too expansionary.

Senator DOUGLAS. Perhaps the European bankers may have their faith in the United States increased.

Mr. BELL. If they have good economic advice, I should think they would, Senator.

Senator DOUGLAS. Now, I would like to end on a very minor note, on sugar and transportation.

Last year I became somewhat alarmed at the way in which the Cuban sugar quota had been distributed. It amounted to about 3⅓ billion tons. And we had been paying 5 cents a pound on sugar when the world price was something under 3 cents a pound, and therefore had been providing a subsidy paid by the American taxpayer of approximately $45 a ton and close to $150 million on the sugar which we bought from Cuba. Nevertheless, Dr. Castro said this was an indication of how we had been exploiting Cuba.

When this Cuban sugar quota was redistributed to various countries, we continued to pay 5 cents a pound, and this constituted a windfall profit to the sugar industry in the countries which received quotas: India, Mexico, Brazil, Peru, and a number of other countries.

I do not think much of it got down to the workers. The people who held sugar in storage made a killing. The sugar planters are making perhaps a killing now.

I proposed that the Government should levy import taxes equal to the difference between the world price and the price of our products, and in this way recoup for the American taxpayers at least the $150 million which otherwise would be a windfall profit to a relatively small group of people.

I was surprised that we got this through the Finance Committee by a unanimous vote. We went on to the floor, and were opposed by the State Department, which said that this would gravely injure Latin American relations.

I notice in the current budget that you have adopted this suggestion. Am I correct?

Mr. BELL. You are correct, sir.

Senator DOUGLAS. I want to congratulate you. How did you overpower the State Department?

Mr. BELL. I do not think there was any overpowering required. It is perhaps significant that the President's proposals for assistance to Latin American development in the Alliance for Progress have taken hold much more strongly than they had a year ago. They are much more widely understood. It is a much stronger and clearer and more definite program.

This year the President is recommending that a special title be included in the foreign aid legislation, which will be earmarked, so to speak, or will be public identification of the share of the foreign aid which is intended for Latin America.

I believe that these elements of the situation probably contributed to the willingness of the State Department to agree that it was not necessary to use the last year's method of paying for sugar imports.

Senator DOUGLAS. Very good.

As a matter of fact, so far as I can gather, wages were not increased on the plantations.

Mr. BELL. I think you are quite right, Senator, that this was simply a windfall gain for a few wealthy people.

Senator DOUGLAS. And these people in turn did not reinvest their money in Latin America, but in the main deposited it in Swiss banks.

This has been one difficulty throughout; that the high incomes of the wealthy Latin Americans were not being invested in Latin America, but deposited outside the country or spent in luxury, and that in effect they are asking the United States to make the investments in Latin America which the wealthy groups in Latin America will not make for themselves.

Have you thought of that?

Mr. BELL. I have, sir, and I think to some extent that is quite true.

This is, of course, one of the reasons why the President's program for aid to Latin America has stressed so strongly the internal reforms which we expect those countries to make if they are to expect strong assistance from us—land reform, tax reform, and other measures which would contribute to the purpose you have in mind.

Senator DOUGLAS. Haven't they really got to get under the load themselves of helping to develop that country?

Mr. BELL. Precisely.

Senator DOUGLAS. In other words, just as France and Great Britain and Germany have got to assume a larger share, so Latin America has to assume a larger share of the defense and the development of the free world. Isn't that true?

Mr. BELL. Yes, sir. And this is the basic theory or the basic philosophy of the Alliance for Progress, that they are committing themselves to take actions many of which are quite difficult for them to take, but which will contribute to this.

Senator DOUGLAS. I think this is admirable. But, you know, every time that one urges this, the people abroad say that Uncle Sam is grasping and is not willing to do his duty.

Mr. BELL. These are strings on aid; there is no question about it, Senator.

Sentor DOUGLAS. And we have very fine people inside this country who tend to see the foreign point of view.

Well, I congratulate you on progress in this matter, and I hope that at this point you may have the State Department anesthetized.

Mr. BELL. I think they are in full agreement, Senator; not just anesthetized.

Senator DOUGLAS. Thank you very much.

We will adjourn until next Tuesday at 10 o'clock in the morning in this room, when the Secretary of the Treasury will testify, and at 2 o'clock in the afternoon the Chairman of the Federal Reserve Board will testify.

(Whereupon, at 12: 45 a.m., the committee was recessed, to reconvene Tuesday, January 30, 1962, at 10 a.m.)

JANUARY 1962 ECONOMIC REPORT OF THE PRESIDENT

TUESDAY, JANUARY 30, 1962

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

The Joint Economic Committee met, pursuant to notice, at 10 a.m., in room P-63, the Capitol, Representative Wright Patman (chairman) presiding.

Present: Representative Wright Patman (chairman), Senator Paul Douglas (vice chairman), Senators Proxmire, Pell, Bush, and Javits; Representatives Bolling, Reuss, Griffiths, Curtis, Kilburn, and Widnall.

Chairman PATMAN. The committee will please come to order.

We have as our witness this morning the Secretary of the Treasury, Mr. Dillon.

Mr. Dillon, I assume you have a prepared statement. You may proceed in your own way, sir.

STATEMENT OF HON. DOUGLAS DILLON, SECRETARY OF THE TREASURY

Secretary DILLON. Yes, Mr. Chairman.

Chairman PATMAN. After you are finished, we will ask you to yield for questions; and then, if we do not get to ask all the questions we would like to ask you, we will take the liberty of sending them to you in writing, with the hope that you will answer them and place them in the transcript.

Will that be satisfactory, sir?

Secretary DILLON. I will be glad to do that, Mr. Chairman.

Chairman PATMAN. You may proceed.

Secretary DILLON. Mr. Chairman and members of the committee, the past 12 months have been an active, and I think fruitful, period in terms of our economic policy. In many ways, remarkable progress has been evident. Nevertheless, urgent problems remain. I am grateful for this opportunity to review with you today both our recent experience and our plans for meeting the needs of the future.

Progress and problems: Last year began in recession, but closed with output and income at new record highs. The personal hardship and economic waste of unemployment were reduced. Nearly a million workers were added to nonfarm payrolls. Industry, while working longer hours at higher pay, is also earning greater profits. And, while providing a higher standard of living for our citizens, we have strengthened our military defenses and contributed further to the economic progress of other, less fortunate nations.

This progress was achieved within a context of general price stability. On that solid base, exports reached a record volume, contributing to a significant reduction in our basic balance-of-payments deficit. At the same time, defenses against potentially disturbing short-term capital movements are being greatly reinforced. As a result, confidence in the dollar has been strengthened.

However, the economy is still operating well below its full potential. Our growth rate over recent years has hardly been satisfactory. Unemployment is still at an unacceptably high level. The deficit in our international accounts, while smaller, remains troublesome. And, the very progress of the past year, not only in this country but in other parts of the free world, has brought with it new problems to which we must find solutions.

Financial policies in 1961: There is no single, easy explanation for our progress during 1961. A large part of the answer lies in the natural vitality of our type of market economy operating under conditions of overall price stability—the fundamental prerequisite for all our attempts to achieve faster growth at home while simultaneously working toward a sustainable balance in our international accounts. That price stability, in turn, can be traced primarily to sharp gains in industrial efficiency and worker productivity as output expanded from its recession level—gains that enabled industry to pay higher wages and to increase profits without raising prices.

Government policy supplied another large part of the answer. First, there was the psychological, but nonetheless real, reaction that flowed from President Kennedy's earliest statements and programs. At home, the President's clear intent to deal with the recession promptly and effectively helped restore confidence in the economic outlook, encouraging expanded investment and spending. Similarly, the President's expressed determination to maintain the strength of the dollar internationally without resort to protection, controls, and restraints met with a prompt response. The speculative capital outflow subsided, and the gold drain was sharply reduced.

This positive approach entailed, under the particular circumstances then prevailing, acceptance of a sizable budgetary deficit—which was further enlarged by the higher levels of defense spending called for by the Berlin crisis. At a time when human and industrial resources were readily available to expand output, the rising trend of Government outlays and the consequent deficit were important factors in speeding the recovery without creating pressures on the price structure.

The stimulating effects of the budget were reinforced by monetary and credit policies. Throughout the past year, the credit markets have had ample funds to meet the combined demands of businesses, individuals, and the various levels of Government—thus facilitating a revival in capital outlays, higher levels of homebuilding, and steady progress toward meeting the accumulated needs of local governments. In sharp contrast to other recovery periods since World War II, lending rates have held almost steady, particularly in the long-term area. Both corporations and State and local governments can still raise funds at virtually the same cost as a year ago. Mortgage rates, after declining in the early part of 1961, have been substantially unchanged since last spring. This stability was particularly striking in a year when the total funds raised in the capital markets by corporations, homebuyers, and State and local governments, reached a new alltime peak.

All this was accomplished without permitting rates for short-term money market instruments to drop to the extremely low levels characteristic of earlier periods of easy money and recession. That was a significant achievement, for short-term rates, while less important in influencing investment activity at home, can play a critical role in directing the flow of liquid capital between the financial centers of the world. Here, Treasury debt management policy, as well as greater flexibility in the day-to-day conduct of open market operations, was an important factor.

Working in close cooperation with the Federal Reserve, the Treasury, in financing the deficit, increased the outstanding total of securities maturing within a year by more than $10 billion. At the same time, there was no shortening of the average maturity of the marketable public debt, largely as a result of the continued use of the "advance refunding" technique. This type of financing involves the exchange of outstanding issues for longer maturities, with a minimum impact on market conditions and flows of funds into productive investment.

This combination of a budgetary deficit with flexible monetary and debt management policies, carefully attuned to the realities of the balance of payments as well as domestic needs, was appropriate both in terms of magnitude and timing. The extremes of the 1958 recession—when the deficit reached nearly $12½ billion and interest rates dropped sharply, only to surge abruptly higher as recovery started—were successfully avoided. Financial policies were stimulating without being inflationary; the threat of disturbing short-term capital outflows was ameliorated. Moreover, business expansion has proceeded in orderly fashion. Today, signs of the sort of excesses that breed instability and require sudden changes in policy are notable for their absence.

Our basic goals: This does not mean, of course, that all the policies appropriate to the past 12 months are suitable for meeting the challenges of 1962. With recovery largely completed, the domestic focus must now be on maintaining forward momentum while guarding against inflationary pressures as our resources are more fully utilized. Confidence in the dollar has been maintained. To sustain that confidence, further progress toward a longrun equilibrium in our basic international accounts is a necessity.

Our fundamental objectives—domestic growth and a payments balance—must be pursued together, within the framework of free markets. All administration policy is pointed toward that end. We reject policies that presume irreconcilable conflict between our objectives; policies that attach sole priority to growth, or sacrifice growth to external equilibrium. These purported solutions are both unacceptable and unworkable in a world in which our capacity to grow is being challenged and our allies in freedom need the strength and stability assured by a solid dollar.

Success in reaching our twin objectives will require hard decisions, not only by those who shape the financial policies of government, but also by those who set price and wage policies for management and labor.

A balanced budget: The President's budget message is a financial reflection of our national needs and priorities. Expenditures will rise moderately in fiscal 1963, almost entirely because of defense needs and despite painstaking elimination of nonessential spending, both military and civilian. These expenditures can and should be supported by a growing economy. In the light of past experience and current trends, the projections of a further rise in the gross national product to $570 billion in 1962 that underlie the revenue estimates are entirely reasonable. Without raising tax rates an advance of this sort will generate revenues slightly larger than expenditures. Under the economic conditions we foresee, the achievement of such a balance is highly important in avoiding inflationary pressures as the economy moves closer to its full potential.

One result of this budget will be to reduce the possibility of severe strains on the monetary system as the economy expands—strains that could bring sharp and sudden increases in interest rates and unsettling market reactions that impede the flow of savings into productive investment. In 1956 and 1957, and particularly in 1959, strains of this sort appeared to be developing at a time when too much of the burden of maintaining balanced growth and curbing excesses was thrust upon the monetary authorities. Monetary policy is an essential and powerful tool for facilitating appropriate adjustments in the economy. But unless it is supported by appropriate budgetary policy, the results can be capricious and unpredictable, contributing too little to either stability or growth.

The debt ceiling: The President's recent request to raise the temporary debt limit to $308 billion is the result of an unavoidable concentration of revenues in the final half of fiscal 1963—a concentration that stems largely from the normal recurring seasonal pattern of tax receipts. Borrowing of about $9 billion will be necessary between the end of this fiscal year and the principal taxpayment dates in fiscal 1963—even though the budget for the fiscal year as a whole is balanced. Moreover, while we anticipate that the total debt on June 30 of this year will be somewhat lower than the current figure of over $297½ billion, prompt enactment of an increased ceiling is needed to restore some margin for flexibility and unforeseen contingencies—a margin that has been virtually exhausted by the higher defense expenditures required to meet the Berlin crisis, which developed after the enactment of the current limit of $298 billion.

Measures to encourage investment: A balanced budget in times of relative prosperity means that the Federal Government on an overall basis does not draw on the national flow of savings available for investment. Thus, a balanced budget in these circumstances promotes the flow of private investment.

Why is an increase in such investment so important to us today?

At the heart of the matter is the fact that it makes possible greater productive efficiency. Gains in efficiency are necessary for growth at home, for price stability, and for aggressive penetration of foreign markets. Thus, increased investment is the key to achieving our major objectives—growth and external balance—simultaneously in the years ahead. And, this is where the American economy has fallen furthest behind in recent years.

Since the mid-1950's investment in capital equipment in the United States has averaged less than 6 percent of the gross national product, as compared to about 7 percent during the earlier postwar years. By contrast, German investment has been averaging about 12 percent of GNP during recent years; French between 8 and 9 percent; and the Common Market countries as a group, about 10 percent. It is not a coincidence that these countries have been growing by roughly 5 percent per year, while generally maintaining a strong external payments position. Nor is it mere happenstance that some other countries, where productive investment has been a relatively small proportion of GNP, have had to cope with relatively slow growth and recurrent payments difficulties.

Certainly growth alone, or larger investment by itself, is no guarantee of external balance. But foreign experience strongly suggests that our twin objectives can be not only compatible, but mutually reinforcing.

In our economy, investment in plant and equipment is properly the province of private businesses, individually responding to the profit motive and competitive pressures by increasing production efficiencies and seeking out new markets. The Government nevertheless has an essential role to play in maintaining an economic climate that will encourage and facilitate the investment process.

I have mentioned the role of budgetary policy in this regard. But a balanced budget alone cannot meet our urgent need to increase our rate of investment in productive capital equipment. It is also vitally important that our tax system should recognize the need to accelerate the modernization of our physical plant and equipment.

This is why the administration has attached first priority, among tax reform measures, to the investment credit and the related revision in depreciation schedules. The first steps toward depreciation reform have already been taken with the new depreciation allowance guidelines for most of the textile industry. Revisions in guidelines for other industries will be announced this spring.

Based on exhaustive statistical and engineering studies, these administrative actions, consistent with the present law, recognize past experience and practices as well as the impact of technological advances and other factors on the economic life of plant and equipment. They will provide a much more realistic basis for taxation, and will stimulate business modernization and expansion. They cannot alone, however, assure the necessary flow of funds into new productive facilities, nor will they place American firms on an equal footing with their competitors abroad, where special incentive allowances are commonplace. To achieve this, revision of depreciation guidelines must also be accompanied by the proposed investment credit. These coordinated reforms go together and should not be separated.

In enacting the investment credit, we must also recognize the need to avoid a loss of revenue that could jeopardize the prospects for a vigorous recovery with stable prices. It is for this reason that the President is urging the simultaneous enactment of tax reforms that will balance the cost of the investment credit and at the same time eliminate certain defects and inequities in our tax structure.

Meanwhile, the Treasury is continuing its intensive review of the broad issues of tax reform, including the structure of the personal income tax. Fundamental changes of this sort inevitably require careful preparation, and close analysis of a welter of detail. In the end, congressional hearings will provide the best assurance of a full and fair appraisal of the implications of any basic change in the tax laws. The President plans to submit to the Congress later in this session a broad program of tax reform so that this process of public scrutiny can get underway promptly, looking to enactment of the reform in 1963. Any comment now on the nature of these proposals would be premature, but a thoroughgoing reform of this type will most certainly entail some adjustments in the basic individual tax rates.

Toward payments equilibrium: Tax reform to stimulate modernization of our industrial equipment provides a foundation for other efforts to improve our balance-of-payments position, including measures aimed directly at increasing exports to the large and rapidly growing markets of Europe and other developed countries. The administration is pursuing with vigor its program to make more American businesses aware of the opportunities in foreign markets, to familiarize those markets with American products, and to enlarge and speed the flow of information between American producers and their potential markets. A new and comprehensive program of export credit insurance, undertaken by the Export-Import Bank in cooperation with private insurance companies and banks, is now ready and will provide simplified procedures and comprehensive risk guarantees fully equivalent to those long available to most of our competitors abroad.

In today's world, export markets are highly competitive. The rapid growth and consolidation of the European Common Market, creating a free internal market but protected from outsiders by a wall of uniform tariffs, poses a serious problem—but it also presents a great opportunity. The problem is that we must assure ourselves of access to the richest of our foreign markets—a market to which we export almost $3½ billion per year, a far larger amount than we import from the same area. The opportunity lies in the mutual negotiation of lower tariffs on a reciprocal basis for broad groups of products, at one and the same time expanding our export potential and forging a strong Atlantic trading partnership. To seize this opportunity, President Kennedy has sent to Congress a new Trade Expansion Act.

Increased exports are, over the long run, the most effective means of eliminating our basic balance-of-payments deficit in a manner consistent with our other objectives and responsibilities. But because of our current position, other efforts to reduce the drains directly related to our overseas commitments must be continued and reinforced.

One of the most important is the negotiation of arrangements with certain of our allies to offset the dollar outflow arising from maintaining our military forces overseas. In addition, a large portion of our economic assistance is being tied to purchases in this country. And, the proposed legislation to equalize the impact of the corporate income tax on business operations at home and in developed countries abroad would eliminate a special stimulus to investment in industrialized nations.

The balance of payments in 1961: Although some of these measures have been in effect for only a limited period of time and others are yet to be undertaken, our balance of payments showed substantial improvement for 1961 as a whole. While firm data are still not available, current indications are that the basic deficit—the net of all our recorded transactions except volatile short-term capital flows—declined to roughly $600 million, as compared to almost $2 billion during 1960. A part of this improvement—almost $700 million—can be credited to advance repayments by foreigners of long-term Government loans. Nevertheless, the improvement in the remainder of the basic account was substantial. Preliminary figures point to an overall deficit, including short-term capital outflows, approximating $2.5 billion, down from $3.9 billion in 1960 and from an average of $3.7 billion over the 3 years 1958–60.

Much remains to be done before equilibrium is restored. Some year-end figures now becoming available and tentative data for the fourth quarter emphasize the need for caution. The overall deficit appears to have risen to well over $1 billion in the final quarter, considerably above the average for the first three quarters of the year.

The increase in the deficit from the third to fourth quarters appears to have been entirely a matter of short-term capital outflows, one of the most elusive items to pin down statistically. Estimates now at hand suggest that these flows, for the year as a whole, were almost as large as in 1960.

There were, however, clear and significant differences in the character of these outflows. In 1960, reflecting some uncertainty over the stability of the dollar, the outflow had been in considerable part of a speculative character, and the flows were quickly translated into a drain of gold. This disruptive speculation ceased early in 1961. There was, however, a continuing outflow of short-term funds over the first three quarters of 1961, related largely to an increase in the financing of foreign trade by American banks.

In the fourth quarter, a further outflow from this source was coupled with large shifts of liquid funds to foreign markets, partly in response to interest rate differentials, and partly related to certain quirks in the impact of domestic and foreign tax treatment of earnings of American companies with operations in Canada resulting from changes made in Canadian tax laws during the past year. Some shifts recorded as an outflow were apparently promptly reinvested in the New York market by agencies of foreign banks. This again seems to be the case particularly with Canadian banks and their agencies. We cannot as yet pinpoint the relative weight of all these factors. There are serious questions whether our conventional classifications of short-term capital flows accurately reflect their true significance for the balance of payments. This difficult subject is presently a matter of intensive study.

Certainly, the fact that the exchange markets have been calm for months belies any implication that these recent outflows are a symptom of concern about the dollar. So does the fact that a much smaller proportion of the dollars flowing abroad was converted into gold during 1961. In addition early and necessarily fragmentary data for January indicate that these unusual outflows now have ceased.

Strengthening the International Monetary System: Whatever their cause, the large flows of short-term capital since the institution of currency convertibility by major foreign countries provide evidence of the need to bulwark the dollar and the whole international payments mechanism against their potentially disturbing impact. In a world of convertible currencies and free markets, sizable flows of liquid funds between markets can be expected as a natural response to myriad changes in both our own and foreign economies. The danger is that, under certain circumstances, they may set off self-propelling speculative movements.

During the past year, we have used three approaches in dealing with this problem. For many months, the Treasury, operating within the framework of the newly created Organization of Economic Cooperation and Development, has been conducting fruitful consultations with other financial powers on a periodic basis. These discussions have laid the foundation of common understanding and cooperation that is a prerequisite for effective international action to prevent, limit, or offset currency movements that could undermine a stable monetary system. They have been supplemented by Federal Reserve participation in the regular meetings of European central bankers at Basle, and by bilateral consultations with our principal financial partners.

The Treasury also has undertaken the purchase and sale of foreign currencies for the first time in a generation. These operations helped at certain critical periods to reduce incentives to shift funds abroad on a speculative basis or to take advantage of temporary differentials in the exchange markets. The Federal Reserve has also recently decided to undertake operations in foreign currencies, a development which we in Treasury regard as highly promising. Chairman Martin will be elaborating further on this approach during his testimony this afternoon. I look forward to our continued cooperation with the Federal Reserve in the international field, just as in the domestic area.

Finally, and most significant for the strengthening of the international monetary system, is the agreement reached among 10 of the major industrialized countries to buttress the resources and capabilities of the International Monetary Fund by lending it specified amounts of their own currencies when necessary to cope with temporary stresses. This $6 billion of standby facilities, including almost $2½ billion of European Common Market currencies, will both reduce the likelihood of a "run" on any member currency and provide the means to withstand the impact of a speculative attack should one develop. The new arrangements will powerfully reinforce the effectiveness of the Fund, and could be of great assistance to the United States. Enabling legislation will be submitted to the Congress shortly.

Economic security and stabilization: The President has proposed a series of measures to promote greater economic security for all our people, to permit more of our citizens to share fairly in the growth of the economy, and to reduce the hardships and waste of recurrent recessions. Aid to depressed areas and worker retaining can help speed growth and eliminate pockets of hardship. Broadened unemployment insurance can both reduce personal misfortune and strengthen the "automatic stabilizers" that have helped prevent our postwar recessions from turning into full-scale depressions. And, a reserve shelf of public works will strengthen our defenses against a possible future recession.

The President has also set before you a carefully devised plan for introducing an element of flexibility into our tax structure. The measure would facilitate a timely, but temporary, reduction in personal income tax rates, at his initiative, in the event of a serious business downturn. Its significance lies in the fact that a reduction in personal tax rates could speedily give a powerful boost to consumer spending power at critical junctures, when delay might permit cumulative downward forces to take hold. Adequate safeguards are provided, including strict limits on the amount and duration of any such tax reduction. This carefully circumscribed delegation of authority to the President, always subject to congressional veto, would be a significant addition to our arsenal of antirecessionary weapons.

The continuing challenge: The continuing economic challenge before us is clear: We must fashion the most effective arrangements possible to assure that our free economy will reach its unrivaled potential and enable us to fulfill our responsibilities for leadership in the free world. In meeting that challenge, we are acting in those areas where Government can appropriately and helpfully initiate new programs and policies. Equally important, we have tried to be conscious of those things Government cannot do, or that the private sector of our economy can do better.

The essential and unique characteristic of the American economy is the strength it derives from individual freedom for all of us—as workers, employers, owners, and consumers. In shaping our program for the years ahead, we are working toward the sort of environment that will strengthen and preserve that precious heritage.

Thank you, Mr. Chairman.

Chairman PATMAN. Thank you, Mr. Dillon.

You mentioned your meetings with foreign officials and international bankers. Have our representatives won any agreement, Mr. Dillon, or any understanding, from the European central bankers, to the effect that they are not to draw on our gold reserves, or that they will exercise some restraint in drawing on our gold reserves?

Secretary DILLON. Mr. Chairman, we have not asked for any restraint or any limits on the right of foreign countries to draw on our gold reserves, should they feel it appropriate to do so.

I do think that there has developed a much greater and better understanding of the forces at work in the exchange markets, whether they are temporary or whether they are likely to be more permanent; and I think this in general would lead to greater stability in the drawings of gold.

Chairman PATMAN. Is there any agreement, informal or otherwise, that we will guarantee dollars, either in terms of gold, or other exchange, in the event we should devalue the dollar?

Secretary DILLON. No, there has been no such demand or any such agreement.

Chairman PATMAN. You mentioned holding the line on prices and wages. You did not mention anything about interest rates. Do you not think that the cost of money enters into the cost of doing business in the same way, although not in such a significant way, as prices and wages?

Secretary DILLON. Yes, Mr. Chairman; I do.

Chairman PATMAN. Do you not think something should be said about that?

Secretary DILLON. Mr. Chairman, as I mentioned in the statement, I think our policy has been and so far we have been able, through a combination of Federal Reserve and Treasury policy, to maintain interest rates at the same level, without any significant increase, after some 11 months of recovery.

It is our hope that, through the provision of a balanced budget, as I indicated, we will reduce the strain on the monetary authorities as we move forward, and that any action that they may take will be therefore much more moderate than might be required in other circumstances.

I would assume that as business advances, should it advance as well as we expect it to, there could be some very moderate increases in interest rates; but I should not think that there is any reason for any very sharp increase—nothing like what occurred in the preceding rise in 1959. That certainly is our objective.

Chairman PATMAN. You are acquainted with the rumor that there is going to be an increase in the prime interest rate. Do you look with favor or disfavor on that, Mr. Dillon?

Secretary DILLON. Well I have seen reports of that. Certain bankers, either in articles or in speeches, have recently indicated that is a possibility or a probability; but as I understand it, they have in all cases said that this would probably take place at some time considerably in the future, maybe in the third quarter, or something like that. I think that that is so far off that it is very difficult for me to have an opinion on what would be right at that time. Certainly I see no indication, no reason, for any change in the near future or the medium-term future, and I would hope it would not be necessary even then.

Chairman PATMAN. There is a lot being said about the tax relation between mutual financial institutions and savings and loans associations as compared with the commercial banks. Do you look upon them as being competing, in the sense that there should be an adjustment between the reserves and savings, Mr. Dillon?

Secretary DILLON. What we feel is this: We feel that the time has now come—and this is the general tax philosophy of the administration, running right across the board—for greater equality in taxation everywhere. We do feel that the savings and loan and the mutual savings bank industry has reached a point in its growth—which has been, as you know, very remarkable—where these banks are now strong enough to bear their share of the national tax burden. The savings and loan and mutual savings banks now have well over a hundred billion dollars of assets and have paid essentially no taxes at all. We see no reason why, over a reasonable transition period, they should not be subjected to the same sort of taxes as everybody else, which includes commercial banks.

As to this question of whether they compete, I think it is perfectly clear that there has been competition all around—and that is probably perfectly healthy—between savings and loan institutions, mutual savings banks, and commercial banks, for savings accounts. There have been advertisements in the papers and things like that.

Chairman PATMAN. Mr. Dillon, I will follow you and the administration in regard to institutions that are truly competing; but I urge you to give further consideration to your statement that the commercial banks and savings and loans associations are in the same category, competitively. I do not believe that they are. And I want to invite your attention to a statement that Mr. Bob Anderson made when he was Secretary of the Treasury under Mr. Eisenhower, in which he stated:

> Banks are different from other lending institutions. When a savings and loan association, an insurance company, or a credit union, makes a loan, it lends dollars that its customers have previously paid in. But when a bank makes a loan, it simply adds to the borrower's deposit account in the bank by the amount of the loan. The money is not taken from anyone else's deposit. It was not previously paid into the bank by anyone. It is new money created by the bank for the use of the borrower.

Don't you see a great difference between an institution that lends the money that has been deposited with it, which is the same as a hundred percent reserve basis, and a bank, on the other hand, with a 5-percent reserve, that can create or manufacture its money for loan purposes? Don't you see a big difference between them, Mr. Dillon?

Secretary DILLON. Certainly. There are very real differences, Mr. Chairman. I did not mean to say that savings and loans should pay a fair share of taxation because they were the same as banks, but just that we feel that every economic element in our economy should pay a fair share of taxes.

Chairman PATMAN. There is no dispute there. You see, I am talking about competing institutions. It is all right to tax them all the same. But I am saying that savings and loan associations and banks are not the same; they are not competing in the same way. And I wish you would confine your answer to that, if you would, please, sir.

Secretary DILLON. I was about to get to that, Mr. Chairman.

In the statement you read, life insurance companies were mentioned. Life insurance companies do pay taxes. Our objective now is to reach the same sort of situation with the savings banks and the savings and loan associations.

We are not certain exactly what form this taxation will take. That is under discussion today, particularly in the Ways and Means Committee. But I am sure that after full consideration there, the end result will be a fair proposal for this taxation.

Chairman PATMAN. Did you have an occasion to notice a speech that I made last fall, in which I showed that commercial banks receive annually the equivalent of a subsidy of $5 billion a year; and that commercial banks have been going out of the banking business, largely?

In 1921, 40 years ago, we had 31,000 banks; now, they are reduced to 13,000. In other words, we have 43 banks now where we had 100 40 years ago. Yet we are in the greatest growth in all history.

Now, I think it is quite clear that the banks have forsaken a lot of this business, like savings and loans, and have concentrated on the more lucrative aspects of their businesses.

I think these factors should be considered when you think about penalizing or harming or retarding the savings and loans associations which have done so much to build our country and our homes; I do not mean that they should have the same reserve requirements that the banks have, but they should have a more liberal reserve than they do now.

Secretary DILLON. I certainly have no idea or intention in any way of detracting from the tremendous job the savings and loan and mutual savings bank industry has done in building up from a small start to a $100 billion industry. What they have done for housing in this country is tremendous, and it should continue, and we rely on it.

We want a healthy mutual savings industry. All we say is that we feel that the time has come when they should pay on that $100 billion industry more than the $7 million of taxes that they paid in the last year.

Chairman PATMAN. My time has expired.

Senator Bush?

Senator BUSH. Mr. Secretary, I came a little late. I wondered whether you touched in your statement on the question of withholding interest and dividends.

Secretary DILLON. No, I did not.

Senator BUSH. Would you comment on that for the committee, as to what your views are on that? And particularly have your studies on this convinced you that it is practical to make this all across the board, so to speak, the savings banks, the bondholders, the commercial banks, thrift accounts, and so on? I would like to have you tell us what your findings and recommendations are on that.

Secretary DILLON. I would be glad to, Senator.

Our recommendations originally were for withholding on interest and dividends on all bank accounts, savings accounts of all sorts, savings bonds, and all coupon bonds, and also on all dividends.

We do not ask, of course, for withholding on payments by individuals of interest on mortgages or things of that nature.

The reason for this is that, despite every effort through publicity, there has been a continuing gap that shows up in national income statistics between the amount of interest and dividends paid and the amount that shows up in the tax returns.

Senator BUSH. What is the order of magnitude of the gap?

Secretary DILLON. The order of magnitude of the gap is about $3,700 million, of which a portion, maybe something less than a billion dollars, we assume, would belong to nontaxable individuals. So obviously the gap would never be totally closed, because they would not report.

But the revenue gap to the Government on our figures comes to about $850 million a year. It is being lost every year, because the taxes that are owed and due are just not being paid. And we feel that by withholding at 20 percent, which is the first or lowest bracket rate, we would collect about $600 million a year automatically of that $850 million.

The remainder represents payments on which a tax at higher than 20 percent is due, and that could only be collected through better enforcement procedures, better publicity, and so forth.

Now, we think that this is a perfectly practical system. We have spent months in the testimony before the Ways and Means Committee, working over various exceptions to this procedure and various methods whereby this procedure will put the least possible burden on the paying institutions and at the same time will be the most equitable possible for any individuals who probably would not owe a tax.

The major exceptions we now have are that on savings accounts and on savings bonds there would be permanent exemptions for all children under 18 years of age, on the presumption that their income would not be high enough to require a payment of taxes.

There would also be a provision for exemptions for individuals over 65, at which time there are special allowances, as you know, available in the tax system. Also, of course, this is a time when most people are retired and their income is reduced.

There is no provision for exemption to age 65, because there are very few such people exempt, and exemption would require a great deal of extra work for the institutions in segregating accounts and handling them, which would not be worth the difficulty.

We have arranged a system for refunds whereby, within a matter of a month after the end of each quarter, refund checks would be in the hands of everyone who filled out little forms and applied for a refund; and we think with this procedure there will be a minimum of difficulty.

It will go into effect in a way very similar to the withholding system on wages and salaries; and our fundamental view is that there is no reason why those who work and are paid wages and salaries should have a withholding system, and those who receive dividends and interest should go without, particularly when there is such a large amount of funds due the Government which has not been received.

Senator BUSH. Will this withholding apply to Government bonds of all kinds?

Secretary DILLON. Yes.

Senator BUSH. Savings bonds included?

Secretary DILLON. The only Government securities it will not apply to are short-term bills sold at a discount. These 1-year or less issues are held largely by financial institutions; so there is no problem there.

Senator BUSH. And your studies have convinced you that the savings institutions, like the savings and loans and the mutual savings banks, can practically do the job that is involved in this withholding?

Secretary DILLON. Oh, without a doubt. There is no provision here for complicated information returns, and certainly the alternative, if we did not go ahead with this, would be to require information returns down to small amounts of interest, such as $10 a year, whereas presently we only require it to $600.

So in any event there would have to be, to get proper enforcement, a very considerable degree of extra work for savings institutions, and we do not think that withholding would, probably, be as much work as having to file these information returns.

Senator BUSH. And you do not see any problem in the dividend withholding?

Secretary DILLON. None whatsoever. There is no provision for exemption there, because it is not practical. So many stocks are owned in street names. They shift all the time. And it just does not appear practical to the industry.

Again, we have worked with industry here, the stock exchange. And dealers in securities are strongly against any exemptions because they do not believe they are workable.

Senator BUSH. Going over to the balance-of-payments problem again, I though your outline and your discussion of that was very interesting indeed. Are you giving any thought to this matter of curtailing, at all, the investment of American capital abroad, which has been running at the rate of, well, I should say $2,300 million or something on that order in the last year or so? Is this a matter that is under discussion or consideration?

Secretary DILLON. Yes, only I would not use the word "curtailing," because we have rejected any idea of controls on such investment. Our proposal, which was made last year, was to equalize the tax treatment of investment abroad with investment here in the United States. This would serve to reduce somewhat the incentive to invest abroad, and it might thereby somewhat diminish the outflow. But we would assume there would be a very substantial continuing outflow in any event.

Senator BUSH. That tax incentive really was an incentive tax bill, was it not, that gave the preferential tax treatment to investors abroad? Was that not made for the purpose of stimulation?

Secretary DILLON. I do not think it was, Senator. This was something that was incorporated in the income tax from the very beginning, in 1913, at a time when there was very little investment abroad by us, and there is really no indication that anyone considered the problem very seriously. It has become serious now because of our balance-of-payments problem.

Senator BUSH. My time is up, Mr. Chairman.

Chairman PATMAN. Senator Douglas is recognized.

Senator DOUGLAS. Mr. Secretary, I found myself somewhat mystified by the rather cryptic paragraph of yours at the bottom of page 14, which speaks of quirks in the impact of domestic and foreign tax treatment on earnings of domestic companies with operations in Canada, evidently resulting from changes in the tax laws occuring during the year.

What do you mean by that?

Secretary DILLON. I am glad to have the opportunity to explain that, Senator, more fully.

What happened was that during the past year the Canadian Government changed their income tax law, and they enacted a new tax on Canadian branches of foreign corporations. At about the same time, the Canadians terminated a provision in the United States-Canadian Tax Treaty by which the maximum withholding tax on dividends from a subsidiary to a parent was restricted to 5 percent. The result was the imposition of a 15-percent withholding tax on all dividends of foreign-owned investments in Canada that were remitted abroad. In other words, any dividend from an American subsidiary in Canada paid to the United States was subject to a 15-percent tax, which was a new tax. This tax was over and above the regular Canadian corporate income tax. The regular Canadian corporate income tax is 50 percent.

As a result, the effective rate on any dividends repatriated to this country was 50 percent, plus 15 percent of the 50 percent that remained, or 7½ percent, which made a total of 57½ percent.

Now, the unexpected impact of that relates to the interrelationship of that tax rate and our own tax system. As you know, we allow foreign taxes paid as an offset against taxes that are paid here in the United States. Our tax level here in the United States is 52 percent.

Senator DOUGLAS. And on Canadian investments 38 percent?

Secretary DILLON. No, sir.

Senator DOUGLAS. What about the 14-point Western Hemisphere tax credit?

Secretary DILLON. It does not generally apply to U.S. operations in Canada.

Senator DOUGLAS. It does not apply to Canada? It is only south of the Rio Grande?

Secretary DILLON. Generally speaking, yes, sir.

Senator DOUGLAS. Well, I am very happy to have my education on this matter increased, then.

Secretary DILLON. Because of this extra 7½-percent rate, it has been very useful for some companies who have investments in Canada, and who are returning their income to the United States, to find some other income abroad, which is not taxed. This will bring their overall income up, so that the rate of what they have paid in Canada comes to a total of 52 percent of the total earned. Otherwise, they would lose 5½ percent, the unused U.S. tax credit. This figure on the unused credit is based on the assumption that dividends are "grossed up" for tax purposes to include the tax on the profits out of which the dividends are paid, which the Ways and Means Committee recently agreed to.

The loss of the unused U.S. tax credit can be avoided by depositing funds in banks in Canada. The tax rate in Canada is only 15 percent of the interest being returned from Canadian banks.

Another thing that can be done is to transfer such funds to Europe. If they are held in Great Britain, for example, there is no tax at all on the return from capital which is lying in a bank in London. Therefore, that can be added to foreign earnings subject to the credit up to 52 percent provided by our own tax system.

One other aspect of this situation is that this Canadian tax applies also to income from branches, American branches, that operate in Canada; and branch income is, of course, subject to our 52-percent rate regularly, but they also have to pay this extra 15 percent; so it is equally helpful to them to offset that by extra income received, on which no tax is paid abroad.

Senator DOUGLAS. Mr. Dillon, I wonder if your staff would prepare a memorandum on this question of the 14 percent Western Hemisphere credit; because on page 119 of the bulletin which this committee published in 1961 on "The Federal Revenue System," the following statement is made—

> A special rate reduction of 14 percentage points is granted to so-called Western Hemisphere trade corporations.

It says that 95 percent of the gross income must be derived from outside the United States.

But your statement seems to be in direct conflict with this statement in the bulletin which we had prepared by very competent authority.

Secretary DILLON. I would be glad to speak on that.

A part of it flowed from what I had to say with reference to an ordinary branch of a U.S. corporation, which is not commonly covered by the Western Hemisphere trade corporation provisions. A great many investments in Canada operate as branches. And I think that the rest of it flows from the particular form that certain corporations take in Canada.

Senator DOUGLAS. Would some member of your staff make a full statement on that?

Secretary DILLON. We will be glad to do that, yes.

(The following was supplied for the record:)

FOREIGN TAX CREDITS AND CANADIAN INCOME

A U.S. company engaged in business in Canada is allowed a credit against its tax liability for income taxes imposed by Canada. If the company operates there through a Canadian subsidiary, the aggregate taxes imposed by Canada on the subsidiary and on the dividends it transmits to the U.S. parent exceeds the amount of tax for which credit is allowable under U.S. law with respect to the profits distributed by a Canadian subsidiary. The excess credit is 6.5 percent of the dividends received from Canada.

If the U.S. company operates in Canada through a branch, the excess credit would be 5½ percent, assuming that none of the Canadian branch profits were reinvested in Canada. The unused credit would be substantially larger in the case of a domestic company which qualifies as a Western Hemisphere trade corporation, i.e., one that derives all its income in the Western Hemisphere, 95 percent of it outside the United States and 90 percent from the active conduct of a trade or business. Such a company is subject to tax at a U.S. rate of 38 percent, instead of 52 percent, so that the gap between the Canadian taxes on its profits and the U.S. tax is 14 percentage points greater than in the case of a U.S. company operating in Canada through an ordinary branch establishment. The amount of income derived in Canada through Western Hemisphere trade corporations is believed to be small. An analysis made of the tax returns for 1955 of the 100 largest companies indicated that 83 derived income from Canadian sources. However, only three claimed a Western Hemisphere trade corporation deduction.

An unused foreign tax credit establishes an incentive for a U.S. company to seek foreign investment income which is subject to little or no foreign tax so as to utilize the available foreign tax credit. By so doing, the company can realize the investment income substantially free of both United States and foreign tax. This can best be seen from an example. Assume that a Canadian corporation earns $100 in profits on which it pays a Canadian tax of $50. It thus has $50 available for distribution, and assume that it declares a dividend of that amount. When the dividend is paid, Canadian tax is withheld at the rate of 15 percent, or $7.50. The aggregate taxes collected by Canada with respect to the profits earned in Canada and distributed as dividends is $57.50.

The U.S. parent includes in its U.S. taxable income the $50 of dividends received from the Canadian subsidiary. At a 52 percent rate, its tax liability is $26. However, the U.S. company is entitled to a credit for the taxes imposed by Canada. It is entitled, first, to a credit for the taxes actually withheld from the dividends that would otherwise have been remitted to it, namely, $7.50. It is also entitled to a proportionate part of the Candian income tax on the profits of the subsidiary out of which the dividends were paid. Since the dividends declared by the Canadian corporation and included in the taxable income of the U.S. parent were one-half the Canadian company's profits (before tax), the proportionate part of the Canadian tax to be taken into account is one-half the tax paid by the Canadian subsidiary, or $25. Thus, the total Canadian tax allocable to the $50 of dividends is the sum of $25 and $7.50, or $32.50. Since the U.S. tax liability is only $26, there is an unused credit of $6.50. These figures are shown in the attached table.

If the U.S. corporation receives investment income from Canada, that income will be subject only to a Canadian witholding tax of 15 percent. Although the income will be taxable in the United States at the ordinary corporate tax rate of 52 percent, the gap between the Canadian and U.S. rate can be filled by the unused credit. In order for the full $6.50 of unused credit to be absorbed, the American company needs to receive investment income of $17.57. The U.S. tax on this amount would just equal the 15 percent Canadian withholding tax on such investment income plus the unused $6.50 credit. The calculation is shown in lines 11–17.

The net yield to the American company from the $17.57 investment income amounts to $14.95, this being the amount left after the Canadian withholding tax. Since there is no additional U.S. tax on the investment income, this is the total disposable income of the U.S. corporation from its portfolio investment.

The same tax impetus to portfolio investment applies in the case of U.S. companies operating in Canada through branches in contrast to subsidiaries. However, for technical reasons concerning the method of computing the tax credit, the unused credit in the case of a branch would be less than in the case of a subsidiary, $5.00 instead of $6.50. Consequently the investment income necessary to use up the excess foreign tax credit is also smaller, $14.86 instead of $17.57.

On the other hand if the Canadian operation is a branch of a U.S. corporation that qualifies as a Western Hemisphere trade corporation, the unused credit is substantially larger, $19.50, and the investment income could be as high as $84.78 before the excess credit was completely utilized. However, a Western Hemisphere trade corporation must derive 90 percent of its gross income from the active conduct of a trade or business, and investment income is not considered to be such income. Hence the Canadian investment income which the company could receive, without jeopardizing its Western Hemisphere trade company status, would generally have to be less than the indicated figure. Only if the company had $763 or more of gross income from which it realized the operating profit of $100 would the company be able to derive the maximum amount of investment income. "Gross income" is not reported in Statistics of Income and hence the typical relationship between gross income and net income is not ascertainable. It should be noted, however, that gross income is not equivalent to gross receipts, since it is arrived at after the deduction of the cost of goods sold.

Illustration of the potential use of a U.S. company of an unused credit for Canadian tax to portfolio investment income

	Subsidiary	Ordinary branch	Western Hemisphere branch
1. Profits of Canadian corporation or branch	100	100	100
2. Canadian income tax (50 percent)	50	50	50
3. Dividends declared or branch profits transferred	50	50	50
4. Canadian tax on distribution (15 percent)	7.5	7.5	7.5
5. Total Canadian tax	57.5	57.5	57.5
6. Income for U.S. tax purposes	50	100	100
7. Amount of U.S. tax before credit (52 or 38 percent)	26	52	38
8. Potential credit for Canadian tax (before limitation)	[1] 32.5	[2] 57.5	[2] 57.5
9. Credit after limitation	26	52	38
10. Unused credit	6.5	5.5	19.5
11. Income from portfolio investment	17.57	14.86	84.78
12. Canadian withholding tax at 15 percent	2.63	2.23	12.72
13. U.S. tax on investment income	9.14	7.73	32.22
14. Credit for withholding tax	2.63	2.23	12.72
15. Net U.S. tax on interest	6.51	5.5	19.50
16. Less unused credit above	6.5	5.5	19.50
17. Net U.S. tax overall			
18. Net investment yield (11–12)	14.94	12.63	72.06

[1] $\frac{\text{Dividends}}{\text{Subprofits}} \times$ Canadian tax rate + withholding tax.

[2] Canadian tax on branch plus withholding tax.

Senator Douglas. Mr. Secretary, I think many of us have felt frustrated by the fact that while we have a favorable balance of trade in terms of commodities of around $4 billion a year, we have an unfavorable balance of payments of around $3½ billion a year. While we recognize that part of this is due to the expenditures of American troops abroad and part to the investment of American capital abroad, that part of it is certainly due to foreign aid and military expenses, both of which I believe are necessary, we know that you have been trying very hard to get the NATO countries to contribute a larger proportion of troops to the defense of Europe. We know also that you have been trying to get these countries to assume a larger share of the burden of foreign aid. We also know that you have been trying to get the Common Market to give as favorable terms to the United States as possible.

While I understand the present industrial tariff schedules are reasonably satisfactory, the agricultural schedules are still to come. From my own conversations in Europe last summer, I came to the conclusion that the position of none of the continental countries was really favorable to us on the question of agricultural restrictions. And I take it that while you have had some success in these other matters, the general experience has not been very satisfactory.

I am sure that you are doing your best. Is there anything that the Congress can do?

Secretary DILLON. I do not think that there is anything much further that the Congress can do. Maybe in the field of foreign aid, where we have been stressing the need to give foreign aid in the form of American products, for balance-of-payments reasons—American goods and services, rather than in the form of dollars that can be spent somewhere else, and which would affect our balance of payments—some indication that the Congress agrees with this philosophy might be helpful, because this is a continual struggle with certain countries which desire to have their aid in the form of straight dollars.

Senator DOUGLAS. But, Mr. Dillon, if I may say this: We are running an unfavorable balance of payments of almost $3½ billion for 4 years; and while there is no immediate danger, if this keeps on, year after year, we are going to be in trouble.

If our European allies would only bear a larger share of NATO expenses, would only contribute more to foreign aid themselves, would be willing to admit our farm products into their markets, then this drain upon us would be relieved.

But, very frankly, they seem to me to be as tough as they possibly can be. I came to the conclusion that they think that the altruism of the American public and the American Congress and the American Government is unlimited, and that they can push us just as far as they can, and we will always yield at the end.

What would you think of giving the power to the President to increase tariffs as well as to reduce them, so that he may have a club as well as a bait?

Secretary DILLON. I had not considered that. I would rather that the Department of State commented on that. But certainly I would think that of the things you mentioned, probably the most important at the moment is what will eventually be done regarding agricultural imports into western Europe; and I think any indication of congressional interest in that area would of course be helpful to the efforts that our State Department has been making.

Senator DOUGLAS. Would you think that the possibility that we might increase the tariff on automobiles might cause them to reduce the tariff on American products?

Secretary DILLON. That is certainly an argument. Yes, I can well see that.

Now, as far as the defense area goes, we have had quite some success in obtaining an agreement with at least one country—Germany—where we have our largest foreign military expenditures, to increase their purchase of equipment in the United States and their use of U.S. facilities, for which we will be reimbursed to an extent that this will offset the balance-of-payments costs of maintaining our soldiers in Germany. That is very helpful. We are now trying to extend that, or will be, over the coming months, to some other countries.

Certainly our basic deficit, which is what we are talking about in these terms, has improved, and we hope will continue to improve substantially. Not counting the special debt prepayments last year, it was only about $1¼ billion as against the much higher figures there have been before.

Senator DOUGLAS. My time is up, Mr. Secretary. I will simply say that I recognize the danger of getting into a retaliatory tariff war with Europe, and I want to avoid that; but I also feel frustrated by the lack of success which we have had and I think we still will have especially with at least two of our NATO allies. And I wonder if we should not give to the President the power to be tough as well as the power to be kind.

I will stop at that point.

Chairman PATMAN. Congressman Kilburn?

Representative KILBURN. Mr. Secretary, it is always a pleasure to have you testify.

I do not want to belabor this, but I just wanted a short explanation of interest withholding. Many small banks have small deposits of people who earn very little, but they are small savers, and of course, as their interest is added to their accounts, the amounts are always irregular, pennies and so on. Now, did I understand you to say that in the case of somebody who has an income account and who gets $13.19 interest, that the Government takes 20 percent of that; so he has got to then fill out a form, send it to the Government, and get back $3.49 or whatever it is?

Secretary DILLON. Mr. Kilburn, that presumes that the individual is in a bracket where he would pay no tax whatsoever, which means a very low income bracket.

The great bulk of such individuals are in the area of children under 18 and people over 65, and for these we do provide a system of exemptions whereby these withholdings would not be made; so that this would not arise.

In the case of people between 18 and 65, the records show that there are really very few individuals who are not in an area where they have to pay some tax; and if they have to pay a tax, they fall generally in the 20-percent area, which is the first level.

So the chances are that there would be very few people in that area that would need to have refunds. However, there is a provision for refunds to cover this type of individual, and the refunds would be made on application at the beginning of each year. On indication that the person will not be taxable, the refund would be made quarterly within a month after the quarter, and the Federal Government, under the arrangements we have with the Internal Revenue Service, would then take upon itself the responsibility of sending to the taxpayer each quarter thereafter a form for him to fill out in case the situation stayed the same and he still was tax exempt. So he would not have to think about it. He would have to sign it and send it in.

Representative KILBURN. But he would have to fill out the form?

Secretary DILLON. Yes, fill out the form.

Representative KILBURN. It just seems to me these small banks, the little ones, with the small accounts, will have so much burden put on them, and the Bureau of Internal Revenue, that it is not worth it, I would not think.

Secretary DILLON. Actually, Mr. Kilburn, this system of having exemptions for people under 18 and over 65 was worked out after intensive consultation with the banking industry, the savings and loan industry, and the other savings industries. It is largely their feeling, and it is in accordance with their views, that no provision be made for exemptions for people between 18 and 65, because that would have created more complications for them in dividing up their accounts of people in that age group. They felt it would have made greater difficulties for them, and it is largely for that reason.

Actually, last summer, when the Ways and Means Committee first studied the bill, there was a provision for exemptions for anyone who claimed that he would be tax exempt and would not have to pay taxes. He could file this paper, and then he would not be withheld on it. As a result of these intensive consultations during the fall, this mutual agreement was reached on these changes, which have been now tentatively accepted by the Ways and Means Committee.

Representative KILBURN. Thank you, Mr. Chairman. That is all.

Chairman PATMAN. Congressman Reuss?

Representative REUSS. Mr. Secretary, I would like to explore the fundamental point you raised in your presentation this morning, the tension between the role of domestic growth and maximum employment on the one hand and our balance of payments on the other.

First let me get a figure straight. It is a fact, is it not, that our balance-of-payments deficit overall in 1961, if one disregards the $700 million advance repayment of long-term Government loans, would be on the order of $3,200 million?

Secretary DILLON. That is correct.

Representative REUSS. So that, without wishing any more than you do to become, unduly, an alarmist, it is a fact that for each of the past 4 years our overall balance-of-payments deficit has been in excess of $3 billion?

Secretary DILLON. If you do not count these repayments.

Representative REUSS. If you do not count the repayments. And in fact there were no substantial repayments in the other 3 years prior to 1961, no substantial advance repayments?

Secretary DILLON. Oh, no. There were substantial advance repayments in 1959.

Representative REUSS. In 1959?

Secretary DILLON. Yes.

Representative REUSS. But not in 1958 or 1960?

Secretary DILLON. There were no advance repayments in 1960. I do not have the figures in my mind for 1958. They were substantial in 1959.

Representative REUSS. Now let me get back to my fundamental point and ask you this: If there were no balance-of-payments problem, if we had no deficits, and if, therefore, we did not need in our domestic economic policy to pay any attention to the international implications, we would then, in the months to come, be following a fiscal and monetary policy designed to bring about maximum employment without inflation, would we not?

Secretary DILLON. Yes; maximum employment without inflation.

Representative REUSS. And that would mean, particularly in the light of the policy of the administration, of using fiscal tightness as much as possible, a policy of relatively easy credit, relatively low interest rates, with an important part of the anti-inflationary fight entrusted to fiscal policy, taxing, and spending?

Secretary DILLON. That is correct. I think that is roughly what we are trying to do, anyway.

Representative REUSS. Yes. Now let me ask you this: To what extent, if at all, is this country going to have to alter its monetary policy in the months to come because of the balance-of-payments situation?

I will put that question in another way: Are we going to have to have credit tighter and interest rates higher because of the balance-of-payments situation than we would have based purely upon domestic considerations?

Secretary DILLON. I would see no reason whatsoever in the balance of payments to have credit any tighter than we would otherwise have it. There may at some time be a balance-of-payments reason to have short-term interest rates higher, but with plenty of credit available at those rates.

In many countries abroad, the higher rates have been connected with tighter credit at home, with the objective of reducing consumption at home so that there would be a greater incentive to export.

I do not think, with our present situation of unused capacity and unemployment, that is a type of policy that would be suitable at all, and I do not think any of the monetary authorities in Europe or anywhere else think it would.

On the question of the interest rate, as I have pointed out, some funds are still moving abroad in the short-term area because of their ability to get a higher return on time deposits and things of that nature than they can in this country. It is conceivable that if this should continue it may become advisable at some later date, or possibly become necessary at some later date, to take some sort of action which would lead to an increase in short-term rates here to offset that.

Representative REUSS. Well, I thought I was cheered by what you were saying. I want to be sure that I have cause to be as elated as I want to be. If all you mean by some action to raise short-term rates is a continuation of our present policy, the policy adopted within the last year, of seeing that within a given interest rate structure short-term rates are allowed to rise a higher percentage than long-term rates are allowed to rise, then I think it can indeed be said that we do not propose to tighten credit or raise interest rates overall because of the international balance-of-payments situation.

There are those, however, who have been quoted as saying that since money is attracted abroad by higher interest rates, therefore, we ought to raise our whole interest rate structure. And I think I understood you as saying that this we would not do. If so, I am glad to hear that.

Secretary DILLON. It may not have been quite that. What we would say would be that, under certain conceivable circumstances, we should direct our efforts at obtaining, by one means or another, possibly by an increase in the rediscount rate, a higher level of short-term rates. And we would hope that by leaving plenty of reserves available, the differential between short- and long-term rates would continue to narrow, as it has in the last year.

That does not mean that there might not also flow from any such increase, if that became necessary at all, some increase in longer term rates, but we would certainly hope that that increase would, in accordance with the basic policy which you have enunciated, be less than the increase in shorter rates and less noticeable.

And we certainly, by keeping credit available in substantial quantities, would think that it would still be perfectly profitable for industry to move ahead and finance at that rate.

Representative REUSS. But you have suggested that we might have to be prepared to see long-term rates go up as an incident to a raising of short-term rates.

Secretary DILLON. This might conceivably be necessary, if this short-term outflow continues, and if it results in a greater drain on our gold stock. One of the good things last year was the very small amount of that drain. We lost a total of some $850 million in our overall gold stock. The exact loss was $857 million in the year. Of that, some $325 million went out during the month of January, which was a continuation of the flight of capital of the previous fall. So from the 1st of February on, we lost under $550 million; and during that same period we incurred the entire deficit in our overall balance of payments of $2½ billion since there was no payments deficit in January.

So the gold loss was a very small percentage of the deficit compared to the percentage in the years before.

Representative REUSS. What are you saying, though, I regret to say, is that for balance-of-payments reasons we are prepared to raise short-term interest rates in order to keep money at home; and while we do not want this to increase long-term interest rates, it may well and probably will do so, and do so at a time when a monetary policy designed for maximum production, employment, and purchasing power at home would call for lower rates.

Secretary DILLON. Stable rates, anyway. Certainly last year in the long-term markets it is very significant that the overall amount of financing of mortgages, State and municipal bonds, and corporate bonds reached a new alltime record at the rate level that we presently have. It shows that borrowers are willing to pay that price, and big volume is moving at that price.

Representative REUSS. My time is almost up, but in my second round I would like to explore with you whether it is really necessary to let this rather small tail, short term capital wag the economic dog and keep us from doing those things which you say are so necessary.

Secretary DILLON. I would be glad to discuss that further. I certainly would agree with you in hoping that it would not be necessary. I merely said that conceivably at some point this could be necessary.

Chairman PATMAN. Congressman Widnall?

Representative WIDNALL. Mr. Secretary, as a fellow New Jerseyite, I am certainly very pleased to see you before the committee today.

Now, in your testimony about the savings and loan taxation, you said something about a reasonable transition period. What do you have in mind when you say that? What is "reasonable"?

Secretary DILLON. We had in mind, if someone asked us what that was, that we would respond that a 3-year period seemed reasonable to us, but if someone else thought a 5-year period was acceptable, that would be reasonable, too.

Representative WIDNALL. You mean to step up the requirements for the savings and loan industry over a period of 5 years?

Secretary DILLON. Over a period of 3 to 5 years. We would prefer 3 years, but if it was felt that 5 was preferable, there is not much difference.

Representative WIDNALL. In speaking about new sources of tax revenue, you mentioned the mutual savings banks and the savings and loan industry. You did not say anything about cooperatives. Was that intentionally omitted?

Secretary DILLON. No. I just was answering questions, and I mentioned that we were trying to achieve equality everywhere. In this present bill, in addition to mutual savings banks and savings and loans, which are of course much the biggest item of this nature in the bill revenuewise, there are also provisions for taxation of cooperatives, and also for taxation of mutual casualty and fire insurance companies, which will provide that these two types of institutions bear their full share of the national tax burden.

Representative WIDNALL. Actually, as some of the cooperatives have grown into monsters, they have gobbled up much private business in many areas and eliminated a lot of tax revenue from private business. And their shareholders in many instances get very good dividends at the end of the year.

If the administration is emphasizing the increased responsibility of mutual savings banks and the savings and loan industry, I wish they would place the same emphasis on cooperatives, which are having a very fine time taxwise at the present time.

Secretary DILLON. I do think they do that, Mr. Widnall. Actually, in the original presentation of the administration position last year to the Congress in the Ways and Means Committee, we had specific proposals for cooperatives and for mutual casualty companies and did not have for savings and loans and mutual savings banks. That has only been developed as a result of later studies, which is maybe one of the reasons it is in the forefront today in the news. But the bill has had in it since last summer, and reaffirmed by recent decisions, substantial taxation of cooperatives, which you are interested in.

Representative WIDNALL. Now, what would happen to dividends on service life insurance policies? Would there be withholding on those dividends?

Secretary DILLON. I would have to answer that specific question for the record, because I am not sure taxwise whether those are actually dividends, or a return of payment.

There is a provision for withholding on dividends paid by life insurance companies on funds, interest-bearing funds, that are left with the life insurance companies. That is the only provision that I know of. And I would not think that these dividends were in that category, but I would be glad to give you an answer to that for the record.

(The following was later received for the record:)

There would be no withholding on dividends paid to policyholders of National Service Life Insurance contracts. This is because dividends paid to these policyholders are not taxable income but rather are considered a return of premiums. "Dividend," for purposes of the withholding tax, would be defined as any distribution made by a corporation which is a dividend as defined in section 316 of the Internal Revenue Code. Section 316(b)(1) specifically provides that the definition of the term "dividend" in section 316 does not include dividends of insurance companies paid to policyholders.

Representative WIDNALL. In placing the age exemption up to 18, what is to prevent a person of affluence placing large sums of deposits in a number of savings and loan associations, in the name of a child, and thus avoiding the tax?

Secretary DILLON. They would be avoiding withholding. They would not be avoiding tax liability. It would be fraud if they did that.

Representative WIDNALL. But there would be no reporting?

Secretary DILLON. There would be no withholding and no reporting unless it exceeded the reporting requirements, which are presently $600 per year for interest. So if it was up to $600, it would not be reported. If it was over that, it would.

Representative WIDNALL. Now, to get to the balance-of-payments question: a statement was made, I believe, by the President in his message on trade, that we had a $5 billion export surplus: Does that not include nonsales, like agricultural exports?

Secretary DILLON. I think that the figure the President gave does include that.

The figure not including that for the past year, in our exports, showed a surplus of about $3 billion. That is in merchandise trade. We also have a surplus in services. And our total commercial surplus of goods and services I think was between $4½ and $5 billion.

Representative WIDNALL. Would not that amount be further reduced if we inventoried the exports from the United States on an f.o.b. basis rather than a c.i.f. basis? We are inventorying the imports to the United States on an f.o.b. basis?

Secretary DILLON. I am afraid I cannot answer that question. I do not know how it is inventoried.

Representative WIDNALL. I think there is about a 20-percent or 25-percent differential, if we considered our exports and imports on the same basis, and the 25 percent is unfavorable to us. And I wish you would give the viewpoint of the Treasury Department on that and submit it for the record.

Mr. Chairman, may we have that for the record?

Chairman PATMAN. Certainly.

Without objection, it is so ordered.

That is agreeable with you, is it not, Mr. Secretary?

Secretary DILLON. Certainly. This is a new question for me.

(Information referred to follows:)

The U.S. balance of payments statistics show both the value of exports and of imports on an f.o.b. basis. In this manner the cost of the goods can be differentiated from the cost of shipping and insurance and payments or receipts between the United States and foreigners in these accounts appropriately recorded.

If a U.S. ship carries the goods being imported into the United States there is no foreign transaction involved and no entry need be made for the shipping costs in the U.S. balance of payments. If a foreign vessel carries the goods being imported into the United States, the cost of the goods at the foreign port is shown in the statistics as an import payment (f.o.b.), and the shipping cost is shown as a payment or a debit in the transportation account of the balance of payments.

Similarly, in the case of an export the value of the goods at the port of export would be shown as an earning or a credit on merchandise account. If a U.S. ship carries the goods to the foreign purchaser there would be earnings reflected in the balance of payments as a credit in the transportation account. If a foreign vessel carries the goods being exported there would be no transaction involving the United States and no entry in the balance of payments. The same kind of treatment would apply to the insurance.

If the census method were changed for some reason to go to a c.i.f. basis an adjustment would be required in the balance of payments statistics to bring the export and import figures back to an f.o.b. basis just as these data are shown now. It should be noted that the balance of payments manual of the International Monetary Fund provides for reporting exports and imports valued f.o.b. the exporting country.

Representative WIDNALL. That is all. Thank you.

Chairman PATMAN. Senator Proxmire?

Senator PROXMIRE. Mr. Secretary, you have had an unusual experience in positions of top responsibility in Government, and before that you were an outstanding leader in the financial world. Can you tell me any year, or preferably a series of years, in the past, when you would have recommended that the President program a larger surplus than presently proposed, because the outlook seemed to be more expansionary than your current projections are?

Secretary DILLON. In the past?

Senator PROXMIRE. That is right.

Secretary DILLON. I think we have had one difficulty in the past. There was one time when you could have had a very large surplus, and I think when we did have it, was in the years immediately after the close of World War II.

However, our problem is that for many years we have had a substantial amount of unemployment, and we have not operated—I mean for the last 5 or 6 years—at a rate of full employment or full capacity. We will not be operating there during calendar year 1962; even though we should be approaching it by the end, we are not anywhere near it now. Our revenues would be something like $5 billion more if we would be operating throughout this year at a 4-percent unemployment rate, which would be about $97 billion, or something like that.

Now, if we were operating at that rate, I should think we could have a substantially larger and should have a larger surplus than we are presently budgeting for in a year in which we are just moving up toward full employment.

Senator PROXMIRE. In other words, the justification, and the only justification, really, for such a small surplus in the booming year you are predicting is the substantial rate of unemployment. As I look back over the past years, since 1946, you are projecting a larger increase in the gross national product, percentagewise, than we have ever had, and the largest absolute increase by far that we have ever had.

In 1946 over 1945 there was a decline; in 1947 a decline; in 1948 an increase of 4 percent; in 1949 an increase of one-half of 1 percent; in 1950 an 8 percent increase; in 1951, an 8 percent increase; in 1952, 4 percent; in 1953, 4 percent; in 1954, a decline; in 1955, 8 percent; in 1956, 2 percent; in 1957, 2 percent; in 1958, a decline.

I am doing this, of course, in dollars, constant dollars, because you are assuming a constant price level, in the coming year.

In 1959 a 7 percent increase; 1960, a 3 percent increase; 1961, a 2 percent increase.

Now, in view of the fact that our past experience has indicated that this would be an almost unparalleled expansion of the economy, it seems to me unusual that we would program almost no surplus whatsoever, or a surplus of relatively small proportions.

Secretary DILLON. In the first place, I am glad you mentioned that this was on a basis of constant dollars.

Senator PROXMIRE. Isn't that a fair assumption in view of the position the administration has taken, that they assume we are going to have stable prices?

Secretary DILLON. No, I think this increase for next year or the figure for next year is estimated on the prospect of current dollars, and even this year, when we had general price stability, there was an increase in the consumer price index of about a half of 1 percent, and a somewhat larger increase in the GNP deflater. And I think there would be a similar increase, and there probably will be, this present year that we are in, because I cannot see that we will have a better record than we had last year.

On the basis of current dollars the increase in GNP in 1955 was $9\frac{1}{2}$ percent, and we are presently talking about in 1962 a 9.4 percent increase, which is an equivalent increase—somewhat smaller but an equivalent increase—and we do not think that what we are prognosticating is unusual for that reason.

Now, I think you are quite correct that the reason we are talking about a surplus that is not larger is that we are not yet at full capacity. Full capacity applies to use of facilities, factories, plant equipment, and it applies in the case of unemployment to the full capacity of labor. I think that is the reason, which you have put your finger on, that we do not budget for a higher surplus at this time.

Senator PROXMIRE. What concerns me particularly is that such a very heavy reliance is placed on fiscal policy. I feel, I think, as deeply as anyone, that unemployment is a very, very serious problem. I think you are right, as you indicated on "Meet the Press" a few days ago, when you said that you felt it was our most serious problem. I think I would agree wholeheartedly.

But I just feel that more reliance should be placed on monetary policy, more reliance on other programs, on manpower training, on any number of other things that we should consider more than we have, and less on trying to spend our way to fuller employment.

I would like to ask also: Can you describe the kind of a situation which would obtain, say, on January 1, 1963, for example, that might make it advisable for the President to put the discretionary personal income tax cut, which the administration is asking, into effect? In other words, what would happen to unemployment or to GNP to warrant such an action?

Secretary DILLON. Well, I would not want to set up a hypothetical situation, because each one of these situations is somewhat different. But I think that there probably is general agreement that certainly it has been the policy of every administration that has been faced with recession since the war, in every recession, that it is necessary to give some stimulus to the economy to prevent it from spiraling downward.

Now, the only stimulus that has been available so far has been increases in expenditures. Most of these can be increased only rather slowly—some of them rapidly, such as unemployment insurance, which is an automatic stabilizer—but ordinarily other expenditures take some time to increase, and quite frequently the full impact of the increase only comes after recovery is well underway, and maybe at a time when it is too great a stimulation. This is probably what occurred in 1959, when we ran that very large budget deficit.

And there is, I think, a very general feeling that a tax reduction, a temporary one, for a period of some 6 months, could give the type of stimulus that is needed to the economy at a long-range cost that probably is less than increasing expenditures to a level from which it probably is very difficult to reduce them in the future.

I think that is the reason that we think this is such an important tool and that it has been favored by the Commission on Money and Credit, a distinguished organization of private individuals that spent 2 or 3 years studying this matter, and lately has been favored by the Committee for Economic Development.

Senator PROXMIRE. I recognize this proposal has support. But I am trying to get a picture of the fiscal situation to our Government. What would actually happen if this tool were used? This is really a reliance, and a very heavy reliance, on compensatory fiscal policy to pull us out of a recession.

Secretary DILLON. It certainly would cause a budget deficit, but I do not think it would cause necessarily any larger budget deficit than a combination of increased expenditures with falling revenues, which has been characteristic of the last two recessions.

Senator PROXMIRE. What I had in mind was that if we had this situation, say, in fiscal 1959, presumably that might be the kind of a situation where this might be used; a $5 billion tax cut on top of the $12½ billion deficit we had would be an extraordinarily big and burdensome and crushing deficit.

Secretary DILLON. I quite agree with you, and maybe the answer is that we have never assumed that this would be over and above a deficit such as that $12½ billion. We have thought that it would be in lieu of some of the increases in expenditures, which were very substantial, something like $8 or $9 billion that year, some which were incurred merely for the purpose of stimulating the economy. That would not be necessary.

Senator PROXMIRE. Isn't that exactly the kind of a situation in which you would be using this discretionary tax cut; when you already have a very serious deficit, automatic deficit?

Secretary DILLON. Automatic, yes. But we would use this, instead of increasing that automatic deficit, by having new programs that would cost a lot more money at maybe a later date, when they would not be as effective.

Senator PROXMIRE. My time is almost up.

Also in your statement you talk for, or at any rate the administration certainly asked for, discretionary spending authority so that they could move ahead on that front, too.

Secretary DILLON. That is correct. But what we are trying to do there is to limit it very strictly to certain kinds of projects that could be gotten underway very rapidly and terminated very rapidly. So this would be strictly limited in amount and it is nowhere near as large as, for instance, the programs that were undertaken in 1959, and which led to expenditures, many of which came to fruition a year after the bottom of the recession.

Senator PROXMIRE. My time is up, Mr. Chairman.

Representative REUSS (presiding). Mr. Pell?

Senator PELL. You suggest in your testimony that even more important than the gross national product from the viewpoint of growth of the country is the percentage of capital investment that goes along with it. I was wondering if any study had yet been made, or analysis, as to whether the trend was going up or down or staying static during the last 12 months.

Secretary DILLON. I do not think there is anything we have found that seems to be conclusive as to any long-term trend in that short period of time. It is clear that during recent years the trend has been somewhat downward as a percentage of GNP.

In the last 2 years we have seen a decline, and we are now seeing an increase in capital investment, but traditionally that sort of increase lags somewhat behind in the recovery. It is not the first thing that companies do. They usually wait until they find more need for it as the recovery has progressed.

So I would think percentagewise there would not be any improvement for the past year as a whole because the first part that we see is an improvement in our GNP and in our general economy, usually not matched by an equivalent increase in investment spending. But the indications are that as profits increase, which they have now, and the cash flow to companies increases, there will be a more substantial increase in investment, and that would begin to take effect in spending maybe next fall.

Senator PELL. Do you feel that the tax credit measure and depreciation measure that you propose will be adquate to encourage a trend toward increased capital investment which would help to fight the return of recession?

Secretary DILLON. The answer to that is that these two measures combined—and we have made a full and careful study of this—would put our industry as a whole on an equivalent basis to the industries of Western Europe, and they have been investing more relative to their gross national product.

Now, you can also go beyond that and look at the time when certain of those countries introduced similar measures, and it shows that with the introduction of those measures their investment went up. So I presume the same thing will happen here, and we think that this is an adequate answer to this one problem.

Now, of course, another element in the equation is the need to maintain our economy moving at a reasonable speed, so that there is adequate demand, so that people can sell their goods.

Senator PELL. In connection with capital investment, I wonder if thought has been given in the Treasury Department as to the present sterile policy of investments made by pension funds of unions. Generally there is not too much knowledge as to how these funds are being invested.

Have you any view—I know Mr. Heller did not—as to what the appropriate agency of the Government is to supervise those, and have you given any thought to how those investments could be used more productively in capital investment?

Secretary DILLON. No, but that is one area, as Mr. Heller so stated, that is in the economic report, where we have established an interdepartmental study group to study this whole area of pensions to answer just that point, as to whether they need further regulation, and if so, what agency of Government should be the proper one.

This is one of the recommendations, one of the main recommendations and important recommendations, again, of the Commission on Money and Credit, which we have not accepted as yet, but we have accepted that this is something which needs study, and it is very complex, and we are going to study it.

Senator PELL. Going for a moment to the question of the withholding tax, I wonder what your opinion would be about continuing to enforce the filling out of form 1099's and 1096's for reporting the income paid if there is an automatic withholding tax. Would both be done?

Secretary DILLON. I am glad you mentioned that. I think the reason for filling it out, in the case of interest, is still obvious. It applies presently to interest payments only of $600 or more. That is fairly substantial and would indicate that the person who received that might well be in a tax bracket over the 20 percent bracket, so that these information returns could be helpful.

On the other hand, dividend returns or information returns are presently required on all payments of $10 or more. And I think, although we haven't decided exactly what the right level would be, it would be the intention of the Internal Revenue Service, after this law goes into effect, assuming it does, by regulation to raise that cutoff limit to a more appropriate level and relieve the dividend-paying companies of the necessity of filing form 1099's on a great many of the dividends they now file them on.

Senator PELL. Would you be willing to hazard a guess as to what a more appropriate level would be?

Secretary DILLON. It might be $100. It might be $300. It might be something of that nature. It will require some studies, which are presently underway, as to the pattern of these reports.

I think this is one of the things we can do to greatly simplify and I think maybe reduce by 50 percent the number of these forms that are required to be filled out by dividend-paying companies.

Senator PELL. Has any study or estimate been made of the estimated cost of withholding to banks, and financial institutions, and brokers.

Secretary DILLON. I do not have any figures for it. We have had estimates of varying amounts. Nobody seems to have come up with any figure that is a very solid figure on this. We have had testimony, which varies widely, depending on the individual that gives the testimony. And these are bankers. Some bankers feel it will cost a lot more, and another one equally competent feels it will cost very little.

Senator PELL. But you could not hazard a guess whether the cost would be $10 million or $100 million to the industry?

Secretary DILLON. I do not think it would be anything like $100 million, and I doubt if it would be as much as $10 million.

Senator PELL. Including the cost of new machines, and of personnel?

Secretary DILLON. I do not think that there would be any need for a lot of new machines or personnel here. The basic system in the bank is that they would just take all the accounts of people between 18 and 65 and subtract 20 percent from the total figure and send the Government a check.

Senator PELL. And one final question on this general subject of withholding: If there is going to be any system of segregation for youngsters under 18 or people over 65, why could not the same system be used for tax-exempt institutions?

Secretary DILLON. It is. I did not go into all the details. This is a complex bill. Tax-exempt institutions, State and local governments, also have exemptions.

Senator PELL. Hospitals and public libraries and institutions of that type—would their income not be withheld?

Secretary DILLON. To the extent that it is in banks and savings accounts and time deposits or anything of that nature, where an exemption certificate would work, it would not be withheld.

Senator PELL. But not with dividends?

Secretary DILLON. It is not possible with dividends, but there are special offsets provided for tax-exempt institutions. These would apply particularly to hospitals and colleges, where they could offset this withholding against the amount they are required to withhold themselves on salaries of their employees, and so forth; so that they have really an automatic immediate offset. There would be no tax impact on institutions of that kind, no unfavorable impact.

Senator PELL. One final, very general question: Have you ever thought of the danger of our being dependent on the gold standard, as we are, when the source of production of gold is either in a country with which we are engaged in battle or a country where there is great unrest? I was wondering if thought has been given to gradually removing our close links with the gold standard.

Secretary DILLON. Well I think that the general feeling is that the gold exchange standard that we presently have, particularly after the very close examination and all the attention that has been given to it in the past years, is the best thing that has been devised. It may be possible sometime in the future to make improvements on it, but I think the general feeling in the world is that this is a workable system and can work fine.

Now, should south African gold, which you mentioned, suddenly become unavailable for an extended period of time to the world, certainly that would pose very real problems, and I do not know just what the answer would be.

Senator PELL. And if the Soviet Union sold its reserves?

Secretary DILLON. I do not think, if the Soviet Union sold its extra supply, that would cause any particular problem. I think the world could easily absorb the extra Soviet stocks.

Representative WIDNALL. On January 29, 1962, Mr. Secretary, the Wall Street Journal editorialized under the heading "Political Magic." I would like to read from that editorial and invite your comment:

> Perhaps the weirdest shibboleth is a good old gross national product. It is truly wonderful what sematic tricks Government economists can play with this supposed measure of the Nation's total output of goods and services. For one thing, they can show you that Federal outlays are stationary or even declining as a percentage of GNP, when the plain fact of the matter is that they are increasing hugely.
>
> One reason the GNP lends itself so shamefully to such verbal legerdemain is that it includes Government spending as part of total output. Since most Government spending is nonproductive, that is an erroneous device, but it makes things easier for economic advisers. Let Government spending increase. They can point to a rising GNP, and hence, presto, economic growth.

What observations can you make with respect to that?

Secretary DILLON. I would say that at the time there is an increase, there is nothing remarkable about the situation at all. GNP, for instance, this year is increasing very rapidly, and we expect an increase from $520 billion or $521 billion up to $570 billion for the year. During the year, Government expenditures will also increase, but they will not increase percentagewise as much as the 9- or 9½-percent increase that is looked for in gross national product.

So it is no surprise that Government expenditures can increase and still maintain themselves at the same proportion, or actually a declining proportion, as will be the case in fiscal 1963, when Government expenditures will be a smaller proportion of the GNP than they are this year, in 1962.

Now, the GNP concept is a concept that was first developed in this country some 30 years ago in detail. It has been regularly used since by the Government, and it is something that is used by technicians, highly competent technicians, in the Department of Commerce, and it certainly is thought by economists to represent the most useful measure that can be devised of the total product of goods and services of the United States.

Now, certainly it is not correct at all, as stated by the Wall Street Journal, that a great part of Government expenditures are unproductive. If they talk about them being unproductive in the sense that they are not manufacturing industries and they are not producing anything that way, that is correct; but if they talk about them as not being a needed service, part of the goods and services of the United States, that is totally erroneous. Certainly the tax agent that we pay in the Internal Revenue Service is a very necessary individual. The postal clerk who delivers your mail is a very necessary individual. He may not be productive, but I cannot contemplate how our system would operate if there was no postman to deliver the mail. And that is what, in effect, the Wall Street Journal was saying by saying you should not count Government expenditures as part of the goods and services of the United States.

Representative WIDNALL. Of course, over 10 percent of our budget today is interest on the debt, so that we certainly have an interest in the amount of the debt. And as that mounts, it is going to take a bigger and bigger percentage out of the taxpayer's dollar.

I heard a rather interesting colloquy at the beginning of these sessions, in which Congressman Bolling and Professor Heller were saying there is nothing sacrosanct about a budget balance. I think this fails to recognize the tremendous amount that we have to pay just in interest on the public debt.

Secretary DILLON. Of course we have to pay a very big amount. This arose as a result of a substantial increase in the debt during World War II.

At the end of World War II, our total debt amounted to 130 percent of our gross national product, and therefore, the interest on that debt was a heavy burden. Since that date, our gross national product has risen steadily, year after year, in the 15 or 16 years since the war, and is now something well over double what it was at that time, whereas our debt has increased only slightly. The result is that at the end of next year, for the first time, on our projections, since 1941, I think it is, the debt will be back, as a percentage of gross national product, to just about what it was the year before the war, 1941; namely, 50 percent of our gross national product.

So the debt at 50 percent of our gross national product is an easier debt to carry by far than the debt was after the end of the war, when it was 130 percent of our gross national product.

Representative WIDNALL. That is all. Thank you.

Representative REUSS. Mr. Secretary, I would like to return to the subject we were exploring before; namely, the thesis that it may be necessary for the monetary authorities to have a higher interest rate structure in this country than would be desirable from the standpoint of domestic maximum employment without inflation, because of our international balance-of-payments position.

I know that thesis disturbs you, as it does me, and I would like to explore it with you.

The first question I would raise is this: Do we really know that there is a close relationship between differential interest rates in the developed countries and the movement of short-term capital? From my own look at the picture, I many times find that there does not seem to be any relationship at all.

For example, in the second quarter of last year, the average short-term interest rate on 90-day bills in this country was 2.32 percent, and it stayed the same in the third quarter. Overseas, however, in Canada, Belgium, France, Germany, among other countries, short-term rates declined in the third quarter as opposed to the second quarter.

Despite this decline, despite the fact that short-term rates in this country and abroad seemed to have drawn considerably closer together in the third quarter than in the second quarter, actually our short-term outflow in the third quarter was at an annual rate of $916 million, about double what it was in the second quarter.

I could give many other examples like this to show that there is an inverse relationship, if there is one at all, between interest rates and the movement of short-term capital.

I therefore ask you: Has there really been a thoroughgoing study of the correspondence between interest rate differentials and short-term capital movements? And if so, can you give me the benefit of that study, so that it can be filed with our committee records?

Secretary DILLON. Well, I would like to just make a few observations.

In the first place, I think the thesis that you were trying to make does not rest on these particular figures. There actually were very few, if any, short-term outflows in the third quarter; they were substantially less than in the second quarter; and the short-term outflow that developed did develop in October and November rather than during the third quarter; but I think the same comments that you made still would apply to that.

Representative REUSS. In other words, interest rate differentials were, if anything, smaller in a period when the flow was greater.

Secretary DILLION. That is correct as far as short-term Government securities, the bill rates, are concerned; and it is quite true that there is no longer, I would say, and there has not been for nearly a year, any real differential in that area at all.

That does not mean that there are not interest differentials that are attracting short-term capital flow abroad.

One of these is the fact that banks abroad are prepared to pay, and have been paying, higher interest rates on time deposits than our banks are permitted by regulation to pay, and considerably higher, as much as 4 percent and in some cases slightly over 4 percent, as compared to 3 percent, which was our maximum by regulation. That has now been lifted to 3½ for deposits with a term of 6 months to a year, and I think most of our banks have answered by raising their rates to about 3¼. But there still is a substanial difference there.

There also are differences in certain kinds of investments, investments in paper that finances installment sales in Great Britain, called hire-purchase paper. Also in Great Britain they have a financial system or financial practices somewhat different from ours, in that their municipalities and townships make a practice of financing some of their permanent improvements on a very short-term basis, with 90-day funds; and these presently are bringing 6½ to 7 percent in the London market.

Now, some of our banks and corporations have become aware of this, and their funds are flowing into these different areas which are more sophisticated than implied just by the straight comparison of Government bill yields. So there are still funds flowing out.

This flow of funds, which I mentioned in my statement, to Canadian banks last fall was due to the fact that they came down here and actively sought deposits and agreed to pay a higher rate of interest than our banks could pay. It was no great surprise that some of these funds went to Canada; and actually they were then returned in good part by Canadian banks to the United States money markets and reinvested here. The Canadian banks were just willing to take a smaller margin than our banks operate on, between what they paid to the person who deposited with them and what they charged to borrowers.

Representative REUSS. In your discussion of the problem of outflow to Canadian banks, you made the following statement, and I quote:

> There are serious questions whether our conventional classifications of short-term capital flows accurately reflect their true significance for the balance of payments.

I myself have been appalled from time to time by these enormous amounts called errors and omissions, which show up in our accounts, indicating that the science of balance-of-payments statistics is still in a rudimentary form.

If this is so, and if we have not really made a thoroughgoing and sophisticated study of the extent to which, if at all, short-term capital really does flow because of interest rate differentials, isn't this a frail reed indeed on which to base a policy of having less than full employment and less than maximum growth in this country?

Secretary DILLON. Yes. That is why, as I say, we are studying this matter very seriously.

I think I could expand on this a little to show what we mean. To give an example of this situation, take this Canadian situation.

An American company, call it company X, has some free funds which it wishes to invest as a time deposit, and it finds that it can receive at the Canadian bank half of 1 percent or three-quarters of 1 percent more in interest than it receives from a big bank in New York. So it moves part of this deposit over to the Canadian bank, and this is then registered in the head office of the Canadian bank in Canada as a deposit by the American company.

Thereupon the Canadian bank promptly transfers these funds back to its agency in New York, and that agency turns around and lends it out to another American company, or lends it out in the call money market in New York at, say, 4½ percent, and it makes only a half a percent differential.

In those cases, the result is that the money in effect has never left New York. It is still being used in the New York money markets and has no effect on the exchanges to lift or change the exchanges, but it is recorded in our balance-payments statistics as an outflow.

And the reason for this is because the outflow is the deposit with the Canadian bank that has the right to recall it at any time.

The real problem is that we in the United States set up our balance-of-payments accounting on the basis of a situation when we had the only convertible currency, and there were no other convertible currencies in the world, and we provided for ourselves rules that are far stricter than those used by any other country, and far stricter and far different from those used even by the United Kingdom, which has another world currency, sterling.

We do not count our private liquid assets in foreign currencies and convertible currencies as an offset to our liabilities as many others do. We do not count it as an offset to the deficit. But we do count any foreign liquid dollar holding or short-term holding of our dollars as a liability and part of our deficit.

And those are the two things that are possibly somewhat inconsistent, because if we wish to change our interest rate structure, it is perfectly clear that a great amount of these short-term deposits would come back to the United States, and could be called back immediately.

Representative REUSS. My time is up, but I would summarize this phase of our discussion by saying the following: That it does appear that our accounting systems for balance of payments, short-term capital movements, are so out of date and superconservative that they might well lead us into thinking that short-term movements were worse than they were. And if deflationary action with respect to this country's domestic economy were based upon such rudimentary statistics, this would be a most unfortunate thing, would it not?

Secretary DILLON. I would say "Yes." And that is the reason, as I stated, that we are studying this in conjunction with the Federal Reserve and the Federal Reserve Bank of New York just as rapidly as we can, in the hope that we can see whether there are any improvements that should be made.

I do think that there is some case for a more conservative policy on the part of any currency which is a basic world currency, such as the dollar, or sterling, but, as I say, our accounting is even far more restrictive and shows a worse picture than the accounting that the British use for sterling.

Senator PROXMIRE. On that same Meet the Press program I referred to, you were asked about what you considered the most important problems facing us, and you listed three, employment, growth, and balance-of-payments.

Possibly because I come from Wisconsin, but also for other reasons, I am concerned that you might think about another problem that is not in your statement today, either, and that is the farm problem. I consider this an extremely serious problem, not only from a fiscal standpoint, which we all recognize, but also from the standpoint of just plain economic justice. And I am wondering if there is a feeling in the administration at all that this problem has either taken care of itself or that it is of a lesser order than some of these other things.

Certainly in my State, and I can see this from my experience on the Agricultural Committee elsewhere, it seemed to me to be still extremely serious and very perplexing and a long way from solution.

Secretary DILLON. No, I was merely talking from the standpoint of the overall economic or overall financial situation that particularly confronts me. I think that was the way that the question was phrased as it came to me.

But certainly in that overall situation, the health of our agricultural sector of our economy is vital, because it is a very large and important sector of our economy, and where a good many millions of our people work.

And it is today, as I understand, that the President is sending up his message and his program for agricultural reform, and as I understand, it is a very thorough and wide-reaching reform which he feels will bring benefit to the agricultural regions of this country.

Senator PROXMIRE. I ask this question particularly because it relates to what Senator Douglas asked earlier, about the importance of considering the American farm economy with relationship to the Common Market problem that has been so serious there.

Now, in your statement, you say:

> In sharp contrast to other recovery periods since World War II, lending rates have held almost steady, particularly in the long-term area. Both corporations and State and local governments can still raise funds at virtually the same cost as a year ago.

I think this is commendable, and I for one am very happy to see it. At the same time, I also recognize that that steadiness is at a pretty high level. It is at a higher level than it was in two of the past three postwar recoveries and not far below the other.

I am just wondering, in view of the unemployment problem and the fact that we are pushing fiscal policy about as far as we can, if perhaps a more aggressive monetary policy might not be appropriate.

Secretary DILLON. Well, I think that the question that is always hard to measure is: How high is high? The problem here is that over the past decade we have been gradually adjusting to normal market rates, from the rates that were controlled rates during the war, and for the 5 or 6 years thereafter, and that adjustment just naturally did not all come at once.

I think the answer as to whether in their effect on the economy these rates were too high is clearly in the negative, as shown by the fact that the volume of mortgage lending, of financing by State and local institutions, and by corporations was, as I said, an alltime record last year, and there is every indication that that record flow of funds is continuing. So it indicates that borrowers do not seem to feel that current rates are too high.

Senator PROXMIRE. Well, except for the fact that we have an expanding economy—I presume it would be possible with even higher interest rates to have a big volume of borrowing and so forth.

I am just wondering what you have in mind by "normal rates." It is true, I recognize, that rates were perhaps artificially too high, in the period of the 1930's and the 1940's. I do not want to discuss it in terms of that. I recognize that would not be proper. But at the same time, they do seem to be quite high even in relationship to the 1950's. And I am anxious to get any kind of influence the Government can exert other than this fiscal policy, which I think is the most burdensome of all in the long run, to help expand our economy.

Secretary DILLON. I think that the rates we presently have here in the long-term area are certainly still well below or below the rates that are generally prevalent in Western Europe and the Common Market countries that have shown very rapid and tremendous growth; so I do not think that they are rates that can be said to be inhibitive——

Senator PROXMIRE. That is what is used all the time, but is it not true that France, Germany, and Italy do have an entirely different problem? They are recovering from a war period in which their economies were devastated. They had a fantastic amount of reconstruction to do. And now they have the great advantage of having built plants that are newer than ours and are maybe more efficient than ours in many ways, and they have that moving for them.

At the same time, if you compare our rates with Switzerland and compare our rates with what we have had in the past, compare our money supply with the gross national product as compared to what it has been historically, it seems that if we are really going to move ahead and expand and encourage our economy at a time when we have heavy unemployment, without putting too heavy a burden on fiscal policy, far more consideration might be given to an expansionary monetary bill.

Secretary DILLON. I just wanted to mention on the money supply—you mentioned that—that during 1961 the money supply in this country increased by about 4 percent, which was slightly more than the year-by-year increase in gross national product.

Senator PROXMIRE. At the same time, it was one-half the increase in the gross national product during that time.

Secretary DILLON. The gross national product from year to year increased about 3½ percent, and the money supply from the end of 1960 to the end of 1961 increased about 4 percent.

Senator PROXMIRE. I beg your pardon. I mean in terms of the last gross national product as of the last quarter of 1960 and as of the last quarter of 1961. It seems to me it increased about 8 percent. It is now $540 billion. It was just above $500 billion.

Secretary DILLON. That is correct.

Senator PROXMIRE. And therefore the increase in the money supply did not keep pace. For this reason I would contend that there has not been an expansionary impact on the economy through actions of our monetary authorities.

What I have in mind particularly is the activity of the Treasury and the Federal Reserve Board with regard to buying and selling Government securities, the portfolios of each. I notice that the Federal Reserve Board increased its holdings of over-10-year securities, from June to September, the only figure I have got, unfortunately, and also 5- to 10-year securities.

The Treasury, I presume, influences U.S. Government agencies in trust funds as an adviser, and it increased by a billion dollars its over-10-year holdings, which I think is appropriate and proper under the circumstances, but it decreased holdings of obligations with maturities between 5 to 10 years.

Secretary DILLON. I think what probably happened there—and it happens often—is that just by the passage of time certain securities move from 5- to 10-year category into the 1- to 5-year category. I do not think that that, probably, represented active selling and buying operations, switching from one to the other, at all. I do not know of any such operations on the part of the Treasury or the trust accounts.

We did make these substantial long-term investments, and we thought that those were appropriate, because we could get a higher interest rate for the trust fund, which is, as trustees, what we should get—a better return.

And there was no reason why a proportion of these long-range trust accounts should not be in long-range bonds, because their obligations will not come due until many years ahead. So we thought that was perfectly proper.

And we in the trust accounts assumed, in cooperation with the Federal Reserve, the main burden of purchasing out in that long area, whereas they assumed the main burden in a somewhat intermediate area.

Senator PROXMIRE. Are you trying to follow a policy of buying the long-term securities to keep those rates down and perhaps selling as much as possible the short-term securities to safeguard our balance-of-payments situation?

Secretary DILLON. I think, as has been pointed out, the objective was to try to use whatever tools we had to maintain a short-term interest rate at a level that would prevent outflows; and at the same time to use whatever influence there was so that long-term rates did not go up in the same amount. And that has been successful, because the gap between short-term and long-term rates has been narrowed by a one-fourth of 1 percent or more in the past year.

Senator PROXMIRE. Now, you say:

> Without raising tax rates an advance of this sort will generate revenues slightly larger than expenditures. Under the economic conditions we foresee, the achievement of such a balance is highly important in avoiding inflationary pressures as the economy moves closer to its full potential.

You go on to discuss the impact on the budget and economy, and I am wondering why the national income accounts budget would not be a far more appropriate budget than the administrative budget, in view of the fact that it includes transfer payments, and particularly since it shows that this budget in fiscal 1963 may be somewhat conservative as compared with past budgets. That is, it shows a surplus of $4½ billion, including everything.

Secretary DILLON. Yes. I think that certainly from the point of view of its economic impact and economic effects, national income and product accounts are probably more accurate, or they are the best tool we have. That was I think pointed out primarily by the members of the Council of Economic Advisers, and I dealt primarily with administrative budgets, because that was the budget that the Treasury is usually a little more closely associated with in the public mind in handling revenues and receipts rather than income and product accounts.

But I certainly agree with what you have to say.

Senator PROXMIRE. I think it would be very helpful—Mr. Bell seemed to feel the same way, and I am sure the economic advisers feel very strongly about it—that we get as much discussion and debate in terms of the national income accounts as we can, because we miss so much in not recognizing the effect.

Secretary DILLON. I thoroughly agree with you; and that was one of the reasons why we included in the budget document itself the figures on the national income and product account; so that anyone who read that could see both of them.

I think this is the first time that was done, and we think that is a very useful and helpful thing. But it does require education to get people to understand it.

Chairman PATMAN (presiding). Senator Pell?

Senator PELL. Mr. Secretary, I have just one question.

I notice you give the figures of capital investment for the Western European countries and our own. I was wondering if there was any estimate of the capital investment in the Communist countries, in the Soviet Union.

Secretary DILLON. Well, that is a very high figure. I think it probably runs 15 to 20 percent on a comparable basis and maybe even over that.

Senator PELL. The difference between that and Western Europe is probably just as marked as between Western Europe and us?

Secretary DILLON. I would think so, yes.

Senator PELL. Thank you. No further questions.

Representative REUSS (presiding). Senator Proxmire?

Senator PROXMIRE. Yes; I just have a brief question.

You discuss this tax credit for investment. I am wondering in the first place: Relatively how important is that tax credit as compared with the depreciation reforms which you have been making in the Treasury, and which you anticipate in your statement here you intend to make in the future? Can you give us any order of significance in terms of the impact, (*a*), on revenue, (*b*), on investment?

Secretary DILLON. I think it is difficult to give an exact figure, because our studies regarding reform and depreciation guidelines should take effect with revisions of Bulletin F later in the spring, but are not yet completed. So I do not want to indicate, I cannot indicate, what the answer is going to be.

But the only thing I can say is that if the answer comes out relatively the same as it has in the textile industry—and it may or may not—then the revenue cost of a change in the guidelines would probably be approximately equivalent to and equal to the gross revenue cost of the investment credit.

Both of these items will stimulate further investment, we feel, so that the net cost will be considerably less.

The second question you ask, "Which would be the greatest stimulus?" I think without doubt the investment credit would be a somewhat greater stimulus, because in the first place it is only available for expenditures for modernization of equipment, whereas the funds that are available, that would become available, from a change in guidelines, is spread across the whole gamut, and some of those would not be used presumably for modernization, but would be used maybe to increase dividend payments or for any other purpose, any other corporate purpose.

Senator PROXMIRE. Just one more question: Recognizing the preference for balancing the cost of the investment credit with the tax reform proposals which you have discussed here, if you cannot get the tax reform, would the tax credit—in view of the value that it might be in stimulating employment—by itself conceivably be accepted?

Secretary DILLON. Well, I think that is something that would have to be decided by the President when the bill gets to his desk.

Of course, a great many of these reforms, such as the reform on expense account expenditures and a number of the others, are very desirable in themselves. They are equitable. And I am sure that a lot of those will come through. Whether there is an exact balance in the end, we will just have to see.

Representative REUSS. Thank you very much, Mr. Secretary, for a very thoughtful performance here this morning.

The committee will now stand adjourned until 2 o'clock in this chamber, when we will hear Mr. Martin of the Federal Reserve Board.

(Whereupon, at 12:30 p.m., the committee was recessed, to reconvene at 2 p.m. the same day.)

79660—62——12

AFTERNOON SESSION

Chairman PATMAN. The committee will please come to order.

We will be privileged to hear this afternoon the Honorable William McChesney Martin, Jr., Chairman of the Board of Governors of the Federal Reserve System.

We are delighted to have you, Mr. Martin.

I notice you have a prepared statement. You may proceed in your own way, sir.

STATEMENT OF WILLIAM McCHESNEY MARTIN, JR., CHAIRMAN, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, ACCOMPANIED BY RALPH A. YOUNG, ADVISER TO THE BOARD

Mr. MARTIN. Thank you, Mr. Chairman.

My comments today on economic and financial developments will be directed toward the two central problems on which the Nation's efforts should be focused in 1962. One is domestic; the other, international. The first problem is to move economic activity higher and unemployment lower. The second is to strengthen our position for dealing with the adverse balance of international payments of the United States.

For the time being, at least, some of the requirements for dealing with these two problems may seem to be in conflict. But for the long pull, the more basic needs are the same, because they are the fundamentals on which all enduring economic growth must be based.

The prime need is a steady increase in productive efficiency. But to achieve this will require many things. Among them are investment in new and improved plant and equipment to turn out better products at lower costs; savings, to facilitate that investment; and stability in the value of our money, to induce those savings.

That, of course, is just part of the chain reaction that can be set into motion by progress in meeting these needs.

The surest way, in my judgment, to get sales expansion leading to expansion of output, and output expansion leading to expansion of job opportunities, is to give the consumer a break by offering him more for his money.

In my judgment, much of our postwar economic trouble has been brought about by pricing consumers out of the market instead of into it. Increasing our productive efficiency offers the most promising avenue for correcting that process by providing a gain for business and labor to share with the consumer, as business and labor should do, in their own long-term interests.

These are matters that seem to me worth bearing in mind in considering the problems and performance of the economy, domestic and international, in recent times.

Taken as a whole, 1961 was a year of vigorous economic advance, happily free from an accompanying upswing in general prices, a fact that bolsters prospects for further growth.

Total economic activity, as measured by gross national product data, and industrial production both moved into new high ground. Gross output rose about 7½ percent from the fourth quarter of 1960, and 8 percent from 1961's first quarter low. Industrial production advanced 12 percent over the year, and 13 percent from the February low. The Consumer Price Index moved up approximately one-half of 1 percent, but wholesale price indexes dipped below their year ago levels.

Meanwhile credit expansion in general was greater than in any previous year except 1959. Funds advanced in credit and equity markets totaled about $50 billion, well above the $40 billion of 1960 although far below the $61 billion of 1959, a year of recordbreaking credit demand. Interest rates moved within a relatively narrow range.

Credit expansion by commercial banks approximated $15 billion, a record surpassed only in 1958, and then by a narrow margin. Loans accounted for some $6 billion of that total, although loan demands were moderate as they usually are in the early phases of an economic recovery. Investments, also following a characteristic course, increased about $9 billion.

But even though the number of people holding jobs rose again to record level, unemployment failed to respond to general improvement in demand as rapidly or as greatly as had been hoped. Not until near the end of 1961 did unemployment show an encouraging drop, to about 6 percent of the labor force from the 7-percent level at which it had held for almost a year. Even so, the number of long-term unemployed continued relatively large, totaling about 1.5 million in the seasonally adjusted figures at the end of the year.

With the rising levels of income and business activity now taking place, total employment should expand further this year and absorb into gainful activity many of those currently classified as unemployed as well as new entrants into the labor force. To assist this process, we must stay attentive to changes in the composition of the working force, a matter to which your committee is alert, as demonstrated by the development of much pertinent new information at recent hearings of your Subcommittee on Economic Statistics.

In 1961, from the recession's February low to the end of the year, about 1 million persons were added to nonfarm payrolls. This virtually restored the level of nonfarm employment to the prerecession high. Yet in manufacturing industries, although employment in December 1961 was well above the low point of the previous winter, there were one-half million fewer factory workers than when the recession began in the spring of 1960. At the same time industrial production was greater than ever before in our history.

Thus some of the employment patterns of the recession and recoveries since 1953 seem to be repeating themselves. After each recession, total employment has rebounded to new record levels, but fewer factory workers have been needed to produce an increased volume of goods. The decline in the number of blue-collar job opportunities even while white-collar job openings were increasing has been an important factor causing the rise in persistent unemployment since 1953. If we are to realize the full benefits of our increasing productivity, we must solve the difficult problems of transition and adjustment for the displaced workers, many of whom lack the skills and training required in the expanding sectors of the economy.

The fact that long-term unemployment has been disturbingly large over the last decade, even during periods of high-level activity and rising prices, indicates that the problem it poses is too complex to be solved by any single or simple approach.

It is evident that our economy requires continuing, sustainable growth, attended by an ever-rising level of overall demand to provide an ever-rising number of job opportunities for our steadily growing population. But it seems equally evident that we require specific steps to make headway against the problems posed by certain types of structural unemployment that are not readily responsive to general monetary and fiscal measures. Special programs to increase occupational and geographical mobility are necessary for this purpose. Training and retraining under management, labor, and Government supervision would greatly benefit workers who need new skills to adapt more readily to changing technology. Both employers and employees would gain from better provision of information on the current and prospective job market; that is, where job openings may be found, and where qualified workers can be located.

Let me turn now to the second problem cited at the start: The deficit in the balance of international payments, although much reduced from that of the preceding years, rose again in the last part of 1961.

In the first half of the year the payments deficit had shown encouraging shrinkage. Net sales of gold from U.S. reserves were only $200 million. The main reasons for this fairly good result were clear, even at that time: a low level of imports occasioned by slack demand because domestic business activity was low; an advance debt repayment to us, by Germany, of more than half a billion dollars; and a strengthening of confidence in the U.S. dollar in the wake of a declaration by the President that the administration was determined to defend the international value of the dollar.

Nevertheless it was also clear, even at the time, that we could not be complacent. To have the balance of payments in reasonable equilibrium on the average over a period of years means that we need to have a balance-of-payments surplus, not merely a reduced deficit, at certain times. The first half of 1961, when imports were low, was a time when a payments surplus would have been appropriate. I do not say that this was a realistic possibility in 1961. The point is simply that the good results of the first half of the year were not good enough, considering the low level of import demand at the time.

Balance-of-payments pressures again turned adverse in the second half of 1961, when the deficit began to rise again. Net sales of gold during the half rose to some $650 million. They might have gone much higher if there had not been a big increase in foreign holdings of dollar reserves, working balances, and short-term investments in the United States.

The increase in the overall payments deficit in the second half of last year also had its special causes. Confidence in the dollar has been well maintained, and that was not the trouble. The causes of the rise in the deficit lay elsewhere.

For one thing, imports rose sharply from their abnormally low level in the first half of 1961, advancing to levels about in line with the level reached by the gross national product in the latter part of the year. Exports held steady: while those exports financed by aid programs increased, commercial exports not financed by Government grants and credit fell short of their mid-1960 level. The failure of commercial exports to increase in 1961 tied in with the slowing down last year of European economic expansion. In Europe there was an especially noticeable reduction in buying of materials and semifinished goods for inventory.

It is quite possible that imports will rise further, as business activity increases here. However we can also fairly expect that growth in exports will resume. In fact the latest export figures, for October and November, were higher than for any pair of months earlier last year.

Sooner or later we need to get a large increase in our export surplus. To make this increase in the export surplus come sooner rather than later, and to make it big enough to count, let me emphasize again the necessity that we preserve a competitive climate of business in this country, raise our productivity, hold down costs, and see to it that our prices are not out of line with those of other producing countries.

We must also put ourselves into a position to negotiate with our principal trading partners so as to minimize trade barriers that might otherwise keep us from achieving this needed increase in our exports. The task of correcting our balance-of-payments deficit would become far more difficult if the countries in the European Common Market were to maintain high tariff walls against our goods while progressively moving toward free trade within the Common Market.

In our balance-of-payments difficulties, however, exports and imports are not the whole story. The essence of the problem is that we have not had a big enough export surplus to cover our commitments on economic aid and military expenditures abroad, and our outflow of private loans and investments abroad. To cover the deficit, we have been called on to sell some gold, and we have had to increase our short-term liabilities to foreigners. This increase in short-term liabilities is dependent upon the willingness of foreigners to build up dollar reserves, working balances, and short-term investments in this country. In reality, it constitutes foreign lending to the United States. We cannot count forever and without limit on that sort of lending to support the position of the U.S. dollar. That is why we must get a better balance between the export surplus and our outpayments for economic aid, for military expenditures, and for private capital outflow from the United States.

In reference to our economic aid commitments and U.S. military expenditures abroad, let me note that a large part of aid is being linked to exports, and ways to obtain offsets for part of the military expenditures abroad are being sought. We must continue to make every effort to get other countries to take a fair share of the burden of these costs. Whatever part of these expenditures cannot be linked or offset must be covered by net earnings in purely commercial trade, investment income, and other private transactions.

So far, I have said very little about private capital movements, apart from the buildup of foreign liquid assets in the United States. One of the big difficulties in the U.S. balance of payments in 1961 was that outflows of long-term and short-term capital were still very large, even though the kind of volatile movement we had in the latter part of 1960 was not much in evidence in 1961.

In fact, net outflows of long-term and short-term capital seem to have been even larger in the second half of last year than they were in the first. Here I am talking mainly about bank loans and acceptance credits, corporate investments in subsidiaries, new foreign issues, and purchases of outstanding foreign securities that offset foreign purchases of U.S. corporate securities. Along with these, there were trade credits, and also some "movements of funds" in the sense of acquisitions of liquid investments or balances abroad, particularly in Canada.

All told, the net outflow of all the various types, including a guess for unidentified movements, seems to have approached $4 billion in the year 1961. This was only moderately less than the outflow in 1960, and it was more than the overall deficit in our balance of payments in 1961. While the deficit in the balance of payments cannot be related to any one single class of outpayments, clearly the capital outflow was an important factor .

Restraining these capital outflows is particularly difficult because they represent various normal kinds of lending and investing. These outflows reflect the ready availability of credit in U.S. markets. Only in part can they be influenced by the level of short-term interest rates. By and large, such differences as did develop last year between money rates here and abroad do not appear to have been a primary determinant of captial movements either from or to the United States. On the other hand, the ready availability of credit at rates competitive with other markets may have exerted an important influence.

In the circumstances prevailing today, the Federal Reserve has found it necessary to balance domestic and international factors in arriving at policy decisions. The System's responsibility for the value of the dollar extends beyond domestic price stability to the value of the dollar in terms of gold and of other convertible currencies. This is partly a matter of restoring basic equilibrium in the balance of payments, and partly a matter of preserving stability in exchange rates in international markets.

Until recently official operations by the United States to maintain the exchange value of the dollar have been limited to purchases and sales of gold by the Treasury's stabilization fund—at $35 an ounce—to foreign monetary authorities for monetary purposes. Recent developments, however, have made it desirable for the United States to play an active role in exchange markets themselves.

Persistent deficits in our international payments have put very large amounts of dollars into the hands of foreign holders. This has made the dollar both susceptible and vulnerable to large and sudden movements of funds. Movements of this kind can be touched off by international political uncertainties, or by bearish or bullish reports and rumors about economic and financial developments at home or abroad. With the pound sterling and the main other European currencies again convertible, to a large extent, funds now can move freely and in large volume between New York, London, and the financial centers of continental Europe.

For these reasons, the Secretary of the Treasury decided last March to use the stabilization fund for operations in foreign convertible currencies, for the first time since the Second World War. The stabilization fund has acquired holdings of some major European currencies, and undertaken transactions in the market with the aim of defending the dollar from speculative forays.

These operations have been conducted on a fiscal agency basis by the Federal Reserve Bank of New York for the account of the stabilization fund. The resources of the stabilization fund for these purposes are, however, quite limited.

The Federal Open Market Committee and the Board of Governors are fully cognizant of the increasing importance of international financial relations for the working of our domestic monetary system. We further recognize that, under present-day conditions, maintenance of an efficient international payments system based on the interconvertibility of currencies requires close cooperation among the central banks of major industrial countries and with established international financial institutions.

As one step in such cooperation, the System is now prepared in principle and in accordance with its present statutory authority to consider holding for its own account varying amounts of foreign convertible currencies. Toward this end, we are now exploring, in consultation with the Secretary of the Treasury, methods of conducting foreign exchange operations in convertible currencies with due and full regard for the foreign financial policy of the United States.

These System operations, along with those conducted by the stabilization fund, would have the primary purpose of helping to safeguard the international position of the dollar against speculative flows of funds. They would not, and could not, serve as substitutes for more basic action to correct the deficit in this country's balance of international payments.

The problems I have been discussing have weighed heavily with those of us in the Federal Reserve in our endeavors over the last year to keep credit conditions attuned to national needs.

On the domestic side, to help bring about recovery, expansion, and sustained growth in production and employment, the Federal Reserve has been operating to bolster the banking system's ability to meet all reasonable borrowing needs.

On the international side, to help hold down the outflow of capital and gold prompted by the continuing balance-of-payments deficit, the Federal Reserve has been operating to minimize drains stemming from international differentials in interest rates.

Activities in pursuit of these dual objectives were carried out in the open market for U.S. Government securities. Before taking up these operations, however, I would like to mention one other recent Federal Reserve action.

On December 1, the Board and the Federal Deposit Insurance Corporation announced an increase in the maximum rates that banks may pay—if they choose—on savings and time deposits. The change became effective on January 1 of this year. In general terms, the action authorized banks to pay 3½ percent on any savings deposits, and 4 percent on those left in the banks for a year or more; also, to pay 3½ percent on time deposits with a maturity of 6 months to 1 year, and 4 percent on those with a maturity of a year or longer. There are some $50 million of these savings and time accounts in the 6,100 member banks of the Federal Reserve System alone.

This action was taken after extensive study and consideration. In arriving at its decision, the Board was influenced by a variety of factors. One of considerable weight was the fact that some short-term balances were being attracted away from American banks by higher rates paid on such balances in other parts of the world, and that this process contributed, in some measure, to our continuing balance of payments problem. Another was the question of whether there could be any longer any justification for restricting the rate of interest that commercial banks may pay on savings deposits to a level substantially below that paid by other institutions on similar accounts. Finally, but by no means less importantly, we were concerned over the longer run impact of a maximum rate that might limit artificially the rewards received by small individual savers, whose saving, as I have said before plays such an important role in financing the investment vital to our economic growth.

The changes that have been made in rates offered by the banks since the action took effect have been designed, for the most part, to encourage genuine saving. If this continues to be the case, the result should be an increase in the volume of funds available for long-term investment in mortgages, in State and local securities issued to finance expanded community facilities, and in securities issued by business to finance expansion of productive resources.

Your committee may be interested in the results so far of the authorization for payment of higher rates on savings. Based on a survey in mid-January of a sizable sample of Federal Reserve member banks, it appears that about two-thirds of all member banks are offering some rate in excess of the 3 percent maximum rate previously in effect.

Regular or passbook savings accounts represent about three-fourths of total time and savings deposits at member banks. Some 40 percent of the banks, holding 70 percent of total time and savings deposits, raised their rates on regular savings accounts above 3 percent. About half of these banks, or 20 percent of the total, went to the newly authorized 4 percent for deposits held over 1 year. The other half, generally, are paying 3½ percent on savings accounts.

With respect to time certificates of deposit and other time deposits, arrangements vary widely from bank to bank. But many banks are now offering up to 4 percent on 1-year certificates, including a sizable number which have not moved up to the 4 percent rate on savings accounts. Rates of 3 to 3½ percent are being offered on 6-month deposits, including the negotiable certificates offered by many of the larger banks.

Some 60 percent of the member banks still pay rates on regular savings accounts of 3 percent or less. If experience with a previous change in permitted maximum rates can be used as a guide, any further move toward increased rates on these accounts is likely to be gradual, as it was after the preceding change in 1957.

Now I should like to devote the rest of my remarks primarily to Federal Reserve operations in the Government securities market during 1961.

To assure ready availability of credit in the American economy, the Federal Reserve supplied the banking system in 1961 with reserves in amounts sufficient not only to offset the credit-tightening effect of gold drains and currency withdrawals but also to provide additional reserves to meet requirements against expanding deposits. Member bank required reserves increased in 1961 by about $1 million, while Federal Reserve holdings of Government securities increased by $1.5 billion in consequence of open market purchases. The reserves thus supplied made possible the near-record expansion of bank credit in 1961.

As a result of that expansion and of increased financial saving by the public, liquid assets held by consumers and business increased substantially in 1961. In consequence, the overall liquidity of the economy showed an increase about in line with the expansion in overall economic activity. Although total liquid assets of the public increased by about 6½ percent during 1961—compared to the 7½ percent increase in gross national product—demand deposits and currency, the more active elements that usually are termed the "money supply," increased by only about 3½ percent. The pace of increase in the money supply, however, accelerated substantially in the latter part of the year.

The stability that prevailed in interest rates was one of the striking parts of the financial scene. Interest rates showed only a moderate increase in the 1961 business upturn, just as they had shown only a moderate decline during the downturn that began in the spring of 1960. Accordingly, since mid-1960 interest rates have moved within a relatively narrow range well above the low levels reached in 1958 and below the high levels reached in late 1959. To some extent, Federal Reserve policies and operations, in addition to Treasury operations, were responsible for this stability. Although the Federal Reserve supplied reserves adequate to enable expansion of bank credit on the scale earlier described, it sought to avoid downward pressure on short-term interest rates. The Treasury, a heavy borrower, obtained most of its new money in the short-term sector of the market, thereby putting upward pressure on short-term rates.

Let me note that factors other than official monetary and debt-management policies played an important part in keeping the general level of interest rates during the 1960–61 recession above levels reached in earlier recessions. These factors included the mildness of the latest recession and the large volume of new security issues floated by corporations and State and local governments in the first half of 1961. Although 1961 did not witness as great a decline in interest rates—at least in long-term rates—as 1958, neither did it witness a sharp speculative rise and subsequent fall such as that which characterized 1958.

I should like to add, at this point, something on the way the Federal Reserve System went about supplying bank reserves. Because of the Nation's international payments problem, the System sought to provide these reserves in a manner that would minimize their effect upon short-term rates, to which international money flows are particularly sensitive.

To this end, the Federal Reserve in early 1961 extended the area of its open market operations to include purchases of longer term securities as well as short-terms, in which open market operations formerly had ben confined as a general rule. The purchase of long- instead of short-term securities, when circumstances warranted, served at least to relieve the short-term market from the direct impact of these purchases on yields, and transfer that direct impact to the longer term area.

The $1.5 billion addition to Federal Reserve holdings of Government securities that I mentioned earlier reflects merely the net result of gross transactions totaling vastly more. Most purchases or sales, in fact, are made to adjust the availability of bank reserves in accordance with temporary variation in needs, chiefly of seasonal character.

In its gross transactions over the course of 1961, the Federal Reserve purchased about $7 billion of Treasury bills and other issues maturing in less than 2 years, not including those acquired for brief periods under repurchase contracts. Over the same period, it sold or redeemed at maturity a slightly larger amount of such issues. Purchases of issues maturing within 2 to 5 years aggregated about $1.5 billion, while purchases of those maturing in over 5 years amounted to nearly $800 million, nearly all in the 5-to-10-year area. Sales of issues in these groups were negligible. The System also acquired some securities maturing in over a year by participating in refunding offers of such securities in exchange for maturing issues, but the effect of any such shifts upon the maturity distribution of the System portfolio was more than offset by the approach to maturity of other issues held.

Treasury purchases of long-term Government securities for investment accounts exceeded in amount those by the Federal Reserve. They were, mostly, of issues maturing in over 10 years. The Treasury, in addition, borrowed much of its new money in the short-term area, thus helping to maintain short-term interest rates and minimize the flow of short-term funds abroad.

Most of the purchases of longer term securities by the Federal Reserve and the Treasury were made during March, April, and May, when aggregate new issues of securities by corporations and by State and local goverments were in heavy volume. Official (Federal Reserve and Treasury) operations in that sector of the market doubtless helped to kep interest rates from rising in the face of large demands, and thus to facilitate the flotation of these corporate, State, and local issues.

The significance of these operations from the standpoint of market impact may be indicated by relating their volume to total market transactions in each maturity category of Government securities. Official market purchases of Treasury bills and other issues maturing in less than 1 year, although making up the bulk of Federal Reserve and Treasury operations, comprised in 1961 only about 4 percent of total dealer sales of such securities (excluding those to other dealers). The proportion for issues maturing in 1 to 5 years averaged 9 percent for the year, although in some months official purchases exceeded 30 percent of dealer sales in this area. In the 5-to-10-year area, the proportion amounted to more than 20 percent for the year as a whole and in the period from March through July was more than 33⅓ percent of the total. For securities maturing after 10 years, official purchases comprised over 30 percent of all market purchases for the year and nearly two-thirds of total purchases in the second quarter, when the bulk of the official purchases were made.

In conclusion, I should like to stress that, along with its problems, 1962 also brings us opportunities. Foremost among them is the opportunity to achieve further progress toward higher economic activity, lower unemployment, and restored equilibrium in our international balance of payments.

We can make the most of that opportunity by working—all of us—to bring about conditions that will generate the chain reaction that I described at the outset—a process that leads from dollar stability to savings, investment, rising productive efficiency, lower costs, better prices, greater buying demand, increased production, and expanding employment. The prospects for progress are excellent. Let us apply ourselves to the realization.

Chairman PATMAN. Thank you very much, Mr. Martin.

You stated something about interest rates that attracted my attention—about the maximum rates on savings accounts. Are you in favor of the banks paying interest on demand deposits as well as time deposits?

Mr. MARTIN. No, I am not, Mr. Patman.

Chairman PATMAN. I do not see how you reconcile that. Do you not think it is regimenting the bankers to say that they cannot, by private contract with people, pay them for the use of their money?

Mr. MARTIN. Banking is a regulated industry, as you know.

Chairman PATMAN. I know, but they do not want to be regimented. This is regimenting them.

Mr. MARTIN. Well, I think it is wise to regiment them in this respect. I think it would be unwise to regiment them any further than we have with respect to time and savings deposits.

Chairman PATMAN. The statement is made that we should keep down increases in the wages and prices. Do you not think that interest rates represent a cost of doing business?

Mr. MARTIN. I do indeed.

Chairman PATMAN. Do you not think they should be kept down, too, and the prime rate should not be raised?

Mr. MARTIN. I do not know what will happen to the prime rate. I have always testified up here that I would like to see as low interest rates, along with other costs, as it is possible to achieve, without producing inflation. The emphasis that I have been trying to give here is that if we want to increase demand for products and encourage new products that will lead to increased production and more output and more jobs, we have to improve our productivity and pass along some of the improvement in that productivity to the consumer rather than just dividing it up among labor, stockholders, and management.

Chairman PATMAN. The consumers also pay interest, though, Mr. Martin, and they pay taxes.

Mr. MARTIN. I just want to emphasize, Mr. Patman, that the United States has the lowest rates of interest of any important industrial country in the world today.

Chairman PATMAN. Are you trying to compare us with a South American country where they pay 15 and 20 percent interest?

Mr. MARTIN. I am talking about just the industrial countries of the world. I am talking about Britain, France, Germany, Italy, Sweden, and Canada. There are no countries that I know of that have lower interest rates generally than the United States of America.

Chairman PATMAN. Well, if we could get them lower, you would be in favor of it, would you not, consistent with a stable and sound economy?

Mr. MARTIN. I certainly would. We are all seeking to have as sound an economy as we can get.

Chairman PATMAN. Have our representatives received any agreement or understanding from the European central bankers to the effect that they are not to draw on our gold reserves, or that they will exercise some restraint in drawing on our gold reserves?

Mr. MARTIN. There are no understandings that I know anything about.

Chairman PATMAN. Expressed or implied?

Mr. MARTIN. Expressed or implied. We have discussed with our foreign central banks all aspects of the international monetary problem, and we have tried, through discussion to get a general understanding of mutual domestic problems. All of us recognize that we have a responsibility for the payments mechanism, that we ought to do our level best to make this payments mechanism work. Therefore, no central bank today ought to act in an arbitrary or capricious manner with respect to the use of that payments mechanism.

Chairman PATMAN. In regard to price fixing among companies and other practices that we consider against the public interest and in violation of the law, oftentimes we find that the most effective device is what might be called an unconversational understanding. The wrongdoers do not have any conversations about it, but yet they go ahead and do it. You do not have even any unconversational understandings about this gold?

Mr. MARTIN. I have none—unconversational or conversational.

Chairman PATMAN. Is there any agreement, informal or otherwise, that we will guarantee dollars, either in terms of gold or foreign exchange in the event that we should devalue the dollar?

Mr. MARTIN. There are none. I think the President drew the line very clearly in his balance-of-payments statement last spring, that this country intends to maintain the value of the dollar, and I support that completely.

Chairman PATMAN. Mr. Martin, every year, you know, we have a conversation about the annual report.

Mr. MARTIN. We do indeed, Mr. Patman.

Chairman PATMAN. What is the prospect for that?

Mr. MARTIN. We are working hard on the annual report and we hope to get it up to you just as rapidly as we did last year.

Chairman PATMAN. I think it was earlier last year than ever before was it not?

Mr. MARTIN. That is right, and we give you some of the credit for it.

Chairman PATMAN. When did it come in last year?

Mr. MARTIN. I think about the 15th of March.

Chairman PATMAN. It would be very helpful if you could get it here by that time.

I will forgo asking any further questions at this time.

Senator Bush?

Senator BUSH. Mr. Chairman, I am sorry I missed the opening part of Chairman Martin's statement, but I have been looking at the first couple of pages and I want to commend him very highly for calling attention to what he calls the prime need, the pressing need, the increase in productive efficiency.

I think the thing that is lacking in connection with our ability to handle the balance-of-payments problem is a lack of public understanding that we must improve our competitive position, not only at home but also so that we can increase our competitive ability abroad. We are faced now with a brandnew trade program which has tremendous implications. It holds out great promise for the future. We are all in favor of improving our exports. But the thing that I am afraid the administration has not done is to stress enough the philosophy that is contained in the first two pages of your report, to wit: that if we are to improve our competitive position, we have to pass on some of these gains in productivity to the consumer. We also have to pass them on to the producers so that he can have some reserves to modernize plant, extend plant and improve efficiency so as to further increase productivity. Of course, where inequities do exist, labor rates should be adjusted within the bounds of productivity. But the idea that I think has been given that you can take all of the gains in productivity and pass them along to labor is a very dangerous philosophy for labor, itself, and impairs our ability to improve our competitive position.

I am very glad to see you stress the importance of dividing these gains in productivity as you have done in this paper.

I do not have any questions, Mr. Chairman, but I do appreciate the chance to commend the Chairman of the Federal Reserve Board for this very splendid statement.

Chairman PATMAN. Mr. Martin, would it be all right with you if any member prefers to ask any question in writing, that you will try to answer it when you look over your transcript and make it a part of your record?

Mr. MARTIN. I will be delighted to, sir.

Chairman PATMAN. Mr. Bolling?

Representative BOLLING. Mr. Martin, the reason for this question is purely for information. There is no other purpose to it. You say:

The stabilization fund has acquired holdings of some major European countries, and undertaken transactions in the market with the aim of defending the dollar from speculative forays.

You also say:

As one step in such cooperation the system is now prepared in principle, and in accordance—

and so forth.

I would like to know what kind of market transactions they are, with the aim of defending the dollar. What happens?

Mr. MARTIN. I think it has to be looked at on an ad hoc basis. I want to make clear, Mr. Bolling, that the Federal Reserve is not anxious to engage in this type of activity. It is only because we feel we have a responsibility—with convertible currencies as they are today, currency values—including that of the dollar—are more subject than for a long time to speculative movements. I used here a term that I happen to like, "forays." If we held some of these currencies—and the amounts and variations in them would have to be on an ad hoc basis—we might be able, by disposing of the currencies, to minimize or offset these temporary speculative movements. The Treasury stabilization fund has experimented with this kind of operation since March of this year, in a very small way, and we have come to the view that however we should acquire these currencies—

and it is not possible to spell out how here—what we are aiming our activities at is to keep the speculators from unseating us, to try to minimize speculative movements. We would need to operate in a variety of ways. But we have resources in addition to what the stabilization fund has. We do not claim that this is going to correct our basic deficit. You will notice I went out of my way to state that.

Representative BOLLING. I understand, but I mean exactly what I said at the beginning. I do not understand how this works. I do not want you to say anything you should not say, but I want to know what you do, within the bounds of what you should or should not say.

Mr. MARTIN. Well we could open an account with some foreign central bank and hold in that account either pounds, lire, francs, or other currencies, depending on the circumstances. That would put us in a position to dispose of them if there was a sudden need for them. That is the simplest type of operation. Another possibility would be for us to make reciprocal currency transactions with foreign central banks; in the language of the street, these are "currency swaps." Last March and April the pound sterling had quite a problem at the time of the reevaluation of the guilder and the deutsche mark. There were a lot of movements and the central banks did cooperate at that time to minimize the impact of that in a variety of ways. I do not think you can spell out in advance precisely what you might do, nor ought we to spell out magnitudes for this type of operation because we are operating in a goldfish bowl. We would report what we do in our Federal Reserve statements from time to time, but we ought not to be indicating ahead of them what the limits are or what we are going to do. If you do that, then you are inviting the speculator to take advantage of your operations.

Representative BOLLING. I think that answers my question. I just wanted to be sure that I understood.

Thank you.

Chairman PATMAN. Congressman Curtis?

Representative CURTIS. I certainly appreciated your statement, Mr. Martin. I always do. There is one particular area I would like to explore a little bit and that is our long-term private capital investment. There has been an increase, too, of foreign long-term capital investment in this country, has there not?

Mr. MARTIN. Well there has been some but not as much as I would like to see.

Representative CURTIS. That is what I was going to ask. I was first going to lay the groundwork as to how much there has been. I was trying to compute these figures on page 151 of the President's economic report. Table 18 shows assets and liabilities. As near as I can figure, the long-term direct investment in this country, I presume that would be the liability, is $18.4 billion, adding the direct investment and other private investment, as opposed to what it was in 1949 at $7.1 billion. Then, relating that to the figures of our private investment—I guess those are abroad—it would be something like $45.3 billion. It looks like our increase has been from 15.6 to 45.3, which is a little less than tripled, and the other has been from 7.1 to 18.4, which is a little less than that. But it is fairly comparable as increases, would you not say?

Mr. MARTIN. Yes, sir.

Representative CURTIS. You say you think it should be more. That is what I was interested in.

Mr. MARTIN. Yes, I would like to have more foreign investment, long term as well as short, in this country.

Representative CURTIS. Do you see any reason, or are there any deterrents that you see to foreign investment coming into this country?

Mr. MARTIN. I do not think there is any hindrance to it. We have had some direct investments here. I was told the other day this Pan American Building in Grand Central Station is going to have some foreign investment in it. In the last 6 months of last year, I have seen very little indication of any sizable amounts of either direct or indirect investment over here.

Representative CURTIS. Most of the restrictions against convertibility or bringing back of our foreign investments in Western Europe have been removed, is that correct?

Mr. MARTIN. Most of them. They are not all removed.

Representative CURTIS. Are there still some restrictions on that?

Mr. MARTIN. Yes, there are. I could not spell them out to you, but I think that there are some. I do not think it is completely convertible. That is why in my statement I say "to a large extent."

Representative CURTIS. Are the restrictions still a major factor at all?

Mr. MARTIN. In my judgment, no. That is not a major factor. I think the major factor I have highlighted here is in the fact that we must not let the Common Market discriminate unduly against us, if we are to continue our progress.

Representative CURTIS. Some of the President's recommendations in the tax area have been to make the tax incidence on our investment abroad greater. Would you feel that is one way of possibly cutting down on the amount of our foreign investment abroad?

Mr. MARTIN. Do you mean to increase taxes?

Representative CURTIS. Yes, our taxes. There are two primary proposals. One is in regard to so-called tax havens. The other is in applying the new gross-up principle. But the net result, of course, is more taxes on foreign investments. I wanted to ask you from the standpoint of its effect whether this is desirable or undesirable.

Mr. MARTIN. Well, I think to the extent it equalizes taxes, it is a good thing, but I will have to plead ignorance. I have not studied tax proposals carefully enough.

Representative CURTIS. In your presentation, do you feel it would be advantageous to cut down the rate of increase of our investments abroad, or do you think it good policy to encourage further American long-term investment abroad?

Mr. MARTIN. I think that ought to be determined by the market. I would not want to have any controls placed on our investments abroad.

Representative CURTIS. You would let the market operate?

Mr. MARTIN. I would let the market operate, yes.

Representative CURTIS. In other words, you do not see this as an area where there is any danger or any cause for concern?

Mr. MARTIN. No more so than in the general picture, that we have to be competitive in the world. One of the problems has been that some of our industries have gone abroad on the basis of, "If you can't lick them, join them."

Representative CURTIS. That is what I am really getting to. I wondered whether or not you see in the amount of American investment going abroad any increased rate that would indicate that is what is occurring and, therefore, something that you would feel we should have concern about.

Mr. MARTIN. I think we should watch it very carefully. I think we have to watch every aspect of this balance-of-payments problem.

Representative CURTIS. There is no indication that our foreign portfolio in the private sector is not a good and solid one, is there?

Mr. MARTIN. None that I know of.

Representative CURTIS. I think we have been receiving about $2 billion annually on investments, which I guess would be about $45 billion. Would you regard that as an unreasonable rate?

Mr. MARTIN. I would not regard it as an unreasonable rate against our total investments.

Representative CURTIS. One final question on this. Do you believe that in our considerations of trade problems we ought to be directly relating them to our foreign investment problems as well? Do you feel that the two mesh, or that we can consider trade somewhat apart from investment?

Mr. MARTIN. I think they should both be considered. I think they do mesh to a certain extent.

Representative CURTIS. Thank you.

Chairman PATMAN. Congressman Reuss?

Representative REUSS. Mr. Martin, last year when you were before this committee, I discussed with you a chart which showed the relationship between unemployment and the amount of free reserves provided the banking system by the Federal Reserve. I think you will recall that I suggested that where net free reserves of the system were kept at around a half billion dollars, the unemployment picture tended to get better. However, when reserves were put into net borrowed position, this tended to cause the improvement in the unemployment picture to cease, and frequently to bring on recession conditions. In 1954, for example, when the unemployment rate started to improve at the end of the year, in the beginning of 1955, the free reserves were retracted and the system was put in a borrowed condition with the result that unemployment hovered at a plateau there without getting any better for 2 or 3 years. Then again in 1958, when the unemployment curve started to go down, you notice that almost immediately the net free reserves were retracted, and the system was put into a net borrowed position.

Early this year when we discussed the matter, I indicated to you that I thought the brakes had been applied too fast in the past and expressed the hope that the monetary authorities would keep the net free reserves of the banking system at around the $500 million level until there was a very substantial improvement in the unemployment picture.

I am very happy to see by the chart, which I have had brought up to date, that, in fact, despite some, though not nearly enough, improvement in the unemployment curve. the monetary authorities have kept net free reserves of the system at around the half-billion-dollar level. (See p. 230.)

I just want to say congratulations and keep up the good work.

I do have this question on monetary policy generally: Balance of payments aside, I take it that the object of our monetary policy, and I am trying to paraphrase what you have said many times, is to provide that amount of reserves and, to the extent that you can, a level of interest rates which will make for full employment and maximum growth without inflation.

Mr. MARTIN. That is right.

Representative REUSS. When you have a balance-of-payments problem, such as we now have, we would also agree that you should add to the weapons in your armory, the thing that you have in fact done this year; namely, attempt to see that within a given interest rate structure, short-term interest rates are the ones that go up to the maximum possible extent and long-term interest rates are the ones that go up to the minimum extent. That, in effect, has been what you and the Treasury have tried to do this past year, have you not?

Mr. MARTIN. We have had complimentary debt management and reserve operations which have dispersed through the market the direct impact of our activties so as to maintain short-term rates, but not fix them, and to try to encourage the flow of funds by activities when they can be judiciously applied in the longer sector of the market, without for one minute believing that we can eliminate arbitrage through the different sectors of the market.

Representative REUSS. I was not suggesting that. I was simply describing and indicating my agreement with the proposition which you and the Treasury have in fact followed in the last year. You have at least taken some steps to see that short-term interest rates do not go down unduly in relation to long-term interest rates.

Mr. MARTIN. To the best of our ability.

Representative REUSS. Now, let me ask this question: Is there anything over and beyond what you have done that you as a monetary manager feel you have to do because of the movement abroad of short-term funds by reason of interest rate differentials? If that is not clear, I will try to rephrase it.

Mr. MARTIN. No, that is perfectly all right. I think I have tried to point that up in this statement by indicating that it is not always the rate, it is also partly the availability of funds. So we have to be quite aware of both problems—the availability of funds problem and the rate problem.

Representative REUSS. My question referred to both the availability of funds and interest rates. My question boils down to this: Granted that your abandonment of the bill's only policy and the Treasury's similar activity is entirely sound and sensible under the circumstances that faced us in the past year, is there anything more which you as a monetary manager feel that you have to do now by way of tightening money, by way of making credit less available, and by way of making interest rates higher than they should otherwise be from a purely domestic standpoint? This is a very fundamental question, because if the answer is "yes, there is," you are saying that this country has to tolerate a higher rate of unemployment and a slower rate of growth than it would otherwise tolerate because of a relatively minor problem, that is, the propensity of short-term funds to move around for higher interest rates.

Mr. Dillon, this morning, I think, answered that really he was not prepared to recommend the distortion of an otherwise sensible domestic monetary picture for this balance of payments' reason. What is your view on it?

Mr. MARTIN. Well, my view is that it is not possible to forecast what may develop in 1962. I do think, of course, that we have to put all of this against the domestic situation as long as goods and services are in adequate supply, over supply in many instances——

Representative REUSS. Just a minute. The hypothesis which I was putting to you was that from the domestic standpoint it was necessary to provide X amount of credit leading to Y interest rates, whatever those were. Then my question is: Do you need to depart from that goal by reason of fears that people are going to take their bank accounts abroad because they can get a higher interest rate in Germany?

Mr. MARTIN. Well, you have to weigh it all the time. That is the problem we have been wrestling with for the last year.

You see, we all have our theories on this, Mr. Reuss. I am talking about myself, here too. I do not say that my theories are correct. I happen to think that the balance of payments problem, the unemployment problem, and the growth of the economy are all interrelated, and that what we have developed here and there is no point in our arguing about the past is the result of the inflation since the end of World War II having gotten ahead of us. In other words, all of these problem chickens have come to roost together. Now we have a very real problem of doing what we can to help the domestic economy while recognizing that the domestic economy must, at the same time, become competitive in world markets and the whole world now is competing for the available supply of credit, capital, and savings.

Representative REUSS. Let me interrupt you. I could not agree with you more. I am for keeping the domestic economy competitive, but you keep, if I may say so, escaping from my hypothesis. My hypothesis was that we should do domestically by monetary policy each and every thing necessary to produce full employment and maximum growth without inflation. This you want to do, and I want you to do. My question was: Do you depart from that goal, do you ease up in your zeal for maximum growth and maximum employment, because you feel somehow that you have to restrict credit and raise interest rates a little bit to keep money, domestic and foreign, from skipping out of the United States and going overseas because the interest rate is somewhat higher?

Mr. MARTIN. My answer is that under certain circumstances you might have to. I do not say those circumstances are here. I would not forecast the future. But I would not want to preclude that as something you might have to do.

Representative REUSS. In the light of your answer, because I think this is a crucial point, and I have only a minute to go, I would like to state three questions which you do not possibly have time to answer now, but I would appreciate an answer from you and your associates as best you can.

Mr. MARTIN. We will do the best we can, I assure you.

Representative REUSS. Question No. 1: Has it really been demonstrated that there is an invariable relationship between the relative interest rates among developed countries and short-term capital movements? Has a thorough study been made of this subject, and, if so, can this committee have it?

Question 2: To the extent that it is felt that short-term capital in this country goes overseas because of higher short-term interest rates abroad, to what extent are we now, at the highest diplomatic and financial levels, trying to get the other great trading nations of the world and of Europe, particularly, to do what we are apparently doing here in this country, namely, using fiscal means, spending and taxing, as a primary method of fighting inflation, thus putting less of a burden on monetary policy and requiring lower interest rates than otherwise would be the case?

Parenthetically, I would shudder to think that we would deliberately abort recovery from a recession and have higher unemployment than we would like to have without having knocked ourselves out trying to urge fiscal tightness upon our trading partners.

Question 3: Is there not an important difference between the so-called basic items in a balance of payments—trade, services, military expenditures, Government investments, and private capital investments—and those items reflecting short-term capital movements? Is not a flight of short-term capital due to discrepancies in interest rates a different kind of money movement not necessarily reflecting fiscal or monetary irresponsibility on the part of the country having somewhat lower interest rates? If this is so, might it not be worthwhile to see if we could not erect a new principle of international monetary morality along the following lines: Central bankers are welcome to demand gold for any of the deficits caused by basic structural shifts, but if the deficit is caused, and to the extent that it is caused, by one of these innocent short-term capital outflows, central bankers should not, in the interest of the free world monetary system, demand gold in the same amounts and quantities as they otherwise might.

I think when you read the record these questions will be intelligible. If they are not, I will try to make them so. I would appreciate an answer.

Mr. MARTIN. We will do our best.

(The following was later received for the record:)

Question 1. Has it really been demonstrated that there is an invariable relationship between the relative interest rates among developed countries and short-term capital movements? Has a thorough study been made of this subject, and, if so, can this committee have it?

Answer. Interest rates represent a cost of money to the borrower and a return on money to the lender. They are necessarily a factor affecting the movement of funds—short-term and long-term—between the money markets and capital markets of developed countries. There is, however, no invariable relationship between relative interest rates in such markets and capital movements. While interest differentials can be an important factor in movements of capital, other factors also exert a conditioning influence. These other factors include the availability of credit, the supply of credit instruments of ready marketability, the demand for credit for borrowers of good standing, and—of predominant importance at some times—expectational and confidence factors.

Capital movements are sometimes viewed in the narrow context of funds seeking liquid investment in prime market paper of short maturity. The differences that existed last year between money rates here and abroad on this kind of paper do not appear to have been a primary determinant of international movements of funds of this type. Interest rates in the U.S. markets on this kind of paper were relatively attractive during most of last year, especially if it is taken into account that funds placed in sterling in London, where rates were high, had to incur either exchange risks or a cost of forward cover that was equivalent most of last year to 2 percent per annum or more.

The forward exchange mechanism functions as a kind of buffer that allows interest differentials to persist between international markets on highly liquid paper. For example, if rates in London applicable to prime short-term market paper are 5 percent and in New York are 3 percent, the forward rate for sterling will tend to be at a discount of 2 percent (per annum) from the spot rate. If it is less than 2 percent, there is an incentive for liquid funds to move from New York to London on a covered basis to gain whatever interest advantage there may be as against prime short-term investment in New York. On the other hand, if the discount exceeds 2 percent by a sufficient margin, short-term funds will find an incentive to move to New York with exchange risk covered.

In other words, when foreign exchange for future delivery sells at a significantly different rate from its interest equilibrium level, funds may even move from a country with high interest rates to one with lower rates if the gain from selling the currency of the latter at a premium for future delivery more than offsets the loss from the lower interest rate return on the investment. (In the example given the forward dollar is at a premium in relation to forward sterling.)

The point, for present purposes, is that forward cover of an asset or obligation in foreign exchange may involve either a cost or a profit, and investors of short-term funds usually take this into account in deciding in which international financial center they should invest their funds. Gross differences in the levels of interest rates in different financial centers therefore do not tell the whole story.

While there is a tendency for movements in forward exchange rates to eliminate or at least to reduce the net incentive to move liquid funds from one center to another, the fact of different structures of interest rates among international markets is also part of the story. With different structures of interest rates—of money market rates, of bank deposit rates, and of bank lending rates—in different countries, it is unlikely that at any one time all interest rates and all forward discounts and premiums will be in such relation to each other as to eliminate all incentives for international movements of funds. Moreover, it must be stressed that forward exchange discounts and premiums are affected not only by international short-term investment movements, but also by commercial demand and supply in spot and forward exchange markets. They may also be influenced by official intervention as well as by free market forces. Since the latter part of 1960, for example, the German central bank has provided special inducements to encourage outflow from Germany of liquid secondary reserve funds of German commercial banks.

Although the forward exchange rate has an important influence on short-term movements of liquid funds, it should be recognized that many short-term capital transactions between markets take place without forward cover. The incentive or necessity to move funds without forward cover will increase as maturity of the transaction is extended and its liquidity reduced. In these cases, absolute interest-rate differentials play an important role, together with other factors such as the availability of credit and conditions with regard to credit risks.

A very important category of short-term capital movement takes the form of lending by U.S. lenders to foreign businesses, banks, and governments, in some cases in nonindustrial countries. This kind of capital movement depends on various factors, including the changing needs of borrowers for such accommodation, the nature of bank-customer relationships, and the availability of bank credit here and elsewhere. With regard to this type of capital movement, it is important not to overemphasize the role of interest rates per se. Nevertheless, it is important to recognize that if U.S. interest rates are competitive with those abroad and other factors are operating to make the services offered by U.S. lenders attractive to foreign borrowers, short-term capital outflow will take place. Such conditions obtained in 1961.

Investors motivated by speculative objectives may move funds internationally not only in short-term forms but also for the purchase of long-term securities and equities on a temporary holding basis. Such holdings are to be sold when short-term capital gains are realized or if capital losses are experienced. Accordingly, expectations of changes in long-term interest levels and market prices of bonds or in prices of equities may contribute to international capital flows that are essentially short term but not necessarily closely related to short-term interest-rate differentials.

Movements into liquid investments by U.S. nonfinancial corporations may also vary with changes in corporate policies related to their liquidity positions. Moreover, some movements may be influenced by tax considerations primarily.

As a continuing assignment for the information of the Board of Governors, the Board's staff analyzes currently international movements of short-term funds with a view to assessing the various forces affecting them. The period over which such analysis has been pursued is necessarily relatively short since the major European countries did not attain full external convertibility until the end of 1958. Also, the influence of interest-rate differentials on the movement of short-term and other funds during this period has been obscured at times by such developments as the repercussions on the exchange markets of the upward revaluation of the German mark and Dutch guilder in March 1961 and by market uncertainties regarding the dollar and sterling associated with the balance-of-payments problem of the United States and the United Kingdom. The continuing staff analysis of these factors has not been brought together in a single study suitable for submission to the committee and it would be premature to do so at this stage. It is believed, however, that the foregoing discussion outlines the considerations involved in the analysis in a manner responsive to the question asked.

Question 2. To the extent that it is felt that short-term capital in this country goes overseas because of higher short-term interest rates abroad, to what extent are we now, at the highest diplomatic and financial levels, trying to get the other great trading nations of the world and of Europe, particularly, to do what we are apparently doing here in this country, namely, using fiscal means, spending and taxing, as a primary method of fighting inflation, thus putting less of a burden on monetary policy and requiring lower interest rates than otherwise would be the case?

Answer. As Secretary Dillon has already indicated, effective international cooperation to prevent or limit excessive capital and monetary reserve movements has been one of the dominant themes underlying the financial discussions in recent months in the OECD in Paris, and in the periodic discussions among central bankers at the monthly meetings of directors of the Bank for International Settlements in Basel. In all these discussions, the effects of differences in levels of short-term interest rates prevailing in different countries, desirable and undesirable, has been one of the subjects receiving attention. The desirability of some coordination between countries of fiscal and monetary policies with a view to developments in other countries is increasingly recognized as a necessary condition for a viable system of interconvertible currencies. Indicative of this development, several European countries, starting as far back as the fall of 1960, made deliberate efforts to reduce the levels of their short-term rates—partly in consideration of our problems, but more immediately because large-scale inflows of funds were tending to defeat the aims of their own domestic stabilization policies.

Nevertheless, the fact that, for reasons already given, the interrelation of interest rates and short-term capital movements is not clear cut indicates that there is no strong case for urging on other countries a priority for fiscal policy over monetary policy as a means of influencing their internal situations. Moreover, while a stronger fiscal policy should normally make possible a somewhat easier task for monetary policy, the two are not completely substitutable one for the other. An effective stabilization program requires both types of policy. Particular countries will undoubtedly find it necessary to adapt their policy mix in accordance with the shifting internal and external problems they individually confront, though at all times giving account to their longer run stabilization and growth objectives.

Undue stress by other leading countries on fiscal policy might produce results fully as unsatisfactory, from the standpoint of maintenance of their maximum employment and their contribution to international payments equilibrium, as those that would be brought about by undue stress on monetary policy.

Question 3. Is there not an important difference between the so-called basic items in a balance of payments—trade, services, military expenditures, Government investments and private capital investment—and those items reflecting short-term capital movements? Is not a flight of short-term capital due to discrepancies in interest rates a different kind of money movement not necessarily reflecting fiscal or monetary irresponsibility on the part of the country having somewhat lower interest rates? If this is so, might it not be worth while to see if we could not erect a new principle of international monetary morality along the following lines: Central bankers are welcome to demand gold for any of the deficits caused by basic structural shifts, but, if the deficit is caused, and to the extent that it is caused, by one of these innocent short-term capital outflows, central bankers should not, in the interest of the free world monetary system, demand gold in the same amounts and quantities as they otherwise might.

Answer. The discussion of the first question indicated that international movements of short-term funds respond not only to interest-rate influences but are also affected by various other factors. It was noted that movements of short-term credit are influenced by borrowers' demands and by the availability of credit in one lending country or another as well as the competitive cost of credit as between countries. While movements of funds for short-term investment in liquid forms are naturally affected by interest-rate differences among developed countries, the influence on such fund movements of the interest-rate differences is modified by the action of forward exchange markets. Finally, expectational and confidence factors at times give rise to large-scale speculative movements of funds that are committed on a short-term basis.

In the answer to the second question it was noted that international discussions of the effects of national policies on international payments have given due attention to interest-rate relationships, but have also concerned other influences affecting international payments flows. National policies in other countries, it was suggested, may influence the U.S. balance of payments in various ways. Short-term capital movements, therefore, cannot be viewed in isolation from other forces shaping a country's balance of payments.

Progress has been made in the past year toward effective measures of international cooperation to deal with emergency or temporary situations that might threaten the stability of the international payments mechanism. The principle underlying such cooperation is not that short-term capital movements, per se, call for a special kind of treatment. The principle is rather that any large and sudden drain on a major country's monetary reserves represents a threat to the functioning of the international monetary system, and that all countries have an interest in forestalling or coping with such threats to the system.

Short-term capital movements, partly motivated by confidence factors, are characteristically an important contributory cause of the large and sudden drains on a country's monetary reserve position that are here in question. Such adverse changes in reserve position are less likely to occur when a major country's fiscal and monetary conditions are in approximate equilibrium with those of other countries and when its international payments on current and long-term capital accounts are in sustainable balance.

The Basel arrangements of March 1961 to help the United Kingdom cope with a sudden and wholesale outflow of short-term funds, and equally the recently concluded agreement between 10 industrial countries to stand ready to lend their currencies to the International Monetary Fund under certain circumstances, are evidence of a spirit of international cooperation and interresponsibility in making the mechanisms of international payments work satisfactorily. But the viability of this kind of international cooperation depends very much on the ability and determination of countries that receive assistance to play their full part, through appropriate domestic and foreign economic policies, in bringing their own international payments into reasonable and durable equilibrium.

While these arrangements do make for economy in the world's use of gold as a means of final settlement in international payments, there is no way under the existing organization of monetary systems among the major countries to obviate, automatically, demands for final settlement in gold. Gold has a statutory role assigned to it in the monetary systems of these countries; it is a means of international settlement that in fact has general acceptability; and it has the prestige of long tradition in performing international settlement functions. The monetary authorities of each country, in the light of their trusteeship responsibilities, are obliged to give account to the allocation of their reserve resources between gold and other assets eligible to meet reserve needs.

A country whose payments are in deficit on current and long-term capital accounts cannot safely disregard short-term capital outflows as an additional element magnifying its overall deficit and affecting its monetary reserve position. Nor can it ask other countries to abstain from converting to gold those accretions to their reserves that are related to the capital outflows—even if it were conceivably possible to determine that certain capital flows had resulted from interest-rate differences. Consistent application of a principle that gold should not move with short-term capital flows would work to the disadvantage of a deficit country in some circumstances, as for example at a time when it might need to attract inward movements of capital as one way of overcoming its deficit in international payments.

Senator DOUGLAS (presiding). Mr. Javits.

Senator JAVITS. Mr. Chairman, I would like to fix your attention on one major point, and that is the unemployment point. As it is often useful to exclude as well as to include, I would like to ask you, without putting words into your mouth but just by way of phrasing the question, whether you mean to tell us that structural unemployment, in your opinion, is not, as you say at the top of page 5, "readily responsive to general montearv and fiscal measures" any more?

Mr. MARTIN. I don't think that it is. I think it has very limited impact on it. I think we have to attack both structural unemployment and cyclical unemployment. I don't think that the structural unemployment is effectively dealt with by fiscal and monetary measures.

Senator JAVITS. I say that because it is often a fiction that you can manipulate money around and credit, and that will fix everything. It is so important to get your highly informed judgment on the fact that this is not the problem in dealing with this in the economy. You said—

The fact that long-term unemployment has been disturbingly large over the last decade, even during periods of high-level activity and rising prices, indicates that the problem it poses is too complex to be solved by any single or simple approach.

You add to that that it is obviously too complex to be readily responsive to general monetary and fiscal measures. Do we take that to be your view?

Mr. MARTIN. That is my view, sir.

Senator JAVITS. Do you feel that the entire section of industry, business, and government, are all required to deal with occupational and geographical mobility, training and retraining, and better information on the current and prospective job market? Is that correct?

Mr. MARTIN. I agree completely.

Senator JAVITS. Do you feel also, Mr. Chairman, and this goes a little bit outside of your specialized line but it is very important, that there is something else to be added in terms of the American worker, and that is some new objective other than what has been the objective stated by Samuel Gompers for now almost five decades: "more?" Would you agree with that, that we need some new objective, some new incentive to greater efforts than has been represented up to now by the word "wages" and salaries: "more?"

Mr. MARTIN. Yes, I think I would agree with that.

Senator JAVITS. There are two, it seems to me, avenues for that, aside from what Government can do in specific measures. We have the retraining measures before us now, as a matter of fact, and which the Senate has passed. It is pending in the House. There is the idea of adjustment assistance. There is the idea of encouraging automation, and I suppose before very long we will be thinking about adjustment assistance in that respect, too. But other than that, there are two things which I would like to get your view on. One is the idea of a far greater emphasis than has ever been the case before on stock ownership or profit participation as being a sideways move, away from the line which American labor has taken all these years, more wages and more salary.

Mr. MARTIN. I am not competent in that area, Senator, but I think it ought to be carefully explored.

Senator JAVITS. The other question I would like to ask is this: It is not directly in your line, but it troubles me very much. Do you think we have adequately laid before the American worker the demands upon him in terms of patriotism as they were laid before him in World War II, and at a time when, in my opinion, they are at least as urgent, or perhaps more so?

Mr. MARTIN. I think that goes for management as well as for labor. I think that we are in the cold war today, and I think that it is important that this be understood more widely than it is today.

Senator JAVITS. I was going to ask you that as my next question. You anticipated me. As to management, what in your view, as the chairman of this great body, can be done about management? Let's assume we all ask Arthur Goldberg about labor, but I think we have a right to ask you and the Secretary of the Treasury, the other high officials that deal with business and management and banking, what can be done about firing management's imagination and patriotism in terms of this tremendously grave issue which we face? You will recall that we had a very extended debate on the floor of the Senate last year on the steel price increase, in which, I think, a very heavy element of debate was the appeal to the innate public interest of management. I just would like to have your comment on that.

Mr. MARTIN. I think that is very desirable and very essential. We tried, in my prepared statement, to point up the necessity of new and better products, and the fact that employers and employees have a very real responsibility in this country, vis-a-vis the world today.

Senator JAVITS. Has there been any thinking in the Board of any technique by which this can be done? For example, I have suggested the idea of a Peace Production Board, to try to prevail upon labor and business, as we did through Donald Nelson and Sidney Hillman in World War II, to try to coordinate in the same way due to the exigencies which we face.

Mr. MARTIN. No, I can't say that there has been any discussion of it, but I will take your comments as an incentive for us to have some discussion of the problem in the Board.

Senator JAVITS. In any case, your feeling is that we certainly have to go beyond the fiscal and the monetary in this field?

Mr. MARTIN. That is right.

Senator JAVITS. And that it is urgent and that it has a very critical relation to not only the economic condition of our country but is generally healthy in terms of its security.

Mr. MARTIN. I do.

Senator JAVITS. I thank you, Mr. Chairman.

Senator DOUGLAS. Senator Proxmire.

Senator PROXMIRE. In the annual report of the Council of Economic Advisers, on page 90, there is a statement that says:

> The behavior of interest rates during the year may also have signaled the ending of the upward trend in rates from the low levels at which they were peaked prior to the Treasury-Federal Reserve Board accord of 1951.

Would you share that opinion, that this year may have signaled the end in the upward trend in interest rates? I am not asking if rates wouldn't be higher under a strong inflationary pressure. But is it your feeling that the upward trend has probably ended?

Mr. MARTIN. I wouldn't make a categorical prediction on that, Senator. I just wouldn't feel that it would be justified.

Senator PROXMIRE. You don't think then, as the Council of Economic Advisers—on the basis of the facts as you know them, you feel that there is no economic basis for justifying that kind of conclusion?

Mr. MARTIN. I don't say there is no economic basis, but I say it is a judgment. I am very respectful of their judgments, but I wouldn't want to get into bed with them on that.

Senator PROXMIRE. Why would you feel that the trend would continue to climb? How would you expect that, in view of the fact that we have had a period now of more than 10 years since the end of the Treasury-Federal Reserve accord, and a sharp increase in interest rates since then?

Mr. MARTIN. I would hope as they would hope, that with a judicious blend of fiscal and debt management and wage cost policies, if we have that meshing, that we could achieve what they are suggesting as possible here. We have had too many fits and starts since the end of World War II for me to have confidence that we have achieved that goal. We have made progress toward it.

Senator PROXMIRE. Let me try this another way. Looking at the present level of interest rates, historically, from a historical standpoint, and internationally, compared with interest rates abroad, would you think it unreasonable to say that this level of interest rates we have now might be regarded as a standard possibly in the future?

Mr. MARTIN. I wouldn't know how to gage it because, as I said earlier, our interest rates are lower in relation to the world at a time when capital and credit can move pretty freely from one country to another and all important countries are competing for the available supply of capital and credit.

Senator PROXMIRE. Well, of course, there are many reasons for that, as you know far better than I do. The fact is that we have a Government that has been stable for a much longer period, we have conditions which have been stable—which have been stabilized, we have less risk, perhaps, et cetera.

Mr. MARTIN. All of those are factors, I agree.

Senator PROXMIRE. The main thrust of your testimony is, as I understand it, in the beginning part of it, is that productive efficiency, an increase in productive efficiency in the American economy, is the answer to unemployment, or a very important part of the unemployment, as far as growth and stabilized prices are concerned, is that correct?

Mr. MARTIN. And the balance-of-payments problem.

Senator PROXMIRE. I agree with you wholeheartedly on this great desirability, of course. But the studies that I am familiar with indicate that there is no such correlation as you imply between greater efficiency and reduced unemployment. I am talking particularly about the Solomon Fabricant and Harold Levinson studies. The absence of any statistically significant shortrun relationship between productivity and employment has previously been established by

Solomon Fabricant for the periods 1899 to 1909, 1909 to 1919, 1919 to 1929, and 1929 to 1939, and by Harold Levinson for 1947 to 1958.

In the light of that, plus the fact that we can see this vast improvement in productivity in the coal mining industry, for example, and some substantial productivity improvement in the railroad industry, concommitantly with a sharp increase in unemployment, and no improvement in the employment picture there. I am wondering on what basis do you feel increased efficiency might help solve our unemployment situation?

Mr. MARTIN. Well, I think that you have to increase demands. That is why I said a number of times recently that I think in the 1950's to a large extent the consumer was the forgotten man. I think one of the ways that we can increase demand and encourage the consumer is to get lower prices or new products and better products through research and development which will attract him to spend his money on them. I think the time has passed when we can pass on to the consumer whatever price increases we happen to develop in the economy. I do think there is a difference between structural and cyclical unemployment. I think both of them have to be attacked. But I think that the basic problem we are dealing with here is becoming, again, one of meeting world competition. I think it is only by increases in productivity and investment in capital and in plants and equipment that we are going to do it.

Senator PROXMIRE. I agree. I think the case is very strong that we are going to have all kinds of benefits from increased productivity. I am certainly as enthusiastic for that as anyone. But I am wondering about the tough, perplexing, constant problem we have in unemployment, in which we don't seem to be making much progress. I am wondering if the contribution here is as great, if we rely on increases in efficiency to solve this particular problem, and I say there is nothing in economic history to indicate efficiency improvements will reduce unemployment. Let me move into another area as quickly as I can. There are two studies that this committee has had, one presented last year by Mr. Tobin, of the Council of Economic Advisers, indicating that in his judgment at the present time structural unemployment was a far lesser factor than deficient demand in unemployment, and the other was a study that you may be familiar with made by the Statistical Subcommittee of this committee?

Mr. MARTIN. I made reference to that in my statement.

Senator PROXMIRE. Yes, you did. Then, in this particular study, in the summary of the findings, they have a series of points which it seems to me are very hard to answer in saying that the structural unemployment is not really very significant.

They say:

> In manufacturing the rate of advance has been slower during the postwar period than in the 1920's; while some nonmanufacturing industries have shown a faster rate of advance than in the 1920's. The evidence for 1957–60 is ambiguous but on balance indicates no acceleration compared to the 1948–57 period.

They go on to say:

> There has been no autonomous increase in the variability of employment changes in manufacturing, either since the 1920's or since 1957.

That is if you compare various industries, you don't find there is more unemployment in some industries as compared with others any different than we have had in the previous periods of American economic history.

The next point is:

Unemployed workers have been at least as geographically mobile since 1957 as earlier in the postwar period.

I point out, as a matter of fact, that we have a greater degree of education in our work force now than in the past, so that our workers are more easily trained now than they were at any time in our economic history.

The staff report goes on to say:

Unemployment rose among all groups of workers between 1957 and 1960, regardless of industrial or occupational attachment, which would indicate nonstructural.

Changes in unemployment in 1957 and 1960 duplicated the patterns which previously occurred.

Independent investigations indicate the existence of an extraordinary amount of interindustry mobility.

And finally:

Available evidence indicates the number of nonfarm job openings was lower in 1959–60 than in 1955–57 in every major occupational category.

All of this seems to me to be a pretty unanswerable argument. That the problem is not one of structural problems primarily, but one of deficiency in demand.

Mr. MARTIN. It is partly this deficiency in demand that I want to correct by lower prices and new products. That is why I talked about the consumer. Nevertheless, while I think that study is a very useful one, I don't think that it indicates that we shouldn't do everything we can to attack structural unemployment as well as cyclical unemployment. The significance of a correlation is always in question and all of these correlation studies have pitfalls when they extend their correlation results into generalizations. I think that we have to be very wary of basing conclusions on them because the period we are in has been arrived at by a lot of steps, a lot of miscalculations, a lot of misjudgments, a lot of mistakes made at one time or another in the past. I don't believe that these correlations can be fitted into modern conditions on the basis of what has happened previously. Again, as I said to Mr. Reuss, we all have our theories on this. I advanced this only as a theory in part. But I say that there is no question but that this country since 1957 has entered a new era of competition embracing the whole western world. If this theory is valid, there are different factors and different correlations that would apply today. Since 1957, in my judgment, we have had a new world to deal with.

Senator PROXMIRE. I see my time is up. Thank you.

Senator DOUGLAS. Mr. Kilburn.

Mr. KILBURN. Mr. Chairman, as always I learn a great deal from Mr. Martin when he testifies before us.

I have just one question. We have a bill up in the House about foreign branches of national banks and the supervision that the Federal Reserve gives them. The thought behind the bill, as I understand it, is to make them more competitive with their competitors in foreign countries. The question was raised: Do those banks take any money out of this country to lend abroad? They do supplement, certainly, the Export-Import Bank. It is private enterprise taking over from a Government institution. I would think we should encourage them to do it. But the question was asked as to whether they take money out of this country and take it overseas. Do they?

Mr. MARTIN. I think some money goes into those branches. If you were traveling abroad, you might make a deposit in a branch over there. I don't think it is a great deal. I personally think that bill ought to be passed. I think that the foreign branches of American banks ought to be allowed to compete with their fellow foreign institutions on about the same basis and not be hampered by the sort of regulations that we have here. I think we ought to encourage them.

Mr. KILBURN. Don't most of their deposits come from the country where they are located?

Mr. MARTIN. In large measure, yes, sir.

Mr. KILBURN. In fact, what they are doing is taking a deposit from that country and lending it, on the basis of their judgment of course, to develop that country?

Mr. MARTIN. That is right. That is the great bulk of their business.

Mr. KILBURN. Instead of having the United States put it up through a Government corporation?

Mr. MARTIN. That is correct.

Mr. KILBURN. Thank you.

Senator DOUGLAS. Mrs. Griffiths.

Representative GRIFFITHS. I would like to ask one question for Mr. Rice. Do you know accurately or do you have to estimate the amount of short-term funds going abroad?

Mr. MARTIN. No, we don't know accurately, Mrs. Griffiths. That is one of the things that we have to try to develop better information on that we have.

Representative GRIFFITHS. How do you estimate it now?

Mr. MARTIN. We do it largely by word of mouth in covering the area until after the funds have flowed abroad.

I might ask Mr. Young, who has worked on this, to discuss that. Ralph?

Mr. YOUNG. We do get monthly reports, of course, from quite a number, and weekly reports from some, financial institutions that would be in a position to furnish the information that would be helpful or at least indicative of what was happening. Of course, this all has to be all added up together. But it is an extremely difficult area in which to develop an effective means of collecting information and having that information promptly available.

Representative GRIFFITHS. Historically, if we have increased the interest rates on short-term funds here, has the amount of money that goes abroad dropped?

Mr. MARTIN. The problem there, Mrs. Griffiths, is the level of interest rates, and the general attitude of people as to where they want to have their funds. Interest rate differentials and availability of funds do have some impact. Now that we have convertible currency there is more tendency for people in London to look at New York, and New York to look at London. We have every day at the Board now a sheet of paper that gives us rates on most of these currencies.

Representative GRIFFITHS. If you increase the interest rates on short-term bonds, you buy short-term bonds and there isn't a drop in the amount of money going abroad, then do you gage the impact because there is no increase?

Mr. MARTIN. Do I understand you to mean no increase in the outflow?

Representative GRIFFITHS. In the outflow of money.

Mr. MARTIN. How the flow of money responds is one of the factors we take into account. I don't want to be technical here, but on the matter of interest rates we don't raise them. We merely operate in a market.

Representative GRIFFITHS. Yes, I know. But do you gage the impact of this because there is no increase on the other factors that you are able to observe?

Mr. MARTIN. Yes.

Representative GRIFFITHS. Thank you very much.

Senator DOUGLAS. Senator Pell?

Senator PELL. Mr. Martin, in connection with the Stabilization Fund which you mentioned, the Treasury Stabilization Fund, does it have a working relationship with the International Monetary Fund?

Mr. MARTIN. Yes, it has a working relationship with the IMF. It was established under our Gold Reserve Act of 1934. That is how the Stabilization Fund came into being. It was out of its resources in part that the resources for the International Monetary Fund came.

Senator PELL. In connection with the Gold Reserve Act, do you believe that the 25-percent gold reserve requirements should be kept or should they be removed?

Mr. MARTIN. I don't think that the 25-percent requirement, Senator Pell, is essential, but it is a safeguard. It is a matter of timing. In my judgment, it is not urgent to remove the 25-percent gold cover at the present time, as long as it is understood that we are going to place all of our gold behind the dollar and do everything else in our power to maintain the value of the dollar. Our President has gone on record that that is our position.

Senator PELL. Do you see any political danger in keeping our currency tied in with gold when the gold is produced primarily by either the Soviet Union or the Union of South Africa, both of which are posed with many problems?

Mr. MARTIN. Gold has had a long historical role. It may be that you could substitute a lot of things, barley, platinum, a lot of other things for it. But it still is the one acceptable media the world over. It may take a great many years before you substitute anything for it.

Senator PELL. In conclusion, Dr. Heller, when he was here, mentioned the importance of the union pension funds in the country's economy, and said that he thought that they should be more stringently supervised, analyzed, studied and followed by a Government agency. He did not mention which one. I have heard the thought expressed that it might be the Federal Reserve Board. Does that make any sense to you?

Mr. MARTIN. Well, we have enough problems at the present time, Senator, without asking for any more.

Senator PELL. You would be opposed to that, to having it under your jurisdiction?

Mr. MARTIN. I would not seek it.

Senator PELL. Thank you. Thank you very much.

Senator DOUGLAS. On at least the two previous occasions when you have returned from the meetings of the banking authorities you have stated how the officials of the European central banks are greatly worried about deficits in this country and increases in the American price level. I thought it appropriate to ask the Bureau of the Budget when the Director testified last week, about the comparability of the budget figures of the major European countries, and I brought out the fact that whereas we include capital improvements in our administrative budget the European countries almost uniformly exclude them and have a separate category for them. I then asked if they would prepare figures on a comparable basis to indicate the degree to which our country and the European countries had made comparable records. I have just been given a report which interests me and which may interest you. It speaks of the study carried on by Mr. Grant. It compares the budget results of the central government of Great Britain, France, Western Germany, and the United States, adjusted to a basis comparable to the United States consolidated cash statement, that is, Federal receipts to and payments from the public. The study showed that England ran deficits in 9 of the last 11 calendar years; France in every one of the last 10 calendar years; and Germany in 4 of the last 6 calendar years. In the 11 calendar years, 1952–60, inclusive, the United States ran surpluses in 5 years and deficits in 6 years.

In other words, the United States made a much better record than England, France and Germany. In view of the very sarcastic comments made by Mr. Blessing at Vienna about the very bad financial practices of the United States, in which he was echoed by Mr. Baumgartner, president of the Bank of France who himself carried out inflationary policies, I thought it would be interesting if you would send these figures to them with our blessings. It might lend a certain degree of humility to these gentlemen and it would strengthen your hand in defending the record of the United States before these banking pundits.

Mr. MARTIN. I will be very glad to send it to them.

Senator DOUGLAS. Of course, as far as stability in the price level is concerned, if one takes the wholsale index, the index for 1957 was 119.2 and for December 1961 it was 119.2, so there has been almost complete stability in the wholesale price levels. The increase in the retail price index, as our good friend from Missouri has brought out, may be illusory, because it may be accounted for by improvements in quality. I do not despair of the United States record. I would not think it occasioned stringent monetary measures.

If you could only get them, Mr. Martin, to take a larger share of the cost of NATO, provide a larger degree of foreign aid, to be more liberal in their trade policies and admit, at least, our farm production, the temptation that you would have to increase interest rates would be less, is that true?

Mr. MARTIN. Yes. I took a strong position along those lines in this statement, Senator Douglas.

Senator DOUGLAS. Is there anything we can do to strengthen your hand? We are anxious to be of assistance to you in your struggle with the European banking authorities.

Mr. MARTIN. I am not the one to negotiate with the Europeans.

Senator DOUGLAS. You have a great tangential influence, though.

Mr. MARTIN. Well, I use that influence along the lines that you suggested at every opportunity.

Senator DOUGLAS. Would you like to have me write letters to them myself or will you take this up with the European banking authorities?

Mr. MARTIN. I will do whichever you would like.

Senator DOUGLAS. I wish you would send it to Mr. Blessing.

Mr. MARTIN. Mr. Baumgartner is now out of office.

Senator DOUGLAS. Send it to all those who are complaining about America's financial policies who in the past have greatly impressed you.

The next question I want to raise is highly theoretical and not a subject that can be acted on immediately. It is important, though, I think, for the future. In the 19th century we had was was assumed to be more or less a free working competitive order, with prices, wages, interest rates and so forth, fluctuating. I think the country has properly taken the stand that it does not want to have unemployment created permanently by high interest rates. Frankly, I think our balance of payments problems and the higher interest rates associated with it has been one of the difficulties in this country, and in England. We do not want to hold back an adequate rate of economic growth by high interest rates, but we have not been entirely free to pursue proper domestic policies certainly in England and in this country. So I think the needs of the Nation are such that ordinary monetary policy is, in a sense, antiquated.

We know that the competitive pricing system of the 19th century has been largely replaced by a monopolistic pricing system, in which reductions in prices are almost impossible to effect, and that wage policy has been effected both by the coming of unions and other factors so that the possibility of a downward movement in wages does not exist. So the internal flexibilities in prices have been greatly reduced.

On top of that, the central banking authorities have adopted a fixed exchange ratio, under the gold exchange standard, and it is, I think, interesting, and not unconnected with the fact, that the two nations which, in a sense, furnish the currency reserves in addition to gold, namely Great Britain and the United States, have had the lowest growth records of any two major countries in the Western World. I think it is some evidence to indicate that this low growth rate is connected with a desire to protect our international banking position.

I would like to raise this question: Instead of having fixed exchange rates, why would it not be a good thing for the Western World to adopt a fluctuating exchange rate? Then we wouldn't have to worry about the balance of payments on gold reserves. Exchange rates would fluctuate according to the relative balance of imports and exports, claims and debits, and there would be an automatic adjustment. By providing freedom in exchange rates, this would permit the system to function without being greatly impeded by all these factors heaped on top of each other. I don't expect this proposal to be adopted tomorrow morning at 8 o'clock, but is not this something that should be considered?

Mr. MARTIN. The International Monetary Fund has been debating this question of fixed versus fluctuating rates ever since it was organized.

Senator DOUGLAS. But it has always turned down the idea of fluctuating rates and has always come out for fixed rates?

Mr. MARTIN. There are advantages in fixed rates. This is a long subject, Senator, but there are advantages and disadvantages that have to be weighed.

Senator DOUGLAS. You have had personal conversations with a great many of the experts at the Federal Reserve, and I must say I have felt that they had fixed ideas in favor of fixed exchange rates?

Mr. MARTIN. Maybe they are justified in that.

Senator DOUGLAS. Well, it is possible, but I think it is very interesting that there are banking authorities who have in recent years turned their back on a flexible international system of exchanges. This is the point that they hold to. I think they have contributed a great deal, if I may say so, to the difficulties that the world is now in. You don't want to go into it further?

Mr. MARTIN. No, sir.

Senator DOUGLAS. Are you examining this subject? Have you a closed mind on it?

Mr. MARTIN. No, I do not have a closed mind on it. I don't think I have a closed mind on anything, Senator.

Senator DOUGLAS. Do you ever discuss this subject when you gentlemen get together at the palaces of Europe to discuss the world monetary problems?

Mr. MARTIN. I think probably you are more familiar with the palaces of Europe than I am, Senator.

Senator DOUGLAS. No, not at all. Do you ever discuss this in meetings?

Mr. MARTIN. Yes, indeed. Many times.

Senator DOUGLAS. And the verdict is always "No"?

Mr. MARTIN. No, it is always that there are some advantages and disadvantages.

Senator DOUGLAS. Would you prepare a memorandum for this committee on the advantages and disadvantages, or have some of your staff prepare that memorandum?

Mr. MARTIN. We will do our best.

Senator DOUGLAS. Thank you.

(The material requested was not received at the time the hearings were printed. When received it will be made a part of the committee files.)

Mr. Curtis.

Representative CURTIS. No further questions.

Senator DOUGLAS. Senator Proxmire?

Mr. MARTIN. Could I just say to Senator Douglas that Mr. Young tells me there is a recent book at the University of Chicago on this subject.

Senator PROXMIRE. I have suggested various studies of unemployment factors in this unemployment situation. The only ones we seem to have indicate that structural factors are far less important than demand deficiency. I highly respect your opinion and position. It has been cited by many others as just about the best evidence that structural is very important. I wonder if the Federal Reserve can make a study of this that might indicate some of the reasons why you think the structural factors are responsible, substantially responsible?

Mr. MARTIN. We would be very glad to. We have some very good people on our staff.

Senator PROXMIRE. Now on another subject. Would letting the market operate with regard to investments abroad, freely, which you said you favor, as I understand it, mean that you would eliminate the 14-percent corporation income tax advantage that now goes to South America investments, and the deferral of taxation on investments abroad until the money is repatriated?

Mr. MARTIN. No, I didn't mean to make any comment on taxation, Senator. All I meant to say was that I would be against placing direct controls on American private investments abroad. I am against that type of control. That is really the point I was trying to make.

Senator PROXMIRE. It is true at the present time that with the tax advantage we give investments abroad, it can hardly be considered a free investment market, can it?

Mr. MARTIN. Well, those incentives—I am never very happy about that type of thing, because essentially I am a free market man.

Senator DOUGLAS. Except on the exchange rates.

Mr. MARTIN. We will cover that, Senator, in our memorandum.

(The material requested was not received at the time the hearings were printed. When received it will be made a part of the committee files.)

Senator PROXMIRE. You discuss the Federal Reserve's efforts with regard to Treasury bills, 1- to 5-year, 5- to 10-year, and more-than-10-year obligations. The argument was used yesterday when the advisers to the Federal Reserve Board appeared before the Senate Banking Committee, and the argument that you seem to imply here, is that you couldn't have played a much more aggressive role with regard to obligations of 5 to 10 years and 10 years and over because you were already such a big factor in the market. That is, when you account for 20 percent of the trading, you might feel that if you did any more you would destroy freedom in the market. Would that be correct?

Mr. MARTIN. That is correct. It is always a matter of judgment. I think we went as far as we were warranted in going on this.

(In response to a staff request for further explanation of these figures, the following additional information was supplied:)

All of the figures given in this paragraph relating official market purchases to dealer sales exclude, from the dealer sales base, sales to other dealers, as indicated in the parenthetical phrase at the end of the second sentence of the paragraph. The reason for excluding sales to other dealers is that for the most part these sales represent transfers from one dealer's shelf to another and not additional securities sold to customers, and would give a distorted picture of the market demand for the securities if included.

It may be helpful to give in dollars the figures involved for issues maturing in 5 to 10 years. In this area, total sales in 1961 were $6.9 billion; of this total, about $2.5 billion were sales to other Government securities dealers and brokers. Subtracting the latter figure gives an adjusted total of $4.4 billion for dealer sales. Official purchases were about $900 million. This represents approximately 20 percent of dealer sales, excluding sales to other dealers.

Senator PROXMIRE. There are just two things that bother me about this. In the first place, when you are this big a factor it seems to me that you can play a really important part so far as the economy is concerned in lowering interest rates on long-term obligations, to the great benefit of the economy. In the second place, I notice, for example, between June and September—I don't have later figures—the Treasury Department purchased a billion dollars of additional long-term securities, apparently, or at least they advised Government agencies and trust funds to do so, while the Federal Reserve increased their portfolio relatively slightly—$63 million.

Mr. MARTIN. Well those trust accounts were being invested for longer term reasons. The last thing that the Federal Reserve ought to do in my judgment is to destroy the long-term market. We want the Treasury to be able to sell long-term bonds, and we want a good long-term market. The long-term market is a very different market from the short-term market. A lot of people seem to think that these long-term securities are just here on a shelf the way they are in a grocery store, and that you can just go up and grab some of them off. Here is a pension fund in a trust account that hasn't any intention of selling a long-term Government security. You don't have too many of those people left in this country. You start playing around with that market and after a while, the first thing you know, you have no market. When we got up to 33 percent of dealing in that market, I think we went as far as we should. This was a matter of judgment that weighed heavily with the Federal Reserve Open Market Committee in its discussions every 3 weeks, in attempting to disperse our influence through that market, without trying to control or make the market or return to fixed interest rates.

Senator PROXMIRE. But the difficulty is that your additional purchases have been concentrated very largely in the 1- to 5-year category. As far as the impact on housing loans, and this seems to be the area where monetary policy is, it seems to me, most constructive, useful, and encouraging, these are much longer term and we still have these relatively high interest rates compared to most of the past periods.

Mr. MARTIN. I have tried to emphasize repeatedly here that it is the flow of funds that we are concerned with, and I think the record of the second quarter indicates that we were quite successful on the flow of funds because we had a record number of State, municipal, and other securities floated in that period with a maximum of stability in interest rates. In other words, we did have some influence. I never claim too much interest rate effect for this because interaction does occur between markets, and we are not in a position to fix rates unless we become the market entirely and put ourselves in the position where the only way the Government sells its securities is to sell them to itself, which I think would be a very unfortunate thing. If we were successful in this operation—and I claim some of the credit for it—it was in getting a flow of funds and not in fixing interest rates. But we were successful in having a strong flow of funds in the second and third quarters of this year, in the longer term market. I believe our activities and the Treasury activities made some contribution to that.

Senator PROXMIRE. I think they probably did, as compared to a situation in which there was a net borrowed reserve position, for example. My only argument is that if the free reserves were higher than they are, there might have been more incentive for the banks to lower interest rates and for others to have lower interest rates on long-term obligations.

Mr. MARTIN. It probably would have come about if the free reserves had been higher. But the judgment that the Open Market Committee has to make is what the level of these reserves ought to be in terms of the best interests of the economy.

Senator PROXMIRE. It is the best interests of the economy that concerns this committee so much. The Budget, the Secretary of the Treasury, the Council of Economic Advisers, are all thinking so much now in terms of the economic impact of Government, particularly the Budget, on the economy, and somehow I am wondering if the monetary authorities, which have always been the one instrumentality that everybody agrees should be used for economic stabilization, if they feel now that they can be more aggressive with regard to economic situations but less concerned for the technical problems, which are a real responsibility, but less concerned perhaps than for the economic stability, the economic growth.

Mr. MARTIN. Well, I think the record in the last year shows that in our judgment we have been making as much of a contribution in this direction as we could. We can always, as a matter of judgment, say there ought to be more. Our problem would be a whole lot easier if we could just take a slide rule and determine what the level of reserves ought to be at a given time. We have no control over what uses the banks make of these reserves. What we have to do is to supply the needed reserves, or perhaps a little bit more, but without producing a sloppy money market that will induce foreigners and others to take advantage of that money market for speculative purposes. At one point early last year we had a stock market that looked very silly in terms of a good many things. There was some money floating around and some of it went into manipulations of one sort or another that may be unavoidable in the economy. But, nonetheless, that is the sort of thing we have to deal with in making judgments. If you were on the Federal Reserve Board, you might think that you could have a little bit more or a little bit less. But we have 19 men, 12 of them that vote, that sit around every 3 weeks and try to gage this in terms of all these factors.

Senator PROXMIRE. Let me just try and sum up and conclude by asking this: Would you share the opinion that has been voiced in this committee by the Council of Economic Advisers, by the Director of the Budget, that the conditions now seem appropriate for a continued period of credit ease and of monetary policy that might be encouraging the economy?

Mr. MARTIN. I wouldn't make any prediction on the future. I don't think you should. Markets are watching what I say today. I don't think I should be forecasting the future. The demands for funds is something that is not predictable. One of the things this year that has been interesting is that banks have constantly expected the loan demand to be greater than it has turned out to be. There are many factors, many reasons why that hasn't been so. But what the situation will be 3 months from now I don't know. I don't think I ought to put my open market committee in the position——

Senator PROXMIRE. No, I didn't mean that. With the situation in which we have still 6-percent unemployment, in which we have stable prices, as Senator Douglas pointed out.

Mr. MARTIN. Conditions at the moment are favorable. How long those conditions will remain that way I wouldn't want to forecast. That is where it comes out.

Senator PROXMIRE. Thank you very much.

Thank you, Mr. Chairman.

Senator DOUGLAS. Mr. Curtis?

Representative CURTIS. I have just one question that is a little offbeat, but I would appreciate it if you would give an opinion on it. With the public debt the way we have it now, the size it is, would the use of a consol be of some value? What are the reasons? I don't know, but what are the reasons that we have never gone to that use of an open-end security?

Mr. MARTIN. It has been considered a number of times. Again it is a long subject. I hope that we won't issue any consols that will sink as low as our British consols have sunk.

Representative CURTIS. Are they not a pretty good category though?

Mr. MARTIN. I wouldn't say they are an indicator, but I might say in terms of the United Kingdom economy that this is a judgment. But I say they don't have any substantial Government securities market outside of the Bank of England today, and I hope that this country won't reach the point where the only market for Government securities is the Federal Reserve.

Representative CURTIS. What brought this to my mind is, as you were discussing with Senator Proxmire, with our pension fund going up the way it has, it would look like that kind of security would be of some advantage.

Mr. MARTIN. It could be. It certainly ought to be considered. I am sure the debt-management people in the Treasury have been turning over all of these ideas.

Representative CURTIS. Thank you.

Senator DOUGLAS. Thank you very much.

We will recess and reconvene tomorrow morning at 10 o'clock.

(Whereupon, the committee recessed at 4:10 p.m., to reconvene on the following day, Wednesday, January 31, 1961, at 10 a.m.)

JANUARY 1962 ECONOMIC REPORT OF THE PRESIDENT

WEDNESDAY, JANUARY 31, 1962

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

The Joint Economic Committee met, pursuant to recess, at 10 a.m., in room P–63, the Capitol, Senator John Sparkman presiding.

Present: Representative Wright Patman (chairman), Senators Sparkman, Proxmire, Pell, Bush, and Javits; and Representatives Reuss and Widnall.

Senator SPARKMAN. The committee will please come to order.

This morning the committee continues hearings on the Economic Report of the President. We are privileged to have with us this morning, the Secretary of Labor, the Honorable Arthur J. Goldberg. Mr. Secretary, I notice you have a prepared statement, and each of us has a copy of it. You may proceed in any way you like. If you wish, you can read the statement or if you prefer to summarize you may do that, and the statement will be printed in the record as a whole.

For the benefit of the record, will you identify your associates who accompany you? We shall appreciate that, and then you can proceed in your own way.

STATEMENT OF HON. ARTHUR J. GOLDBERG, SECRETARY OF LABOR; ACCOMPANIED BY CHARLES DONAHUE, SOLICITOR OF LABOR; DR. SEYMOUR WOLFBEIN, DEPUTY ASSISTANT SECRETARY; AND DR. EWAN CLAGUE, COMMISSIONER OF LABOR STATISTICS OF THE DEPARTMENT OF LABOR

Secretary GOLDBERG. Senator Sparkman and gentlemen of the committee, I appreciate very much, Mr. Chairman, your very kind reception.

I would like to present my colleagues, I think that you know them all: This is Mr. Ewan Clague, Commissioner, Bureau of Labor Statistics; Mr. Charles Donahue, the Solicitor of the Department; and Dr. Seymour Wolfbein, the head of our Office of Automation.

Mr. Chairman, with your permission, I will offer the statement for the record and I will not read every word, but I will summarize the main features.

Representative REUSS. I wonder if the Secretary would be good enough when he summarizes the statement to tell us from time to time about where he is?

Secretary GOLDBERG. I will indicate where I am in connection with the statement.

I am pleased to have this opportunity to appear before this most distinguished committee to discuss the Economic Report of the President. I am particularly pleased to do so because, first of all, it gives me an opportunity to meet with you for the first time to discuss matters of great economic importance to the country before a committee which has distinguished itself for a bipartisan and comprehensive analysis of the country's economic problems, and also because it gives me an opportunity to pay tribute to this very fine Economic Report.

The President's message, of course, speaks for itself, and it is not appropriate for me to give it the praise to which it is really entitled. I would like to say a word about my colleagues on the Council of Economic Advisers.

I have had a great deal of communication with the Council during the period that I have been in office. I find them to be a very eminently qualified group of men, a dedicated group and I have not always agreed with them or they with me, which is natural and understandable, but our points of agreement have been far more than our points of disagreement.

I would hope that the country as a whole would read this fine report. It is presented in excellent fashion; whether everybody agrees with it or not is not the important question, but there is, in the Economic Report submitted by the Council, material which is of great value to the country at large. I want to pay tribute to this very fine report.

I want to address myself to a problem which has arisen in connection with the report, largely based on the fact that many people have formed an impression of the report from reading newspaper accounts, which have not been inaccurate, but necessarily do not encompass the full body of the report. I address myself particularly to people in the labor movement who have taken exception to some of the reports that they have had concerning the Economic Report. I refer particularly to the statement in the Economic Report concerning the 4-percent rate of unemployment. This has been assumed by many people in the labor movement—and they are going to testify before you and they can speak for themselves, and I no longer can speak for them—but this has been assumed by many people in the labor movement to mean that this administration believes that a 4-percent rate of unemployment is a satisfactory goal. I want to say that the report does not say this.

The Council of Economic Advisers did not say this. The President did not say this, and the administration does not consider 4-percent unemployment to be a satisfactory goal.

Let me quote from page 8 of the President's Economic Report, and I am now quoting:

> We cannot afford to settle for any prescribed level of unemployment. But for working purposes we view a 4-percent unemployment rate as a temporary target * * *. The achievable rate can be lowered still further by effective policies to help the labor force acquire the skills and mobility appropriate to a changing economy * * *. Ultimately, we must reduce unemployment to the minimum compatible with the functioning of a free economy.

Now, this represents the goal to which I am sure we are all dedicated—the administration and the Congress and all people who are concerned with the effective functioning of our free economy.

I want to say for myself, and I am sure I can speak here for the President and the administration, that we cannot be satisfied with anything less than the full employment of everyone who is ready, willing, and able to work. This, I think, was the intent of the Congress, when the Congress enacted the Employment Act of 1946. This is the intent of our administration.

Now, we all know that in any circumstances, even the most favorable, there is bound to be a certain amount of what economists call frictional unemployment—unemployment resulting from normal job changes, from the decision of free people to leave jobs, to secure better jobs elsewhere, and, of course, in a society as large as ours and in an economy as large as ours and with a population as large as ours, there will always be a certain amount of this type of unemployment. But, nevertheless, we must never overlook our essential goal, which is to provide everyone who wants to work with the opportunity to work at a useful, productive job in our free enterprise system.

This is the goal of the administration. This is the goal of the Congress, which prescribed this in the Employment Act of 1946. And when we refer to 4 percent, as the Council has done, it is only by way of indicating what is the immediate goal, starting as we did a year ago from a rate of unemployment of 6.8 percent, which went up to 6.9 percent a month or so after we took office.

Today I have some good news to report to this committee, and I thought it was an appropriate time, since today was the release date anyhow, to use this committee and the forum that you provide to make the announcement.

We have the January employment and unemployment figures, and I am very happy to report to you, sir, that the rate of unemployment, seasonally adjusted rate, has fallen for the first time in 16 months, below 6 percent. It is 5.8 percent. For the first time it has been below the 6-percent level since September 1960.

Now I do not want, by that statement, to indicate that I am happy or the administration is happy about a 5.8 percent rate of unemployment, but I think we can take satisfaction from the point that unemployment has fallen below the 6-percent level. The actual total for January is nearly three-quarters of a million below the figure of a year earlier.

Now, of course, unemployment normally rises at this point of the year, in December and January, because of seasonal factors. The number of unemployed rose from 4,091,000 in December to 4,663,000 in January, but this is a rise in unemployment which is less than the seasonal amount normally anticipated at this time of the year, when construction activity falls off and farm employment falls off and when other seasonal factors operate.

Now, in keeping with the policy which the President has followed and which I have tried to follow since I took office, we have to look at all aspects of the situation, not only those aspects from which we can derive encouragement. One of the aspects which remains troublesome—in addition to the level of unemployment, which still is very high—is the fact that the number of long-term unemployed, those who have been out of work for 15 weeks or longer, has dropped less than 100,000 from last January's total of 1,339,000.

As a matter of fact, the number of those out of work half a year or more, as appears later in this report to you, sir, is at a very high level. It was nearly 700,000 in January, and that is a very high level indeed. I am going to talk about this problem a little later.

The total employment this month, the month of January 1962, was 65,100,000, a new record for January. It was 600,000 better than a year earlier, despite a continuous drop in farm employment. As the Secretary of Labor, I would like to pay tribute to the tremendous productivity in the farm sector of our economy. It continues at a very high rate, and we are producing food and fiber in enormous abundance with a sharp drop in farm employment.

Nonfarm employment in January was 60,600,000, 800,000 above last January. This is a pickup and this, too, is an alltime high for the month, nearly 10 percent above the levels of a decade earlier.

Now, I might at this point interject to say that this gain has occurred despite the fact that we have been going through a period of tremendous automation. Recently we had a report which was published by the Center for Study of Democratic Institutions, that on "Cybernation," which is a fancy word to indicate the consequences of automation, and I do not agree with the gloomy conclusions of that report. We have a problem of automation, but automation can also be a great boon to our economy and we have been automating all during the last decade, as we are now doing. And yet we have nearly a 10-percent increase in nonfarm employment over the last decade and I assume that there will be an increase in the period that lies ahead in nonfarm employment as our economy increases, and as our needs for goods and services increase.

I think that that is a very valuable report, and we welcome all reports, private and governmental, but I think that picture was slightly overdrawn. I want to indicate that to you.

Now, among the signs of our economic recovery is the fact that productivity and the workweek are also increasing at a very strong rate. In December, the factory workers averaged 40.5 hours a week, a rise of 1.3 hours from last January after taking into account the seasonal factors. Productivity, in which we are all very greatly interested and concerned, has risen sharply and I will give you the figures on that in a few minutes, but the net result of the fact that hours have been lengthened and productivity has been rising is that reemployment has not risen as sharply as otherwise might have been anticipated. As a consequence, unemployment did not drop until toward the end of the year, but we welcome the drop in unemployment which took place in the figures that I mentioned where it has fallen below 6 percent for the first time in 16 months.

Personal incomes rose to an alltime high in 1961. I think we can all take great satisfaction from the fact that the average factory worker earned in December $96 a week before taxes. It is the highest level in our history. This is a welcome development, as is the fact that in our durable goods industries, where traditionally earnings have been higher than in the nondurable goods industries, they, for the first time in history, reached earnings of more than $100 a week before taxes. When we talk about the American standard of living, this is what represents the American standard of living. Some of you gentlemen, as I look over, not many of you but maybe one of the committee, can remember back in the times of the Roosevelt administration when we talked in hopeful terms of an annual income for a factory worker in America of $5,000 a year, as an unachievable goal. Well, the factory worker in the durable goods industry has earnings of more than $5,000 a year. We have realized what looked like an unachievable goal back in the 1930's.

Now, the relationship between employment as stated in the Employment Act of 1946 and the business welfare of the country is illustrated in what has happened in profits. They are, of course, directly related. When people are at work, then factories are operating at higher rates of capacity, and profits start to climb. Of course, our profits are connected with the health of our enterprise system and are also a great concern to me as Secretary of Labor, because only profitable industry can afford to pay good wages.

The annual rate of profits in the fourth quarter was in excess of $50 billion before taxes—the highest rate since the boom in the second quarter of 1959 just before the steel strike of 1959.

The total for 1961, considering that we had a very poor first half of the year, more than $46 billion before taxes, is not much below the alltime high of $46 billion recorded in 1959, and is $4 billion, or more than 9 percent above the level of the decade earlier, which was the high mark following the Korean period. Those who are primarily concerned with profit squeezes in the economy should look at this, and again we have a vivid illustration that profit levels can be maintained and improved provided that we can realize the objectives of the Employment Act of 1946. That is to put people at work, to enjoy a full employment economy, to see to it that the capacity of industry is properly utilized, and as we look ahead in 1962, I think we can anticipate a very highly profitable period for American industry.

This means that the unused part of our plants will be put increasingly to use, as every businessman knows, and I am sure every labor man knows, that this means that profit margins will enlarge because overhead, which is fixed, becomes better absorbed when everybody is at work and the plant capacity is used and profit margins thereby increase.

One of the very good developments during the last year is the fact that prices were remarkably stable, and one of our great challenges in the country is to see to it that this occurs, not only when we are in recession, as we were during the last year, but when we are in periods of recovery. I shall have something to say about that a little later.

The buying power of the average factory worker with three dependents in 1961 was at a new high as a result of the lengthening of hours of work, and the increase in income about 1½ percent above the year earlier, and nearly 19 percent higher than it was 10 years ago. This, of course, is really meaningful progress.

I can say from my own experience, representing the labor movement over a quarter of a century, that workers are very much interested in price stability. They, above all, recognize that it is illusory to get wage increases that are eaten away by increases in prices. They have a great stake, as everybody does, in price stability. It has already been pointed out by the excellent report of the Council that wholesale prices have even declined from the levels they were last year.

We cannot depend in our free economy, if we want to preserve our freedoms, upon governmental action alone, whether it is fiscal or monetary or by way of encouragement or whatever form it takes to insure that there is proper restraint and proper responsibility in the price and wage policies of the country. Among the most important problems facing the domestic economy today, I would rate the problem of prices and wages in America in 1962, which is a great challenge for our businessmen, our labor leaders, as well as for the Government, both in the congressional and in the executive branch of the Government.

I would like to take this occasion to comment, if I may, upon our collective bargaining process, upon which we necessarily must rely to insure that the wage aspect of this situation is handled in appropriate fashion.

In collective bargaining you do not discuss prices and it would be inappropriate to do so, but you make wage determinations which necessarily have an impact upon prices. When you make a wage bargain, of course you have, because you either add to or stabilize the costs of industry, and you have an impact upon prices. This imposes an important responsibility upon labor and management in collective bargaining, and there is also an important responsibility upon the managers of industry to consider their own actions in relation to the price factor. We want to make progress in the country, and we want to protect our free collective bargaining and no one of responsibility is urging that we impose at the present time price and wage controls upon our economy, because we operate within that framework that calls for a great responsibility on the part of managers of industries and on the part of the leadership and rank and file of the labor movement. We need responsible decisions on wages, and we need very responsible decisions through collective bargaining. This year in particular we are going to have some important collective bargaining take place in the United States that will have a great impact upon our economy and upon our goals of maintaining price stability and preventing inflation in the United States. I cannot avoid the responsibility, therefore, of commenting to you about some of these major collective bargaining developments.

Of course, the key one this year will be in steel, an industry with which I have a passing acquaintanceship. In the steel industry the managers of that great industry and the leadership and membership of that great union, which represents 95 percent of the industry—95 percent of the productive capacity of the steel industry—will have a very important responsibility to the national interest. It is a responsibility which they may dislike, just like very often we dislike the responsibility as a Nation in meeting our responsibilites in world affairs. It is often very painful to have to exercise the responsibility of leadership. I can understand, since I had association with the industry, very often the complaint which members on both sides make when they say, "Why are we singled out? After all, there are other important industries in America, and they go about their business without the focus of public attention, and congressional concern and Executive concern, which is manifested with respect to our particular industry."

I would say in answer to that, that it is unavoidable. Steel is our most basic industrial commodity. The steel industry, whether it likes it or not, and the steel unions are charged with responsibilities that go to the Nation as a whole. Steel is a bellwether of our economy, and it has been for many years and will remain so for many years in the future. Therefore, what happens in steel is of great consequence to all of us.

Now it seems to me that what is called for there is very evident. First of all, we cannot afford a repetition of the 1959 steel strike. That strike was a 116-day strike, and was the longest strike involving as many men in the history of civilization. There have been longer strikes involving fewer people, shorter strikes involving more people, but not in the history of civilization has there been a strike of that character involving as many people, that lasted for so long a period of time.

We cannot afford it because our economy is coming out of a recession, and a strike of that character would seriously affect our recovery from the recession, would not be in the interest of the industry which has had its problems, and would not be in the interest of the men who have had their problems, and would definitely not be in the interest of the Nation as a whole.

Now, this is just a truism. There is no need, nor is there any benefit in anybody not asserting that obvious fact. What is called for in steel without getting down to the details that would interfere with the responsibility of the parties to do what they have to do by collecttive bargaining, what is called for is very clear. The President has made it very clear. I am sure the American people share this. We need an early settlement in the steel industry. After all, the formalities of contract expiration ought not to deter the parties from voluntarily doing what ought to be done in the public interest. That is to have an early settlement. It has been done before.

I remember some early settlements in the steel industry that were achieved by voluntary agreement of the parties within my recollection, when I was associated with the union—not only in the steel industry but it has been done in other industries as well.

The contract expiration dates are very important and normally govern, but when important national considerations prevail, national considerations ought to govern.

In 1959, one of the bad consequences of the disturbed situation of that period was that there was accelerated inventory accumulation in anticipation of a strike which it was very evident to many people would occur.

Also, there was a great buying of foreign steel, because many suppliers felt that they had to protect themselves, and since the mills of America were operating at capacity, they went abroad to get their steel that normally would be filled by domestic sources. You cannot blame the supplier for taking action to protect his own interests. That is normal and that can be anticipated, and very often when we make commitments abroad, the supplier abroad very understandably from his standpoint is not willing just to meet the immediate needs of the moment, but as a quid pro quo for meeting those needs, insists upon a long-term commitment, so he can plan his schedule of production accordingly.

Now, it is the counsel of wisdom on everybody's part that we avoid this situation. Inventory accumulation is very hard, particularly on the small buyer, and the small businessman. Perhaps the large enterprises can afford to commit the capital and commit the physical resources by way of warehousing and other ways that are required for inventory accumulation, but the smaller purchaser cannot afford the capital, nor can he afford the physical facilities required by way of inventory accumulation.

Finally, we all ought to avoid the distortion in the business cycle which occurs when we concentrate all of our business in one period of the year and do not have an orderly development of business.

Now, the President has pointed this out and I have pointed this out, but I want to make one thing clear. We are not naive about this. We cannot appropriately tell suppliers that "you will be protected if you do not accumulate inventory."

This does not mean that the Government will not take energetic action to do everything within the Executive power to deal with a strike if a strike is threatened or occurs, but the very best assurance that can be made to people in the industry who are buying steel is for the parties to allay the fears which understandably have arisen as a result of the history of collective bargaining in steel.

Now, we welcome very much, and the President welcomes, and I welcome the action of the union in calling its policy committee into session in Pittsburgh next week. If past history is any example, this is an indication of a readiness on the part of the union to respond to our appeals for earlier collective bargaining.

I welcome the statement made by Mr. Roger Blough, the chairman of United States Steel, at the meeting yesterday with the press, when he released his corporation's statement for the year 1961, in which he indicated on the part of his great company a willingness also to cooperate in this end.

Now, I do not want anybody to believe that this administration believes in peace at any price, either in foreign affairs or in domestic affairs. It is important that the settlement in steel be a responsible settlement, and that is that it recognizes the equities of the workers and the owners, but above all recognizes the equity of the country in preserving price stability, our competitive position in the world markets, and that it be a settlement compatible with the national interest.

These are general terms, and many people will say, "What do you mean by that? Why don't you lay out the prescription?"

We want to preserve free collective bargaining in the United States, and we don't want the Government to dictate the terms of settlement in steel or elsewhere. But the Council has done a very valuable job in defining national goals and guidelines, and certainly the parties are very experienced parties. They know what the national interest is, and I think they understand what is required in the overall interests of the country.

I want to take this occasion, Mr. Chairman and gentlemen of the committee, to do what I am sure has your complete support—and that is to address an appeal to that important industry to do what really ought to be done, and that is give a demonstration of industrial statesmanship to the country which will be so helpful to us in advancing the recovery which we are experiencing.

Senator JAVITS. Would the witness answer a question on that point or would you prefer to continue?

Senator SPARKMAN. What is the wish of the Secretary? Do you want to continue your statement? Of course, our usual course is to let the witness present his full statement and then let each member of the committee have 10 minutes for questioning.

Senator JAVITS. The only reason I said that, is that this seems to be an excellent statement which the witness is making. I didn't find it contained in this written statement, and I didn't know whether he wanted to make that especially and have us ask him about it especially, or should we go on. I will rely on the chairman, of course.

Senator SPARKMAN. I rather believe that we will make better progress to wait and let each one take his turn.

Senator JAVITS. That is satisfactory with me.

Secretary GOLDBERG. I want to now turn to another important question of great interest, and should be of great interest and I am sure it is, to the labor movement and the people who work for a living, with respect to whom I have special statutory responsibilities. That is the question of foreign trade and employment. It also relates to this question I have been discussing in steel.

We are no longer a Nation living in isolation from the rest of the world, either in their national affairs or in economic affairs. We must see to it that all of our actions, private and public, take into consideration our international position. Our position in international trade is important, and our problem with respect to reducing the deficit in our balance of payments is likewise important. Therefore, the working man of America has an important stake, as does the businessman, in improving our position and remaining competitive in the area of international trade.

Mr. Chairman, we have published, and we will cover for the record and give copies to the committee, a study about our stake in exports. Our study shows, a study of the Bureau of Labor Statistics, that in 1960 our exports created jobs for more than 3 million workers—that is 3,100,000. As we estimate it, this includes about 13 percent of total farm employment, and 8 percent of manufacturing employment. Now, this represents direct employment in making the goods we export and also indirect employment in the sense that it also includes those who produce the materials used in manufacturing the product, and those who generate the power, supply the transportation and perform similar functions related to manufacturing the exports.

It does not represent the number of workers engaged in serving the people who are employed in export trade by way of retail stores, service occupations, and so forth, or those who are producing manufactured goods for consumption by workers engaged in export trade.

You may have seen in the newspapers the statement made the other day in a study published by the Department of Commerce, which used a 6 million figure. There is nothing inconsistent in these two figures. We are talking about two different things. The 6 million are all the people employed in the manufacturing establishments where export trade is an important part. The 3,100,000 are those engaged in the production of exports.

Now, therefore, the American worker has an important part in the export trade of this country, and an important part in liberalization of our exports, just as the country as a whole today must depend upon export trade and liberalization of it to make sure that we preserve the integrity of the dollar, and we can finally make adequate disposition of the problem of maintaining a favorable balance of payments.

I would like to make a comment on this subject, which I know you are much concerned about. Our studies show that despite the fact that wages are, of course, lower throughout the world than they are in the United States, we export precisely in the industries with high wages. This is where most of our exports take place. Therefore, our exports are not adversely affected, overall—they may be adversely affected in a particular situation—but overall by the high American wage standard which exists. Now, how does this phenomenon come about?

The fact of the matter is that very often in America we don't have the self-confidence that we ought to have. The high export industries are precisely the more efficient industries, the better managed industries, and they have workers with better skills. As a result, we can compete effectively in world markets, notwithstanding that we are the highest-paid country throughout the world.

I want to emphasize that, because I think too often our own workers do not recognize this. Therefore, we have an important stake in our foreign trade, and in liberalizing our foreign trade. Now we are doing a study in the Bureau of Labor Statistics, which we will make available to the committee and the Congress as soon as it is completed.

On the other side of the coin, what is the impact of imports on our labor forces? We haven't completed the study. But I want to say that we have done enough work to indicate a conclusion, and later we will support it by facts, that the adverse effect of import trade is considerably smaller than the benefits that we get from our export trade. It is not small to the particular worker concerned, and I will never assert that, but overall it is true. Later I am going to comment about some of the President's proposals to ease the impact upon those affected.

Now I would like to talk a little more about what our overall domestic employment figures indicate. The employment figures, which we have been publishing and which we published today, indicate some long-term trends that we have been noting in the past, and that is this:

We have rapid growth in the service industries as compared with the goods-producing industries. We are having a decline in the number of people involved in the goods-producing industries. We are having rapid growth in white-collar and nonproduction jobs, and little growth and some loss in terms of relative numbers in employment of blue-collar and production workers.

Also, we are having a very significant thing, which is very important for youngsters to know who are considering careers. That is growth where skills are required, and lack of opportunity for the unskilled young person who enters the labor market.

You will see some of the important statistics on this. During the recession of 1960, until February of 1961, there was a gross loss of 1.5 million nonfarm payroll jobs. One million of this loss during the recession was in manufacturing alone, with the metal and metalworking industries accounting for more than 60 percent of this total.

Now, this is very understandable when you had the steel industry, for example, a year ago operating at a little less than 50 percent capacity. There were losses in transportation and construction and trade, which totaled half a million. At the same time, on the other hand, there was an expansion of employment even during the recession in the school systems and in the finance and service industries, so the net loss at the bottom of the recession was about 1 million jobs.

Now, we have made up that million during the last year. We ought to analyze what has taken place. One-fourth of this gain was accounted for by employment increases in State and local governments, and it is quite clear to me that factory workers did not move over to those jobs. There was a strong gain also in the finance and service industries, and there, too, I am afraid that by reason of lack of training and skills, the factory worker didn't move over to those jobs.

Now, what is very troublesome is that, even with the recovery which has taken place today, we are still about half a million factory workers short of the early 1960 levels. The total drop of this half million was in blue-collar workers—production workers. Nonproduction workers in manufacturing establishments remained largely unchanged, and now are beginning again to show signs of expansion.

Also, some industries hit hard by the recession haven't recovered. Construction is an example, and transportation and mining are other examples. They have not recovered. This is a clear indication, if we want to analyze it, of where our hard-core unemployment really exists. It is in manufacturing, transportation, construction, those sectors of the economy.

Now, at the very helpful request of the Congress, we have been studying, and we will shortly report, the characteristics of the unemployed. We were asked to do this by the Senate Finance Committee, and we are going to shortly file our report, but I would like to preview this report with you.

The analysis of the unemployed indicate several essential characteristics involving age, color, and skill. First, men 45 years of age and over represent one-third of the very long-term unemployed—that is, over-26 males—even though they account for only one-fourth of the working force. This is in my statement:

Workers in the durable goods industries, metal, and related industries, account for 14 percent of the labor force, and 25 percent of the very long-term unemployed. Construction workers accounted for 6 percent of the labor force, and 9 percent of the very long-term unemployed.

Then, we have a problem of race and discrimination and lack of skills. They are all mixed in together. Negroes accounted for 24 percent of persons jobless for over 6 months, but only 11 percent of the civilian labor force. Now semiskilled and unskilled represented 45 percent of the very long term unemployed compared to 24 percent of the labor force. This of course is a statistic which dovetails with the others. Negroes, for example, constitute a great part of the unskilled force so that these figures must be read together.

In contrast, professional workers, technicians, laboratory people, accountants, and so on made up less than 3 percent of the very long term unemployed even though they account for 11 percent of the labor force.

Now, also, finally young people without any previous work experience, who accounted for less than 1 percent of the civilian labor force, made up 9 percent of the persons looking for work for over 6 months. This highlights the problem we have in this country of doing something about our young people who are going into the labor market, and today are not finding jobs. Perhaps this is one of the great explanations for juvenile delinquency problems that we have been increasingly confronted with.

Now, there is another factor, which is a disturbing factor, which illustrates that our economy is not operating the way it should, and that is the labor forces are not growing at the rate we anticipated.

In 1961 the total labor force grew about 1 million. We anticipated a growth of about 100,000 to 200,000 greater, and we should normally have a growth of that character. This is a trend which has been going on during the last several years, where our growth in the labor force is not as great as we anticipated.

Now, in analyzing that, we don't have all of the answers, but there are several reasons, some of which are good reasons. People are retiring now at a younger age. Now, insofar as this represents the fact that social security has been improved, and private employer supplements by collective bargaining or otherwise are better, this is a good development. We would hope that people who want to, on a voluntary basis, could afford to retire.

Insofar as this slowdown in labor force growth represents the fact that youngsters are not dropping out of school, this is a good development. And also if married women are not entering the labor force because they are financially in a position to stay at home and take care of their children, that is a good development.

But if this means that people, for example from farms, should enter the labor force because farm productivity has increased to the point where they are not needed, are rebuffed in entering there because jobs are not available, and they stay on a farm in a position of unemployment or underemployment, that is not a good development. If it means that some people don't enter the labor force who might normally do so because they felt there is no use for old people who would like to do a little work as permitted by social security and within the earning standards imposed by Congress, that is not a good development either. While we ought to encourage retirement, everybody who deals with the problem of geriatrics believes that if older people want to do some useful work they ought to be encouraged to do it.

Now there is another possible explanation, and that is the recent expansion of our Armed Forces, which would explain what happened last year, but doesn't explain what happened in previous years since 1955. As we know, we drew into the service recently about 300,000 men, mostly from the civilian labor force. Now this is a factor because our labor force is our national resource and we must always be concerned with lack of growth in the labor force, if in fact this is not a wholesome development.

I want to refer again to a question I made passing reference to before: automation. Of course we are going through automation, and we have gone through automation for a considerable period of time.

Last April we established the Office of Automation and Manpower in the Department of Labor, headed by Dr. Wolfbein, and we have had the benefit of a distinguished advisory committee from Labor-Management: Labor and Industrial Relations. This year we have presented a budget request so we can expand our activities in this area. We need accurate information about this important phenomenon in American life, and we are proposing two definite studies and reports which will appraise this great development in our economy.

I want to report to this committee a very significant development in this area. Our President's Labor-Management Advisory Committee has made a report on this. And here, too, there has been a little confusion in the press.

This report is only one of the reports that will deal with this subject. I have noticed one of the criticisms was that the report didn't give enough consideration to the whole question of growth. Well, it did not, out of jurisdictional grounds. We have another subcommittee of that Committee studying the problem of economic growth, and that Committee will report very shortly.

But the fact of the matter is that a committee representative of important people in management and labor and the public, did agree upon three essential points, although there is some disagreement about some other points.

The three points were: First. We want automation, and this heads in a different direction, really, from the private report that I mentioned came out the other day. Second. That, if we automate, we must still protect human values. Third. Both public and private actions are required in this area. Then, there are details, and I am going to offer for the record copies of this report for your committee's files.

The fact that I have said that I thought the private report on "Cybernation" was a little exaggerated doesn't mean that we don't have a problem in this area. We do. We are automating on the farms and we are automating in the factories. This means that in order to achieve our goals of employment, there have to be very high standards, and we have to step up our rate of economic growth.

I want to give you, which is not in my prepared testimony, our estimates of what we have to do if we are to meet the Council's stated immediate goals of 4-percent unemployment, to show you the dimensions of the problem. I have a little statement here which I will read into the record of job needs in 1962, to show you the proportions and the problems and the challenges we face in the year ahead.

Unemployment in January of 1962, as I have just reported to you, is 4,663,000. Now the normal labor force increase in 1962 that is anticipated is 1,200,000. We are increasing productivity at about, taking the long-term rate for the economy as a whole, 2.7 percent. This means that, if we increase productivity, we offset some workers. We would have to have 1,800,000 jobs to offset the normal increases of productivity. We also have, of course, several million people who are employed only part time. If we were to put them all to work at full time, we would need another million jobs.

So if we were to achieve the theoretical goal of full employment, with everybody working, which of course is impossible to achieve because we will always have in this group some people changing jobs—we would need, in the year ahead, 8,700,000 jobs over our present working force.

Now if we had unemployment at the seasonally adjusted rate of 4 percent in January of 1963——

Senator BUSH. Does that go to full employment?

Secretary GOLDBERG. That is with everybody in the country working.

Senator BUSH. You take the 4,663,000, and you add these other factors to it?

Secretary GOLDBERG. That is correct, sir.

Now, if we were to take unemployment at the seasonally adjusted rate of 4 percent in January of 1963—the Council does not project this, they projected it to some time in the middle of 1963—but even if we were to really set our sights to doing it this year, bringing down unemployment to 4 percent in January of 1963, we would be left with 3,200,000 unemployed people, and we would then need to create, this year, 5,500,000 jobs, quite a formidable goal.

If we were to try to achieve a 4-percent rate of unemployment by January of 1963, that would be necessary.

Senator BUSH. What is that net figure?

Secretary GOLDBERG. 5,500,000, Senator. This illustrates the challenge that lies ahead in American life. You don't have to arrive at the shocking conclusions of the automation report, but nevertheless to arrive at a sober conclusion, we find we have real problems in the period that lies ahead.

This isn't a simple task, and I don't believe that this task could be achieved by a program of sharing work. This leads me to an observation which I am sure you will want me to make regarding recent proposals which have been made to shorten the workweek, as a way of achieving this goal. Shortening the workweek in a country which still has great unrealized needs as we do, with 7 million families still enjoying incomes of less than $2,000 a year, with many needs in our Nation, does not seem to me to be the desirable way to achieve the goal.

Now, therefore, our administration has said that our primary task is to see to it that people work 40 hours a week because we need this work to produce the type of well-being in America that we ought to achieve.

I can understand the concern with people and workers in a period of unemployment, about job security. But, I think that the measures which are designed to really bring down the hours of work on a sharing basis don't really meet the problem at the present time.

Far better that we concentrate on measures, public and private, to increase our rate of economic growth so that we can have people working constructively, producing the goods and services we really need.

Therefore, I would like to turn now to some of these measures which are of great concern to me as Secretary of Labor in our Department, as a means of doing this job which has to be done.

And I would like to comment briefly on some of these programs.

The President has recommended that we enact a manpower development and training bill. This has passed the Senate, is before the House Rules Committee, and I am hopeful today the House Rules Committee will take some action on this important measure.

I think this measure has considerable support in both parties and throughout the country, and it is really based on the very simple theory which is sustained by the report I just gave you.

We need a better skilled and a newly trained working force in America, because at the same time when we have unemployment we have job vacancies. Also, one of the answers to automation in my opinion is not restrictive practices, but for new industries to develop, which will in turn require employment of people skilled to meet the needs of those industries.

We have never had such a program in American life, designed to provide a cooperative program between Government, Federal, State, employers, labor unions, communities, to develop new skills for a new age. This is what we are attempting to do.

Mr. Chairman and gentlemen, we have now a limited experience in this area, the first we have ever had. That is under the Area Redevelopment Act, which contained a very limited training program.

I welcome this opportunity to say something about it, because in the press there have appeared various accounts, not wholly based upon the information which is available to me as the administrator of the training section of that program.

One story, for example, appeared in the press about a problem in Huntington, W. Va., which has led many people to question whether or not this program of training under the Area Redevelopment Act is a good program.

I welcome this opportunity to state that our experience in Huntington and elsewhere, under the area redevelopment program, is an unqualified success, even though there are many limitations on training programs under the Area Redevelopment Act which are not present in a general retraining program.

We can only offer training under the Area Redevelopment Act if there is a general plan for area redevelopment. This, of course, is an appropriate limitation for training under the Area Redevelopment Act.

Let me say to you that when I wrote this report, we had already approved 29 training programs under the act. Since then we have approved a 30th program, in Texas; and we are very pleased about that. I am sure Congressman Patman is, too. It is in his district.

More than 4,400 trainees are involved; and the programs are located in 9 States. We have listed them in an appendix attached to my testimony.

We have been very careful about these programs. We are only training people where they can find jobs. We are not just adding to the general skills of the country in anticipation of jobs. Here we are training people for jobs that are available.

It is interesting to see what the reaction of people has been to this, and it is interesting to see whom we are training. Fifty percent of all trainees enrolled so far have been out of work for a half a year or more. In fact, one-third have been jobless for over a year. One-third are over 35 years of age. One in seven is 45 years of age and over.

Now, for the people themselves, despite the common conception that you are going to have difficulty selling people on training, this has been greeted with great enthusiasm.

Under the act we may not support a program of training for more than 16 weeks, but in Providence, R.I., the type of training we contemplated was a 20-week program. And the people involved readily volunteered to go to a 20-week program, even though they would receive no training allowances for the last 4 weeks, they are being trained without allowances for the additional period because they believe it is necessary.

We are going to run out of funds. For those who wonder whether we can expend our funds under the Area Redevelopment Act, let me say plainly that with the number of training proposals in the pipeline right now, we will run out of funds and will have to go to the Congress before the end of the year for a supplemental appropriation to take care of our needs in this area.

There are many good projects, which we will not be able to undertake with the means at hand.

The Area Redevelopment Act, therefore, shows what can be done on a much larger scale and what needs to be done on a much larger scale. It also shows what we have consistently believed, that there are job opportunities available for skilled workers who are retrained.

If you will look at attachment 2, at the end of my testimony, you will see the wide range of occupations that we are training people for: aluminum sash and door maker, automobile mechanic, automatic transmission specialist, chemical operator, draftsman, ship electrician, electronic assembler, electronic mechanic, farm mechanic, machine tool operator, maintenance mechanic, woodworking millman, nurse's aid, radio and TV service and repairman, aircraft riveter, sewing machine operator, tractor operator, stenographer, typist, welder, drycleaner, presser, spotter, boot and shoe worker.

In each of these areas where we are training people, jobs are available in those categories.

Now, you, of course, since the Senate passed the manpower development and training bill, are familiar with the broad program of manpower retraining which we contemplate, and I will not take the time to describe that further here as my prepared statement does so.

In my testimony, I deal with another proposal that we have made, that the President has recommended, and that is the question of youth employment opportunities. As I have indicated, almost a million of the unemployed are young people between the ages of 16 and 21. And while they comprise 1 percent of the population, they comprise a far disproportionate area of unemployment.

Now, we have to give special attention to the young people. This does not mean that we can solve their problems without reference to solving the total problem of economic growth. But we can show, as a matter of national concern, that we are interested in the young people, and that when they enter working life they are not rebuffed. And therefore we have proposed three pilot programs to deal with youth unemployment.

We have proposed a special training program for the young people, recognizing their special problems. We have proposed a pilot program for public service employment. All over the country, cities and local communities and States need additional help in certain areas, and we can help them supplement their own resources in this area. Young people are ideally suited for work with welfare agencies, schools, hospitals, and areas of this type, and we hope, through this pilot program, to demonstrate that this is feasible.

Finally, we have proposed a pilot program with respect to a Youth Conservation Corps, which served us so well in the 1930's, and which can serve us so well again.

We have also proposed that we permanently improve our unemployment compensation system. Twice we have had in a recession period to tinker with this system; in 1958, and again last year. We ought to now permanently improve our unemployment compensation system, because as we move to our goal of maximum full employment, we are bound to have people who are casualties of even the best transition from one activity to another.

It is the counsel of wisdom for us to upgrade our unemployment compensation system.

I have been recently saying to employers—and I would like to emphasize here: One of the problems in collective bargaining in America right now is that collective bargaining is assuming too much of a burden. And this is having price consequences which may be unfortunate.

The American workingman, like the rest of us in America, is a very pragmatic animal. If he cannot get relief for his legitimate problems through legislation, he will turn to his union to get it through collective bargaining.

And if you want really to analyze this unfortunate trend to artificially shorten the workweek, one of the reasons for this is that the levels of unemployment compensation in the country have been too low.

I think it would be the counsel of wisdom for everybody in America that we improve our unemployment compensation system, which takes care of everybody in an economical way, rather than imposing on a particular employer, and therefore a particular class of consumer, the very burdensome costs of providing job security in times of unemployment.

I would hope that there would be a new approach; that instead of blind resistance to these matters there would be a considered discussion of the role, the proper role, of unemployment compensation in meeting these problems.

Now, there have been other proposals that have been made and that have been discussed in the Council's report, that I will not take much time with.

I regard as very important the proposals made by the President in his report for standby authority for capital improvements. I think here we are facing a very fundamental problem. If we are going into a recession, and we cannot provide private jobs, and fiscal and monetary policies will not do the job, what happens to the people involved who are out of work? What has happened to the long-term unemployed?

We are a humane country. We do not allow them to just starve. So we provide for them either by unemployment compensation or by welfare fund payments. We make a provision, not adequate provision, but we make provision.

This is costly. This costs a lot of money. And it does not achieve the result of providing a job. And it is very demoralizing for the workers involved and their families to be without jobs.

Friday, I was in Pittsburgh to address a meeting of the National Academy of Arbitrators. And when I got to the hotel, I found 175 women with picket signs, which created great alarm in Pittsburgh. I was being picketed. I did not take alarm. I invited the women into the hotel, and I discussed with them their problem. They were the wives of steelworkers in the Denora mills of United States Steel, American Steel & Wire mill, in that town. Their husbands had been out of work for 2 years. That is not a good situation for a country like ours. And I discussed their problems with them.

It is not easy to tell people to pick up and move. Moreover, they have not been told by the company that these mills are down forever. The company has made no announcement that the mill has shut down. Therefore the men live in hopes that the mill will resume operation as it did in past times.

They have been taken care of in one way or another, not adequately, through unemployment compensation, supplementary unemployment benefits, negotiations under the union contract, welfare fund payments, and other ways; but the women, to a single person—and I am sure the men would have joined them—said that what they wanted were jobs. They thought it was very demoralizing to raise their families under conditions where the men were out of work for 2 years. And I agreed with them.

I would have thought that it would have been the counsel of wisdom, if we had standby legislation during that recesssion as we are proposing now for other recessions, so that the Government could expand the necessary capital improvements and see to it that those men were put to work by private employers, because they would be the contractors for this work, but they would be put to work while the economy was in the state that it was this last year. And I think this is a very important element of the President's program.

Now, I would like to say a word about tax incentives. Here, too, I would like through this medium to address myself largely not to this committee but to the labor people in this country.

There is an automatic reaction against tax incentives for business. I do not think it is justified on the part of the labor movement or working people. We need to stimulate investment in America on the part of business.

Our rate of investment is much less than it has been in Europe in recent years. And one of the ways to stimulate business investment is to give tax credit for modernizing and improving our capital plant; also to improve our depreciation allowances.

We do not want our businessmen going abroad in order to seek higher profits. We want our businessmen to expand and modernize their equipment here at home. I think we have to be realistic about it and recognize that if substantial incentives are offered abroad, we have got to be competitive in this area, as we have to be in the wage and price area in general.

So I think the tax credit and incentive proposals which have been proposed by the administration are desirable proposals and in the interest of improving job opportunity.

Finally, we have got to improve our employment service by way of giving counseling and direction. We are doing that. Since last year, the Congress has allotted us more funds, and we are stepping up the caliber of the U.S. Employment Service and the State services which cooperate with the Employment Service and are an indispensable part of it. We need this very much, in order to properly mobilize our labor force.

The last word I want to say is about discrimination in employment. We cannot afford discrimination in employment in American life any more; not only because it is wrong basically, but because it also affects employment and unemployment, as our figures indicate.

Now, I am very proud of the record which is being made in this area, and I want to say that discrimination in employment is not geographic. I think we have to say that in all fairness. It has been assumed that northern employers are without sin and southern employers are those who are sinning. Our figures show that discrimination occurs throughout the country and is not localized in one geographic area. As a matter of fact, right now, for example, as a result of the "plans for progress and employment" that our Vice President's Committee on Equal Employment Opportunity has promulgated, we have a better employment situation in Lockheed, in Marietta, Ga., than we have in comparable employers in California or in the North. This indicates that the good sense of the American people will respond to energetic leadership to provide equal employment opportunity. This we are attempting to do very vigorously in the administration.

Discrimination against Negroes is not the only discrimination in American life. We have discrimination against our Puerto Rican citizens. We have discrimination against Mexican-Americans. And this is most notable in the migratory labor area, where they comprise the bulk of our migratory labor population. We are very determined, in this administration to improve the lot of migratory farm labor. And it ought to be improved. It is not a good thing for our country to have workers who enjoy incomes for their families of about $1,000 a year, which is characteristic in this area.

A part of the problem here is to improve farm income; because the farmer has not been getting his fair shake, either. And just as in industrial employment, a profitable employer can afford to pay good wages, a profitable farmer can afford to pay good wages; and the farming has not been profitable enough.

I have been overly long, Mr. Chairman.

I would like to conclude that I have tried to stress here the great concern that the administration has and that the Department of Labor has with the need for providing for a full employment economy and for providing every possible means for eliminating unemployment. This remains the dedicated goal of the administration, under the mandate which the Congress gave us.

Thank you very much.

Senator SPARKMAN. Thank you, Mr. Secretary. You have given us a very helpful statement.

By the way, the committee will be very glad to receive the various exhibits which you have provided for the file.

I shall be very brief in my questions. I was interested in your discussion of the retraining program. You give an optimistic report.

Now, has it gone far enough to see if you are actually able to place these people in jobs, after being retrained?

Secretary GOLDBERG. Of course, this is a new project under the Area Redevelopment Act.

Senator SPARKMAN. Yes, I realize that.

Secretary GOLDBERG. We only got our funds in September to embark on these programs, after the program was adopted by the Congress, but so far, those that we have retrained under the Area Redevelopment Act we have found not much difficulty placing in jobs.

Senator SPARKMAN. I notice in that table you were training 1,225 tractor operators. Are those jobs available?

Secretary GOLDBERG. This is in New Jersey and in Mississippi. In New Jersey, the program is moving ahead, and in Mississippi we have run into some problems, which we hope to be able to resolve, in this area. But the interesting thing is that our studies show that tractor operators are essential. As a matter of fact——

Senator SPARKMAN. Is that in construction work, primarily?

Secretary GOLDBERG. No, this is in agricultural work, Senator Sparkman.

I discovered, for example—and I met with a group of interested Congressmen from Texas, Arkansas, New Mexico, and California yesterday—I discovered that we are importing tractor drivers, for example, from Mexico, in our agricultural work. And part of that is due to the fact, peculiarly enough, that we do not have domestic tractor operators available.

Part of that is due to lack of training. And it is interesting that many people who work on the farm have not been trained in the operation of tractors. We hope to improve that situation.

Senator SPARKMAN. Let me say that I enjoyed your presentation on the necessity of studying and understanding a little more the trade conditions, the trade legislation, that we are going to be confronted with.

It seems to me that you have brought out some facts there that the country ought to be made more familiar with, what this matter of training means to the job situation of the country, in addition to the other matter that you mentioned—the balance of payments. You brought out some very interesting points, and I am glad to see you do so.

By the way, I should like also to comment very briefly upon the statement you made regarding the steel situation.

I think the country as a whole can be pleased with the action that has been taken to encourage an early settlement of that situation. I know we have seen occasions when we kept our feet dragging until it was too late to get a settlement, and there resulted a devastating strike. This committee I think perhaps more than any other committee in Congress has been, from its inception, concerned with this very problem. Our chairman, Congressman Patman, who was on the committee from the beginning—I believe he and I are the only members who were on the committee from the beginning—will recall that we have had many studies dealing essentially with the wage-price setup in the steel industry, because we did recognize it as the bellwether of wages and prices throughout the country. I am very glad that you brought out the statements that you did.

By the way, the chairman is not going to be able to stay here. I think I should yield to him for his questions. I will cease at this point and will call on the chairman for a question.

Chairman PATMAN. May I invite your attention to the fact that this committee, 7 years ago, took up the question of automation. We have had hearings every year since. I think it is the only committee that has really specialized in the subject, and I think that we have rendered fairly good service in connection with it.

I congratulate you, Mr. Secretary, on a fine statement. I appreciate the statement you have offered and the statement you have made here, abstracted from the speech that you had prepared.

About the question of discrimination, I am disturbed about discriminations against people who have reached the age of 35 and 40, too. Don't you think that we could well afford to give a little more attention to the fact that people are finding it extremely difficult to get jobs after 35 years of age, and certainly 40 years of age? What is the age where this problem begins to creep up on people?

Secretary GOLDBERG. Mr. Chairman, I share your concern about this problem. It is very serious. As a matter of fact, there is a noticeable trend in American industry to discriminate against people above 35. It has got down that low, now. This is unfounded. Every study we have made indicates that men of this age, 45 or 50, are at the height of their skill, at the height of their experience, they are very productive workers, and discrimination of this type is unwarranted.

Part of the problem which has arisen, and which we have to frankly acknowledge, and which I hope that this committee will give further study to, is the impact upon employment of provisions in company pension plans and other benefit plans in relation to the employment of people at 35, 40, 45, and 50. This was considered by the President's Advisory Committee on Labor-Management Policy; and this committee unanimously agreed that there was need for consideration of investigating these and other provisions in these private arrangements; so that the employment possibilities of workers would not be curtailed but would be enhanced by these benefits which have been won.

But you are absolutely right that this is a notable discrimination and one that has been assuming large proportions in the country.

Chairman PATMAN. I wonder if we should make it race, color, creed, and age?

Secretary GOLDBERG. Yes, by all means. In fact, in my testimony I point to that as one of the factors.

Senator SPARKMAN. If the chairman will yield to me briefly, I would like to inject a thought, that the Government is one of the worst offenders on this age problem, in dealing with personnel. It seems to me that something could be done in that field.

Secretary GOLDBERG. Mr. Chairman, I want to say that we recognize this, too.

One of my actions in the Department of Labor was to issue an order to the Department saying that in employment policies of the Government, age should not be a factor except insofar as Congress has a mandate above the age of 70, which is a respectable age for retirement; but beyond that, that there should be no discrimination on account of age in employment policies in the Department of Labor.

Senator SPARKMAN. Senator Bush?

Senator BUSH. Mr. Secretary, I congratulate you on a very brilliant summary of a very comprehensive statement. It was very interesting, indeed.

I only have 10 minutes, so I will be only able, I think, to cover one aspect of it with you. There are many others I would like to discuss.

I refer to the question of foreign trade in employment, which you discuss in the beginning of your statement. Let me say first that I have long been in sympathy with the basic objective of the administration program in this respect, and as a member of the Rankin Commission and as a member of the Senate these last 10 years, I have advanced the cause of reducing tariff barriers and improving international trade; and we have made great headway in the field, there is no question about that. Our record of exports, I believe, for the last year or two is at an alltime high and may be improving. Furthermore, we are also the lowest tariff country in the world, including all of the Common Market countries.

We will not know some of the reservations one may have about this program, except to mention the fact that aside from the part that you are discussing, it also leaves one wondering who is going to take care of the Latin American countries. If the Common Market countries have a mutually exclusive program over there, mutually exclusive and externally exclusive program, which they indicate they are going to have, who is going to take care of Japan, which they have been shutting out of their markets, because they say the labor cost differential is too great and they cannot stand that competition; although they are at twice as much advantage vis-a-vis as Japan is with them?

Then there is the question of East-West trade. Are they going to go ahead and sell goods to Russia and so forth, diametrically opposed to our policy? These things are related to the total program.

But the one that is particularly in your province is, of course, the effect that it may have on employment in this country, and naturally we will be most interested to see the findings that you come up with, which I hope would be more accurate than some of the things I have read in the paper, as to the number of people engaged in the export business.

For instance, I saw a clipping in the paper the other day that in the State of Connecticut there were 173,000 workers employed in factories who do export business.

But, I mean, the export business in those factories may be only 1 or 2 or 5 or 10 percent of their business. This is, therefore, an entirely misleading factor.

I notice that you spotted that, yourself. I was glad to see it. And I hope that your figures on your estimate of damage here will be as accurate as possible. I know that it is an awfully hard thing to assess.

But you point out that our goal here in 1962 is to find 8 million jobs. And you realize that is one "dickens" of a task, because the administration sets an intermediate goal of 4 percent, which I think is a reasonable thing for them to do. But even to attain that goal, for the reasons that you stated, we need 5½ million jobs, which is no mean undertaking in itself.

Now, the program that the President has sent down, with all the merits—and I pay tribute to all the merits it has in its objective—admits implicitly in the program that this will cause substantially increased unemployment in the country, in this country; because it comes up with the so-called trade adjustment section of the act, which is to deal with the unemployment factor which is to be created.

It is said by administration spokesmen—and I think you were just one this morning—that this is not a big problem; but it is a big problem to those 200 women who came to see you in Pittsburgh. It is a big problem to the working men and women in New England who have seen their workers being protected by Government action over a great many years, and their business has built up and their community has built up, and their whole environment has been nurtured with this modicum of protection from the Federal Government. They are alarmed to see the Federal Government about to take an action itself which is going to bring unemployment to them. In certain areas this would be very widespread, although it might not be nationwide.

I wonder, if the problem is so small why we have to deal with it so harshly. This is, I think, a very serious matter in connection with the trade program, and it is one that falls directly in your domain.

So I ask you if you would care to comment on what I have said.

As I say, I am sympathetic with your objectives. I think they are fine. But I think other things perhaps should be taken into account before we plunge into a program which is destined by its own admission to aggravate the very serious problem which you have discussed this morning.

Secretary GOLDBERG. Senator Bush, let me say that this is a problem that I am particularly conscious of. I have participated personally in the discussions that have led to the development of the trade program and its submission to the Congress.

I would like to make these observations about it. You are quite correct that the overall statistics, while they reflect the great benefits that we have in export trade, do not gainsay the fact that, since trade is a two-way street, some people will be affected by liberalization of trade.

Overall, part of the solution to our unemployment problem is in liberalizing trade, to have greater markets, greater access to markets, less tariffs in the world. We will, therefore, benefit in that we will have more of our people at work and less unemployed than we have now. That is the overall fact. It is evident in the figures that we have had since the Congress approved the reciprocal trade laws and we have liberalized trade.

Therefore I am a strong advocate of the liberalization of trade, because I believe it is going to help us meet the problem that I have been discussing in providing these jobs.

We of course have to be conscious that in particular situations people are going to be affected, because if we are going to have liberal trade, it has to operate both ways. And I agree with you that in our policies we have got not only to consider ourselves, but we have got to consider our good friends and neighbors in Latin America and our ally, Japan.

I was in Japan as part of a joint Cabinet meeting. The Japanese are being unfairly treated in Europe.

Senator BUSH. I should say they were.

Secretary GOLDBERG. And we owe them the obligation of seeing to it that their goods have access to European markets. They are improving their wage standards quite substantially. They, at the present moment, although it is still considerably below our scale, are the country with the most advanced standard in Asia.

They compare with some of the lower wage countries in Europe in terms of their actual benefits. You cannot judge it by wages alone. They grant other forms of security, which do not exist elsewhere. An employee in Japan, for example, is granted job security for life. Once he is employed in a mill, he is employed forever, regardless of the business condition of the mill. And all of these enter into their costs of production.

So we are conscious of this, and we are going to take steps to see to it that they get a fair deal in our negotiations with the Common Market countries.

Now, our proposals contain various safeguards which many people have overlooked. The first is that we have preserved and improved the peril point procedures which Congress has written into prior trade legislation. Now the Tariff Commission can make a finding, but we have methods of seeing to it that findings of peril are publicized and subject to action which are not in the present legislation. When we testify on the trade legislation, we shall point that out.

Secondly, the President has followed my recommendation in a most liberal way for various adjustment allowances and devices to be made available to workers and to industry in the event hardship is imposed by trade liberalization.

At present, we have no special adjustment allowances. At present, if a worker is injured as a result of trade impact, he can receive only whatever unemployment compensation is available if he is eligible.

As a result of what has happened to unemployment compensation statutes in the various States, his protection may be very good in a particular State. Connecticut may be an advanced State, but some other State may not be so advanced.

I have given some evidence here and will present further to the Ways and Means Committee to show that the average protection is far below what it was when the Unemployment Compensation Act was first enacted many years ago, when it was designed to provide 50 percent of protection for a worker's wage if he became unemployed.

We are proposing in this bill that if a worker is hurt by an imposition of tariffs, a worker receives 65 percent of his pay for 52 weeks, and that if he is 60 or over, that period be extended; so at least he will have assurance that where he has been injured he will be given assistance.

In addition, we have integrated this with our training bills to make sure that such a worker will have the advantage of retraining, so that he can be directed to other available job opportunities.

And finally, we have also helped his employer—it is not enough to help him—by very liberal allowances, loans, and grants, to help that employer.

Senator BUSH. Well, I have not got time to pursue it further. I still think that it is a little bit like throwing an anchor to somebody who wants a life preserver. Especially that goes for the employer, where you say, "As you gradually go out of business, we will lend you more money." That is not of great comfort to him.

I was coming down the other morning listening to the radio in the car, and they have this program called "Opinion, Please," and this man phoned in from out in Alexandria. The question under discussion was: "Are you in favor of the President's new trade program?" This fellow said: "Yes, I am all for it." He says: "It will force unemployment, and that is the only way we will get wages down in this country."

Secretary GOLDBERG. I think we will agree that that would not be a desirable goal.

Senator BUSH. But I am a little bit worried about it, Mr. Goldberg. I do feel that these other employers that I mentioned ought to be taken into account at this time, because they are of pressing importance. I feel that we are already carrying a larger share of the world's burden than even our abundant resources make it comfortable for us to do or even possible for us to do well.

And I very much hope that if the discussion of this bill comes, it can be modified in such a way as to insure, in pursuance of this important policy, that unnecessary hardships are not inflicted and unnecessary problems are not created in connection with the big job problem which you so ably and clearly outlined to this committee this morning.

At the moment I am somewhat fearful that the problem that you disclosed is apt to be seriously aggravated in the years immediately ahead. The Council of Economic Advisers testified before our committee, this committee, that they expected imports to rise at a greater rate than exports in the couple of years, in the first couple of years of the program. Beyond that, they were hopeful, but they did not predict. And I have not heard anyone who denies the fact that we have that expectancy facing us there. This was testified to by Professor Wallach, a former member of the Council of Economic Advisers, before our committee last December.

So I do hope that your voice will be a very strong one in this, and I know your interest in the working men and women is the deepest and the most sincere of all of the members of the administration.

A group of these people called on me from New England, labor leaders, and they are very apprehensive about it, I do not mind saying. In spite of any broad statements that were made by Mr. Meany that, "We are 1,000 percent with you, Mr. President," there is down the line a lot of apprehension about it.

So I bespeak your most careful appraisal of the situation, to see if we cannot in some way modify this bill so as to take away some of the hazards and not suddenly plunge into another half million of unemployed on top of this serious question which you have got to face right now.

Thank you, Mr. Chairman.

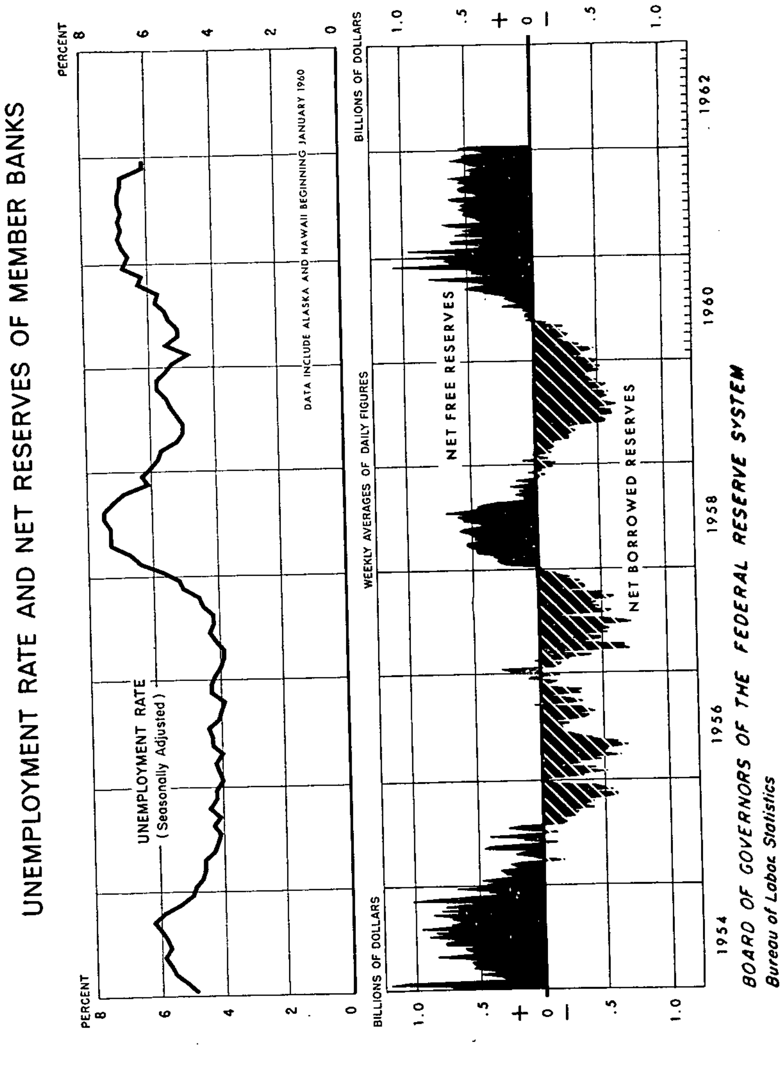
Senator SPARKMAN. Congressman Reuss?

Representative REUSS. Mr. Chairman, I would like to express my agreement with and associate myself with at least part of what Senator Bush has just said, specifically that portion of his remarks in which he has expressed his view that our friends and allies in Western Europe have not done what they ought to be doing in the fields of aid and military defense and trade to help out on the balance of payments situation. And it may be that you would want to mention at some future Cabinet meeting that this dissatisfaction came from both Republicans and Democrats.

Mr. Chairman, yesterday in my discussions with Mr. Martin of the Federal Reserve System, I had reference to a chart showing the relationship between free reserves and the unemployment curve, and since that was involved in my discussion with the Chairman of the Federal Reserve, I ask unanimous consent that that chart be made a part of the record.

Senator SPARKMAN. Without objection, that will be done.

(Chart referred to follows:)



Representative REUSS. Mr. Secretary, I, too, was intensely interested in your thorough presentation and its asides. I have been happy to observe in press reports that you have concerned yourself with what is generally known as culture, that is, art, painting, music, the theater. This interest has not been entirely in line of duty; some of it has to do with your wife's excellent painting; some has to do with the fact that one of the strikes you were called upon to settle had to do with the Metropolitan Opera.

I would suggest, however, that culture as thus defined does have a lot to do with your duties as Secretary of Labor, and I hope that you will increasingly turn your attention to this very important field of American activity. We have a Department of Agriculture, and we talk of a Department of Urbiculture, but we do not have any department of just plain culture. But since you, as Secretary of Labor, represent the interests of perhaps a larger segment of American society than any other Cabinet officer, I would hope that you would continue this interest.

Secretary GOLDBERG. Congressman, may I make a comment at this point? I think it has a direct relationship to the responsibilities I have by congressional enactment.

When I was associated with Mr. Murray, when he was president of the CIO, he made a speech once which I thought really described the relationship; and I do not think anyone could do it better.

He said the reason why he had spent all the years of his life ever since he was 10 years old in the labor movement was because he regarded it to be the objective of the labor movement to see that every person, every working man and woman and child, had an opportunity to have a rug on the floor, a picture on the wall, and music in the room. This was what he regarded his objective in life to be.

Representative REUSS. That was a great speech, and I remember it, and I think it is time we did more about it. I should think that all segments of American society, including the labor movement, which you were associated with until very recently, can do more about it.

You are undoubtedly aware of the fact that in Austria, a country with less material assets per capita than this country, every member of a labor union has on his dues card a number of little places to punch on the side. These entitle him and his family every month to hop on a train, if they do not already live in Vienna, and to go to the state theater, the opera, chamber music concerts, the symphony, the art museum, and so on.

I am not suggesting that we can adopt this Austrian technique unchanged for our country, but at least it should give us pause.

I am wondering if it would be possible for your Department to prepare for this committee a study of two things: One, the extent to which labor unions throughout the world, including this country, are active in the field of culture. I believe it would be most helpful to find out what labor unions around the world are doing to enable working people to have in the living room what Mr. Murray was talking about.

Secretary GOLDBERG. We will be glad to, Mr. Congressman, and we will file something on this for the record.

(The following was later received for the record:)

PARTICIPATION OF FOREIGN UNIONS IN CULTURAL ACTIVITIES

European labor movements seek to advance the cultural and social along with the occupational and economic status of workers. They have pointed out that, in doing so, they contribute largely to general progress. "The function of trade unionism," stated the general council in reporting to the 1946 British Trades Union Congress, "does not end with securing the worker improvements as regards his conditions of work * * *. Beyond day-to-day questions it is concerned with seeing that the worker has the widest opportunity for a full life, and if there are respects in which facilities available to him for the use and enjoyment of his leisure can be improved, in pursuing such improvement." Efforts of European labor organizations to make cultural values available to workers are largely intended to break down educational barriers and to promote and encourage the formation of groups and clubs engaged in the arts or other cultural activities where workers have little or no opportunity to join middle-class societies of such kind. In countries in which the labor movement consists of trade unions, cooperatives, and a party representing labor's interests, cultural activities, to a large extent, are undertaken jointly by some or all of these organizations. In several countries, organized labor cooperates also with public authorities and private bodies. There is, organizationally and otherwise, a close connection between educational and cultural activities of the labor organizations.

For example, the subjects taught in the study circles of the Swedish Workers' Educational Association, to which belong the Swedish Confederation of Trade Unions (LO) and its individual member unions, the Cooperative Union, the Social Democratic Party and its youth and women's associations, the Association of Young Eagles (a children's organization), and a number of other and smaller organizations, included in 1960 art, literature, history, social science, natural science, religion, philosophy, and psychology. In addition, the Swedish labor movement has been establishing "people's houses"—a kind of community center where the labor organizations can perform cultural activities. These people's houses are often used for movie and theater performances, and the labor movement, together with the cooperatives and a number of other organizations, has its own film company and owns a chain of movie theaters. The Society for the Promotion of Art (Konstfrämjandet), in which various voluntary organizations cooperate, carries on educational activity in art by organizing exhibitions and arranging for the sale of good art. The Swedish labor movement also owns two publishing companies which publish and disseminate good literature, primarily through cheap editions.

In Belgium, a National Committee for Workers' Education, established in 1911 by the General Council of the Belgian Labor Party in cooperation with the trade union and the Socialist cooperative movement, functions for the purpose of organizing and coordinating "the work of all working-class educational organizations that will instill into the workers the knowledge and qualities they need to carry on the struggle for the emancipation of their class in every sphere." In addition to offering classes, lectures, study groups, and excursions and guided tours, the committee operates its own section of the book club known as the Guilde du Livre. In 1956 this section had some 6,000 members, of whom 2,500 were regular buyers. The committee also has organized successful national and regional workers' education weeks or fortnights and has founded federations of film clubs, drama groups, and amateur photographic societies. Moreover, it has been taking active steps to encourage better use of leisure and to foster cultural activities among the workers. Workers' educational groups—an outgrowth of adult educational facilities run by the Christian Workers' Movement—operate study groups to discuss topical questions such as independent schools, parents' responsibilities, unemployment, leisure, housing problems, the best newspaper to read, and the attitude of Belgian workers toward foreign workers.

An outstanding feature of the activities of the Cultural Department of the West German Trade Union Federation (DGB) is the annual Ruhr Festival in Recklinghausen, which is attended by groups of unionized workers from all parts of West Germany. It consists of opera and other theatrical performances, concerts, art exhibitions, and the like. The festival is open to the public; its main purpose, however, is to promote worker participation in art events. The district and local committees of the DGB form theater and concert groups and arrange private shows at reduced admission fees for union members only. Local union organizations and municipal theaters cooperate in a considerable degree. The Metal Workers Union and many other unions encourage and promote the formation of art groups on the local level. Finally, the subjects taught in the adult education courses offered by the DGB include the arts.

Private concerts and theatrical performances at low prices arranged for workers by the unions or the Social Democratic Party are customary in Austria likewise. Italian workers, too, may get a discount on tickets to movie houses, theaters, sports events, museums, etc., by special agreement with their unions or the National Association for Workers Assistance (ENAL).

Many British trade union branches organize cultural, recreational, and social activities among their members, including concerts, film shows, lectures, and annual dinners. As mentioned above, the British labor movement shares the conviction of the continental unions that advancement of the cultural status of the workers is within the legitimate field of trade union interest and activity. In contrast to theory and practice of continental labor movements, the British unions, however, believe that they should primarily encourage and assist in a greater provision of cultural facilities by public authorities and voluntary societies and restrict direct promotion of such facilities. Apart from pointing out that most unions could not bear the costs involved in direct promotion of substantial cultural enterprises, the general council stated in its report to the 1961 Trades Union Congress that "the movement has, rightly in the general council's view, hesitated to promote sectarian workers' cultural activities, or to attempt to exploit the arts purely for purposes of propaganda or indoctrination." The British union leadership, thus, considers increased patronage of the arts as primarily a matter of the individual union members and the community, and it objects to the creation or preservation of a separate worker class with separate cultural institutions.

African and Asian unions have as yet been fully occupied with their organization and with economic and political problems and have done little, if anything, to promote directly active interest of their members in cultural matters.

Cultural Activities of the American Labor Movement

The culture of the United States, as we know it today in all its variety, is of course a product of many influences. If the contributions of the labor movement toward the higher aspirations of American culture were to be cataloged, certainly three would be prominent. Probably most trade unionists would list first the unceasing desire to raise the real wages of union members—to make possible, among many other things, "a rug on the floor, a picture on the wall, and music in the room." The profound interest of the American labor movement in education, in its highest cultural connotations as well as in its more practical aspects, would also rank high. The contributions of trade unions in the assimilation of immigrants into American society, while preserving to some degree the heritage of other cultures, would also appear on such a list.

This report, however, is directed to a narrower question—trade union interests in cultural activities, which are defined, for present purposes, as the pursuit and advancement of the fine arts. At the present time, these interests are divided into three distinct parts. First, and by far the most significant, are the points of view, concerns, and economic interests of professional performers—musicians, actors, singers, stage hands, directors, etc.—and their unions. The second, involves the participation of the trade union movement in national and community affairs, and, to the extent that the country as a whole and particular communities are concerned with the advance of the arts, union relationship with the development of subsidies and outlets. The third facet involves that portion of union educational and recreational activities for their members that falls in the range of cultural interests encompassed by the term "fine arts."

The professional performer

Professional performers in the United States, unlike those in other countries, are highly unionized. The country's major symphony orchestras, for example, have long been under union contract, many since before the turn of the century.

A roster of unions in the performing and related arts, and their membership as of 1960, includes the following:

American Federation of Musicians (AFL-CIO)	266,618
Associated Actors & Artists of America (AFL-CIO)	55,000
Branches:	
Actors Equity Association.	
American Federation of Television and Radio Artists.	
American Guild of Musical Artists.	
American Guild of Variety Artists.	
Hebrew Actors Union.	
Italian Actors Union.	
Screen Actors Union.	
Screen Extras Union.	
International Alliance of Theatrical Stage Employees & Moving Picture Machine Operators of the United States and Canada (AFL-CIO)	61,967
Directors Guild of America (Independent)	2,150
Writers Guild of America, East	1,100
Writers Guild of America, West	1,868

The aspirations of professional performers are exemplified by the musicians union. It cannot be maintained that all of the activities of this union were motivated solely by a desire to advance the cause of music, good or otherwise, but music has had no more steadfast and ardent supporter than the musicians. For decades the union has been fighting for, and promoting, live music.[1] Its tactics have changed over the years, but the goal remains the same—live music for everyone's taste. It is interesting to note a new plan for "musicians in residence" set forth in a resolution at the 1960 convention, which stated, in part:

"Cities all over the United States are not now getting their share of live music. Musicians drift toward the main three centers: New York, Los Angeles, and Chicago, because of lack of employment opportunities elsewhere.

"This centralization works against the culture of America by denying live music to most of our country and it creates in the three centers an apparent oversupply of musicians.

"Statistically, 265,000 members of the A.F. of M., not all of whom are playing men, are furnishing music for 170 million people in our country. If they were all regular performers there would be 1 musician for each 641,509 people. Actually, the ratio is even smaller.

"A great art is suffering; the people's chance to hear and know live music is nonexistent, and unemployment among musicians is catastrophic. It is a matter of survival for musicians to solve this problem.

"Even in the major music centers, commercial musical opportunities are drying up due to automation and the ever-increasing proficiency of musicians.

"The natural antidote to canned music is noncommercial live music, which is a well-recognized need of people everywhere. They are not getting it because they do not realize that music they like and need could be available at a nominal cost. In supplying the vast areas of our country with noncommercial live music, employment possibilities on a guaranteed annual wage basis would be unlimited.

"A unit of 15 to 25 men for a city of 50,000 to 75,000 is suggested, capable of performing for dances, shows, etc., also of furnishing the nucleus of a community symphony, and of splitting into various jazz or chamber ensembles. Emphasis is placed on small combinations playing popular music as well as other types, which could be joined together for large events. These muscians would be in residence in the town and on call for any noncommercial cultural usage they could service. Classroom demonstrations, school concerts, service club events, civic events, teenage dances, cultural and jazz concerts are some of the ways such a group could be utilized, therefore, * * *."

Another current interest of the union is an annual international string congress. The second annual congress was described in the March 1960 issue of the International Musician, the union magazine, as follows:

"The Second Annual International String Congress, to be held in San German, P.R., June 21 to August 15, is a continuing scholarship music program dedicated to the development of young string musicians in the United States and Canada.

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[1] For the study of this campaign, see "The Musicians and Petrillo," by Robert D. Leiter, New York, Bookman Associates, 1953.

The American Federation of Musicians is indeed privileged to cosponsor this outstanding program for the furtherance of good music in America.

"The A.F. of M., in cooperation with nationally known leaders in music, education, entertainment, industry and government, is sponsoring its Second International String Congress at the Inter-American University, San German, P.R., June 21 to August 15. One hundred winners of community auditions in the United States and Canada will receive scholarships donated by federation locals. Such scholarships will provide 8 weeks of intensive instruction under noted teachers at the Inter-American University.

"The string congress itinerary calls for scholarship winners to assemble in Washington, D.C., from where they will depart by chartered airliner for Puerto Rico, arriving June 22, to attend the final day of the Pablo Casals Festival, with study beginning the following day at Inter-American University * * *.

"Eighteen public programs are planned for the congress during the summer course. Thirty-four broadcast concerts will be taped. During the last week of the congress 50 of the most skilled students will be guests of the International Conference of Composers at Stratford, Ontario, Canada, where they will perform a program of contemporary music.

"In last year's highly successful congress at Greenleaf Lake, Okla., 83 students from 63 cities in the United States and Canada participated. The goal this year is 100 students. After this has been reached, no additional entrants will be accepted."

The musicians union is a strong supporter of Federal subsidies for the arts, for the education of the public as well as support of performers. This policy is written into the union constitution in the following words: "The international executive board is instructed to do all in its power to persuade the Federal Government to create a national subsidy for music in this country; this fund to be recognized and to be used as educational facilities for the people in this country in the same mannner as our State and national public welfare and educational systems which are now in effect."

On the community level

In recent years, the trade union movement has been developing and increasing union participation in community affairs. Outside of the performing unions, it cannot be expected that local unions would take the lead in developing a community's appreciation for, and opportunity to engage in, the fine arts, although in large cosmopolitan cities unions have played and continue to play a role. On the other hand, there seems to be good reason to expect unions to support any community drive to advance the arts, even if the unions do not aspire to become eminent patrons of the arts.

To the Department of Labor's knowledge, no study of union participation in the arts on a community level has ever been made. In the city of Washington, D.C., instances of such participation would include the following: the retail clerks contributed funds for a second performance of a children's play by the District of Columbia Department of Recreation; three blue-collar unions are listed among the members of the National Symphony Orchestra Association for 1961–62; three stained glass windows in the National Cathedral were made possible by joint contributions by the Phillip Murray and William Green Foundations; the mosaic mural in the AFL–CIO Building, which may now be the most widely known (or photographed) are work in the city; and, possibly to stretch a point, the architectural contributions of the many union buildings erected in recent years in the city.

Union recreational activities

In the preamble of the AFL–CIO constitution, the federation is pledged, among other things, "to the attainment of security for all the people [and] to the enjoyment of the leisure which their skills make possible." Providing recreational outlets for their members has long been a recognized activity of trade unions, particularly at the local level, and if such activities tend to concentrate on team sports, dancing, and picnics, members' tastes occasionally demand something finer.

The International Ladies' Garment Workers Union, still famous as the producer of the show "Pins and Needles" in the late 1930's, is undoubtedly the chief practitioner of the higher artistic education of union members, a tradition in the union dating back to its founding. The work of its education department, as summarized in the report of the general executive board to the 1959 convention, includes the following items:

The traditional work of the department includes study classes, institutes, lectures, educational meetings, film showings, recreational and cultural activity, counseling, and the preparation and supplying of educational materials.

The handicraft and sculpture workshops in New York City have been continued on 4-day-a-week basis and held successful annual exhibits of their work in 1957 and 1958.

St. Louis, Kansas City, and Montreal also have run successful exhibits of their work in 1957 and 1958.

The northeast department has developed musical revues as a staple feature of its educational program. Boston stages an annual musical revue. Also, in the New York area, there are choruses maintained by locals 22, 48, 60A, 62, 91 and the Passaic affiliates.

In New York, timely lectures are given at Hunter College and at the Charles Evans Hughes High School, where they are part of a recreational-cultural-sport program.

In New York, ILGWU locals are making special efforts in behalf of their Spanish-speaking members. English classes for Hispanics, special counseling services, special Spanish language pages in local publications as well as expanded justicia, along with workshops for business agents designed to acquaint them with language and cultural features of the new membership, are some of the activities aimed at integrating the newcomers into the life of the union and the community.

Thousands of ILGWU members have visited the headquarters of the United Nations and its agencies, and the Hyde Park home of Franklin D. Roosevelt.

Trips have been exchanged between locals in New York City and Montreal and Toronto. Groups of members have visited Puerto Rico, Washington, Valley Forge, Philadelphia, Niagara Falls, and Brookhaven Atomic Laboratory.

An outstanding experiment was made by local 62 in 1958, when 89 members visited 9 European countries in 30 days. A smaller group from Montreal made a 37-day European tour. These followed group visits to Italy previously by members of locals 89 and 48.

The book division renders both cultural and financial aid of outstanding importance. For locals as well as individuals, it aids in the selection of books and contributes toward their purchase price.

At Unity House, a vacation resort maintained by ILGWU for its members, concerts and other cultural activities are regular features.

Whether or not other unions now turn their recreational activities to similar ends, such activities can respond quickly to changes in members' interests, possibly spurred by the interests of women's auxiliaries. The retirement halls and pensioner's clubs, increasingly becoming an important part of union life, may also someday provide outlets for more cultural activities. There is, however, no other area of human activity, in unions or elsewhere, where democracy is freer and more effective than in the individual's participation in the finer things of life; when popular taste runs to Bach rather than bowling, trade union educational and recreation programs will adjust accordingly.

Representative Reuss. Secondly, I think something along the following lines might be useful. You have talked a good deal, and so have all our other witnesses, about gross national product. Among other things, you have said today that the administration still favors a 40-hour week, because we need to produce a lot of goods and services.

I think it would be useful to the committee to have before it some concept of what proportion of a $600 billion national product ought to be in the form of the arts, music, recreation, outdoor living, the good things in life.

I am not suggesting that it ought to be up to the Government to control this mix, but since part of the function of this committee is to look at goals, this would seem to me a very useful one.

Do you think you could give us some help on that?

(The following was later received for the record:)

The basic data on dollar volume of expenditures for these items are collected by the Department of Commerce for their estimates of gross national product. This series has a component entitled "Recreation" which includes the following items: Books and maps; magazines, newspapers, and sheet music; wheel goods, durable toys, sport equipment, boats, and pleasure aircraft; radio and television receivers, records, and musical instruments; radio and television repair; flowers, seeds, and potted plants; admissions to specific spectator amusements—motion picture theaters, legitimate theaters and opera and entertainment of nonprofit institutions (except athletics), and spectator sports; clubs and fraternal organizations except insurance; commercial participant amusements; parimutuel net receipts; and other services. Unfortunately, there are no available data on recreation-related items such as vacation transportation, motels, and the variety of art objects included in such categories as household operations and jewelry.

The recreation component constituted more than $19 billion in 1960 or 3.8 percent of the total gross national product. It may be estimated that if the GNP rose to $600 billion in 1963 there would be some $24 billion spent on recreation.

Secretary GOLDBERG. Yes. As a matter of fact, this has been happening on the part of our gross national product. In our own time, increasingly, as we have had the benefit of more leisure, as we have reduced the workweek to 40 hours, we have developed a great interest——

Representative REUSS. May I interrupt you at that point to say that while it is your present policy that a 40-hour week is what this country needs in order to produce the goods and services that are needed, you would agree with me, would you not, that the general trend of our workweek in the years and decades to come must be and should be in the direction of a shorter workweek?

Secretary GOLDBERG. Oh, there is no question. As a matter of long-range time, our people will have more leisure time and more time to spend on many of the worthwhile things of life that are outside of the normal factory or agricultural employment.

I was saying that as we face the immediate future, this is not a desirable development. This does not exclude a development over long range, which may come about and is coming about in a variety of ways.

For example, everybody would say that it is certainly within contemplation that vacations be liberalized as we go along. They have been liberalized in American life. That is part of the trend. There are many ways to achieve better leisure time for people, and this, as a long-range trend, will develop.

But what we are saying is that considering our position in the world, our need for goods, the world's need for goods and services, this is not a very good time to do it.

Representative REUSS. Of course, even with a 40-hour week, we already have a good margin of leisure time. I am sure that you agree that the problem of what people do with their leisure time is one that should concern everybody, private people, government, business, labor, and everybody else.

Secretary GOLDBERG. I certainly do.

Senator SPARKMAN. Mr. Javits?

Senator JAVITS. Mr. Secretary, about the steel strike, I notice some very revealing information given to us by the Council of Economic Advisers, which they call guidelines, and they say:

The general guide for noninflationary wage behavior is that the rate of increase in wage rates, including fringe benefits, in each industry, will be equal to the trend rate of overall productivity increase.

In other words, in short, as the Secretary, I am sure, follows that language, they think that a reasonable guideline for wage increases is if the particular wage of that industry is behind or up to or ahead of the overall productivity increase.

Now, is the administration going to make clear to management and labor in the steel industry, that that is what it expects in the public interest of the steel industry in its coming negotiation?

Secretary GOLDBERG. Senator, let me say this: These guidelines, of course, you read part; I am sure you will agree there are other elements that enter into it. Of course, not all industries are in the same place at a given time.

Senator JAVITS. May I say, Mr. Secretary, that I only keyed you to the particular one, but of course, it includes them all.

Secretary GOLDBERG. I feel that one of the important functions of Government is not to dictate or impose terms of settlement, but to define the public interest. I do not think we have done enough in that area in the past. Now, maybe we did not have to, because we were a free-wheeling country, and we allowed the clash of private interests to arrive at total adjustments which were effective and which would operate.

Our margin of tolerance is decreased because of our position in the world. We are no longer isolated from the world community. And I would answer you directly by saying yes, we would like the parties themselves to do the job; but we will define and assert the public interest as we go along, not in terms of attempting to impose a dictated point of view upon the parties concerned, but rather in the sense of providing guideposts and economic data upon which private collective bargaining can operate.

The answer is "Yes."

Senator JAVITS. And, Mr. Secretary, I am sure you will do the same with respect to the guidelines on price, which are also here referred to, as far as management is concerned.

Secretary GOLDBERG. That is correct. It will be an equal-handed statement.

Senator JAVITS. May I point out, too, Mr. Secretary, that you are sustained in that by what I consider quite a composite of statements in the public interest when we debated the steel price rise on the floor of the Senate. We all realize that our tolerance is very low now for letting collective bargaining go, in the sense that it might jeopardize the national interest. We want to have our say before, without trying to direct the parties.

Secretary GOLDBERG. Senator, I agree with you entirely. I do not think postmortems are as effective as some direct expression before the fact occurs.

Senator JAVITS. I am very glad to hear that you, speaking so authoritatively, feel the administration will do that, and I think it is very helpful.

Now, may I also point to another aspect which the steel strike will involve. I notice that in the kit of what you call, in your statement, "important measures recommended by the President," there is nothing that deals with the machinery for strikes which involve the national interest; and we are well aware of the fact, on the Labor and Public Welfare Committee, on which I have the honor to serve, that this is an area which urgently needs legislation. I think the Secretary himself has called attention to the inadequacy of the Taft-Hartley law 80-day injunction and the machinery which surrounds it, for giving a national interest finding to the parties, if necessary, in order to avoid a strike or shorten one, rather than to bring a dangerous and serious national situation to an end by the injunction route.

Would the Secretary care to—and I say that advisedly, because you are the Secretary; not the President—comment upon that, in terms of what is really needed?

Secretary GOLDBERG. We did not include in this recital of proposed legislation all of the matters which will be the subject of the President's messages to the Congress. We have, as you know, and as you correctly point out, been concerned with the adequacy of the legislation we have at hand to deal with strikes of national import. And the President has asked me to make recommendations to him, so that in turn he can make recommendations to the Congress in this area.

As a fellow member with you of the Senate Committee on Labor and Education, he has always had a great interest in this subject, as you have had.

Presently, I am awaiting two reports. One is that of the President's Labor-Management Advisory Committee which has under consideration this problem and hopes very shortly to advise the President and me as to the attitude of this important group on the subject.

I have also asked the advice of a group of experts in the area, independently of advisers to the Secretary of Labor, and I have received in part their advice. They are still working on the problem.

We would hope, after we get this advice—I will make recommendations to the President, and I would anticipate that the President will send a message to the Congress dealing with this subject.

Senator JAVITS. Now, does the Secretary feel that a message of that character and a proposal of that character can make a material contribution to the hopes of avoiding or producing early settlement of the steel strike, if we should unfortunately have one?

Secretary GOLDBERG. I think probably we would not be able, in the legislative process, to have that make an impact, unless it becomes necessary, in connection with steel. But I believe that the atmosphere is such at the present time that independently of legislation, there is good will on both sides to try this time to avoid entanglement with the national emergency provisions of the law.

Senator JAVITS. Am I to take that, then, that the Secretary expresses some optimism that a steel strike may be avoided?

Secretary GOLDBERG. It is always dangerous to prophesy, but I do believe that the signs are hopeful for avoiding a strike this year.

Senator JAVITS. The Secretary speaks, I think, as more than a Secretary of Labor in that field in terms of his expert knowledge. I am sure he has no other information, but I do respect his knowledge.

Now, Mr. Chairman, I have a minute or two, and I would like to turn to another subject.

I noted with great interest that at a conference at which I happened to have the honor of being one of the speakers, the President of the AFL-CIO had the following to say, which bears directly on the Secretary's statement today as to the effort to deal with unemployment, and I quote George Meany in his opening address:

> The great lack of the administration and the country is a sense of the urgency of this problem. The unemployed have become the invisible men in America. They have become statistics instead of people. I say that is an attitude we simply can't afford.

The papers, Mr. Secretary, bill that, as the Secretary knows, as assailing the President. I am referring to the New York Times. I wonder whether the Secretary would be interested to comment, in view of the feeling he has expressed in his statement that the administration measures are designed to deal specifically with that in what he considers an adequate way.

May I say, Mr. Secretary, that I am not examining you as a cross-examiner. If there is any question you want to file a statement on or defer the answer to, please feel free to do so.

Secretary GOLDBERG. No, Senator Javits, on the contrary, I regard this to be an opportunity to say something through this committee to Mr. Meany and the labor movement.

I understand, and I certainly welcome, Mr. Meany's statement showing the great concern that he has, as the head of the American labor movement, about the unemployment situation. It is very natural and very understandable that this problem looms so large in his mind.

I would say to him and the American labor movement that, as is apparent from the Council's report, from the work of this committee, from the President's message to the Congress, from my testimony, we share this concern that he manifests in full measure.

The unemployed worker in America is not a man neglected in the programs of the administration or in the concern of the Congress.

I remember that a few days after I took office your committee called me before the committee to talk about this problem. The members of this committee will remember that one of the first actions I took as Secretary of Labor, with the President's complete approval, was to go around the country and look into this.

This is our major concern, as a matter of fact, in the domestic economy. The President said, in filing his report, which this committee is considering:

> It is intolerable in a democracy that we have a continuous high rate of unemployment, and our policies, administrative and legislative, and our public and private policies, must be directed to a solution of this problem.

It is not only a matter of domestic concern. I have discovered, in the three presidential missions on which I have had to go abroad since I took office, that this is a matter of great international concern.

The first question I have been invariably asked when I have been abroad is not whether we are going to resume nuclear testing, although that is a matter of great concern to many people, and not about international affairs, peculiarly enough, but, "What about your unemployment situation in the United States?"

The health of our domestic economy affects our posture in the world; and it is a matter of major concern to the administration.

Senator JAVITS. Thank you, Mr. Secretary.

Senator SPARKMAN. Senator Proxmire?

Senator PROXMIRE. Mr. Secretary, I want to join the general encomiums. I have been hearing testimony on unemployment since December 18. I heard Mr. Clague, among others, and thought his testimony was very, very helpful. But in terms of a comprehensive presentation of the whole unemployment problem, I think this is about the best I have heard anywhere, and it is very encouraging and very good.

I am especially happy about how you smack very hard at the beginning at the position of the administration that 4 percent is not the goal, that the administration is not satisfied with 4 percent unemployment, that this is just a temporary benchmark.

Day before yesterday, we had a briefing by the Advisers of the Federal Reserve Board, very learned, scholarly, able men, and there was some confusion about this point, and there was a feeling of at least some members of the committee that the administration felt that 4 percent was about as well as we could do without serious inflation. I am glad that you underline that this is not your goal, is not your position in your text and underline it in your tone of voice, and I hope you keep repeating it.

Secretary GOLDBERG. I shall.

Senator PROXMIRE. Now, there are several things I would like to ask about, but what mainly concerns me about this whole situation—when I say this is the best I have seen and read: I feel that we are not recognizing that unemployment is not simply a cyclical problem; that this is a long-term problem. And I call your attention to something you undoubtedly know very well, but which is dramatized in the charts in the Economic Report of the President, which shows the latest figure you have given us of 5.8 percent, 1 year after the trough of the recession, and at the beginning of the upswing, is about as high as we have had it in any of the four post-World War II recessions. It is discouragingly high. As you said, it means 4,663,000 people out of work.

Now, 1 year after our recovery, we still have this percentage of the work force out of work. Will you agree this is not simply a cyclical problem?

Secretary GOLDBERG. I agree. It is a combination of factors and cannot be explained only in cyclical terms.

Senator PROXMIRE. The reason I stress this is because I think most of the measures that have been proposed by the administration are designed to cope with cyclical unemployment. This I think is true of the tax proposal, the temporary tax cut. This is true of the public works proposal. It can only be used at the bottom of the trough. If anything, they would borrow employment from the recovery period. And also it seems to me there is a lack of attention given by the administration, even in this very excellent report, to the supply side of the labor situation.

I think that perhaps one of our most constructive contributions to believing in the unemployment situation as it has been in the 1930's has been on the supply side, not just in shorter hours of work and longer vacations, but also in terms of the terrific impact of increased transfer payments.

As you know, transfer payments increased 150 percent in the last 8 or 9 years. People who are receiving social security and have an adequate social security check do not have to work, are not forced to go into the work force, stay out of the work force. Some young people whose parents are receiving unemployment compensation or grandparents social security can stay in school longer; are out of the work force and doing constructive activity which is going to help them in the future.

I think if we can look at this as a long-term problem and do all we can to encourage people, if they wish to do so, to have the chance to retire earlier and get out of the work force constructively in that sense, and encourage our young people, which contribute so heavily, as you have stressed, to our unemployment problem, to stay in school until they have a skill, this can be a very constructive contribution to the unemployment problem.

Secretary GOLDBERG. I agree with you. But I think we have made some steps in that direction that are very good steps. I did not mention the figure, but in my testimony you will see already one of the impacts of the legislation enacted by the Congress at the last session.

Senator PROXMIRE. Yes, I noticed that. That retirement at 62.

Secretary GOLDBERG. We have doubled the amount of applications for retirement as a result of this legislation; some 275,000 applications for early retirement under the law that was passed last year by the Congress amending the Social Security Act to lower the retirement age for men to 62.

Now, that is very helpful, and I think measures like this, that are designed to do just what you have said, are very important.

School dropouts: This is a very serious problem. We estimate, if it continues at the present rate, 7½ million young people entering the labor foce during the sixties will not have completed high school. We cannot afford that. And we have to attack that problem very vigorously.

The manpower and training bill, for example, is designed to deal with this problem that you are talking about, and that is to take people who are long-term unemployed, structurally unemployed people, many of them, and equip them so that they can move into the area of job vacancies.

Senator PROXMIRE. If I can interrupt you at that point, I think that the difficulty with the Manpower Training Act, for which I voted, which I think is excellent and useful, is that this does cope with structural unemployment, and I am convinced on the basis of studies that we had among our staff that the main problem is deficiency in demand as contrasted with supply. Measures to cope with structural unemployment are helpful, and there is a significant but relatively small proportion of the unemployment problem that can be assisted this way.

But the basic problem is getting an adjustment between supply and demand of labor which can keep those people who want to work usefully employed. And somehow, I just cannot find recommendations in here that cope with this on a long-term basis. Although I approve everything you have in here, I do not find, for instance, any encouragement of further increases or improvements in the social security program to enable people to retire earlier, although perhaps there are reasons why this cannot be recommended to the Congress at this time, but a recognition of the contribution this has made.

And all the training programs, which I think are fine—the Youth Opportunities Act—you have three of them listed there, all of which will take a great deal of Federal money, but I think are warranted.

Still, I think if we can do what we can to encourage the young people to stay in school and encourage our schools to provide vocational training, we can do this far more cheaply, and we can do it more comprehensively than these pilot programs, which, even at this level, are going to involve considerable amounts of money.

Secretary GOLDBERG. Well, let me just say this: I think that we need, as you have indicated, a total program to deal with the unemployment problem generally. And unemployment, as I think you properly said, consists of a combination of factors. We can argue the extent to which one is as important as another, but I think overall I would agree that demand is the most important aspect. We do have structural unemployment, which is indicated in the figures.

Now, I have not, in this proposal, attempted to review all of the legislaitve proposals of the administration. I did not think it appropriate in my testimony. But I would agree with you 100 percent that upgrading the education of the country is very important in this area; and education of various types.

Young people ought to stay in school. It does not mean that every person ought to stay in the same type of school. There is room for a broad area of different types of education in the country.

And this will be helpful in many areas. Not only will it prevent people entering the labor force when they ought not to enter the labor force, without the proper skills and without the proper backgrounds; it will make for a better life for people, a more fruitful life, to have a better education, which in itself is a desirable objective.

In connection with social security, there Congress acted last time. We need a review again—and I indicated part of the area—of the total social security area, including the private and the public sector. And that has to be studied.

Senator PROXMIRE. On that point, is it not true that more than half of our people over 65 have incomes which are—what? Less than a thousand dollars a year?

Secretary GOLDBERG. That is correct for unrelated individuals. For men the latest census data for 1959 show that half of those 65 and over had annual incomes under $1,576.

Senator PROXMIRE. And our social security system, advanced as it is compared with what it was 10 or 15 years ago, is perhaps not as advanced as are the social security systems of Europe, Germany and some other countries, where in view of their lesser standard of living, they seem to be making a greater effort in this area, relatively, at least, than we are.

Here it seems to me a man who has an income of $1,000 a year is pretty much constrained to go to work, regardless of social security. He has to in many cases.

Secretary GOLDBERG. I certainly think we could look forward to and justify improvements in our social security system.

Senator PROXMIRE. And here are 16 million people over 65. It seems to me this could be an important segment of our work force.

Secretary GOLDBERG. That is true. I would agree with that.

Senator PROXMIRE. You see, what I am particularly concerned about is that, as you say, we are going to have, or we need, 5 million jobs, in order to get to 4 percent unemployment by the middle of 1963; and we do have this very serious automation problem, where we are going to have people coming off the farms at a very great rate.

And I just cannot see, looking at this as objectively and realistically as I can, how we are going to really put these people to work without giving some attention to limiting the supply.

I just want to bring out one more point.

You stressed very well that the work force did not increase as was expected during the last half of this year. And in a way, it is a good thing. You pointed out a reason why it is a bad thing, but there are also good elements about it. I think that we might recognize that this contribution to unemployment is something we can act on constructively.

Secretary GOLDBERG. I said in my testimony that if the reason for this lack of increase in the work force was that young people remained in school, and if the reason was that older people enjoyed the benefits of reasonable retirement, that was a good development. And I agree with you that this ought to be one of the areas that we ought to intensify.

Senator PROXMIRE. I see my time is up, Mr. Chairman.

Senator SPARKMAN. Congressman Widnall?

Representative WIDNALL. I would like to add my praise, Mr. Secretary, to your very lucid and intelligent presentation. I enjoyed listening to it.

In your formal statement, you said: "The recession loss of 1 million jobs had been virtually made up by the end of 1961." You further said that, "One-fourth of the gain was accounted for by employment increases in State and local governments."

Was not another 10 percent accounted for by an increase in Federal jobs, 100,000 Federal jobs?

Secretary GOLDBERG. After taking into account the rise in post office employment in December, the 1961 increase in Federal employment was rather small, almost 10,000 since January.

Representative WIDNALL. Was there not also an increase in employment of 360,000 by reason of the Reserve callup?

Secretary GOLDBERG. Yes. I point out that there is no question that the callup in the latter part of this year had an effect upon diminishing the labor force. This did not have to do with jobs, but it took people out of the labor force. We do not count those as jobs.

Representative WIDNALL. But they were replaced by new workers?

Secretary GOLDBERG. Yes, undoubtedly it had an impact upon employment by the fact that other people went in and took those jobs, although we don't know whether all the called-up persons were replaced.

Representative WIDNALL. In adding this all up, I figure that private enterprise only furnished about 25 percent of the making up of that recession loss: Federal, State, and local government, and a call upon the Reserves accounted for 75 percent of it.

Secretary GOLDBERG. You are undoubtedly correct, that much of this increase was due to the fact that it was picked up by Government—that is correct—and also picked up by the fact that people had to move into jobs that were vacated by people called into service.

Representative WIDNALL. In making these remarks, I am just hopeful that, to get down to your 4 percent figure and provide 5 million jobs, you are not going to have 4 million Federal, State, and local government and others being called back into the service. I would hate to see that same pattern prevail all the way through.

Secretary GOLDBERG. As a matter of fact, when we posed the challenge of the period, we contemplated from amounts given by the Secretary of the Army that we were going to return Reserves, by the middle of the year, we hope, back into the civilian labor force, and the Federal budget does not contemplate expansion in a major degree, or Government employment. So that we are going to have to rely upon recovery in the private economy to pick up these jobs.

Representative WIDNALL. A very essential part of the new program would be, then, to create the incentives for private enterprise to go ahead and expand productive capacity, to remodel plants, and to provide job opportunities that way?

Secretary GOLDBERG. I emphasize in my prepared testimony—and I want to emphasize, now that you have given me the opportunity—the important necessity for increasing investment in this country in modernizing our plant and equipment. We have fallen behind very badly. A great deal of our plant and equipment is obsolete. In spite of the fact that we talk about automation, we are going to lose jobs if we do not modernize our plant and equipment in this competitive race that we have in the world.

Representative WIDNALL. Mr. Secretary, I think you said that your studies have shown that the impact of imports on the United States had not been in the areas where high wages were paid, essentially in the durable goods industry.

Secretary GOLDBERG. That is correct.

Representative WIDNALL. Now I would like to call your attention to some statements in the Survey of Current Business, issue of January 1961, as it pertains to steel. On page 12 it states:

> The United States has been a net importer of steel mill products since 1958. Last year the margin in favor of imports was 1.1 million tons. This compared with nearly 400,000 tons in 1960 and 2.7 million tons in the steel strike year of 1959. For the 3-year period as a whole, the import balance amounted to 4.2 million tons, by way of contrast to 1955–57, when our exports exceeded imports by 10.3 million. The 1961 exports constituted less than 3 percent of total steel shipments, compared with 5½ percent in 1955–57 and over 4 percent in 1950–54. The share of imports has increased from a long-term average of a little over 1 percent to 4½ percent currently.
>
> These data do not take into account the steel import in final product, such as autos, which in recent years have become increasingly significant.

Isn't this something that could be increasingly worrisome if we get into the trade program that the President has advocated?

Secretary GOLDBERG. Well let me address myself to the steel problem, about which I know a little bit.

I think, in order to get a correct picture of the steel exports and imports, in addition to the material that has been presented by that story, we ought to know about the dollar volume, which has not been mentioned in that report.

Steel imports and exports are of various types. We export generally steel of the bigger type and the more expensive type; so that while there have been percentage increases in imports, and there is no question that there is a problem, nevertheless, dollar volume figures have remained high for exports, because of the type of steel we export.

So we really have to get the total picture, which is not presented by this story. It is not quite as bad as appears from a percentage account as related to the dollar volume.

Now there are other factors that enter into this, which this committee has looked into in the past. I think one of the reasons we are so anxious to avoid a repetition of the strike again: There is no question that when we have an interruption of work, suppliers make long-term agreements abroad to get their needs taken care of. And that entered into the pattern of steel imports that has taken place in the last few years.

The people abroad are good businessmen. They are not willing to enter into arrangements to meet the needs of American suppliers only when they are in trouble because of a strike. They insist upon some long-term commitments. That has entered into it.

There is a third factor, which is not discussed in this report, and that is that the steel industry is in trouble, in some areas competitively situated, because of the lack of modernization of our mills.

I saw a steel plant in Senator Sparkman's State where there has been great progress in the steel mills of the State. It is one of our great steel-producing States. But I also saw equipment in one phase of the operation which is particularly subject to competition, in the nail-and-wire end of that plant, which is terribly inadequate. It is no surprise that that could not compete with the modern plants abroad. That is a factor.

The fourth factor, of course, is not only the wage factor, but we have to look at the pricing policies of our industry. They have got to be competitive.

I know that there are problems involved in this in terms of productivity, wages, and so on; and so both sides have to look at that equation.

Now on the trade policy I would think that liberal trade policies in general would help the steel industry. The steel industry, it must be remembered, is also a great importer, and is very interested in liberal trade policies from an import trade standpoint. They import a lot of iron ore, and as importers they have an interest, then, in being liberal traders.

This has caused some problems in our country from that standpoint, because our people in Minnesota who work in the iron ore mines are not too happy about that. But it demonstrates that trade is a two-way street even for a particular industry. The steel industry cannot be protectionist when it comes to one aspect of their problem and be liberal traders when it comes to what they want to import. It indictates that we have to have an overall trade policy of a liberal character.

So this is something I think you share when we look at a report such as this. We have to look at the total picture.

Representative WIDNALL. Thank you.

A statement has been made recently that the vocational schools in many instances are teaching outmoded skills, and that something definitely has to be done in order to bring them up to date in the teaching of skills. Is anything being done along that line at the present time?

Secretary GOLDBERG. Yes, Mr. Congressman. The President has appointed a panel which is hard at work analyzing the vocational educational programs to make sure that they are upgraded and kept current with the needs of modern technology. We are participating in the work of that panel.

It is a very excellent panel; and just the other day I presided at a meeting of the President's Committee on Youth Employment, where the staff directors of that work reported that they were making excellent progress.

Representative WIDNALL. Mr. Secretary, I was very interested in your report on the retraining of workers. I had more than a casual interest, because, you may remember, I had a substitute area redevelopment bill, which, incidentally, had more than twice as much for retraining as your own bill had, and you might like to have some of that money at the present time.

Secretary GOLDBERG. We could use it, Congressman, because we are running out of money on this bill.

Representative WIDNALL. You said that one of your first projects was the training of a thousand tractor operators in New Jersey?

Secretary GOLDBERG. No. We have a project which is listed here to retrain tractor operators in New Jersey and Mississippi. And this is the total for both of those States.

Representative WIDNALL. What is the demonstrated need in New Jersey for tractor operators?

Secretary GOLDBERG. Can I ask Dr. Wolfbein, who supervises that program and is more familiar than I with the details, to respond to that?

Dr. WOLFBEIN. Just briefly, this is in Atlantic County, N.J., Congressman, where the agricultural education people and the community officials of Atlantic County in our employment office made a survey and found that there was a substantial need for men who could operate the tractors and make minor repairs on them, and if we approved the training program, every one of these people would be employed. The total number involved in Atlantic County is 25, which is rather small.

Representative WIDNALL. How long does it take to train a tractor operator?

Dr. WOLFBEIN. This particular program, including giving them some skills on the repair, is 12 weeks.

You see, the bill does not permit, as the Secretary has pointed out, more training than 16 weeks.

Representative WIDNALL. Is there anything going on in the training of secretaries in retraining programs? I think there is a greater shortage of good secretaries in the United States than almost anything else.

Secretary GOLDBERG. I agree with you on that. If you will look at attachment 2, you will find that as part of the training program there is a training program for secretaries and typists.

I want to point this out: We must remember that this is not an overall training program for the country. This is a training program where first we must get a plan, as you know, from a redevelopment area. There is no question that when we go into our broad program, if the Congress gives us the broad program, that this will be one of the important areas.

As a matter of fact, I have just put in a proposal within the Government, in my own Department, to train people in the Department, and particularly clerical help, in typing, stenography, and so on. And I think this is a very interesting program.

Representative WIDNALL. Thank you very much.

Senator SPARKMAN. Senator Pell?

Senator PELL. Secretary Goldberg, I apologize for being late, but I have read your testimony, and I join with my colleagues in commending you on both your written testimony and oral presentation.

In connection with Senator Bush's questioning, I, too, am worried about the impact of the President's trade expansion program. The message that was sent up to us discussed trade adjustment. In my view, it did not go sufficiently far. It did not discuss grants, merely matching loans. And there was no mention of communities.

I was wondering if any study had been made of the jobs that may be lost in these 2 years, particularly in the rubber and textile industry. And in your statement, in that connection, I notice that you say that textiles will benefit by this trade expansion program. I wonder if you could enlarge on that for us.

Secretary GOLDBERG. First let me reply to your first question. We are doing a study of the relation between imports and employment. We will make that available to the appropriate committee of the Congress, and we will see to it that this committee also gets the benefit of that study.

Senator PELL. Will that be broken down by industry and by States, or how?

Secretary GOLDBERG. Perhaps you would like to hear from Dr. Clague about that. He is conducting the study.

Dr. CLAGUE. We will provide certain information by industry. We will try to do it by States. I would not want to be sure. But since the effect of imports at present is on particular industries, and that is the way imports operate generally, they hit at particular places where the industry is located. The total for the Nation as a whole may not be large, but it may be heavily located in a particular industry.

Now, as far as textiles are concerned, of course, there is some export employment also connected with textiles, as we have shown in our study, here. It works both ways in that connection, also.

Senator PELL. It would be most helpful if you could try and make a point of breaking it down by areas as well as by industry.

Dr. CLAGUE. Well, let me explain. Since we do have employment by States in this country for individual industries, and also by at least a hundred major labor market areas, the answer is that the general impact by community is bound to show up. If there is a decline in textile employment, we may be able to distinguish Connecticut from Rhode Island, or from New Jersey or other States.

Senator PELL. Will the jewelry industry or the rubber industry, for example, be included in this study?

Dr. CLAGUE. We are trying to study all the industries in which we find any significant impact of imports.

Senator PELL. Thank you.

Mr. Secretary, would you turn for a moment to the Welfare and Pension Plans Disclosure Act?

The President in his annual Economic Report, suggested that these funds should be more adequately and more stringently supervised. As you know, their growing importance makes it desirable that these funds be invested not sterilely but with imagination, with a view toward their impact on our economy. I notice on page 25 of the President's Economic Report it states that authority to regulate should be vested in "a responsible Federal agency."

The act calls for it to be vested in the Labor Department. I was wondering what the reason was behind such a discrepancy in viewpoint.

Secretary GOLDBERG. There is no discrepancy, and I would like to explain. There are two concepts involved, and I do not think they ought to be confused. I know you are well aware of this. We have discussed this in the past.

First of all, this is a very important question. As I have indicated in my prepared testimony, plans now, in this area of welfare funds, add up to the astonishing total of $58 billion in assets. And the way they are going, by 1970 these plans may reach $100 billion.

Now, the present bill pending before the Congress, which will be before the Senate and before the House, contemplates no change in investment policy. I would not think it proper that the Department of Labor administer the investment policy of these trust funds. I do not think it would be appropriate that we do so, and I have made no recommendation to the President that the Department of Labor be that agency.

The present bill is a very limited bill. It does not attempt to deal with this important subject that Congress ought to study and I hope will receive, as the President recommends, attention of the Congress; because after all, the investment policies of this astonishing amount of the Nation's capital should receive the study of the Congress.

Senator PELL. Excuse me for interrupting.

Has any study been made, to your knowledge, of the character of the investment policy governing these funds?

Secretary GOLDBERG. I am not aware of any governmental study on this subject, other than what the Council may be doing in just following it generally.

Senator PELL. Perhaps one of the subcommittees of this committee might very well consider that.

Secretary GOLDBERG. This is a very important problem.

Now, what we are recommending to the Congress—and this I think should be administered by the Department of Labor, because there we have the expertise and the knowledge, arising out of the fact that Congress has entrusted us with the responsibility of supervising union funds generally—is disclosure to insure honest administration of the operations of these funds; not anything to regulate their investment character, not anything of that type.

Now, the Congress entrusted us with the responsibility of doing this in the union field, for union funds, for this reason: Why did they give that to the Department of Labor and not to the Department of Justice, the SEC, or someone else? They did it because Congress said, as the basic mandate of the Department of Labor, that we have the responsibility of looking after the welfare of the working man of the country. That is our basic statute. That is the charter of the Department.

They said that obviously working people have an interest in the operation of union funds, to see they are honestly expended, correctly reported, and so on; so they have vested us with this responsibility.

We have discharged that responsibility I think to the general satisfaction of the Congress and everybody else, carefully. Largely, we have done it by preventive techniques. We have tried to educate the trade union community as to their financial responsibility.

Now, in the field of welfare funds, these welfare funds, whether they are by collective bargaining agreement or created by the employer, are created for the benefit of the working people, the employees of these companies. And the problems of disclosure are almost identical with the problems that we have in the trade union field. They permit the same techniques. They apply the same experience.

Now, SEC, for example, has written to the Congress, in response to an inquiry, and they say they do not feel that they appropriately can deal with this problem on which they have no expert knowledge or competence.

And it is not a jurisdictional reason which impels me to say that at this stage we ought to move into this area, that we are long delayed. We should not rely on just internal safeguards to see to it that $58 billion of funds is being administered honestly. This is not appropriate, any more than we rely upon it to see that banks are administered honestly, or our stock exchanges, and the like. We ought to take action and ought to take action now. Almost everyone in Congress agrees to this, as is shown by the record. And I would hope very much that we can do this.

When it comes to the other question, of looking into the more substantive problem, then I would tell you quite frankly I will appear and say that we are not the proper body to do it.

Senator PELL. May I ask one further question, which I imagine you may not have the answer to at your fingertips, but maybe you could submit it for the record at a later date; that is, what number of men are engaged in analysis of these portfolios, how many of these portfolios is each of these men responsible for, and how often do the portfolios get a look-see by the analysts?

Secretary GOLDBERG. As presently set up?

Senator PELL. Yes.

Secretary GOLDBERG. Oh, our present arrangement—the law which was passed, which the prior administration felt was extremely inadequate, and which I do, does not permit us to do anything about it.

We have a group of people—I can put in the record the number—who filed the plans as they were received, and who make a very limited check, which is all we are permitted to make under the statute, to see to it that the filings are there.

Senator PELL. But there is no analysis being made presently of the funds, so that odd investments or disproportionate investments in a particular company can show up?

Secretary GOLDBERG. We are not authorized to do that under the present statute.

Senator PELL. Would you be authorized to do that under the act that is proposed?

Secretary GOLDBERG. We would be authorized to make an investigation; only we are not authorized to examine into the question of management decision as to where the investment is to go, or how it is to be made. The only thing we would be authorized to do is to conduct investigations to make sure that any fact reported in these plans is correctly reported.

Senator PELL. But if the act is passed, I was wondering if you could have one of your staff furnish for the record what your plans would be as far as regular portfolio analysis is concerned, and how many portfolios would be assigned to a single analyst.

Secretary GOLDBERG. Oh, yes. You are correct in pointing out to me that we are also authorized under the present statute to make studies of what the data indicate; which will be very helpful when Congress considers the other question.

Senator PELL. My point is that a skilled analyst can look at the portfolio, and if there are any irregularities, they often are very quickly discernible.

Secretary GOLDBERG. We are authorized to do that, and I will file for the record what our proposal is in connection with staff in the new legislation.

Senator PELL. Thank you, sir.

(The following was later received for the record:)

At the present time the Division of Health, Welfare, and Pension Plans in the Bureau of Labor Standards has 85 employees with an annual budget of $556,000. If the proposed amendments are adopted it is expected that there will be an increase of 175 positions in this Division exclusively, with an added cost of $1,644,000 annually. In short, we estimate that this Division would be composed of 260 positions with an annual budget of $2.2 million.

Senator PROXMIRE. The hour is late, and you have been very patient, Mr. Secretary. I will be as brief as I can.

The Economic Report provides data and analysis concerning productivity of the total economy and total manufacturing. Steel, which we discussed, was not covered specifically. I wonder if you can supply the data for steel for the record, comparable to that broader category that is in the report. It would be very helpful.

Secretary GOLDBERG. Yes, we will be very glad to do that.

(The following was later received for the record:)

INDEXES OF OUTPUT PER MAN-HOUR FOR SELECTED INDUSTRIES, 1939 AND 1947–60—ANNUAL INDUSTRY SERIES, DECEMBER 1961

(From the U.S. Department of Labor, Arthur J. Goldberg, Secretary; Bureau of Labor Statistics, Ewan Clague, Commissioner)

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INTRODUCTION

This report extends the industry indexes of output per man-hour, output per employee, and unit labor requirements prepared by the U.S. Department of Labor's Bureau of Labor Statistics. The data cover the years 1939 and 1947–60 for some industries but extend only through 1958 and 1959 for the remaining industries.[1]

The industry indexes presented here deal with the relationship between production in physical units and employment and man-hours. The Bureau also publishes, for broad economic sectors, indexes of net output per man-hour and per employee which deal with the relationship between value added (in constant prices) and employment and man-hours.

The employment and man-hour components of the industry indexes are based on data from various sources which are identified in the accompanying tables. In concept, indexes based on man-hour data from the Bureau of the Census and the Bureau of Mines relate to hours at work. Man-hour data from the Bureau of Labor Statistics include not only hours at work but also such payroll hours as vacations, holidays, and sick leave paid by the establishment directly to the employee. The indexes based on data from the Interstate Commerce Commission are a mixture of the two concepts. In general, because of increases in paid leave during the period, output per man-hour worked would tend to show a higher rate of gain than output per man-hour paid. However, actual differences may result from statistical limitations in the data as well as from conceptual reasons.

The selected industries for which output per man-hour indexes are available are not necessarily a representative cross section of American industry. They

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[1] Some revisions have been made in the indexes which had been previously published, because the output indexes of most manufacturing industries have been adjusted to preliminary 1958 levels based on data from the 1958 Census of Manufactures. The indexes for two industries previously published, the telegraph industry, and lead and zinc mining are excluded because of limitations which have developed in the available basic data.

should not be combined in any fashion to obtain an overall measure for the entire economy nor for any sector.[2] Each index is intended to represent only the change in output per man-hour for the indicated industry or combination of industries.

Although the measures relate output to employment and man-hours, they do not measure the specific contribution of labor, of capital, or of any other factor of production. In short, they do not reflect solely changes in the productiveness of labor. Rather, they reflect the joint effect of a number of interrelated influences such as changes in technology, capital investment per worker, utilization of capacity, layout and flow of material, managerial skill, skills of the work force, and labor-management relations.

More detailed information on the methods and sources is contained in "Trends in Output Per Man-hour and Man-Hours Per Unit of Output—Manufacturing 1939–53," BLS Report 100; "Trends in Output Per Man-Hour, 1935–55, Selected Nonmanufacturing Industries," BLS Report 105; and in a number of individual industry reports. These publications, as well as indexes for prior years for some of these series, are available upon request from the Bureau of Labor Statistics.

CHANGES IN OUTPUT PER MAN-HOUR OF PRODUCTION WORKERS

Changes in output per production worker man-hour in 1960 ranged from a gain of 11 percent in bituminous coal mining to a slight decline in the coke industry. In 1959 they ranged from a gain of 15 percent in the synthetic fibers industry to a decline of 7 percent in the full-fashioned hosiery industry. Thus, there was substantial variation in the annual changes in output per man-hour among industries.

Over a short time period, such as 1 year, changes in output per man-hour in manufacturing industries often tend to be closely related to changes in output. However, this relationship does not appear to have held in all the industries for which measures are available for 1959 and 1960.

When the gain in output per hour was large, the increase in production was also high. Outside of this high range, however, the relationship was not clear—small gains in output per man-hour may have been accompanied by small or large increases in production. Declines in output per man-hour were sometimes accompanied by decreases in production (e.g., canning and preserving, smelting and refining of copper, lead, and zinc), sometimes by increases (e.g., coke, seamless hosiery).

The changes for a single year are not, of course, indicative of the general trends for an industry. For this purpose, it is more useful to examine changes over a longer period of time. Thus, since 1947, in anthracite mining, bituminous coal mining, and railroad transportation, there have been very large gains in output per production worker man-hour accompanied by declines in output and substantial decreases in employment. In the synthetic fibers industry output per man-hour and output both increased very substantially, but the former by a greater amount, and employment declined.

In other industries, there were small to large gains in output per man-hour in the period since 1947 (there were no decreases). In some cases output did not keep pace or declined and the aggregate hours of production workers decreased (e.g., beet sugar, canning and preserving, coke, confectionery, flour and other grain mill products, hosiery, cigars).

CHANGES IN OUTPUT PER MAN-HOUR OF ALL EMPLOYEES

The changes just described have been in terms of output per man-hour of production workers. However, over the longer period since 1947, the rapid growth of so-called nonproduction workers (technical, professional, clerical, supervisory, etc.)[3] has resulted in a decline in the proportion of production workers to all employees. Thus, measures of output per production worker man-hour, while useful for many purposes, no longer provide a satisfactory indi-

[2] For the Bureau's indexes covering the private economy and the major sectors, agriculture, nonagriculture, manufacturing, and nonmanufacturing, see "Trends in Output Per Man-Hour in the Private Economy, 1909–1958," BLS Bulletin 1249, 1960, and the release of Aug. 18, 1961, "Output Per Man-Hour in the Private Economy in 1960."

[3] The term "production worker" has been used for many years to cover manufacturing employees who work at the plant and who are generally in nonsupervisory occupations. The term "nonproduction workers" is used to identify those industry employees who do not fall into the production worker category. This term is not intended to imply that these workers are nonproductive.

cator of output per all employee man-hour. Consequently, the BLS is developing indexes of output per all employee man-hour for as many industries as will be feasible.

The first industry for which such measures are now available is the basic steel industry. Indexes for this industry and a brief note explaining the derivation of the indexes follows:

Output per man-hour in the basic steel industry

Output per man-hour[4] of all employees in the steel industry increased by 25 percent during the postwar period, 1947–60 (table 1–A). Over this 13-year period, output increased 17 percent and total man-hours declined about 7 percent.

Year-to-year changes in output per employee man-hour varied considerably during the period, ranging from an increase of 14 percent to a decline of 5 percent. In general, the larger gains tended to occur in years during which there was a considerable expansion in output such as 1955 or 1959, while decreases in output per man-hour occurred, in general, when output declined or improved only slightly, as in 1960.

The increase since 1947 in output per all employee man-hour was less than the 36-percent gain in output per production worker man-hour. The difference reflected primarily the change which has been occurring in the composition of the work force in the steel industry. While production worker employment declined by 12 percent from 1947 to 1960, total employment decreased only 5 percent. The differences arose from the increasing numerical importance of nonproduction workers.

Nonproduction workers.—The number of nonproduction workers increased by more than 46 percent in the postwar period. They rose in relative importance, from 12 percent of total employment in 1947 to 19 percent in 1960. This shifting composition of the labor force is reflected in the changes in labor employed relative to output. As shown in the following tabulation, nonproduction worker man-hours per unit of output have increased about 25 percent, production worker man-hours per unit of output have declined about 30 percent.

Indexes, 1947=100]

Year	Nonproduction workers			Year	Nonproduction workers		
	Employment	Output per man-hour	Man-hours per unit of output		Employment	Output per man-hour	Man-hours per unit of output
1947	100.0	100.0	100.0	1954	119.6	89.2	112.1
1948	104.8	100.6	99.4	1955	122.9	114.6	87.2
1949	102.1	90.9	110.0	1956	132.3	104.9	95.3
1950	107.8	109.2	91.6	1957	143.3	93.1	107.4
1951	114.4	111.9	89.4	1958	135.5	75.4	132.6
1952	115.1	98.2	101.9	1959	143.0	80.9	123.6
1953	127.5	104.3	95.9	1960 [1]	146.6	80.5	124.3

[1] Preliminary.

These indexes for nonproduction workers are based on aggregate man-hours derived from employment data regularly collected by the Bureau of Labor Statistics and from an estimate of average weekly hours. The estimate of average weekly hours may be subject to some margin of error. Reasonable alternative estimates which might be computed could alter the results for this group somewhat for the period as a whole, and by a few points for any single year.

Weekly hours per nonproduction worker were estimated from data on scheduled hours (hours in the standard workweek) for office and other nonproduction workers, available from various studies of the U.S. Department of Labor.

[4] Hours refer to plant hours plus hours of company paid vacations, holidays, and sick leave.

The most recent and complete estimate of nonproduction worker scheduled weekly hours in the steel industry was derived from unpublished data from the recent survey conducted by the BLS on employer expenditures for selected supplementary remuneration practices. In this survey, respondents furnished, among other facts, data on the hours in the standard workweek in 1959. For the steel industry, the overall estimate for nonproduction workers was 40.1 hours per week. This estimate served as a benchmark of average weekly hours.

The trend of nonproduction worker hours was based on data from the Bureau's annual community wage surveys, which covered schedule hours of office-workers for the all-manufacturing category in various cities for the period 1949–59. The derived trend was considered to be indicative of the movement for the steel industry. The pattern of movement was characterized by a slight decline in hours from 1947 through 1954—estimated at 0.05 weekly hours per year—and a generally stable level thereafter.

This estimate of nonproduction worker weekly hours was derived primarily for the purpose of preparing indexes of the aggregate hours for all employees. The latter, as used in this report, are based on three components: (1) Published data on employment, (2) published data on production worker man-hours,[5] and (3) the derived nonproduction worker weekly hours. Errors, or differences which might occur in using reasonable alternative estimates of the latter (which is a relatively small component) would have very little effect on the estimate of all employee aggregate man-hours.

TABLE 1–A.—*Basic steel:*[1] *Output, man-hours, and output per man-hour, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Employment		Man-hours		Output per—			
		All employees	Production workers	All employee	Production worker	Employee	Production worker	All employee man-hour	Production worker man-hour
1939	58.6	80.1	81.7	(2)	73.9	73.2	71.7	(2)	79.3
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	105.3	103.7	103.5	104.8	104.9	101.5	101.7	100.5	100.4
1949	92.6	93.0	91.8	91.6	90.1	99.6	100.9	101.1	102.8
1950	117.3	103.1	102.4	105.1	104.8	113.8	114.6	111.6	111.9
1951	127.4	108.3	107.5	112.8	112.7	117.6	118.5	112.9	113.0
1952	112.3	95.9	93.2	97.9	95.5	117.1	120.5	114.7	117.6
1953	132.0	109.5	107.0	113.0	111.1	120.5	123.4	116.8	118.8
1954	105.8	97.1	94.0	94.8	91.3	109.0	112.6	111.6	115.9
1955	139.6	106.2	103.9	109.7	107.9	131.5	134.4	127.3	129.4
1956	137.5	105.4	101.6	108.8	105.5	130.5	135.3	126.4	130.3
1957	132.3	107.5	102.5	107.7	102.7	123.1	129.1	122.8	128.8
1958	101.3	89.8	83.3	87.0	80.1	112.8	121.6	116.4	126.5
1959	114.7	87.3	79.5	88.6	80.9	131.4	144.3	129.5	141.8
1960 [3]	117.0	95.2	88.0	93.3	85.8	122.9	133.0	125.4	136.4

[1] Covers blast furnaces, steel works, and rolling mills.
[2] Not available.
[3] Preliminary.

[5] These data are regularly collected by the Bureau of Labor Statistics and published monthly in Employment and Earnings. The employment data are brought into agreement with benchmarks derived from the various census of manufactures.

TABLE 1–B.—*Basic steel:*[1] *Unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Per unit of output			
	Employees	Production workers	All employee man-hours	Production worker man-hours
1939	136.7	139.4	(2)	126.1
1947	100.0	100.0	100.0	100.0
1948	98.5	98.3	99.5	99.6
1949	100.4	99.1	98.9	97.3
1950	87.9	87.3	89.6	89.3
1951	85.0	84.4	88.5	88.5
1952	85.4	83.0	87.2	85.0
1953	83.0	81.1	85.6	84.2
1954	91.8	88.8	89.6	86.3
1955	76.1	74.4	78.6	77.3
1956	76.7	73.9	79.1	76.7
1957	81.3	77.5	81.4	77.6
1958	88.6	82.2	85.9	79.1
1959	76.1	69.3	77.2	70.5
1960 [3]	81.4	75.2	79.7	73.3

[1] Covers blast furnaces, steelworks, and rolling mills.
[2] Not available.
[3] Preliminary.

TABLE 2.—*Anthracite mining:*[1] *Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	91.0	112.0	112.1	82.3	81.2	81.2	110.6	123.1	123.2	90.4
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	100.0	100.8	101.6	98.1	99.2	98.4	101.9	100.8	101.6	98.1
1949	74.7	97.4	97.5	73.1	76.7	76.6	102.2	130.4	130.5	97.9
1950	76.8	94.6	94.6	80.6	81.2	81.2	95.4	123.2	123.2	104.9
1951	72.7	87.1	87.1	70.0	83.5	83.5	104.0	119.8	119.8	96.3
1952	69.1	79.9	79.8	66.6	86.5	86.6	103.7	115.6	115.5	96.4
1953	52.7	68.0	67.4	50.5	77.5	78.2	104.4	129.0	127.9	95.8
1954	49.6	50.5	48.0	39.1	98.2	103.3	127.2	101.8	96.8	78.8
1955	44.7	39.5	37.9	33.6	113.2	117.9	132.9	88.4	84.8	75.2
1956	49.3	36.9	35.9	31.3	133.6	137.3	157.5	74.8	72.8	63.5
1957	43.2	35.8	35.4	29.2	120.7	122.0	148.0	82.9	81.9	67.6
1958	36.1	25.5	24.8	19.0	141.6	145.6	190.1	70.6	68.7	52.6
1959	35.2	20.6	19.5	16.0	170.9	180.5	219.8	58.5	55.4	45.5
1960 [2]	32.1	15.7	14.7	12.6	204.5	218.4	255.1	48.9	45.8	39.3

[1] Represents Pennsylvania anthracite only.
[2] Preliminary.

Sources: Output based on data from the Bureau of Mines, U.S. Department of the Interior. Employment and hours based on data from the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 3.—*Bituminous coal and lignite mining: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Employment: All employees	Employment: Production workers	Production worker man-hours	Output per—: Employee	Output per—: Production worker	Output per—: Production worker man-hour	Labor requirements per unit: Employees	Labor requirements per unit: Production workers	Labor requirements per unit: Production worker man-hours
1939	62.6	91.2	92.4	70.2	68.6	67.7	89.1	145.7	147.6	112.1
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	95.0	102.5	102.2	94.9	92.7	93.0	100.0	107.9	107.6	99.9
1949	69.3	92.4	91.5	66.4	75.0	75.7	104.4	133.3	132.0	95.8
1950	81.9	86.4	85.4	71.5	94.8	95.9	114.5	105.5	104.3	87.3
1951	84.6	87.4	86.5	74.3	96.8	97.8	113.8	103.3	102.2	87.8
1952	73.9	77.1	75.6	61.5	95.8	97.8	120.1	104.3	102.3	83.2
1953	72.4	67.9	66.5	56.1	106.6	108.9	129.0	93.8	91.9	77.5
1954	62.0	53.7	52.0	41.6	115.5	119.2	149.2	86.6	83.9	67.1
1955	73.6	51.4	49.8	46.0	143.2	147.8	159.9	69.8	67.7	62.5
1956	79.3	53.7	52.0	48.3	147.7	154.5	164.3	67.7	65.6	60.9
1957	78.0	54.1	51.9	46.7	144.2	150.3	166.9	69.4	66.5	59.9
1958	64.9	45.9	43.2	36.2	141.4	150.2	179.2	70.7	66.6	55.8
1959	65.2	39.5	37.1	33.7	165.1	175.7	193.3	60.6	56.9	51.7
1960 [1]	65.8	37.4	34.6	30.7	175.9	190.2	214.0	56.8	52.6	46.7

[1] Preliminary.

Sources: Output based on data from the Bureau of Mines, U.S. Department of the Interior. Employment and hours based on data from the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 4–A.—*Copper mining, crude ore: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output [1]	Employment: All employees	Employment: Production workers	Production worker man-hours	Output per—: Employee	Output per—: Production worker	Output per—: Production worker man-hour	Labor requirements per unit: Employees	Labor requirements per unit: Production workers	Labor requirements per unit: Production worker man-hours
1939	62.9	(2)	101.6	95.0	(2)	61.9	66.3	(2)	161.5	151.0
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	96.4	99.3	100.0	100.9	97.1	96.4	95.6	103.0	103.7	104.7
1949	86.6	94.2	93.9	88.7	91.9	92.2	97.7	108.8	108.4	102.4
1950	107.6	93.8	92.7	93.1	114.7	116.1	115.7	87.2	86.2	86.5
1951	108.7	94.2	91.9	94.5	115.4	118.3	115.1	86.7	84.5	86.9
1952	113.8	96.4	93.0	94.7	118.0	122.4	120.1	84.7	81.7	83.2
1953	115.0	104.0	99.6	101.8	110.6	115.5	112.9	90.4	86.6	88.5
1954	106.6	101.5	96.8	91.8	105.0	110.1	116.1	95.2	90.8	86.1
1955	128.1	105.1	99.1	97.6	121.9	129.3	131.3	82.0	77.4	76.2
1956	150.0	121.1	115.0	111.9	123.9	130.4	134.1	80.7	76.7	74.6
1957	147.6	118.6	111.0	101.4	124.5	133.0	145.7	80.4	75.2	68.7
1958	130.8	104.0	95.1	83.0	125.8	137.5	157.6	79.5	72.7	63.5
1959	118.0	81.1	73.2	69.1	145.5	161.2	170.8	68.7	62.0	58.6
1960 [3]	153.7	107.6	97.6	94.3	142.8	157.5	163.0	70.0	63.5	61.4

[1] Represents output in terms of copper ore (including old tailings) sold or treated.
[2] Not available.
[3] Preliminary.

Sources: Output based on data from the Bureau of Mines, U.S. Department of the Interior. Employment and hours based on data from the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 4–B.—*Copper mining, recoverable metal: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output [1]	Employment: All employees	Employment: Production workers	Production worker man-hours	Output per—: Employee	Output per—: Production worker	Output per—: Production worker man-hour	Labor requirements per unit: Employees	Labor requirements per unit: Production workers	Labor requirements per unit: Production worker man-hours
1939	85.7	(2)	101.6	95.0	(2)	84.4	90.2	(2)	118.6	110.9
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	98.3	99.3	100.0	100.9	99.0	98.3	97.4	101.0	101.7	102.6
1949	87.7	94.2	93.9	88.7	93.1	93.4	98.8	107.4	107.1	101.1
1950	106.4	93.8	92.7	93.1	113.4	114.8	114.3	88.2	87.1	87.5
1951	108.3	94.2	91.9	94.5	115.0	117.8	114.5	87.0	84.9	87.3
1952	108.3	96.4	93.0	94.7	112.3	116.5	114.3	89.0	85.9	87.4
1953	108.8	104.0	99.6	101.8	104.6	109.2	106.8	95.6	91.5	93.6
1954	98.0	101.5	96.8	91.8	96.6	101.2	106.7	103.6	98.8	93.7
1955	117.5	105.1	99.1	97.6	111.8	118.6	120.4	89.4	84.3	83.1
1956	129.9	121.1	115.0	111.9	107.3	113.0	116.1	93.2	88.5	86.1
1957	127.5	118.6	111.0	101.4	107.5	114.9	125.7	93.0	87.1	79.5
1958	115.3	104.0	95.1	73.0	110.9	121.2	138.8	90.2	82.5	72.0
1959	96.9	81.1	73.2	69.1	119.5	132.4	140.1	83.7	75.5	71.3
1960 [3]	127.1	107.6	97.6	94.3	118.1	130.2	134.6	84.7	76.8	74.2

[1] Represents output in terms of copper recovered from copper ore, old tailings, and precipitates.
[2] Not available.
[3] Preliminary.

Sources: Output based on data from the Bureau of Mines, U.S. Department of the Interior. Employment and hours based on data from the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 5–A.—*Iron mining, crude ore: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Employment: All employees	Employment: Production workers	Production worker man-hours	Output per—: Employee	Output per—: Production worker	Output per—: Production worker man-hour	Labor requirements per unit: Employees	Labor requirements per unit: Production workers	Labor requirements per unit: Production worker man-hours
1939	50.4	(1)	66.7	59.3	(1)	75.6	84.9	(1)	132.3	117.7
1947	100.0	100.0	100 0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	110.7	106.7	106.2	109.2	103.7	104.2	101.4	96.4	95.9	98.6
1949	92.0	98.2	96.2	95.0	93.7	95.6	96.8	106.7	104.6	103.3
1950	110.3	103.5	100.9	102.7	106.6	109.3	107.4	93.8	91.5	93.1
1951	133.4	109.9	107.0	113.1	121.4	124.7	118.0	82.4	80.2	84.8
1952	112.5	97.7	92.6	101.2	115.1	121.5	111.1	86.8	82.3	90.0
1953	137.4	116.9	112.0	118.2	117.5	122.7	116.3	85.1	81.5	86.0
1954	95.9	102.5	96.5	90.8	93.6	99.4	105.6	106.9	100.6	94.7
1955	124.8	99.7	94.0	94.0	125.2	132.8	132.7	79.9	75.3	75.3
1956	128.2	102.3	96.2	95.2	125.3	133.3	134.6	79.8	75.0	74.3
1957	141.1	113.4	107.3	105.5	124.4	131.5	133.7	80.4	76.0	74.8
1958	96.4	89.7	82.6	74.3	107.5	116.7	129.7	93.0	85.7	77.1
1959	90.0	79.3	71.8	66.8	113.5	125.3	134.7	88.1	79.8	74.2
1960 [2]	135.9	96.1	89.5	89.1	141.4	151.8	152.4	70.7	65.9	65.6

[1] Not available.
[2] Preliminary.

Sources: Output based on data from the Bureau of Mines, U.S. Department of the Interior. Employment and hours based on data from the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 5-B.—*Iron mining, usable ore: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Employment: All employees	Employment: Production workers	Production worker man-hours	Output per—: Employee	Output per—: Production worker	Output per—: Production worker man-hour	Labor requirements per unit: Employees	Labor requirements per unit: Production workers	Labor requirements per unit: Production worker man-hours
1939	55.8	(1)	66.7	59.3	(1)	83.7	94.2	(1)	119.5	106.3
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	108.6	106.7	106.2	109.2	101.8	102.3	99.4	98.3	97.8	100.6
1949	91.1	98.2	96.2	95.0	92.8	94.7	95.9	107.8	105.6	104.3
1950	105.3	103.5	100.9	102.7	101.7	104.4	102.5	98.3	95.8	97.5
1951	125.2	109.9	107.0	113.1	113.9	117.0	110.7	87.8	85.5	90.3
1952	105.1	97.7	92.6	101.2	107.6	113.5	103.8	93.0	88.1	96.3
1953	126.8	116.9	112.0	118.2	108.5	113.2	107.3	92.2	88.3	93.2
1954	83.5	102.5	96.5	90.8	81.5	86.5	92.0	122.8	115.6	108.7
1955	110.1	99.7	94.0	94.0	110.4	117.1	117.1	90.6	85.4	85.4
1956	104.6	102.3	96.2	95.2	102.2	108.7	109.9	97.8	92.0	91.0
1957	113.8	113.4	107.3	105.5	100.4	106.1	107.9	99.6	94.3	92.7
1958	72.3	89.7	82.6	74.3	80.6	87.5	97.3	124.1	114.2	102.8
1959	64.2	79.3	71.8	66.8	81.0	89.4	96.2	123.5	111.8	104.0
1960 [2]	95.0	96.1	89.5	89.1	98.9	106.1	106.6	101.2	94.2	93.8

[1] Not available.
[2] Preliminary.

Sources: Output based on data from the Bureau of Mines, U.S. Department of the Interior. Employment and hours based on data from the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 6-A.—*Railroad transportation,[1] total revenue traffic: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Employment: All employees	Employment: Production workers [2]	Production worker man-hours [3]	Output per—: Employee	Output per—: Production worker [2]	Output per—: Production worker man-hour [3]	Labor requirements per unit: Employees	Labor requirements per unit: Production workers [2]	Labor requirements per unit: Production worker man-hours [3]
1939	50.8	72.8	71.9	68.3	69.8	70.7	74.4	143.3	141.5	134.4
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	96.5	98.3	98.2	97.9	98.2	98.3	98.5	101.9	101.8	101.5
1949	79.9	88.5	87.8	82.4	90.3	91.0	96.9	110.8	109.9	103.1
1950	87.5	90.7	90.2	79.2	96.5	97.0	110.5	103.7	103.1	90.5
1951	96.0	94.9	94.7	82.3	101.2	101.4	116.7	98.9	98.6	85.7
1952	91.6	91.4	90.9	78.1	100.2	100.8	117.3	99.8	99.2	85.3
1953	89.8	90.0	89.4	76.1	99.8	100.4	118.0	100.2	99.6	84.7
1954	81.6	79.5	78.4	65.8	102.6	104.1	124.0	97.4	96.1	80.6
1955	91.4	79.0	78.0	66.6	115.7	117.2	137.2	86.4	85.3	72.9
1956	94.4	78.2	77.1	65.8	120.7	122.4	143.5	82.8	81.7	69.7
1957	90.0	74.2	72.9	61.5	121.3	123.5	146.4	82.4	81.0	68.3
1958	80.4	63.2	61.6	51.8	127.2	130.5	155.2	78.6	76.6	64.4
1959	83.2	61.4	59.7	50.5	135.5	139.4	164.9	73.8	71.8	60.7
1960 [4]	82.6	58.8	57.1	47.9	140.5	144.7	172.3	71.2	69.1	58.0

[1] Class I railroads and class I switching and terminal companies.
[2] Corresponds to hourly basis employees as originally classified by the Interstate Commerce Commission.
[3] Represents hours worked for all hourly basis employees plus constructive allowances for transportation (train and engine) personnel.
[4] Preliminary.

Source: Based on Interstate Commerce Commission data.

TABLE 6–B.—*Railroad transportation,*[1] *total car-miles: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1949=100]

Year	Output	Employment		Production worker man-hours[3]	Output per—			Labor requirements per unit		
		All employees	Production workers[2]		Employee	Production worker[2]	Production worker man-hour[3]	Employees	Production workers[2]	Production worker man-hours[3]
1939	68.8	72.8	71.9	68.3	94.5	95.7	100.7	105.8	104.5	99.3
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	97.8	98.3	98.2	97.9	99.5	99.6	99.9	100.5	100.4	100.1
1949	87.6	88.5	87.8	82.4	99.0	99.8	106.3	101.0	100.2	94.1
1950	92.1	90.7	90.2	79.2	101.5	102.1	116.4	98.5	97.9	86.0
1951	96.2	94.9	94.7	82.3	101.4	101.6	116.9	98.6	98.4	85.6
1952	94.4	91.4	90.9	78.1	103.3	103.9	120.9	96.8	96.3	82.7
1953	94.6	90.0	89.4	76.1	105.1	105.8	124.3	95.1	94.5	80.4
1954	88.4	79.5	78.4	65.8	111.2	112.8	134.4	89.9	88.7	74.4
1955	94.7	79.0	78.0	66.6	119.9	121.4	142.2	83.4	82.4	70.3
1956	95.6	78.2	77.1	65.8	122.3	124.0	145.4	81.8	80.6	68.8
1957	92.5	74.2	72.9	61.5	124.7	126.9	150.4	80.2	78.8	66.5
1958	84.5	63.2	61.6	51.8	133.7	137.2	163.2	74.8	72.9	61.3
1959	85.6	61.4	59.7	50.5	139.4	143.4	169.8	71.7	69.7	59.0
1960[4]	84.0	58.8	57.1	47.9	142.9	147.1	175.3	70.0	68.0	57.0

[1] Class I railroads and class I switching and terminal companies.
[2] Corresponds to hourly basis employees as originally classified by the Interstate Commerce Commission.
[3] Represents hours worked for all hourly basis employees plus constructive allowances for transportation (train and engine) personnel.
[4] Preliminary.

Source: Based on Interstate Commerce Commission data.

TABLE 7.—*Beet sugar: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	94.0	(1)	88.0	87.5	(1)	106.8	107.4	(1)	93.6	93.1
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	74.5	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1949	84.3	82.7	84.0	76.2	101.9	100.4	110.6	98.1	99.6	90.4
1950	106.6	94.2	94.5	86.5	113.2	112.8	123.2	88.4	88.6	81.1
1951	84.2	86.3	86.0	78.9	97.6	97.9	106.7	102.5	102.1	93.7
1952	80.7	78.8	75.9	70.7	102.4	106.3	114.1	97.6	94.1	87.6
1953	97.3	83.6	82.7	79.6	116.4	117.7	122.2	85.9	85.0	81.8
1954	105.9	82.2	81.1	76.8	128.8	130.6	137.9	77.6	76.6	72.5
1955	96.7	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1956	110.3	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1957	123.1	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1958	129.7	77.0	77.7	80.8	168.4	166.9	160.5	59.4	59.9	62.3
1959[2]	135.9	78.6	79.5	80.0	172.9	170.9	169.9	57.8	58.5	58.9

[1] Not available.
[2] Preliminary.

Sources: Output based on data from the Commodity Stabilization Service, U.S. Department of Agriculture; and the Bureau of the Census, U.S. Department of Commerce. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 8.—*Canning, preserving, and freezing: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Employment: All employees	Employment: Production workers	Production worker man-hours	Output per—: Employee	Output per—: Production worker	Output per—: Production worker man-hour	Labor requirements per unit: Employees	Labor requirements per unit: Production workers	Labor requirements per unit: Production worker man-hours
1939	62.6	(1)	74.6	69.5	(1)	83.9	90.0	(1)	119.2	111.0
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	98.9	100.4	99.6	95.8	98.5	99.3	103.2	101.5	100.7	96.9
1949	102.2	95.3	93.8	91.7	107.2	109.0	111.5	93.2	91.8	89.7
1950	109.3	94.9	93.3	92.4	115.2	117.1	118.3	86.8	85.4	84.5
1951	124.0	98.2	96.9	97.6	126.3	128.0	127.0	79.2	78.1	78.7
1952	119.2	95.8	93.9	93.0	124.4	126.9	128.2	80.4	78.8	78.0
1953	125.1	100.3	98.2	96.8	124.7	127.4	129.2	80.2	78.5	77.4
1954	126.4	94.7	92.6	90.3	133.5	136.5	140.0	74.9	73.3	71.4
1955	131.9	95.7	93.2	90.8	137.8	141.5	145.3	72.6	70.7	68.8
1956	147.5	98.2	95.6	95.2	150.2	154.3	154.9	66.6	64.8	64.5
1957	141.3	93.0	89.1	87.5	151.9	158.6	161.5	65.8	63.1	61.9
1958	139.2	92.8	88.6	88.3	150.0	157.1	157.6	66.7	63.6	63.4
1959	148.2	93.9	89.8	88.4	157.8	165.0	167.6	63.4	60.6	59.6
1960 [2]	120.5	95.8	91.5	89.6	125.8	131.7	134.5	79.5	75.9	74.4

[1] Not available.
[2] Preliminary.

Sources: Output based on data from National Canners Association; National Association of Frozen Food Packers; Western Canner and Packer; U.S. Department of the Interior; U.S. Department of Agriculture; U.S. Department of Commerce. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 9.—*Hydraulic cement: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Output	Production worker [1]	Production worker man-hours	Output per—: Production worker [1]	Output per—: Production worker man-hours	Labor requirements per unit: Production worker [1]	Labor requirements per unit: Production worker man-hours
1939	65.9	79.7	73.5	82.7	89.7	120.9	111.5
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	110.2	104.3	104.3	105.7	105.7	94.6	94.6
1949	112.1	105.9	103.9	105.9	107.9	94.5	92.7
1950	120.9	105.6	104.2	114.5	116.0	87.3	86.2
1951	130.5	107.6	106.5	121.3	122.5	82.5	81.6
1952	132.7	105.1	104.9	126.3	126.5	79.2	79.1
1953	140.0	107.0	107.1	130.8	130.7	76.4	76.5
1954	144.6	100.0	100.4	144.6	144.0	69.2	69.4
1955	159.1	105.0	105.6	151.5	150.7	66.0	66.4
1956	168.5	103.4	104.0	163.0	162.0	61.4	61.7
1957	158.7	104.2	104.5	152.3	151.9	65.7	65.8
1958	164.3	99.8	100.2	164.6	164.0	60.7	61.0
1959 [2]	179.3	100.3	100.7	178.8	178.1	55.9	56.2

[1] Represents man-days worked
[2] Preliminary

Source: Based on data from the Bureau of Mines, U.S. Department of the Interior.

TABLE 10.—*Clay construction products:*[1] *Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–58*

[Indexes, 1947=100]

Year	Output	Employment: All employees	Employment: Production workers	Production worker man-hours	Output per—: Employee	Output per—: Production worker	Output per—: Production worker man-hour	Labor requirements per unit: Employees	Labor requirements per unit: Production workers	Labor requirements per unit: Production worker man-hours
1939	89.7	103.3	100.5	95.1	86.8	89.3	94.3	115.2	112.0	106.0
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
1949	109.1	107.8	103.7	99.6	101.2	105.2	109.5	98.8	95.1	91.3
1950	123.6	114.0	112.7	107.5	108.4	109.7	115.0	92.2	91.2	87.0
1951	132.1	116.6	116.7	114.8	113.3	113.2	115.1	88.3	88.3	86.9
1952	120.1	111.6	110.8	106.8	107.6	108.4	112.5	92.9	92.3	88.9
1953	122.2	105.5	102.7	100.2	115.8	119.0	122.0	86.3	84.0	82.0
1954	128.2	108.6	106.0	103.8	118.0	120.9	123.5	84.7	82.7	81.0
1955	149.5	112.7	110.3	110.1	132.7	135.5	135.8	75.4	73.8	73.6
1956	152.8	116.7	114.5	110.1	130.9	133.4	138.8	76.4	74.9	72.1
1957	126.6	107.2	104.2	96.8	118.1	121.5	130.8	84.7	82.3	76.5
1958 [3]	123.6	108.5	104.8	96.8	113.9	117.9	127.7	87.8	84.8	78.3

[1] Includes brick and hollow tile, and sewer pipe industries.
[2] Not available.
[3] Preliminary.

Source: Based on data from the Bureau of the Census, U.S. Department of Commerce.

TABLE 11.—*Coke industries group: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Production worker [1]	Production worker man-hours	Output per—: Production worker [1]	Output per—: Production worker man-hour	Labor requirements per unit: Production workers [1]	Labor requirements per unit: Production worker man-hours
1939	61.5	66.9	66.2	91.9	92.9	108.8	107.6
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	101.8	106.1	105.9	95.9	96.1	104.2	104.0
1949	86.5	94.8	94.4	91.2	91.6	109.6	109.1
1950	98.8	100.0	99.6	98.8	99.2	101.2	100.8
1951	107.4	106.5	106.2	100.8	101.1	99.2	98.9
1952	92.2	95.7	95.0	96.3	97.1	103.8	103.0
1953	107.2	97.5	97.8	109.9	109.6	91.0	91.2
1954	79.7	79.2	79.4	100.6	100.4	99.4	99.6
1955	101.7	87.8	88.0	115.8	115.6	86.3	86.5
1956	101.6	85.4	85.5	119.0	118.8	84.1	84.2
1957	103.5	86.7	86.7	119.4	119.4	83.8	83.8
1958	73.7	68.5	68.8	107.6	107.1	92.9	93.4
1959	76.2	65.9	66.0	115.6	115.5	86.5	86.6
1960 [2]	78.8	69.6	69.7	113.2	113.1	88.3	88.5

[1] Represents man-days worked.
[2] Preliminary.

Source: Based on data from the Bureau of Mines, U.S. Department of the Interior.

TABLE 12.—*Confectionery: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	65.5	(1)	76.7	73.2	(1)	85.4	89.4	(1)	117.1	111.8
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	100.0	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1949	96.3	101.3	97.0	96.4	95.1	99.3	99.9	105.2	100.7	100.1
1950	99.8	107.9	99.2	97.7	92.5	100.6	102.1	108.1	99.4	97.9
1951	96.9	89.1	84.7	85.2	108.8	114.4	113.7	92.0	87.4	87.9
1952	99.9	92.1	85.9	87.7	108.5	116.3	113.9	92.2	86.0	87.8
1953	100.3	90.3	87.4	85.6	111.1	114.8	117.2	90.0	87.1	85.3
1954	97.8	88.9	85.1	82.6	110.0	114.9	118.4	90.9	87.0	84.5
1955	102.4	90.6	84.6	81.6	113.0	121.0	125.5	88.5	82.6	79.7
1956	105.8	91.7	84.1	82.1	115.4	125.8	128.9	86.7	79.5	77.6
1957	110.2	89.0	82.1	79.0	123.8	134.2	139.5	80.8	74.5	71.7
1958	113.3	88.3	83.6	80.1	128.3	135.5	141.4	77.9	73.8	70.7
1959 [2]	115.3	85.9	80.5	79.2	134.2	143.2	145.6	74.5	69.8	68.7

[1] Not available.
[2] Preliminary.

Sources: Output based on data from the Business and Defense Services Administration and the Bureau of the Census, U.S. Department of Commerce. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 13.—*Flour and other grain-mill products: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	74.6	(1)	79.0	68.2	(1)	94.4	109.5	(1)	105.9	91.4
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	91.3	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1949	77.8	90.5	89.3	82.0	86.0	87.1	94.9	116.3	114.8	105.4
1950	75.1	87.2	85.8	76.8	86.1	87.5	97.8	116.1	114.2	102.3
1951	76.9	87.9	86.4	79.6	87.5	89.0	96.6	114.3	112.4	103.5
1952	76.7	87.8	85.0	80.3	87.4	90.2	95.5	114.5	110.8	104.7
1953	74.4	79.1	77.8	73.4	94.1	95.6	101.4	106.3	104.6	98.7
1954	74.4	73.2	69.6	64.2	101.6	106.9	115.9	98.4	93.5	86.3
1955	76.4	72.8	68.7	62.7	104.9	111.2	121.9	95.3	89.9	82.1
1956	77.7	70.7	67.0	60.8	109.9	116.0	127.8	91.0	86.2	78.2
1957	81.6	68.4	64.7	58.7	119.3	126.1	139.0	83.8	79.3	71.9
1958	85.1	71.3	66.6	59.1	119.4	127.8	144.0	83.8	78.3	69.4
1959 [2]	85.7	72.0	67.5	62.3	119.0	127.0	137.6	84.0	78.8	72.7

[1] Not available.
[2] Preliminary.

Source: Output based on data from the Bureau of the Census, U.S. Department of Commerce. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 14.—*Glass containers: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	43.4	62.3	61.4	56.2	69.7	70.7	77.2	143.5	141.5	129.5
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	84.3	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1949	76.6	85.5	86.4	84.7	89.6	88.7	90.4	111.6	112.8	110.6
1950	88.8	89.7	91.2	88.6	99.0	97.4	100.2	101.0	102.7	99.8
1951	96.6	102.2	103.8	99.9	94.5	93.1	96.7	105.8	107.5	103.4
1952	94.7	100.9	102.4	99.0	93.9	92.5	95.7	106.5	108.1	104.5
1953	105.0	107.4	108.0	102.7	97.8	97.2	102.2	102.3	102.9	97.8
1954	101.6	104.8	105.1	100.2	96.9	96.7	101.4	103.1	103.4	98.6
1955	110.7	108.5	109.1	105.3	102.0	101.5	105.1	98.0	98.6	95.1
1956	113.5	109.8	110.3	107.6	103.4	102.9	105.5	96.7	97.2	94.8
1957	117.1	115.1	115.5	111.3	101.7	101.4	105.2	98.3	98.6	95.0
1958	114.4	116.6	116.0	111.5	98.1	98.6	102.6	101.9	101.4	97.5
1959 [2]	122.4	119.3	119.5	112.9	102.6	102.4	108.4	97.5	97.6	92.2

[1] Not available.
[2] Preliminary.

Source: Based on data from the Bureau of the Census, U.S. Department of Commerce.

TABLE 15–A.—*Hosiery, total: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	104.7	(1)	125.8	120.3	(1)	83.2	87.0	(1)	120.2	114.9
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1949	103.2	97.9	96.0	93.6	105.4	107.5	110.3	94.9	93.0	90.7
1950	115.7	103.2	102.3	100.3	112.1	113.1	115.4	89.2	88.4	86.7
1951	112.9	98.8	96.4	91.9	114.3	117.1	112.9	87.5	85.4	81.4
1952	118.9	94.3	91.5	89.8	126.1	129.9	132.4	79.3	77.0	75.5
1953	116.7	97.5	95.4	92.2	119.7	122.3	126.6	83.5	81.7	79.0
1954	112.4	91.5	90.6	86.5	122.8	124.1	129.9	81.4	80.6	77.0
1955	111.8	93.8	92.5	88.7	119.2	120.9	126.0	83.9	82.7	79.3
1956	106.5	90.0	88.7	84.8	118.3	120.1	125.6	84.5	83.3	79.6
1957	104.1	86.2	84.6	80.7	120.8	123.0	129.0	82.8	81.3	77.5
1958	106.1	76.5	74.7	70.3	138.7	142.0	150.9	72.1	70.4	66.3
1959 [2]	109.0	78.7	77.1	74.9	138.5	141.4	145.5	72.2	70.7	68.7

[1] Not available.
[2] Preliminary.

Sources: Output based on data from the National Association of Hosiery Manufacturers; and the Bureau of the Census, U.S. Department of Commerce. Employment and hours data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 15–B.—*Hosiery, full fashioned and seamless: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Full-fashioned				Seamless			
	Output	Production worker man-hours	Output per production worker man-hour	Labor requirements per unit (production worker man-hours)	Output	Production worker man-hours	Output per production worker man-hour	Labor requirements per unit (production Worker man-hours)
1939	114.3	141.0	81.0	123.4	95.1	99.8	95.3	104.9
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	114.0	(1)	(1)	(1)	94.0	(1)	(1)	(1)
1949	114.3	100.0	114.3	87.5	93.5	87.6	106.7	93.7
1950	129.2	105.9	122.0	82.0	104.4	95.0	109.9	91.0
1951	127.1	96.8	131.3	76.2	101.2	87.2	116.1	86.2
1952	127.4	90.6	140.6	71.1	111.8	89.1	125.5	79.7
1953	123.4	90.3	136.7	73.2	111.2	94.0	118.3	84.5
1954	117.9	83.4	141.4	70.7	108.1	89.3	121.1	82.6
1955	114.8	81.5	140.9	71.0	109.4	95.4	114.7	87.2
1956	107.3	72.2	148.6	67.3	106.0	96.6	109.7	91.1
1957	93.5	61.8	151.3	66.1	111.5	98.3	113.4	88.2
1958	90.4	50.1	180.4	55.4	116.8	89.3	130.8	76.5
1959 [2]	82.1	48.9	167.9	59.6	128.5	99.3	129.4	77.3

[1] Not available.
[2] Preliminary.

Sources: Output based on data from the National Association of Hosiery Manufacturers; and the Bureau of the Census, U.S. Department of Commerce. Employment and hours data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 16.—*Malt liquors: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	56.2	(1)	74.1	65.7	(1)	75.8	85.5	(1)	131.9	116.9
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	97.3	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1949	99.0	95.4	90.9	84.2	103.8	108.9	117.6	96.4	91.8	85.1
1950	99.9	98.3	91.2	83.0	101.6	109.5	120.4	98.4	91.3	83.1
1951	103.1	99.4	93.3	85.4	103.7	110.5	120.7	96.4	90.5	82.8
1952	105.0	98.3	93.2	84.2	106.8	112.7	124.7	93.6	88.8	80.2
1953	108.5	102.8	96.7	86.9	105.5	112.2	124.9	94.7	89.1	80.1
1954	105.5	98.6	91.1	80.6	107.0	115.8	130.9	93.5	86.4	76.4
1955	108.0	97.4	91.1	80.1	110.9	118.6	134.8	90.2	84.4	74.2
1956	108.9	96.2	89.3	78.7	113.2	121.9	138.4	88.3	82.0	72.3
1957	108.5	93.8	86.8	75.4	115.7	125.0	143.9	86.5	80.0	69.5
1958	109.7	86.6	81.3	69.6	126.7	134.9	157.6	78.9	74.1	63.4
1959 [2]	113.7	85.7	81.2	69.7	132.7	140.0	163.1	75.4	71.4	61.3

[1] Not available.
[2] Preliminary.

Sources: Output based on data from the Internal Revenue Service, U.S. Department of the Treasury; the Bureau of the Census, U.S. Department of Commerce. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 17.—*Paper and pulp: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Output	Employment: All employees	Employment: Production workers	Production worker man-hours	Output per—: Employee	Output per—: Production worker	Output per—: Production worker man-hour	Labor requirements per unit: Employees	Labor requirements per unit: Production workers	Labor requirements per unit: Production worker man-hours
1939	64.4	(1)	64.7	59.0	(1)	99.5	109.2	(1)	100.5	91.6
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	104.2	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1949	96.9	96.9	95.1	90.8	100.0	101.9	106.7	100.0	98.1	93.7
1950	115.8	99.7	98.1	97.1	116.1	118.0	119.3	86.1	84.7	83.9
1951	126.2	104.4	102.0	100.7	120.9	123.7	125.3	82.7	80.8	79.8
1952	120.0	103.0	100.0	97.0	116.5	120.0	123.7	85.8	83.3	80.8
1953	128.0	109.7	106.0	103.4	116.7	120.8	123.8	85.7	82.8	80.8
1954	130.5	109.3	105.1	101.0	119.4	124.2	129.2	83.8	80.5	77.4
1955	146.4	112.2	108.1	106.4	130.5	135.4	137.6	76.6	73.8	72.7
1956	155.3	114.6	109.4	107.1	135.5	142.0	145.0	73.8	70.4	69.0
1957	151.2	114.4	108.5	103.3	132.2	139.4	146.4	75.7	71.8	68.3
1958	151.9	112.8	106.7	100.9	134.7	142.4	150.5	74.3	70.2	66.4
1959 [2]	169.0	116.0	108.9	105.8	145.7	155.2	159.7	68.6	64.4	62.6

[1] Not available.
[2] Preliminary.

Sources: Output based on data from the Bureau of the Census, U.S. Department of Commerce. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 18.—*Primary smelting and refining of copper, lead, and zinc: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Output	Employment: All employees	Employment: Production workers	Production worker man-hours	Output per—: Employee	Output per—: Production worker	Output per—: Production worker man-hour	Labor requirements per unit: Employees	Labor requirements per unit: Production workers	Labor requirements per unit: Production worker man-hours
1939	78.3	(1)	85.5	79.8	(1)	91.6	98.0	(1)	109.2	101.9
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	97.8	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1949	94.8	94.6	90.8	87.1	100.2	104.4	108.8	99.8	95.8	91.9
1950	108.3	94.9	92.0	89.2	114.1	117.7	121.4	87.6	84.9	82.4
1951	107.1	91.4	87.	86.0	117.2	122.7	124.5	85.3	81.5	80.3
1952	110.0	90.8	86.	85.7	121.1	126.7	128.4	82.5	78.9	77.9
1953	116.5	92.8	89.4	88.2	125.5	130.3	132.1	79.7	76.7	75.7
1954	109.5	92.1	86.5	79.1	118.9	126.6	138.4	84.1	79.0	72.2
1955	123.7	91.5	86.7	82.0	135.2	142.7	150.9	74.0	70.1	66.3
1956	132.3	96.7	92.4	88.4	136.8	143.2	149.7	73.1	69.8	66.8
1957	131.4	95.8	90.6	84.8	137.2	145.0	155.0	72.9	68.9	64.5
1958	113.6	85.3	78.6	72.2	133.2	144.5	157.3	75.1	69.2	63.6
1959 [2]	99.3	76.8	70.4	63.7	129.3	141.1	155.9	77.3	70.9	64.1

[1] Not available.
[2] Preliminary.

Sources: Output based on data from the Bureau of Mines, U.S. Department of the Interior; and the Bureau of the Census, U.S. Department of Commerce. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 19.—*Synthetic fibers: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–59*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	37.8	77.2	83.5	80.6	49.0	45.3	46.9	204.2	220.9	213.2
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	117.2	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
1949	109.4	93.7	91.1	95.6	116.8	120.1	114.4	85.6	83.3	87.4
1950	141.9	100.0	95.9	93.6	141.9	148.0	151.6	70.5	67.6	66.0
1951	152.2	101.4	97.1	93.8	150.1	156.7	162.3	66.6	63.8	61.6
1952	137.1	89.9	83.6	82.3	152.5	164.0	166.6	65.6	61.0	60.0
1953	151.8	100.0	92.7	89.1	151.8	163.8	170.4	65.9	61.1	58.7
1954	148.0	87.7	81.7	79.3	168.8	181.2	186.6	59.3	55.2	53.6
1955	198.5	91.4	89.7	87.9	217.2	221.3	225.8	46.0	45.2	44.3
1956	199.3	92.2	88.3	84.7	216.2	225.7	235.3	46.3	44.3	42.5
1957	230.9	93.3	87.9	85.0	247.5	262.7	271.6	40.4	38.1	36.8
1958	219.3	87.9	79.4	78.0	249.5	276.2	281.2	40.1	36.2	35.6
1959 [2]	273.7	91.4	86.2	84.8	299.5	317.5	322.8	33.4	31.5	31.0

[1] Not available.
[2] Preliminary.

Sources: Output based on data from the Textile Economics Bureau, Inc., and the Bureau of Labor Statistics, U.S. Department of Labor. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 20–A.—*Tobacco products, total:*[1] *Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	81.1	(2)	110.2	101.4	(2)	73.6	80.0	(2)	135.9	125.0
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	103.7	98.3	98.7	97.3	105.5	105.1	106.6	94.8	95.2	93.8
1949	101.8	93.5	93.6	90.1	108.9	108.8	113.0	91.8	91.9	88.5
1950	102.2	88.4	87.8	86.0	115.6	116.4	118.8	86.5	85.9	84.1
1951	106.6	87.5	87.0	86.4	121.8	122.5	123.4	82.1	81.6	81.1
1952	110.7	88.7	88.1	87.1	124.8	125.7	127.1	80.1	79.6	78.7
1953	110.3	88.7	88.0	87.2	124.4	125.3	126.5	80.4	79.8	79.1
1954	107.5	88.5	88.0	86.4	121.5	122.2	124.4	82.3	81.9	80.4
1955	108.6	87.5	87.4	87.3	124.1	124.3	124.4	80.6	80.5	80.4
1956	109.5	84.7	84.3	84.9	129.3	129.9	129.0	77.4	77.0	77.5
1957	112.7	82.8	81.6	81.9	136.1	138.1	137.6	73.5	72.4	72.7
1958	119.3	81.0	79.5	80.8	147.3	150.1	147.6	67.9	66.6	67.7
1959	124.1	79.8	78.0	79.7	155.5	159.1	155.7	64.3	62.9	64.2
1960 [3]	127.2	78.0	76.2	75.0	163.1	166.9	169.6	61.3	59.9	59.0

[1] Does not include stemming and redrying.
[2] Not available.
[3] Preliminary.

Sources: Output based on data from the Internal Revenue Service, U.S. Department of the Treasury; and the Bureau of the Census, U.S. Department of Commerce. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 20–B.—*Tobacco, cigars: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	96.0	(1)	114.3	105.2	(1)	84.0	91.3	(1)	119.1	109.6
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	103.3	97.9	98.0	97.8	105.5	105.4	105.6	94.8	94.9	94.7
1949	100.2	90.4	90.1	87.7	110.8	111.2	114.3	90.2	89.9	87.5
1950	99.7	83.8	83.2	81.4	119.0	119.8	122.5	84.1	83.5	81.6
1951	103.8	83.2	82.2	82.0	124.8	126.3	126.6	80.2	79.2	79.0
1952	108.6	83.9	83.2	82.7	129.4	130.5	131.3	77.3	76.6	76.2
1953	110.5	83.1	82.2	82.4	133.0	134.4	134.1	75.2	74.4	74.6
1954	109.0	81.8	81.0	79.1	133.3	134.6	137.8	75.0	74.3	72.6
1955	108.3	79.0	78.3	77.3	137.1	138.3	140.1	72.9	72.3	71.4
1956	107.9	72.3	71.4	71.1	149.2	151.1	151.8	67.0	66.2	65.9
1957	110.2	69.1	67.9	67.7	159.5	162.3	162.8	62.7	61.6	61.4
1958	115.8	62.4	60.8	60.9	185.6	190.5	190.1	53.9	52.5	52.6
1959	122.7	58.1	56.3	56.2	211.2	217.9	218.3	47.4	45.9	45.8
1960 (2)	125.1	54.6	52.8	52.4	229.1	236.9	238.7	43.6	42.2	41.9

1 Not available.
2 Preliminary.

Sources: Output based on data from the Internal Revenue Service, U.S. Department of the Treasury; and the Bureau of the Census, U.S. Department of Commerce. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

TABLE 20–C.—*Tobacco, cigarettes, chewing and smoking tobacco, and snuff: Output, man-hours, output per man-hour, and unit labor requirements, 1939 and 1947–60*

[Indexes, 1947=100]

Year	Output	Employment		Production worker man-hours	Output per—			Labor requirements per unit		
		All employees	Production workers		Employee	Production worker	Production worker man-hour	Employees	Production workers	Production worker man-hours
1939	67.3	(1)	104.9	96.7	(1)	64.2	69.6	(1)	155.9	143.7
1947	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1948	104.1	98.8	99.7	96.7	105.4	104.4	107.7	94.9	95.8	92.9
1949	103.6	97.4	98.0	93.1	106.4	105.7	111.3	94.0	94.6	89.9
1950	105.0	94.0	93.6	91.5	111.7	112.2	114.8	89.5	89.1	87.1
1951	109.9	92.7	93.0	91.7	118.6	118.2	119.8	84.3	84.6	83.4
1952	113.2	94.4	94.2	92.4	119.9	120.2	122.5	83.4	83.2	81.6
1953	110.1	95.5	95.2	92.9	115.3	115.7	118.5	86.7	86.5	84.4
1954	106.0	96.7	96.8	95.3	109.6	109.5	111.2	91.2	91.3	89.9
1955	108.8	97.8	98.9	99.4	111.2	110.0	109.5	89.9	90.9	91.4
1956	110.9	99.6	100.6	101.6	111.3	110.2	109.2	89.8	90.7	91.6
1957	114.8	99.5	98.9	99.0	115.4	116.1	116.0	86.7	86.1	86.2
1958	122.0	103.5	103.1	104.6	117.9	118.3	116.6	84.8	84.5	85.7
1959	125.0	106.2	105.3	107.9	117.7	118.7	115.8	85.0	84.2	86.3
1960 (2)	128.4	106.4	105.8	102.2	120.7	121.4	125.6	82.9	82.4	79.6

1 Not available.
2 Preliminary.

Sources: Output based on data from the Internal Revenue Service, U.S. Department of the Treasury and the Bureau of the Census, U.S. Department of Commerce. Employment and hours based on data from the Bureau of the Census, U.S. Department of Commerce; and the Bureau of Labor Statistics, U.S. Department of Labor.

Senator PROXMIRE. Very good.

Now you discuss the foreign trade employment situation and your proposals with regard to that. Is it not true that a major, and I think the major, but this is debatable, contribution to the trade program would be in the area of inflation and stable prices? It seems to me that if we increase our competition, getting as much of a trading area as possible between this Nation and the Common Market, it would certainly have a tendency to stabilize prices, maintain competition, prevent the increases in prices that we have had in the past.

Secretary GOLDBERG. It will be a big factor, because as our Nation more broadly participates in foreign trade, as it is developing and becoming true now, we as a nation will have to measure up to the fact that we are part of the world community and have to consider competitive factors.

Senator PROXMIRE. It seems to me that from a public standpoint, this is the biggest benefit. The other things I think are very arguable and debatable.

You may be completely right on the increasing jobs and so forth, but I think there is a good, solid, commonsense argument on the other side.

But everybody is a consumer, and to the extent that we get lower priced commodities from overseas, as a consumer, you benefit. Is that not right?

Secretary GOLDBERG. I think competition is generally good, and I think it will be good in this area.

Senator PROXMIRE. All right. Now you talk about our exports accounting for 8 percent of manufacturing employment, and so on. How much of this was because of Public Law 780, because of the foreign aid program? We had testimony the other day from the Federal Reserve advisers that of our favorable balance of trade, about three-quarters could be accounted for by our foreign aid program tie-ins. You know they are required to buy from this country.

Secretary GOLDBERG. Perhaps Dr. Clague would like to answer that.

Dr. CLAGUE. I cannot answer that offhand, because what we have done is take the total volume of exports by dollars, distributed by industry, then we have estimated the employment that would be required in the making of those particular products, regardless of the reasons for which they were sent overseas. So in that sense I cannot at the moment tell you the answer to your question.

What we have is the direct employment in the exporting industries themselves, plus the indirect employment of the raw materials, the transportation, the shipping across the ocean, and all the other types of employment connected with the exports of about $22 billion worth of American products.

Senator PROXMIRE Has there ever been a study, to your knowledge, made of the impact of the foreign aid program on American jobs?

Dr. CLAGUE. I believe there has, but I am not aware of the facts at the moment.

Secretary GOLDBERG. I do not want to venture the figure, because I may be wrong. But I recall Mr. Dillon, in figures that he presented to us in the Cabinet, having made a breakdown of this type. If you would like, I can check with him and see to it that either Treasury or the appropriate agency files that data with this committee.

(The following was later received for the record:)

A report by the Department of State, April 1959, pursuant to section 413(c) of the Mutual Security Act of 1954, as amended, entitled "The U.S. Economy and the Mutual Security Program" stated on page 3 as follows:

"Direct and indirect employment created in the United States in 1957 by the 1957 foreign aid expenditures was estimated at 530,000 people by the National Planning Association. It is estimated that approximately half a million people are presently employed in the United States producing goods and services generated by mutual security funds."

Senator PROXMIRE. We would like to have that very much. Now certainly we would agree that a great deal of the agricultural export is in connection with Public Law 480?

Secretary GOLDBERG. There is no question about that.

Senator PROXMIRE. It is very difficult for me to accept the position that we have 3 million jobs based on exports, while the impact of imports is negligible, in view of the fact that the economic indicators suggest the import of goods and services is $23 billion, and the export $27 billion.

Secretary GOLDBERG. I do not want to anticipate our study, but there are obvious reason for this. For example, many of the imports create jobs in America——

Senator PROXMIRE. I am sure they do, in a sense.

Secretary GOLDBERG (continuing). In the sense of bringing in materials on which we fabricate and produce goods. Not all imports are competitive with our goods. They create the basis for manufacturing goods.

Take, for example, even in the textile area, which is becoming the most debatable area: We bring in woolens and other goods from Australia, and we make men's suits and other products, some of which are exported. I mentioned one in steel. We bring in iron ore in great amount, which goes into our steel production, some of which goes into export.

So that I think we have to wait. We will make the same kind of analysis that we made on exports. It is not our desire to do anything but report the facts. And then, when we do that, we will demonstrate what is the fact.

Senator PROXMIRE. Because, for example, you imply in your statement that there is about $5 billion or so of imports of finished manufactured goods. I presume that much of this is the replacement of goods that could be produced here.

What budget effect will result from the passage of the bill in people put out of work, or whose investment is damaged by import? Has there been any estimate of the budget effect that this will have, how much the President will have to increase the budget to pay the 65 percent of wages and to provide the loans and tax benefits?

Secretary GOLDBERG. I believe it is in the 1963 budget. I do not have the figure at hand, but I can file it after I check it up.

Senator PROXMIRE. Well, would the 1963 budget show the full effect?

Secretary GOLDBERG. No. Of course not; because it would take effect in a period ahead.

Senator PROXMIRE. It would be very helpful to have a picture of what this would do if fully operative, say in 1964 or something.

Secretary GOLDBERG. I will have to file that with the committee, since I do not have it at hand at the moment.

(The following was later received for the record:)

The bulk of the basic cost for worker adjustments was included in the budget in the estimates for the administration's bills for unemployment insurance improvement and for manpower development and training. The costs of assistance to firms and the additional cost of worker assistance in 1963 will be several million dollars, and can readily be covered by the general allowance for contingencies in the 1963 budget. Any supplemental estimates necessary to cover the costs of the readjustment allowances of the Trade Act will be submitted after its enactment.

Yours sincerely,

ARTHUR J. GOLDBERG,
Secretary of Labor.

Senator PROXMIRE. I noticed an article in the newspaper that puzzled me a great deal and perplexed and troubled me a lot. That was that with the area redevelopment program in West Virginia there was an attempt to secure people to come in as trainees, and they had a rough time getting the full quota of people for training.

I see you shaking your head. It seems to me this contrasts with the happy problems experience.

Secretary GOLDBERG. One newspaper story can cause you more trouble when it appears.

Senator PROXMIRE. You are familiar with that story?

Secretary GOLDBERG. Yes. This is the Huntington story.

I want to state categorically that that is not a well-founded story. And if we can take a moment, Mr. Chairman, I would like for Dr. Wolfbein to tell the Huntington story in detail, so that we can put that to rest once and for all through the medium of this committee.

Dr. WOLFBEIN. Very briefly, Senator Proxmire, several community programs were approved in Huntington, especially for auto mechanics. And I want to say just a few words about that one, because the program approved involved the fact that we had many unfilled job orders in West Virginia for auto mechanics, for those who could work on power transmission, power steering, power drive.

So what we approved is a training program for people who already had the skill of auto mechanic, building on this skill, being able with 12 to 14 weeks of training to fill the jobs, which involved power transmission.

There is also a training program for nurse's aid.

The number of people who applied for training in these occupations was between double and triple the available slots for training.

The newspaper article did not mention the fact that there were about 70,000 unemployed people in the particular area at that time. Then why didn't they all come down for the training?

The answer is that this was a particular kind of training that involved, for example, auto mechanics, so that not all of these unemployed could be trained. And this poses something very, very important.

Before, as the Secretary has pointed out, we approve a training program, there has to be first a need shown for the skills that are being trained for.

Senator PROXMIRE. Well, now, was the newspaper article accurate when it said there were radio and TV ads that appealed to people to come in, and you got a small result?

Dr. WOLFBEIN. No, sir; that was inaccurate.

Senator PROXMIRE. You talk about training being given to employed people. You later say that you expect it to run from about 160,000 the first year to 380,000 the third and fourth years in training. And in view of the fact that funds are short, and there are four or four and a half million unemployed now, how can we possibly justify providing training at Federal expense for people who are now employed and have jobs?

Secretary GOLDBERG. Well, part of our problem in this area is that you have to look at the locality. You may have a situation where a person employed today, by reason of an announcement of a future plant shutdown, is going to fall out of work, and you may have a question where a new plant is there, or another plant has expanded.

Senator PROXMIRE. You do not say that in your statement.

Secretary GOLDBERG. No, I developed it in my testimony before Congress, where I pointed out we have to anticipate the training requirements of people.

Senator PROXMIRE. Good.

Then the final point—and I am happy about your migratory farm labor fight. I think this is the point of perhaps the greatest economic injustice in America, what happens to migratory farm laborers, partly because they just do not have an elected official representing them anywhere. But what concerns me especially is the fact that we still permit the importation of 300,00 to 400,000 Mexican laborers at 50 cents an hour to compete with these people.

There is nothing the administration can do now. The President signed the bill that the Congress passed in reenacting the act in the last session.

I am wondering if there is anything in the migratory labor proposals, any administration of this act, which can help allay the effect of this on migratory laborers who are already unemployed to a certain extent and actually cannot compete? This was originally an emergency bill, was it not? It was passed during wartime when we needed this labor and had a shortage of agricultural labor; is that not right?

Secretary GOLDBERG. This was originally designed to provide for a shortage. And we have developed it now into legislation which has continued from period to period.

I want to tell you this, Senator Proxmire, that as a result of what Congress said, even in renewing the bill, I will attempt in the administrative program, which I hope will be fairly administered—I have to administer it in accordance with the intent of Congress—to see to it that the employment of this labor is both temporary and seasonal, and is not to have an adverse effect upon our domestic employment. And we are engaged in a program designed to give effect to that congressional intention; not without difficulty, I may say.

Senator PROXMIRE. I am glad to hear it. But the difficulties are going to be perfectly tremendous. It is my feeling that, of course, you cannot get many self-respecting Americans to work for 50 cents an hour, or 70 cents an hour. It is tough, onerous, hard work. And we have this supply-and-demand factor taking effect. We would have plenty of people if farmers would pay $1.75 or $2. You might have to increase the price of the product to pay it.

(Secretary Goldberg's prepared statement and inclusions follow:)

STATEMENT OF ARTHUR J. GOLDBERG, SECRETARY OF LABOR, BEFORE THE JOINT ECONOMIC COMMITTEE ON THE PRESIDENT'S ECONOMIC REPORT, JANUARY 31, 1962

I am pleased to have this opportunity to meet with the Joint Economic Committee as you consider the Economic Report of the President. It gives me particular pleasure because, in my opinion, this report is one of the most significant in many years. It recognizes that the central economic problem of the United States today is to provide sufficient economic growth in 1962 and year after year thereafter so that meaningful employment will be available for all of our people who want to work.

Significantly, the report does not give the answer in one easy lesson, any more than it seeks to turn back the clock. Instead, it points out, that, while adhering to our time-proven freedoms, we must increase effective demand for our output, we must exercise restraint in our price and wage policies, and we must eliminate the roadblocks which prevent so many of our people from working to the best of their abilities.

The President, in his State of the Union Message and in his Economic Report, has given highest priority to measures designed to reduce unemployment, to alleviate its effects when it does occur, and to make sure that there are suitably trained men and women ready to fill the job openings as they become available.

I want to devote most of my discussion today to those measures which are the primary responsibility of the Department of Labor. Before doing so, however, I should like to make several general points.

An unfortunate and entirely erroneous impression has arisen among some groups who may not have read the Economic Report in full, that a 4-percent rate of unemployment is considered to be a satisfactory goal by this administration. Let me quote from page 8 of the President's Economic Report:

"We cannot afford to settle for any prescribed level of unemployment. But for working purposes we view a 4-percent unemployment rate as a temporary target * * *. The achievable rate can be lowered still further by effective policies to help the labor force acquire the skills and mobility appropriate to a changing economy * * *. Ultimately, we must reduce unemployment to the minimum compatible with the functioning of a free economy."

I want to emphasize the President's statement that "*we must reduce unemployment to the minimum compatible with the functioning of a free economy,*" and that "*We cannot afford to settle for any prescribed level of unemployment.*" [Emphasis supplied.]

I want to make it completely clear that the goal of this administration with respect to unemployment is the lowest level which can be attained "compatible with the functioning of a free economy." This formulation, to me at least, says that we don't know how low a statistical rate of unemployment we can really attain. But certainly a free and democratic society cannot be satisfied with anything less than the full employment of everyone who is ready, willing, and able to work. If a certain amount of unemployment is "necessary" to achieve price stability for flexibility, or mobility, or whatever the term is which economists use to describe the continual shifts which are taking place in our economy, then we have a responsibility to reduce the amount of time these persons must waste between jobs and to maintain their levels of living while they make the necessary adjustments. Our unemployment target must get progressively lower as we are increasingly successful in warding off recessions, in removing pockets of unemployment, in increasing the mobility of labor, in matching men and jobs, and in training and retraining for new skills.

Therefore, the unemployment rate of 4 percent which has been used in this year's Economic Report can be considered as only a temporary target for the current economic recovery period. The President has said, the Council of Economic Advisers has said—and I repeat—this is not our ultimate goal.

Our hopes for laying the groundwork in 1962 for a smoothly accelerating expansion during the years ahead are encouraged by the strength of the recovery in 1961.

I have just received the first figures on employment and unemployment for January 1962, and they confirm the continued improvement in the economy, while at the same time emphasizing the fact that our problem of hard-core unemployment is not yet diminishing.

The figures for the month just ending show a rise in unemployment of less than the usual seasonal amount, from 4,091,000 in December to 4,663,000 in January. As a result, the seasonally adjusted rate of unemployment fell to 5.8 percent, the first time it has been below the 6-percent level since September 1960. The actual total for January is nearly three-fourths of a million below the figure of a year earlier. Despite this drop over the year, however, we must emphasize the number of long-term unemployed—those who have been out of work for 15 weeks or longer—has not changed from last January's total of 1,250,000.

Total employment this month was 65.1 million—a new record for January, 600,000 better than a year earlier, despite a sharp drop in farm employment which has been declining for many decades. Nonfarm employment in January was 60.6 million, 800,000 above last January. This, too, is an alltime high for the month, nearly 10 percent above the levels of a decade earlier.

These are all the figures we now have for January, but I would like to cite a few figures for 1961 which show not only the extent of the recovery but also the extent of the remaining problems.

As the recovery gathered momentum, productivity and the workweek also increased at a strong rate. In December, the factory workweek averaged 40.5 hours, a rise of 1.3 hours from January, after taking into account the season factors. Productivity, which I will discuss later, spurted sharply. In consequence, reemployment lagged behind rising output and, with the growth in the labor force, unemployment did not drop until toward the end of the year.

Personal incomes rose to alltime highs in 1961. The average factory worker earned in December $96 a week, before taxes, the highest level in history. And, for the first time in our history, factory workers in our durable goods industries averaged during 1961 more than $100 a week before taxes.

Profits, too, made an excellent recovery in 1961. The annual rate for the fourth quarter was apparently in excess of $50 billion before taxes and $25 billion after taxes—the highest rate since the boom in the second quarter of 1959, just before the steel strike. The total for 1961, more than $46 billion before taxes, is not much below the alltime high of $46.8 billion recorded in 1959 and is $4 billion, or more than 9 percent, above the level of a decade earlier, which was the high-water mark of the Korean boom.

Prices were remarkably stable during 1961, so that increased incomes were not eaten up by increased costs. The buying power of the average factory worker with three dependents in 1961 was at a new high, about 1½ percent above a year earlier, and nearly 19 percent higher than it was 10 years ago. This is real and meaningful progress.

Wholesale prices, which have continued virtually unchanged for nearly 4 years, have been a little lower than a year earlier each month since last spring. The December index of 119.2 (1947–49=100) was three-tenths of 1 percent lower than a year earlier. Consumer prices rose by only one-half of 1 percent over the year, with small declines in November and December; this is the smallest rise in any year since 1955. The yearend index of 128.2 (1947–49=100) was five-tenths of 1 percent above a year earlier; the steadily rising costs of services was the major factor in the rise, but these costs rose at a slower pace than in any year since 1955.

I want to return later to certain details on our employment and unemployment situation, but I believe that it is clear that the stage is set for a continued favorable trend throughout 1962, in terms of employment, incomes, prices, and purchasing power.

Prices and wages

To achieve a really satisfactory level of recovery, and at the same time to lay a foundation for long-term economic growth, will require, as the report points out, action on many fronts. Most of the improvement we seek must come from the initiative and cooperation of individuals, of business, of labor—in other words, from the private economy.

It is especially important to maintain a stable general level of prices. If we can do so, our domestic gains in purchasing power will be real gains, and the competitive position of our goods and services both at home and abroad should improve. In an expanding economy, this continued stability will not come automatically or by wishful thinking. It will require thoughtful and responsible action by both management and labor.

I find considerable grounds for confidence that workers and businessmen, conferring together, will measure up to their responsibilities this year. The climate of industrial relations today is much better than it was in 1959. Our Nation learned some costly lessons from the last steel strike, in addition our people are becoming increasingly aware of the many challenges that come to us from abroad. Furthermore, this administration has taken positive steps to improve labor-management relations and these steps are beginning to show results, which cannot, of course, be quantified, but which nevertheless will begin to be manifest in a more understanding atmosphere around countless bargaining tables.

The goals of the administration imply the abandonment of restrictive and protectionist policies that retard the economy and impair efficiency, the exercise of statesmanship in meeting the social consequences of change, and the formulating of wage and price policies which permit productivity gains to be shared by workers, by owners, and by an ever-increasing number of customers.

We are trying to encourage these attitudes within the framework of collective bargaining, because we believe that collective bargaining is essential to a free society. I know full well, of course, that these goals and these responsibilities are not easy ones and will not all be met in 1962. But our leaders in business and labor are becoming increasingly determined that collective bargaining is a give-and-take process which must continue to work, that it must work without controls, and that it is their responsibility to exercise their freedoms and to use their strengths for the long-range good of the country.

Responsible decisions on wages and prices and job security are important to help establish the necessary economic climate for an increase in job opportunities. The Government's contribution to these decisions consists, in addition to the steps we have already taken, of defining the national goal, of improving good-offices procedures, of providing better and more pointed economic data, and finally of having the courage to clearly assert the national interest so that the country as a whole can derive the full benefit of our advancing technology.

Foreign trade and employment

As I said earlier, our cost and price levels are of key importance in improving our position in international trade and in reducing the deficit in our balance of payments. In this, labor has a big stake, not only because of its importance to our general domestic economic policy, but because of the need to widen our markets in order to expand employment at home. In 1960, our exports created jobs for more than 3 million workers—about 13 percent of total farm employment and 8 percent of manufacturing employment.

This 3 million includes those who produce the final products we export such as aircraft and chemicals, those who produce the materials like steel and textiles included in the exported products, and those who generate the power, supply the transportation, and undertake all the other functions necessary to the production of goods.

I am not taking any account of the innumerable additional jobs generated by the consumer needs of these 3 million workers and their families.

Let me at this stage say that it is a serious mistake to generalize that our high wages are responsible for pricing us out of world markets. Our total exports of finished manufactures in 1960 were $10.5 billion—exactly double our imports. Thus, we are certainly not being priced out of international markets. In fact, our exports are largely in those industries, such as machinery and coal mining, where our wage levels are the highest. Our high wage industries are able to succeed in foreign markets and to meet competition because they are more efficient, are better managed, and have workers with better skills—and they can improve or weaken their position as they improve or worsen their efficiency.

The importance of our foreign trade transcends any of today's figures, large though they are. The foreign market means new opportunities not only for today's workers but also for coming generations, as the world grows in education and in prosperity.

Employment and unemployment

I now want to return to what is the central economic problem of the day—the need to expand employment and reduce unemployment.

With the committee's permission, I would like to ge behind the totals for an indication of where our efforts need to be concentrated.

The achievement of our goals—a rising standard of living, a greater output of goods and services, and full employment for our working force—will not be accomplished without problems. Perhaps an examination of recent events can be profitable in this connection.

In many respects employment developments in 1961 illustrated and confirmed some of the long-term trends we have been noting in the past: rapid growth in the service-producing industries as compared with the goods-producing industries; rapid growth over the long term in white-collar and nonproduction worker employment and stability of their jobs in the face of business recessions; on the other hand, little or no growth in employment of blue-collar and production workers. Also, a point of particular importance to youngsters preparing for a work career: the less educated and less skilled worker has the greatest susceptibility to unemployment.

From the spring of 1960 until February 1961, there was a gross loss of more than 1½ million nonfarm payroll jobs. One million of these losses were in manufacturing alone, with the metal and metal-working industries accounting for more than 60 percent of this cutback. Losses in transportation, construction, mining, and trade totaled half a million. These losses were partially offset by expansion of employment in the school systems and in the finance and service industries, so that the net loss until the bottom of the recession was 1 million jobs.

Now, so far as the totals go, this recession loss of 1 million jobs had been virtually made up by the end of 1961. However, one-fourth of this gain was accounted for by employment increases in State and local governments. It is quite clear that few of these added jobs, most of them in the educational system, were filled by factory workers who had lost jobs during the recession. A strong gain also occurred in the finance and service industries, which rose, on a seasonally adjusted basis, by 200,000 between February and December 1961. However, none of the other major groups has yet reattained its early 1960 levels.

Manufacturing, at the end of 1961, was still some half a million jobs short of the early 1960 levels, taking seasonal factors into account. It is significant that the entire drop in manufacturing employment between 1960 and 1961 occurred among production workers; nonproduction worker employment was largely unchanged for the year and even showed signs of expansion at the yearend.

At the same time, other industries hard hit by the recession have not yet shown any recovery. Construction, transportation, and mining together have dropped a total of 80,000 jobs (seasonally adjusted) since recovery has been underway, in addition to their recession losses of more than 300,000.

This is a clear indication of where our unemployment problem lies, especially our long-term unemployment. The number of hard-core jobless, those who have been out of work for more than half a year, averaged 800,000 in 1961, the largest average in more than two decades.

The very long term unemployed in 1961 were concentrated in several groups out of proportion to their number in the labor force. The factors connected with their unemployment are related and overlap to a large extent, but they need to be looked at separately if we are to make headway toward a solution. Very briefly, the problem involves age, color, and skill:

(1) Men 45 years of age and over represented one-third of the very long term unemployed, even though they accounted for only one-fourth of the labor force.

(2) Workers from durable goods industries accounted for 14 percent of the labor force and 25 percent of the very long term unemployed. Construction workers accounted for 6 percent of the labor force and 9 percent of the very long term unemployed.

(3) Negroes accounted for 24 percent of persons jobless for over 6 months but only 11 percent of the civilian labor force.

(4) Semiskilled operatives and unskilled laborers represented 45 percent of the very long term unemployed compared to 24 percent of the labor force. In contrast, professional workers made up less than 3 percent of the very long term unemployed even though they account for 11 percent of the labor force.

(5) Persons with no previous work experience, who accounted for less than 1 percent of the civilian labor force, made up 9 percent of the persons looking for work for over 6 months. These were chiefly young workers in search of their first jobs.

There is one additional factor in the high level of unemployment, which I now want to discuss briefly, and that is the growth of the labor force.

In 1961 as a whole, the total labor force grew by about 1 million to an average of 74.2 million, slightly less than would be expected from projections based upon full employment assumptions. This difference between anticipation and actual results amounting to 200,000 in 1961, has been apparent since 1955. It has resulted mainly from larger declines in labor force participation among older men and teenage boys than had appeared likely. Men over 65 years have been retiring earlier than anticipated, in part because of liberalized and expanded public and private retirement programs. More teenagers are completing or extending their formal education. While these developments have resulted in a slower than expected labor force growth, there has been a partially offsetting tendency in the unexpectedly sharp increase over the past several years in the entrance into the labor market of women aged 45 and over, many of whom take part-time jobs while their children are in school.

The average rise of 1 million in the labor force between 1960 and 1961 was the result of an extremely large increase during the first half of the year and sharply decreased growth in the latter half, for reasons which we cannot yet fully explain.

Part of the explanation for the recent small growth in the civilian labor force is, of course, the recent expansion of the Armed Forces, which drew into service some 300,000 men, mostly from the civilian labor force. Another factor is an unusually large over-the-year decline in farm employment in the past two quarters, mostly among teenagers, women, and older men, many of whom were unpaid workers on the family farm who did not seek other jobs when there was no farmwork, a not unusual phenomenon. One very important factor is the acceleration of retirements among older men. Social Security Administration figures indicate almost a doubling in recent months—from about 75,000 to 140,000 a month—in the number of old age benefits granted to men aged 65 and over and women 62 and over as compared with the year before. In addition, the Social Security Administration reported some 275,000 applications for earlier retirements under the new provision of the law since July 1961.

Now, it is one thing if this slower rate of labor force growth reflects earlier retirement because of the establishment of more private pension programs and more liberal social security benefits, or the desire and ability of youngsters to put off getting jobs in order to continue their schooling. It means something else entirely if it reflects the inability of youngsters or women to find needed work, or the discouragement of older workers in their search for jobs. There is no doubt a combination of these factors at work, and we shall have to explore them further to determine their import for future policy.

Automation

As this committee knows, I established in April of last year an Office of Automation and Manpower to coordinate the work of our Department in this field and to work out a program of action and study on the impact of automation and technological change. We have worked out such a program, with the advice of a distinguished advisory committee from labor, management, Government and industrial relations, and we have submitted it to the Congress, through the regular appropriations procedures. It calls for what I think is a significant program of getting advance information in this field, of communicating it to where it counts, of stimulating programs for minimizing and even preventing the impact of automation and technological change on our workers.

One big area of action in this connection is represented by programs of training and retraining for workers displaced by the effects of technological change. I will refer to these matters a little later on. At this point, I want to say that a good part of the solution to this problem lies right in the collective bargaining field, and I am very pleased with the general attitude of both labor and management so far. In fact, I would submit that the recent statement by the President's Labor-Management Advisory Committee is a real forwardlooking document in this area. The settlements in autos and in meatpacking during 1961 represent responsible action on the part of both parties.

As the President has indicated, some of the reactions to this problem, e.g., in the sharp cut in hours in the construction industry in New York City, have many unfavorable connotations. At the same time, however, industry has to accept responsibility for making accommodations which will mitigate the effects of automation on its workers. Our philosophy can best be stated this way:

We need continued and even accelerating technological improvements for our own domestic growth and for bettering our position in the international field.

For that very reason, these improvements must be accompanied by viable public and private programs for permitting the continued employment of workers at their highest skills. All of this must take place in the context of collective-bargaining arrangements which reveal a full understanding of the productivity trends in our country and of the constraints of our cost-price situation, especially in terms of our international posture.

How important this can be is perhaps apparent from the productivity record of the past year.

As might be expected, in a period of business recovery such as experienced during 1961, substantial productivity gains are not unusual. Thus, during the last three quarters of 1961, output per man-hour in the private economy apparently rose by nearly 10 percent, which is an extremely high rate of gain. In fact, this is higher than the increase for any previous recovery period of like duration since 1947. This general picture of productivity during 1961 applied both to agriculture and to the nonfarm economy.

The low pickup in employment in the last 9 months relative to the rise in output, therefore, may be due in part to a very large gain in productivity.

Of course, we do not know whether this rapid rise in productivity will continue throughout 1962. In fact, when we compare the average gain for the year 1961 (2.8 percent) over the year 1960, the increase for the private economy is not far off from the average annual rate of gain for many years in the past. In other words, the improved productivity at the end of the year of 1961 was partly offset by the low rate in the first quarter of the year.

Let me say that I do not agree with the pessimistic conclusions of the recent report "Cybernation: The Silent Conquest," just released by the Peace Research Institute and prepared for the Center for Study of Democratic Institutions. As I have already pointed out, automation and technological change are vital to our national purpose and can result in opening up broad new vistas of better living for all our citizens. But, there must be public and private responsibility for seeing that all of these beneficient results will take place.

As we look ahead, we must set our sights to provide employment opportunities for an increasing number of people who are able and willing and who seek work. By the mid-1960's the number of young people coming of working age will increase very rapidly. Then we will need not 1 million or 1,200,000 more jobs a year to take care of our growing labor force, but closer to 1½ million: add to these the jobs which must be found to replace those in which men are displaced in the short run by machines, or new processes, or better organization—in short, by the rising productivity which is one of our national aims. It then becomes clear that we are talking in terms of several million new jobs each year after we attain a satisfactory rate of unemployment.

This is no simple task we have before us. During 1962, we shall need 5½ million net additional jobs, if we are to meet the Council's first target of a 4-percent unemployment rate. This includes the expected increase in the labor force, the expected displacement because of automation and getting part-time workers back to full-time jobs.

The new jobs must not be made work, or shared work. They must be jobs which are in the full tradition of the technology which made America great, and they must become available without inflation and without harm to our free way of life.

To say that we can do this only, or even mainly, by reducing the hours of work is to say that we do not need all the goods and services that we are capable of producing. This, to my mind, is untenable, in the light of our obvious needs. It is also a defeatist admission that our free enterprise system can develop the tools and the know-how to achieve fabulous standards of living, yet cannot develop the channels for getting the fruits of our ability into the hands of our people.

Again, to say that we can put all of our people to work in useful and satisfying activities only or mainly by upsetting our monetary system, or by massive intervention of the Government into the millions of free decisions which are the basic essence of our economic system—to say these things is to demonstrate a lack of understanding of our dynamic system. We do not advocate growth for growth's sake, nor can we advocate stability for stability's sake. We need both if, in the President's words, "the full potential of our free economy is to be released in the service of the Nation and the world."

LEGISLATIVE AND ADMINISTRATIVE PROGRAMS, ACTIONS, AND RECOMMENDATIONS

The President has recommended a whole series of measures which are an integral part of this administration's concerted effort to achieve its stated economic goals of full employment, economic growth and stability, and equity.

Several of the President's top priority items are, of course, within the direct responsibility of the Department of Labor. I have found, however, that the Department of Labor's programs are inextricably bound up with the economic welfare of the Nation, and therefore with the work of this committee. Thus some of the President's recommendations which are not the direct responsibility of the Department of Labor, are of the most urgent concern to the Department. It is obvious that any measure which contributes to the economic growth of this country, to the creation of jobs, to the solution of our unemployment problems, and to the general strengthening of our economic system are of the utmost importance to the workers of this country.

A mere listing of some of these programs will emphasize why this is so. Among the important measures recommended by the President are measures dealing with manpower retraining, youth employment, unemployment compensation, strengthening of the public employment service, standby public works authority, standby tax reduction authority, tax incentives to business, the expansion of foreign trade, aid to education, more effective protection of the funds of employee welfare and pension plans, removal of discriminatory bars in employment practices, and improvement of the conditions of migratory farm labor.

The interrelation of these measures is apparent at a glance. Together they reflect a rounded approach to greater economic growth and stability. The adoption of these recommendations would give this country a tremendous start toward solving some of its most basic and most complex problems. We know that we cannot evade these problems. We know almost certainly that delays in developing and applying solutions will only mean that the problems will increase.

The President's state of the Union and economic messages recognize the magnitude of these problems and boldly face up to their challenge.

Manpower development and training

Foremost among the measures on the President's program with which this Department is directly concerned is the manpower development and training bill. The President has emphasized time and again in various speeches and messages, as have I, how critically important the programs are which would be provided by this bill.

As the President stated in his economic message, the labor force of the United States is its most valuable productive resource. The manpower measure is designed to develop this resource more fully by improving the skills and adaptability of this Nation's workers through a continuing review and assessment of our manpower needs, both on a national and local basis, and the provision of broadly based programs for the training and retraining of workers to match their skills to needed jobs.

At this point I believe it is appropriate to take this opportunity to report to this committee and the Nation on our relevant experience in establishing training programs under the Area Redevelopment Act of 1961. This latter act provides on a very small scale for the type of training programs which would be made available by the Manpower Act to other workers throughout the Nation who are in need of training whether in a depressed area or not.

I am attaching to my testimony some of the basic information on the training and retraining programs we have approved so far.

This is my first report on our activities under this act, which became effective on October 1 of last year, and I want to begin by saying that our experience has been excellent. We now have solid proof that such programs can be conducted successfully and that some of our most intractable problems of unemployment can be dealt with in a meaningful way through the use of carefully designed training and retraining programs.

As this committee knows, redevelopment areas, after the approval of their overall economic development plans, may submit suggested training and retraining programs for their unemployed. These programs are then reviewed by our own staff, by the Department of Health, Education, and Welfare, and by the Department of Agriculture for programs involving farm occupations. Training programs may be approved up to a maximum of 16 weeks, and trainees may receive as allowances the average unemployment insurance payment which prevails in their State.

There are two key criteria for our approval of these programs. There must be evidence of job openings for the trainees, based on a survey of needs in the community; and there must be evidence that there are trainees with the capability of taking the required courses of training.

As you can see from the attached materials, we have approved 29 training programs so far; 30 different occupations are represented, and almost 4,400 trainees are involved. The programs are located in nine States and are concentrated especially in such States as Massachusetts, Pennsylvania, and West Virginia, which have a disproportionate share of depressed areas.

Let me say also at this point, that we already have in the pipelines training programs from these and additional States which are going to use up all of our available funds for these programs well before the end of this first year.

But much more important is the sum of the actual experience we have had with the trainees themselves. I want to emphasize the fact that 50 percent of all the trainees enrolled so far have been out of work for half a year or more. In fact, one-third had been continuously jobless for over a year. Significant, too, is the fact that one-third are over 35 years of age; in fact 1 in 7 is 45 years of age and over.

I am also impressed by the willingness of these unemployed to take training. Let me give you a specific example of this connection. Under the act, we may not support a program of training for more than 16 weeks. But in Providence, R.I., we approved a course of training for 20 weeks, because that was the time required for the occupations being trained for. I am very glad to report that the trainees have accepted this course of action, even though they will not be compensated for the last 4 weeks, or 20 percent of the time they will spend in training. These workers do want to be trained, they do want to get back to work as quickly as possible.

What impresses me, in other words, is that trainees of different educational backgrounds (18 percent went no further than grade school), from different areas, of different ages, of quite varied work backgrounds, are getting training which will put them back on a job. And I am delighted to see a major impact being made on the most difficult parts of the unemployed labor force—on the older worker, on the long-term jobless. It can be done.

All of this is directly relevant to the legislative program mentioned first by the President in his state of the Union message—the Manpower Development and Training Act. It demonstrates in a small way what can be done for unemployed and underemployed workers of this country under this urgently needed act. We believe the experience under the Area Redevelopment Act has demonstrated that if you carefully determine in advance where jobs are available and what skills are needed to fill them, that a real attack can be made on a large part of our unemployment problem.

In he past as a Nation we have lagged to an unconscionable degree in assessing our manpower needs and potentials and in trying to match workers to jobs. We can no longer afford either to lag or to stand still. We must move ahead with all the tools which can be made available to us. The programs which will be provided under the Manpower Development and Training Act are an essential part of these tools.

The Area Redevelopment Act, and properly so, is limited in scope because of its limitation to workers in so-called depressed areas. The Manpower Development and Training Act by applying broadly across the country will give us for the first time really adequate tools with which to work.

The principal features of the measure are:

(1) The bill, a 4-year program, provides a nationwide opportunity for occupational training—with priority given to unemployed persons. Training will also be given to employed persons in order to update and upgrade their skills. The training offered to the unemployed would be supported by 100 percent Federal financing—the training for others on a 50–50 State matching basis.

(2) The Labor Department will conduct a continuing study of manpower resources and needs, and provide a program to test and select those to be trained. It will also provide placement services to trainees upon completion of their training program.

(3) Training allowances, roughly equal to unemployment compensation payments, will be paid to unemployed trainees who are not receiving unemployment compensation benefits.

(4) The total number which will be given training is estimated to run from about 160,000 the first year to 380,000 the third and fourth years. The exact balance between unemployed persons and others receiving training will vary between States and at different times. The length of the training period will vary depending upon the occupations involved and the labor market needs.

(5) Training will be primarily carried out through the various existing State vocational agencies; if public institutions are not available, the State vocational agencies shall make arrangements with private training institutions.

(6) The bill provides for a stepped-up program of promoting on-the-job training. Since a wage will be paid by employers to on-the-job trainees, training allowances will be reduced accordingly.

(7) The bill contains safeguards which will assure that States maintain existing levels of expenditure for vocational training from their own funds, and to encourage prospective trainees to accept training opportunities rather than remain on unemployment compensation.

(8) The bill sets forth a formula for the equitable apportionment of Federal funds among the States, based generally upon the size of the labor force and the incidence of unemployment within each State.

(9) Although this provision was stricken by the Senate and House Labor Committees the original administration bill also provided for relocation allowances on a limited basis for workers who couldn't find jobs in their home community.

(10) The annual manpower report will be submitted to the Congress. The Secretary of Labor will make available information regarding skill requirements, occupational outlook, job opportunities, labor supply in various skills, and employment trends.

Youth employment opportunities

Of perhaps equal importance is the President's recommendation for enactment of the administration's Youth Employment Opportunities Act.

We were gratified that hearings were held on this bill during the first session of Congress in both the Senate and House Labor Committees and that both committees reported out bills. The need for a measure such as this and the employment opportunities it would provide for the youth in this Nation has received almost unqualified support from persons and organizations of widely varying background.

Recognizing the urgency of this need, in addition to recommending the enactment of the pending Youth Employment Opportunities Act, the President created the President's Committee on Youth Employment on November 15, 1961, to give added impetus to the finding of solutions to the problems of youth employment.

One challenge facing this Nation is the tremendous increase in the number of young people who will enter the labor force in the 1960's.

During the 1950's, 19 million young people entered the labor force. In the 1960's, this will increase by 7 million to some 26 million young people between 16 and 25. Because of the sharp upturn in the birth rate in the mid-1940's, a great increase will come in the mid-1960's. In 1965, for example, 3.8 million young people will become 18 years of age, an increase of 1.2 million over 1960. Since many young people enter the labor force before they reach 18—school dropouts for example—a tremendous increase will take place as early as 1963 and 1964.

Because of their lack of training, and often of education, and certainly of experience, the unemployment rate for the age group between 16 and 20 is more than twice the national average. They also constitute a high percentage of long-term unemployment. As a nation we cannot tolerate this situation to continue and must find adequate solutions. The administration's Youth Employment Opportunities Act is designed for this very purpose. We all know that the number of unskilled jobs is constantly declining and the demand for skilled and semiskilled workers is constantly increasing because of the nature of the technological changes in our economy.

The youth employment opportunities bill would provide three types of programs to give young people from 16 to 21 employment opportunities which would enable them to acquire both exerience and much needed skills. These programs would include employment in public service jobs by public and private nonprofit agencies, on-the-job training, and employment and educational opportunities in a Youth Conservation Corps.

These millions of young people not only deserve but must be given employment and opportunities to acquire skills and to do useful work. The price of failure is not only frustration and disillusion among our youth but a tremendous loss to our efforts to promote needed economic growth in this country.

A brief description of the bill follows:

Youth training program

The training to be provided would be tailored to fit the needs of the young person and the job opportunities which might be available at the conclusion of training. It would include on-the-job training to the extent that employers would be able to provide such opportunities. It would also include technical school or classroom instruction, normally provided by local school authorities. The program could be a mixture of both techniques or one could follow another. Thus a period of "school" training could precede and lead into employer-sponsored on-the-job training.

The administration proposed to institute this program on a pilot basis of 3 years, and budgeted $25 million for this program to be spent principally in teachers' salaries, equipment, counseling and promotion—traditional functions performed at Federal expense in the training field.

To a limited extent Federal funds, not to exceed $20 per youth per week, would be used to provide training allowances where it was found necessary to provide minimum subsistence financing during the training periods. Primary responsibility for the operation of this program would be assigned to the Secretary of Labor.

This program, originally a part of the administration's youth bill (S. 2036), was added by the Senate to the administration's manpower and training bill through special provisions to accomplish the same objective.

Youth public service employment program

This program may be in State and local public agencies, in publicly owned and operated facilities, or in nonprofit operated facilities, such as welfare agencies, schools and hospitals, or on State and local projects, such as may be directed to the improvement or expansion of recreational or other community facilities.

The employment of enrollees must—

(1) increase their employability;

(2) make a contribution to the public welfare which otherwise would not be provided;

(3) not displace regular workers.

Such jobs could be provided in conjunction with additional schoolwork or training provided under the training program.

The Federal Government may pay up to 50 percent of the wages, but not in excess of $20 a week, as well as 50 percent of the cost of tools, transportation and similar items for trainees. The compensation should be consistent with rates for comparable work in the locality.

The administration's proposal in this area was also on a pilot basis, budgeted at $25 million the first year, and $33 million for each of 2 subsequent years of a 3-year program. On the assumption that the expenditure per enrollee per annum would be $2,000 ($1,000 each from Federal and local funds), the program would furnish employment to 25,000 enrollees the first year and 33,000 thereafter.

The committees on both sides of Congress reported the public service programs substantially unchanged, but broadening them to include programs operated by nonprofit agencies and approved by the State youth agency. The administration's original bill was limited to public programs. The Senate committee also added provisions for a national advisory council which would review each project and make recommendations to the Secretary of Labor.

Youth Conservation Corps

This program would be somewhat similar to the CCC which was in existence for approximately 10 years in the 1930's.

Enrollees in the YCC would be utilized by Federal and State agencies in carrying out their conservation programs—natural resources and recreational areas. The work performed would in general not be the kind normally performed by outside contractors and skilled craftsmen.

Subject to regulations of the Secretary of Labor, enrollees in the YCC would live in camps supervised by the conservation agency for whom they are performing work. They would receive a nominal monthly salary, would also receive food, clothing, transportation, medical services, training opportunities, and other benefits as part of their remuneration.

The administration proposed a pilot program with an expenditure of $25 million for an annual enrollment of about 4,000 enrollees per 3 years. The House committee doubled these figures. The Senate committee recommended a greatly expanded program which over a 4-year period would build up to 150,000 enrollees. This figure compares to the 300,000 average maintained under CCC.

Unemployment compensation

A third major measure recommended by the President to insure that this Nation has a "defense-in-depth" against future recessions is the program for permanent reforms in the unemployment compensation system.

The administration's proposals in this area are now pending before the Senate Finance Committee and the House Ways and Means Committee as S. 2084 and H.R. 7640. They reflect a crystallization of many years' experience in administering the UC system, as well as valuable lessons learned in the last two recessions concerning both the strengths and weaknesses of the system.

These recessions have pointed up the vital base which our unemployment compensation system is to our purchasing power, the well-being of our workers, and our economic stability.

Under the regular State programs alone, some 7.1 million unemployed workers drew benefits at one time or another during calendar year 1961. The total amount of benefits paid out amounted to $3.4 billion, to which must be added another $368.2 million paid to jobless railroad workers, Federal employees, and ex-servicemen. Two and seven-tenths billion dollars was paid out in 1960 and a record $3.5 billion in 1958 under the regular State programs.

In addition to the amounts paid under the regular State and Federal programs in 1961, more than $565.9 million was disbursed to jobless workers under the temporary extended unemployment compensation program. This program, which became effective April 1961, provided for the extension of benefits up to an additional 13 weeks to eligible jobless workers who had exhausted their benefit rights under the regular programs. From April through December, a total of 2.2 million persons received additional jobless compensation through this program.

Thus, in summary, a total of nearly $4.4 billion was paid out in benefits to jobless workers under all unemployment compensation programs during 1961—exceeding the previous high of $4.3 billion under all programs in 1958.

There can thus be no doubt that the money which the unemployment compensation system pours into our economy has a tremendous economic impact both at the local and national level.

But confident as we are in the resiliency of our economy, we know, and both recessions have reaffirmed, that we need permanent authority to meet emergency increases in unemployment as they may occur in the future, as well as to meet the needs of those experienced workers who suffer long periods of unemployment because of technological advances which have made their skills obsolete.

We also know, and the recessions have further made clear, that the present maximum benefit a worker can receive under the State laws is inadequate in relation to present weekly earnings.

In 46 States, the benefit schedules in effect as of January 1, 1961, contained maximum weekly benefit amounts that were less than 50 percent of the respective State's average weekly covered wage. In each of these States, the maximum would prevent a substantial number of claimants from receiving 50 percent of their average weekly wage.

In 31 States, for example, regardless of how high their weekly wages may have been, one-half or more of all 1960 claimants received the statutory maximum weekly benefit amount. In 17 States, 3 out of every 5 claimants in that year received the statutory maximum, even though their weekly wages in many cases might have been more than double this benefit.

For most workers then, in more than 30 States, the program has been tending to become a flat benefit system rather than one where weekly benefits are related to weekly wages.

In contrast, in 1939, the second year in which benefits were paid in most States, maximum weekly benefits were over 50 percent of the average weekly wage in all but 2 States, and were over 60 percent in all but 16 States.

Thus, if we are to fulfill the purpose of our unemployment compensation system, we must enact permanent improvements. Our bill is designed to do this in several important ways:

(1) In coverage—more than 3 million additional workers would be protected.

(2) In extended benefits—by as much as 13 weeks for workers with at least 3 years' experience in covered employment. These benefits would be Federal benefits equal to one-half of their regular entitlement. For all covered workers, similar benefits could become available by Presidential proclamation when insured unemployment reaches 5 percent, and the number of benefit exhaustions over a 3-month period reaches 1 percent of covered employment.

(3) In financing—by increasing the taxable wage base for the Federal unemployment tax from $3,000 to $4,800 a year; by making permanent the temporary increase in the tax rate from 0.4 percent to 0.8 percent a year; and by providing equalization grants to States which have high benefit costs.

(4) In increased benefits—through incentives for the States to provide that the great majority of covered workers will be eligible for weekly benefits equal to at least half of their average weekly wage.

Early action by the Congress on this proposal is of the utmost importance. It is particularly desirable to improve our unemployment compensation system because of the failure of collective bargaining adequately to provide job security. The move to a shorter workweek, for example, is evidence of the concern of the unions for more jobs and job security. An essential element here is the provision of adequate unemployment compensation when a worker is out of a job. We all know that a decent level of employment is best. But the cost of guarantees of employment and shorter workweeks with maintenance of take-home pay may be too costly to absorb without upsetting our goal of price stability. It is here that the role of an improved and strengthened unemployment compensation system becomes so vital.

Standby authority for capital improvements

I am sure I do not need to detail the importance of giving the President the standby authority he has requested to initiate and accelerate capital improvement programs.

As the President has emphasized many times, this administration will not sit idly by when unemployment rises. Many of the measures he urges the Congress to enact, and which I wholeheartedly endorse, are designed to give the Government the tools both to reduce unemployment and to keep it from rising. However, as he has also stated, in a free economy fluctuations in business and consumer spending will undoubtedly continue to occur.

When unemployment rises and other economic developments indicate a weakness in our economy, the Government must have the authority and funds to assure that sufficient jobs are created rapidly enought to put the unemployed back to work, thus creating the necessary consumer purchasing power to reverse the trend.

The President's proposal in this area is designed to do just that. When unemployment rises 1 percent over a period of 3 out of 4 months (or 4 out of 6) the President, if he finds economic developments required such action to achieve the objectives of the Employment Act, would be authorized to use some $2 billion for Federal and State capital improvement programs. The grants-in-aid to States and localities would be for projects of "high priority" which could be started quickly, while accelerated Federal projects would consist of resource conservation and public works programs.

I consider this measure to be of the utmost importance in order to be able to counter immediately any downward turn in our economy, and I strongly urge its speedy enactment.

Tax incentives

Closely related to the standby authority the President has requested with respect to capital improvements are his proposals for flexible standby tax reduction authority and various other tax proposals, primarily those dealing with a tax credit to business for investment in depreciable capital equipment.

I consider these proposals of the utmost importance in giving the Government adequate machinery for stimulating economic growth both in recession and nonrecession periods.

The President's standby tax reduction proposals would authorize him temporarily to reduce rates on income tax when he found such action necessary to meet the objectives of the Employment Act. His proposals for reduced rates would be subject to congressional veto. As the President stated in his economic message, a temporary reduction of individual income tax rates across the board can be a powerful safeguard against recession.

The President's tax credit proposal would increase productive investment by our business communities by reducing the net cost of acquiring new equipment. This proposal is therefore also directly related to the broad goals of full employment and economic growth. More jobs will be created. Modernization should increase productivity and output. More money would be put into circulation; and last but not least, as the President pointed out, the competitiveness of American exports in world markets would be increased.

Of vital importance in this connection are the administrative measures the President has taken to speed up recovery and economic growth. By accelerating various forms of financial, tax, procurement, and construction programs, substantial amounts of additional funds have been poured into the economy which undoubtedly have speeded its recovery. Accelerated depreciation measures, by helping business to modernize its plant and get rid of outmoded technology, will also do much to speed economic growth and make us stronger as a nation.

Public employment services

Another measure in which the Department is directly interested is the President's request for more funds for the U.S. Employment Service.

The public employment offices which operate under the Federal-State employment service system in some 1,700 local communities over the country constitute the frontline in our unemployment defenses. In every locality of any size in every State of the Union, job opportunities to a great extent pivot around the local employment offices. There the unemployment problem appears in its most human form. It is not a statistic but a worker looking for a job.

The U.S. Employment Service has already strengthened its operations, improving its staff and placement services, particularly in the largest urban centers. At my direction it has been improving its counseling and testing services and is providing greatly increased services to those groups in the labor force who find it the most difficult to secure jobs. These are the older workers, the youth, the handicapped, the minority groups, as well as the mature worker with long years of experience in a skill the need for which technological change has destroyed.

But much more needs to be done. Our projections of the manpower needs in the next decade clearly demonstrate that we cannot afford the cost of failure to add to these essential and all-important services. If we do not do so, much of our unemployment problem cannot be solved. We know that the price of unemployment is too high for us to afford. We must devise more effective techniques for matching men to the most suitable jobs and of counseling and channeling workers into training programs vital to their individual advancement and that of the economy. With more funds the Employment Service can go forward toward these goals, goals which must be pursued if we are to reach the high level of national and individual prosperity which is both essential and possible.

Welfare and pension plans

Another important measure which the President has recommended is the administration's proposal for strengthening the Welfare and Pension Plans Disclosure Act.

Private employee welfare and pension benefit plans have become an economic factor of major importance. Plan assets totaled nearly $48 billion in 1959; are probably now around $58 billion; and may well reach the staggering total of $100 billion by the early 1970's.

Approximately 90 million people, workers and their dependents, one-half of the population of the United States, rely upon one form or another of the welfare and pension plans subject to the Disclosure Act.

Typical welfare plans cover group medical, hospital, and surgical, temporary disability, sickness, accident plans, and life insurance.

Pension plans operate on a group basis to provide income for the wage earner when his years of active earnings are ended.

In other words, the plans protect the working men and women of America and their families when illness strikes or accidents befall. They protect the worker against being an object of charity, public or private, when old age destroys his ability to support himself or when the day comes when he wants to enjoy his remaining years in a pleasant and well-earned retirement.

The present Disclosure Act is an inadequate tool for assuring these workers that their investment in these plans is secure.

The administration's proposal for amending the act will enable us to do more adequately the job for which it was originally designed. The act's shortcomings would be attacked by a broad program that breaks down into six component parts which combine together into a highly effective whole:

(1) Adequate investigative power would be given the executive branch.

(2) Specific power to compel compliance and restrain violations of the law through civil judicial proceedings would be given the Government.

(3) Power to issue binding and authoritative opinions and interpretations of the law would be conferred on the Secretary of Labor.

(4) Bonding of persons who handle the funds and other property of these plans would be required.

(5) Three new sections would be added to the Federal Criminal Code prohibiting kickbacks and certain conflict of interest payments to influence certain actions of the giver or receiver, embezzlement, and false entries.

(6) Miscellaneous amendments of existing law, designed to improve operations under the act.

At present the act relies almost entirely upon court proceedings brought by individual employees to remedy noncompliance with its provisions. Experience under other legislation has demonstrated that this is a totally inadequate means for enforcing Federal legislation.

As the President said in his economic message: "We are derelict if we do not provide adequate administrative and enforcement provisions to protect the tremendous financial interests of participants in these funds."

Discrimination in employment

My discussion earlier of the characteristics of the unemployed has demonstrated that one of the major problems with which this Nation must cope in developing its manpower resources is the problem of discrimination in employment. Large percentages of the unemployed, and particularly the long-term unemployed, are in this category because of discriminations against them because of their color or race or other similar factor.

This administration has made it clear that this Nation cannot tolerate either the social or moral implications of such discrimination, or the reckless waste of manpower which results.

I do not believe that it can be fairly disputed that this administration has set an example in the use of existing powers of the Executive and in the enforcement of the letter and spirit of existing laws to the end of achieving equality of opportunity. As you are well aware, Executive orders in this area, and Committees established thereunder, have been a part of the paraphernalia of Government.

Except for a brief period during World War II, efforts under these Committees have been given only limited support and have had only limited success. However, we are particularly proud of the activities of the Committee on Equal Employment Opportunities headed by our distinguished Vice President and of the substantial progress which has been made by this administration on a broad front in its relentless efforts to eliminate employment discrimination.

Now people are beginning to believe that their request for help will produce results.

A Federal employee or applicant for such employment has twice as good a chance today to have his problem corrected than has been true over the past several years. There have also been substantial gains in corrective action resulting in new jobs, new job assignments, promotions, or new training opportunities in cases filed with the Committee concerning Government contractors.

Statistics are useful for certain purposes, but grossly limited in utility in telling the whole story. There are many instances in the experience of the current Committee which can be cited in more human and specific terms. Negroes and other minority workers are today employed in new opportunities as a result of the concerted action by the Federal Government contracting agencies and the President's Committee.

It is with understandable pride that I report that those new employment opportunities in virtually every State of the Union have resulted from the activities of the Federal Government.

I can state with confidence that this administration will continue to take every possible measure to further expand the employment opportunities of these minority groups.

Migratory labor

One other important area in which our manpower base needs to be strengthened is that of the migrant agricultural worker. There are approximately 1 million men, women, and children in the Nation's migrant farm labor system. This "depressed" class is excluded from almost all of the social and economic legislation which protects the vast majority of our wage earners.

Many migrant workers are bereft of training and education. They may travel for long distances in vehicles that are unsafe and overcrowded. It is not uncommon for them to be stranded in a remote area without food, or shelter, or friends. Among agricultural workers the migrant farmworker has found it the most difficult to eke out a living under these adverse economic and social conditions.

We cannot continue to permit these workers to remain outside the broad scope of public concern or policy. The time has come for the Federal Government to take effective action to improve the lot of these forgotten workers. This must not only be done for humanitarian reasons. It must be done as a part of the Nation's overall efforts to expand its economic growth and achieve an economy of full employment.

Our immediate goal is to secure House approval of the five bills passed by the Senate last year. They include proposals requiring the registration of farm labor contractors and crew leaders, extending the child labor provisions of the Fair Labor Standards Act to children of migrants, and providing Federal health services to migrants. They also include proposals to make Federal grants available to the States on a matching basis for the education of migrant children and adults and to establish a National Advisory Council on Migratory Labor.

This is only a beginning. We need to do much more to help these unfortunate individuals. Consideration must be given to providing minimum wage protection for farmworkers and to providing them with other protections and benefits which industrial workers have enjoyed for many years. We must begin the task of bringing relief and a better life to these underprivileged citizens.

Conclusion

Let me say in conclusion that one of the greatest concerns of this administration is for providing a full employment economy, and for providing every possible means for eliminating the scourge of unemployment. We are determined to do something about it. The President's messages are clear evidence of this determination. The measures which I have discussed, moreover, are all a part of this determination. I am convinced that this can be done without inflation, with proper money, credit, and fiscal policies and with the sincere cooperation of business and labor and all segments of our system.

ATTACHMENT 1.—*Summary of redevelopment area occupational training projects approved through Jan. 26, 1962, for training to be initiated in fiscal year 1962*

State and area	*Number of trainees*
Total, 29 projects	4,362
Connecticut:	
Ansonia	200
Danielson	151
Bristol	95
Maryland:	
Cumberland	25
Washington County	240
Massachusetts:	
Fall River	32
Lowell	16
New Bedford	100
North Adams	14
Mississippi: Yazoo-Delta (16 counties)	1,200
New Jersey: Atlantic County	25
Pennsylvania:	
Johnstown	50
Perry-Newport	90
Pittsburgh (Donora)	10
Pittsburgh (Washington)	100
Pottsville	60
Pottsville (Ashland)	16
Sayre-Athens Towanda	80
Scranton	216
Uniontown-Connellsville	180
Wilkes-Barre-Hazleton	90
Wilkes-Barre-Hazleton (Kingston-Nanticoke)	80
Wilkes-Barre-Hazleton (Pittston)	24
Rhode Island: Providence-Pawtucket	178
Tennessee: La Follette-Tazewell-Jellico	110
West Virginia:	
Grant County	130
Harrison County	365
Huntington	325
Mingo County	160

ATTACHMENT 2.—*Occupations*[1] *and number of trainees in 30 approved ARA training programs, Jan. 26, 1962*

Total, all occupations	4,362
1. Aluminum sash and doormaker	10
2. Automobile mechanic	83
3. Automatic transmission specialist	94
4. Chemical operator	16
5. Draftsman	50
6. Electrician, ship	90
7. Electronic assembler	50
8. Electronic mechanic	168
9. Farm mechanic	20
10. Machine tool operator	881
11. Maintenance mechanic	20
12. Millman, woodworking	77
13. Nurse aid	120
14. Radio and TV service and repairman	25
15. Riveter, aircraft	250
16. Route salesman	30
17. Sewing machine operator	160
18. Sheet metal machine operator	40
19. Small appliance repairman	55
20. Stenographer	189
21. Tractor operator	1,225
22. Typist	215
23. Waiter and waitress	45
24. Ward attendant	100
25. Welder, combination	79
26. Drycleaner	45
27. Presser, machine	45
28. Spotter, general	45
29. Presser, hand	45
30. Boot and shoe worker	90

[1] In most of the skilled and technical occupations, the training provided is at the entry level for the job.

ATTACHMENT 3.—*Characteristics of persons selected for ARA training, Jan. 17, 1962*

Characteristics	Total		Male		Female	
	Number	Percent	Number	Percent	Number	Percent
Total number of trainees	1,175	100.0	704	60.0	471	40.0
Age:						
Under 20	196	16.7	110	15.6	86	18.2
20 to 34	590	50.2	388	55.1	202	42.9
35 to 44	235	20.0	122	17.3	113	24.0
45 and over	154	13.1	84	11.9	70	14.9
Education:						
8 years or less	210	17.9	157	22.3	53	11.2
9 years to 16 years	916	78.0	518	73.6	398	84.5
Over 12 years	49	4.2	29	4.1	20	4.2
Duration of unemployment (weeks):						
Under 5	161	13.7	95	13.5	66	14.0
5 to 14	214	18.2	167	23.7	47	10.0
15 to 26	210	17.9	127	18.0	83	17.6
27 to 39	124	10.6	73	10.4	51	10.8
40 to 52	69	5.9	44	6.3	25	5.3
Over 52	389	33.1	198	28.1	191	40.6
Never employed	8	.7	0	0	8	1.7

Senator SPARKMAN. We have announced that Secretary Ribicoff will be here at 2 o'clock.

One correction in the schedule as published. Secretary of Commerce Hodges, scheduled to testify tomorrow morning, will not be here at that time. There will be no session tomorrow, but there will be a session on Friday. Secretary Hodges will testify Friday afternoon.

The committee stands in recess until 2 o'clock.

I thank you, Mr. Secretary, and your associates.

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

AFTERNOON SESSION

Chairman PATMAN. The committee will please come to order. Will you identify yourself for the record, please, sir?

STATEMENT OF HON. ABRAHAM RIBICOFF, SECRETARY, AS PRESENTED BY WILBUR J. COHEN, ASSISTANT SECRETARY (FOR LEGISLATION); ACCOMPANIED BY LUTHER W. STRINGHAM, ASSISTANT TO ASSISTANT SECRETARY (FOR LEGISLATION), DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE

Mr. COHEN. I am Wilbur J. Cohen, Assistant Secretary of Health, Education, and Welfare.

Chairman PATMAN. Would you explain the situation with respect to the absence of the Secretary?

Mr. COHEN. I want to extend the regrets of Secretary Ribicoff at his inability to be here this afternoon. He has been testifying since yesterday morning at 10 o'clock before the House Appropriations Subcommittee on the HEW appropriations. He is there right now, and there is an indication that he is going to remain there for quite some time. He asked me, Mr. Chairman, to extend to you and to the members of the committee his extreme regret. Although he had planned to be here, he finds that the age-old principle that it is impossible to be in two places at one time still is the law of the land.

Chairman PATMAN. They have him on the witness stand so they have priority in view of that. We are glad to have you, Mr. Cohen, and you may proceed in your own way, sir.

Mr. COHEN. Mr. Chairman, and members of the joint committee.

Chairman PATMAN. Are you reading the Secretary's statement?

Mr. COHEN. I will read the Secretary's statement verbatim, Mr. Chairman.

Chairman PATMAN. Why don't you summarize it and then yield for questions, if you please. We will put the whole statement in the record.

(The statement referred to follows):

STATEMENT BY ABRAHAM RIBICOFF, SECRETARY OF HEALTH, EDUCATION, AND WELFARE

Mr. Chairman and members of the Joint Economic Committee, I am pleased to participate in your consideration of the Economic Report of the President.

Health, education, and welfare are ingredients of stability and growth. They also benefit from economic development. Thus, you and I share the interest in full employment, in stabilization, and in national growth. We have a common concern for policies and programs that will promote sustained prosperity, foster equality of opportunity, broaden the manpower base, reduce the waste of unutilized resources, and otherwise make for a stronger economy.

My purpose here today is to supplement those parts of the President's report that show how investments in human resources contribute to economic development. I will discuss some current problems in health, education, and welfare and major needs of the years to come. In that connection I will review our legislative proposals from an economic point of view, stressing, as President Kennedy has stressed, that they "are not unrelated measures addressed to specific gaps or grievances in our national life." Rather they are a set of proposals that will expand both the opportunities of our people and extend the frontiers of our economy. For, when all is said and done, what is the purpose of our economy and of economic growth? Is it to produce fatter hogs or taller mountains of grain or more and more intricate gadgets in a spiritual and intellectual vacuum? No indeed. Our purpose, I'm sure you will agree, is to increase the good health, the wisdom, and the general well-being of all our people.

I have brought with me several charts, to which I will refer, and some supporting statistical tables that the committee may want to include in the record as appendixes.

Public and private expenditures for health, education, and welfare

The President, both in the state of the Union address and in his Economic Report, stresses the importance of human resources to national strength and national development. I would like, therefore, to point out the magnitude and importance of the expenditures this Nation makes for health, education, and welfare.

In the present fiscal year 1962, if expenditures for health, education, and welfare from both public and private sources are combined, they total about $95 billion. (Chart 1.)

This impressive total includes funds provided by government under Federal, State, and local programs; money paid out of trust funds for social insurance; and payments by individuals and private organizations.

Expenditures for health this year will total some $31 billion (chart 2). Three-fourths of the total, $24 billion, are private expenditures, of which the largest amounts are for medical services. The remainder consists principally of Federal, State, and local government expenditures for medical and hospital services, including vendor payments under public assistance programs, medical research, and medical facilities construction.

Education expenditures this year (chart 1) will exceed $25 billion. Over 80 percent of this total, nearly $21 billion, will be public expenditures.

Social insurance and welfare expenditures will come to almost $38 billion. Approximately $33 billion, 86 percent, are payments under public programs, principally old-age, survivors, and disability insurance; railroad and public employee retirement; unemployment insurance; public assistance, institutional care, school lunch, surplus food, and veterans.

By any standard these totals are impressive. They approximate $500 for every man, woman, and child in the United States.

These expenditures represent investments in the common good, and they should be a source of satisfaction to all Americans. Ours is a proud record, a source of great strength at home and dramatic proof that a free society can serve its people in a way unmatched across the world.

Economic effects of DHEW programs

Included in these totals are the expenditures of the Department of Health, Education, and Welfare. In fiscal year 1962 the Department's expenditures will total some $18.9 billion, $4.5 billion from appropriated general funds, and $14.4 billion from the old-age, survivors, and disability insurance trust funds.

These expenditures are made under some 100 programs that Congress has established. Most of these programs aim to treat and control illness, to promote knowledge, and to reduce want. Nevertheless, as the Report of the Council of Economic Advisers emphasizes, many of our programs do, in fact, help to strengthen the economy in several ways.

We administer:

(1) Programs that prevent or reduce illness, disability, and premature death: These programs serve to extend the productive years of life and to decrease time lost from work and school because of sickness or injury. The community health

services, maternal and child health, crippled children's, and the accident prevention programs are in this category.

(2) Programs that increase our knowledge of the causes of illness, of mental retardation, of the learning process, and of the causes of delinquency and dependency. These are the research programs of the National Institutes of Health, the Office of Education, Office of Vocational Rehabilitation, and Social Security Administration that will pay large dividends in years to come, as they have in the past, in lower death rates, in more effective methods of dealing with sickness and disability, in higher quality of education, and in a reduction in dependency.

(3) Programs that extend the availability of health services and the facilities, equipment, and supplies needed for medical care. Medical care payments under the public assistance program, the chronic disease programs, the Hill-Burton medical facilities and construction program, and the new community facilities program enacted last year are in this category.

(4) Programs that promote the rehabilitation to productive living of individuals who because of injury, illness, congenital deficiency, or other defects are in need of restorative treatment. These programs include vocational rehabilitation and those that seek to help the drug addict, the alcoholic, and delinquent, and the many others who, because of physical, mental, or emotional problems, are unable to contribute constructively to society.

(5) Programs that contribute to the conservation and development of natural resources and to the safety of the environment. These are the programs directed to the problems of the pollution of water and air and the control of radiological hazards to health.

(6) Programs that protect the consumer by insuring a safe supply of food, drugs, and cosmetics. These programs are administered by the Food and Drug Administration and the Public Health Service.

(7) Programs that contribute to the size, quality, mobility, and productivity of the labor force. In general, these same programs promote opportunity, enhance the earning power of individuals, and add to the income stream of the Nation. They include such Federal aid to education programs as the National Defense Education Act, vocational education, and training programs to increase the supply of research workers, nurses, and other health, education, and welfare professions.

(8) Programs that help to extend the quality and availability of educational services, facilities, equipment, and supplies. These programs include grants for teacher training; for guidance, counseling, and testing; for the strengthening of science, mathematics, and modern foreign language instruction; and for specified educational institutions, such as Howard University and the land-grant colleges.

(9) Programs of social security that provide income payments to retired, disabled, and dependent persons. The old-age, survivors, and disability insurance program now covers almost 90 percent of all paid employment in the United States. It provides benefits to retired workers and their dependents, to permanently and totally disabled workers and their dependents, and to surviving dependents.

(10) Programs that provide assistance to needy persons. The Federal Government shares in the cost of assistance of four categories of needy persons: the aged, the permanently and totally disabled, the blind, and children in need because of the death, desertion, absence, or unemployment of the parent.

From the many programs that fall under these headings I have selected two, consumer protection and vocational rehabilitation, for additional comment on their economic impact.

Economic effects of consumer protection

The Food and Drug Administration's principal consumer protection program is the enforcement of six Federal laws designed to assure that foods are safe, pure, and wholesome; that drugs, cosmetics, and therapeutic devices are safe; and that all of these products are honestly labeled and that hazardous household products bear sufficiently informative labeling to permit their safe use in the home.

Activities under this program touch the lives of every person—185 million men, women, and children. The retail value of the products over which the Food and Drug Administration has jurisdiction now exceeds $100 billion per year. An estimated 104,000 establishments are subject to FDA inspection.

These activities have significant economic effects:

(1) Without a strong enforcement program it would be easier to market products that were slightly under the weight or volume declared. Consumers spent almost $72 billion for food last year. If shortages in weight and volume averaged only 2½ percent (less than ½ ounce per pound or pint) it would cost American consumers $1.8 billion a year.

(2) Without a strong enforcement program it would be easier to market foods that are adulterated with less expensive, less nutritious, or with actually injurious ingredients. The adverse effect of many of these practices on the public health would be great. If such adulteration amounted to but 2½ percent of the value of the food dollar, another $1.8 billion would be lost to the consumer each year.

(3) An active FDA sanitation program has contributed substantially to the decrease in the quantity of foods which are destroyed by insects and rodents each year.

(4) The establishment of food standards has contributed to the quality of food. These standards in turn have helped the general health of the Nation, such as by contributing to the reduction or elimination of certain diseases caused by dietary deficiencies.

(5) Strong FDA programs have fostered enlightened food sanitation and carefully controlled food manufacturing practices that have the effect of lowering the annual number of cases of food poisoning in this country.

Such safeguards and accomplishments have significantly bolstered public confidence in our food supply. On the whole, the American consumer trusts the food industry, and believes that reliable manufacturers are providing good, wholesome products. This public confidence in our foods has several additional economic effects:

(1) Though American consumers waste an estimated $500 million annually on nutritional quackery, the figure would be much higher if confidence in the food supply were lacking.

(2) Consumer confidence has led to the widespread acceptance and use of prepared foods and has materially increased the rate at which completely new food industries—such as the frozen food industry—have grown.

(3) Widespread use of prepared foods has at least made easier an ever-increasing participation of women in the labor force. Over 24 million women (60 percent of whom are married) now represent approximately 34 percent of the civilian labor force.

(4) More adequate diets, fostered in part by general confidence in the food supply and ready availability of a plentiful and varied supply of good food, have contributed to a national health level never before achieved. A healthy population means less man-hours lost because of illness, injury, or death.

Other economic effects can be attributed to enforcement of Federal laws and regulations relating to drugs. Almost $4.5 billion annually is spent by consumers for drugs.

The Food, Drug, and Cosmetic Act requires drug manufacturers to prove that a new drug is safe before it may be marketed commercially. One result of this law (passed in 1938) was that firms with little or no research activity had to prepare for modern research to meet the requirement, and manufacturers already having research facilities found it necessary to expand them. In addition to enabling the firms to meet legal requirements, this expansion of scientific capability placed the drug industry in a position to capitalize on the tremendous scientific advances accompanying and following World War II much earlier than would otherwise have been possible. Consequently miracle drugs have been developed and made available to physicians years earlier than would otherwise have been possible.

Because of the many factors, other than the availability of new drugs, that have contributed to the dramatic changes in medical care in the past 20 years, I would not try to estimate what portion of the improved medical picture should be attributed to the activities of the Food and Drug Administration. But there is no doubt that the speed-up in medical research produced earlier marketing of such miracle drugs as anti-infective agents, tranquilizers, antihypertension agents, and antihistamines. These drugs and others have been a major factor in extending productive lifetime, reducing the time lost from work through disease, and improving the efficiency of large segments of the population, with great economic gain to the country as a whole.

Other consumer protection activities, such as the removal of dangerous or ineffective drugs and devices from the market, drug warnings to insure safer employment of drugs, and the advice given to drug manufacturers through inspection and other educational activities, produce other economic benefits.

In concluding this example of the economic effects of consumer protection, I would contrast the economic savings that run into billions of dollars with the Food and Drug Administration's total enforcement appropriation of $23 million for fiscal year 1962.

Vocational rehabilitation and the economy

One of the key operating agencies of the Department of Health, Education, and Welfare is the Office of Vocational Rehabilitation. Its program is the rehabilitation of physically and mentally disabled people so that as many of them as possible may earn their own living and may make their own contribution to the economic welfare of this country.

There are in the United States today more than 2 million disabled people who could through vocational rehabilitation services be able to work either in the competitive labor market, in sheltered employment, or in their own homes. Of the persons who become disabled each year, over 270,000 could benefit from vocational rehabilitation services.

The State vocational rehabilitation agencies last year served more than 320,000 disabled people and rehabilitated 92,500 into employment. This year's goal is 100,000 rehabilitations. The following are illustrations of the economic effects of the vocational rehabilitation program:

1. *Reduction in unemployment and increased earnings.*—Last year about 70,000 of the 92,500 disabled who were rehabilitated and placed in employment were not employed when their rehabilitation began. The remaining 22,500 were underemployed or employed in unsuitable occupations. Total earnings of these people in the year before rehabilitation was $70 million. It is estimated that the entire group will earn in their first full year of employment $180 million, a gain of $110 million.

2. *Public assistance cases returned to economic productivity.*—Last year about 15,000 of the 92,500 disabled who were rehabilitated and employed were receiving public assistance at the time they were accepted for or while receiving rehabilitation services. Their estimated public assistance payments were at the yearly rate of $15 million. The total estimated cost of their rehabilitation also was $15 million, but the resulting saving will continue year after year. I believe that the program can be strengthened so that even larger numbers of persons on relief rolls can be rehabilitated.

3. *Increase in size of labor force.*—The 92,500 disabled people who were rehabilitated last year alone will contribute 137 million work-hours annually. Approximately 4,000 of the disabled rehabilitated in 1961 are in the professions such as teaching, engineering, and medicine which are in short supply. Over 11,000 are in skilled work, 8,000 in agriculture, and the remaining are in clerical, sales, service, semiskilled, and unskilled work.

4. *Payment of taxes by rehabilitants*—It is estimated that the disabled people who are established in employment through the public vocational rehabilitation program will pay, during the remainder of their work lives, about $7 in Federal income tax for each Federal dollar invested in their rehabilitation.

Our experience with the vocational rehabilitation program has been so successful that I hope we can take steps to strengthen the program to rehabilitate more people in the future.

Extending the objectives of prevention and rehabilitation

I have talked at some length about the contribution of vocational rehabilitation because it embodies a philosophy which we are extending to other areas. I wish to see the concepts of prevention and rehabilitation infused to the greatest extent possible into all of the Department's programs. Our objective, as the President has said, is to "stress services instead of support, rehabilitation instead of relief, and training for useful work instead of prolonged dependency."

During 1961 we have made an important beginning in advancing these concepts in the Nation's extensive welfare operations.

Some 7.6 million persons were receiving public assistance in December 1961 (chart 3). Of the total, 6.5 million were aided under programs in which the Federal Government participates, and 1.1 million under general assistance, which is financed entirely from State and local funds.

The largest Federal program is that of aid to dependent children, with 3.6 million recipients this past December. Of the total, 2.8 million were children and 0.8 million were caretaker adults. Included in these totals are 220,000 children and adults who have qualified, in 14 States, under the new authority to provide assistance in cases in which the father is unemployed. The next largest program in which the Federal Government participates is old-age assistance with a total of 2.3 million on the rolls. Some 80,000 persons are receiving medical assistance for the aged.

During 1961 I received advice and reports from several groups of distinguished individuals on needed changes in the welfare programs. In December I directed the Commissioner of Social Security to undertake 10 important forward steps that could be accomplished by administrative action. These steps are—

(1) More effective procedures to locate deserting fathers.

(2) Administrative actions to reduce and control fraud.

(3) Allowing children to conserve income for education and employment.

(4) Services to safeguard children in families of unmarried parents.

(5) Services to safeguard children in families in which the father has deserted.

(6) Services to safeguard children in hazardous home situations.

(7) Improvement of State staff training and development programs.

(8) Developing services to families through the Bureau of Family Services (until recently the Bureau of Public Assistance).

(9) Encouraging States and localities to provide more effective family welfare services.

(10) Coordination of family and community welfare services.

While these forward steps can be taken under present authority, additional progress will depend upon the new legislation which the President is requesting of Congress. The President is recommending changes in our Federal laws so that the Nation will be able to discharge its welfare responsibilities in light of the experience and needs of today. We must move swiftly to assure that public welfare is a constructive force in a free society. Our goal must be a positive one: to move people off relief, to renew their spirit, and to create economic and social opportunities for them.

Present and emerging needs in education

To strengthen our manpower base the administration has urged speedy passage of the Manpower Development and Training Act and the Youth Employment Opportunities Act. Measures to strengthen and promote manpower development also include those parts of the President's program to advance elementary, secondary, and higher education, to reduce adult illiteracy, to improve the quality of teaching, and promote education in the health and other professions.

Last fall 48 million children and adults were enrolled in elementary and secondary schools and in institutions of higher education (chart 4). Of these, 33 million are in kindergarten through grade 8; 11 million are in grades 9–12; and nearly 4 million are in institutions of higher education.

A decade ago—in 1950—31 million students were enrolled in educational institutions at all levels. A decade hence we estimate there will be 60 million pupils: 38 million in kindergarten through grade 8, 15 million in grades 9–12, and 7 million in institutions of higher education.

These increases will impose enormous demands for good teachers and good teaching; for classrooms and equipment; for continued diligence that educational opportunities are not denied any able and willing youth for economic or any other reason. Intensive efforts will be needed to reduce illiteracy among adults, to meet head on the problems of those who drop out of school before the realization of their potential, to modernize instruction, and to make sure that the whole educational system meets the scientific, technologic, and cultural needs of a free society.

Both diligence and resources must be provided to meet both these general needs and the requirements in the more specialized manpower fields.

There will be great demands for more doctors, dentists, and nurses. There will be great requirements for schoolteachers, college professors, and for the whole range of skills of those who work with the rehabilitation, counseling, and serving of people in meeting their community and individual needs. All these will be added to the requirement for scientists, engineers, technicians, businessmen, and the leaders of the mind and spirit.

Other needs of today and the future

There are two other problems of today and the future that are important to this committee.

1. We now have some 17 million persons in the population who are over 65 years of age. By 1970 there will be 20 million. Further measures are needed to meet the needs of these people. We know that older persons have more days of illness. They go to the hospital more frequently and stay longer. Many of them need special provisions for nursing and convalescent care.

Older persons have less income and their illnesses entail greater economic hazards. Stays in the hospital are expensive and are becoming more costly. The proportion of hospital bills covered by private insurance is much less for older persons. Coverage also decreases as the length of stay increases. These are the economic facts upon which the administration's proposal for health insurance under social security is based.

2. Another group of needs that are now upon us and will be even greater in the future as population grows and the economy expands relate to the hazards of a polluted and unhealthful environment—of bad air, dirty water, and dangerous radiation.

Review of accomplishments in 1961

Congress and the executive branch are conscious of the policy responsibilities that derive from these national problems. Progress was made last year and the President has charted a course for even greater progress in 1962.

Thirteen significant legislative improvements in health, education, and welfare were passed during the last session of Congress. Several of them are of particular interest from an economic point of view. Under the Social Security Amendments of 1961 4.7 million persons are receiving new or increased benefits. An additional $815 million will become available to social insurance beneficiaries in the first year of operation.

Partly because of immediate needs resulting from the economic recession of a year ago, the new administration sought, and Congress enacted, legislation to extend Federal public assistance to dependent children whose parents are the victims of unemployment.

The Federal Water Pollution Control Act Amendments of 1961 provide for a greatly stepped-up program of waste-treatment works construction. Under the legislation, $80 million will be available during fiscal year 1962 to some 800 communities for waste treatment plant construction—an increase of $35 million over last year's appropriation, supporting projects in an additional 230 cities and towns. This act also authorizes increased Federal support of State and interstate pollution control programs and calls for intensified research activities looking toward more effective methods of pollution control.

The Community Health Services and Facilities Act of 1961 provides support for extending out-patient health services, primarily for the chronically ill and aged, accelerated construction of public and other nonprofit nursing homes, expanded hospital and medical facility research, increased construction of health research facilities and increased training grants to graduate schools of public health.

Last year Congress also provided for occupational training under the Area Redevelopment Act, for training of teachers of the deaf, and passed the Juvenile Delinquency and Youth Offenses Control Act of 1961.

Other noteworthy steps were taken by the executive branch during the year. The President established an Advisory Committee on Mental Retardation to prepare a comprehensive national plan for a coordinated attack on a problem that affects, at great cost to the Nation, some 5 million persons. Also appointed in 1961 was an advisory committee to study vocational education needs and a new Citizen's Advisory Committee on the Food and Drug Administration.

The legislative program for 1962

Our 1962 legislative program was prepared to secure further progress in meeting the needs I have discussed. Each of the President's proposals in health, education, and welfare will contribute to human development in ways that will promote economic growth.

1. A 5-year program of loans to institutions of higher education for the construction of academic facilities. We also support an amendment to the National Defense Education Act to provide for 4-year scholarships to undergraduate students, together with cost allowances to institutions.

2. A 3-year program of assistance to public elementary and secondary schools by means of grants to States to assist them in paying more adequate teachers' salaries, in hiring needed additional teachers, and in constructing urgently needed public school facilities.

3. Programs to improve the quality of teaching in elementary and secondary schools and to encourage the broader application of improved instructional practices.

4. A 5-year program to secure a reduction of adult illiteracy. Approximately 8 million adults—8 percent of our population age 25 or over—are defined as "functionally illiterate"; that is, they have less than a fifth grade education. In addition there are other millions whose educational attainment is so limited that they constitute a drag under conditions of modern industry. Their own adaptability to changing requirements of employment is limited. They are unable indeed to meet many of the community and national needs of today.

5. A 10-year program of construction and planning grants for health professions teaching facilities and a program of grants for student scholarships and for supporting costs to the schools. These programs are urgently needed. Even to maintain the present levels of physicians and dentists in relation to population, we must in the next decade increase the admissions to medical schools by almost 50 percent and nearly double the admissions to dental schools.

6. Health insurance for the aged. This proposal is designed to provide the means whereby older people can purchase the hospital and related services essential to their health. It would add a health insurance program for aged persons to the social security system. By 1964 the proposed program would protect 14¾ million of the 18 million persons aged 65 and over, and practically all of those not covered under the proposal would be eligible for benefits or assistance under other public programs.

7. Major changes in the public assistance and welfare programs to improve services and to promote prevention, rehabilitation, and training.

8. Establishment of a National Institute of Child Health and Human Development in order to provide much-needed impetus to research in the area of intellectual and physical development of the child, the particular problems of the elderly, and the process of maturation generally.

9. Authorization for grants, contracts, and cooperative arrangements for research relating to maternal and child health and crippled children's services.

10. Grants to States and localities to promote intensive community vaccination programs. These programs will be aimed at the virtual elimination of such enemies of our children as polio, diphtheria, whooping cough, and tetanus.

11. Extension and strengthening of the Air Pollution Control Act. We must have new tools to fight air pollution if we are to avoid enormous economic losses and serious health hazards to the people living in urban communities.

12. Amendments to the Food, Drug, and Cosmetic Act to promote consumer protection.

Conclusion

In concluding this statement I would again stress two points:

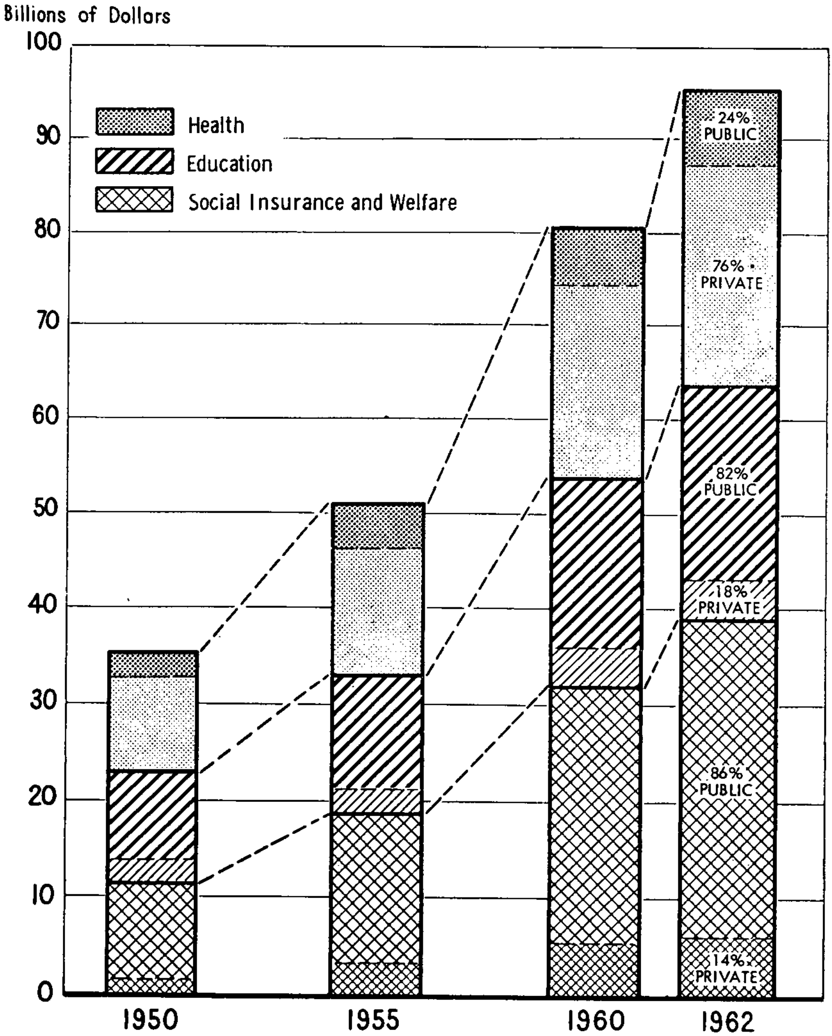
1. The economic progress of the Nation is intimately related to advances in the well-being of the people. Each acts upon the other. Better incomes provide the base for better education and a greater command of health services. Better education produces greater ability to earn. And so on in other aspects of the health and security of people. The results complement and reinforce each other.

2. We must embrace the concepts of prevention and rehabilitation. They must be infused to the maximum possible degree in all governmental programs that concern the human body and mind. An ounce of prevention is better than a pound of cure. It applies whether we are dealing with delinquency, mental retardation, accidents, polio, or school dropouts.

Accordingly, we can promote both the general welfare and economic development by moving forward with "prevention, rehabilitation, protection, and growth."

CHART 1

PUBLIC and PRIVATE EXPENDITURES FOR HEALTH EDUCATION and WELFARE



Source: U.S. Department of Health, Education, and Welfare

CHART 2

PRIVATE and PUBLIC HEALTH EXPENDITURES

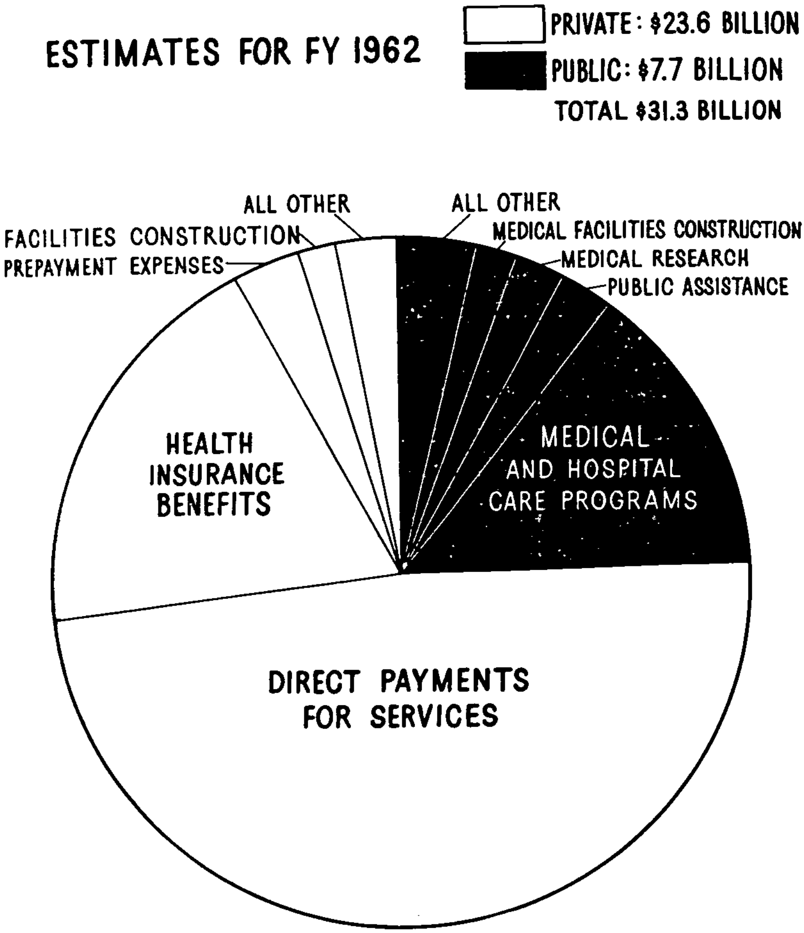
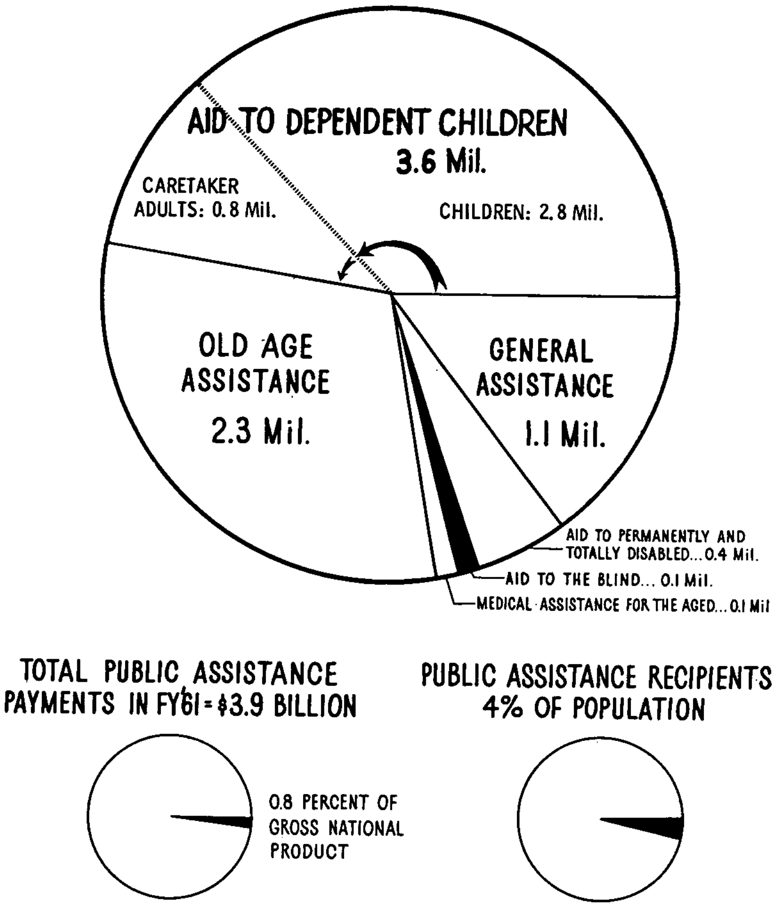


CHART 3

PUBLIC ASSISTANCE RECIPIENTS

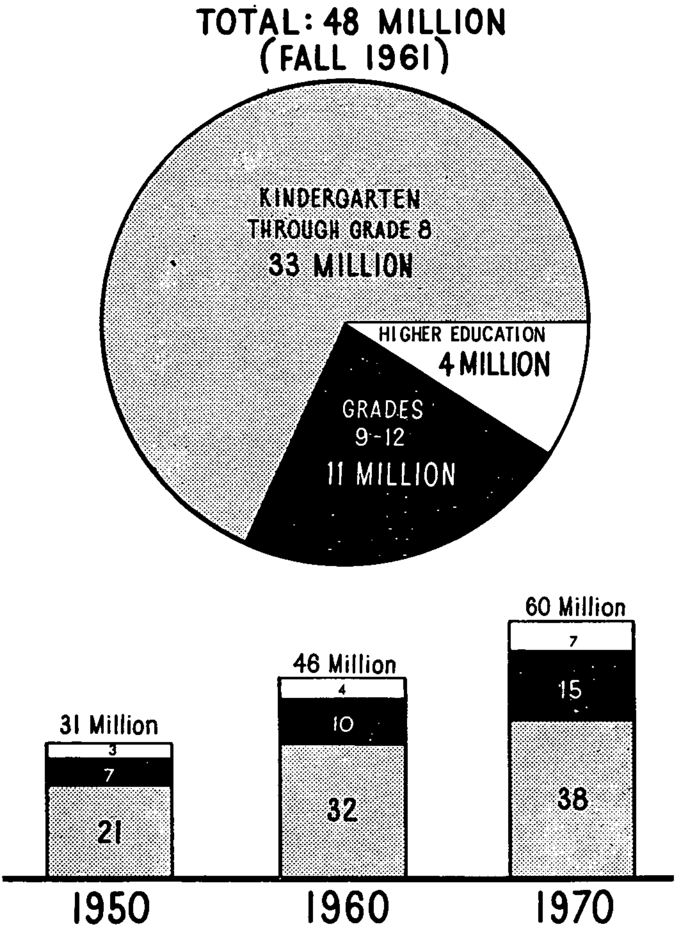
ESTIMATED TOTAL DECEMBER 1961:
7.6 MILLION



Source: U.S. Department of Health, Education, and Welfare, Social Security Administration.

CHART 4

EDUCATIONAL ENROLLMENTS



Source: Department of Health, Education, and Welfare, Office of Education. Estimates for 1970 Assume Attendance Rates Follow 1950-60 Trend; Census Bureau Series II Population Projections Used

APPENDIX A.—*Public and private expenditures for health, education, and welfare*

[In millions of dollars]

Program or activity	1950	1955	1960	Estimated	
				1961	1962
Total expenditures [1]	35,165	50,937	80,440	88,000	95,230
Public	23,041	32,025	51,674	56,950	61,735
Private	12,124	18,912	28,766	31,050	33,495
Health—Total expenditures	12,365	17,738	26,503	28,740	31,315
Public expenditures	3,323	4,283	6,228	6,860	7,670
Health and medical services	2,738	3,897	5,672	6,265	7,025
General medical and hospital care—civilian programs	1,174	1,450	2,174	2,365	2,575
Defense Department and medicare programs	332	603	639	735	845
Veterans' hospital and medical care	586	722	867	895	930
Public assistance [2]	------	212	492	585	760
Workmen's compensation and TDI medical benefits [3]	194	321	446	480	515
Medical vocational rehabilitation	7	9	18	20	20
Maternal and child health services	30	93	139	145	155
School health	31	66	99	105	110
Medical research	55	106	392	510	665
Other public health services	328	316	406	425	450
Medical-facilities construction	585	386	557	595	645
Veterans' Administration and Defense Department	156	42	88	105	130
Other	429	344	468	490	515
Private expenditures	9,042	13,455	20,275	21,880	23,645
Health and medical services	8,827	13,130	19,759	21,340	23,075
Direct payments	7,125	9,388	13,303	14,155	15,060
Insurance benefits	878	2,357	4,698	5,315	6,010
Expenses for prepayment	274	595	793	870	960
Industrial inplant services	150	210	265	275	285
Philanthropy	400	580	700	725	760
Medical facilities construction	215	325	516	540	570
Education—Total expenditures	10,885	14,654	22,015	23,700	25,200
Public expenditures	9,166	11,928	18,094	19,500	20,700
Current	7,930	9,254	14,694	(4)	(4)
Elementary and secondary [5]	4,696	7,618	12,625	(4)	(4)
Higher education other than veterans	545	936	1,664	(4)	(4)
Veterans	2,689	700	405	(4)	(4)
Construction	1,236	2,674	3,400	(4)	(4)
Elementary and secondary	1,019	2,362	2,864	(4)	(4)
Higher education	217	312	536	(4)	(4)
Private expenditures	1,719	2,726	3,921	4,200	4,500
Current	1,437	2,216	3,377	(4)	(4)
Elementary and secondary	632	1,077	1,535	(4)	(4)
Higher education	805	1,139	1,842	(4)	(4)
From current philanthropy	101	190	(4)	(4)	(4)
Endowment earnings	96	135	(4)	(4)	(4)
Construction	282	510	544	(4)	(4)
Philanthropy	73	125	(4)	(4)	(4)

APPENDIX A.—*Public and private expenditures for health, education, and welfare*—Continued

[In millions of dollars]

Program or activity	1950	1955	1960	Estimated	
				1961	1962
Social insurance and welfare—Total expenditures [6]	11,915	18,545	31,922	35,560	38,715
Public expenditures	10,552	15,814	27,352	30,590	33,365
Social insurance	4,716	9,543	18,856	21,465	23,620
Old-age, survivors, and disability insurance	784	4,436	11,032	12,160	14,000
Railroad and public employee retirement	1,048	1,955	3,495	3,985	4,440
Unemployment insurance and employment service	2,350	2,273	3,039	3,925	3,700
Temporary disability insurance and workmen's compensation	534	879	1,289	1,395	1,480
Public assistance	2,490	2,729	3,549	3,770	4,050
Other welfare	400	633	1,203	1,420	1,555
Vocational rehabilitation	23	32	83	90	100
Institutional and other care, school lunch, and surplus food	273	466	909	1,100	1,200
Child welfare services	105	135	211	230	255
Veterans' programs: Compensation and pensions and other welfare services	2,946	2,908	3,744	3,935	4,140
Private expenditures [7]	1,363	2,731	4,570	4,970	5,350
Philanthropy [8]	685	850	1,075	1,100	1,150
Private employee benefit plans	678	1,881	3,495	3,870	4,200
Retirement	340	790	1,600	1,800	2,000
Temporary disability	338	510	755	800	850
Supplemental unemployment benefits	-------	-------	90	120	100
Life insurance, death benefits, and accidental death and dismemberment	(4)	581	1,050	1,150	1,250

[1] Excludes housing expenditures.
[2] Payments made directly to suppliers of medical care in behalf of recipients; beginning November 1960, includes medical assistance for the aged payments.
[3] Excludes medical benefits paid under public law in California and New York by private insured and self-insured plans; such benefits included in insurance benefits under private expenditures.
[4] Not available.
[5] Excludes school health expenditures, which are included under "Public health and medical services."
[6] The estimated cost of providing medical services under many of the welfare programs are excluded from welfare and included under health.
[7] Private welfare expenditures do not include consumer expenditures for welfare services, such as payments made by individuals in their own behalf.
[8] Total expenditures of private agencies from philanthropic contributions for: family services, maternity home care, institutional and foster home care and other services for children, institutional care for adults, services for the handicapped, and sheltered workshops.

Source: U.S. Department of Health, Education, and Welfare.

APPENDIX B.—*Public assistance recipients*

[Estimated total recipients, December 1961]

Program	*Millions*
Federal-State programs: [1]	
Aid to dependent children (children, 2,800,000; caretaker adults, 800,000)	3.6
Old-age assistance	2.3
Medical assistance for the aged	.1
Aid to the permanently and totally disabled	.4
Aid to the blind	.1
General assistance [2]	1.1
Total	7.6

[1] Programs administered by the States with participation by the Federal Government under the Social Security Act of 1935 as amended.
[2] Supported entirely by State and local funds; excludes recipients of only those services for which payments were made directly to the suppliers of medical and remedial care.

APPENDIX C.—*Fall enrollments in regular public and private elementary and secondary day schools and institutions of higher education*

[In millions]

Level	1950	1960	1961	1970 [1]
Kindergarten through grade 8 [2]	21.5	32.3	32.8	37.9
Grades 9–12 [2]	6.7	10.2	11.1	15.1
Higher education	2.3	3.6	3.9	7.0
Total	30.5	46.1	47.8	60.0

[1] Based on Bureau of the Census population projections (series II). Attendance rates are assumed to follow the 1950–60 trend.
[2] The split in enrollments between grade K-8 and 9–12 was estimated on the basis of sample survey data from the Bureau of the Census.

Mr. COHEN. I will summarize the main parts of it, and then respond to questions.

Health, education, and welfare are ingredients of stability and growth in our Nation. They also benefit from economic development. Thus you and I share the interest in full employment, in stabilization, and in national growth. We have a common concern for policies and programs that will promote sustained prosperity, foster equality of opportunity, broaden the manpower base, reduce the waste of unutilized resources, and otherwise make for a stronger economy.

The purpose here today is to supplement those parts of the President's report that show how investments in human resources that we deal with in health, education, and welfare contribute to the economic development. I will discuss some current problems in health, education, and welfare and major needs of the years to come. I have brought with me several charts, to which I will refer, and with respect to some of them I have put the large copies here for you to see.

Chairman PATMAN. Without objection, the charts may be made a part of the record, and also any material which you consider germane to your statement.

Mr. COHEN. Thank you, Mr. Chairman. There are some appendixes that we have sent along with the statement which will be included then.

The President has indicated the importance of human resources to national strength and national development, and I would like to point out to you that in the present fiscal year 1962, if all expenditures from health, education, and welfare from both public and private sources are combined, they will total about $95 billion. That fact is shown on chart 1, which is this one right here. It is a rather impressive chart that shows how these expenditures have increased.

Chairman PATMAN. That includes all expenditures, States, counties, city and subdivisions.

Mr. COHEN. And public and private. This is an attempt to give you a picture in terms of the Nation as a whole—irrespective of the source of the payment, or the source of the expenditure rather—what funds are provided for these three types of expenditures.

Expenditures for health, which I will take first, this year will total some $31 billion, and that is shown on chart 2. That includes all expenditures, public and private. Now, three-fourths of the total of these expenditures, $24 billion, are private expenditures, of which the largest amounts are for medical services. The remainder consists principally of Federal, State, and local Government expenditures for medical and hospital services, including vendor payments for medical care under public assistance programs, medical research, and medical facilities construction.

If you take education expenditures as a unit, which are shown on chart 1, they will exceed about $25 billion. Over 80 percent of this total, nearly $21 million, will be public expenditures.

Turning to the field of social insurance and welfare expenditures, they will come to about $38 billion. Here $33 billion of that, or 86 percent, are payments under public programs, principally old-age survivors, and disability insurance; railroad and public employee retirement; unemployment insurance; and public assistance.

By any standard, if you take all of these totals and put them together they are very impressive. They approximate $500 for every man, woman, and child in the United States. These expenditures represent investments in the common good and they should be a source of satisfaction to all Americans. Ours is a proud record, a source of great strength at home and dramatic proof that a free society can serve its people in the health, education, and welfare areas in a way unmatched across the entire world.

Included in these totals are the expenditures of the Department of Health, Education, and Welfare. In the fiscal year 1962 the Department's expenditures will total some $18.9 billion, $4.5 billion of which comes from appropriated general funds and $14.4 billion which comes from the earmarked trust accounts of the old-age, survivors and disability insurance systems.

I think you will be interested to know that these expenditures of the Department are made under some 100 different programs that have been established by Congress over the years. Most of these programs aim to treat and control illness, to promote knowledge and to reduce want, but they also have economic effects. In the Secretary's statement are listed 10 general ways that the programs we administer have a bearing on the economic status of the economy, its stability, and the development of appropriate manpower to achieve economic growth and stabilization. I will just touch on one as an illustration.

No. 7 that I listed are programs that contribute to the size, quality, mobility, and productivity of the labor force. The kinds of programs include Federal aid to education, such as the National Defense Education Act, Federal aid for vocational education, and training programs to increase the supply of research workers, nurses, and other health, education, and welfare professions.

From the many, many programs—over a hundred, as I said—that we administer, I have selected two for additional comment to illustrate to you the economic impact that our programs have upon individuals and the economy. I am going to take consumer protection and vocational rehabilitation as illustrative.

The Food and Drug Administration's principal consumer protection program is the enforcement of six Federal laws designed to assure that foods are safe, pure, and wholesome; that drugs, cosmetics, and therapeutic devices are safe; and that all of these products are honestly labeled and that hazardous household products bear sufficiently informative labeling to permit their safe use in the home. The retail value of the products over which the Food and Drug Administration has jurisdiction now exceeds $100 billion per year, and an estimated 104,000 establishments are subject to their inspection. These activities have significant economic effects, and I will illustrate several.

First, without a strong enforcement program it would be easier to market products that were slightly under the weight or volume declared. Consumers spent almost $72 billion for food last year. If shortages in weight and volume averaged only 2½ percent, less than a half ounce per pound or pint, it would cost American consumers $1.8 billion a year. You can see what a strong enforcement program can mean in terms of the economic pocketbook of consumers.

Second, without a strong enforcement program it would be easier to market foods that are adulterated with less expensive, less nutritious, or with actually injurious ingredients. If such adulteration amounted to but 2½ percent of the value of the food dollar, another $1.8 billion would be lost to the consumer each year.

Third, though American consumers waste an estimated $500 million annually on nutritional quackery, the figure would be much higher if confidence in the food supply were lacking.

Another aspect of the economics of consumer protection is that widespread use of prepared foods has at least made easier an ever-increasing participation of women in the labor force. Over 24 million women, 60 percent of whom are married, now represent approximately 34 percent of the civilian labor force. The fact that prepared foods are available and that consumers have confidence in them is a part of the ability of women to participate in the labor force and still, of course, meet their family obligations.

Other economic effects can be attributed to enforcement of Federal laws and regulations relating to drugs. Almost $4½ billion annually is spent by consumers for drugs. The Food, Drug, and Cosmetics Act requires drug manufacturers to prove that a new drug is safe before it may be marketed commercially. Because of many new factors that have been contributed to dramatic changes in medical care in the past 20 years, I would not try to estimate what portion of the improved medical care picture should be attributed to the activities of the Food and Drug Administration, but there is no doubt that the speedup in medical research produced earlier marketing of such miracle drugs as anti-infective agents, tranquilizers, antihypertension agents, and antihistamines.

In concluding this example of the economic effects of consumer protection, I would contrast the economic savings that run into billions of dollars for the consumer and economy with the Food and Drug Administration's total enforcement appropriation which is $23 million for the fiscal year 1962.

As another illustration of our programs and their impact on the economy, I would like to take the Federal-State program of the Office of Vocational Rehabilitation. Its program is the rehabilitation of physically and mentally disabled people so that as many of them as possible may earn their own living and may make their own contribution to the economic welfare of this country.

There are in the United States today more than 2 million disabled people who could, through vocational rehabilitation services, be able to work either in the competitive labor market, in sheltered employment, or in their own homes. Of the persons who become disabled each year, over 270,000, it is estimated, could benefit from vocational rehabilitation services.

The State vocational rehabilitation agencies last year served more than 320,000 disabled people and rehabilitated 92,500 new employment. This year's goal is 100,000 rehabilitations.

Last year about 70,000 of the 92,500 disabled who were rehabilitated and placed in employment were not employed when their rehabilitation began. Total earnings of these people in the year before rehabilitation was $70 million. It is estimated that the entire group will earn, in their first full year of employment, $180 million, a gain of $110 million. So you can see the economic value that this program has not only in restoring people to gainful employment, but in aiding, as well, regular members of the labor force.

Last year about 15,000 of those who were disabled and rehabilitated were receiving public assistance at the time that they were accepted for, or while receiving rehabilitation services. Their estimated public assistance payments were at the yearly rate of $15 million. The total estimated cost of their rehabilitation also was $15 million, but the resulting savings will continue year after year.

I believe that the program can be strengthened so that even larger numbers of persons on relief rolls can be rehabilitated.

It is estimated that the disabled people who are established in employment through this program will pay, during the remainder of their lives, about $7 in Federal income tax for each Federal dollar invested in their rehabilitation.

One of our objectives is to see if we can't extend some of these concepts of prevention and rehabilitation into other programs of the Department. One objective, as President Kennedy has said, is to "stress services instead of support, rehabilitation instead of relief, and training for useful work instead of prolonged dependency."

During 1961 we have made an important beginning in advancing these concepts in the Nation's extensive welfare operations.

Some 7.6 million persons were receiving public assistance in December 1961, and that is shown on chart 3 right here [indicating]. The largest single group, as you can see, is made up today of aid to dependent children, which consists of 2.8 million children and about 800,000 of their caretakers or relatives or parents or someone who is caring for the children, which makes 3.6 million persons on those rolls. The old-age assistance program consists of 2.3 million persons and has been slowly declining.

Shown on the chart are 1.1 million persons who receive general assistance through funds put up by the States and localities. There is no Federal fund for that purpose. The other small groups include about 400,000 who are permanently and totally disabled, 100,000 who are blind, and less than 100,000 who receive medical assistance for the aged under the Kerr-Mills provision of 1960.

Recognizing these problems that we have in welfare, during 1961 advice and reports were received from several groups of distinguished individuals on needed changes in the welfare programs, and Secretary Ribicoff took 10 steps to initiate some changes that could be made in the welfare programs. These are listed in Secretary Ribicoff's complete statement. On Monday Secretary Ribicoff announced some other changes that he was making in connection with the meeting of the State welfare commissioners who were here in town.

To strengthen our manpower base the administration has urged speedy passage of the Manpower Development and Training Act and the Youth Employment Opportunities Act. Measures to strengthen and promote manpower development also include those parts of the President's program to advance elementary, secondary, and higher education; to reduce adult illiteracy, to improve the quality of teaching; and promote education in the health and other professions.

Last fall 48 million children and adults were enrolled in elementary and secondary schools and in institutions of higher education. These are shown on chart 4. Of these, 33 million are in kindergarten through grade 8, 11 million are in grades from 9 to 12, and nearly 4 million are in institutions of higher education.

If you look at the bottom of that chart I think you will see a very interesting fact, which is of concern to all of us, and will be of concern to those on the Senate side when you begin discussion of the higher education bill and those on the House side where you have just completed action in one area: that a decade ago, in 1950, there were 31 million students enrolled in educational institutions at all levels—made up of 21 million in the elementary level, 7 million at the secondary, and 3 million at the higher education level—but a decade hence we estimate that there will be 60 million pupils, roughly doubling in that 20-year period; that 38 million will be in kindergarten through grade 8, 15 million in grades 9 to 12, and 7 million in institutions of higher education.

I think this gives you some idea of the tremendous problem that the Nation is faced with, both in public and private education, in meeting enormous demands for good teachers and good teaching, for classrooms and equipment, for continued diligence that educational opportunities are not denied any able and willing youth for economic or any other reason. Intensive efforts will be needed to reduce illiteracy among adults, to meet head-on the problems of those who drop out of school before the realization of their potential, to modernize instruction, and to make sure that the whole educational system meets the scientific, technological, and cultural needs of a free society.

This problem has been made all the more apparent to us by the recent publication of the volume on Soviet Education by Mr. DeWitt, which I think is something that all of you may wish to dip into. It is a very substantial volume, but an analysis of the training and educational programs that the Soviet Union has undertaken in the last 20 or 25 years compared to what we have undertaken, despite the differences in our objectives or ideas, certainly should be such as to make every thoughtful person reflect on what we need to do in the educational field during this coming decade.

I would like to summarize a few other needs of today and of the future that we think are of importance to the purview of this committee. First, we have some 17 million persons in the population who are over 65 years of age. By 1970 there will be 20 million. Further measures are needed to meet the needs of these people. We know that older persons have more days illness. They go to the hospital more frequently and stay longer. Many of them need special provisions for nursing and convalescent care.

Older persons have less income and their illnesses entail greater economic hazards. Stays in the hospital are expensive and are becoming more costly. The proportion of hospital bills covered by private insurance is much less for older persons. Coverage also decreases as the length of stay increases.

These economic facts bearing on the problems of the aged are of great importance economically to the Nation as a whole and to the Government, which may have to put out substantial amounts of money from the general revenues. They also have a bearing on investment and savings with respect to private pension and retirement problems and the mobility of labor.

There is probably no more fundamental question that has so many far-reaching aspects as the question of meeting the economic and health and housing needs of our growing aged population. Every day the aged population of this country increases by 1,000 persons, so that tomorrow morning there will be 1,000 people 65 and over greater than there are today. It is a problem that with passing time will be even greater.

Another group of needs that are now upon us and will be even greater in the future as the population grows, and as the economy expands, relates to the hazards of a polluted and unhealthful environment of bad air, dirty water, and dangerous radiation. With the population growing on an average of about 30 million persons a decade, congregating in large metropolitan areas, this problem of polluted and unhealthful environment is one in which we will have to have greater investment in meeting the needs of our growing population.

I would like to summarize for you briefly what is included at the conclusion of the Secretary's statement on the legislative program for 1962 and the items included in the President's program and his budget which we think have priority in dealing with these health, education, and welfare problems that contribute to human development and economic growth.

First, is a 5-year program of loans to institutions of higher education for construction of academic facilities. It was this program with grants and loans which passed the House yesterday, and which is now being readied to be taken up in the Senate. We also support 4-year scholarships to undergraduate students to go with cost allowances to institutions.

Secondly, a 3-year program of Federal assistance to public elementary schools by means of grants to the States to assist them in paying more adequate teacher salaries and hiring needed additional teachers and in constructing urgently needed public school facilities. No program in my opinion could be more important than this one, which would provide Federal aid to meet the problem of the elementary and secondary schools. You cannot get that man or woman into college unless you first have him through elementary school; so we do need a strong program in this country of aid to elementary and secondary schools.

Third, programs to improve the quality of teaching in elementary and secondary schools and to encourage the broader application of improved instructional practices. This is a new bill, a new program, which the President has recommended for consideration by the Congress this year.

Fourth, another new program is for a 5-year program to secure a reduction in adult illiteracy. I think this is one program that your committee might want to give very considerable consideration to. It is shocking, it seems to me, that in the United States of America today there are approximately 8 million adults, 8 percent of our population aged 25 years or over, who are defined by educators as functionally illiterate; that is, they have less than a fifth-grade education.

Chairman PATMAN. Excuse me. What age did you say, above what age?

Mr. COHEN. Twenty-five or over.

In addition there are other millions whose educational attainment is so limited that they constitute a drag under conditions of modern industry. Their inability to read or write, their inability to pass ordinary employment tests, their inability perhaps to even get a driver's license or to meet any of the minimal standards that are required in a society so complex as ours means that many of them are unable to make a substantial contribution either to their own independence or to the needs of their families or community.

I feel very strongly that this is one of the programs that we ought to commence as soon as practical because it has a very serious retarding effect on the economy. Many of these people when they become unemployed are not able to get jobs. Many of them will be the first fired and the last hired. Many of them will find their way onto the welfare rolls for the rest of the community to support, and, as has been shown by the selective service in both World War II and in the Korean situation, it is showing that roughly 20 percent of the men who were called up during the first year of the Korean War had to be rejected for educational deficiency. So it seems to us that the program to combat adult illiteracy is one that has a very important bearing not only upon employment and unemployment, economic growth, but also on self-support, national security, and a number of other factors as well.

Fifth, a 10-year program of construction and planning grants for health professions, teaching facilities, and a program of grants for student scholarships and for supporting costs to the schools. These programs are urgently needed. Even to maintain the present levels of physicians and dentists in relation to population during this next decade, we must increase admissions to medical schools by almost 50 percent and nearly double the admissions to dental schools. That, Mr. Chairman, is just to stay where we are relative to population today. It would not make for any improvement whatsoever in the relative supply of these needed groups. Hearings on a bill on that subject are being held in the House Interstate and Foreign Commerce Committee now and there is a bill pending on that subject in the Senate Labor and Public Wefare Committee.

Sixth, health insurance for the aged. This proposal is designed to provide the means whereby older people can purchase the hospital and related services essential to their health. It would add a health insurance program for aged persons to the social security system. This, we believe, is a program to which the Congress should give consideration this year.

Seventh, major changes in the public assistance and welfare programs to improve services and to promote prevention, rehabilitation, and training.

Eighth, establishment of a National Institute of Child Health and Human Development in order to provide much-needed impetus to research in the area of intellectual and physical development of the child, the particular problems of the elderly, and the process of maturation generally.

Nine. Authorization for grants, contracts, and cooperative arrangements for research relating to maternal and child health and crippled children's services.

Ten. Grants to States and localities to promote intensive community vaccination programs.

Eleven. Extension and strengthening of the Air Pollution Control Act.

Twelve. Amendments to the Food, Drug, and Cosmetic Act to promote consumer protection.

In concluding this review, Mr. Chairman, I would again stress two particular points. The economic progress of this great Nation of ours is intimately related to advances in the well-being, the security, the health, the education, and welfare of all of the American people. Each acts upon the other. Better incomes provide the base for better education and a greater command of health services, and, as we all know, better education produces greater ability to earn, and so on, in other aspects of the health and security of people. The results complement and reinforce each other.

Of all of the proposals that we have made that relate to economic growth, I would say none is more important than the proposals that this administration has made to improve education at the elementary, secondary, and higher level. I feel that they are the fundamental basis of improvement of income, of development of scientific skill and knowledge, and are the basis for our ability to maintain our strength in the free world.

Second, in all of our programs, I believe we must embrace and expand the concepts of prevention and rehabilitation. They must be infused to the maximum possible degree in all governmental programs that concern the human body and mind. An ounce of prevention is better than a pound of cure. It applies whether we are dealing with delinquency, mental retardation, automobile accidents, polio, or school dropouts. Accordingly, it is our opinion that we can promote both the general welfare and economic development of this country by moving forward with prevention, rehabilitation, protection, and growth.

That completes my statement, Mr. Chairman.

Chairman Patman. Thank you, sir.

Mr. Cohen, I would like to ask you a few questions. You stated that the aged population, 65 years and over, is increasing at the rate of about 1,000 per day. Does that mean net?

Mr. Cohen. That is net, sir.

Chairman Patman. How many pass away on an average each day?

Mr. Cohen. The number of people who reach age 65 each day is in the neighborhood of 3,800. About 2,800 persons die a day. They are more at the upper age groups. The net accretion to the total aged group is about 1,000 a day. Those are rough figures.

Chairman PATMAN. The number who pass away each day are 50 percent greater than the daily increment.

Mr. COHEN. For every four persons who reach age 65, three persons who are 65 or over die.

Chairman PATMAN. The adult education program seems very interesting to me, too, but how much would it help people who are past 35 or 40 or 45 years of age to get a job?

Mr. COHEN. Well, sir, I would say this. I think that, if those persons could be encouraged to go to night school, take this additional training, it might in many cases help them to compete better in the labor market. I am greatly impressed by what the adult education program in this country did in the Americanization of the great numbers of immigrants during the period from 1910 to 1920. I am familiar myself with what those schools did, for instance, in Milwaukee. We have a very outstanding adult education, vocational education, Americanization program that was developed in Wisconsin, for instance, and that kind of program, if it could be developed in every State, and in every community, I think would bring immeasurable help to many people who now have liabilities in the labor market. I have talked just recently with the people from the State education agencies, with the educators, who feel that we are not today making full use of the facilities and knowledge that we have in the schools to make them available in the evening, to make them available after school hours, to help some of these people, who have been underemployed, unemployed, or who can't get jobs because of these difficulties, to go to these classes.

I think it would be well worth a greater investment in adult education, because past experience has shown that much more can be done than we are doing today.

Chairman PATMAN. You used a word there that I have had in bills of different kinds for 20 years, but one was never enacted into law until recently, the word "underemployed."

I don't believe that appears in any law except the Area Redevelopment Act.

Mr. COHEN. I haven't read the Full Employment Act——

Chairman PATMAN. I mean the Area Redevelopment Act.

Mr. COHEN. I was going to refer to the Full Employment Act because I would say that if it doesn't appear there it is well worth having it considered.

Chairman PATMAN. It is in there by implication.

Mr. COHEN. One of our big problems is the person who is underemployed in the sense that he is not using his maximum skill and knowledge, and, when unemployment occurs and then he is unemployed by virtue of whatever liability he has, there is probably a greater difficulty in his becoming reemployed.

Chairman PATMAN. I don't want to take too much time. I will ask one or two questions and then I will yield to the other members.

Do you feel that the aged people are discriminated against in employment?

Mr. COHEN. Yes, I would say there are many aged people today who have competence, who have ability, who have knowledge, who have wisdom, that could be put to greater use if there weren't so many limitations and difficulties that exist in the labor market, and I think much more could be done in that direction.

Chairman PATMAN. I think Secretary Goldberg agreed with me this morning that when we referred to discrimination against race, color, and creed, we should add age too; race, color, creed, and age.

Mr. COHEN. There have been, as you know, Mr. Chairman, a number of State laws passed which provide that discrimination against age shall be unlawful, where hiring practices have been based upon age. I would say that in principle hiring practices should be based upon ability and not upon age.

Chairman PATMAN. I want to ask you about the trust funds. Can you tell us to what extent the portfolio composition of trust funds has changed during the last year toward holding a larger amount of long-term Government obligations?

Mr. COHEN. I don't know that I have it immediately with me.

Chairman PATMAN. Thank you, sir. Do not look it up because I don't have that much time.

Mr. COHEN. All right.

Chairman PATMAN. If you will supply it for the record I would appreciate it.

Mr. COHEN. We will do so, Mr. Chairman.

(The material referred to follows:)

On the whole, in the fiscal year ended June 30, 1961, there was relatively little significant change in the portfolio composition of the invested assets of the old-age and surviors insurance trust fund and the disability insurance trust fund. The reason for this is that in recent years the policy has been carried out or having the special issue investments in a pattern of equal amounts invested in maturities ranging from 1 year in the future to 15 years, and this pattern was in effect at both the beginning and the end of the year. More details on this general basis are given in an article by Robert J. Myers in the Social Security Bulletin for March 1961 entitled "Special Issue Investments of OASDI Trust Funds."

The great majority of the investments of the trust funds are in special issues. As of June 30, 1961, $3.3 billion of the $19.5 billion of investments of the old-age and survivors insurance trust fund was in public issues. Correspondingly, for the disability insurance trust fund $87 million out of the total invested assets of $2.4 billion was in public issues. During the fiscal year ended June 30, 1961, the total amount invested in public issues remained virtually unchanged, but there was a turnover of these investments in the direction of holding a larger amount of long-term obligations. For the old-age and survivors insurance trust fund, about $700 million of public issues was disposed of, and most of these had both low interest rates and maturities scheduled to occur within the next few years. On the other hand, the $700 million of acquisitions of public issues for the old-age and survivors insurance trust fund consisted largely of issues with a coupon rate in excess of 3 percent and with a maturity date of 1980 or later. The same general characteristics were present for the public issue transactions of the disability insurance trust fund.

The statute provides that the two trust funds shall be under the supervision of a Board of Trustees consisting of the Secretary of the Treasury, Secretary of Labor, and Secretary of Health, Education, and Welfare. The Secretary of the Treasury is designated as the managing trustee and is given the complete authority to invest the portion of the trust funds that is not required to meet current withdrawals. The statute states that the managing trustee shall invest in marketable issues only when he determines that the purchase of such obligations is in the public interest. The other two trustees do not make specific decisions on the management policies, although the statute does provide that it is the responsibility of the entire Board of Trustees to review the general policies followed in managing the trust funds and to make recommendations for changes in these provisions of the law.

At the end of each of the last 3 fiscal years the special issue investments of both trust funds were equally spread over issues maturing at the end of each year for the next 15 years. This spread has been accomplished, on the whole, by making any new investments in special issues within the fiscal year to mature at the end of the fiscal year. Any redemptions necessary in the year to meet current disbursements have been made first from the issues of less than 1 year's duration and then, if there are no such fractional-year issues, from the full-year special issues that mature at the earliest date.

At the end of the fiscal year, all fractional-year issues and the regular full-year issues maturing at that time have been reinvested in full-year issues that, when added to the existing full-year issues, result as closely as possible in a uniform maturity distribution over the next 15 years. To accomplish this result, an amount is invested in 15-year obligations to "match" the annual amount of the other 14 series of full-year issues that had previously been purchased, and then any amount still available has been spread over all special issues of the 15 years so as to have more or less equal amounts maturing each year.

Chairman PATMAN. Do you believe that the trust funds are getting the benefit of the increased interest of the past 10 years?

Mr. COHEN. I didn't quite get you.

Chairman PATMAN. Do you believe that the trust funds are getting the benefit of the increased rate of interest in the last few years?

Mr. COHEN. Over a number of years the trust fund was not getting the full benefit of the interest rate as it should.

Chairman PATMAN. You are talking about the one, the social security trust fund?

Mr. COHEN. Yes. However, a number of amendments were made in 1960 along the lines of a bill that Congressman Reuss, I believe, introduced which do now and will in the future enable the trust funds to more adequately reflect the going market interest rates, but over the past they weren't.

Chairman PATMAN. Representative Reuss.

Representative REUSS. Would the chairman yield at that point?

Chairman PATMAN. Certainly.

Representative REUSS. The chairman is raising an extremely important point, and, while Congress did improve on the situation with respect to the fairness to trust fund beneficiaries in terms of interest rate, I am not sure that an entirely adequate job was really done, and it might be in order that you ask the Department to submit a little report on that.

The Secretary, I believe—check me on this, Mr. Cohen—is represented on the committee that manages those trust funds, and the Secretary of the Treasury is, I believe, the chairman of the committee. Is that not so?

Mr. COHEN. The Secretary of the Treasury is the managing trustee. Thus he has really the final say as to the investment matter, except that the interest rate on special issues is prescribed by law.

Representative REUSS. One of the things that bothered me several years ago was that the Secretary of the Treasury was placed in a possible conflict-of-interest position. He wants to pay as little as possible on the national debt, but when he is wearing his other hat as trustee, he should want to earn as much for the old folks as possible. Accordingly, I think it would be useful if we asked the Secretary of Health, Education, and Welfare, who certainly has no conflict of interest, if we might have a current report on the adequacy of the interest rate now being paid.

Chairman PATMAN. Are you willing to furnish that?

Mr. COHEN. Yes, sir.

Chairman PATMAN. Without objection it will be made a part of the record at this point.

(The information referred to follows:)

Question has been raised as to the adequacy and equity of the interest rates applicable to the investments of the old-age and survivors insurance and disability insurance trust funds. This question, of course, can relate only to the interest rate prescribed by law for the special-issue investments of these trust funds because in respect to the relatively small amount of such investments that is in public issues, the interest rate is, in essence, the market rate that is applicable to all purchasers of such securities.

At the present time, the law prescribes that the interest rate on special issues shall be about equivalent (because of rounding to the nearest one-eighth of 1 percent) to the average market-yield rate of all longer-term (4 or more years to call or maturity from the end of the month preceding the month of issue of the special issues) interest-bearing obligations of the United States.

There can thus be no question that the interest rate on new investments in special issues is equitable to both the trust funds and to the General Treasury. It should be noted, however, that this interest rate applies only to new investments made after the enactment of the 1960 amendments. As a result, there is a considerable block of special-issue investments of the trust funds that carry interest rates at the relatively low rates previously applicable (when they were based on the average coupon rate of all long-term—issued for 5 or more years—interest-bearing obligations of the United States).

Considering the old-age and survivors insurance trust fund alone, as of June 30, 1961, about 90 percent of the special-issue investments were on the old basis at an interest rate of 2½ percent or 2⅝ percent (as compared with an interest rate in the neighborhood of 3¾ percent for special issues being currently acquired).

In the long run, all the special-issue investments will be on the basis of the market rate of interest so that there is no doubt that the situation is equitable. The fact that the initial portfolio of investments on hand when the 1960 legislation was enacted was not immediately rolled over on the new interest basis is not necessarily inequitable to the trust funds, although it would have been financially advantageous to them if this had been done. It can well be argued that the trust funds, just as any other investor, must take the responsibility of holding on to investments acquired in the past, even though these may have unfavorable interest rates as compared with those currently available on new issues. The Board of Trustees (comprised of the Secretary of the Treasury, the Secretary of Labor, and the Secretary of Health, Education, and Welfare) considered this situation thoroughly when the proposals for the 1960 legislation were being considered and unanimously agreed that the new interest basis should apply only to new issues. Similarly, the Congress thoroughly considered this matter and took like action.

Chairman PATMAN. How are decisions made concerning composition of trust fund portfolios? Specifically, to what extent do you coordinate trust fund decisions with decisions made by the Federal Reserve System and Treasury?

Mr. COHEN. Basically, that would be a responsibility that the Secretary of the Treasury would have as managing trustee of this fund in relation to these other responsibilities. The Board of Trustees does meet periodically and of course any such matter might be presented to them for consideration, but I would say that would more largely be the function of the Secretary of the Treasury than it would be of the Secretary of Health, Education, and Welfare.

Chairman PATMAN. Thank you very kindly.

Mr. Widnall?

Representative WIDNALL. No. I will pass for the time being.

Chairman PATMAN. Mr. Reuss?

Representative REUSS. I want to commend you, Secretary Cohen, on the very able presentation you have given, and also the most constructive job you are doing in the Department generally. I have just two questions. One, what is the attitude of the Department of Health, Education, and Welfare on the use of voucher payments for certain forms of public assistance, aid for dependent children, for example? The case for voucher payments is that it insures that the public funds will be used for the purpose of aid to children. I don't know that there is anything on that in the list of reforms that the Secretary has promulgated.

Mr. COHEN. No, there is none in the reforms that have been announced administratively because it would take a legislative change to accomplish that purpose. In a memorandum which Senator Byrd has released that the Secretary sent to the Senator in connection with the discussion of the welfare proposals which will be sent to Congress tomorrow the Secretary did include this statement which I will read. Since Senator Byrd released it from his office I believe it is proper to read from it.

> The Secretary indicated that he was considering the following legislative proposals:
>
> Provide for permitting the States to make protective payments to a very limited number of individuals where the individual is having difficulty in satisfactorily managing funds. Such protective payments could only be made to some individual who had a direct interest in the welfare of the recipient, such as a relative, neighbor, friend, or a person in a private or public welfare agency. There would have to be adequate safeguards by the State agency with respect to such protective payments, including periodic review to assure that they were not continued indefinitely and to provide the necessary services to enable individuals to develop a greater capability in managing their funds. Direct payments to landlords and grocers would not be permitted under this provision.

In essence, what that means is that the Secretary looks with favor upon an amendment to the law which would broaden the existing authority so that Federal financial participation could continue, which it cannot do now in those cases where, let's say, the Milwaukee County Board wanted to continue to make the payments through a friend or a relative or someone in the welfare department to assure that the funds were being used for the welfare of the children and not being misapplied.

Representative REUSS. The Department does approve such an amendment to the law?

Mr. COHEN. That is correct, Mr. Reuss.

Representative REUSS. I should think if the Department is willing to do that, it would have been willing to issue vouchers to be paid the grocer, the landlord, and other recipients where the primary public assistance beneficiary has established a record of irresponsibility. What is the reason for that distinction in your thinking?

Mr. COHEN. The distinction in our thinking is that the Welfare Department is not primarily a collection agency. It is providing these Federal funds for the welfare of these children in these families. If the mother or the father misapplies the funds, the primary objective should be to see that the children are taken care of and the funds are not misused and that proper services are given to the children and the family to make themselves supporting.

If the payments are made directly to just the grocer or to the landlord, there is very little rehabilitative element in that. You are seeing that the funds are not misapplied, but you are not getting the family back on its feet to see that they accept the normal responsibility. So it was our thought that, in order to accomplish both objectives, to see that the funds were not misused and at the same time to find a way to help this family, there should be some channel—that is, a relative, or a friend, or a trustee, or some other fiduciary in a sense—who could act on behalf of this mother or family to see that the welfare of the children was taken care of.

Representative REUSS. I must give you my offhand reaction to that distinction, which is that you have rejected a relatively straightforward way of doing it and adopted a rather complicated way of doing it. It seems to me that to appoint a trustee or guardian is a complicated process, and that the issuance of a voucher which can be used only for authorized purposes is more straightforward. I cannot offhand see much difference in terms of rehabilitation. I thoroughly agree that that should be the aim as much as feeding, clothing, and housing.

Perhaps we can pursue this at another time.

Mr. COHEN. I grant you it is an arguable question and I think that people who have gone into this question feel strongly on both sides. May I put it this way? We have decided in principle, since this is a wholly new way of going at it, that we would try and see if we couldn't attack the problem from the standpoint of this more limited version first, and our recommendation is going to be that it go into effect merely for five years, with a view to studying whether there is any better way of doing it.

Representative REUSS. Do I gather that this proposal which you have gone along with is one approved of by Senator Harry Byrd?

Mr. COHEN. That I couldn't say. We have had discussions with him and he released this memorandum on the basis of the discussions that the Secretary and I had with him. The bills will probably be sent to the Congress tomorrow.

Representative REUSS. That is all, Mr. Chairman.

Chairman PATMAN. Senator Proxmire?

Senator PROXMIRE. Mr. Chairman, the buzzer just rang for rollcall in the Senate but I have probably 5 or 6 minutes before I have to go. I hope I have a chance to come back and conclude my questions.

I think this is an excellent report. I am happy that you tie in the health, education, and welfare with economic policy. Before I go into any questions on that, you mentioned something about the DeWitt study of education in Russia.

Mr. COHEN. Yes.

Senator PROXMIRE. It is a very fine study. I put it in the Congressional Record. I was deeply impressed by it. I did not see much of a comparison, however, of their system with ours. It was not as complete, for instance, as the Derthick study of overall education, was it? It was primarily confined, as I understand, to the scientific and engineering impact.

Mr. COHEN. That is correct. In the DeWitt study—on page 341, if I remember correctly—there is a most devastating table, Senator Proxmire, which summarizes the number of graduates. I think, in 1958, in the Soviet Union and the United States in a number of fields, including engineering, medical, and others. It shows the tremendous extent of concentration in the Soviet Union on the scientific, medical, and engineering fields in which they have trained two to three times as many as we have.

(The table referred to follows:)

Structure of graduating classes in the U.S.S.R. and the United States

U.S.S.R. 1959 "Diploma" graduations by field of study			United States, 1958, Bachelor's and first professional degree by field of study		
Field	Thousands	Percent	Percent	Thousands	Field
Grand total	338.0	100.0	100.0	366.0	Grand total.
I. Engineering, all fields	108.6	32.2	10.2	37.3	I. Engineering, all fields (35.3) and ROTC programs (2.0).
II. Agricultural, including agronomy and animal husbandry, forestry and veterinary medicine.	34.5	10.2	2.1	'7.6	II. Agriculture (5.5), including agronomy and animal husbandry, forestry (1.3) and veterinary medicine (0.8).
III. Socioeconomic (economics, management and jurisprudence)	25.0	7.4	18.6	68.2	III. Business and commerce (51.3), economics (7.5) and law (9.4).
IV. Educational-cultural, total	140.4	41.5	62.7	229.6	IV. Educational-cultural, all fields, and among these:
1. Of which university programs, total	37.6	11.1			
And among these: (a) Mathematical, physical and biological sciences	(21.0)	(6.2)	9.7	35.7	1. Science majors: mathematical (6.9), physical (14.4) and biological (14.4).
2. Teacher training establishments. (Of which mathematics and science teachers only).	91.4 (40.0)	27.0 (11.8)	22.7	82.9	2. Education (teacher training establishments and education majors only).
3. Other cultural service fields	9.0	2.7	26.5	97.2	3. Humanities, languages and social sciences—English and journalism (19.2), foreign language and literature (4.5), geography (0.8), social sciences (except economics) (40.7), psychology (6.9), philosophy (3.0), religion (8.8), home economics (4.3), library science (1.7), other miscellaneous (7.3).
4. Fine arts	2.4	0.7	3.8	13.9	4. Fine arts (12.3) and architecture (1.6).
V. Health fields, total	29.5	8.7	6.4	23.2	V. Health fields, total:
Among which: (a) physicians only	(27.0)	(8.0)	(1.9)	(6.9)	Among which: (a) M.D.'s only.
Engineering, sceince and applied science professions (excluding science teachers) (sum of I, II, IV-1a, Va).	191.0	56.6	23.9	87.7	Engineering, science and applied science professions (excluding teachers-science majors) (sum of I, II, IV-1, Va).

Source: Nicholas DeWitt, Education and Professional Employment in the U.S.S.R., National Science Foundation: 1961, table IV-51, p. 341.

Senator PROXMIRE. This Soviet advantage in scientific education is such a tremendously important development. I notice the President of the United States in his press conference before this last one led off with a statement on the challenge this is to our defense and our national security. It has also been brought out here when Mr. Bell appeared that the space agency is going to need 13,000 engineers and scientists in the next couple of years, and this could cripple our graduate education program in engineering and science.

I am wondering is there any contemplated recommendation by the administration to provide additional scholarships in addition to the National Defense Education Act and others? I did not notice in your statement much in the way of recommendations either for a GI bill, which some support in the Congress, or for the extensive scholarship program, which many of us feel is desirable in view of the fact that so many able young people just cannot afford to go to college or to graduate school.

Mr. COHEN. I am glad you brought that point up because if I in any way didn't give it adequate attention I would like to do so now. We strongly support in the bill that is pending on the Senate floor now on aid to higher education the scholarship provisions that were reported out by the Senate Labor and Public Welfare Committee.

Senator PROXMIRE. How many scholarships does this provide?

Mr. COHEN. There were 25,000 for the first year, 37,500 for the second year, and 50,000 for the third year, which over the entire lifetime of that program would have been 212,500 scholarships. Those were deleted in the House bill that passed yesterday. The administration strongly and unequivocally supports the scholarship provisions that are in the Senate bill.

Senator PROXMIRE. Are these scholarships weighted to try and encourage engineering and science as much as possible?

Mr. COHEN. No. Here you have a problem, Senator. There already are some fellowships in the National Defense Education and the National Science Foundation Acts. We believe to overcome the imbalance which already exists the scholarships that are in the new proposal should be for talented youth who are needy generally for 4 years of basic higher education.

In other words, if we are going to get some of these people in, whether it is in science, or art, or any field that will help keep America great and free, you have to get them in as freshmen.

Senator PROXMIRE. I highly approve. I think it is a mistake to slight our social sciences and the humanities, but at the same time there is such an intense, and obvious, an imperative need in science and engineering that I am wondering what the proportionate number of scholarships would be, and if it would be sufficient, for example, even to take care of such need as we are sure to have in the next few years in the space agency itself, or whether this will be pretty much of a "drop in the bucket" in that area.

I would not want to slight these other fields because I think they are at least as important.

Mr. COHEN. No. I do feel though, if I might summarize what we think has been the situation since 1958. The National Defense Education Act, in my opinion, was a very great piece of legislation and long overdue. While it is inadequate in many respects and ought to be expanded greatly—I hope Congress next year, when the 2-year extension has been completed, will go thoroughly into a wholesale revision of the National Defense Education Act—it has resulted in many of our able and talented boys and girls going into science and engineering and in a sense denuding other areas which are of great importance to us.

Senator PROXMIRE. As the President pointed out, however, since 1952, I believe, there has been an absolute, not a proportional, but absolute diminution in the number of people graduating in science and engineering. At this very time we have had a substantial increase in the overall graduates of our country.

Mr. COHEN. That is right. Let me tell you, though, what has happened in these last 5 years. Let's take the medical field. In the medical field, as a result of all these scholarships and fellowships in science, mathematics, engineering, all of which we endorse, the number of applicants, as I recall, for medical schools in the last 10 years has dropped from about 20,000 a year to less than 15,000, but the second thing that has happened is that the quality of applicants to medical schools in the last few years has declined.

I was trying to look up, and I will put in the record for you, the grade average of these boys and girls entering medical schools has declined tremendously. We are taking many more B and C students into medicine because those able students are taking up the science, engineering, and other scholarships.

(The information referred to follows:)

In 1950, 40 percent of the students entering medical school had college grade averages of A, by 1960 this percentage had declined to the point where only 13 percent of the new medical students had grade A averages.

Mr. COHEN. Aid for science and engineering students is fine for our technological development, but as human beings we need doctors, too. As I tried to outline before, if the present trend continues, we are not only going to have fewer doctors to population in the coming years, but we are going to have less capable medical research workers to attack the problems of cancer, heart disease, metabolic disease, arthritis, and childhood diseases. We have to think of the balance here, too.

Senator PROXMIRE. I want to come back in just a minute. I have to stick my head in the door and vote and I will be right back.

Representative WIDNALL. Mr. Secretary, it is good to see you here.

Mr. COHEN. It is good to see you again, Congressman.

Representative WIDNALL. I am a little bit intrigued by the dropoff in the people going into the medical field when this is supposed to be a millionaire's profession with the doctors having yachts in Palm Beach and all these other things. Why do you have a dropoff if it is so good?

Mr. COHEN. It is a very interesting problem. First I think is this point that I mentioned. There are in the last few years vastly more scholarships and fellowships available without repayment to a young boy who wants to go into science, or mathematics, or engineering. He can usually in 4 or 5 years, Congressman, graduate from a great university, go into a science or engineering area at usually rather good pay, and if he is talented get a fellowship that will lead him into either a Ph. D. or advanced training, practically all of which will be paid through some Government program or through some private program.

However, if he wants to go to medical school, let us say, he not only has to look forward to 4 or 5 years, as some of these others do, but rather to maybe 10 years, or even longer, to get to a point where he has repaid his obligations, is taking care of his family, and is making what he thinks is a minimal income in relation to his professional qualities.

For instance, a boy going to medical school now may have to borrow through the National Defense Education Act. He has to get a loan rather than a grant, and I would think that the proposal that we have pending that would give scholarships as well to our medical students is an absolute essential. I recognize it is a very difficult question for me to comment on because in advocating this kind of scholarship I am certain, as in the question that you asked, that eventually these people will be making $15,000, $20,000, or $30,000, or more. The question arises, Why can't they pay it back?

Representative WIDNALL. May I interrupt at this point and just say this. I think that the principal point of your comment was that they were going into other professions because they were getting it all for free and that there was no repayment. We are very fond of comparing our educational system with the Russian system. In the Russian system they get their tuition, their room and board, and they get some subsistence allowance, but they have to give 2 years of their life to the Government when they get through. They have to give something back.

Is that not where we are making a mistake now with all this free business as far as our own students are concerned, where there is no sense of responsibility imparted to them as to what they must do in order to get this? Would we not get them back into the medical profession if we did not give them the for-free business in all the other lines?

Representative REUSS (presiding). May I interrupt, Mr. Widnall?

Representative WIDNALL. Mr. Secretary, there is an emergency phone call for you, and unless there is objection I would like to excuse the witness for long enough to make the phone call, and then I hope you can answer the question.

Mr. COHEN. Yes.

(Brief recess.)

Senator PROXMIRE (presiding). We are happy to have you continue, Mr. Cohen. Mr. Widnall asked you a question. Would you like to have the question reworded, or do you have it pretty well in mind?

Mr. COHEN. You were talking about some kind of a condition relating to service for a grant.

Representative WIDNALL. Maybe we did not require enough responsibility upon the part of those who are getting these grants or scholarships toward repayment so that they would feel a value, a responsibility, that they don't seem to feel today; also it might channel more people back into the medical profession.

I was particularly interested, and I think you answered this partly before, in why there should be a sloughing off in applications to medical schools when the press always stresses how fortunate the doctors are. I should think everybody would flock to the profession because it gives them a chance to make so much by way of wordly goods.

Mr. COHEN. I would say the objective that you state, Congressman, is certainly one that I think is well worth considering. There are a great many national needs for physicians in rural areas, in research, in the National Defense Establishment, in Government, and elsewhere that would make a great contribution to our national interests and our national welfare. Perhaps some method could be found to give some kind of an emphasis, or priority, or preference to those needs.

On the other hand, none of us likes to see any kind of an indication to a young man or woman as to where they have to work or what they have to do. I appreciate that this would be contingent upon receiving the grant or the scholarship, but, as I said, our view is that in providing more doctors for the Nation as a whole, you best serve the national interest because each individual, by looking after his own welfare, will enhance the national welfare.

We are rather concerned that any kind of measure that attempts to direct a particular profession into an area might well be misguided or inapplicable.

Representative WIDNALL. Well, I would agree with that comment, Mr. Cohen, but is not this one important consideration in connection with the medical profession, and also the applications that are being made today? Is not there a basic prejudice in America against women being doctors?

As I understand it, over in Russia, 88 percent—88 percent of the medical profession—is composed of women.

Now here, I understand, there are very few women who apply to medical schools, and the reason is mainly because of the prejudice of medical schools against women, and the prejudice of the public against women as doctors. Now, is this true or not?

Mr. COHEN. Well, you raise an interesting point that I made recently with the medical profession out in California, and I was roundly denounced by some of them for making exactly the point that you did. I came back from Yugoslavia this last year, where the same situation prevails as you indicated in the Soviet Union. The European countries make much more use of women in the medical professions than we do. There I visited a great number of hospitals and medical centers in Yugoslavia in which, particularly in the field of pediatrics they were almost completely staffed by women. I agree with you wholeheartedly that there are many women who would be very competent physicians, particularly in this whole emerging field of child care and pediatrics and child development and child psychology, that could be utilized, providing that we are willing to make the necessary adaptations—and this goes beyond medicine—in our economic system to enable them to take care of their family responsibilities simultaneously.

The average employment of a doctor is about 60 hours a week. If you ask women to work 60 hours a week and still take care of their husbands and their children and their families, it is obviously almost impossible. So some modifications have to be made.

Representative WIDNALL. Is not this being done in millions of families in America today, where the wife is working as a schoolteacher or is working in some other capacity?

Mr. COHEN. I think that in the schoolteacher job that you indicate, there is one great advantage, and that is that she can get home by 4:30 or 5 o'clock in some instances, so that she can still take care of her family responsibilities. I have always felt that if you want to use more women in employment generally, you will have to make some adjustments in the pattern of work to enable women to do this more satisfactorily.

There is another problem with respect to loans you will find if you talk with people in universities. Women will not take loans to continue to go on to school and higher education, because they are afraid to come to marriage with this huge debt which they would then have to pass on to their husbands. Therefore, I think that if you have repayable loans, you are not as helpful in getting women to go on through higher education and into other fields. I think scholarships would help much more in connection with getting women into the professional fields.

Representative WIDNALL. Mr. Cohen, I understand my time is up. I would like to ask you a couple of other questions later on.

Mr. COHEN. Yes, sir.

Senator PROXMIRE. Senator Pell.

Senator PELL. Mr. Cohen, I have received a great deal of mail of late from optometrists, who would like to be considered in the same category as doctors and dentists and other professional specialists. I realize this is a detailed question, but you have so much detailed knowledge, I thought you might be able to send us something to be added to the record about what your views are.

Mr. COHEN. Yes, Senator, I have received some of those same letters, so I am quite well acquainted with the issue. The optometrists, as I understand it, would like to be included in the administration's health professions bill, in connection with instruction scholarships.

Senator PELL. In my mind, there seemed to be merit to their argument.

Mr. COHEN. Well, there is this difference, Senator, and that is that the shortage of physicians and of dentists has been well documented, well documented for a long period of time. The shortage of physicians has been documented by a report that the previous administration instituted under the chairmanship of Frank Bane. The shortages of dentists also have been very well documented, and even is greater relatively than that for physicians.

Now, when you get beyond those two health professions, as to what the shortages are, and how we are going to meet them for the future, they have not yet been documented.

Pursuant to the request of the President, we have set up an Advisory Committee on Nursing. There is obviously a very great shortage of nurses for the future, and we have special committees going into that. We do not know, nor has there ever been a study on the need for or the shortages of optometrists. So I think that my answer to you would be, until that need has been demonstrated, we think that we should go ahead with the physicians and the dentists.

Senator PELL. From the viewpoint of training, do you have any views as to the relative adequacies of both courses? Because the optometrists now have almost as many years of college background as do the doctors and dentists.

Mr. COHEN. I just do not think that whole area has been gone into, Senator Pell. As far as I know, or at least as far as we have knowledge of, there has been no study of the training, manpower needs now and in the future of the whole area of optometry, and therefore, I really cannot answer that question.

Senator PELL. By whom would you say the study could be most oppropriately made?

Mr. COHEN. Well, I think if such a study were to be made, it would have to be made by some impartial group advisory to the Surgeon General and the Public Health Service.

Senator PELL. Were you thinking of initiating or starting such a study?

Mr. COHEN. Well, we really have not given too much thought to it right now, because we are in the midst of the nursing study. We hope that it will be done this year. Then we will come up with recommendations. Thus, we now are responding to the study of physicians and dentists, and the nursing one is on the horizon. I would say that when we finish with these, we could go on to whatever else might be necessary.

Senator PELL. That might well be in relation to optometry?

Mr. COHEN. We would certainly consider that. I understand that there were some suggestions from other fields, too.

Senator PELL. Thank you very much. Another question. In connection with the surplus food distribution, would you describe a little bit the relationship between the HEW, and the Department of Agriculture, in the distribution of food, or is there a relationship?

Mr. COHEN. Well, there is no formal or legal relationship. The surplus food program is administered by the Agriculture Department. When surplus food is available, it is distributed through the welfare departments of the States. The food is provided directly from the Agriculture Department, to the State welfare department, and through it to the local welfare department. So there is no chain of command at the Federal level between Agriculture and our Department.

Senator PELL. Referring to the study of Dr. DeWitt that you mentioned earlier, the parent study of Soviet education, that publication, as you know, is quite expensive. It is about $4.95, and even in digest form it costs a dollar. To my mind, it should be made available to every high school principal, and much more widely disseminated than at present. Is there any thought given to the idea of publishing it under the auspices of HEW?

Mr. COHEN. No, but it was passing through my mind the other day that some enterprising Senator might get a summary prepared as a Senate document and have it circulated. I think it is extremely important that it be widely disseminated. I think some kind of a precis of summary that gives the gist of it, because it is very complicated, and filled with tables, should be circulated through the length and breadth of this land.

Senator PELL. In your view, how long would the observations made in that document continue to be applicable? Will it be a valid document a year from now, 3 years from now, or do you think we are now in a transitional period?

Mr. COHEN. I am hesitant to say this, but at the pace we are going in the United States in making the necessary expansion in our educational system, the DeWitt observations are going to be applicable for quite some time. Because the Soviet Union, as you look at the record over this 20-year period, has emphasized the value of education for so long, and has so developed its educational instruments, financial support, and the incentives it is putting in, that even if we were to start today, we would still be way behind for a long time to come.

Let me just give you this illustration again on medical education. If you pass that medical education bill today, it would probably be 10 years before one additional new doctor were produced under that legislation. You have got to build a medical school—I am talking about new medical schools—which takes 2 or 3 years to provide the faculty, and to get new students in it. That takes at least 4 years of undergraduate education, and then the years of medical education, and of internship and residency. So when we are talking today what we have to do in this field, the net results will not be apparent to the people of the United States until a decade from now. That is how long ahead you have to plan.

Senator PELL. Pursuing that thought a step further, can we consider the question of motivation for going into the professions? I believe it is a correct statement that the caliber of applicants to medical school, is about one ladder lower than it was. It used to be B minus and better, and now it is C minus and better, and so with engineering. Furthermore, the number of applicants has declined.

I had a little survey run of a group of engineers in my home State as to what they thought the reason was for the smaller number entering the profession. To my mind, their answer was very interesting. The plurality of their answers indicates that the basis for the decline was the loss of status, not economic motivation or anything else. I was wondering what your reaction would be to that?

Mr. COHEN. Well, I just happen to have published a book this year on educational motivation, so you are touching on a question that I have been working on quite some time.

It is a very complex factor, but there is no question in my mind that somehow or other we have to develop greater motivational factors in here, and this little table or chart that I have produced here from census material is something well worth pondering over, because it attempts to bring two factors together. The education of the father of family and income, which shows that there are these two factors that are related.

Senator PROXMIRE. If you will yield at this moment, I think in view of the fact that you are discussing this memorandum and the charts, I am going to ask to have it included in this record at this point, so your discussion will be clearer.

(The information referred to follows:)

EDUCATIONAL ATTAINMENT: ITS RELATION TO FAMILY BACKGROUND[1]

According to a survey taken by the Census Bureau in October 1960, there were 4.7 million men 20 to 24 years old in the United States. Of this number, 1.7 million either had graduated from college or had some college attendance.

The survey reveals a relationship between the level of education attained by young people and certain factors in their family background.

There is a direct relationship between the college attendance of young men and the education of their fathers.

College enrollment rates of men in their early twenties whose fathers were college graduates are several times as large as those for persons of the same age whose fathers never finished high school.

When the fathers had completed college, 88 percent of the sons 20 to 24 years of age had graduated from college or had some college attendance.

In contrast, when the father had completed only high school, 65 percent of the sons had graduated from college or had some college attendance.

In the nonwhite group where the father did not graduate from high school, only 7 percent of the children 16 to 24 years of age were enrolled in college.

However, in the nonwhite group where the father did graduate from high school, 18 percent of the children 16 to 24 years were enrolled in college.

There is also a direct relationship between high school graduation of young men and education of their fathers.

Where the fathers had graduated from high school, 92 percent of the sons had graduated from high school including 65 percent who had some college attendance.

But when the fathers had not completed high school, only 57 percent of the sons graduated from high school including 23 percent who had some college attendance.

Educational attainment is related to family income.

Among the families whose income was less than $5,000 a year, 55 percent of the children 16 to 24 years old had graduated from high school but only 19 percent went on to college.

Where the families had an income of $10,000 or more per anum, 87 percent of the children had graduated from high school and 60 percent continued on to college.

The educational level which a person attains is a product of both the education of the father and the family income.[2]

Where the father did not graduate from high school and the family income was less than $5,000 only 13 percent of the children had some college attendance.

In contrast, where the father graduated from college and the family income was $10,000 or more, 89 percent of persons aged 16 to 24 years old had some college attendance.

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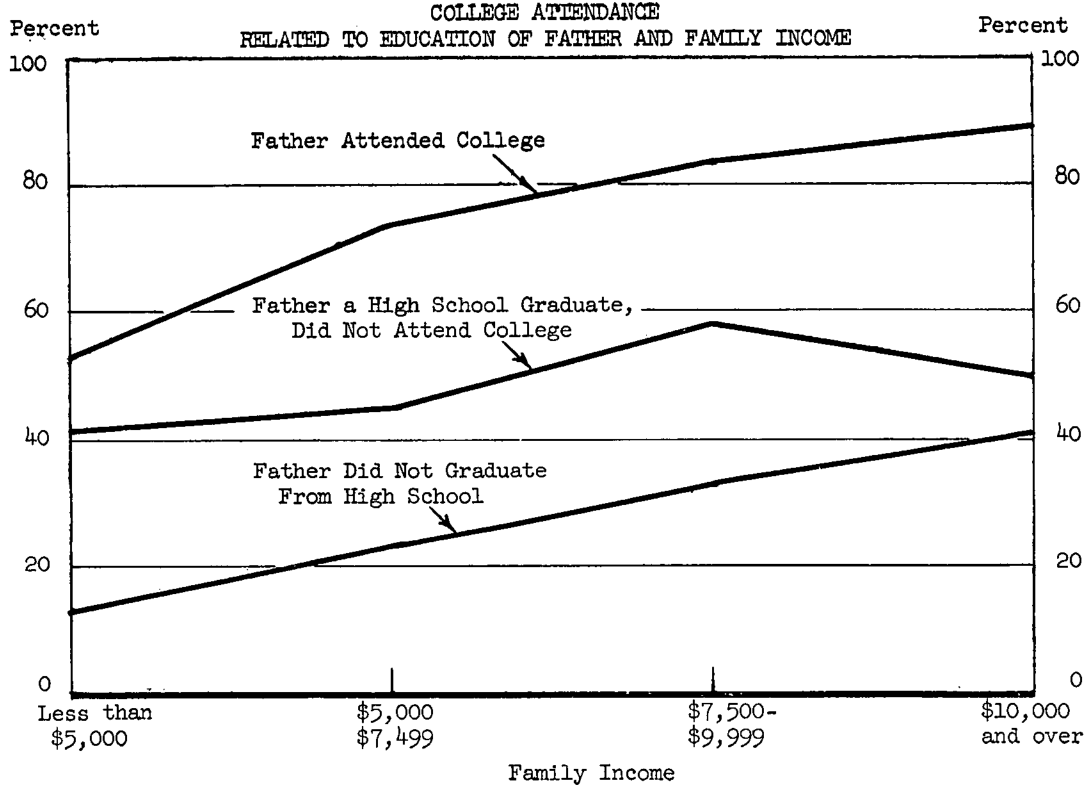
[1] Based on U.S. Department of Commerce, Bureau of the Census, "School Enrollment, and Education of Young Adults and Their Fathers," October 1960; Current Population Reports, series P-20, No. 110, July 24, 1961.

[2] College attendance is also related to the occupation of the father This relationship is indicated in the U.S. Department of Health, Education, and Welfare; Office of Education; Cooperative Research Monograph No. 8, "Factors Related to College Attendance," which states "* * * High school seniors whose fathers (*a*) were in executive or professional occupations, (*b*) owned or managed business, or (*c*) did office or sales work were much more likely to attend college than the seniors whose fathers (*a*) owned or managed farms, (*b*) were factory workers, or (*c*) were in the skilled or semiskilled trades."

COLLEGE ATTENDANCE
RELATED TO EDUCATION OF FATHER AND FAMILY INCOME



Mr. COHEN. Yes, let me just summarize from the chart here.

Where the father did not graduate from high school, and the family income was less than $5,000, only 13 percent of the children had some college attendance.

Now we will go over to the other extreme. In contrast, where the father graduated from college, and the family income was $10,000 or more, 89 percent of persons 16 to 20 years old had some college attendance. Now by looking at the chart, you can also see how these two factors had some bearing. I do believe that both factors are important. I believe that where the father has had more education he will impart this feeling of the importance and value of an education to his children.

Senator PELL. Forgive me. I did not make myself clear when I said the majority in their replies based their reasons for the lack of enthusiasm for the engineering profession today on the lack of status. Their thought was that the engineering profession had more status 20 years ago than today, and something should be done to build up their prestige.

Mr. COHEN. Yes, the problem of the prestige and status of professions is very complex. It is also involved in the question that Representative Widnall asked before.

To some extent, there is inherent in your question the fact that ranked as against other professions, the profession of physicians doesn't have as much relative prestige. I don't mean it has declined absolutely, but other professions have come along in the course of the last 20 or 25 years, the scientists, the physicists, the research technician, the man working on space problems, which have a lot of prestige in our society. That has resulted in some of these other professions dropping relatively in their prestige. I think that is what has happened as well.

I think the problem of the prestige of the teacher, for instance, which has not risen as it should also is a matter of concern. These are a composite of many factors in our society.

I do think that the point that Representative Widnall made is well worth thinking about, that in all of this, we must give consideration to the national interest.

We need engineers, we need teachers. We need social workers. We need all of these people to have a well functioning economy.

Senator PELL. That is all.

Senator PROXMIRE. Mr. Cohen, you were discussing the National Defense Education Act, when I had to leave to go to the floor.

Mr. COHEN. Yes, sir.

Senator PROXMIRE. I have heard a lot of complaints from high school principals that much of the money that goes to high schools to buy laboratory equipment, particularly, and other facilities, has had almost no effect on education, but has all kinds of effect on the profits of the companies that sell this equipment.

I have heard this so often and so insistently, and some of them have said that they have looked at the catalogs, and they find that there was a sharp increase, an unprecedented price increase, right after the Congress passed the National Defense Education Act. I am wondering if the Department has made any study of this, if you have received enough complaints that you feel that a study is warranted?

Mr. COHEN. Senator, I have heard some of those, too. You are talking merely about title III equipment grants.

Senator PROXMIRE. That is right.

Mr. COHEN. We have heard that that has been so. So far, without looking into it myself, I have attributed it largely to the enterprising genius of many of these equipment manufacturers, who when they saw that Congress had made that money available, did go around to the principals and to the schools and try to sell some of this equipment.

Senator PROXMIRE. My point was not that they did a fine job of selling it—that is great—but that the increase in funds available to buy equipment went primarily into higher equivalent prices, and therefore, higher profits for a few companies, which is certainly not the intent of Congress.

Mr. COHEN. That is right. I don't know the facts of that myself and I don't know that we have done any study on that.

Senator PROXMIRE. Have you received substantial complaints?

Mr. COHEN. I could not tell you how many there are, but I have been in meetings or sessions in which this kind of a point was made, but I do not know from any occasions——

Senator PROXMIRE. It seems to me it would be fairly easy to check, because you would just have to take three or four standard items of laboratory equipment which were widely purchased, and find out whether there was a substantial price increase, how it compared with the past, and the proportion of money that goes into this that has come from the Federal Government.

Mr. COHEN. Well, I will look into that. Of course, there probably would be other factors in connection with it. The equipment is changing, and I do not know what particular types of equipment have been most subject to that. We might take a look and see if there is anything that we can objectively look into.

(The information referred to follows:)

From time to time since the inception of the National Defense Education Act, the Office of Education has received scattered reports of increased prices of scientific equipment, and we investigated all such reports. Naturally, they were disturbing to us in our administration of title III of the National Defense Education Act. On July 12, 1960, the Commissioner of Education alerted the State educational agencies, which are administering State plans under title III of the act, to the matter of price increases and invited them to report irregularities which come to their attention.

We are, of course, aware that there have been increases in the cost of equipment and materials purchased for education instructional uses. However, it might be pointed out that catalog list prices are not always a good index of actual selling prices, inasmuch as most catalogs contain the statement that "prices are subject to change without notice." In addition, selling prices sometimes vary in terms of purchasing practices, such as quantities of individual items purchased as well as the total amount of an individual order. Some companies, desirous of obtaining orders from new customers may quote larger discounts to the prospective customers than they would to customers with whom they have been doing business. Informal conversations with some suppliers indicate that, in their opinion, price increases are due to general increases in the cost of living as well as to increases in prices of basic materials used in the manufacture of laboratory apparatus and materials. Coupled with these factors have been general increases in labor and selling costs.

We have, nevertheless, analyzed the prices of some of the major equipment suppliers, comparing prices from 1954 through 1960 on items commonly purchased by schools under National Defense Education Act, title III. This study revealed that, in general, there has been a steady annual price increase.

In November of 1961, we made some additional comparisons of prices which were in effect during 1959, 1960, and 1961 on 60 selected items of equipment manufactured by two leading companies. We found the following:

For one company, comparison between 1961 and 1960 prices:

On 58 items, no price changes.

On two items, the prices were changed as follows:

Desiccator, reduced from $9.15 to $8.75.

Washington School rock collection, increased from $20 to $21.75.

Comparison between 1960 and 1959 prices:

On 15 items, no price changes.

On 35 items, there had been increases.

On one item, there had been a decrease.

On nine items, information was not available.

For the other company, comparison between 1961 and 1960 prices:

On 58 items, no increases.

On two items, there had been increases.

Comparison between 1960 and 1959 prices:

Sixteen items were not comparable in specifications for identification purposes.

On 21 items, no price change.

On 23 items, there had been increases—examples of two of these being as follows:

Wimehurst (electrostatic) machine increased from $87.50 to $95 (but the disk diameter had been increased from 12 to 14 inches).

Aquarium, increased from $18 to $21.50 (while the capacity had been reduced from 8 to 6 gallons).

One State has recently reported to us that a statement, which came to its attention to the effect that title III has simulated price increases, is not in accordance with information in that State and is injurious to many of the firms supplying scientific equipment. We were advised that a survey had been conducted in February of 1960 of the major firms doing business with the schools in that State. Listed were 35 items of equipment most commonly purchased with title III funds, and each company was requested to furnish the retail price for the items on January 1, 1954, January 1, 1957, and January 1, 1960. The findings, in general, were as follows:

1. Price increases have been moderate and, in general, have only kept pace with the cost of living index as published by the Bureau of Labor Statistics.

2. In many cases, a price increase accompanied a change in design or composition that improved the quality of the item.

3. For some items there was no increase in price during the survey period from 1954 to 1960.

The State official concluded that he had no reason to believe that any substantial unwarranted increase had occurred since 1960, but that the State was repeating its survey this month to secure more exact information. He pointed out that one of the problems which had been encountered was the use of old science apparatus catalogs by the schools. He stated that the normal price increase on many items has been from 3 to 5 percent per year; that, if a catalog is 3 years old, then the price is off from 9 to 15 percent; and that this is rapidly being remedied by more frequent publication of catalogs by the suppliers.

In September of 1961 another State reported to us concerning the matter of alleged price increases. On that occasion, the State superintendent stated:

"School personnel complaining about exorbitant price increases represent isolated cases. Many officials have verbally stated that because of large orders through competitive bidding, they have been able to buy at reduced prices.

"If we are realistic we know, of course, that prices of title III equipment have advanced. This is due in part, no doubt, to general price raises and perhaps in part to the unusual demand for these products. We do not believe, however, that any school district is paying unreasonable prices for equipment of this nature."

Senator PROXMIRE. You are familiar with former Harvard President Conant's book, "Slums and Suburbs"?

Mr. COHEN. Yes, sir; I thought it was a wonderful book.

Senator PROXMIRE. It is a great book, and one of the points he makes most persuasively is economic as much as sociological, and that is that of heavy unemployment among young people who have dropped out of school, and are not yet at work, particularly concentrating in big cities.

Mr. COHEN. Yes.

Senator PROXMIRE. Unemployment among youths is much less, and this is, I think, a lesson that we can perhaps get from it, in the small cities where there is a far better relationship between companies, trade unions, and the schools, so that when people graduate from high school they can get a job.

Now in view of the very heavy proportion of unemployment that is in the lower age ranges, I wonder if any thought has been given to, No. 1, greater encouragement to some kind of vocational education in the school and the tailoring of vocational education to the specific needs of the particular communities and, No. 2, the possibility of trying to persuade these schools to think about increasing the age of leaving school from 16 to 17 or 18.

After all, the legal age for school attendance has been a long-term trend, but it has not increased very much in recent years. As long as students are getting a useful education, it might help prepare them for work. It would be much better to have them in school than on the streets where they get in trouble and where they are unemployed.

Mr. COHEN. Senator, you raise a question that I think is of very high importance. Immediately last year, when we had our first discussions on the whole problem of education, the Secretary and I became convinced that there needed to be a wholesale reexamination of the whole vocational education program in the United States. While vocational education, which was started some 40 years ago, has done a great deal of good, it has not basically been reexamined and revalued in terms of the whole new development of automation and advancing industrial technology, as well as this problem of youth, school dropouts, urbanization, and delinquency.

Recognizing the tremendous scope of these developments and needs, and particularly because in the previous administration there even was a proposal for dropping Federal aid for vocational education completely, we appointed, at the request of the President, a very outstanding group of people to restudy the whole vocational education program. They are doing so now.

They have been meeting for some 3 or 4 months. They are a very outstanding group of people with representation from industry, agriculture, home economics, and education. We hope to have their report this year. On the basis of their recommendations, we are hopeful next year of coming back to Congress with a basic, and I hope a very far-reaching, change in vocational education to do some of the things that you had in mind. The present vocational education emphasis and provisions in my opinion are completely outdated.

Now with respect to the second part of your question, on youth employment, this is a very big one. Speaking as a parent with three sons in that age group, it is one that I have thought of many, many times myself, to see what we ought to be able to do.

We have undertaken some kind of a study to see what, if anything, the State laws provide on this score. This matter of employment of young people is very, very touchy. I was out in Madison about 2 or 3 months ago discussing this problem, and when I even mentioned the point that you are mentioning right now, I had practically all of my friends from the University of Wisconsin just jump on me about retrogression. You know, with respect to the possibility of giving youth more flexibility in employment during this intermediate period.

Not the question you raised of raising the age, but it seems to me part of that whole picture is giving young people an opportunity to work in various kinds of employment, maybe at 16, maybe at 17.

Senator PROXMIRE. While they are going to school?

Mr. COHEN. While they are going to school.

Senator PROXMIRE. With on-the-job training?

Mr. COHEN. Maybe on-the-job training. What I am trying to say is I don't think we have gotten the people together who have worked on that problem—the people in education, in the labor unions, and in vocational education. I hope that the report I mentioned earlier, will have something in it on this subject.

Senator PROXMIRE. You say there was a spontaneous adverse reaction to the notion of keeping them in school longer?

Mr. COHEN. No, I misled you. Not that point. I was discussing with them the question of giving them work opportunities at an earlier age, while they were still going to school.

Senator PROXMIRE. I see.

Mr. COHEN. So that as they moved out of education, they would move into the labor market with less friction.

Senator PROXMIRE. It would take time away from their academic life?

Mr. COHEN. Take time away. The issue came up of exploitation, child labor, adequate standards for young people in industry.

I am impressed with this point about school dropouts. The question arose this way: The typical problem, as I see it, is the young boy, particularly, for whom the normal academic education in our school today is completely uninteresting. He is, say, 14 or 15, and they are teaching him intellectual subjects for which at that particular point he has no interest at all.

They are giving him history, civics, English, or other subjects that we think are needed for a good education. As far as he is concerned, however, he is just sitting there, completely uninterested. He would like to be working on an automobile; he would like to be turning a lathe; he would like to be doing something manually with his hands vocationally. In short, he is the boy who may well drop out at 15.

The question I was directing to myself was: How can we do something about keeping that boy in school and give him the basic education, but also direct him into a vocational field where he will be able to support himself?

I think that is a very big problem, because that boy who drops out of school is very likely to be able to get a job at 15 or 16, somewhere, probably a pretty good job. He might even be able to make more money at let's say 16 or 17 when he drops out of school in relation to what his father can make, especially if his father is unemployed, or at a very low skilled level.

Senator PROXMIRE. Now this isn't the one that is the economic problem. What I am concerned about is the one who drops out at 16, at the minimum age, and who doesn't have any skill. He has no job and very little to offer his employer.

Mr. COHEN. That is right.

Senator PROXMIRE. Dr. Conant's point was that in some areas he found as many as 70 percent of those between 16 and 21 out of school and had no job, and, of course, they were a burden on the city. There were temptations for delinquency which were very great, and the destruction of personality is a very real one here. If a real effort, a successful effort had been made for any substantial number of these children to give them a vocation of any kind, it would have been a great contribution to them as human beings and also to society.

Mr. COHEN. Now you see though, Senator, merely raising the school-leaving age——

Senator PROXMIRE. That, by itself, I know, would not——

Mr. COHEN. By itself, as a matter of fact, that makes conditions even more difficult for the school system, because having a boy in class by requirement when he does not like what is happening, he becomes a disruptive influence in the educational system. That is the other side of the coin, and that is what led me to this—and I think this is in some respects borne out by what Dr. Conant says—that you have got to have a variety of educational experiences that fit different kinds of needs of these children.

Senator PROXMIRE. Well, my time is just about up. I would like, in the few seconds I have, to call attention to this chart you have got here. It is, as you say, enormously impressive.

As I calculate it, $95 billions is about one-sixth of our gross national product. I realize this isn't a fair comparison, because much of this isn't part of the gross national product, it is transfer payments, but I think it might be useful if you could adjust that for two things: No. 1, for price increases, so that you had constant dollars, and No. 2, for population increases, so that you get a per capita picture.

So we still have an impressive showing, this is almost a tripling. You have an increase of perhaps 75 percent, even if you allow for the price increases and allow for the increases in population. It would be a most encouraging and enlightening statistic if that were available.

Mr. COHEN. Yes, I believe we have some of that, which we can put in the record.

(The information requested is contained in the following table:)

Public and private expenditures for health, education, and welfare adjusted for population and price increases

Fiscal year	Total public and private expenditures for health, education, and welfare (millions of dollars)	Total population (including Armed Forces overseas) as of Jan. 1 (millions)	Per capita expenditures (dollars)	1947–49 dollars		
				Consumer price index (1947–49=100) (January)	Total expenditures (millions of dollars)	Per capita expenditures (dollars)
1950	35,165	[1] 150.6	234	100.6	34,955	232
1955	50,937	[1] 164.0	311	114.3	44,564	272
1960	80,440	179.4	448	125.4	64,147	358
1962	95,230	[2] 185.2	514	[3] 128.2	74,282	401

[1] Excludes Alaska and Hawaii.
[2] Estimated.
[3] December 1961.

Mr. COHEN. I may also point out that on some of these elements here there is already an inbuilt expansion on some of them for the future. I don't know how they will relate——

Senator PROXMIRE. I was going to come to that a little later, to ask you about 1970.

Mr. COHEN. All right.

Senator PROXMIRE. Representative Widnall.

Representative WIDNALL. Mr. Cohen, have you ever made any kind of a survey on dual jobholding? By that, I mean husband and wife holding jobs in cities as compared to suburban areas, as compared to farm areas, and its relationship to juvenile delinquency?

What I have in mind is this: I firmly believe that one of the problems today is the fact that there is no homemaker. There is nobody back there supervising the growth of the children within the home, and I do not think there is any governmental force that can step in in its place.

I am just wondering if there is anything by way of fact that can substantiate that thought on my part?

Mr. COHEN. I have never looked at the statistics of dual jobholding by husband and wife. The Census Bureau does have double jobs of individuals, but I don't know that they have, or I don't recall offhand seeing whether there are, any statistics with respect to husband and wife employment.

I will look that up and if we find it I will put it in.

Representative WIDNALL. I wonder whether or not there was more of that in the cities than in the suburbs, more in the suburbs than in the farm areas, where if the wife was employed, she was employed on the farm, where she still was with her children, and the relationship, possibly, of that to what had taken place by way of the growth of juvenile delinquency.

Mr. COHEN. I see. Well, I will look that up to see if we have anything.

(The information referred to follows:)

(The Department of Labor has published information on the marital and family characteristics of workers for March 1960 as follows:)

LABOR FORCE ACTIVITY OF MARRIED WOMEN

As previous surveys have shown, the age and presence of children most heavily influence the labor force activity of married women. Wives with no children of minor age are more likely to be in the work force than other married women of similar age. However, their overall rate of participation in March 1960 (34.7 percent) was somewhat less than that for women with school-age children only (39 percent) because of the inclusion of a large number of elderly women. Only 18.6 percent of the married women with children under 6 years of age were in the labor force. Mothers of small children had a somewhat higher participation rate if they also had children of high school age (23.8 percent) or if there were another adult in the family who could take care of the young children (about 30 percent for those who had a female relative 18 years old or over living with them).

Over the past 10 years, the largest absolute increase in labor force participation rates of married women was for those with school-age children only; they accounted for one-half of the total labor force increment among married women. The rise in labor force rates for the group with no children of minor age was dampened by the increased proportion of elderly women.

Labor force and marital status of ever-married women, by age and presence and age of children, March 1960

[Numbers in thousands]

Age of women and presence and age of children	All ever-married women			Married women, husband present			Other ever-married women [1]		
	Population	Labor force		Population	Labor force		Population	Labor force	
		Number	Percent of population		Number	Percent of population		Number	Percent of population
Total	52,355	17,114	32.7	40,205	12,253	30.5	12,150	4,861	40.0
No children under 18 years	25,952	9,096	35.0	16,426	5,692	34.7	9,526	3,404	35.7
14 to 34 years	2,737	1,694	61.9	2,273	1,389	61.1	464	305	65.7
14 to 24 years	1,512	871	57.6	1,304	748	57.4	208	123	59.1
25 to 34 years	1,225	823	67.2	969	641	66.2	256	182	71.1
35 years and over	23,215	7,402	31.9	14,153	4,303	30.4	9,062	3,099	34.2
35 to 44 years	2,347	1,385	59.0	1,836	1,011	55.1	511	374	73.2
45 years and over	20,868	6,017	28.8	12,317	3,292	26.7	8,551	2,725	31.9
45 to 54 years	(2)	(2)	(2)	4,582	1,968	43.0	(2)	(2)	(2)
55 years and over	(2)	(2)	(2)	7,735	1,324	17.1	(2)	(2)	(2)
Children 6 to 17 years only	12,037	5,120	42.5	10,477	4,087	39.0	1,560	1,033	66.2
14 to 34 years	2,148	977	45.5	1,854	768	41.4	294	209	71.1
35 years and over	9,889	4,143	41.9	8,623	3,319	38.5	1,266	824	65.1
35 to 44 years	5,799	2,531	43.6	5,144	2,051	39.9	655	480	73.3
45 years and over	4,090	1,612	39.4	3,479	1,268	36.4	611	344	56.3
Children 3 to 5 years, none under 3 years	4,848	1,326	27.4	4,438	1,114	25.1	410	212	51.7
14 to 34 years	2,837	834	29.4	2,586	691	26.7	251	143	57.0
35 years and over	2,011	492	24.5	1,852	423	22.8	159	69	43.4
Children under 3 years	9,518	1,572	16.5	8,864	1,360	15.3	654	212	32.4
14 to 34 years	7,845	1,281	16.3	7,297	1,100	15.1	548	181	33.0
14 to 24 years	3,021	528	17.5	2,768	429	15.5	253	99	39.1
25 to 34 years	4,824	753	15.6	4,529	671	14.8	295	82	27.8
35 years and over	1,673	291	17.4	1,567	260	16.6	106	31	29.2

[1] Includes widowed, divorced, and married, spouse absent. [2] Not available.

Source: "Marital and Family Characteristics of Workers, March 1960," Special Labor Force Report No 13, Bureau of Labor Statistics, U.S. Department of Labor. In Monthly Labor Review, April 1961.

The Children's Bureau, Social Security Administration, has made a study of child care arrangements of full-time working mothers. The survey was based on women in the labor force as of June 1958. The part of the report relating to mothers employed full time with children under 12 is as follows:)

MOTHERS EMPLOYED FULL TIME WITH CHILDREN UNDER 12

During the survey month, June 1958,[1] there were an estimated 2,873,000 women in the labor force who were working full time and had at least one child under 12. These women accounted for about 1 out of every 7 mothers in the country as a whole, and for about 1 out of every 2 mothers in the labor force, who had a child of this age. Thus, only about 53 percent of the women in the labor force with children under 12 were employed full time. Unfortunately, there are no data to indicate the extent and direction of changes in this proportion in the last decade. The fact remains, however, that nearly half of the mothers in the labor force in June 1958 who had children under 12 were working on a part-time basis or were unemployed.

MARITAL STATUS AND FAMILY SIZE

The large majority of the mothers with children under 12, and working full time in June 1958, were married women living in the same household as their husbands. There were 2,334,000 such, representing 81 percent of all mothers working full time with children under 12. Another estimated 231,000 mothers had husbands absent from home because of separation, service in the Armed Forces, hospitalization for mental illness, imprisonment, or who were not in the household for other reasons. Another 308,000 of them were either divorced from their husbands or widowed.

On the average, the number of children under 18 in the families of these mothers did not differ from the average number of children in all those families in the United States which have children. Both had an average of 2.3 children.[2]

Among them about one-third had 1 child, another third had 2 children each, nearly a fifth had 3 children each, and slightly more than a seventh had 4 or more children. Those mothers living in rural areas had a slightly higher average number of children than the mothers living in urban areas, 2.5 as compared to 2.2. Table 1 provides data on number of children by marital status of the mother.

TABLE 1.—*Mothers employed full time with children under 12—Marital status and number of children under 18, June 1958*

[In thousands]

Marital status	Total mothers	Mothers having specified number of children				Total children
		1	2	3	4 or more	
Total	2,873	931	951	534	457	6,665
Married	2,565	796	849	490	430	6,057
Husband present	2,334	700	778	458	398	5,570
Husband absent	231	96	71	32	32	487
Widowed or divorced	308	135	102	44	27	608

[1] The survey was conducted in June 1958 but questions about care of children related to May in order to cover arrangements at a time when most children were in school Therefore, some mothers working full time in June but not in May were excluded from this survey.

[2] See U.S. Department of Commerce, Bureau of the Census, Current Population Reports, Consumer Income, series P-60, No. 30, December 1958, table 6, p. 22.

CHILDREN IN SPECIFIC AGE GROUPS IN WORKING-MOTHER FAMILIES

When classified by the presence of children in the age groups under 6, 6 to 11 years, and 12 to 17 years, the largest number of families with children under 18 in the United States are those with children under 6 years of age only; the next largest number are those with at least one child under 6 and one between 6 and 11. As might be anticipated, the families with at least one child under 6 have less representation proportionately among women in the labor force than those without such children. Only one exception precludes the generalization that mothers with children under 6 are less likely than mothers with children 6 or more years old to be in the labor force and working full time. The exception is the mother who in addition to having a child under 6 also has one who is 12 to 17 years old. This is indicated by the data in table 2, which show that about 1 out of every 10 women in the United States with children under 6 only or in addition children 6 to 11 years old is employed on a full-time basis. The ratio for women with children 6 to 11 years old only or in addition children 12 to 17 is about one out of every five. The data also indicate that about 7 out of every 10 women in the labor force with children under 6 and 12 to 17 are employed full time.

Urban-rural differences in the presence of specific age groups of children are not significant. In both areas about 51 percent of the women have at least one child under 6. The most notable difference is that a higher proportion of mothers in rural areas than in urban areas also had a child 12 to 17 years old.

TABLE 2.—*All mothers in the labor force and mothers employed full time with children under 12: Labor force participation rates, by presence of children in specific age group*

Specific age group	Number of mothers [1] (in thousands)			Percent of civilian population	
	In civilian population	In total labor force	Employed full time	In labor force	Employed full time
No children under 6	11,297	4,647	(2)	41.1	(2)
Some 6–11 only	3,433	1,356	713	39.5	20.8
Some 6–11 and 12–17	3,239	1,205	708	37.2	21.9
Some 12–17 only	4,625	2,086	(2)	45.1	(2)
Some children under 6	14,146	2,847	1,452	20.1	10.3
Under 6 only	6,600	1,350	697	20.5	10.6
Some 6–11	5,018	897	438	17.9	8.7
Some 12–17	586	156	109	26.6	18.6
Some 6–11 and 12–17	1,942	444	208	22.9	10.7

[1] Unpublished data on civilian population and on total labor force as of March 1958 from Bureau of the Census.
[2] Not available.

Mothers working full time who reside in the Northeast are more likely to have children in the older age groups. About 42 percent of them have a child who is 12 to 17 years old. The proportion of mothers in the other regions with a child of this age range from 32 to 36 percent. Conversely, the proportion of working mothers in the Northeast all of whose children were under 6 was lower than that for the other regions. In addition, a smaller proportion of them have a child 6 to 11 years old as well as one under 6, than is the case with mothers in the other areas. This suggests the possibility that mothers in this region with young children are not as prone to enter the full-time working labor force as are such mothers in other regions.

TABLE 3.—*Mothers employed full time with children under 12: Presence of children in specific age group, and residence, June 1958*

Specific age group	Total mothers	Regional residence				Urban-rural residence	
		North-east	North-central	South	West	Urban	Rural
Number ... thousands	2,873	633	684	1,061	495	1,823	1,050
Percent distribution	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Under 6 only	24.3	21.2	24.1	26.1	24.4	25.8	21.5
Under 6 and 6 to 11	15.3	11.0	17.3	16.2	15.9	14.6	16.3
6 to 11 only	24.8	26.1	22.5	24.2	27.7	26.3	22.3
Under 12 and 12 to 17	35.6	41.7	36.1	33.5	32.1	33.3	39.9

OCCUPATIONAL GROUP, COLOR, AND MARITAL STATUS

Of all the women in the labor force in March 1958 who were or had been married, the largest proportion were clerks or sales personnel and the smallest proportion were farmers or farm laborers. This holds true, also, for the mothers who were employed full time in June 1958 with children under 12. There were some differences, however, in the distributions of these groups by occupational categories, as indicated by the data in table 4. There was a higher proportion of clerks and sales personnel and a lower proportion of women in professional and managerial positions among the women employed full time in June 1958 with children under 12 years of age than among the total group of women in the labor force in March 1958 who were or had been married.

Among the white mothers employed full time with children under 12, the largest proportion were clerks or sales personnel; among the nonwhite the largest proportion were household or service workers. Another difference in the distribution of the white and nonwhite mothers is that among the former there is a larger proportion in professional and managerial positions than among the latter. Farmers and farm laborers are represented to a greater extent among the nonwhite mothers than they are among the white mothers. The proportion of women who are craftsmen, operators, or laborers in each group is about the same.

As the data in table 4 show, the most significant differences between mothers who are married with husband present and those of another marital status, is that among the former there is a higher proportion of women who are farmers or farm laborers than among the latter and a lower proportion of women who are private household or service workers.

TABLE 4.—*Mothers employed full time with children under 19—Occupation, color, and marital status June 1958*

Occupation of mother	Ever-married women in labor force March 1958 [1]	Mothers employed full time with children under 12				
		Total	Color		Marital status	
			White	Non-white	Married, husband present	Other
Number ... thousands	15,475	2,873	2,468	405	2,334	539
Percent distribution	100.0	100.0	100.0	100.0	100.0	100.0
Professional and managerial	16.9	13.3	14.3	7.4	13.7	11.5
Clerical and sales	35.0	39.1	43.8	10.8	39.1	39.4
Craftsmen, operators, laborers	18.7	19.6	20.1	16.1	19.7	19.1
Private household or service workers	25.9	21.6	17.0	49.6	20.1	27.8
Farmers or farm laborers	3.5	6.4	4.8	16.1	7.4	2.2

[1] U.S. Department of Commerce, Bureau of the Census, Current Population Reports, Labor Force, Series P-50, No. 87, January 1959, p. 15.

REGIONAL AND URBAN-RURAL RESIDENCE

About two out of every three of the mothers resided in an urban area. Regionally, this ratio varied. In the South, the 1,061,000 mothers were about equally divided between those residing in urban areas and those residing in rural areas. In the North-Central States and in the West, about 7 out of every 10 mothers resided in urban areas, while in the Northeast about 3 out of every 4 resided in urban areas.

TABLE 5.—*Mothers employed full time with children under 12—Regional and urban-rural residence, June 1958*

Region	Total mothers	Percent distribution		
		Total	Urban	Rural
Total	2,873,000	100	63.5	36.5
Northeast	633,000	100	74.2	25.8
North-Central	684,000	100	69.4	30.6
South	1,061,000	100	50.6	49.4
West	495,000	100	68.9	31.1

Mr. COHEN. Let me express myself, though, on the point that you mentioned.

As a parent myself, I think that one of the most tragic conditions in the United States is where children come home from school at 3:30, 4, or 5, and there is nobody home until 6:30 or 7. As a parent myself that is something that I just couldn't stand for in connection with raising my own children.

I think to the extent that there are families—and I know there are many, many such families—where the children are completely unattended for 2 or 3 hours in a day, where there is no adult supervision, direction, or motivation, a very, very unfortunate situation results.

Representative WIDNALL. The second thing, the emphasis in comparing Soviet education and ours here in the United States, has been on the growth of the engineering sciences within Russia as compared with over here.

Today, I suppose they are graduating two to three times as many as we are. When it comes to physics and chemistry, we are still graduating more people in physics and chemistry here than they are there, and far more in the liberal arts than they are there, because they have no concentration on the humanities. Isn't that so?

Mr. COHEN. That is correct. I don't recall the figures in detail, but, if you will look at the table I was talking about, when you get down to the end product, the residual group in the humanities, we train more than they do. That is simply because they have redirected the whole of the total more toward engineering and other fields.

Representative WIDNALL. So that it has been a question of national emphasis, not really so much as how many are graduating?

Mr. COHEN. That is right, but now you raise a very great problem that we in the Department have thought about. In the United States, education is decentralized, as it probably should be, to the States and localities, to the colleges and universities. There is very little opportunity for us to promote the national interest, except through one device, the only device that I know of that we can effectively have at the national level, and that is scholarship money which indicates some kind of a priority or preference that the Congress decides is in the national interest.

Representative WIDNALL. Of course, in Russia, the emphasis is on the fact that not everybody can have a college education. It is for the top people——

Mr. COHEN. That is right.

Representative WIDNALL. The top people, and then in return they have got to give something back to their country for giving it to them.

Mr. COHEN. That is right, but don't forget that there is something in the Russian system that none of us would want to duplicate here. Take that young spaceman. When he was a young fellow out in Siberia somewhere, they saw that he was an enterprising, able fellow. His teacher recommended him and saw that his university training was all paid for. By these recommendations, he was just taken out of his home community, I don't know whether he wanted to go or not, but anyway, he left this small Siberian community and went to the University of Moscow or some other one there in the metropolitan area and was given free education to become what they thought and what he thought was desirable.

Now in our educational system, we cannot do that except through incentives, and that is why it seems to me scholarships and this other aid, both public and private, are important, because it is the only way of expressing the national interest.

Representative WIDNALL. Now again in the educational field, to what extent are applications duplicated with respect to college entrance? Now I know person after person who applies to five or six or seven colleges, and this college can say they have got 5,000 applications, this one 6,000, this one 3,000, when actually these are just second, third, fourth, and fifth choices, if the same names are on each list.

Mr. COHEN. That is right.

Representative WIDNALL. Now doesn't this give a false figure with respect to the real demand on going to college here in the United States?

Mr. COHEN. Yes, I don't think you should look at the total applications. I know that most teachers in high schools are saying "please don't apply to more than four institutions," because it has all become such a big paperwork job for the institutions and for the high schools which have to make out the papers.

On the other hand, let's look at it from the standpoint of the individual and the parent. When I was at the University of Michigan, along in April or May I would get telephone calls from parents who were friends of mine, saying that a son or daughter, who was an A student had applied to three eastern colleges or universities, but couldn't get in. "Is there something that you could do to see if you could help me get into the University of Wisconsin, or the University of Michigan?"

From the parent's standpoint, failure not to apply in a number of places would be very——

Representative WIDNALL. Mr. Cohen, of course they should make as many applications as possible, but it could give us a distorted notion of the demand for a college education.

Mr. COHEN. That is correct, that is why you should look at these kind of net figures shown on the chart, here, where this has nothing to do with the bodies that you have to find a place for in the educational system.

Representative WIDNALL. Just one more question. I would like to get back to another field. This has to do with social security.

Now, I believe I briefly discussed this with you when I saw you the last time. As I understand it, social security was originally set up as an insurance system. Today, it seems to me it is more and more of a welfare program, as you relate the needs test to the ability to get social security.

I find in my office that the greatest demand today from those who have gone on social security, is to have the ability to earn more, now that they are on social security.

Because of the change in the expectancy of life, the improvement in health of older people, and the enforced retirement of those people in certain areas, lots of them will be forced to suffer from inaction. They will have the feeling, that if they take a job they will lose their benefits.

Most of them want to see that ceiling lifted, and I sense from some of your earlier remarks that you feel that we are going to have to adopt a more realistic figure today than we have at the present time. How much of an impact would raising the figure, say from $1,200 to $1,800, have on the social security system?

Mr. COHEN. Well, I don't believe I have the exact figures with me. About raising that from $1,200 to $1,800, I will put the exact figure in the record, but it would involve an increase of, I would say in the neighborhood of maybe an eighth or a quarter of a percent a payroll.

However, let me put it this way: My preference would be, if we are going to modify the retirement tests, and I do believe that some modifications are necessary to reflect the situation, it would be better to modify the other provision in the work test which I believe, as I recall now, goes up to something like $1,700, in which you can get half of your earnings not taken into account as you work above $1,200.

It seems to me that would be a better way of doing it. Give the person an incentive to earn more, by not taking away benefits equivalent to earnings let's say, above the $1,700 level. Go up to, let's say, $2,400.

In other words, if you want to give an incentive, which I think is probably what you have in mind, a better result could be by raising that second level.

(The following information was supplied:)

To increase the present $1,200 earnings amount, below which no benefits are withheld, to $1,800, and to provide that, as at present, benefits withheld could be equivalent to one-half of earnings in excess of this amount up to $500, and that above the $500 amount benefits would be reduced by the same number of dollars that earnings were higher, would increase the costs of the old-age survivors and disability insurance program by approximately one-fourth of 1 percent of taxable payroll on a level premium basis.

Representative WIDNALL. Well, I am a little bit amused because on some pieces of social legislation, if I happen to be for something which really involves what you might call a needs test, say on pension legislation, I get slammed for saying, "You have got to take a pauper's oath in order to qualify."

Well, it is almost reaching the point now in social security where you have to go take a pauper's oath in order to qualify for social security.

Mr. COHEN. Well, let me differ from you there, Congressman, in this respect: the basic concept behind social security, as well as with any retirement system, is the test of retirement.

No civil service retirement system or any such retirement system when it is set up is to replace the wage loss that occurs, and economic loss due to retirement. Now what Congress has done in the retirement test is put a dollar value on an economic test of retirement. We might think that is too low, but I don't think it is a pauper's test or an income test. It is a dollar evaluation of what is the line of retirement.

In other words, if the original law of 1935, which almost said that in order to retire you have to be not working at all, were to still be the law of the land, which was what the Congress had in mind then, why, none of these people could do any work whatsoever. Periodically, Congress has revised that position, and I think rightly so. So my only point now is that it is not an income test—that is, not a pauper's oath; that is, not a means test—it is simply an economic evaluation of the dividing line between retirement and work, and I think Congress quite appropriately should redefine that level in relation to the labor market at any given moment.

Representative WIDNALL. But you do believe that we should modify the present setup, in view of present conditions and present earning conditions, present circumstances?

Mr. COHEN. Let me put it this way: I think we should modify it. Of course, in relation to dealing with the cost, as you yourself indicated, what would have to be added on to the cost to keep the insurance system in actuary balance.

Representative WIDNALL. Thank you.

Senator PROXMIRE. Mr. Cohen, on that last point, I have observed on the basis of the hearings we have had since the middle of December that these transfer payments, and especially social security, play a very great role in unemployment by affecting the supply of labor and keeping the supply of labor lower than it otherwise would be.

It is not just a matter of statistics; it is a matter of recognizing that there is already pressure on available jobs, and I can see that there are real values in encouraging people to retire, unless they are willing to take some cut in social security if they continue to work.

I would like to ask you about this chart, where we left off. First, I notice that since 1950, there has been a greater increase in the cost of health services than any other element in the cost of living. Is that correct?

The New York Times reported this, I think.

Mr. COHEN. Generally speaking medical costs have risen faster than the overall cost of living since the 1957–59 index.

Senator PROXMIRE. Can you think of any other important element, significant element, in the cost of living that has risen faster?

Mr. COHEN. I believe there is one small element in the cost of living that has risen as fast.

Senator PROXMIRE. Substantial or significant element?

Mr. COHEN. None. As a matter of fact, though, when you come to it, and on this perhaps you may have another question, there is one element in the medical care index that has risen the fastest of any element in the whole index, and that is hospital services.

Senator PROXMIRE. I see. I was going to say that there is some feeling that quality of medical care has increased, and that that can't be measured very well statistically, and that therefore the statistics may overstate the increased cost of similar medical care.

Mr. COHEN. Well, there is no question that the medical care being given in 1960 is a different package of medical care than in 1950. There are different drugs, and there are different procedures. The length of stay in hospitals is different. Certainly if you go back 15 years, I would say you can hardly compare the two. They are two different programs, almost.

Senator PROXMIRE. Now can you give us any notion of the kind or the size of this Health, Education, and Welfare—well, the total cost to the public in 1970? It is now $95 billion, you say?

Mr. COHEN. Yes.

Senator PROXMIRE. About one-sixth of the gross national product. Now what would it be, in your judgment, in 1970?

Mr. COHEN. You are asking me for the whole total, or medical care?

Senator PROXMIRE. The whole total?

Mr. COHEN. Well, let me say this first: it has been going up. It went up from $88 billion, in 1961, to $95 billion in 1962. That is about $7 billion. It went up about $8 billion from 1960 to 1961.

Now if I were to make an estimate that was based upon knowing what this problem is in education——

Senator PROXMIRE. Knowing what the——

Mr. COHEN (continuing). And knowing what is probably going to happen to hospital costs during this next 10 years, I would say——

Senator PROXMIRE. Then might I say that may be almost as big as would be the increase in social security payments.

Mr. COHEN. Yes.

Senator PROXMIRE. The biggest increase by far in personal income in the last 8 years has been in transfer payments, which as I understand increased 150 percent, as compared to wages, which have increased about 50 percent.

Mr. COHEN. Well, we went up from $35 billion in 1950 to, let us say, $100 billion in 12 years. That is a tripling, with a price factor about 22 percent, or something like that, in that interval, so you had $70 billion, and I would say the net increase was at least in the neighborhood, by present prices, of maybe $50 billion.

So that I would say that, at a minimum, in 10 years public and private health, education, and welfare expenditures would be close to $150 billion. While I think the total will be higher than that, I am on the conservative——

Senator PROXMIRE. That assumes price stability?

Mr. COHEN. And I am assuming price stability; yes. Let me give you one statistic. In 1946, average hospital costs per patient-day in the United States were $9.39. At about the Korean war, they were

$15.26 a day. At the present time, the average for the United States is $32.23 a day for 1960. They have doubled in one decade. Whereas you might say the general price index increased about 25 percent, hospital costs quadrupled.

Now every study that I have seen concerned with hospital costs in the United States indicates that hospital costs, without any change in the situation, are going to continue to go up. Cumulatively, they may rise 50 percent or more in a decade. A 50-percent increase would mean that by 1970, hospital costs on the average would be approaching $50 per day.

Now if that is so, that element, that $31 billion for health, may be a bigger figure 10 years from now than what I have allowed in my estimate.

Senator PROXMIRE. Now what are the reasons for this, what are the ingredients for driving this up so fast?

Mr. COHEN. Well, there are several ingredients, Senator.

First, hospital costs start from a much lower base, let's say back in 1930, than practically any other large quantity of service. Hours of work were, let's say, in the neighborhood of 60 or more. Wage rates were very low, and hospital labor was unorganized. Then coming into the 1940's with the outbreak of war and competition for womanpower and manpower, plus unionization in many cases, in order to keep the hospital staff, they had to raise the wage level. Hospital costs are about 60 to 70 percent wages, and in order to hold these people, to get technicians and to get nurses, there was no other way but to raise the wage level.

Secondly, the tremendous amount of technical equipment and technical staff that is needed to run a hospital.

Senator PROXMIRE. Do you allow for the efficiency factor? Elsewhere you have had this same increase in wages of 50 percent or so in almost everything else, but elsewhere we have had far less price increases?

Mr. COHEN. That is right, but we have some efficiency factors here. For many kinds of stays in hospitals, the number of hospital days per illness is substantially less than they were two decades ago. Take childbirth, for instance. Whereas, let's say 20 or 30 years ago, 10 to 14 days was the average confinement; now, it is usually half that long. Similarly with appendectomies, and quite a number of other conditions. So, while the per patient day costs have gone up, there have been some efficiencies.

On the other hand, there have been many more admissions to hospitals. In 1930 something like two-thirds of the children were born in hospitals, whereas today, almost all babies are born in hospitals, and this has created a great deal more pressure on hospital admissions.

On this economy point, the average length of hospital stay was 15.3 days in 1931. It was about 9.6 in 1959. So you see there has been an increase in efficiency as a result of the technological equipment and knowledge.

Senator PROXMIRE. Well, there probably has been some incentive, too, in the costs which are so great people can't afford to stay in the hospital as long as they used to.

Mr. COHEN. Well, there may be something to that.

Senator PROXMIRE. Two and a half times greater, now, you said, than it was in 1946: $32 a day, compared with $9 a day in 1946.

Mr. COHEN. I said—yes, I see what you mean, $9.39 compared with $32.23 in 1960. Is that what you were referring to?

Senator PROXMIRE. That is a real incentive for making your hospital stay shorter.

Mr. COHEN. Well, on the other hand, though, keep in mind that we have had the introduction of a wholly new factor, and that has been the large-scale development in the last few years of voluntary health insurance, which has eliminated for many people part, if not all, of the financial barrier, which is a good thing.

Senator PROXMIRE. Well, let me just say part and only part of the coverage, because—and you give me the figures right now—you don't get anything from Blue Cross like a hundred percent coverage over your hospital stay. You are lucky to get half of it. Am I right?

Mr. COHEN. Well, I remember we have a statistical study here which shows which part of the hospital bill is taken care of by insurance. It is very interesting. I have a little analysis here which we can put in the record on that point.

Senator PROXMIRE. It will be put in the record, without objection.

(The material referred to follows:)

HOSPITAL INSURANCE AND PROPORTION OF HOSPITAL BILL PAID BY INSURANCE[1]

HOSPITAL INSURANCE COVERAGE

Two-thirds of the civilian noninstitutional population of the United States was covered by some form of hospital insurance in the latter half of 1959.

The proportion of the population covered by hospital insurance was generally highest in the Northeast and North Central regions and lowest in the South. The proportion covered in the West was between the extremes and somewhat below the national average.

Hospital insurance was held by 72 percent of the population in urban areas as compared with 68 percent in rural-nonfarm areas and 45 percent in farm areas.

Persons in the age range in which the working population is concentrated (25–64) were more likely to have health insurance than children or old people. Among persons age 65 and older, approximately 46 percent were covered by some form of hospital insurance.

In families where the income during the previous 12 months was under $2,000, approximately 33 percent of the persons had hospital insurance. But in families with the highest income, $7,000 or more, 84 percent had such insurance.

PROPORTION OF HOSPITAL BILL PAID BY INSURANCE

Among all patients discharged from short-stay hospitals in the 2-year period July 1958 through June 1960, 68 percent had some portion of the hospital bill paid by insurance, and 51 percent had three-fourths or more of the bill paid. About three out of four persons who reported some insurance payment had 75 percent or more of the bill paid.

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[1] The facts set forth in this digest are from two recent health statistics publications of the Public Health Service, U.S. National Health Survey: (1) "Interim Report on Health Insurance," PHS Publication No. 584–B–26, December 1960, based on 19,000 nationwide household interviews conducted during the period July–December 1959; and (2) "Proportion of Hospital Bill Paid by Insurance, Patients Discharged From Short-Stay Hospitals," PHS Publication No. 584–B–30, November 1961, based on 5,000 household interviews from July 1958 through June 1960.

Geographic region

The proportion of discharges for which some part of the bill was paid by insurance was higher in the Northeast and North Central regions (74 percent) than in the South (64 percent) or West (56 percent).

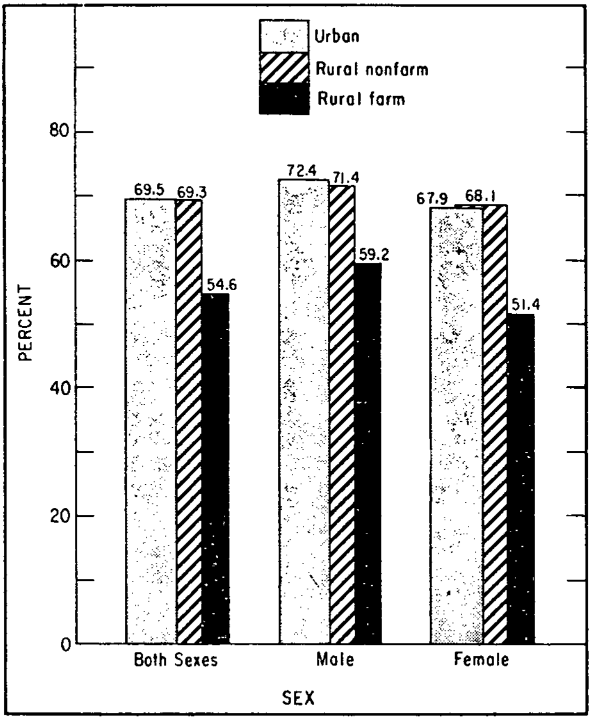
Race

About 71 percent of white persons discharged from hospitals had some portion of the bill paid by insurance. For nonwhite persons the rate was 42 percent.

CHARACTERISTICS OF PERSONS WHO HAD PART OR ALL OF HOSPITAL BILL PAID BY INSURANCE

Urban-rural residence

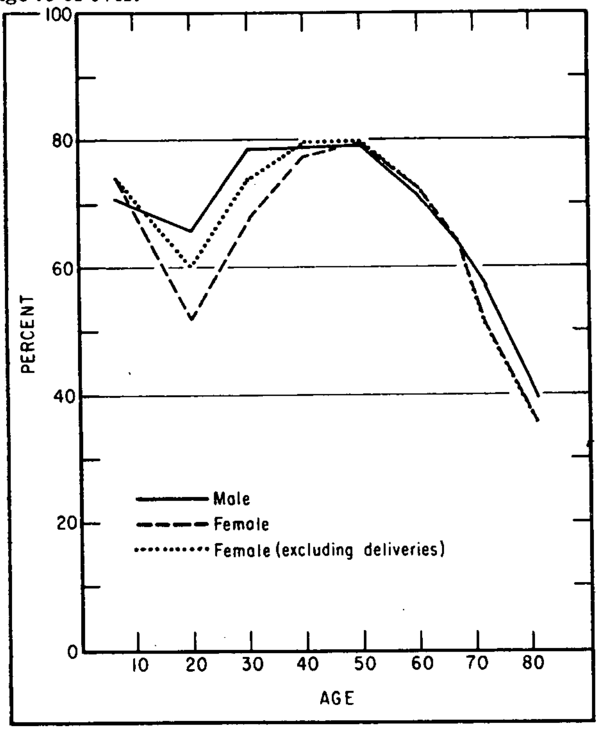
The proportion of hospital discharges for which some part of the bill was paid by insurance was about the same for residents of urban and rural nonfarm areas (69 percent). However, the rate for residents of rural farm areas was much lower (55 percent).



Percent of hospital discharges with some insurance payment for the hospital bill by sex and residence

Age and sex

Between 70 and 80 percent of persons below age 65 (with the exception of the age group 15–24) had some portion of their hospital bill paid by insurance. Of persons 65 years and over, about 53 percent of men and 49 percent of women had some part of the bill paid. After age 65 the proportion of hospital discharges with some insurance payment dropped sharply, from about 63 percent for both men and women age 65–69 down to 39 percent for men and 36 percent for women age 75 or over.



Percent of hospital discharges with some insurance payment for the hospital bill by sex and age.

Percent of persons discharged from short-stay hospitals who had insurance payments for the hospital bill

Sex and age	Total discharges: Percent with any insurance payment for the bill	Total discharges: Percent with ¾ or more of bill paid by insurance	Percent of discharges with any insurance payment who had ¾ or more of the bill paid by insurance
Both sexes:			
All ages	68.0	51.3	75.4
Under 15	72.1	58.3	80.9
15 to 44	66.9	50.6	75.6
45 to 64	76.0	58.0	76.3
65 and over	51.2	30.3	59.2
Male:			
All ages	70.6	55.7	78.9
Under 15	70.7	57.0	80.6
15 to 44	74.7	62.2	83.3
45 to 64	75.5	59.1	78.3
65 and over	53.1	33.4	62.9
Female:			
All ages	66.4	48.7	73.3
Under 15	73.9	59.9	81.1
15 to 44	64.5	47.1	73.0
45 to 64	76.4	56.9	74.5
65 and over	49.3	27.3	55.4

Work

About 79 percent of all persons who usually work had some part of the hospital bill paid by insurance. Persons age 65 and over who usually work had about the same proportion (80 percent) of hospital discharges with some insurance payment of the bill as did younger usually working persons. Nearly one-half (45 percent) of retired persons age 65 and over had some portion of the bill paid by insurance.

Income

The higher the family income, the larger the proportion of discharges for which some part of the hospital bill was paid by insurance. In families with incomes under $2,000 a year, two-fifths of the persons discharged reported that at least some part of the hospital bill had been paid by insurance. The rate increased from 59 percent for the $2,000–$3,999 group to 79 percent for the $4,000–$6,999 group and to 81 percent for the $7,000-and-over group. However, for persons age 65 and over whose annual income was $7,000 or more the proportion of discharges for which some part of the hospital bill was paid by insurance (51 percent) was the same as that for all income groups age 65 or over.

Percent of discharges with some insurance payment for the hospital bill by annual family income

Sex and age	Family income (percent)					
	All incomes	Under $2,000	$2,000 to $3,999	$4,000 to $6,999	$7,000 or more	Unknown
Both Sexes:						
All ages	68.0	39.6	59.2	79.0	81.0	58.8
Under 15	72.1	32.9	59.4	81.1	80.4	71.9
15 to 44	66.9	33.0	54.7	78.0	81.3	51.2
45 to 64	76.0	50.1	71.7	83.8	89.0	69.4
65 and over	51.2	42.7	59.8	63.5	51.1	45.6
Male:						
All ages	70.6	41.2	62.8	81.7	83.3	64.1
Under 15	70.7	31.1	56.4	79.3	83.6	68.5
15 to 44	74.7	45.2	63.0	85.0	85.7	63.8
45 to 64	75.5	45.8	69.6	84.5	87.6	66.5
65 and over	53.1	39.5	62.2	65.7	58.0	54.1
Female:						
All ages	66.4	38.6	57.1	77.5	79.5	56.1
Under 15	73.9	35.5	63.3	83.2	77.0	75.5
15 to 44	64.5	29.3	52.0	75.9	79.8	47.4
45 to 64	76.4	53.4	73.7	83.2	90.7	71.0
65 and over	49.3	45.8	56.8	61.0	42.5	40.1

Mr. COHEN. It indicates that of the people discharged from the hospital in the 2-year period, June 1958 through June 1960, only about 50 percent had three-fourths or more of their hospital bill paid by insurance. When you get to the people aged 65 and over, only 30 percent had that much of their bill paid by insurance.

There is still, as you say, a lot of the hospital bill, even when you have insurance, that is not paid.

Senator PROXMIRE. One of the factors that is likely to increase it, if we pass the bill—which I thoroughly favor—which the administration has been pleading for, the Anderson-King bill, then there will be hospitalization taken care of for many of our people over 65. There again you will have a demand factor that will tend to drive up the cost, just as the health insurance proposal did in the past, only more so.

Mr. COHEN. Yes, although I constantly make the point, sir, when that factor is made as an objection to the Anderson-King bill, that, to the extent that voluntary insurance insures more of these people, demand also increases. This demand factor is just as much an element in the spread of voluntary insurance as it would be if the Anderson-King bill were enacted.

I agree with your point that there is a demand push there. That is probably important, because the way society is developing, we would like everybody who needs hospital care and who can be admitted by a physician to have it without regard to the financial barrier at the time they are sick.

Senator PROXMIRE. Apropos of this whole situation, do you think medical care quality has increased so much that there is really less inflation than the Consumer Price Index indicates?

Mr. COHEN. Well, the trouble is with the Consumer Price Index; I don't think the Consumer Price Index—and I have talked with Mr.

Clague about this several times—I don't think the Consumer Price Index is a satisfactory indicator at the present time of price, and certainly not of quality in medical care.

Senator PROXMIRE. We have had some of the best academic specialists in the country—I am chairman of the Subcommittee on Statistics—testify before us on this. We have had the users come in, from industry, labor, from every source, the top professors in the country, and they universally agree that we have the best statistics in the world; they will agree that there is some small distortion on the basis of quality.

They agree that it is rather slight; and perhaps the increase that we had last year in the cost of living was no increase at all—because it was only one-half of 1 percent—that might be accounted for by quality improvement. They seem to feel very strongly that these statistics are accurate, reliable, and pretty much indicative of what is going on. Would you dispute that?

Mr. COHEN. You are talking about the Consumer Price Index statistics?

Senator PROXMIRE. Yes, indeed. We had hearings on that last year.

Mr. COHEN. Unfortunately, since I have been down in Washington I haven't had a chance to read as many of these kinds of reports, which I had ample opportunity to read a year before, so I am not acquainted with them—but I have always felt that on the quality of medical care, there are so many other aspects to consider.

Take, for instance, this matter of the duration of stay. I don't know how you reflect that, except through an independent series. I don't know how you reflect this element. Take, for instance, another important fact; namely, that many more terminal illnesses are probably hospitalized now than they might have been in the past. You see, that is all involved when you say "quality"—I am talking about the consumer, now, not as a medical man, because I wouldn't be competent to judge—and I don't know how you would evaluate all those.

I have no doubt that you are going to spend a lot more money on many of these areas, and I think quality will have been improved in the sense that people will have more units of medical care. I think that an element of the quality of medical care is the frequency with which a person in the course of a lifetime sees a physician. The more times he visits the doctor the more likely there will be prevention. I think that is an element in quality, too.

Senator PROXMIRE. Now, I have a series of questions on which I will try to be as brief as I can.

No. 1, do you have any estimates on the contributions that the social security system and the welfare programs make to antirecession policy by maintaining consumer purchasing power?

Mr. COHEN. Well, of course the program in the Social Security Act that is most sensitive to change in economic conditions is unemployment insurance. And in both the 1958 recession and in the most recent recession, it was very important.

However, I don't think the unemployment insurance system makes its maximum contribution. I think that an improved unemployment insurance system could provide at least a billion or 2 billion more a year now in a recession than it has with the present limited duration and amounts of benefits.

Now the social security system itself, I think, was quite important in the last recession, because as you know, one of the first things we did last year was to make six changes in the social security system. One of the important ones was to reduce the age for men from 65 to 62 on an actuarial basis. However, this same fill-up effect wouldn't have as much value in future recessions, because it will already be part of the structure. Nevertheless, it would give the individual who became unemployed an opportunity to get his benefits.

I would say those are the two areas in which the system can have a significant antirecessional effect.

Senator PROXMIRE. You notice that in 1954, when wages increased very little due to the recession, transfer payments went up $2 billion, and that in 1958, when we had another recession, transfer payments climbed nearly $5 billion; and they have been proceeding at such a tremendous pace, right in the heart of recessions, and so much of this is social security payments, it seems to me that the role is enormously important.

Probably, the social security and unemployment compensation together are more important than any kind of antirecessional action that the President might take with a tax cut.

Mr. COHEN. With respect to social security and unemployment insurance there are two points that should be stressed. One is that both of those programs go into effect almost automatically with no legislative action. Insofar as an individual is concerned, he can get his unemployment insurance, if he is unemployed, or his social security, if he is over the age, immediately, without any other action by Congress. The trust funds and the availability of those funds are important.

Secondly, what is frequently overlooked is it is highly individualized. If a particular locality is adversely affected, individuals can apply either for their social security or for their unemployment insurance. So it has both a global effect on the economy, and, what I think is perhaps even more important, it sustains the buying power, security, and confidence of that individual in that community at a point of crisis. This is very significant. Likewise it is self-operative.

The effects of unemployment compensation would be improved by adoption of the President's proposal for extending and strengthening the unemployment insurance program.

Senator PROXMIRE. Very good. Thank you.

Now I have a series of questions. In view of the lateness of the hour, and your great patience, I believe I would prefer to read them right now for the record, and you can supply answers for the record, if that is satisfactory with you.

Mr. COHEN. Certainly.

Senator PROXMIRE. First, does the drop in retirement age as provided by OASDI have any labor force implications?

Administration antirecession program, the standby capital improvements measure, what does the Department see as its role and what would it believe the impact would be on health and educational facilities?

This has to do with hospitals and schools to some extent.

Then does the Department do any analysis on costs of particular diseases, illnesses, and so forth, and economic benefits from their cures, eradication, and elimination? What are the results of such analysis?

What are the needs of the vocational rehabilitation program whose results seem most impressive?

Then, what effects do recessions have on State and local welfare budgets and on their health and education long-term growth benefits?

What is the optimum physician population ratio? Can new organizational arrangements help reduce the ratio?

And what is the relationship between income distribution and availability and utilization of physicians?

And what are the prospects for increasing the productivity of physicians and health personnel, teachers and other educational personnel?

Can you tell us how the decisions are made on the composition of Government security portfolios held by trust funds such as the social security trust funds? I am particularly interested in the monetary impact, whether in long term or short term, and so forth.

(The following answers were supplied:)

Question: Does the drop in retirement age as provided by OASDI have any labor force implications?

Answer: A preliminary 16-week tally of claims for benefits reported between September 8 and December 28, shows that nearly two-thirds of the men applying for reduced benefits before age 65 were not employed at the time of their application, as compared with only two-fifths of the men 65 and over. Furthermore, the data show that the proportion of male applicants who were not employed but looking for work exceeded one-third in the case of those 62 to 64, but was under one-fourth for older men.

Through December 22, 275,000 men 62 to 64 years of age had applied for benefits. At the end of November, 229,000 were already on the rolls.

These data suggest that persons taking advantage of the early-retirement provision are more likely than men 65 and over to have been out of work and to be looking for work. It should be recognized, however, that the difference between persons under and over 65 may be minimized when the early-retirement provision has been in effect for a longer period.

It is also too early to tell whether the provision for retirement at reduced benefits under OASDI will encourage use of early-retirement provisions under private pension plans.

Question: What does the Department see as its role and what does it believe the impact would be on health and educational facilities of the standby capital improvements measure?

Answer: The Department's role in the action contemplated under the standby capital improvements proposal would be to identify needed construction projects in fields of health, education, and welfare most likely to have an antirecessional effect and to utilize the resources and authority provided by the measure, if enacted, to encourage the identification of needed facilities, formulation of projects, their submittal and approval, and the construction of needed capital improvements.

The use of such authority could have a definite impact on recession tendencies in areas of serious unemployment and would also increase the number of hospitals and other medical facilities, of schools, of waste treatment plants, and the like. Many of these projects would involve substantial numbers of personnel in construction and allied fields over a period of months. They would also require the use of a quantity and variety of industrial supplies and materials.

The average time required from the beginning to completion of construction of health and educational facilities is 16 to 20 months. In areas of serious unemployment such projects could have considerable stimulatory effects over an extended period of time.

Question: Does the Department do any analysis on costs of particular diseases, illnesses, and so forth, and economic benefits from their cures, eradication, and elimination? What are the results of such analysis?

Answer: The Public Health Service has made estimates of the costs of diseases for various purposes from time to time. It has estimated, for example, that tuberculosis costs the American people about $725 million a year, and that glaucoma costs the taxpayer about $90 million a year in public assistance alone.

In making these estimates the Public Health Service has found it virtually impossible to compute the whole costs, even of particular diseases, to individuals, to communities, and to the Nation as a whole. In general, the estimates have not taken into account the contribution to our national life that the victims of these diseases might have made if their disability had been prevented. Nor do they count the secondary costs—such as the disruption of families, especially when it is the breadwinner or the mother of a family who is the patient.

It is even harder to estimate the savings of the success of disease prevention. No one knows, for instance, how many cases of paralytic poliomyelitis there would have been in 1960 had there been no vaccine to prevent it. However, there were about 900 reported cases in 1961 as compared with nearly 14,000 cases in 1955.

Because of these difficulties of measurement and analysis, the Department is closely following the increased interest by scholars outside Government in the measurement of the direct and indirect costs of illness and the benefits to individuals, to communities, and to the Nation at large from preventive and other actions that reduce the incidence and prevalence of disease and disability. Examples of these studies are the "Economics of Mental Illness" by Rashi Fein and the "Economics of Public Health: Measuring the Economic Impact of Diseases" by Burton A. Weisbrod. These studies have served to clarify the problems of measuring the costs of sickness in such fields as mental illness, cancer, tuberculosis, and poliomyelitis.

Question. What are the needs of the vocational rehabilitation program whose results seem most impressive?

Answer. An estimated 2 million disabled people in the country today could benefit from vocational rehabilitation. Furthermore, each year about 270,000 persons are added to the group who could benefit through vocational rehabilitation. As the Nation's population increases, the needs for vocational rehabilitation will increase further.

Attached is a chart and table entitled "Vocational Rehabilitants by Types of Disabilities." The data show that in the 15-year period from 1945 to 1960, the number of persons rehabilitated annually through the vocational rehabilitation program more than doubled, from 42,000 to 88,000 and for 1961 still another increase to 92,500.

The largest number of persons served during this period were those with orthopedic, visual, and hearing disabilities. Substantial numbers with cardiac ailments, mental illnesses, and epilepsy also were rehabilitated. Although there have been marked gains in the numbers rehabilitated with severe handicaps—such as mental illness and mental retardation—much remains to be done.

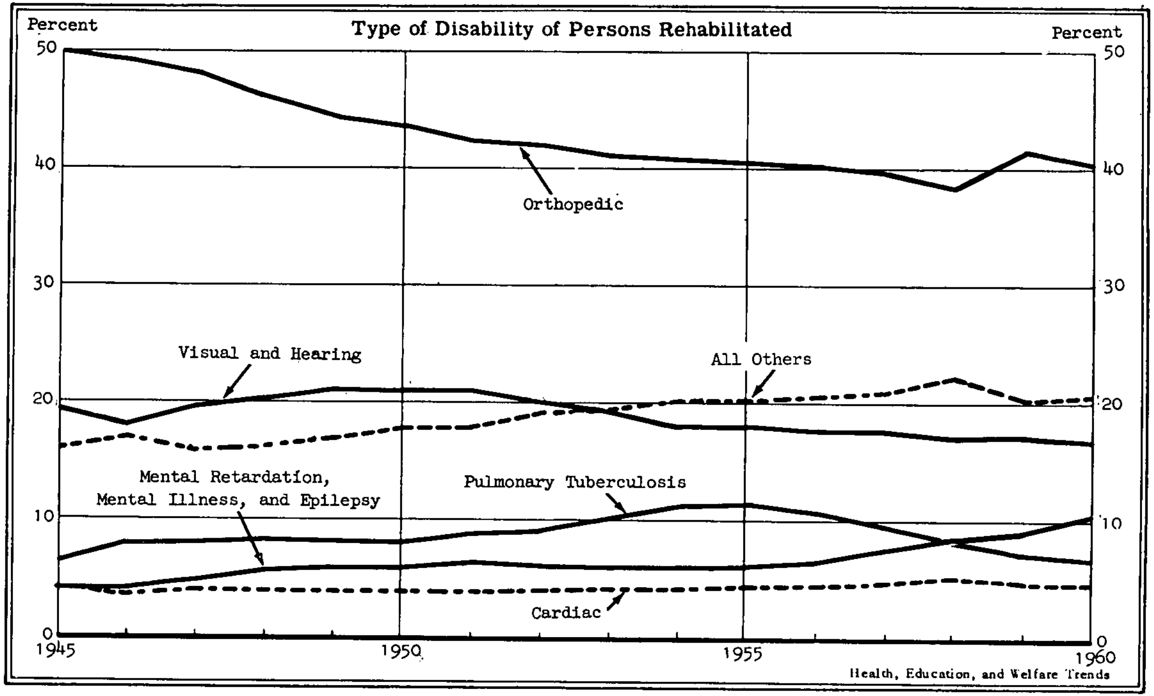
The long-range goal of the Department of Health, Education, and Welfare is to double the annual number of disabled persons rehabilitated and placed in employment through the public program from the estimated level for 1962 of approximately 100,000 per year to 200,000 per year. In order to achieve this doubling, there will need to be a great acceleration of the Federal-State rehabilitation services program, which will require a much higher level of financing.

To achieve 200,000 rehabilitants annually much needs to be done in the development and demonstration of new and improved techniques of rehabilitation. This is particularly the case because many more severely disabled people will need to be rehabilitated in the future. New techniques of rehabilitation must be developed. There also needs to be a major expansion of demonstration projects to stimulate the incorporation of new and more effective techniques into the vocational rehabilitation programs of the States and their local communities.

One of the most critical needs in doubling the present annual rates of rehabilitants is an adequate national pool of skilled professionals in the field of rehabilitation. Illustrations of the professional needs are the following. Today there are 400 physicians trained and accredited in the specialty of physical medicine and rehabilitation. The need under an expanded program is for 3,000. Presently the universities are graduating 500 rehabilitation counselors each year. The need under the expanded program would be for 1,200 graduate rehabilitation counselors per year. The expanded program would also require 500 social workers each year with training in rehabilitation, and only a third of that number are being graduated at this time. There would also need to be a sharp step-up in the training of nurses, occupational and physical therapists, speech pathologists and audiologists, and psychologists.

VOCATIONAL REHABILITANTS BY TYPE OF DISABILITY

During the 16 years from 1945 through 1960 the total number of rehabilitants doubled and the number of rehabilitants in each disability group increased markedly. The proportions of total rehabilitants increased for those handicapped by mental illness, mental retardation, and epilepsy; they declined for persons with orthopedic, visual, and hearing disabilities. The proportion of rehabilitants having pulmonary tuberculosis declined in the last 5 years.


Type of Disability of Persons Rehabilitated
Percent
Percent
50
40
30
20
10
0
1945
1950
1955
1960
Orthopedic
Visual and Hearing
All Others
Mental Retardation, Mental Illness, and Epilepsy
Pulmonary Tuberculosis
Cardiac
Health, Education, and Welfare Trends

NUMBER OF REHABILITANTS

Fiscal year [1]	Total persons rehabilitated [2]	Type of disability								
		Orthopedic [3]	Visual	Hearing	Cardiac	Pulmonary tuberculosis	Mental retardation	Mental illness [4]	Epilepsy	All others
1945	41,925	20,900	4,945	3,120	1,784	2,651	106	1,285	318	6,680
1946	36,106	17,852	3,859	2,614	1,264	2,896	175	995	345	6,071
1948	53,131	24,318	6,200	4,500	2,125	4,433	479	1,626	839	8,576
1950	59,597	25,803	7,090	5,291	2,308	4,913	493	1,919	1,073	10,692
1951	66,193	27,818	8,165	5,696	2,592	5,807	592	2,260	1,325	11,931
1952	63,632	26,484	7,750	4,959	2,531	5,835	615	1,962	1,281	12,174
1953	61,308	25,060	7,455	4,361	2,649	6,241	573	1,938	1,134	11,897
1954	55,825	22,628	6,533	3,439	2,372	6,229	561	1,708	1,070	11,284
1955	57,981	23,352	6,623	3,755	2,562	6,563	531	1,793	1,186	11,615
1956	65,640	26,298	7,395	4,223	3,040	7,045	756	2,192	1,374	13,317
1957	70,940	28,033	7,773	4,687	3,444	6,825	1,094	2,796	1,521	14,767
1958	74,317	28,551	7,915	4,803	3,943	6,278	1,578	3,221	1,543	16,485
1959 [5]	80,739	33,355	8,690	5,136	3,876	5,969	2,016	3,663	1,683	16,162
1960	88,275	35,541	9,438	5,410	4,241	6,198	2,937	4,453	1,856	18,201

PERCENT OF ALL REHABILITANTS IN FISCAL YEAR

Fiscal year [1]	Total persons rehabilitated [2]	Orthopedic [3]	Visual	Hearing	Cardiac	Pulmonary tuberculosis	Mental retardation	Mental illness [4]	Epilepsy	All others
1945	100.0	50.0	11.8	7.5	4.3	6.3	0.3	3.0	0.8	16.0
1946	100.0	49.5	10.8	7.2	3.5	8.0	.5	2.7	1.0	16.8
1948	100.0	45.8	11.7	8.5	4.0	8.3	.9	3.1	1.6	16.1
1950	100.0	43.3	11.9	8.9	3.9	8.2	.8	3.3	1.8	17.9
1951	100.0	42.1	12.3	8.6	3.9	8.8	.9	3.5	2.0	17.9
1952	100.0	41.6	12.2	7.8	4.0	9.2	1.0	3.1	2.0	19.1
1953	100.0	40.9	12.2	7.1	4.3	10.2	.9	3.3	1.8	19.3
1954	100.0	40.6	11.7	6.2	4.2	11.2	1.0	3.1	1.9	20.1
1955	100.0	40.3	11.4	6.5	4.4	11.3	.9	3.1	2.1	20.0
1956	100.0	40.0	11.3	6.4	4.6	10.7	1.2	3.3	2.0	20.5
1957	100.0	39.5	11.0	6.6	4.9	9.6	1.5	4.0	2.1	20.8
1958	100.0	38.4	10.7	6.5	5.3	8.4	2.1	4.3	2.1	22.2
1959 [5]	100.0	41.4	10.8	6.4	4.8	7.4	2.5	4.5	2.1	20.1
1960	100.0	40.3	10.7	6.1	4.8	7.0	3.3	5.1	2.1	20.6

[1] Includes data for all States and territories as vocational rehabilitation programs were established; e.g., Hawaii and Puerto Rico (1936), Alaska (1947), Virgin Islands (1957), and Guam (1958).
[2] The total for all disabilities is slightly larger than the sum of the various disability groups in some years because the type of disability was not reported for every person in those years.
[3] Amputations or impairments of limbs, back, head, or chest from any cause.
[4] Psychosis and psychoneurosis.
[5] Excludes data on type of disability for the 189 rehabilitants of the Hawaii general agency.

Source: U.S. Department of Health, Education, and Welfare; Office of Vocational Rehabilitation. The Rehabilitation Record, a bimonthly publication, contains fiscal year data in the October issue. "Vocational Rehabilitation Trends" (mimeographed) in the Rehabilitation Service Series contains analyses and more detailed data on State agencies for the fiscal year in the 4th quarterly issue—supplements bearing the same overall number in the series carry data for each quarter. The Vocational Rehabilitation Manual contains definitions and methodology. Legal authority for the program comes from the Vocational Rehabilitation Act, as amended (29 U.S.C., ch. 4); the Randolph-Sheppard Act, as amended (20 U.S.C., ch. 6A); and the Medical Facilities Survey and Construction Act, as amended (42 U.S.C. 291).

Question. What effects do recessions have on State and local welfare budgets and on their health and education long-term growth benefits?

Answer. (*a*) Welfare: Rising levels of unemployment may have a serious or a minor impact on State and local welfare expenditures, depending on the ability and willingness of State and local governments to meet the financial needs of the unemployed.

Unemployment insurance is, of course, the first recourse in a recession but some workers are not eligible, some exhaust their benefit rights, and some cannot manage on their benefits. Some persons in need because of unemployment or reduced hours are able to obtain assistance, others are not. Until aid to dependent children was extended in May 1961 to children in need because of a parent's unemployment, it was to general assistance that the needy unemployed had to turn for support for themselves and their dependents. In two-fifths of the States, however, employable persons and their families are not eligible for general assistance. In some of the remaining States, the needy unemployed may not qualify for assistance because of other eligibility conditions, such as residence requirements and property limitations. Finally, there is the important factor of the availability of State and/or local funds. When State and local governments are financially unable to meet the needs of all needy unemployed persons, only persons most critically in need can be added to the assistance rolls. Other needy persons may receive surplus foods.

Assistance recipients, such as ADC mothers, who are employed are likely to be marginal workers and to lose their jobs early in a recession, and as a result to need higher payments.

Furthermore, many assistance recipients receive some contributions from relatives. If these relatives become unemployed or work fewer hours, they may be unable to continue making such contributions, or have to reduce the amount of support. This too means that the recipients need larger assistance payments from welfare agencies.

Recent studies of the reasons for opening and closing public assistance cases show that a significant number of cases are opened primarily because of loss of employment of the recipients themselves or other persons who had been contributing to their support.

Public assistance expenditures rose steadily during the 1960–61 recession, from an annual rate of $3,673 million in May 1960 at the start of the recession, to $3,974 million in May 1961, at the end of the recession. This increase of some $300 million (on an annual basis) is more than three times as large as the increase to May 1960 from May 1969, when unemployment was moderate.

Two-thirds of this increase occurred in the general assistance and aid to dependent children programs, which are the most sensitive to economic conditions. (The May 1961 total for ADC includes for the first time payments for children of unemployed parents authorized by Public Law 87–31; the total for this group was at an annual rate of $18 million.) Trends in 1960–61 were quite similar to trends in the 1957–58 recession.

Of particular importance to State and local governments are the general assistance programs which are financed entirely with State and/or local funds. General assistance expenditures increased at a faster rate from May 1960 to May 1961 than expenditures under the federally aided programs, 16.5 percent compared with 7.4 percent.

Since the spring of 1961, general assistance expenditures have dropped sharply, due in large part to the transfer of cases from general assistance to the aid to dependent children program under the provisions of Public Law 87–31, which extended Federal public assistance to dependent children whose parents are the victims of unemployment (ACD–UP). In November 1961, 13 States paid $6.7 million to 200,000 recipients of the ADC–UP program. From April 1961—the month preceding the start of ADC–UP payments—to November 1961, general assistance expenditures dropped from $36.5 million to $27.1 million. The most significant declines took place in the 13 States which were making ADC–UP payments. In these 13 States payments declined by 36 percent from $17.3 million in April to $11.1 million in November 1961. By contrast, in the 41 States which had not extended their ADC program, general assistance expenditures in this period dropped 16 percent, from $19.2 million to $16 million. In the 2 preceding years, total general assistance payments in these States changed only slightly from April to November.

(*b*) Health: Since the end of World War II, the United States has had four brief, but sizable, recessions. In comparison with the deep depression of 1929–33, these setbacks have been relatively mild, but despite their mildness and despite the fact that great progress has been made since the war in providing for medical care for the American people through private health insurance, these recessions have reduced private personal financing of medical care. The same probably would be true in the future.

In the United States voluntary health insurance is geared to employment, since most workers get coverage at their place of work. Of the 132 million persons estimated by the Health Insurance Council to have some form of health insurance in 1960, hospitalization coverage was the most common—73 percent covered, 27 percent not covered. About 121 million, or 67 percent of the total population, had some type of surgical coverage, with 33 percent not covered. Only about 15 percent of the population had coverage for expenditures outside the hospital—e.g., doctors' visits, drugs, dentists, and other professional services—yet at least 50 percent of the Nation's private medical bill arises from expenses outside the hospital.

The 1958 recession was reflected in a slackening in the expansion in enrollment in voluntary health insurance that had been taking place, and in States like Michigan in a reduction in the proportion of the population enrolled.

Enrollment in voluntary health insurance is uneven throughout the country. The highly industrial States have 80 percent of the population enrolled. Urban industrial workers and their families are almost all enrolled. Recessions and consequent unemployment result in noticeable loss of insurance coverage because for the great majority of group enrollees, coverage stops automatically within a short time of going off a payroll. Some insurance companies extend benefits to the end of policy month following the date of layoff, and Blue Cross and Blue Shield generally permit continuation of the employee's group coverage as long as arrangement for payment of premiums is made, or they permit conversion from a group to a nongroup basis. However, the unemployed worker and his family, unable to finance the entire premium from reduced income generally lose all protection during a period of prolonged layoff. Such situations are not only bad for the employee, but also affect the providers of such services.

The worker who may be older, but still ineligible for social security benefits may be particularly hard hit during a prolonged layoff or recession. Such a worker may have a chronic disease and need costly prescription drugs. Most community pharmacies are not in a financial position to carry the unemployed worker for any length of time. In most instances the only alternative is public or private charity, which increases the burden on public welfare, private philanthropy and hospitals.

When a recession occurs our current tax system results in the Government (both Federal and State) reducing the amount of money that it withdraws from the private sector of the economy for its own use. This mechanism affects the amounts of money States can devote to welfare, including medical care for the indigent.

During a recession when a State's budget for general assistance programs must be increased, State and local health agencies compete with other State and local agencies for the reduced tax dollar.

Postponement of capital expansion for hospital construction may mean delays in achieving an adequate number of general or mental hospital beds for a growing population. Even with Hill-Burton funds, the ratio of beds to population has remained the same as in the immediate postwar period. Postponement of such capital expansion increases the rate of expenditure necessary in the future to catch up when the economy may not be equal to filling the cumulative unfulfilled demand.

While hospitals have attracted the greatest amount of public and private support, nursing homes, outpatient and home care facilities have been neglected and the effects of recessions have added to this neglect.

In the field of preventive health services, in periods when personal incomes are reduced, there is a definite diminution in the use of such services. The economic effect may not be discernible for a long time to come. The national health survey has furnished some significant clues to population groups unquestionably underutilizing services. The average number of immunizations received per child in families with over $7,000 in income is more than double (0.7) the level per child in the under $2,000 income family (0.3).

There are significant regional differences in the level of use of medical services. In the South, doctors are seen 4.7 times a year per capita; in the West 5.7 times. In the South, on the average, people see the dentist just once a year while in the Northeast region they average 2.1 visits per capita. Periods of recession aggravate such disparities.

(*c*) Education: Ninety-six percent of all public elementary and secondary education expenditures are drawn from State and local tax sources. There seems to be little relationship between trends in State and local educational expenditures and the economic cycle, at least where recessions rather than depressions are involved. But no conclusive data on the subject are available.

Some specific effects have been observed however. For instance, several cities have reported that during recessions qualified teachers become easier to recruit, thus enabling these communities to reduce the number of uncertified teachers and substitutes used.

Question. What is the optimum physician population ratio? Can new organizational arrangements help reduce the ratio?

Answer. It is generally agreed that there is no one ratio of doctors to population that can be held to be optimum for all places. Many factors must be considered, such as the density of the population, the age distribution among the population to be served since it is the children and the older people who need the most medical care, and the ability of the people to pay for physicians' services. We have in this country an average ratio of 133 doctors of medicine for each 100,000 population, but they are not evenly distributed. In the Northeastern States the ratio is 158, in the North Central States it is 113, in the Southern States it is 103, and in the Western States it is 140. By State, the range is from 61 per 100,000 population in Alaska, 71 in South Dakota, and 76 in Alabama and New Mexico to 164 in Connecticut, 175 in Massachusetts, and 190 in New York State.

While it is not possible to name an optimum ratio, it is possible to state that many of these ratios are much too low. And in areas where the ratio is on the high end of the scale, it is safe to say that there are not too many doctors for those particular areas.

New patterns of organization of physicians have been primarily the outgrowth of the increasing complexity and specialization of medicine, rather than a way of caring for more patients. Increasingly, medical care has been given in a hospital setting where there is a highly structured medical staff. Group practice of physicians for the care of ambulatory patients has also increased and continues to do so. It is possible that these organizations care for more patients than an equal number of physicians in solo practice, but it is doubtful that there is any significant difference.

Question. What is the relationship between income distribution and availability and utilization of physicians?

Answer. When the States are ranked according to their physician-population ratios, the six lowest States are the same six States that have the lowest per capita income. This pattern is not followed exactly as one goes up the scale, but in general the States with the higher per capita income tend to have the higher physician-population ratios. There is one notable exception. Alaska, with a high per capita income, has the lowest physician-population ratio.

As to the relationship between income distribution and utilization of physicians' services, studies done by the national health survey show that the number of physician visits per person rises as the family income rises. In families whose income is under $4,000 a year, the average number of physician visits is 4.6 per year. When the family income is $7,000 or above, the average number of visits rises to 5.7 per year.

Question. What are the prospects for increasing the productivity of physicians and health personnel?

Answer. The prospects of further increasing, to any substantial degree, the productivity of physicians and other health personnel in terms of increasing the number of people they can take care of in the immediate future are not good. In recent years the increased urbanization of the population, the substitution of office for home visits, the increased use of hospitals, the greater availability and utilization of nurses and other allied medical personnel, all have increased the capacity of the individual physician. In 1930 the average physician saw about 50 patients a week; now he sees more than a hundred in a week.

One possible way to increase the productivity of physicians is through group practice plans.

While it is true that medical research has simplified the treatment of some illnesses and made possible the prevention of others, so that the amount of care needed by any one patient in such cases is greatly reduced, it nevertheless has not made visits to a physician unnecessary. At the same time, modern medical care has made it possible to do much more for patients with other illnesses—illnesses that cannot be cured or prevented—but the disabling effects of which can be prevented or at least greatly ameliorated. Not too many years ago there was very little that a physician could do about such illnesses and consequently there was less demand for his services. The net effect of advances in the effectiveness of medical care has naturally been to greatly increase the demand for it.

On the other hand, the prospect of continuing to increase the productivity of health personnel in terms of their effectiveness in prevention and treatment is virtually limitless. Continuing medical research, the training of health personnel to enable them apply research findings, the development of more efficient organization and higher standards of health care services and the improvement of community facilities as contemplated by the recently enacted Community Health Services and Facilities Act of 1961, all of these combine to make the prospect very bright, indeed. How widely the American people can benefit from these advances will depend largely on the number of physicians and other health personnel who are available to apply them.

Question. What are the prospects for increasing the productivity of teachers and other educational personnel?

Answer. The prospects for increasing the productivity of teachers and other educational personnel depend largely on research and development in the following areas:

1. Research leading to increased understanding of the learning process and the development of more effective methods based on such findings.
2. Reorganization of the various curricula to incorporate new knowledge and relate it more effectively to the old.
3. Better trained teachers and supervision, skilled in both content and method.
4. Development and use of better teaching materials and equipment, such as audiovisual aids, teaching machines, etc. These devices supplement rather than supplant the teacher, making her able to (1) work with larger groups whose members can proceed at their various paces, and (2) improving the quality of learning.
5. Improvement of educational administration and finance at the level of the school, the local school systems, and at county and State level.

Recent and proposed legislation, including the cooperative education research program, the National Defense Education Act, the administration's new proposals to promote educational quality—are directly concerned with increasing the basic knowledge of the learning process, the availability and effectiveness of educational media, and the quality of teaching and supervision.

Forty years of research and experimentation have shown that motion pictures, radio, television, and the more recently developed programed self-instructional media can be successfully used in teaching. Although the full potential of these media is not yet fully known, there is ample evidence that they can, singly or in combination, motivate the student, transmit information, demonstrate complex skills, and shape attitudes and appreciations.

In addition to their effectiveness in teaching students, there is a substantial body of research which indicates that the media can assist in directly upgrading the quality of teaching. A number of projects supported under title VII of the National Defense Education Act have shown that, as the teacher uses well-prepared television programs and motion pictures in her regular teaching situation, she learns more about the subject which she teaches and more about how to teach that subject to her pupils.

There is also ample evidence that the media-teacher team contributes more in combination to the learning process than does either member of the team alone. When use is made of teaching media by a superior teacher the learning results are beyond what is possible with the same media used by an inferior, or even an average teacher. At Syracuse University, for example, a title VII research study indicated that, although both average and superior teachers were effective over television, the superior teacher over television led his students to wider application of the content learned than the average teacher, either on television or in person.

Thus, the newer media, by assuming the routine functions of information-transmission and skill development, can increase the productivity of the superior teacher by permitting her to devote greater portions of her time to those functions at which she is unexcelled: the diagnosis of learning problems; counseling with students, individually or in groups; organizing elements of information into meaningful entities; and planning and supervising of instruction.

Question. How are decisions made on the composition of Government security portfolios held by trust funds such as the social security trust funds?

Answer. Ever since the inception of the old-age, survivors, and disability insurance system in 1937, the investments of its available funds have been restricted to (1) interest-bearing obligations of the United States and (2) obligations whose principal and interest are guaranteed by the United States. The second category consists of only a relatively small number of issues, and none have ever been purchased for the trust funds. The investments in the first category can be either in special issues—legally designated as "public debt obligations for purchase by the trust funds"—or in any other securities of the Federal Government, bought either on the open market or at issue. In the past, some regular issues have been purchased, both on the open market and at the time they were offered to the general public, but they have represented only a small proportion of the invested assets of the trust funds (16 percent on June 30, 1961). Most of the investments have thus been in special issues.

The statute has always made specific provisions as to the interest rate that should be borne by special issues. The present law, however, does not provide for any specific maturity dates or schedules for these special issues. Rather, it merely states that they "shall have maturities fixed with due regard for the needs of the trust funds." The maturity scheduling of the investments, as well as their interest rates, strongly affects the amounts received in interest earnings. If, for example, a substantial portion of the special issues were frozen in relatively low-rate, longer term maturities at the beginning of a period of rising interest rates, the interest income of the trust funds might be substantially less than would otherwise have been the case.

Under the 1960 amendments, these special issues bear an interest rate about equivalent (because of rounding to the nearest one-eighth of 1 percent) to the average market-yield rate of all longer-term (4 or more years to call or maturity from the end of the month preceding the month of issue of the special issues) interest-bearing obligations of the United States.

Senator PROXMIRE. Finally, that chart you gave us shows that the child of a father who is a high school graduate, did not attend college, the likelihood of his going to college declines as the income increases, over $7,500.

Mr. COHEN. I can't——

Senator PROXMIRE. Now this is very strange. It seems that the fellows who do very well, and have a high income, for a graduate of high school, tend to discourage their sons from going to college, perhaps on the ground that "the old man did mighty well without going to college." The son doesn't need to go to college.

Mr. COHEN. It is too sharp a drop, it seems to me, to be explained by just what we know. I would imagine that there is something peculiar in it statistically. I have exactly the same question that you did, Senator.

Senator PROXMIRE. It is a very, very interesting statistic, if it could be corroborated. I imagine that you had a pretty large sample, so I would say that probably the chances of error aren't very great.

Mr. COHEN. If we were doing it over we would just draw a straight line between the 42 percent and the 50 percent groups. It wouldn't be that sharp, there at the $7,500–$9,999 level.

Senator PROXMIRE. So the fact there is no increase would be significant. The father can afford it, obviously.

Mr. COHEN. Yes, even if there were a plateau. It does indicate that in the other two, it goes up so sharply with income that, as you say, even if it were stable, you would still have a question of why it didn't go up more sharply.

Senator PROXMIRE. I want to thank you very much. As I say, you are mighty patient, and very, very expert. I thank you a great deal.

Mr. COHEN. Thank you, Senator. One always learns a great deal, when he testifies before a congressional committee, too.

Senator PROXMIRE. The committee will stand adjourned until Friday morning at 10, when we will hear from other witnesses.

(Whereupon, at 4:20 p.m., the committee was recessed to reconvene at 10 on Friday, February 2, 1962.)

JANUARY 1962 ECONOMIC REPORT OF THE PRESIDENT

FRIDAY, FEBRUARY 2, 1962

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

The Joint Economic Committee met, pursuant to recess, at 10 a.m., in room P-63, the Capitol, Representative Wright Patman, chairman of the committee, presiding.

Present: Representative Patman (chairman), Senators Bush, Pell, Douglas, Sparkman and Proxmire; and Representatives Reuss, Widnall, Kilburn, and Curtis.

Chairman PATMAN. The committee will come to order.

This morning we continue hearings on the Economic Report of the President for 1962. We have with us this morning a distinguished panel of economists who will discuss the topic of wages and prices. We will hear an opening statement from each of these gentlemen, and then ask questions.

We have with us Professor Brozen of the University of Chicago, whom we have had the pleasure of hearing on previous occasions. We have Prof. Otto Eckstein, of Harvard, who has a special place in the roster of the committee's academic friends. Professor Eckstein conducted the committee's searching investigation during the previous Congress.

We also have Prof. Ben William Lewis, of Oberlin College, and we have Dr. Gardiner C. Means, who has served in many important posts in the Government, and is the author of a new book entitled, "Pricing Power and the Public Interest," a copy of which you were good enough to send me, Dr. Means.

I recall quite vividly a very famous book which you coauthored with A. A. Berle, entitled, "The Modern Corporation and Private Property." I believe you feel that this is a companion piece of this earlier work, and I trust it will prove to be successful.

I suggest we start with Dr. Means, and then the other witnesses in the order in which you are seated. You may proceed in your own way, Dr. Means.

STATEMENT OF DR. GARDINER C. MEANS, ECONOMIC CONSULTANT, VIENNA, VA.

Dr. MEANS. Chairman Patman and members of the Joint Economic Committee, I greatly appreciate this opportunity to comment on the President's Economic Report. It is a most progressive report. It offers concrete economic goals and methods for achieving them which we as a Nation can examine and discuss and which the Congress, representing the people, can adopt, modify, or reject. This is economic leadership in a democracy. It commands my enthusiasm.

I am here to discuss that part of the report which deals with prices and wages. My discussion will center on full employment without inflation. This will also involve consideration of certain aspects of monetary policy and the balance-of-payment problem.

My first major point concerns inflation. The analysis underlying the President's report makes an admirably sharp distinction between, one, inflation which "may result from excessive aggregate demand," and, two, that which "may originate in those sectors of the economy where competitive forces are weak and large corporations and unions have a considerable degree of discretion in setting prices and wage rates." I will refer to the first of these as "demand inflation," and the second, which involves administered prices and wage rates, as "administrative inflation."

This report also discusses the inflation since 1953 as partly the product of demand inflation and partly the product of administrative inflation. While it recognizes that in large measure the responsibility for administrative inflation must be divided between management and labor, it does not seek to allocate this responsibility.

This is about the position I was in when I first brought the distinction between these two types of inflation to the attention of a Senate committee 4 years ago and pointed out that much, if not all, of the recent inflation was the result of administrative exercise of pricing discretion.

Since that time, I have made an intensive study of the inflation since 1953, with particular emphasis on steel prices. A part of the results of this study are contained in my new book, to which you have referred, "Pricing Power and the Public Interest," advance copies of which I have had sent to you.

As I shall show you, my conclusions are somewhat different from those implicit in the President's report and lead to important differences in policy having to do with, one, the level of unemployment at which there is likely to be serious danger of demand inflation, two, the rate of recovery toward full employment that is likely to engender demand inflation, and three, the measures needed to prevent administrative inflation.

The first important conclusion I have reached is that since 1953, there has been no inflation due to excess aggregate demand. Rather, the rise in the wholesale price index since 1953 has been an administrative inflation largely concentrated in steel and the steel-using industries.

In presenting evidence on this point, let me first call your attention to the year 1953. That was a year of very low unemployment—the average for the year was 1.9 million unemployed, or less than 3 percent of the labor force, and in the second quarter unemployment, seasonally adjusted, was almost down to a million and a half or only 2½ percent of the labor force. Yes it was a year without inflationary pressure from the demand side.

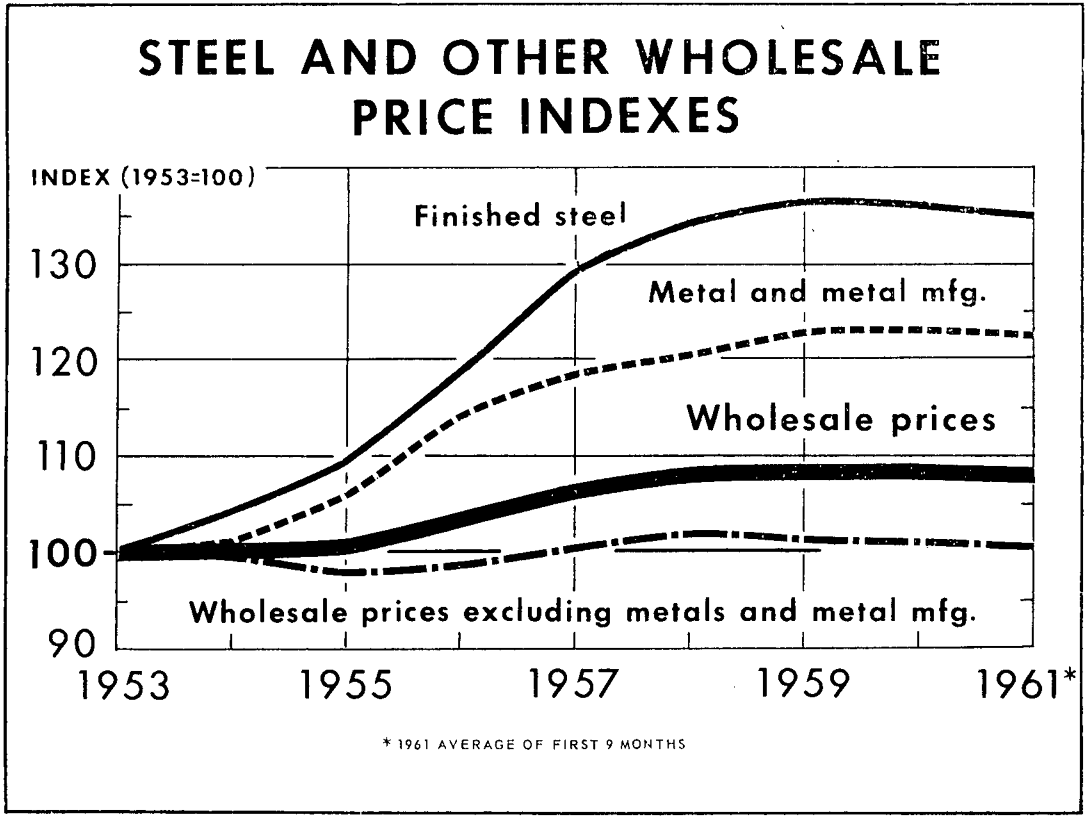
At the beginning of the year, price controls were in effect, but when these were removed in the first quarter, there was no general rise in wholesale prices. The wholesale index was lower in the second quarter than in the first quarter.

Also, 1953 was a year of excellent wholesale price balance. Indexes of administered prices and market prices were in almost exactly the same relation to each other that existed in 1926 to 1929 and in 1913–14, both periods of high employment and price stability.

Finally, 1953 was a year in which a reduction in the money supply to reduce aggregate demand actually converted a full employment situation in the first half of the year into the beginnings of depression as you can see from chart 2 on page 52 of the President's report.

(The chart is as follows:)

CHART I


STEEL AND OTHER WHOLESALE PRICE INDEXES
INDEX (1953=100)
Finished steel
Metal and metal mfg.
Wholesale prices
Wholesale prices excluding metals and metal mfg.
130
120
110
100
90
1953
1955
1957
1959
1961*
* 1961 AVERAGE OF FIRST 9 MONTHS

Mr. MEANS. What actually happened to wholesale prices after 1953 is shown in chart I. The solid black line shows the 8.2-percent rise in wholesale prices. The top line shows the 35-percent rise in finished steel prices. The next lower line shows the 22-percent rise in an index for metals and metal products, including steel. The bottom line, which represents the wholesale price index less metal and metal products, shows no rise at all, or rates a slight dip, with some rise, and then some fall.

Clearly, steel was the primary source of the rise in the wholesale price index after 1953. The 35-percent rise in steel prices stimulated the price rise in the steel-using industries partly by the direct increase in costs and partly by example.

It has been suggested that, while this price rise was not due to a general excess in aggregate demand, it was due to heavy demand in the durable goods industries. Yet at no time was the rate of operation in durable manufactures as a whole nearly as close to capacity operation as it was in 1953.

The most plausible case for an excess demand in durables is for the last quarter of 1955, when durable production was 6 percent over the peak of 1953. But in the meantime, capacity in the durable goods industries had increased by more than 15 percent. It is true that auto sales were expanded to unprecedented levels in 1955, but in spite of an 18-percent increase in steel prices over 1953, the index of motor vehicle prices went up only 6 percent. And steel at its 1955 peak was operating at a smaller proportion of capacity than at its peak in 1953. It was clearly not demand in excess of capacity which caused durable goods prices to rise in 1955.

After 1955, the gap between durable goods demand and capacity progressively widened as capacity expanded and demand increased little or declined.

Even in steel there is little relation between price increases and the level of operation. As you can see from chart I, steel prices rose in the depression year 1954 when steel was operating at 71 percent of capacity; in 1955 when it was operating at 93 percent of its capacity; and in 1958 when it averaged only 61 percent of capacity operation. Thus it seems to me clear that excess demand was not the cause of inflation between 1953 and 1955 or in the subsequent inflation.

This conclusion is important because of the 5-percent unemployment goal proposed in the President's report.

This 4 percent figure has been selected on the ground that, unless the frictional and structural unemployment is reduced, a level of unemployment below 4 percent is likely to engender demand inflation. Support for this conclusion rests on the basis that in the last period in which unemployment was as low as 4 percent (seasonally adjusted)—that from May 1955 to August 1957—prices and wage rates rose substantially. The report recognizes that a part of this price rise was administrative inflation but implies that a significant part was demand inflation.

If I am correct in the conclusion that no part of the 1955–57 price rise was due to general excess in demand or excess in the demand for durable goods as a whole, then the minimum level of unemployment that can be reached without significant danger of demand inflation is lower than 4 percent.

I believe an appropriate goal would be no greater than 3 percent. We achieved better than this in 1953 without inflationary pressure from excess demand and I believe we could have pushed demand in 1955–57 to the 3 percent level of unemployment without demand inflation if administrative inflation could have been avoided. And the same holds for the near future. Thus, I recommend an immediate goal of reducing unemployment to 3 percent—a goal that can be lowered further as frictional and structural resistances are overcome.

Also, if the safe full employment goal so far as demand inflation is concerned is 3 percent and administrative inflation can be prevented, then the rate of recovery to full employment can be accelerated somewhat. This could add $15 or $20 billion to our gross national product and bring in an extra $4 or $5 billion in Federal revenue in fiscal 1963 with the present tax structure, or allow lower tax rates. I therefore recommend a somewhat more rapid rate of recovery than is suggested in the President's report.

But to achieve this gain without inflation there is the necessity of preventing administrative inflation.

How administrative inflation should be prevented must depend very much on its source. Why did steel prices rise by more than a third from 1953 to the present? Management has placed the major responsibility on labor and labor has reciprocated. It could be that labor has pushed wage rates up faster than the increases in productivity and that management has had to increase prices to cover increased costs. Or it could be that management has increased prices to widen profit margins.

From my intensive study of steel prices and costs, I have reached the conclusion that something like three-quarters of the steel price increase since 1953 has resulted directly or indirectly from a widening of profit margins and only a quarter has resulted from increased labor costs. At 1953 prices and wage rates, an 80-percent rate of operation would have yielded something like an 8-percent return on capital after taxes.

This is for industry as a whole. At 1959 prices and wage rates, an 80 percent rate of operation would have yielded closer to a 16 percent return. In 1953, the break-even point for U.S. Steel was close to 50 percent, i.e., with 50 percent of its capacity in operation, the corporation would have neither made nor lost money. In 1959, prices were so much higher relative to wage rates that the corporation would have broken even if it had operated at around 30 percent of capacity. This widening of profit margins appears to have been the main source of the price rise.

Even the increase in labor costs per unit of steel must be attributed in some degree to management. To increase prices enough to double profit margins and to blame labor for the price increases is an ever-present incentive for labor to seek its share.

The effect of this administrative rise in steel prices on our economy has been profound. It has forced and stimulated price increases in steel-using industries. It has induced the monetary authorities to adopt a tight money policy in the belief that demand inflation was underway. And it has contributed importantly to the imbalance in our international payments—if the recent decline in our steel exports and increase in imports could have been avoided in this last year, our gold loss would have been more than cut in half.

How, then, should we deal with administrative inflation? This question comes to a focus in the new 3-year steel contract. Whatever is done in this contract will either contribute to or inhibit administrative inflation not only in steel but throughout the economy.

I believe that the public interest requires a substantial reduction in steel prices and a year's moratorium on wage increases. I suggest that the 3-year labor contract be negotiated on this basis, with the steel prices and wage rates in the second and third year of the contract patterned after the recommendations in the President's report.

Such a development could have great public benefit. It could be expected to increase steel sales both at home and abroad. Labor would probably gain as much or more from increased volume as it would forgo in immediate wage increases. Stockholders would lose some of the extra profits from the use of pricing power contrary to the public interest but the loss of business to foreign competition would be reduced and expanded volume of business would make up in part for a reduced profit margin.

The imbalance in this country's international payments would be substantially reduced. And the danger of administrative inflation in the near future would be practically eliminated. This would allow us to expand aggregate demand to the extent needed for full employment without fear of inflation.

This brings me to my second major point. If we are to expand aggregate demand to full employment levels more rapidly than the President's program calls for, how can this be brought about? As the Council of Economic Advisers has rightly indicated—

> There is in principle, a variety of mixtures of fiscal and monetary policies which can accomplish a given stabilization objective.

One can expand aggregate demand either by an expansionist fiscal policy, or by expanding the money supply.

I fully approve the President's aim to balance the budget in fiscal 1963, and I do not propose a change in his fiscal policy rates. I would bring about the more rapid rate of recovery through a somewhat more rapid, though controlled, monetary expansion.

I am persuaded that the widening gap between potential and actual production, particularly since 1955, has been due to a decline in the real money supply.

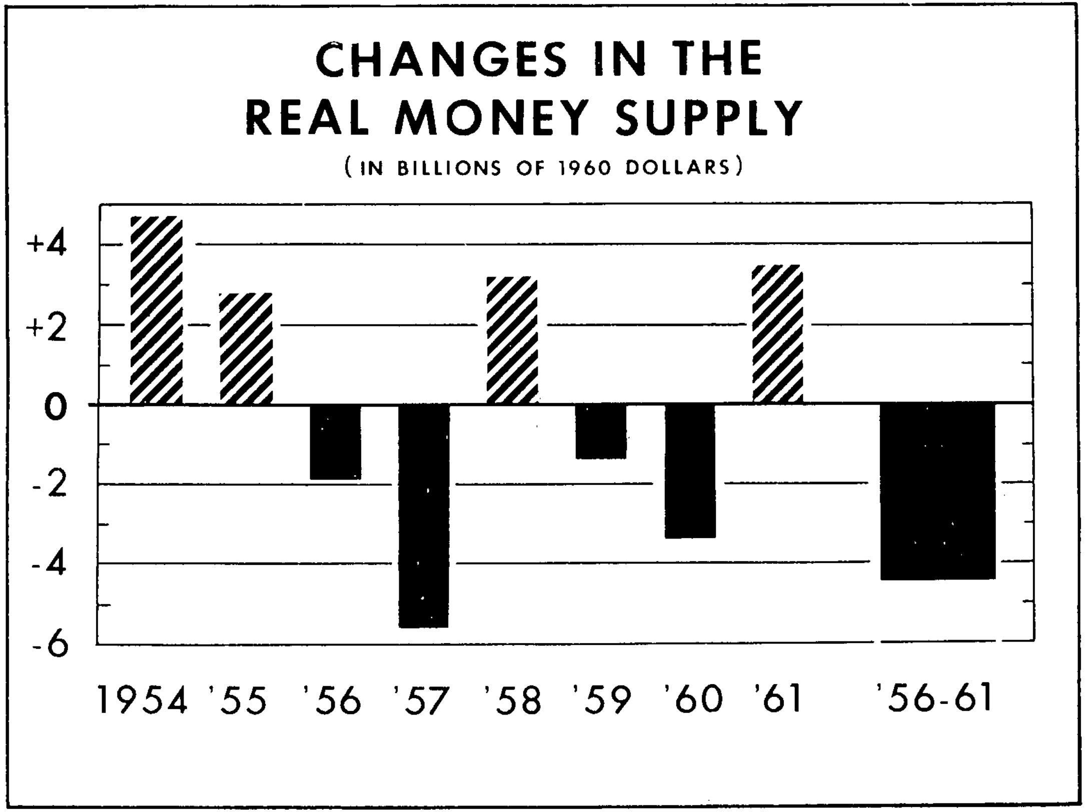
Some have suggested that the widening gap has been due to increased structural friction in our economy but your staff has effectively disposed of that argument.

On the other hand, the contraction in the real money supply is clear. It can be seen in chart II, which shows for each year since 1953, the change in the real money supply, i.e., the change in the total demand deposits and currency after adjusting their value to the 1960 dollar. As you can see, the real stock of money was contracted in 4 of the 5 years following 1955.

From the beginning of 1956 to the end of 1960, the real stock of money was reduced by nearly $10 billion or 7 percent—and this in an economy with a steadily growing potential. Even with the $4.5 billion increase in the money supply in 1961, we still have $4.6 billion less in the real money supply than in 1955.

(The chart is as follows:)

CHART II


CHANGES IN THE
REAL MONEY SUPPLY
(IN BILLIONS OF 1960 DOLLARS)
+4
+2
0
-2
-4
-6
1954
'55
'56
'57
'58
'59
'60
'61
'56-61

Dr. MEANS. A fiscal policy involving too high a full-employment surplus has undoubtedly contributed to the gap between potential and actual production previous to 1961, or throughout. But I believe the tight money policy which greatly reduced our money supply was more importantly responsible. Certainly the $4.5 billion increase in the money supply during the last year has importantly contributed to the increase in aggregate demand.

Just what rate and level of monetary expansion is needed to support a more rapid rise to full employment without demand inflation will depend in part on the level of interest rates. The lower the level of short-term interest rates, the greater the monetary expansion which would be needed to achieve full employment. But the problem of interest rates cannot be considered apart from that of our balance of international payments.

This leads me to my third major point, which has to do with the impact of monetary expansion on our balance of payments.

First, I want to say that my view of the very real problems created by our loss of gold and our imbalance of international payments is quite different from that which seems to be generally held both here and abroad.

In my opinion, our loss of gold in the last 4 years has been one of the best things that has happened in recent years, both for this country and for the free world. It is the crowning success of the Marshall plan.

At the end of World War II, much of the industry of Europe was destroyed, the European economies were operating at low ebb, and by 1959, we had about 70 percent of the free world's monetary gold. I was in on the early discussions on the construction of the Marshall plan and the subject I am going to outline here was discussed then.

The Marshall plan had three major objectives: to help reconstruct the European industrial plant; prevent an adverse balance of payments on their part—what we used to call the dollar shortage—from holding back their economic recovery; and finally to allow the European countries to draw back the excess of gold we had acquired in order to strengthen their financial systems. The gold outflow of the past 4 years has been fulfilling that third objective and our gold holding still represents close to 45 percent of the free world's monetary gold outside that held by the international institutions. I am not sure but what some further reduction in our gold holdings would be desirable in our own interest and that of the rest of the free world.

On the other hand, we cannot have an indefinite drain on our gold holding. Just how soon and in what ways the outflow should be brought to a stop is a very real problem and a problem for specialists. We are now appropriately reversing many of the measures which were adopted in connection with the Marshall plan to deal with the dollar shortage which has now become a dollar surplus. A substantial reduction in steel prices would also contribute to better balance. I have no doubt that these and other steps plus perhaps rising prices abroad can bring the outflow to a suitable stop.

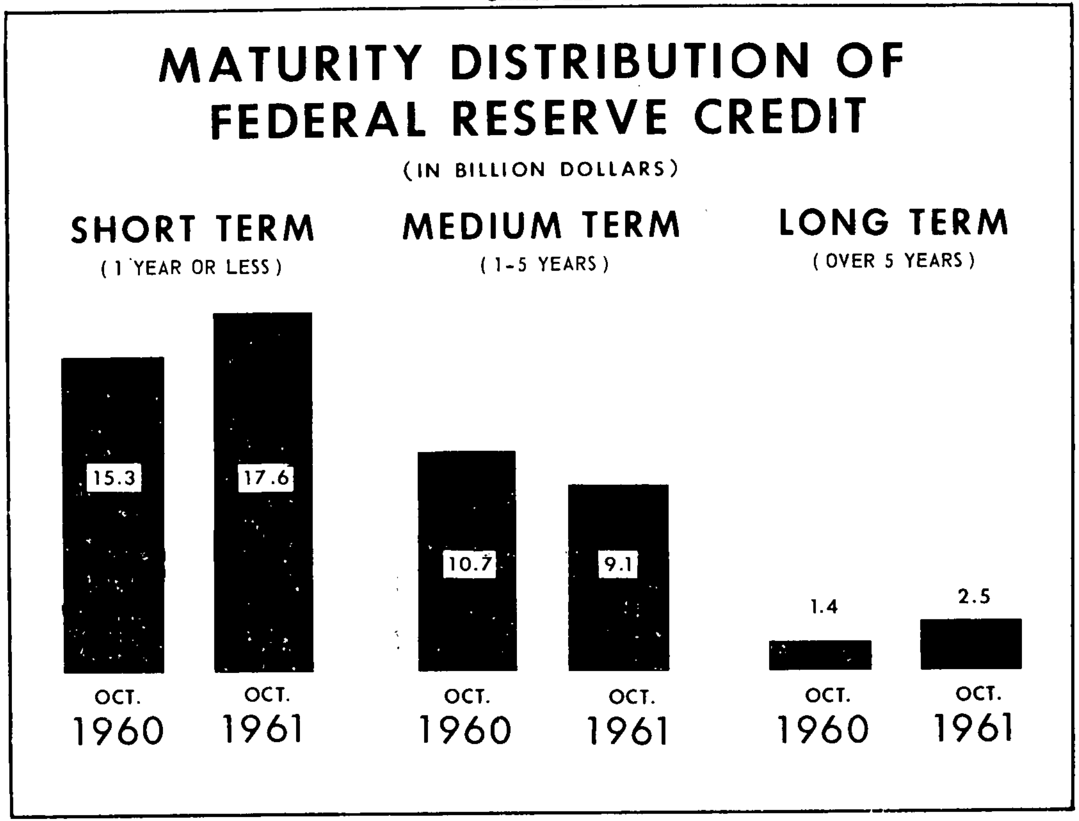
But the outcome will be eased or made more difficult by the relation between short- and long-term interest rates which results from monetary expansion. As you know, if our short-term rates are low, both foreign and American funds move to other countries, worsening our current balance of payments. Yet short-term interest rates have relatively little effect on real investment.

It is low long-term rates which stimulate housing and other long-term construction. In the present situation, it would make it easier to handle the imbalance in payments and stop the gold outflow if short-term interest rates were higher. At the same time, it would stimulate our internal investment if long term rates were lower.

And it is within the power of the Federal Reserve Board to bring this about through changes in its portfolio. The composition of the Federal Reserve Board's portfolio at the end of October 1960 and October 1961, is shown in chart III. Three-fifths of the portfolio was in assets with 1 year or less to run and most of the rest of the portfolio was in medium term assets with 1 to 5 years to maturity. Only a small though increased proportion was in assets with more than 5 years to maturity.

(The chart is as follows:)

CHART III


MATURITY DISTRIBUTION OF
FEDERAL RESERVE CREDIT
(IN BILLION DOLLARS)
SHORT TERM
(1 YEAR OR LESS)
MEDIUM TERM
(1-5 YEARS)
LONG TERM
(OVER 5 YEARS)
15.3
17.6
10.7
9.1
1.4
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Dr. MEANS. The preponderance of short-term assets is largely a result of the past focus on Treasury bills in current transactions. The so-called bills-only policy was a very appropriate policy at the time it was adopted. Then there was the "dollar shortage" and we were trying to prevent undue strain on the European balance of payments. But now that there is a dollar surplus, the reverse policy is appropriate.

There is nothing inherent in economic forces which make short-term rates lower than long term. Throughout most of the prosperous 1920's, short-term rates were higher than long term.

And the Federal Reserve Board, by shifting short term into long term, could raise short-term rates and lower long-term rates. Consider what would happen if $10 billion of short terms were converted into long terms. Just how much short terms should be raised and how much of a shift to long term would be required to produce an appropriate rise, is a technical matter. But such a shift could bring the outflow of gold to a stop when that becomes desirable. I believe that a substantial rise in short-term rates should be brought about.

I can summarize my recommendations, insofar as they go further than those of the President's report, as follows:

1. A substantial cut in steel prices combined with a 1-year moratorium on wage increases.

2. A more rapid expansion in aggregate demand through a controlled monetary expansion.

3. A lifting of short-term interest rates and reduction in long-term rates by shifting a substantial part of the Federal Reserve portfolio from short- into long-term assets in order to stimulate internal investment and reduce or eliminate the outflow of gold.

I believe that if the President's very excellent program were modified in these three respects, we could achieve full employment more rapidly and with a level of unemployment well below 4 percent and do this with better than a balanced budget, with some tax reduction, without significant inflation, and with a better balance in international payments.

Chairman PATMAN. Thank you, Dr. Means. Now, after the members of the panel are heard, we will then ask some questions.

Professor Lewis, I believe you are next, please.

STATEMENT OF PROF. BEN WILLIAM LEWIS, PROFESSOR OF ECONOMICS, OBERLIN COLLEGE

Dr. LEWIS. Chairman Patman and members of the committee, my statement will be directed to certain longrun features of the price-wage problem, and to some interesting and, I believe, significant implications of chapter 4 of the January 1962 Annual Report of the Council of Economic Advisers.

Chapter 4 discusses price behavior in a free and growing economy; and it undertakes to furnish guideposts for wage objectives and price decisions in those important sectors of the economy where, by reason of size and organization, private parties may exercise considerable discretion over wages and prices—where, to use the Council's words, at page 185—

> * * * at least in the short run, there is considerable room for the exercise of private power and a parallel need for the assumption of private responsibility.

My statement will be concerned with the fact that the Council now finds it advisable to furnish guideposts for private price and wage decisions; I will not examine the substantive merits of the guideposts which the Council has erected.

One preliminary observation: I approve entirely of the Council's action in providing guideposts. In my judgment, the Council could have done no less; we have already waited a long time.

It is, of course, an anomaly in a free enterprise economy, where price decisions are supposedly dictated by the impersonal forces of competitive markets, for the Government to provide guideposts for price decisions. It suggests, to put the matter mildly, that at least as to those sectors of the economy where guideposts are thought to be particularly useful and appropriate, some doubt may reasonably be felt about the ability of the impersonal forces of the competitive markets to perform acceptably in their pricemaking role.

To be blunt about it, it suggests strongly that in these sectors price competition has broken down. In a price-oriented economic system such a breakdown can be serious. Hence, guideposts; and, it is fair to predict, more action to come.

Let us go back a step. An economic system, or economy, or political economy is a set of man-made and man-accepted arrangements designed (and constantly redesigned) to economize our natural and human resources; that is, to bring about the continuing use of our resources as men, in society, want them to be used. Our resources are limited; not all of the desires of everyone can be satisfied; conflicts of interest must be resolved.

Economizing, by its very nature, involves the disposition of conflicting claims, all of which may be reasonable and "good." Of necessity, we purchase our satisfactions at the cost of other satisfactions foregone. Economic decisions carry denials with every approval, refusals with every grant.

This, of course, is why we care, why we economize. This is why society as a whole—all of society—is concerned with economizing decisions. This is why economizing is society's business.

There is another reason why the business of economizing is society's business. Any economic system—"market," "Marxist," or "mixed"—involves control by society over the behavior of individuals.

An economy points the way and sees to it that the way is followed. Its weapons and sanctions may be direct or indirect, sharp or blunt, but their function is clear: to make individuals behave as society wants them to behave and as they would be quite unlikely to behave in the absence of society's economic controls. It is the function of controls to control, to be unpleasant and even to hurt; and so to affect the actions of individuals. This is true both of the directives and legal penalties of authoritarian systems and the price-cost directives and coercion by competition that characterize free enterprise economies.

But whatever the arrangements and forces, they represent the application of socially sanctioned power to the behavior of individuals; they can properly express no will or purpose other than the will and purpose of society.

Economizing, then, is society's affair. The problem is society's problem, and society must set the standards and provide the answers either by naming the standards and spelling out the answers directly through its political machinery or indirectly by establishing or acquiescing in a set of processes to produce answers which are acceptable because the processes from which they derive are accepted.

It is neither the privilege nor the responsibility of any private individual, however conscientious or statesmanlike, voluntarily to render economizing decisions in the name of society.

The economic system in operation in any country at any time represents the way in which the people of that country, at that time and as they are then persuaded, want the economizing function in their society to be performed.

In our own case, we have long placed heavy reliance upon the forces of (1) free, individual initiative and choice, (2) economic (profit) motivation, and (3) unrestrained rivalry (competition) between independent, profit-seeking sellers and between independent, profit-seeking, or satisfaction-seeking buyers. Through these forces we have hoped to achieve optimum use of our resources at the level and in the directions we desire.

Competitive profit seeking in the free market is the core of our economizing process. Under this philosophy we abhor—we must abhor any substantial lessening of competition as opening the door to the violation of society's pattern of resource use and enjoyment, and as derogating from society in favor of individuals whom society has not selected for the role the performance of the economizing function which society alone is competent to perform or to command.

This is why many of us have attached great significance to the admonitions which have issued increasingly in recent years from leaders of industry and labor to other leaders of industry and labor, and from the White House, irrespective of its occupant, to leaders of industry and labor—admonitions to be responsible in the matter of wage demands and price decisions.

Such admonitions are no part of the apparatus of a free market economy. In an effectively operating competitive market economy they are not only unnecessary, they run counter to its central drive. In an effectively operating competitive free market economy, individual responsibility consists in seeking, within established rules and ways, maximum individual gain.

It is the social-economic role of the individual—businessman, industrialist, laborer, alike—to seek the maximum personal gain which the system will permit him to take. The logic of a competitively controlled economy will not permit the drive of economic motivation to be dulled or its direction to be diffused by the social conscience of individuals. In a competitive economy, competition—not individual conscience and not admonitions to exercise conscience—is society's good right arm for insuring socially responsible economic performance from individuals.

Some of us have seen in the admonitions issuing from high places a growing awareness of a condition in our free market economy which had already attracted our attention and concern. The admonitions have tended substantially to reinforce our developing conviction that in important sectors of our economy, as its exists today, our strong right arm, competition, is in a sling. That competition is more controlled than controlling.

This is not the occasion to debate the precise state and condition of competition in the American economy—whether it is workable or effective or satisfactory or acceptable—or whether bigness is compatible with price competition, or whether there is, in fact, abroad in the land a "dynamic" competition which, if we would only raise our eyes, would console us for any fancied loss of "static" competition. Nor is this the occasion to debate the possibilities and the limits of antitrust.

This is the occasion, however, to state flatly that the American people have been put on notice, by ringing admonitions delivered to leaders of industry and labor, that in the view of President Eisenhowever and President Kennedy, the kind and degree of competition we have and are going to have simply cannot be depended upon to police prices in important sectors of our economy.

Whether price competition is, as some would have it, shutting down for good—an anachronism in our dynamic economy of giant units—or whether it has just gone out for lunch, it is, in plain fact, not on the job in quarters where its absence makes a difference. We cannot be, and we are not indifferent to price behavior. And it follows that we cannot be, and we are not indifferent to the arrangements and processes by which achievement of the price behavior we want can be made certain.

Until a few days ago, however, our concern took the form of fumbling. At the moment, if we look charitably upon ourselves, we are at least fumbling in the right direction. For society to seek to economize by admonition, by appeals to conscience, to responsibility, to economic statesmanship, is to fumble badly.

Commenting, on another occasion, upon the proposition that where competition alone is insufficient to maintain the conduct of giant industrial units at par, the deficiency will be supplied by a newly developed and still developing additive, the "corporate conscience," and hence that appeals to conscience hold hope for a society concerned to economize its resources effectively, I stated: "It is not going to happen; if it did happen it would not work; and if it did work it would still be intolerable to freemen" (Ben W. Lewis, "Economics by Admonition," American Economic Review, May 1959, pp. 384, 395).

What I then had, and still have in mind is that (1) the response to admonitions is very likely to be much less than complete and wholehearted—after all, it asks much of a man, day after day in the regular pursuit of his economic affairs, to donate his interests and those of his dependents and associates, to a vague "social good"—and that (2) it is beneath human dignity for most of society to live its economic life within limits set by the good will and gracious bounty of a precious few whom society does not choose and over whom it has no control, even if the few are persons of unquestionable integrity, with built-in consciences of the highest order and finest quality.

If we are to have rulers, let them be men of good will; but above this, let us choose our rulers, and rule them.

But, of greater significance for our present discussion, the reason we cannot reasonably rely upon admonitions to be "responsible" to serve as a major economizing instrument, is that "responsibility" directed by "conscience" simply has nothing to do with economizing. Economizing is not a matter of choosing good from evil. It is a matter of choosing among competing goods; and an admonition to be responsible tells no one the shape of responsibility or where in the inevitable conflict of responsible actions imposed by the nature of the economic process, the action which society wants—and this is crucial—is to be found. To equate "responsibility to society" with "wise self-interest" offers a semantic, but scarcely a substantive guide; and even to serve as a guide in words the term "wise" has to be mangled beyond recognition.

The simple fact is that 180 million people living and making their living together, require the active presence of an overall organizing and directing force to work out the level and trend and allocation of resource use and the division of product—and this even though everyone of the 180 million is equipped with a burning 24-hour conscience. To rely for this force upon the unguided, uncoordinated consciences of the chance leaders of economic blocs is to abandon order as well as human dignity.

Only society is suited and fitted to deal and play these cards. If its standards are nebulous, at least they are its own, and they can be manifested and carried out with some sense of total purpose in a total pattern which it is society's task alone to design and weave.

And so I welcome the Council's guideposts for wage objectives and price decisions as the logical and reasonable and, hence "to have been expected," second phase of economics by admonition. The Council confirms by explicit reference the authoritative belief implicit in the earlier issuance of admonitions that there are important sectors of the economy where the state of competition leaves considerable room for the exercise of private power over prices; and demonstrates an active public concern over this condition. But it goes further: it calls for responsible behavior and, speaking for the administration, spells out in economic terms relevant to decisionmaking the general overall limits and shape of responsibility.

The Council's venture is modest: it sets limits, it does not prescribe decisions; it concerns itself with levels rather than patterns or structures; it recognizes exceptions; it invites discussion. It also invites departures from the directions which it points. The invitation will be accepted—"Phase 3: Economics by Admonition" will follow shortly.

Because it speaks mildly and with modesty and awareness, it is to be expected that in the months ahead the Council's guideposts will not always be followed; and we shall be treated to representations by noncomplying units that in their special cases, because of peculiar circumstances, they are warranted, if not compelled to step outside the bounds.

But, and this is ismportant, those who stray from the reservation will be impelled to make a case, and the case will be made in the terms which the Council has thoughfully supplied. Being realistic, as well as professionally competent, the Council has included among its terms some which relate to the pattern, as distinct from the level of rates. The allocative function of prices in our economy is nicely outlined on page 189 of the report. At this point, economizing becomes really complicated.

We, too, must be realistic. The Council notes quite correctly that there is "a legitimate reason for public interest" in the content of wage and price decisions. The participants know this, of course; industries and unions regularly carry their cases to the public through extensive and skillful use of all available devices for impressing public opinion. And the Council goes on: "An informed public, aware of the significance of major wage bargains and price decisions, and equipped to judge for itself their compatibility with the national interest, can help to create an atmosphere in which the parties to such decisions will exercise their powers responsibly" (report, p. 185).

The Council is right, within limits. The public can help, in broad, plain cases. But, public opinion is not the most effectively compelling sanction known to mankind; and in the complicated cases involving departures from the Council's broad directions, the exceptions—and these will be the cases that count—the public is simply not technically qualified to sit in judgment.

Enter "Economics by Admonition: Phase 4": The cases will become more individual and unique and, perforce, more technical and more difficult. This will not necessarily be because the participants are sly and grasping, or perverse. It will be simply an outgrowth of the fact that price level decisions, whether we like it or not, inevitably involve decisions on the pattern of prices and, in a price-guided economy, when one figure in the pattern of prices is moved, the whole pattern is affected, and the consequent task of appraisal becomes one for experts—full-time experts. Let us not forget that OPA's 6-foot shelf of regulations was required, not to set forth broad declarations, but to cover the exceptions insisted upon by individual firms.

It is fair to say that we will not move immediately and broadly into public regulation of prices. There will be many halts and many intermediate steps. I am convinced, however, that phase 4 will be the final phase of economics by admonition; and that thereafter, in those sectors of the economy where "there is considerable room for the exercise of private power," public economizing by admonition (with directions, and even with specific directions) will give way to a more precise, more sophisticated, and more powerful public economizing force.

I have great sympathy for the Council's proposition that "mandatory controls in peacetime over the outcomes of wage negotiations and over individual price decisions are neither desirable in the American tradition nor practical in a diffuse and decentralized continental economy." But the same can be said, and just as convincingly, of control by admonition. There is more than a modicum of self-deception in resorting to admonitions to do the work of the market in order to preseve the myth of a market economy. And we certainly deceive ourselves if we dream that it is "practical." The Council forces us to look upon "private power." I am reminded that economizing is society's business.

There will be criticism of the Council for opening the door upon this vista—a vista which the Council would prefer not to see, and which I certainly look upon with no lightness of heart. The Council did not open the door; it was opened decades ago when we embraced bigness in our economy. It was opened wide when the occupants of our White House issued their pleas for responsibility. All the Council has done is to take the door off its hinges. It's just as well, we don't need it; the door is not going to be closed again.

Chairman PATMAN. Thank you, sir, Professor Lewis.

Mr. Eckstein, you are recognized, sir.

STATEMENT OF OTTO ECKSTEIN, ASSOCIATE PROFESSOR OF ECONOMICS, HARVARD UNIVERSITY

Mr. ECKSTEIN. Thank you, Mr. Chairman, and members of the committee. It is a real pleasure for me to be back with the committee participating in its important work.

With a 3-year period of price level stability behind us, it may seem alarmist indeed to speak of a wage-price problem. Rarely if ever in our history have wholesale prices remained so precisely stable as they have these past 3 years. And this stability is not a gratuitous accident of offsetting raises and falls. Even the price indexes for sectors of the economy have remained astonishingly stable, leaving aside the long-term problem areas of services, construction, and government. I think one has to conclude that the price structure of the country has reached a state of equilibrium.

At the same time, the rate of wage increase continued to slow down, and in the last year was slightly below 3 percent in manufacturing, an amount about equal to the rate of productivity advance. It may therefore, seem unduly alarmist to speak of a wage-price problem at this time. Nevertheless, I believe that the present public concern is not misplaced and that it remains one of the toughest problems of economic policy that the Government faces. Let me make my position clear.

I shall make three crucial assumptions. First, I assume that our balance of payments will continue to remain in perilous condition at the least for another year or two. Second, I assume that our cost structure, particularly in durable manufacturing, is out of line with our chief competitors and that it will be extremely difficult to restore equilibrium in our basic balance of payments as long as our exports of manufactured goods suffer from the handicap of that cost structure. Finally, I assume that the United States will not resort to devaluation as a matter of national policy.

It follows from these assumptions that the price and cost structure of the economy must be kept stable even as the recovery continues and unemployment and idle capacity diminish.

How can this goal be accomplished? I think, first, we must come to a realistic understanding of the economic processes which determine the behavior of our wages and prices. Much research has been done by scholars, both for this committee and elsewhere, and while our understanding is certainly imperfect, let me set forth some working principles, drawing on the study of employment, growth and price levels and on extensions of that work, as well as on the general scholarship of this field.

First, on the price side, one can expect price increases when costs rise, when profit targets are raised in oligopolistic industries, and when demand exceeds supply, as evidenced particularly by a buildup of a backlog of unfilled orders.

On the wage side, increases are large when the profits of the companies are large and when unemployment is low. Further, the wage structure in heavy manufacturing industries is very much interconnected by pattern setting and emulation, so that the terms of any single settlement are heavily influenced by the pattern that has prevailed elsewhere. And even outside that sector, there are spillovers to nondurable industries. As for the increases in productivity, the gains are particularly large in periods of rapid recovery, but they slow down as the rate of expansion of output slows down.

Given these working principles, what can we say about the outlook on wages and prices in the coming year in the absence of an explicit Government policy on wages and prices? On the whole, the outlook is good. The very large excess capacity in many industries so far has prevented the buildup of unfilled orders which characterized the inflationary boom of 1955–57. Although the expansion has been rapid, it has so far occurred with little order buildup and, hence, with little excess demand pressure.

Profit targets have not been raised and foreign competition makes a repetition of that ill-fated maneuver of the midfifties unlikely. As for wages, with unemployment expected to continue quite high through the next year and with profits at least somewhat depressed by competition from abroad and the recent cost absorption, there is reason to expect the wage settlements to remain moderate.

It should be pointed out, however, that some increase in raw material prices is inevitable, and that in some lines, such as steel scrap, tin, and copper, a substantial increase has already occurred. Further, as the general margin of slack in the economy diminishes, bottlenecks will begin to occur in some selected products, particularly in industries which will feel the impact of the large increase in the Federal defense budget. It would be unrealistic to expect that we can get through a rapid upswing without some price increases.

But given this generally optimistic view, why is there any need for a wage-price policy? I think there are two reasons: First, the achievement of the goal of price level stability takes on overwhelming importance in our present balance of payments situation and the optimism is only based on conjecture; second, a history of price stability when unemployment ranged from 5 to 7 percent gives little assurance that prices will remain stable at better levels of prosperity. Prices should have fallen, not just remained stable.

In the absence of a policy, one must expect that wage settlements will begin to increase again as profits rise and unemployment declines. As the boom ages and the cyclical recovery of productivity is complete, and as material prices move upward, the hazard of a renewal of inflation in industrial prices becomes substantial.

The time to forestall inflation is not when the prices are in motion, but at the time the strategic price and wage decisions in each business cycle are made. Thus, the unhappy inflation of 1956 and 1957 was determined in 1955, when some key companies raised their profit targets, when the key long-term wage settlements were signed, and when the backlog of unfilled orders was built up in the durable goods industries. There was not much inflation in 1955; but in 1956 and 1957 the inflationary process unfolded inexorably.

It seems to me that in order to avoid a repetition of previous inflationary experience in the latter part of 1962 and 1963, the following conditions have to be met in the near term: First, where management has discretionary market power to set prices in accordance with profit targets, it must exercise this power with restraint.

Second, the rate of wage increase in the major negotiations must be kept to the long-run rate of increase of productivity. Let me stress that it is quite impossible to achieve one of these goals without the other. If business does not exercise restraint on the price side and thereby keep profits at moderate rates for this stage of the cycle, there is not a ghost of a chance that wage demands will be moderate. We know from detailed examination of the historical record that the rate of profits is a crucial determinant of the rate of increase of wages. Conversely, we know that the rate of increase of employment costs is a major determinant of prices. Only a symmetrical approach, with Government encouraging the nobler impulses of both parties to act with restraint in the national interest, stands a reasonable prospect of success.

Let us now turn to the specifics of policies.

At the top of the list of any agenda for policy must be the improvement of the competitive structure of the economy. Vigorous antitrust policy, designed not only to punish wrongdoing but also to promote the objectives of economic policy, can lead to positive results, as the experience in the electrical machinery industry has now shown. Even more important is competition from abroad. A continued and strengthened liberal policy on trade of manufactured goods, particularly of heavy industry, is the surest check on this set of domestic prices. But these structural measures are not enough in the short run, and it would be unrealistic to expect them to stabilize the industrial price structure in the present business cycle expansion.

Limited strategic intervention by Government is a crucial ingredient in sound policy. Because controls are abhorrent in peacetime and divert an excessive amount of business effort into coping with the Government, intervention must be limited to those very few price and wage decisions which are pattern setting for large sectors of the economy.

If the strategic price and wage points of the economic structure are kept stable, the industrial price-wage structure as a whole can be kept stable, aside from some inevitable price rises in bottleneck sectors that should be offset by declines in industries in distress.

What form should the intervention take? I think there are four possible approaches. First, there is the behind-the-scenes approach, in which high administration officials negotiate a wage settlement with labor and management, presumably discussing price behavior at the same time. The history of this approach is rather poor. It has typically led to inflationary settlements. But I think one should add that there is now a greater appreciation of the inflation aspect of the settlements.

Creation of a noninflationary climate of public opinion is a second approach. It makes it possible for business and labor leaders to act in the national interest without facing adverse repercussions from their immediate political constituencies. Fact finding, prescription of general guidelines, and education of the public on the inflation issue are part of this approach.

A third approach creates a public opinion which is hostile to private decisionmakers acting in an inflationary manner. This approach assumes that it is impossible to get business and labor leaders to act responsibly except out of fear. Public hearings in an unfriendly environment are typical of this approach.

A fourth approach imposes a system of controls, perhaps of a very mild sort, such as an agency with a power to suspend price and wage increases, or even of a stronger type.

In our staff report we stated that the road of intervention not be traveled with enthusiasm. I do not believe that there is now justification for engaging in the third or fourth approaches, but that some combination of the first two approaches is necessary.

The administration has taken several important steps already. The President's appeal to the steel companies not to increase their prices last October when an automatic wage increase went into effect was a step of major importance. Some may feel that steel prices would not have risen in any event because of poor market conditions; I do not share this view.

But whatever the correct analysis, the basic fact remains that steel prices were not increased and that the President showed that he cared about prices. Presidential concern has also been expressed and the willingness to act implied in the President's statement of January 19, when he said that wages should be tied to productivity this year, and "This is not merely an exhortation, it is a necessity for all of us."

Another important step is the publication of the Council of Economic Advisers report in which they set down guideposts for noninflationary wage and price behavior. While couched in somewhat more general language than I would have chosen, the implications of these guides in the present context are clear. They say—

> the general guide for noninflationary wage behavior is that the rate of increase in wage rates (including fringe benefits) in each industry be equal to the trend rate of overall productivity increase * * *. The general guide for noninflationary price behavior calls for price reduction if the industry's rate of productivity increase exceeds the overall rate * * * for an appropriate increase in price if the opposite relationship prevails * * *.
>
> The most important modifications are the following: (1) Wage rate increases would exceed the general guide rate in an industry which would otherwise be unable to attract sufficient labor; or in which wage rates are exceptionally low compared with the range of wages earned elsewhere by similar labor because the bargaining position of workers has been weak in the particular local labor markets.
>
> (2) Wage rate increases would fall short of the general guide rate in an industry which could not provide jobs for its entire labor force even in times of generally full employment; or in which wage rates are exceptionally high compared with the range of the wages earned elsewhere by similar labor, because the bargaining position of workers had been especially strong.
>
> (3) Prices would rise more rapidly, or fall more slowly, than indicated by the general guide rate in an industry in which the level of profits was insufficient to attract the capital required to finance any needed expansion in capacity; or in which costs other than labor costs had risen.
>
> (4) Prices would rise more slowly, or fall more rapidly, than indicated by the general guide in an industry in which the relation of productive capacity to full employment demand shows the desirability of an outflow of capital from the industry; or in which costs other than labor costs have fallen; or in which excessive market power has resulted in rates of profit substantially higher than those earned elsewhere on investments of comparable risk.

The crucial wage settlement in this coming year is generally acknowledged to be the steel settlement. I therefore apply the Council's guidelines to this situation: the general guide for noninflationary wage behavior suggests a settlement in the range of 2.5 to 3 percent a year. The modifications suggest that, if anything, the settlement should be smaller, since there is excessive unemployment in steel, the range of wages is rather high compared to other wages, and the bargaining position of the workers has been particularly strong. On the price side, the general guide says that prices should be stable, since the rate of productivity advance has been about equal to the economywide average. The modifications suggest that prices should fall, since there is excess capacity and since there has been excessive market power.

Whether the Government seeks to apply only the general guides or the even tougher modifications to wage and price behavior in this industry depends upon the haste with which it seeks to improve our cost position. It is my own belief that the modifications are a counsel of perfection at the present time. They represent too drastic a break with historical patterns, particularly in the light of other important wage settlements of the past 12 months. Price reductions are also too much to expect in the midst of a rapid expansion.

How should the Government seek to assure noninflationary behavior in this industry? So far, apart from general exhortation and an attempt to create a favorable public opinion, the Government has relied on the behind-the-scenes approach. Given the specifics of the steel situation, including the experience of our Secretary of Labor, this approach may prove successful. As an outsider to Government, I would feel more secure about the matter if the public had a means of passing its own judgment in this situation. Either a public fact-finding panel or a publicly available statistical analysis by the staff of the Council of Economic Advisers would give the public a means for judgment and also a means for debate. Let me add, that ex-post pronouncements on the soundness of settlements by the principals in a behind-the-scenes negotiation are not a sufficient protection of the public interest.

Before closing, let me raise three other areas of public policy which are of particular relevance for the wage-price problem. First, developments in the agricultural program will have an important effect on food prices, which loom large in the cost of living. Obviously, it is undesirable to maintain farm income by methods which raise consumer prices.

Second, now that President Kennedy has expressed serious concern about our strategic stockpile, an important instrument for preserving price stability becomes available. The piling up of these huge stocks inflated raw material prices dramatically in the early 1950's. Let the decumulation serve as an offset to the otherwise inevitable rises in raw material prices during the business cycle expansion.

Finally, I turn to the knotty problem of the continued inflation in the construction industry. Wage increases have been averaging over 4 percent. Price increases have been only between 1 and 2 percent during the past year, having been moderated by declines in building material costs. There is no simple solution to this problem. Productivity gains are slowed by local building codes. Wages are negotiated locally. The courses of action open to the Federal Government are very limited. Perhaps there is an area here in which unions have excessive market power. In any event, when the Federal Government contemplates antirecessionary fiscal policies, it must take the continued inflation in construction into account. The attractiveness of public works is seriously diminished as an instrument of policy as long as such expenditures are channeled into a sector in which inflation continues unchecked.

I have touched on a good many topics in this statement and have tried your patience by its length. I have done so because I believe that the future growth of the American economy is contingent upon a solution to the wage-price problem. Given our balance-of-payments situation, we will pay the price of slow growth and continued high unemployment if our wage and price fixing arrangements continue to have an inflationary bias. It may strike us as preposterous that millions of people should be kept out of work and the rate of expansion be throttled just to keep prices and wages stable. But the simple fact is that a responsible government has no other choice.

Chairman PATMAN. Thank you, Dr. Eckstein.

Professor Brozen, we would be delighted to hear from you now, sir.

STATEMENT OF DR. YALE BROZEN, PROFESSOR OF BUSINESS ECONOMICS, GRADUATE SCHOOL OF BUSINESS, UNIVERSITY OF CHICAGO [1]

Dr. BROZEN. Thank you, Mr. Chairman.

The Council of Economic Advisers should be complimented for its recognition of the fact that wage rates in some industries are too high for the health of the economy and that wage rate increases must be smaller in the future if we are to have more rapid economic growth and decreased unemployment without inflation. The Council recognizes that the upward movement of some wage rates and prices is the result of agreements between strong unions and employers and that "the post-Korean years were marked by the coincidence of relatively large wage increases with declines in industry employment." The fact that unduly high wage rates decrease the number of jobs available and the number of people working in an industry is obviously understood by the Council and is clearly implied in its report.

Several things are left unsaid, however, which should receive explicit recognition. The Council dwells on the inflation which may be caused by unduly large wage rate increases. What they fail to recognize is that unduly large wage increases for some workers come not only at the expense of causing some to become unemployed but also at the expense of workers in other sectors of the economy.

To illustrate in terms of the experience of one State, we find that wage rates in transportation equipment manufacturing in Michigan not only rose more than in other manufacturing industries in the State, but also rose from 1950 to 1957 by 10 percent more than in the same industry in the other four East North Central States (Wisconsin, Ohio, Indiana, and Illinois). Overall employment in the industry declined in part as a result of overly large employment cost increases. In Michigan, the decline was greater than for the industry as a whole. Between 1954 and 1958, there were 85,000 more jobs lost in Michigan than in the other 4 East North Central States. In 1954, Michigan employed 41,000 more workers in transportation equipment manufacturing than the other 4 States. In 1958, it employed 44,000

[1] The data on which these remarks are based were assembled by Dr. Stephen Sobotka and will be published soon in his "Profile of Michigan" (New York: Free Press, 1962).

fewer workers in the industry than the other States. Michigan has become a depressed area, in employment terms, largely because employment costs have been increased so drastically in its major industry.

Not only has employment in Michigan suffered; in addition, workers in other industries in Michigan have suffered. Those becoming unemployed in the transportation equipment industry or failing to find employment in this industry have sought jobs in other fields. Many have found jobs in other manufacturing industries. The consequence has been, however, lower compensation for those in these other industries. Their hourly earnings rose 6 percent less than the rise in these same industries in the other four East North Central States. (Employment in these industries in Michigan increased more than in the other States, but this is a less productive use of the labor than its employment in transportation equipment.) If wage rates and other employment costs in transportation equipment had not been raised so much in Michigan, hourly earnings would have gone up more in the other manufacturing industries. High hourly earnings for autoworkers have come at the expense of workers in other industries.

This brings us to the second point which the Council has failed to make explicit in its concern over the inflation impact of unduly large wage rate increases. The power of unions is focused on certain sectors of the economy, such as transportation, auto manufacturing, and coal mining. Their use of power and the consent of employers to agreements which incorporate unduly large increases in the cost of employment decreases the number of jobs available in these sectors of the economy. Since these are industries in which output per man-hour is high, and men are forced to take jobs in low productivity sectors of the economy who otherwise would have found jobs in these high productivity industries, the net result is a lower average output per man-hour for the economy than otherwise would have been attained. Excessive wage hikes in some parts of the economy cause our productivity to rise less rapidly.

The experience of coal miners illustrates this point. Coal mining hourly earnings rose by $1.95 or 163 percent from 1945 to 1960. Bituminous coal mining employment dropped from 380,000 to 170,000. By way of comparison, in the same period, manufacturing production worker hourly earnings rose $1.24 or 122 percent and manufacturing employment rose from 15,524,000 to 16,762,000. The differential in hourly earnings in favor of coal miners increased from 18 to 39 percent. Many of the coal miners who lost their jobs or men who would have found employment in coal mines took manufacturing jobs. In these jobs, their productivity is lower than in coal mining. If we had more coal miners and fewer in other industries today, average output per man-hour in the private sector of the economy would be higher and the record of the annual rate of increase in output per man-hour would be better.

Excessive wage hikes in some industries slow the increase in output per man-hour in the economy as a whole for another reason besides forcing people out of high productivity into low productivity occupations.

To make men worth employing in coal mining or auto manufacturing at high wage rates, the amounts of capital per man employed must be increased enough to raise productivity of the men remaining in the industry to the point where employment costs can be covered. (This is the process usually known as automation.) Concentration of large amounts of the available capital on a few men reduces the capital available per man in the rest of the economy. With less capital per man, output per man-hour in other industries is lower than it otherwise would be. The distortions in the allocation of capital caused by distortions in the wage structure prevent output per man-hour from reaching otherwise attainable levels and cause a poorer record of increase in output per man-hour.

Finally, a word should be said about the suggested use of the rate of increase in output per man-hour as a general guide for noninflationary employment cost increases. The Council is careful to emphasize that changes in average output per hour cannot be used as a rule. They carefully and correctly emphasize that increases in the average for the economy should be used as a guide, not increases in individual industries or companies. A careless reading of the Council's admonitions, however—there was no collusion between Ben and myself on the use of that term—might lead one to believe that, with a 2.4-percent increase in productivity, in the private sector over the long run, a 2.4-percent increase, on the average, in employment costs per hour in each industry would be noninflationary or cause no change in income shares or otherwise be neutral in the Council's sense of neutrality. I can conceive of circumstances in which employment costs should increase by more than 2.4 percent per year on the average, and others in which it should not increase at all if the Council's objectives are to be served. This, however, is a complicated question concerning the relationship between movements of marginal productivity and average productivity which I will not take the time to discuss here.

The main point I wish to make is that part of the increase in output per man-hour in the economy as a whole is the result of the movement of workers out of low productivity jobs in some industries into high productivity jobs in others. They move in response to the higher earnings available in higher productivity jobs. If all the increase in output per man-hour comes from this source, let us suppose, then no wage rate need be changed in order to raise average hourly earnings. Earnings would rise on the average because of a decreasing number of people in low wage, low productivity jobs and an increasing number in high wage, high productivity jobs.

Various authorities have estimated that output per man-hour rises by 0.6 to 0.8 percent per year because of the shift from low to high output per man-hour jobs. Since hourly earnings change in a similar direction with no change in hourly wage rates under these circumstances, this implies that the Council's guide should be a 1.8 percent or less per year increase in wage rates if output per hour rises 2.4 percent per year. This is not clear in the Council's report and, I believe, was not recognized by the Council in its thinking when preparing the report.

In conclusion, I should emphasize that the correct rule or guide, or whatever we want to call it, for wage setting is not the overall change in the economy as a whole in output per man-hour. The Council recognizes this, although it says otherwise. The Council implies the correct rule or guide when it proposes that "wage rate increases would exceed the general guide rate in an industry which would otherwise be unable to attract sufficient labor" and, in another paragraph, proposes that "wage rate increases would fall short of the general guide rate in an industry which could not provide jobs for its entire labor force." This is exactly how wage rates do behave in a free market. So what the Council has said is that supply and demand in free markets should determine wage rates. To this I say "Amen!"

Chairman PATMAN. Dr. Means, I would like to ask you a question about the goal that you speak of in your paper.

We seem to base our interest rates, particularly the short-term rate, on our fear of the movement of gold out of the country. Now, under recent laws, it is possible for a higher rate of interest to be paid on foreign deposits than on domestic deposits. Isn't there some way to use that to prevent the increase of short-term interest rates all over the Nation, all over the 50 States, just in order to take care of balances in New York?

Dr. MEANS. I would have to look into that before I could give you a clear answer.

Chairman PATMAN. But that is the real problem, isn't it? The balances are created in New York; and we are raising interest rates on everybody, all over the Nation, just to take care of that situation.

Dr. MEANS. I do think that there is real need for increasing the likelihood of foreign banks, central banks, leaving their deposits in this country. I think those deposits could be protected in a way that does not involve a differential interest rate but some kind of a short-term guarantee.

Chairman PATMAN. You mean if gold should begin flowing out again in a way which you would consider dangerous, these banks that operate overseas could bring more back over here?

Dr. MEANS. That is right; and certainly not take it out.

Chairman PATMAN. How many major banks operate over the country?

Dr. MEANS. In this country?

Chairman PATMAN. Yes. Five or six?

Dr. MEANS. No. I do not have that in mind.

Chairman PATMAN. Well, something like that. Five or six. And the American Express Co. operates banks in foreign countries, does it not? And your theory is that if there should be a drain in our gold, they could help us by bringing money back over here?

Dr. MEANS. I think so; yes.

Chairman PATMAN. It seems unusual to me; I cannot understand why all of the people should suffer, all over this Nation, just to take care of a localized situation like this.

Do you agree with me on that, or do you say it is necessary that the situation be as it is?

Dr. MEANS. I would agree with you on that; and these problems have to be dealt with on the basis of a background of national policy, and not entirely in the self-concern of the particular banks.

Chairman PATMAN. What do you believe could be done now with the Federal Reserve in cooperation with the bankers, and particularly those that operate overseas, to solve this gold problem without being disturbed domestically by this short-term interest rate?

Dr. MEANS. I think the shift of balances, short-term balances, between this country and other countries, is dominated by the short-term interest rate.

Chairman PATMAN. We are too apprehensive and too fearful of deposits coming from other countries here, when we do not know exactly how much will come, and certainly there is a limit to the amount that can be brought over here.

Dr. MEANS. I do not think there is a real limit. This country is acting in some degree as an international bank, both for other banks, for foreign banks, and for foreign businesses; and over a long period, if we are going to grow in this function, we can expect our short-term balances to build up.

An ordinary bank is in the position where it hopes to grow, and its short-term obligations in the form of deposits with customers have got to grow. We would not think twice about the fact that an individual bank's short-term obligations increased, provided their reserves were adequate. The same would be true for this country in relation to other countries.

I see no serious objection to a long-term trend of rising short-term deposits in this country. I would not want to see our balance of payments exactly equated. I think we should look for a gradual rise in our short-term obligations abroad.

I do think that we must bring the export of gold to a stop sooner or later; although, as I have indicated in my testimony, I think it would be desirable to have some further outflow of gold.

Chairman PATMAN. But you really think that the banks in this country that operate through foreign branches would be able to solve this problem by bringing their money from overseas.

Dr. MEANS. Well, for instance, there was a big export, or rather a shift, of balances to Canada, in this last year, because of higher interest rates, short-term rates, in Canada than in this country. And these are private balances and not primarily bank balances.

Chairman PATMAN. Have you noticed that the Federal Reserve banks last year, although they held more Government securities by a billion and a half than in the preceding year—received greatly reduced amounts of interest? In the last half year, I noticed yesterday, it was almost $100 million less than the similar period in 1960. And did you look into that to see what the cause of it was?

Dr. MEANS. No, I did not. But I would say that how much interest the Federal Reserve obtains on its portfolio ought to be a very secondary consideration; that the primary consideration should be what is the appropriate money supply to support high employment and what is the appropriate relation between short and long term to maintain a balance of payments.

Chairman PATMAN. My thought was not in opposition to what you say. I was not arguing that. I was just stating the fact that there is a billion and a half dollars more money in bonds, and yet the income was considerably reduced. I just wondered why that was done.

Dr. MEANS. I do not know.

Chairman PATMAN. All right. Thank you, sir.

Senator Douglas?

Senator DOUGLAS. I was particularly interested in your charts 2 and 3. Chart 2 shows that while the real money supply increased by a little less than $4 billion the first year, nevertheless wholesale prices remained stable.

Dr. MEANS. Yes.

Senator DOUGLAS. And that was because there was a commensurate increase in output, so that the ratio between the two was not increased?

Dr. MEANS. That is right.

Senator DOUGLAS. During this past year the Federal Reserve Board at least on paper reversed its longtime policy of dealing in bills only. And your chart shows an increase in their holdings of Government securities of approximately $1 billion. I think this is highly desirable. But I was interested that you also show that they increased their holdings in short-term securities, defining the short term as a year or less, by $2 billion, and decreased their holdings in medium term by $1.6 billion.

Would you say that they had embraced the doctrine of investing in long-term securities, as well as in bills only, very enthusiastically?

Dr. MEANS. I think I would have to give two answers to that.

On a broad basis, no, they have not; and I would urge them to go much further in the direction of nonbills; primarily because our whole position has changed over the time when a bills-only policy was appropriate.

But the second answer I give is that apparently they have decided to maintain short-term interest rates relatively stable; and so, with that objective, they have shifted into long term enough so that with our expanding economy the expansion of money has not brought a reduction in short term.

What I want is a significant rise in short term and a reduction in long term.

Senator DOUGLAS. I would like to put the next question in two parts.

Would you favor the expansion of Federal Reserve holdings in coming years to provide member banks with an increase in the amounts they hold primarily by the purchase of long-term securities?

Dr. MEANS. At the present time, yes.

Senator DOUGLAS. I agree with you on that.

The second question I would like to ask is: Would you favor the Federal Reserve selling short-term notes and simultaneously buying long-term bonds, so that there is a shift from short-term to long-term holdings?

Dr. MEANS. I believe so. But this is a highly technical matter, and I would want to know more about the techniques than I do, to be certain of that.

Senator DOUGLAS. What effect would that have on the short-term interest rate?

Dr. MEANS. I think it would raise short-term interest rates and reduce the long-term: and that would be constructive on both sides.

Senator DOUGLAS. That is just what you are advocating; is it not?

Dr. MEANS. Yes.

Senator DOUGLAS. The sale of short-term notes would depress the price of short-term and raise the yield and consequently raise the rate.

Dr. MEANS. What I have in mind is this, that if you are going to expand the money supply significantly, I mean, another 4 or 5 percent, then if you make the whole expansion in long term, that may be enough. It may be that they do not have to reduce.

On the other hand, it may be that they need to actually make a shift in addition to expanding in long term.

Senator DOUGLAS. And the purchase of the long term would have an effect?

Dr. MEANS. It would reduce long-term rates.

Senator DOUGLAS. Without raising the price, it would reduce the yield?

Dr. MEANS. That is right.

Senator DOUGLAS. Well, I agree with that, and I hope that the representatives of the Federal Reserve Board, who I presume are in the room, will bring that recommendation to the attention of the Board.

Now, there is one general question I would like to ask to all members of the panel.

Have any one of you made any studies of the long-run movement of labor cost per unit of output; namely, hourly earnings divided by hourly output, so that you can get a figure on labor cost per unit of output; which is, I think, a far more significant figure than a figure on hourly wage rates?

Dr. MEANS. I have done that with the steel industry with a great deal of care from the period 1926–29 to the present.

Senator DOUGLAS. What does it show?

Dr. MEANS. That is with particular emphasis on the post-1953.

Senator DOUGLAS. What does it show?

Dr. MEANS. That is in this book of mine.

Senator DOUGLAS. Well, will you tell us about it?

Dr. MEANS. I would have to look it up to see.

In steel the labor costs per unit of output have gone up somewhat.

As I was indicating in my testimony, since 1953, the profit margin has accounted for something like three-quarters of the price rise, and I attribute about a quarter of the price rise to the increase in labor cost, direct and indirect.

Senator DOUGLAS. Dr. Eckstein, you have worked on this question. What are your conclusions, on steel and on general productivity?

Dr. ECKSTEIN. In the case of steel employment cost as a percent of total revenue, has stayed about constant, varying somewhat year by year. Employment costs hit a very, very large fraction in 1948, but basically they remained about constant. Employment costs remained the same fraction of total revenue through these years; which means that employment costs per unit rose as much as prices did.

In the case of the economy as a whole, we have recourse to the Bureau of Labor Statistics' authoritative computations, which show that employment costs per unit rose until about 1958, but since then have remained stable, and perhaps even have fallen a little.

Senator DOUGLAS. Labor costs per unit of output?

Dr. ECKSTEIN. Yes, labor costs per unit of output have actually fallen a little since 1958, if I recall the Bureau of Labor Statistics' study correctly.

Senator DOUGLAS. And prices have remained steady?

Dr. ECKSTEIN. And prices have remained steady.

Senator DOUGLAS. Of manufactured goods?

Dr. ECKSTEIN. Of manufactured goods.

Senator DOUGLAS. Anyone else?

Dr. Brozen?

Dr. BROZEN. I think one point that should be considered in talking about labor costs per unit of output in an industry, let us say, like the steel industry, is that the product has been very much improved in quality over the last 20 to 30 years, and some of this improvement in quality is at the price of using more expensive alloy materials, for example. As a result it is not exactly a simple problem to relate the labor costs per unit of output to the particular units of output that we are talking about. You cannot simply take tons of output because of these more expensive materials entering into a higher quality product.

Senator DOUGLAS. What do you think would be the significant test?

Dr. BROZEN. You would have to look at what is being done in terms of the costs of adding marginal units of capacity, marginal labor costs that are involved; and those may behave somewhat differently than the average has behaved.

Dr. MEANS. The difference between Dr. Eckstein's figures and mine in the case of steel I think should be brought to your attention.

I think if I were to simply divide actual product into actual wages, I would agree with him. Actually, there was an important decline in the ratio of operation, and steel costs, labor costs per ton, are very sensitive to the level of operation.

If you take just production workers alone, perhaps 25 percent is overhead cost, repair crews and so forth; with the result that if you increase the rate of operation 20 percent, you have a very important reduction in cost per unit.

I have taken the earlier figures and the later figures and converted them to a constant rate of operation; and that is where I get my figures.

If he were to do the same thing, I think he would get the same result. So that it is not that our figures are in disagreement, but that what we are trying to measure is different. And if the steel industry averages around 80 percent of capacity, you will find that the labor cost per unit of output has not gone up anything like the rise in the price per unit of the product.

Also in the steel industry, constant improvement of product does not enter significantly, if at all, into the price index; because the steel index is made up of very standard products. They may add products from time to time, but no change in quality occurs, such as occurs in an automobile, where you cannot measure the quality.

Dr. BROZEN. I would like to add, on the question of the use of the steel index, though, that those are the quoted prices of steel companies, and not necessarily the transactions prices. We have to look at the transactions prices to see what is actually going on, rather than the quoted prices.

Dr. MEANS. The industry tells me a very small proportion is not at the quoted prices.

Dr. BROZEN. Well, one of the studies presented to this committee by the National Bureau on the method of computing the wholessale prices indicated that a great many of the transactions prices were considerably different than the prices quoted to the Bureau of Labor Statistics.

Dr. MEANS. In the steel industry?

Dr. BROZEN. In the steel industry.

Dr. MEANS. That conflicts with other information that I have.

Senator DOUGLAS. Am I correct in my understanding of the coal industry, that their tonnage rates have been held relatively constant over a long period of time; that the increase in hourly and daily earnings has been caused by a great increase in productivity in coal?

Dr. MEANS. I am not an expert on the coal industry. I could not answer that.

Dr. BROZEN. My memory is only approximate on the figures, but in the last 12 years or so I think that the output per man-day has gone from something like 6 tons per man-day to 12 tons per man-day.

Senator DOUGLAS. That is my understanding. And this illustrates in a very sharp way the differences you get if you take productivity in a general industry or take general productivity, because I think that labor costs per ton of coal have remained approximately constant during this time. Mechanization of mines has been encouraged. Output has, as Dr. Brozen says, greatly increased. Daily earnings have increased tremendously. And we have the spectacle of high daily wages based on productivity of that industry, which seem very high in relation to the general level of earnings in other industries.

Dr. MEANS. I fully agree with the Council of Economic Advisers that the productivity for the Nation as a whole is the crucial guide; not the productivity for the particular industry.

On the other hand—and I have always been troubled by this—it seems to me in the more concentrated industries it is easier for prices to go up when costs rise than for prices to go down when costs declined. And if the productivity in the particular industry goes up more rapidly than that for the economy as a whole, for instance, by my figures productivity in the steel industry is between 4 and 5 percent a year since 1953, and if steel wages go up two and a half, or whatever, a year, then steel prices ought to come down proportionately, not in absolute proportion, but to a corresponding extent.

Dr. BROZEN. I think we have to be careful in looking at figures. Part of this increase per man-hour comes at the cost of using a great deal more equipment per unit of output. So capital costs per unit have gone up in this period as well.

Dr. MEANS. I do not think that is true in the steel industry. The technology has been improving the capital equipment to such an extent that the cost per unit of output, the capital cost, has been going down.

Take the oxygen furnace, which is the old Bessemer converter, which uses oxygen instead of air. That was developed in Austria and is capable of converting iron and scrap into steel; at a very much smaller labor cost and a very much smaller capital cost per ton. And the same is true of some of the other newer equipment.

Chairman PATMAN. Thank you, sir.

Mr. Reuss?

Representative REUSS. I was very interested, Dr. Brozen, in your discussion of the effects of differences in wage rates. Would you agree that, by and large, speaking in generalities, that economy is best off in which the differences between the wages and salaries received by different segments of the population are relatively small rather than relatively large? That is to say, if one man makes $4 an hour and another man makes $1 an hour, the man who makes $1 an hour is not likely to have enough income to be able to buy the things that the man making $4 an hour produces. Therefore, as a general starting principle, would you not agree that that economy is best able to clear the market of goods that are produced where remuneration is such that it tends toward greater rather than lesser equality?

Dr. BROZEN. That is an awfully difficult question to answer. As a matter of historical tendency in most economies as they develop, wage differences tend to decrease over time; in the United States in particular, as education of the less educated sectors of the population has risen relative to the more educated sectors of the population, wage differences have decreased because the increasing skill and productivity of these people has brought them closer to the productivity of the more highly educated. As a matter of historical tendency, it has occurred.

As to arguing whether it is a good or a bad thing, well, we do not like to see big income differences between people simply as a matter of our belief in the equality of the individuals.

Representative REUSS. Equity aside, though, isn't something approaching approximate equality in wages more likely to take the product off the market in a satisfactory way than if there are vast and sweeping differentials?

Dr. BROZEN. No. I do not think that has anything to do with the issue of whether we have sufficient purchasing power to buy the product or not. I think that comes down more to the thing Dr. Means has talked about in terms of the money supply of the economy. If the money supply is adequate and growing along with the growth and production, the product will be removed from the market.

Representative REUSS. Is everyone at this point agreed with Dr. Brozen's point, that similarity of wage rates has nothing to do with the ability of the system to buy that which is produced?

Dr. Eckstein?

Dr. ECKSTEIN. I think it depends on the broadness of view that you take on the matter. I think it is true, and I think this is the point that Professor Brozen has in mind, that the workers who get $3 an hour spend as much of their income as those who get a dollar and a half an hour, namely, most of it. So pushing the top down a little and the bottom up a little is not going to lead to anything very great in the total propensity of people to spend their incomes.

In a broader sense though, I think it is really a fundamental point, and a correct one. It is true in our economy that in some of those industries in which wages are the highest and have risen the most, costs have gotten most out of line relative to other countries; and it is this spreading of the wage scale which has occurred in the last 7 or 8 years, with the people at the bottom gaining less relative to the people at the top, which has put us into this unhappy state where we have a balance-of-payments deficit, where we have to pursue these overly cautious fiscal and monetary policies, which in turn lead to unemployment, slower growth, and so on.

Representative REUSS. Thank you.

Now let me get back to Dr. Brozen, if I may.

I am a little puzzled by two of the points you made in your paper.

You say that if we had more coal miners today and fewer former coal miners in other industries, our average output per man-hour in the private sector would be higher.

Yes, but wouldn't this be largely redundant? By hypothesis we are producing the amounts of coal that the economy needs. Did not those excess coal miners have to get out of coal mining?

Dr. BROZEN. Well, in part the coal miners that got out became excess, because wage rates became so high that it paid to replace the men with equipment. And then these men in effect were moved into lower productivity occupations.

Now if that capital had not been used to buy equipment for making the remaining coal miners more productive, the coal now being produced would be produced with a larger number of men. Output per man-hour in coal mining would not be quite as high as it is; but it would be higher in other sectors of the economy than it now is. So that the average productivity per man-hour would be higher than it now is.

Representative REUSS. The question is whether they got out because of excessively high wages or because of the great application of capital equipment to each worker, which in turn may have been induced by high wages, it is true.

Dr. BROZEN. As I was arguing, essentially, for producing the same amount of coal, let us say, with a larger amount of men, you would have a somewhat lower output per man per day now for coal mining than you now have, but you would have a higher output per man per day in other industries, and that would more than compenstate for the fact that average output per man day in the industry would be lower.

Representative REUSS. You make a slightly different point where you say to make a man worth employing in coal mining or auto manufacturing you have to apply a lot of capital equipment to him, and when you do that, then you have less capital to apply to a textile worker or whatever low wage person there is.

Dr. BROZEN. Exactly.

Representative REUSS. Is that true at conditions other than full employment? I should think not. I should think there is always potential capital available that could be brought into play, except where you do have full employment.

Dr. BROZEN. I would argue that our supply of capital is whatever it is as determined by the savings habits of the population, the profit retention policies of corporations, the contractual savings required in installment purchases, and so on. Given whatever the supply of savings is, then it is allocated in ways which contribute less to overall productivity than it otherwise could do for us. Even in conditions where you have some unemployment, you have whatever supply of savings is available for applying to various uses.

If we were to increase the total supply of savings in periods when we have some unemployment, I think we would snap out of those periods of unemployment faster than we now do. In part we have these periods because wage rates are too high relative to the value of the man with the equipment available. If more equipment, more capital, were made available, then it would be worth employing these people at the high wage rates set at such times, and you would have less unemployment.

But that would take operations, then, on our tax laws in order to encourage a greater rate of saving and investment. Something like the corporate income tax, for example, is one of the biggest barriers to a higher rate of savings and to a higher rate of corporate profit retention and serves to slow the rate of capital formation and to make it more difficult to employ all the people that might be employed at the present high wage levels.

Senator DOUGLAS (presiding). Senator Proxmire?

Senator PROXMIRE. I am going to start with Dr. Means.

For your statement, Dr. Means, you talk about the widening profit margins in steel. You deal with steel as a sort of a typical industry. And what has impressed me lately is the fact that overall profit margins are much lower now than they were, say, 15 years ago, from everything I have seen; and also I understand that profits, with regard to the gross national product, for example, are about one-half of what they were 15 years ago; whereas with virtually everything else, every other factor of production other than capital, that does not seem to obtain.

I am wondering, therefore, if it is dangerous to generalize from this picture that you paint of what happened in steel.

Dr. MEANS. I had thought the thrust of my argument was that steel was peculiar.

Senator PROXMIRE. I missed that. I am glad to hear it.

Dr. MEANS. It is to me very peculiar. My studies have rather led me to the conclusion, which is entirely on the basis of circumstantial evidence, that a decision must have been made back in perhaps 1951, somewhere in that period, to widen the profit margin. What happened cannot be explained otherwise, as far as I can see.

A decision was made to widen the profit margin and to make the profit margin in steel more commensurate with the profit margin in automobiles, in chemicals, and so forth, where the profit margin on the leading companies tends to be very high.

This effort to bring the steel industry up into the same profit margin bracket, profit rate of return bracket, with some of the other more concentrated manufacturing industries, was a basic factor in giving us a rise in the wholesale price index from 1953; and if that decision had not been taken, I doubt if we would have seen a very great increase in the prices of steel and the steel-using industries throughout the period. Their behavior would be more nearly like that of the rest of the manufacturing industries.

Senator PROXMIRE. Is the 30 percent of capacity break-even point which you say applied in 1959 still true, or is it lower?

Dr. MEANS. No; it has shifted upward in the last 2 years slightly. You can see that the finished steel price index has slid down a little bit in 1961 over 1959.

Furthermore, the labor costs have gone up slightly. I am speaking of labor costs per unit of output, and not wage rates, which have gone up more. The result is that the profit margin has been slightly narrowed. At the same time, I believe there is ample room for a very substantial reduction in steel prices. I would think perhaps as much as 10 percent; certainly well over 5.

Senator PROXMIRE. This 30 or 35 percent break-even point—is that pretty well accepted?

Dr. MEANS. Other people have found it. I do not know whether that is well accepted or not.

Senator PROXMIRE. I had heard 40 percent, and I was surprised it had gone down as low as 30 percent.

Dr. MEANS. Not below 30 percent, but close to 30 percent.

Senator PROXMIRE. You talk about the real money supply, and in your chart 2 you show the real money supply. How do you correct the unadjusted money supply, which rose from $136 to $147 billion, to make it a real money supply?

Dr. MEANS. I corrected it to the Consumer Price Index.

Senator PROXMIRE. The Consumer Price Index only?

Dr. MEANS. Yes. I did not take the wholesale price index or construction index.

Senator PROXMIRE. Why does it make sense to do that, in view of the fact that money, particularly, has a bigger job to do as prices go up? If you correct it for the increase in prices, it seems to me that you do not get an accurate picture.

Dr. MEANS. The correction to a constant price level? Is seems to me that there is a reasonable presumption, not by any means to be precise; but if your level of physical activity remains constant, something like the same level in money is needed, provided short-term interest rates are substantially the same.

Senator PROXMIRE. Why do you not correct it to reflect the gross national product?

Dr. MEANS. If you have an expansion in your real gross national product, then you would expect an expansion in the real stock of money.

Senator PROXMIRE. Right. That is why I would say it seems to me the gross national product would be a more appropriate money deflater, because the gross national product measures the job money has to do. Is that not correct?

Dr. MEANS. I think both are appropriate. And it is much more striking to see that at the same time that our gross national product in real terms has been rising, the real stock of money has been shrinking, up to the beginning of 1961.

Senator PROXMIRE. Yesterday or the day before, Congressman Reuss showed us a very enlightening chart showing that free reserves are now half a billion dollars, and this seems to contribute to a condition which Mr. Martin described as monetary ease. Do you feel that this is a fair description of the situation at the present time?

Dr. MEANS. I think they have misinterpreted the meaning of those free reserves. If you will look at the figures, you will find that practically all of those free reserves are in the hands of country banks.

What happened, as I see it, is this: The legal reserve requirements for country banks, I believe, are around 12 percent, including their vault cash. The amount of reserves which the country banks feel it appropriate to hold is much higher than the legal reserve requirement forces them to hold; with the result that from the point of view of the country banks themselves, they do not have excess reserves.

If I am correct, this means that an increase in total reserves in the system would almost immediately bring about expansion in total money supply, for the reason that the central banks, central city banks, and the city banks already have larger reserves, because the law requires them to, than they would choose to hold. That means that as fast as they get additional reserves, they immediately expand their loans.

You will find that in the last year and a half, or year, at least, their borrowings from the Fed have been negligible. Their free reserves have been negligible. The free reserves are all concentrated down in the country banks, and they do not choose to use them, because they want more reserves than the law requires.

You can see that if the law only required them to hold 2 percent reserves, obviously any good bank would want to hold more than 2 percent.

Somewhere there is an amount that they would hold if there were no vault. And they are holding the extra $500 million of reserves, because their desire to hold reserves exceeds the legal limit.

Senator PROXMIRE. Do you have any study or documentation to establish this? It would be very helpful, because I think this is excellent point, and it has not been called to my attention before.

Dr. MEANS. I think it can be done right out of the general reports. Just look at the free reserves in the hands of country banks, the free reserves in the hands of the city and central city banks. It is very striking. I cannot imagine the statistics proving my point more effectively.

Senator PROXMIRE. Now, my last question for you, Dr. Means, is: You make a point that I have tried to make, and others on this committee have tried to make, over and over again, that by selling part of this huge portfolio of short-term obligations and buying long-terms we might get a situation in which the long-term rate could be dropped and the short-term rate kept up. This would tend to discourage the outflow of capital and discourage the adverse balance of payments, while stimulating economy expansion.

Mr. Martin anticipated my raising the point, and in his statement before us he said this, and I will read very briefly from what he said:

> Official market purchases of Treasury bills and other issues maturing in less than 1 year, although making up the bulk of Federal Reserve and Treasury operations, comprised in 1961 only about 4 percent of total dealer sales of such securities (excluding those to other dealers). The proportion for issues maturing in 1 to 5 years averaged 9 percent for the year, although in some months official purchases exceeded 30 percent of dealer sales in this area. In the 5- to 10-year area, the proportion amounted to more than 20 percent for the year as a whole and in the period from March through July was more than a third of the total. For securities maturing after 10 years, official purchases comprised over 30 percent of all market purchases for the year and nearly two-thirds of total purchases in the second quarter, when the bulk of the official purchases were made.

Mr. Martin said on chart 3 that if the Fed engaged much more heavily in the purchase of these longer term obligations, it would seriously disrupt the market and destroy any possibility of freedom in the market.

I counter that this is the exact kind of situation in which the Federal Reserve can be most effective in lowering these interest rates, but he seemed to feel that it was something that could not be done.

I would like your comment on that.

Dr. MEANS. I think that if you have been trying to organize the transactions of the Fed and concentrate them in one market, with the idea that you will create a very fluid market for that security for your short terms, and at the same time have avoided the long-term markets, obviously you are going to disrupt a situation that has been existing for a number of years.

I am perfectly willing to somewhat disrupt the relation between the short-term and long-term markets in the interest of avoiding 2 or 3 million extra unemployment. We are disrupting the lives of millions of people by not making this shift, in my opinion, and certainly there is the problem of rebuilding the long-term market and the Government's relation to it.

I cannot see that it presents an insuperable or even a serious problem.

Senator PROXMIRE. My time has expired.

Senator DOUGLAS. I think we are all interested in the preservation of competition. I notice Dr. Eckstein favors vigorous antitrust policy, apparently along the lines of the electrical machinery.

Is that not true?

Dr. ECKSTEIN. I took a look at the pieces of the wholesale price index, and it is striking that things like electric motors, which traditionally are administered prices, have fallen about 7 percent in 1961. Even though on the whole business was recovering, this set of prices fell. So apparently it does make a difference.

Senator DOUGLAS. Is it not true, after the convictions and jail sentences in Philadelphia, the price of electrical machinery fell very markedly?

Dr. ECKSTEIN. I have not traced it back very far. I just took a look at 1961 and was struck by the fact that while very few prices of this sort fell, this family of prices took quite a dive.

Senator DOUGLAS. Dr. Lewis, what is your opinion?

Dr. LEWIS. I have no opinion based directly on the facts.

Senator DOUGLAS. Dr. Means?

Dr. MEANS. I am not sure that I got your question.

Senator DOUGLAS. My question was: Is it not true that after the convictions in Philadelphia and jail sentences of Westinghouse and General Electric officials, the price of electrical machinery fell quite markedly?

Dr. MEANS. Yes, very definitely.

Senator DOUGLAS. Dr. Brozen, would you agree to that?

Dr. BROZEN. I do not know whether there is a cause-and-effect relationship there. It happened. But it happened in the same cycle that it has happened before. There seems to be a 3- or 4-year cycle of white sales, when prices do fall markedly.

Senator DOUGLAS. I think you will find much lower prices of bids than previously.

Dr. BROZEN. I think a much clearer case of cause and effect from antitrust action is shown in the 1930's, when the price of tungsten carbide fell from something like $450 a pound to less than $40 a pound after an antitrust case was launched against the makers of tungsten carbide.

Senator DOUGLAS. I am glad to know that.

Do you favor a continuance of this policy, any of you?

Dr. MEANS. I do not believe that the antitrust action in the steel industry would be very effective.

Senator DOUGLAS. That is disguised under variations of the basing point system?

Dr. MEANS. I do not think so. I think it is inherent in the degree of concentration in the industry. And therefore I have been working on the problem somewhat, taking the position that Dr. Lewis takes, that the kind of competition we have in the steel industry, and in some of our other big industries, is not capable of controlling prices in the public interest.

Senator DOUGLAS. Therefore you move toward public control of prices?

Dr. MEANS. No. I say: Is there any alternative to either Government price control, or antitrust, and break them up? The substance of my book here is a quite new approach, which offers a way of dealing with the pricing of concentrated industries in a way that leaves the industries free to do their pricing, even though concentrated, and does not require Government regulation, and does not require the breakup of big companies if they are efficient.

This is a proposal that I hope will get discussed in the next few years. It is not a proposal that one can discuss immediately. One has to have the background that I build up in the book.

I am not trying to sell the book, but I am trying to sell the idea.

Senator DOUGLAS. I am very eager to read the book.

Dr. Lewis?

Dr. LEWIS. I am very eager to read the book, too.

Senator DOUGLAS. At least at the moment I am not in a position to pass on Dr. Means' proposal.

Dr. Eckstein, on the other hand, is favoring a vigorous antitrust policy.

I wonder if you could discuss that, Dr. Lewis. I know you have given a lot of thought and study to this.

Dr. LEWIS. I certainly would favor a very vigorous antitrust policy. I do not hold out great hopes for it. I think it is a useful device. I think we are better off using it than we would be if we did not use it.

I cannot help but feel, as I indicated in my statement, that in these industries in which there is a large measure of private discretion over prices, the path that is indicated in the Council's report, namely, of an informed public opinion, is the right path, but I think that we are going to go much further than this.

I do not feel that there is any reason at the moment to believe that we are going to move at all quickly into complete public regulation of any of these industries. I do think that there are a good many measures and a good many intermediate stops on the way between simply an informed public opinion and final complete regulation. And it seems to me that any one of these intermediate stops could very well become a permanent stop in any individual case. I do not think we have to have a completely symmetrical pattern.

Senator DOUGLAS. Anyone else?

Dr. BROZEN. There is a means that is far more effective than antitrust, and that is foreign competition. Reducing tariff barriers certainly will let foreign competition operate. And the behavior of steel prices in the last year or two, moving downward as they have, I think is partly a result of foreign competition.

Senator DOUGLAS. That is the second proposal that you make, increase in foreign trade?

Dr. ECKSTEIN. Yes. May I add one comment to this whole discussion, and particularly to Dr. Lewis' paper?

When you get into this kind of a problem, the United States really is very pragmatic. We take a pragmatic atitude. And one step does not inexorably lead by rigid adherence to abstract intellectual principle down some road of disaster.

We have a certain problem. Our cost structure is out of line. It is important to the country that we do something about it. Clearly, there are things the President can do and other people can do to try to improve that cost structure.

Now in the long run there are favorable factors. As the advanced countries get more and more closely knit through trade, the competition across frontiers will effectively limit much of this market power. So I see no "doors thrown away" by the Presildent saying that wages should not go up or more than productivity or prices should not go up, or the Council coming out with guidelines. It just seems to me to be what common sense calls for in the present situation, taking for granted that we have big companies and big unions and are going to live with them. We also have a big Government.

Dr. BROZEN. I think we should get some balance into this discussion in stressing that probably the more important monopolies in the economy are labor union monopolies rather than business monopolies. They do have far more power. We do far less to restrict their power. And they use their power far more effectively than any business monopoly does in its present state of power.

Dr. MEANS. I question that very much. With the leaders in the industries, such as chemicals, automobiles, steel, making their prices in terms of a rate of return on capital in the vicinity of 16 to 20 percent, that seems to me exercising a degree of power contrary to the public interest of considerable proportions. When capital is amply available, even equity capital, at certainly 8 percent, industry, and I do not mean a particular company, to be making half again or twice the cost of capital indicates an exercise of pricing power which certainly is contrary to the expectation of classical competition and is contrary, in my belief, to the public interest.

And also there is the extent to which labor is blamed for a situation which in steel, I am quite clear, is not primarily labor's fault. In other industries I suspect it is much less labor's fault than it is management's fault, in widening profit margins. Until it is proved contrary, I think it is quite understandable that business, with access to the press, should constantly be reiterating the fact that wages go up and therefore we have to raise costs. Why wouldn't you? I have been in private business, and if I had to raise my prices, I would raise them after a wage increase, and I would say I had to raise them because of the wage increase. But that does ont prove that I would be completely presenting the actual picture.

Dr. BROZEN. Yet labor costs are about 70 percent of the cost of producing the national income, that is, direct wage and salary payments, aside from the labor costs of self-employed persons, as against corporate profits now amounting to about 5 percent of the national income. So you can double corporate profits and have less effect on costs than increasing labor costs by 10 percent.

Dr. MEANS. I think your figure of corporate profits as a proportion of total——

Dr. BROZEN. Corporate profits after tax.

Dr. MEANS. Yes, I understand; after tax. Earnings, including all the return on capital—that is, interest and net profit after taxes—is much more than 5 percent.

Dr. BROZEN. Well, total property returns run about 13 percent of national income, and the income of the self-employed and wage earners is about 87 percent.

Dr. MEANS. I think that what I have in mind particularly is taking total corporate additions to gross national product and allocating them between labor and capital; and you get a much larger figure than 5 percent. You may get 12 percent.

Dr. BROZEN. In additions to gross national product, you are including depreciation, then, too?

Dr. MEANS. Net, not gross, gross national product. Net gross national product.

Dr. ECKSTEIN. It seems to me it does not matter so much whose fault it is as to recognize the nature of the process. We would not have the wage and price increases in these industries we were talking about if the product market were not highly concentrated, so that companies felt secure they could pass on the wage increases that were granted.

On the other hand, if there were not strong unions in these industries, if wages were set in competition with other industries, they would not have risen so much.

And the policy implication of it is that you are not going to get very far if you only operate on one side of the problem. If you take those few instances where there is concentration on only one side of the market, you get an altogether different experience. If you take the ladies' garment workers union, who are infinitely more powerful than the little companies they deal with, who are really a behemoth in their industry, the behavior of its wages in the last 10 years has really been very poor. There is some question whether these wages have risen at all, and if so, very much less than elsewhere. Why? Because it is a highly competitive product market, and the companies cannot pass on the increases.

Conversely, if you have an industry like tobacco, where the product is very concentrated and the union very weak, the workers are badly paid. So it does take market power on both sides to get into this wage-price spiral.

Dr. MEANS. I am not sure that that is so. Our experience before 1933, before the unions became strong in the automobile industry—we had essentially the same policy, by the leaders of the automobile industry, and very much the same magnitude of profit margin that we now have.

In other words, in those days, in my opinion, the pricing was in terms of a higher rate of profit, way above the cost of capital for the industry as a whole.

Senator DOUGLAS. Mr. Reuss?

Representative REUSS. Mr. Means, I would like to explore with you the money expansion matter you were discussing.

I take it that it is your position that in order to have adequate aggregate demand, we need to increase the average amount of free reserves from its present half billion to some higher figure, because it is your feeling that so much of that half billion free reserves is not really free at all but is immobilized on the shelf of a country bank.

Dr. MEANS. Not quite that. I do not think we need to increase the free reserves as a statistic. If you increase reserves by, let us say, a million, it would, I think, result in almost immediate expansion of the money supply, with the result that free reserves would not increase.

Representative REUSS. In other words, to expand the money supply, businessmen have to come around and borrow from what has been made available?

Dr. MEANS. No, the member banks have to expand their portfolios. Whether they loan to business or buy Government bonds in the open market is of secondary importance, I think. The first impact may be somewhat different. The total impact is to expand the money supply rather than buy Government bonds in the open market or make loans to business.

Representative REUSS. But how do you expand the money supply?

Dr. MEANS. You increase reserves.

Representative REUSS. By either of the two methods? Either buying on the open market or changing the reserves?

Dr. MEANS. Yes. I would prefer open market operations. The Fed System buys Governments, expands reserves. The bank will immediately loan out those extra reserves, so that after a very short period of time the free reserves may still be only those held by the country banks, and the system as a whole has expanded its deposits and therefore its legal requirements for reserves.

Representative REUSS. In whatever way, then, is it your feeling that the money supply should be expanded?

Dr. MEANS. Yes.

Representative REUSS. Now the other day, in his testimony here, Chairman Martin of the Federal Reserve Board indicated that because of the international situation, our balance-of-payments deficits, and the resulting threat of gold loss, the Fed was seriously considering tightening credit, which goes in the opposite direction from what you have been talking about. Is that not so? You think that credit should be eased further? Or at least it should be at the present level?

Dr. MEANS. A great many people talk of the ease and unease of tightening credit. I think the focus ought to be on the expansion and contraction of the money supply; because that is to me the focal point of action.

Representative REUSS. I think, however, we are all talking about the same thing, and when the Chairman of the Fed talks about tightening credit, he means restricting expansion of the money supply.

Dr. MEANS. Given that statement, I would say, "Yes, they ought to ease credit further, but do it in such ways that the primary end effect is to raise short-term rates and reduce long-term."

I would be very much against the expansion of the money supply by lowering short-term interest rates. That to me would be a great mistake.

Representative REUSS. The reason you emphasize that is because this might tend to cause the flight of short-term capital, because of differential interest rates?

Dr. MEANS. Yes.

Representative REUSS. This you would prevent by a full-fledged wholehearted abandonment of the bills-only policy, instead of a timid, halfhearted one?

Dr. MEANS. Yes.

Representative REUSS. OK. I am with you up to this point.

Now let me continue. Suppose, however, that despite the adoption of the policy you propose, namely, a policy of buying rather heavily of long-terms, whether you switch or whether you just concentrate your purchases on long-terms, suppose that this switching to the long-term still produces short-term rates, which, while somewhat higher, still represents a discrepancy between rates here and abroad. Suppose this is so.

Would you at that stage throw in the sponge and say, "Well, we must have lagging growth"? Or would you, for example, urge foreign countries to use more fiscal tightness and less monetary tightness in their control over inflation, so that their interest rate structure was not unduly high in relation to ours? Would you try that?

Dr. MEANS. I would focus on achieving full employment as rapidly as possible. Take whatever gold outflow is implicit in that, but try to reduce it as much as possible, up to a point.

I still think some further outflow of gold is desirable. We do not need 45 percent of the monetary gold of the free world, since we have the additional backing of our international organizations. So I would be glad to see some further outflow of gold.

Representative REUSS. But let us assume you get to the point where you are no longer glad, and gold is down to a proper level. It is your feeling that, one, before throwing in the sponge we should concentrate our higher interest rates in the short term and make our long-term interest rates as low as may be?

Dr. MEANS. That is what I would do.

Representative REUSS. What else would you do in this respect?

Dr. MEANS. Then if we still have what I would call a dangerous outflow of gold, I would——

Well, before that is reached, there are a great many measures that we can use, such as those you have mentioned, such as getting a reduction in steel prices, such as——

Representative REUSS. Just a minute. A reduction in steel prices would be a fine thing which would presumably add to our exports and decrease imports, and thus tend to redress the imbalance of payments under which we are now laboring.

However, it would have nothing to do with the tendency of short-term capital to seek refuge abroad because of higher interest rates abroad, so far as I can see.

Dr. MEANS. No, but if that is a given amount, your unbalance is reduced, if you can increase exports $200 million and decrease imports by $200 million.

Representative REUSS. What I was leading to was this: Are you so sure that the movement abroad of short-term capital in this world of convertibility really is such a catastrophe, and that it should cause us to have monetary hysterics?

Dr. MEANS. At the long end of the road, there is some kind of change in the value of the dollar. I see no likelihood that we will even have to approach that point. I think we could afford a considerable outflow of short term and still come forward with a balance within a few years. And I encourage a continued inflow. And I think our short-term interest rates ought to be so related to the short-term interest rates in the other countries, so that that would occur.

I think that some working out between the central banks of the different countries as to the appropriate relation of the short-term interest rates should take place. But I think the mechanisms that are available to us are of a magnitude, and are being paid attention to, such that we do not need to limit our level of national production in order to balance payments.

Representative REUSS. Thank you.

My time is about up. I know Mr. Brozen has something he wants to add, but perhaps we can get to it later.

Senator PROXMIRE. Go right ahead.

Dr. BROZEN. The movement of the short-term funds in themselves carry their own cure. Inasmuch as they are leading to monetary expansion abroad, prices are rising relative to our level at this point, and that in itself would tend to redress the balance of payments somewhat.

As it is, we have reached exports of over $20 billion of merchandise a year as against $16 billion of imports. In part the rise in exports has been because of the rise in prices and incomes abroad.

There are alternative measures besides monetary measures if we want to prevent further loss of gold. There are possibilities like some pruning of foreign aid, and there are measures available such as cutting our tax rates, that fall most heavily on investment. Corporate tax rates, for example, if reduced, would increase the return on investment and attract foreign funds to this country.

Senator PROXMIRE. I would like to ask Professor Lewis: Would you apply the antitrust laws to labor unions?

Dr. LEWIS. No.

Senator PROXMIRE. In the second place, do you think a more liberal trade program, such as the President has advocated, would act as an important and significant brake on rising prices and tend to stabilize prices or provide the kind of competition which you feel is necessary?

Dr. LEWIS. I do think this would be of great assistance.

Senator PROXMIRE. And then you are familiar with Prof. Edward Chamberlain of Harvard and his book on the theory of monopolistic competition?

Dr. LEWIS. In a general way.

Senator PROXMIRE. I was at Harvard some years ago, and was pretty much persuaded by this, as were members of the Harvard faculty. We have not really had price competition alone in this country for many years. We have not only price competition but competition from the standpoint of personality, locations as to stores, advertising, all kinds of other things.

Under these circumstances, we have a mixed economy in a very real sense. And with this in mind, it seems to me that perhaps the social conscience of individuals can also contribute to this mix to ameliorate some of the worst aspects of our economic system without ending in the kind of unfortunate effects which you describe.

Do you not think this is possible? Or do you think that even though competition is not perfect or pure, you would still feel that any social conscience on the part of labor or on the part of management is amiss?

Dr. LEWIS. Well, my answer to that would be that if in fact individual decisionmakers—whether you are talking about people in unions or whether you are talking about people in industry—do in fact have a considerable degree of market power, then certainly I would like to have them exercise that market power as responsibly as they can exercise it.

Senator PROXMIRE. Isn't this a social conscience, when you say responsible?

Dr. LEWIS. Yes. That is right. On the other hand, I feel that the nature of the decisions they have to make is such that the decisions simply cannot be dictated by reference to as broad a force as social conscience. That is, the decisions are essentially not moral decisions. They are not matters of right and wrong. And we have had enough evidence of that this morning, I think, just in the discussions here.

Senator PROXMIRE. I will just interrupt for a minute to say: supposing you have this kind of a situation, not related so much perhaps to price as to something else. There were employers, factory owners, and I know there were many of them, I know personally some of them, who in the depth of the depression against their economic interest kept their factory workforce at work as long as they could, although they knew it was a cost they could not make up. They did it because they knew the human tragedy of putting these men out of work in the 1930's.

Now why would this kind of a conscience tend to upset the economic system and act adversely?

Dr. LEWIS. This, as I see it, would not tend to upset the system at all.

Senator PROXMIRE. It would certainly upset competition. It would mean you were producing more than necessary, tending to keep the prices down, and acting in a deflationary way at a time when deflation was damaging the overall economy.

Dr. LEWIS. My point is simply that while all of these acts may be commendable, so far as the particular individuals who are immediately concerned are involved, this is just no way to run an economy.

Senator PROXMIRE. I see.

Dr. MEANS. I want to underline that. It seems to me very important. It is splendid, when we have people of breadth of mind running big corporations. But the kind of person who ought to be running a big corporation is a person who can deal with a great deal of detail, can manage this outfit. It is not the kind of person that can think very effectively in social terms. And I think we must try to shape our institutional arrangements so that the leaders of big business do not have to operate in social terms. If they do, so much the better. But we must have people operating our big corporations efficiently, and to put on them the added burden of acting in the social interest——

Senator PROXMIRE. When you say "if they do, so much the better," it seems you tend to contradict yourself. But I feel if we do not have some of this social conscience as much as possible, if you move into a position where, as both of you gentlemen seem to indicate, you are going to have to have the guidelines set down by the Council of Economic Advisers and more, this may progress into a situation of controls. On the contrary, private conscience, private salesmanship is exactly the kind of primary force that helps keep the free enterprise free and tends to make a Federal action or Government action less necessary.

Dr. MEANS. In the present situation, where we have no adequate solution to this problem, I agree with Dr. Lewis 100 percent.

But I am neither satisfied with the social conscience nor am I satisfied with price control; even of the rather minor kind that he is suggesting in his fourth stage, certainly in his third stage, too. And therefore I seek something where we do not depend on the social conscience of our big businessmen and do get prices which approximate the public interest.

Senator PROXMIRE. I see. I think you would say that we should not depend on this. We should not discourage it, we should encourage it, but be prepared to recognize that we are not going to get the final answer in this way.

Do you want to comment?

Dr. LEWIS. May I add a comment here?

Suppose you take a situation in which you have an industry which is running along very nicely, making handsome profits, with full employment, and paying high wages; suppose in that situation the union is asking for an increase in wages. And suppose there is a threat, a very substantial threat, of a long-drawn-out strike, unless the union has its demands met.

The point I would like to make is that this is not a clear-cut situation in which the only thing necessary is to ask the management to consult its conscience or its sense of social responsibility; because if we are going to place responsibility on the management for a decision of this sort, it should be remembered that the management has a responsibility to a wide number of conflicting interests.

And just offhand, knowing no more about it than the facts that I have given, it is not at all clear which is a good decision and which is something less than a good decision as to whether or not the management should grant an increase.

The management does not want a strike. Its stockholders do not want a strike. Its stockholders want continuing dividends. The workers do not want a strike. They want continuing work. They want higher wages, or they would like higher wages. The public does not want an interruption. The people who are doing business with this industry, either as suppliers or consumers, do not want an interruption.

Now what is a responsible decision? And I suggest that probably what is called for here is some set of guidelines of the sort that the Council has furnished. This seems to me to be definitely a step in the right direction.

But this probably, over a period of time, will not be enough. That is, probably over a period of time these guidelines are going to have to be made much more precise; it will be necessary to meet different types of situations.

The kind of thing that I am suggesting at this stage—and I am not concerned to rush into it at this stage—is a kind of forum where the representations and guidelines and considerations can be focused so that the public can have some help in making up its mind.

Senator PROXMIRE. That is an excellent clarification. I am delighted that you responded in this way. This certainly gives me a different slant on your presentation.

Mr. Eckstein, did you want to add something?

Dr. ECKSTEIN. I was going to say that although my knowledge of corporation presidents is very limited, surely they are more than simple maximizers of profits, and in a sense the qualities it takes now to become a corporation president are quite similar to those of being a good politician, namely, knowing when to lead, giving direction to the organization, but also knowing how to respond to the various constituencies with which they have to deal, their workers, their stockholders, their directors, and their management officials. And if the Government takes an interest, they will also respond to the Government.

So it seems to me that in dealing with that kind of people, one will find a response; and one does not have to appeal necessarily wholly to their nobler instincts. They will understand this development as a part of the reality in which they live, and they will find that they are doing their job better if they also take that into account.

Senator PROXMIRE. Dr. Eckstein, in your presentation you say:

> Obviously it is undesirable to raise farm income by a method which raises consumer prices.

I wonder about this, not only because there are lots of farmers in Wisconsin, but I wonder about it as a matter of economic justice.

We have had arguments, for example, on the floor of the Senate last year, as to whether the Mexican farm labor bill, which permits the importation of 300,000 to 400,000 Mexican laborers, to work at 50 cents an hour is necessary, because if you do not have them, you might have to pay American migratory laborers, who are grossly underpaid now, a dollar or $1.50 an hour, and if you did, you would have to charge the consumer more for the vegetables and so forth that these men and women pick and produce. Why shouldn't we be willing to pay a little more.

You have a situation in Wisconsin, where our dairy farmers invest an average $45,000 to $50,000 a farm. They take a great risk, they have enormously increased their efficiency. It requires a great deal of ability now to run a typical farm. But their income is about 60 cents an hour, on the average.

Now, this just does not make sense to me, and it seems to me farmers and farm income should not be a charge of the general taxpayer.

A system such as the President proposed, which I judge is going to work perhaps to some extent, is right and just, because I just do not understand why the taxpayer and the farmer should subsidize the consumer to the extent that we have in the past.

Dr. ECKSTEIN. I have not had an opportunity to analyze the President's program in detail. Also, let me say, as we pointed out in our staff report, there really are two problems in agriculture, the problem of low income in agriculture and the problem of overproduction. When I put this sentence into my statement, what I had in mind particularly was some concern with the overall strategy on the overproduction problem, of essentially raising prices by cutting down output. This solution to the overproduction problem continues the so far unsuccessful search for effective production controls, in order to drive up prices, rather than by some more natural mechanism.

Senator PROXMIRE. It has not been unsuccessful in all areas. It has been eminently successful, for example, in tobacco and in some other areas. Because the farm part of our economy is so purely competitive, in that it has hundreds of thousands of farmers producing an identical commodity, identical in every sense, unless you have some opportunity, through society, through Government, to limit production, you have a situation then because of the great increase in productivity and because of the inelasticity of demand—a situation in which the farmer just gets drowned in the surplus and no matter how efficient he is, he loses ground.

And it is economically unjust, it seems to me, unless you have some opportunity to do what everybody else does, tailor his production to what he can sell.

Dr. ECKSTEIN. Of course, stable prices are not the only goal of our society; and certainly a fair distribution of income is another.

If there are choices in method, in maintaining farm income at some fair level, I would favor methods which do not raise consumer prices.

Senator PROXMIRE. I would agree with that.

Dr. ECKSTEIN. Now, perhaps there are no choices. I do not know.

Dr. BROZEN. Perhaps one thing we might do is not reclaim so much land to add to this production surplus. We could stop spending some Government money there and save it.

Senator PROXMIRE. I could not agree with you more. I think this is a ridiculous policy when we have a surplus of farm production, to pour hundreds of millions of dollars into creating a situation in the West where we can irrigate land, produce alfalfa, and produce more milk. It is insane.

I see my time has expired, Mr. Chairman. I had a few more questions.

Senator DOUGLAS. Thank you very much.

Senator PROXMIRE. Could I ask Dr. Brozen: I take it from what you said that you would perhaps apply the antitrust law to labor unions. You spoke of them as a more powerful monopoly than business.

Dr. BROZEN. I am not sure whether antitrust action is an answer to this problem. I think in part it is simply a matter of applying the law equally with other kinds of laws, besides antitrust laws, to unions.

At the present, when a labor union calls a strike, they can stop the use of the property by violence, and we do not make use in many cases of the local police powers to prevent this use of violence. I think if we had equal application of laws against violence to labor unions as well as to other people, this in part would be an answer to the problem, as well.

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There are many areas of this kind of similar character. Part of the power of the union simply comes out of the unequal application of the laws that are on the books already.

Senator PROXMIRE. You do not take a position definitely on applying antitrust laws to labor unions?

Dr. BROZEN. Well, I think certainly the nationwide bargaining by unions with an entire industry is against the spirit of the antitrust laws, and I think probably should be applied to a situation of that kind.

Senator PROXMIRE. That is an interesting distinction. It would seem to me, though, if you apply it, you would have to reverse the *Danbury Hatters* decision, which recognizes that application of antitrust laws would destroy labor unions. Unions do in fact restrain trade, and they do it to get a higher price for their product. And if they did not do it, you might as well forget about labor unions. Is that not correct?

Dr. BROZEN. I think unions have other areas of importance, in the processing of grievances, the maintaining of industrial democracy, the prevention of tyranny in the factory, and matters of that nature. They certainly have a function there. I do not think they have a function in the wage setting area, however.

Senator PROXMIRE. Unions do not have a function in the wage setting area?

Dr. BROZEN. That is correct. I think just as prices are set in the market, wage rates should be set in the market as well.

Senator PROXMIRE. In view of the fact that prices are not set in the market area, and you know they are not, do you think in the world in which we live we can do without unions taking part in wage setting?

Dr. BROZEN. It is not an ideal world, certainly, and the un-idealism that does exist in product markets I think is not of such major importance as the un-idealism that now exists in the labor markets. I would strain more to do something about making labor markets freer than making product markets free, simply because I think they are much more free now than labor markets.

I do not think this is probably a sufficient answer in the field of labor markets.

Senator PROXMIRE. When you say "labor markets," are you not just looking at a relatively small fraction of this 70 percent of the cost of production, in view of the fact that only one-quarter of our workers are in the union, that an increasingly larger proportion of them are on the administrative staffs, and so forth, in the professions and services there being no organization? Under these circumstances, how would you defend the position which you seem to imply, that it is this extra power of labor unions that has been responsible for increased prices throughout the economy?

Dr. BROZEN. Well, certainly, first of all the power of labor unions is localized. It is not widespread over the whole economy. I would not argue that labor unions have caused the increase in the price level to the whole economy.

As a matter of fact, I have a footnote in my opening statement here, perhaps, which I should read at this point.

I was going to say—

I propose to address myself to the microeconomic aspects of wage behavior. I do not accept the evident feeling of the Council that wage increases larger than productivity increases cause inflation; except through the indirect channel of the reaction of monetary authorities to the existence of unemployment.

I would not argue that our inflation has been a consequence of labor union behavior. Some wage rates are higher because of labor unions, but other wage rates are lower because of labor unions.

The other industries, outside of transportation equipment, for example, that I spoke of in Michigan, have lower wage rates than would be the case if there were no wage setting powers in the hands of the United Auto Workers. I think on the average the wage levels are the same as they would be with or without unions. It is the wage structure that is distorted and not the general wage level.

Senator PROXMIRE. In view of the way that corporations are organized and run, the lumping of all salaries and wages together is one factor, and the interest and dividends as a return on capital is another. That is certainly an imperfect measure, isn't it? What I mean to say is that the salaries of people who run companies—this is particularly true of small companies—that much of the return on capital is the salary the owner of a small corporation pays himself, perhaps his wife, and other relatives. This is not uncommon. And also in the larger corporations, a very large number of people who are considered management personnel, professional personnel, technical engineering personnel, and so forth, whose wages are not determined by union activity at all and are determined in other ways, it seems to me, tends to somewhat modify the position that many economists take that unions are responsible overwhelmingly for increases in prices.

You deny that, I know. And that unions are responsible for about 70 percent of the cost of our production.

Dr. BROZEN. Well, I have dissociated myself from this notion, certainly, and I think the important point is this misallocation of resources that comes out of activities of the coal mine union, the airline pilots association, or some of the transportation workers unions, or the United Auto Workers. The thing I am concerned about is the effect of these activities causing some restraint on the rate of growth and the rate of economic activity and on the rate of increase in output per man-hour in the economy.

Senator PROXMIRE. I apologize for keeping you so long. I just want to ask one more question relating to what you have raised now.

Is it not true that if you had no unions in the mining field, for example, you would have had a bad employment situation still, because of the competition from oil and competitive fuels, in which you would have had a displacement of the production of coal, a reduction in the production of coal, and probably some reduction, not as great but some reduction, and a substantial reduction, in employment in the mines? That is No. 1.

Dr. BROZEN. We have not computed the exact effects of wage increases in coal mining on employment there. I know that in some cases where we have computed the effect, in auto manufacturing, for example, a 1-percent wage increase relative to other prices causes about a 2.8-percent decline in employment assuming no change in output.

Now, to some extent, I think that coal mining may have as high elasticity of substitution as the auto industry, that the wage increase there has been a major factor in causing the decrease in employment; secondarily, it has had an effect on the price of coal.

The price of coal certainly is somewhat higher than it would be in the absence of as large wage increases as have occurred, and the coal market would be somewhat larger than it is today. Perhaps the amount of coal sold would be as great as, let us say, in 1946 or 1947. And that being the case, then, you would have the extra employment of the extra coal sold as well as the extra employment because of displacing fewer workers through automation.

Senator PROXMIRE. And less oil sold. But let me just say that there is one balancing factor that you seem to overlook. And that is higher wages you admit have resulted in automation as a gain to the economy. The fact that we are more productive in automobiles, more productive in the mines, that we are producing more cars with fewer workers and more coal with fewer workers, it seems to me, is a plus, is not something to be ashamed of. We ought to be able to find work for these people in other constructive ways, and that is our job. But this improvement in productivity is nothing to consider as a black mark against increased wages, is it?

Dr. BROZEN. Well, the argument I would make there is that the increase in automation in coal mining and auto work has come at the expense of having less automation in other industries, and productivity has risen less in other industries as a consequence.

Senator PROXMIRE. Other industries should have stronger unions.

Dr. BROZEN. So we would have more unemployment, and more distortion of the allocation of the labor force.

Senator PROXMIRE. And more productivity and more economic growth.

Dr. BROZEN. But the rate of increase in overall productivity is going to be a function of the supply of capital becoming available; and simply raising the wage rates in these other industries is not going to increase the supply of capital. It probably would decrease it, and you would have slower productivity growth, then, in accordance with the lower rate of supply of capital.

Senator DOUGLAS. We will meet at 2 o'clock to hear the testimony of Secretary Hodges.

(Whereupon, at 12:55 p.m., the committee was recessed, to reconvene at 2 p.m. the same day.)

AFTERNOON SESSION

Chairman PATMAN. The committee will please come to order.

We have with us this afternoon the Secretary of Commerce, Governor Hodges. He was on the agenda for Thursday morning, but on account of another engagement he could not be here. So we arranged to hear him this afternoon.

Secretary Hodges, we are delighted to have you, sir. I believe you have a prepared statement.

STATEMENT OF HON. LUTHER H. HODGES, SECRETARY OF COMMERCE, ACCOMPANIED BY WILLIAM L. BATT

Secretary HODGES. Gentlemen, Mr. Chairman——

Chairman PATMAN. You may proceed in your own way.

Secretary HODGES. Thank you.

Mr. Chairman and gentlemen, first of all let me express my thanks to you for your consideration of my schedule in letting me come this afternoon. I have a fairly sizable document, about 35 minutes, something like that, which I will leave for the record.

I have also, Mr. Chairman, a supplementary appendix that I will also leave which deals entirely with the area redevelopment administration, if anybody wants to make a particular study of that.

The economy has recovered rapidly from the 1960, early 1961, setback. In the fourth quarter of last year, total output of goods and services, or the GNP, increased to an annual rate of $542 billion, up 8 percent from the first quarter low. At the present time, all major types of demand are increasing, contributing to the further expansion of the economy.

Consumer spending, which had been lagging for some time, is now in the forefront of the expansion and is moving ahead in line with the higher income flows. Since the February low of last year, personal income has risen $28 billion, at an annual rate of 7 percent. The momentum of the higher purchasing power will carry us through for some time this year and it is my expectation that consumers will continue to expand their purchases and thus add to the extension of the recovery.

The profits picture is particularly encouraging. By the third quarter of 1961, corporate profits before taxes were running at an annual rate of over $47 billion, nearly 20 percent above the low at the trough of the recent downturn. This marked improvement has bolstered business confidence and has turned business investment upward once more. Plant and equipment spending is proceeding at a somewhat higher rate than during last year.

We do not think that it will be of any boom proportion but we think there will be a substantial increase in 1962 in this investment.

I think, further, we will get over $50 billion as an annual rate of corporate profits by the time the figures are out for the first quarter.

In view of the crucial role that private investment plays in providing expanded employment and increased productivity, I strongly urge that you give serious consideration to the President's legislative proposal to augment investment incentives by an 8-percent tax credit on gross outlays for depreciable machinery and equipment. The recent liberalization by the Treasury of textile industry depreciation allowances and contemplated similar action for other industries will provide further investment inducements.

Residential construction has shown sizable gains over the past year, although the rate is still below the peak reached in 1959. With family formations and incomes increasing, some further moderate expansion may be expected in the coming months.

At present, our balance of payments shows a sizable deficit. The prospects this year are for some rise in imports to support higher levels of domestic activity. I am confident that the programs we now have underway should result in increasingly higher exports. With our large commitments abroad and the continuing outflow of funds, I consider that our total balance of payments still remains a major problem area.

Economic developments of the past year have been accompanied by virtual price stability. Some prices moved up moderately, but on the whole, overall prices have shown no marked increase. I feel that in view of the adequacy of capacity and supplies this year, we may be able to achieve, along with continued rapid recovery, a fairly stable price situation. This can only be achieved if management and labor pursue a moderate course in their settlements.

We have learned from painful experience that the production lost through cyclical unemployment and decline in output is never regained. In order to minimize such irretrievable losses, should another such contingency arise, I strongly endorse the President's proposals for standby authority to make temporary prescribed reductions in individual income tax rates, and to initiate a previously approved capital improvements program.

I think, Mr. Chairman, we have found that the lack of getting a growth rate high enough to take care of unemployment and other things has been one of our serious situations over the years.

I view the current economic situation with optimism. I feel we will have continued expansion and demand throughout this year.

However, we still have a very serious problem of a continuing high rate of unemployment. Even with this good recovery we have reduced the rate of unemployment by only modest amounts. It is hoped, as the President has said, that we can get our unemployment down to a rate of 4 percent which will be a tolerable rate, if not desirable.

The Employment Act of 1946 sets forth the responsibility of the Federal Government "to provide maximum employment, production, and purchasing power." These goals must be achieved within the broad framework of U.S. political and economic institutions—free competitive enterprise and the Federal system of government—through means that take into account our other national needs, obligations, and objectives.

Another major goal of economic policy is to reconcile high employment levels with overall price stability, while permitting individual prices and wage rates to vary with changes in costs and demand. Any attempt to stabilize prices through the imposition of direct wage and price controls would be unacceptable, and policies which would pursue price stability without regard for the effects on employment, production and purchasing power would be equally unacceptable. The need for balance in our international payments gives additional and compelling importance to the goal of price stability. To guide resources into full and efficient use, there will, of course, be fluctuation in specific prices, but, hopefully, all within the framework of a generally stable price level.

Full utilization of resources, balance of payments equilibrium, price level stability are the traditional goals of economic policy implied in the Employment Act. To achieve this stablization program, we use monetary-fiscal policy, and a wages and prices policy. But this is not enough. We need a faster rate of growth.

Mr. Chairman, I shall not read all of that. It tells about what the Department of Commerce is trying to do in its reinvigorated departments on the domestic side where we are trying to get out certain information on technical help to various organizations and industries and our international side where we are doing everything we can to help in international investment.

Chairman PATMAN. Your statement will be published as is.

Secretary HODGES. All right, sir. I will go over to page 9 on equalizing job opportunities.

Both the quantity and quality of our economic growth are weakened by racial and religious barriers against economic advancement. These factors reduce our productivity by distributing our labor forces less effectively among employments than otherwise would be the case. The social inequities of job discrimination are enhanced in recessions—when the evils of educational deprivation and job discrimination are compounded by high rates of unemployment. A hard-headed sense of economics and consideration of social justice demand that we continue the progress already made in expanding job opportunities for all our citizens.

Our economy can rise to even greater heights within the framework of our free enterprise system if we can enhance the pace of technological progress which has made us the envy of the world. This can be accomplished by stimulating technological innovation, encouraging plant and equipment modernization, and by selective readjustment measures.

The report includes two proposals designed to improve the financial incentives for new investment. One, already submitted for the consideration of the Congress, would provide an 8 percent tax credit for gross investment in depreciable machinery and equipment.

By increasing the profitability of productive investment through reducing the net cost of acquisition, this tax credit would stimulate an increased rate of plant and equipment modernization and expansion. In addition, the Secretary of the Treasury, I understand, will shortly implement his program to bring the depreciation schedules specified in its Bulletin F, into line with current experience.

The recent acceleration of allowable depreciation for the textile industry indicates what business generally can look forward to in this direction. To reinforce the effects of these measures, the Department of Commerce is studying the merits of Federal credit guarantees of commercial bank loans for productive investment.

The report also suggests measures for improving technological progress by expanding and stabilizing the markets in which our businessmen sell their wares. As I have previously indicated, the report proposes courses of action designed to alleviate the instability which has characterized our economy through most of the postwar period and to move ahead to higher levels of employment and output. Successes in implementing this policy should contribute markedly to the strengthening of business expectations and improving the climate for risk investment.

In addition to this enlargement of our internal markets, the Government, through the Department of Commerce, is pursuing an active policy of expanding foreign markets through our trade exposition and travel programs.

We are also endeavoring to stimulate progress through an active sponsorship of technological innovation and dissemination.

I will skip the next two or three pages, Mr. Chairman, by simply saying that in our Department of Commerce and working with other agencies of the Government, we are doing everything we can to see that industry has a better chance, has incentives for increasing their capital investment because what little I know about economics, if you do not get your capital investment, you do not have profits enough in industry to make capital investment, then you do not create jobs and you do not get your unemployment down.

I mentioned the ARA, things we are trying to do to take care of certain pockets of unemployment. This was not done as an antirecession measure. It was done because we had had those for a long time and it looks like we may have them for some time yet. If I may go to the middle of page 14—with the overall economy moving forward again, it is imperative that we concentrate more Federal effort on these persistent pockets of joblessness. And in helping the people in these areas to share in the Nation's prosperity, we will be contributing further to national growth.

The Trade Expansion Act of 1962, another imperative, may impose some readjustments on a limited number of sectors of the economy adversely affected by increased foreign import competition. The resulting hardships will be but a small fraction of the benefit of the reduction in trade barriers to the economy as a whole. Nevertheless, the Nation as a whole must assume responsibility for any major adverse impacts. Under this act, temporary adjustment allowance and retraining and relocation assistance to displaced labor will be provided. For the affected businessman, a program of technical assistance and tax benefits and loans will be set in motion to encourage modernization and diversification.

For the problems of the textile industry, which are already especially acute, special solutions have been adopted. Temporary relief has been obtained by agreement with other producing nations to hold their exports to the United States at the fiscal 1961 level. Longer term solutions will be forthcoming from the Commerce Department's research project to help the industry and from the Treasury's liberalized depreciation allowances on textile machinery.

The bulk of the investment required to move our economy toward higher levels of output and employment at an accelerated rate will be undertaken under private auspices. In order to permit our productive capital and technology to be used with maximum efficiency, investments are required in the public sector. The need for increased outlays for educational and health purposes has been noted in my references to improving the quality of our manpower resources. The increasing complexity of our economy and increasing congestion of our urban areas has made the issue of adequate transportation apparent to all of us. The report notes that sustained economic growth requires accelerated investment in transportation services. The Department recently submitted recommendations to the President for improvement and encouragement of sound conditions in our transportation industry. It is anticipated that the President will be submitting a message to Congress on this subject shortly. Meanwhile, the Department is carrying out its responsibility in the expanded highway program, in cooperating with the HHFA in developing aids to urban mass transportation, and administering its extensive program for aiding investment and operations in the American merchant marine.

Our international payments position continues to be of major concern. In 1961, the United States incurred a deficit in its international accounts of nearly $2.5 billion. This was a considerable improvement over the deficit of $3.9 billion of 1960. It was also a considerable improvement upon 1958 and 1959 when they were of about the same magnitude.

Two and a half billion dollar payments deficits, while smaller than those in any of the preceding 3 years, cannot be long sustained. In stating his objective with respect to to the U.S. balance-of-payments position, the President said:

> We must attain a balance in our innternational transactions which permits us to meet heavy obligations abroad for the security and development of the free world, without continued depletion of our gold reserves or excessive accumulation of short-term dollar liabilities to foreigners.

We are proud of the way in which America has responded to the challenge of international competition. But we would be deluding ourselves if we thought this problem was licked. Much has been done; much remains to be done. We of the Department of Commerce will assist the President in every way we can to reach these essential objectives.

To a certain extent the improvement last year was due to special transactions, such as large advance debt repayments we received from Germany and other countries. Without these extraordinary receipts, the deficit would have been around $3 billion.

Basic confidence in the dollar has already been restored by the determination of the President to defend the dollar. This can be demonstrated by events in 1961. Our deficit in the second half of the year was considerably higher than in the first half. Yet, the portion of the deficit that was settled in gold in the second half was smaller than in the first half.

The President's budget and his Economic Report should amply dispel any lingering doubts about the dollar that may remain here or abroad. In addition to our general economic policies, we are convinced that passage of the Trade Expansion Act of 1962 and the eliminating of foreign "tax havens" should do much, in themselves, to restore order to our international accounts.

I shall not spend much time on the Trade Expansion Act. It is one of the more important things we have had. I simply want to give my wholehearted endorsement to it and simply say that, as I show on page 19, we must move quickly to get in step with the Common Market. If not, the growth in our exports to Western Europe, about 30 percent of our total exports in 1960, will surely slow down and these exports may even shrink. And, remember, this is the fastest growing and lushest export market in the world for us.

As you know, the six-member nations—Belgium, France, Germany, Italy, Luxembourg, and the Netherlands—soon to be joined by some of their Western European neighbors, are rapidly eliminating their internal barriers to trade, including tariffs. Soon a Frenchman will be able to sell his products in Italy without any national restrictions just as a South Carolinian sells his products in North Carolina or in Texas to California.

With the reduction and eventual elimination of internal European trade barriers, the American will have to hurdle, among other things, an external tariff wall that simply will not exist for his European competitor. As you know, the common external tariff of the six is based in general on the arithmetic average of the 1957 tariffs of the four customs areas (Benelux, France, Italy, and Germany).

Then I have an illustration for the record as to what would happen on certain kinds of machines before the Common Market reduces and after.

If we do nothing about this situation—this external tariff—profit margins in our export business will be squeezed or may in some cases simply vanish. Under these circumstances, many of our export industries will either be forced to abandon this business or, if they can, to transfer their production facilities to Europe. Thus, if we do nothing or not enough, our exports could decline, adversely affecting American jobs and profits, as well as worsening our balance-of-payments position.

The mutual trade liberalizations by ourselves, the Europeans, and our other trading partners will give us a golden opportunity to preserve and expand American jobs and profits through the expansion of exports. It is imperative that the President be given the tools with which to bargain effectively with the European Community. I need not remind you that the President will need plenty of room for maneuver when we sit down at the negotiating table with the representatives of other trading nations.

We in the Department of Commerce have been involved at every stage in the development of this legislation. We recognize the importance of export trade to every State of the Union, as is illustrated in the Export Origins Survey of Manufactures, recently released by the Bureau of Census of the Department of Commerce. We believe its passage essential to the future prosperity of the business community, to this Nation's future, and to the future shape of the free world community.

Mr. Chairman, the rest of this paper has to do primarily with the work that the Department of Commerce is doing in export expansion activity.

(1) A commercial specialist program to increase the effectiveness of oversea commercial services.

(2) A trade missions program, reoriented toward obtaining immediate results to increase exports of U.S. products and commodities for which the host country has a need and the ability to purchase.

I would like to say here parenthetically that just 2 weeks ago we took the 100th trade mission of seven men down to see the Vice President who did not really know this kind of program we were carrying on. These seven men were going to Burma for 6 or 8 weeks. They were taking with them about 350 specific selling opportunities from American firms to the people in Burma. We will have one going soon to Indonesia and so on.

We have this commercial specialists program which I shall not discuss any further. We have just appointed a Chairman of our

Regional Export Committee and National Export Committee by the name of Mr. Hurley from Illinois, a man who has great export experience, and an honorary chairman, Mr. Foy of the Koppers Co. These people are working with 30 regional export expansion committees throughout America.

We have a great ambition of getting several thousand businessmen at their own expense to go abroad and to see what the possibilities are for their sales.

One or two other things we have done that is of particular interest. With the President's permission we have taken the old Army-Navy E out of mothballs and now are offering the E to companies and institutions and groups who do a good job in export. I might say to you right now that we have between 300 and 400 applications already in the last 30 days for this E award. These are people who have done a job or think they are doing a good job in exporting.

We are doing something on travel service. I shall not take time on it except to tell you that with the $2.5 million granted us by the Congress last year we now have oversea offices that people opened up in London and Paris and Frankfurt and Tokyo and Sidney, Australia, and so on. Mr. Chairman, I would like to close by thanking you again and saying to you very informally that I am very bullish on the future, particularly the immediate future. I think that the people have greater confidence than they had a year ago.

I believe they also have a better understanding of the economics of the situation facing this country.

Thank you, Mr. Chairman.

(The complete statements submitted are as follows:)

Statement by Luther H. Hodges, Secretary of Commerce, Before the Joint Economic Committee, February 2, 1962

Mr. Chairman and members of the committee, I appreciate the opportunity to appear before this important committee. Before getting to direct comments on the economic report I should like to present a brief summary of the current economic situation. My comments reflect not only the official statistics which the Bureau of the Census and other Commerce Department agencies compile, but also the many direct contacts we in the Department have with major business groups on a day-to-day basis.

CURRENT ECONOMIC SITUATION AND OUTLOOK

The economy has recovered rapidly from the 1960, early 1961, setback. In the fourth quarter of last year, total output of goods and services—or the GNP—increased to an annual rate of $542 billion, up 8 percent from the first quarter low. At the present time, all major types of demand are increasing, contributing to the further expansion of the economy.

Consumer spending, which had been lagging for some time, is now in the forefront of the expansion and is moving ahead in line with the higher income flows. Since the February low of last year, personal income has risen $28 billion, at an annual rate of 7 percent. The momentum of the higher purchasing power will carry us through for some time this year and it is my expectation that consumers will continue to expand their purchases and thus add to the extension of the recovery.

The profits picture is particularly encouraging. By the third quarter of 1961, corporate profits before taxes were running at an annual rate of over $47 billion, nearly 20 percent above the low at the trough of the recent downturn. This marked improvement has bolstered business confidence and has turned business investment upward once more. Plant and equipment spending is proceeding at a somewhat higher rate than during last year, but our Commerce-SEC surveys indicate that the increase in this type of expenditure will not be of boom proportions.

In view of the crucial role that private investment plays in providing expanded employment and increased productivity, I strongly urge that you give serious consideration to the Preisdent's legislative proposal to augment investment incentives by an 8 percent tax credit on gross outlays for depreciable machinery and equipment. The recent liberalization by the Treasury of textile industry depreciation allowances and contemplated similar action for other industries will provide further investment inducements.

Residential construction has shown sizable gains over the past year, although the rate is still below the peak reached in 1959. With family formations and incomes increasing, some further moderate expansion may be expected in the coming months.

A feature of the recovery earlier last year was the shift in inventory policy by business. However, as the year progressed, the economy moved up, primarily because of rising final purchases, with inventory expansion playing a smaller role. At present, inventories are moving up somewhat faster, reflecting generally increased activity as well as some stocking up of steel by users as a hedge against a possible steel strike.

Federal Government expenditures are rising primarily in support of our defense effort. Expenditures by State and local governments continue their long-term upward growth to meet the requirements of expanding population and the associated local needs.

At present, our balance of payments shows a sizable deficit. The prospects this year are for some rise in imports to support higher levels of domestic activity. I am confident that the programs we now have underway should result in increasingly higher exports. With our large commitments abroad and the continuing outflow of funds, I consider that our total balance of payments still remains a major problem area.

Economic developments of the past year have been accompanied by virtual price stability. Some prices moved up moderately, but on the whole, overall prices have shown no marked increased. I feel that in view of the adequacy of capacity and supplies this year, we may be able to achieve, along with continued rapid recovery, a fairly stable price situation. This can only be achieved if management and labor pursue a moderate course in their settlements.

We have learned from painful experience that the production lost through cyclical unemployment and decline in output is never regained. In order to minimize such irretrievable losses, should another such contingency arise, I strongly endorse the President's proposals for standby authority to make temporary prescribed reductions in individual income tax rates, and to initiate a previously approved capital improvements program.

But this would be triggered only by another downturn, and I view the current economic situation with optimism. I feel that we will have continued expansion in demand throughout the entire year. However, we still have the very serious problem of a continued high rate of unemployment. Even with this good recovery, we have reduced the rate of unemployment by only modest amounts. While some further reduction in unemployment may be expected during 1962, we will still have an undesirable rate. Our job, therefore, is to provide the necessary assistance and guides for the private economy so that, as President Kennedy has projected, we can at least reach a point in 1963 where unemployment will be reduced to the tolerable, if not desirable, rate of 4 percent.

WEAPONS FOR GROWTH AND STABILITY

The Employment Act of 1946 sets forth the responsibility of the Federal Government "to provide maximum employment, production, and purchasing power." These goals must be achieved within the broad framework of U.S. political and economic institutions—free competitive enterprise and the federal system of government—through means that take into account our other national needs, obligations and objectives.

One major goal of economic policy is to achieve the maximum use of our existing productive resources. To do this we must maintain aggregate demand at sufficiently high levels to buy the goods and services that our fully utilized economy is capable of producing. In addition, Government policy must eliminate rigidities in the labor and product markets to bring into effective use a greater proportion of the Nation's productive resources.

Simultaneously, we must insure that our domestic efforts are not thwarted by imbalances in our international payments position. Persistent deficits and gold outflows have made the balance of payments a critical problem of economic policy. We must continue to meet our heavy obligations abroad for the security and development of the free world, without continued depletion of our gold reserves or excessive accumulation of short-term dollar liabilities to foreigners. Increasing our exports relative to imports is a task of highest priority. We must also continue to lead the free world toward greater reduction in barriers to international trade and must induce our allies to help us to increase the flow of resources from developed to developing countries.

A third major goal of economic policy is to reconcile high employment levels with overall price stability, while permitting individual prices and wage rates to vary with changes in costs and demand. Any attempt to stabilize prices through the imposition of direct wage and price controls would be unacceptable, and policies which would pursue price stability without regard for the effects on employment production and purchasing power would be equally unacceptable. The need for balance in our international payments gives additional and compelling importance to the goal of price stability. To guide resources into full and efficient use, there will, of course, be fluctuation in specific prices, but, hopefully, all within the framework of a generally stable price level.

Full utilization of resources, balance-of-payments equilibrium, price level stability are the traditional goals of economic policy implied in the Employment Act. To achieve this stabilization program, we use monetary-fiscal policy, and a wages and prices policy. But this is not enough. We need a faster rate of growth. But we also need an economy even richer in the variety of its opportunities than can be obtained by sole reliance on the traditional stabilization weapons. There are tools which can help us by providing the fuel which will enable our economic engine to operate at peak velocity, but the efficiency of a unit of economic horsepower can be maximized only if the best available lubricants are added. Our fully employed economy can render optimum service to our people if Government moves also to stimulate and to ease the adjustments of our business firms to new markets and production processes, and of our workers to new employment opportunities both occupational and geographical.

This aim of maximum flexibility and adaptability can be attained by such activities as providing business firms, both large and small, with the latest technical and economic information; by the provision of inducements for private research and development and for plant modernization, and of financial assistance to businesses, workers, and communities which are victims of economic blight; and by the elimination of those educational and ethnic barriers which inhibit maximum utilization of existing and potential manpower skills. Successful action in these areas will close the gap between what our economy is accomplishing and what it is capable of achieving. It is in this general policy area that I believe commerce can and should make great contributions. The Department of Commerce is highly sensitive to the needs of business and other sectors of our economy for the statistics and other information required for sound private economic decisions. It is proud of its Bureau of Census and its Office of Business Economics and the key statistical information they provide on economic developments here and abroad. The Department is taking steps to strengthen its research on economic trends and problems. With its two new offices—the Office of Industrial Growth and Research, and the Office of Economic Programs—the Department is strengthening its research effort on trends and problems in U.S. economic development. These offices, within the Business and Defense Services Administration, are working with our industry divisions to develop better means of serving the needs of American industry. These industry divisions form a major intermediary through which data and information gathered by Government are analyzed and interpreted for the business community by experts intimate in the particular needs and interests of each industry.

In order to afford the maximum on-the-spot assistance to American businessmen, the Department has established the one-stop Business Service Center through which businessmen can secure what information they need concerning the entire Federal Establishment and its activities. This one-stop center is duplicated throughout the Nation in 34 Department of Commerce field offices, whose staffs are being strengthened. These offices are also being geared in more closely with the work of our foreign country experts, and our commercial attachés abroad, so that American businessmen will be better alerted to export opportunities.

The economic performance of a society should be judged by the effectiveness with which it uses its economic endowments in furthering the well-being and ultimate objectives of its people. We must work continually to improve the quality of our labor force and its employment opportunities, and modernize the plant and equipment with which it works. Government policy must reinforce with positive programs the effectiveness with which our businessmen and workers compete at home and abroad.

Much can be and should be done to improve the quality of our human resources. The Department of Commerce enthusiastically supports the President's proposals for aid to education, believing that this is the vital factor in long-run economic growth—as well as one that directly affects the future of our free democratic and economic institutions.

Our commitment to economic progress generates demands for new or higher skills, and obsoletes old ones. We must, therefore, help our labor force and our industries develop increased capacity to adjust to economic change. It is evident that larger expenditures and new programs are needed in the areas of worker training and retraining to enable our labor force to supply the kinds of skills which our dynamic industries now require and will increasingly require in the future.

EQUALIZING JOB OPPORTUNITIES

Both the quantity and quality of our economic growth are weakened by racial and religious barriers against economic advancement. These factors reduce our productivity by distributing our labor force less effectively among employments than otherwise would be the case. The social inequities of job discrimination are enhanced in recessions—when the evils of educational deprivation and job discrimination are compounded by high rates of unemployment. A hard-headed sense of economics and considerations of social justice demand that we continue the progress already made in expanding job opportunities for all our citizens.

ENHANCEMENT OF TECHNOLOGICAL PROGRESS

Our economy can rise to even greater heights within the framework of our free enterprise system if we can enhance the pace of technological progress which has made us the envy of the world. This can be accomplished by stimulating technological innovation, encouraging plant and equipment modernization, and by selective readjustment measures.

The report includes two proposals designed to improve the fiscal incentives for new investment. One, already submitted for the consideration of the Congress, would provide an 8 percent tax credit for gross investment in depreciable machinery and equipment. By increasing the profitability of productive investment through reducing the net cost of acquisition, this tax credit would stimulate an increased rate of plant and equipment modernization and expansion. In addition, the Secretary of the Treasury, I understand, will shortly implement his program to bring the depreciation schedules specified in its Bulletin F, into line with current experience. The recent acceleration of allowable depreciation for the textile industry indicates what business generally can look forward to in this direction. To reinforce the effects of these measures, the Department of Commerce is studying the merits of Federal credit guarantees of commercial bank loans for productive investment.

The report also suggests measures for improving technological progress by expanding and stabilizing the markets in which our businessmen sell their wares. As I have previously indicated, the report proposes courses of action designed to alleviate the instability which has characterized our economy through most of the postwar period and to move ahead to higher levels of employment and output. Successes in implementing this policy should contribute markedly to the strengthening of business expectations and improving the climate for risk investment. In addition to this enlargement of our internal markets, the Government, through the Department of Commerce, is pursuing an active policy of expanding foreign markets through our trade exposition and travel programs.

We are also endeavoring to stimulate progress through an active sponsorship of technological innovation and dissemination. The Panel on Civilian Technology—under the joint sponsorship of the Council of Economic Advisers, the Office of the President's Special Assistant for Science and Technology, and the

Department of Commerce—is examining opportunities for stimulating civilian research and development as well as for the more effective use of existing technology. In addition, the new Office of Industrial Growth and Research of the Department of Commerce is engaged in research designed to implement the Panel's mission.

Within the Department of Commerce our Office of Technical Services furthers the cause of technological dissemination by serving as the major communications link between Government-supported scientific activities and those small business firms which lack the resources to undertake their own research. We are seeking to strengthen the relationship between science and economy in the pending legislation requesting authorization of an Assistant Secretary for Science and Technology. Our interest in spreading the benefits of technology throughout the economy is also being implemented in our effort to develop an equitable policy with respect to the division of rights in inventions flowing from Government contracts. Last, but not least, I wish to mention the research conducted by our Bureau of Standards. One of its most significant current efforts involves the development of a complete system of measurements matched to the increased demands for precision standards for American science and industry.

As the report indicates, a high and increasingly stable level of employment may be achieved through effective implementation of the aforementioned fiscal, monetary, trade, and price policies. Even so, certain "hard core" localized areas of substantial unemployment and underutilization of capacity will remain.

In this regard, I would like to comment briefly on the area redevelopment program, which the Congress passed last year largely as a result of the efforts of the distinguished chairman and vice chairman of this committee.

The basic responsibility for economic redevelopment, of course, rests with the community itself. The designated areas prepare their own comprehensive surveys of their resources and develop their own plans for the full development of their economic resources. Nearly 400 redevelopment areas already have completed their basic planning, and ARA has approved 300 of these programs for progress.

To these self-help efforts are added the resources of a task force of Federal agencies—our own Department of Commerce, of which the Area Redevelopment Administration is a part; the Departments of the Interior, Agriculture, Labor, and Health, Education, and Welfare; the Housing and Home Finance Agency and the Small Business Administration.

We are using the new tools provided by the Area Redevelopment Act to reinforce local self-help programs. The loans and grants which have been approved in the four months since the Congress appropriated funds for ARA will lead to the creation of 3,600 direct new jobs—and this is only the beginning. Direct employment is only one of the benefits, since each new job brings secondary employment, greater purchasing power, more tax revenues, and the reduction of welfare and unemployment benefits.

A good example of what economists call multiplier effects can be found in Carbondale, Ill., where a $455,000 Federal loan induced an additional $1.3 million in local private and public investment, to help a new company get started.

An ARA study shows that the new plant will provide 700 direct new jobs and, taking the most conservative estimate of only 40 additional jobs created by each 100 direct jobs (most economists use much higher multipliers), the new plant will bring some 280 secondary jobs. Additional payrolls for the area will be $4.3 million annually, producing new personal Federal income tax of $226,800 each year. The new jobs will cut welfare expenditures by $98,000 every year, and will reduce unemployment payments by $343,000 each year.

All of these benefits will repeat year after year; and all of them flow from a single Federal loan of $455,000—a loan which will be repaid, with interest. We hope we can have many more like this one.

Another long-term effect of this new program comes in the area of retraining workers whose skills have become obsolete. In cooperation with ARA, the Departments of Labor and Health, Education, and Welfare already have approved training programs to prepare 4,000 workers in nine States for jobs requiring new skills.

These courses are, in a sense, pilot projects. Our experience with them will prove invaluable in the development of the broader retraining program now before the Congress—a program that will reach workers in all areas, not merely redevelopment areas, where changing times and changing technologies make it imperative that workers learn new and marketable skills.

Since the establishment of the Area Redevelopment Administratiton, we have brought together a team composed of private enterprise, the community, the State and many agencies of the Federal Government. And we have made a sound beginning.

With the overall economy moving forward again, it is imperative that we concentrate more Federal effort on these persistent pockets of joblessness. And in helping the people in these areas to share in the Nation's prosperity, we will be contrbuting further to national growth.

The Trade Expansion Act of 1962, another imperative, may impose some readjustments on a limited number of sectors of the economy adversely affected by increased foreign import competition. The resulting hardships will be but a small fraction of the benefit of the reduction in trade barriers to the economy as a whole. Nevertheless, the Nation as a whole must assume responsibility for any major adverse impacts. Under this act, temporary adjustment allowance and retraining and relocation assistance to displaced labor will be provided. For the affected businessman, a program of technical assistance and tax benefits and loans will be set in motion to encourage modernization and diversification.

For the problems of the textile industry, which are already especially acute, special solutions have been adopted. Temporary relief has been obtained by agreement with other producing nations to hold their exports to the United States at the fiscal 1961 level. Longer term solutions will be forthcoming from the Commerce Department's research project to help the industry and from the Treasury's liberalized depreciation allowances on textile machinery.

The bulk of the investment required to move our economy toward higher levels of output and employment at an accelerated rate will be undertaken under private auspices. In order to permit our productive capital and technology to be used with maximum efficiency, investments are required in the public sector. The need for increased outlays for educational and health purposes has been noted in my references to improving the quality of our manpower resources. The increasing complexity of our economy and increasing congestion of our urban areas has made the issue of adequate transportation apparent to all of us. The report notes that sustained economic growth requires accelerated investment in transportation services. The Department recently submitted recommendations to the President for improvement and encouragement of sound conditions in our transportation industry. It is anticipated that the President will be submitting a message to Congress on this subject shortly. Meanwhile, the Department is carrying out its responsibility in the expanded highway program, is cooperating with the HHFA in developing aids to urban mass transportation, and administering its extensive program for aiding investment and operations in the American merchant marine.

ENHANCING OUR INTERNATIONAL COMPETITIVE POSITION

Our international payments position continues to be of major concern. In 1961, the United States incurred a deficit in its international accounts of nearly \$2.5 billion. This was a considerable improvement over the deficit of \$3.9 billion of 1960. It was also a considerable improvement upon 1958 and 1959 when they were of about the same magnitude.

Two-and-a-half-billion dollar payments deficits, while smaller than those in any of the preceding 3 years, cannot be long sustained. In stating his objective with respect to the U.S. balance of payments position, the President said, "We must attain a balance in our international transactions which permits us to meet heavy obligations abroad for the security and development of the free world, without continued depletion of our gold reserves or excessive accumulation of short-term dollar liabilities to foreigners." A little later on in his Economic Report, he added, "I am hopeful that the target of reasonable equilibrium in our international payments can be achieved within the next 2 years; but this will require a determined effort on the part of all of us—Government, business, and labor."

We are proud of the way in which America has responded to the challenge of international competition. But we would be deluding ourselves if we thought this problem was licked. Much has been done; much remains to be done. We of the Department of Commerce will assist the President in every way we can to reach these essential objectives.

To a certain extent the improvement last year was due to special transactions, such as large advance debt repayments we received from Germany and other countries. Without these extraordinary receipts, the deficit would have been around $3 billion.

Basic confidence in the dollar has already been restored by the determination of the President to defend the dollar. This can be demonstrated by events in 1961. Our deficit in the second half of the year was considerably higher than in the first half. Yet, the portion of the deficit that was settled in gold in the second half was smaller than in the first half.

The President's budget and his Economic Report should amply dispel any lingering doubts about the dollar that may remain here or abroad. In addition to our general economic policies, we are convinced that passage of the Trade Expansion Act of 1962 and the eliminating of foreign "tax havens" should do much, in themselves, to restore order to our international accounts.

THE TRADE EXPANSION ACT OF 1962

The proposed Trade Expansion Act of 1962 may well be the most important legislation to come before the Congress this year—and perhaps even in the past decade or more. It is vitally important that all Americans understand the full implications and pioneering objectives of this legislation.

The President's Trade Expansion Act is aimed at protecting and promoting the vital foreign policy and economic interests of the American people. It will further the growth and cohesion of the free world, including the Atlantic Community. At the same time, it will strengthen the American economy and benefit in a very tangible way—in dollars and cents—American businessmen, workers, farmers, and consumers.

As the President stated in his Report," * * * An increase in the U.S. trade surplus is of the first importance." Our accounts must be brought into approximate balance. To accomplish this, our exports must increase substantially relative to our imports.

I am convinced that passage of the Trade Expansion Act is essential for the resolution of our balance of payments dilemma. I am equally convinced that denial of the President's request or dilution of it will doom our efforts to failure.

We are confronted today with the hard facts of life about the European Economic Community, the Common Market. In sheer scope and imagination, we must go all the way back to the formation by the Thirteen Colonies of our own political and economic union to find a historical parallel. The United States can be proud of the role it played, as far back as the Marshall plan days, in the events leading to the establishment of the Community only 5 short years ago.

But where do we go from here? We must move quickly to get in step with the Common Market. If not, the growth in our exports to Western Europe, about 30 percent of our total exports in 1960, will surely slow down and these exports may even shrink. And, remember, this is the fastest growing and lushest export market in the world for us.

As you know, the six-member nations (Belgium, France, Germany, Italy, Luxembourg, and the Netherlands), soon to be joined by some of their Western European neighbors, are rapidly eliminating their internal barriers to trade, including tariffs. Soon a Frenchman will be able to sell his products in Italy without any national restrictions just as a South Carolinian sells his products in North Carolina or in Texas to California.

With the reduction and eventual elimination of internal European trade business, the American will have to hurdle, among other things, an external tariff wall that simply will not exist for his European competitor. As you know, the common external tariff of Six is based in general on the arithmetic average of the 1957 tariffs of the four customs areas (Benelux, France, Italy, and Germany).

To illustrate the effects of the interplay between the establishment of a common external tariff and the elimination of tariffs internally, let us look at the European tariffs on bookbinding machinery. Before the Common Market, the tariff on bookbinding machines in Italy was 18 percent; in France 16 percent; in Germany 5 percent, and in Benelux nations 6 percent. The common tariff is the arithmetic average, 11 percent. What this means, of course, is that in all countries the United States will be confronted with an 11-percent tariff disadvantage while free trade will obtain with the Community. More important, perhaps, is the situation which can be illustrated by the German tariff. Formerly, a Belgian manufacturer and an American had to scale a 5-percent tariff. Now the Belgian sends goods to Germany duty free while the United States goods will be subjected to an 11-percent, rather than a 5-percent, levy.

If we do nothing about this situation—this external tariff—profit margins in our export business will be squeezed or may in some cases simply vanish. Under these circumstances, many of our export industries will either be forced to abandon this business or, if they can, to transfer their production facilities to Europe. Thus, if we do nothing or not enough, our exports could decline, adversely affecting American jobs and profits, as well as worsening our balance-of-payments position.

The mutual trade liberalizations by ourselves, the Europeans, and our other trading partners, will give us a golden opportunity to preserve and expand American jobs and profits through the expansion of exports. It is imperative that the President be given the tools with which to bargain effectively with the European Community. I need not remind you that the President will need plenty of room for maneuver when we sit down at the negotiating table with the representatives of other trading nations.

We in the Department of Commerce have been involved at every stage in the development of this legislation. We recognize the importance of export trade to every State of the Union, as is illustrated in the "Export Origins Survey of Manufactures," recently released by the Bureau of Census of the Department of Commerce. We believe its passage essential to the future prosperity of the business community, to this Nation's future, and to the future shape of the free world community.

EXPORT EXPANSION ACTIVITIES

Now let us turn to the question of what the Department of Commerce is doing to help America's businessmen expand exports, which the President has strongly urged.

First, we have been working very closely with American business to provide the information and supplemental services necessary to attain enlarged oversea markets for U.S. goods. This has involved advice and counsel to those currently selling abroad as well as encouragement and assistance to American producers who have not yet embarked on oversea sales campaigns.

Secondly, the Department has been seeking the elimination of foreign governmental restrictions which have the effect of denying us markets in which we might otherwise compete. These efforts are carried forward, in consultation with the Department of State, through intragovernmental and international organizations concerned with trade and commercial policy, and through bilateral contacts. Most important in this connection is our work in the fields of tariffs, nontariff barriers to trade, and commodity agreements.

Another aspect of foreign economic policy which has a direct bearing on business activities and our drive to develop export markets involves U.S. lending policies. Here we are working to mobilize effectively the private sector not only in the interest of our export program but also in support of the Government's foreign assistance programs as a whole.

Business requires the advice and support of the Government, and Government needs the advice and practical experience of business on the many unfolding changes in world trade and investment patterns. The Department of Commerce during the past year has been energetically moving forward through its strengthened Business and Defense Services Administration, in carrying out the role of intermediary in this regard.

We have developed and are strengthening a diversified program of information collection, analysis, evaluation, and distribution on the economic developments in all parts of the world. We provide a source of information and familiarity in depth with international economic events that is basic to all the foreign economic activities of the Department and to American business as well.

Principally through the new Bureau of International Programs, the experience of American business is being brought to bear in the development of Government policies and programs in the fields of commercial policy, commodity policy, and financial policy. Particular attention is being given to measures and activities which tend either to encourage and facilitate or to hamper and restrict international trade and investment. We are increasing our efforts to seek trade liberalization and the removal of foreign discrimination against American goods.

Our new Bureau of International Business Operations is geared to provide sharply expanded services to American businessmen to assure accelerated growth in export trade. While emphasizing the promotion of export trade, this Bureau has the added responsibilities of encouraging expanded participation by private enterprise in U.S. foreign aid programs and identifying opportunities for foreign investment in the United States, particularly in distressed areas.

Three significant additional export promotion program activities are contemplated in fiscal 1963: They are—

(1) A commercial specialist program to increase the effectiveness of oversea commercial services.

(2) A trade missions program, reoriented toward obtaining immediate results to increase exports of U.S. products and commodities for which the host country has a need and the ability to purchase.

(3) A trade and industrial exhibits program to exploit areas where the market potential for American goods is the highest.

The commercial specialist program aims to satisfy a long-felt need for developing within the Foreign Service specialization in oversea commercial activities.

The trade missions program has been subjected to a most critical review and reorientation during the past year. Our major emphasis today and in the future is to develop business contacts and trade leads so as to provide new opportunities for American business and industry, and to bring to the attention of American businessmen specific opportunities for licensing and joint venture operations in host countries.

The trade and industrial exhibits program provides the vehicle for exhibiting the products of American industry in countries and areas of the world where the market potential for such goods is greatest. The successful London Trade Center operation has demonstrated the particular opportunities that exist for small business ventures in export markets. The successful exposure of American industrial equipment to new and emerging nations of the world, striving to build an industrial potential of their own, should assure export markets in these countries for the long-term future.

We are also strengthening our national and regional export expansion committees and mapping out for them a program of practical action which will seek to expand the existing volume of exports and introduce new business firms to the field of foreign commerce. A part of this program—an up-dated version of the Army-Navy "E for excellence" awards—is designed to honor companies, associations, institutions, and individuals for significant contributions to the expansion of U.S. exports. Each "E" candidate will be certified by the Department of Commerce field office and the regional export expansion committee in his area.

The Public Relations Society of America is cooperating with the export expansion committees through recommending that the society's chapters across the country serve as volunteer public relations and promotion counsel in the respective areas.

In addition to these activities, the U.S. Travel Service has been established within the Department in the past year. The United States is one of the last major countries to begin a Government program to encourage tourism. I am happy to report that, despite the short time it has been in operation, we have already made important progress and laid the foundation for major accomplishments in the future.

For example, on the presses right now are posters, informational booklets, calendars of coming events, and other attractive literature about the United States—all being printed in seven languages for use in our best travel markets.

Although the past few months have been devoted largely to "tooling up" they have also produced some end products essential to our tourism plans. Now, with our travel representatives in place, with permanent travel offices opening soon in major travel centers, and with literature, posters, and advertising on the way, we look to the beginnings of a full-scale travel promotion program.

It is still too early, and the Travel Service is too new, to make statistical predictions of the 1962 tourist flow. However, there seems to be a growing impression throughout the world that the United States is a friendly, exciting travel destination, and less expensive than most people imagine.

With the continued support of the Congress we are confident that we can maintain and increase our effectiveness in carrying out all of these programs. We must and will be responsive to the ever-changing patterns and requirements of trade. We will strive to strengthen the U.S. position of leadership in the field of international trade, knowing that this is a vital element in both the cold war and the health of our domestic economy.

CONCLUSION

A successful stabilization policy is vital, but not enough. A successful program for economic growth is vital, but not enough. The appropriate economic policy for America must combine and build on success in these two vital policy areas, and build upon them.

The Department of Commerce is convinced that the challenge of the 1960's is to achieve an economy which brings worth the maximum potential of this society. The needs of our people and our international responsibilities demand nothing less.

SUPPLEMENTARY STATEMENT BY LUTHER H. HODGES, SECRETARY OF COMMERCE, ON THE AREA REDEVELOPMENT ADMINISTRATION BEFORE THE JOINT ECONOMIC COMMITTEE, FEBRUARY 2, 1962

I have prepared a special supplement on the new Area Redevelopment Administration within the Department of Commerce because of the interest in this program in the 9 months since President Kennedy signed the legislation into law.

This committee is familiar with the 6-year legislative history behind this act, including the Presidential vetos of 1958 and 1960. I mention this only because the Area Redevelopment Act has been misconstrued as an antirecession measure, although neither the Congress nor the administration considered this as emergency legislation.

So we should not let our present sound recovery from the recession obscure the fact that areas of chronic unemployment and underemployment still exist—instead, we should use this period of expansion and growth to accelerate our efforts to help these areas help themselves.

This legislation provided new Federal tools—loans and grants, technical assistance and job retraining—for the use of these areas in developing workable economic programs. It also called on us to draw to the fullest extent practicable on the resources and experience already in existence within the Federal Government. Thus, in addition to the Area Redevelopment Administration within the Department of Commerce we have a working team consisting of elements of the Departments of the Interior; Agriculture; Labor; and Health, Education, and Welfare; the Housing and Home Finance Agency; and the Small Business Administration—all of them focusing their efforts on this problem of chronic area joblessness.

There are more than 800 of these redevelopment areas, in 47 States, Puerto Rico, American Samoa, Guam, and the Virgin Islands. They range from Lowell, Mass., to Uniontown, Pa., and Beckley, W. Va.; from the coal towns of East Kentucky and southern Illinois to the cotton and tobacco towns of Arkansas and Mississippi; from the cutover area of Michigan's Upper Peninsula to the lumber towns of the Pacific Northwest and on out across the Pacific to the State of Hawaii and our island possessions.

The underlying responsibility for their economic development programs, of course, rests with the community. The initiative, the basic investment, the planning—all these must percolate up from the local level.

The role of the area redevelopment program is to supplement, not supplant, this local effort; to join the resources of the Federal Government with those of private enterprise and local and State governments. So designation of a piece of geography as a "redevelopment area" confers no automatic Federal financial benefit on the area. It merely invites the area either to begin, or to intensify, local redevelopment activities.

Before the Area Redevelopment Administration can even consider an application for financial aid, the area must prepare its own comprehensive survey of its human and physical resources, and must develop its own plan for the full development of its economic resources.

These plans are worked out at the local level, by committees representing a broad spectrum of community interests—businessmen, organized labor, bankers, educators, farmers, public officials, and others.

Development of these comprehensive community surveys—we call them overall economic development programs—has, to a large extent, occupied the primary attention of local groups, State agencies, and ARA for no other activities could commence until these programs were drawn up.

Already, nearly 400 redevelopment areas—almost half of those designated—have developed these local programs and submitted them to both State authorities and ARA for approval. Of this number, nearly 300 locally conceived plans for economic development have been provisionally approved by ARA, paving the way for consideration of requests for Federal financial participation in specific projects.

And while this planning was moving forward, the pipelines were filling up with project requests. There are 101 projects pending at the present time—projects requesting some $80 million in Federal funds. And many more are in the developmental stage at the local and State level.

ARA already has reserved nearly $30 million for 37 projects. In other words, these have been advanced to the final stages of review and action by the several Federal agencies which share the workload of this program with ARA. Some 17,000 permanent new jobs are involved in these projects for which funds have been set aside by ARA.

In addition, in the 4 months since Congress appropriated funds for the area redevelopment program, 12 projects, involving $2.9 million in Federal funds, have been approved. Of this amount, $2.6 million is in the form of loans, which will be repaid, with interest, to the Federal Government. These funds augment some $6 million in local private and public investment in the same projects. We are using Federal funds to "seed" local economic efforts; to go that "last mile" between what private enterprise and communities can do on their own and what needs to be done.

These projects already approved will provide 3,600 permanent new jobs in these areas.

And this is only direct employment. Economists know that each direct new job in industry creates indirect employment. A new plant needs new suppliers—of material, of equipment, of local services. A new plant means employment in the construction phase. And new payrolls mean new purchasing power, which also generates more jobs.

In my general testimony I referred to the "multiplier effect" of a single ARA project in southern Illinois—the new jobs and new Federal income tax revenues, the reductions in welfare payments and unemployment insurance benefits that will flow year after year from a one-time Federal investment that will be repaid to the Treasury.

There are other examples which reinforce the fact that the dollars that go to the community from the Federal Government under this program are designed to stimulate employment.

A case in point: Mingo County, W. Va., an area where unemployment has been close to the 30-percent mark for several years. ARA's role was to make a half-million-dollar loan, to go along with local private money and State funds for the establishment of a homegrown industry—a firm that will employ 200 in manufacturing furniture parts out of hardwoods that abound in the area.

The loan was made just 3 months ago—on November 1—and the walls of the new plant have only now begun to rise. But the company has already ordered the first of its equipment for the new plant; has already placed orders for two diesel tractor-trailers costing $30,000 each; has already hired supervisory personnel—and all of these mean new money changing hands.

In addition, the new firm has already placed orders for its raw material, and that has meant immediate jobs in logging and sawmill operations. A training program has been launched under ARA for 100 millmen, and the turnout for registration was so great that the employment service office was too small to handle the crowd, and registration was conducted in a church auditorium. As a result of the ARA loan, a businessman has decided to put up a new restaurant near the plant to provide hot meals for the new hands; and a contractor is planning to build 10 to 15 new homes in that community for the key management personnel coming into the area.

Not all of the investment under ARA is immediately measurable, of course. This is particularly true with technical assistance projects—those joint efforts by communities, States, and Federal Government to break down longstanding barriers to economic growth.

One of these projects is a study to help develop improved handling procedures and new markets for the fishing industry in New Bedford, Mass., for many years an area of chronic unemployment. Another involves a series of tests to help produce steel and iron out of low-grade, nonmagnetic ores from the western Mesabi Range of northern Minnesota. Another concerns a possible industrial lake in southern Illinois, where the absence of an adequate, stable supply of water already has deprived the area of considerable industrial expansion.

These are the projects which take time to develop; but they could bear the greatest fruit. If we can break the bottlenecks which have impeded progress in the past, these projects can lead to millions of dollars in private investment and thousand of new jobs.

Attached to this statement is an appendix listing the approved ARA projects to date. We have not included the substantial start which has been made under the retraining and subsistence section of the Area Redevelopment Act because the distinguished Secretary of Labor already has reported to this committee on the training phase of this program.

Let me emphasize here, however, how important the cooperation between ARA, the Department of Labor, and the Department of Health, Education, and Welfare has been in bringing so many of these training programs into being in such a short period of time. Cooperative effort throughout the Federal establishment—among all seven of the departments and agencies involved in this program—and the cooperation between local and States bodies, has contributed to the start that ARA has been able to make.

This teamwork, plus a good measure of American ingenuity, will go a long way toward combating chronic unemployment and underemployment.

APPENDIX A.—*Approved ARA loans and grants*

Location	Date approved	Description of project	Amount involved	Permanent new jobs
Gassville, Ark	July 24, 1961	Water system to Mar-Bax Shirt Co.	$31,000 loan, $129,000 grant.	1,000
Cambridge, Md	Sept. 14, 1961	Sewer system to Chun-King Corp. and Western Publishing Co.	$68,000 loan $204,000 grant	225 650
Carbondale, Ill	Oct. 23, 1961	Expansion of Technical Tape Corp.	$455,000 loan	500
Mingo County, W. Va	Nov. 1, 1961	Establishment of National Seating & Dimension Co.	$572,000 loan	200
Mountain City, Tenn	do	Water and sewer systems to Leco Manufacturing Co.	$60,000 loan, $46,300 grant.	300
Cedartown, Ga	Dec. 22, 1961	Water, sewage systems, and access roads to Inland Homes Corp.	$260,000 loan	100
Ava, Mo	Dec. 29, 1961	Expansion of Rawlings Manufacturing Co.	$81,250 loan	100
Socorro, N. Mex	Jan. 11, 1962	Establishment of Socorro Packaging Co.	$130,000 loan	35
Apalachicola, Fla	Jan. 12, 1962	Establishment of Florida Seafood Canning Co., Inc. Water, sewage systems to same concern.	$652,135 loan $28,000 loan	350 ----------
Lowell, Mass	Jan. 25, 1962	Establishment of Semi-Onics, Inc.	$97,500 loan	110
Demopolis, Ala	Jan. 31, 1962	Expansion of Griffith Packing Co.	$145,685 loan	58

APPENDIX B.—*Summary of Area Redevelopment Act program*

REDDVELOPMENT AREAS

Type of area	Number	Population (millions)
Urban industrial areas	146	21.1
Rural areas, very small labor markets	686	12.5
Total	829	36.6
Indian reservations [1]	47	.2

[1] Many Indian reservations overlap 1 or more geographic areas already designated under other criteria.

OVERALL ECONOMIC DEVELOPMENT PLANS

Total submitted: 380 areas and 11 Indian reservations in 43 States and American Samoa (45.8 percent of all areas designated); total population, 23.7 million.

Provisionally approved: 294 areas and 9 Indian reservations in 38 States and American Samoa (35.4 percent of all areas designated); total population, 20.4 million.

PROJECTS APPROVED

Seven industrial projects; $2.8 million in loans; 1,353 permanent new jobs.

Five public facility projects; $447,000 in loans; $379,300 in grants; 2,275 permanent new jobs.

Four technical assistance projects; $220,000 in contracts.

Chairman PATMAN. Thank you, Governor Hodges.

Will it be agreeable to you, if any member desires to ask you a question in writing, for you to answer it when you have looked over your transcript and submit it for the record, please, sir?

Secretary HODGES. Yes, sir.

Chairman PATMAN. I have some questions I would like to ask you later. At this point I would like to mention the area redevelopment program. You have a statement here about it and we will make it a part of the record, as part of your statement.

Secretary HODGES. Yes, sir.

Chairman PATMAN. You have selected a mighty fine man to administer that program—Mr. Batt from Pennsylvania. He has had a similar program up there.

Secretary HODGES. He is with us today.

Chairman PATMAN. I think he is trying to do a good job but I am afraid it is on dead center in some parts, Governor Hodges. I know Mr. Batt is doing his best to administer it properly and efficiently and effectively. I feel sure he is going to do what is necessary. I am convinced of his sincerity and honesty of purpose. But the program is going along slowly.

Naturally I expect it to go slowly because we are pioneering. As you stated, it is needed without reference to any recession. I consider it a part of the permanent law although we agreed to 4 years, I think. I don't believe there will be any question about extending it and making it a part of the permanent law because it is needed all the time.

I notice that you have a rather full report on it but I do hope that you will give consideration to some of these problems that are really pressing right now but don't seem to get very quick approval. I am not advocating that you approve projects that are not worthy and justified but, with respect to any that are worthy, I hope you will act as quickly as you can.

We will make your statement about the area redevelopment program a part of your statement.

Secretary HODGES. All right, sir. If you want to ask Mr. Batt some questions he will be glad to come up with me.

Chairman PATMAN. He has been very cooperative.

Secretary HODGES. I am acquainted with the program. It does look slow. As you know, I broke loose some months ago and said he should be moving a little faster. The pipeline is now quite full. It takes several months to get started. When you have several cooperating agencies it delays it that much more.

Chairman PATMAN. You have six or seven cooperating agencies.

Secretary HODGES. That is right.

Chairman PATMAN. That lends itself to delay. You know, it is awfully hard for one agency to do everything rapidly or quickly but when you have several agencies to confer with, it adds to the delay. I hope that it does not slow up this project too much. We have not been too well pleased so far and I am not blaming anybody. I am just saying it is a new program; it is pioneering. We expect some bugs in it. We do expect to iron them out and I am convinced that you and your people are doing their best to administer the program properly.

Secretary HODGES. Thank you, sir.

Chairman PATMAN. Senator Bush?

Senator BUSH. Thank you, Mr. Chairman.

Mr. Secretary, I join in welcoming you before the committee.

Secretary HODGES. Thank you, sir.

Senator BUSH. I am very much interested in this trade program, particularly, and I am going to ask you to submit some more data on this so that we can judge more accurately what we are talking about when we talk about exports and imports. I will send you a letter which will ask for the information if it can possibly be made available.

Secretary HODGES. All right, sir.

Senator BUSH. I was looking at the report by the Department of Commerce here dated January 29. I came across this statement:

> The survey reveals that approximately 6 million American workers are employed in manufacturing plants which produce for export, Secretary Hodges said.

Mr. Secretary, I wonder if that is a fair statement to make. The impression that it definitely gives is that the plants employing 6 million workers are engaged in the export business. In other words, that there are 6 million workers engaged in the export business. I think it is a misleading comment. I saw in a Connecticut paper recently a statement that we had 175,000 workers in Connecticut working in plants which did an export business. Well, we only have 400,000 factory employees in the whole State. So, obviously it was a thoroughly misleading statement.

In order to sell this program, it seems to me, there is an undue effort to exaggerate the figures. I do think that it is not fair to present figures which indicate that there are more workers engaged in the export business than there really are.

Now accompanying this report is a table entitled "Value of Exports of Manufactured Product by Region and State and by Major Product Group, 1960." It shows, for instance, in Connecticut—I use this example because it is close to my heart—it says exports of manufactured products, Connecticut, $385 million. But underneath it says $244 million is the estimate given to the Census Bureau by the manufacturers themselves, so that the discrepancy there is $140 million. Under tobacco products your figures show $1,800,000 of exports but the Census could not find any, they denied that there were any exports in tobacco. In connection with lumber and wood products you show $300,000 worth but none were reported to the Census.

All across this table and all through it are great variances between what the Department says and what the Census Bureau says. Now how can we judge these things with that kind of figures before us?

Have you any explanation to give the committee for these figures?

Secretary HODGES. Senator, I would have to agree with you that if you want to be critical of this figure, of the 6 million, it could be misleading. It was not so intended.

Senator BUSH. Mr. Secretary, may I say I don't want to be critical of it. I would like to believe that it was a solid figure.

Secretary HODGES. I think I can explain it because it could bother you when you look at it with other figures. The Labor Department had issued a figure of something over 3 million people who were tied in exports. Our figure simply shows that companies that are doing some export have in there so many workers, a total of 6 million workers. It does not purport to say any more than that.

Senator BUSH. That is not a relevant figure, Mr. Secretary. It is a very misleading figure because the average man who reads that will think there are 6 million people involved in manufacturing exports and they are not.

Secretary HODGES. I agree with you; it could be misinterpreted.

(The following was later received for the record:)

SUPPLEMENTARY STATEMENT OF SECRETARY OF COMMERCE HODGES TO TESTIMONY ON FEBRUARY 2, 1962, BEFORE JOINT ECONOMIC COMMITTEE, IN CONNECTION WITH EMPLOYMENT AND EXPORT TRADE

The Department of Labor has estimated that the employment required in exporting the $20.7 billion of merchandise exported from this country in 1960 was equal to 3.1 million jobs. The Department of Labor has further estimated that of the 3.1 million job equivalent, 1.3 million jobs were connected with the export of manufactured goods. The remaining equivalent of 1.8 million jobs are connected with exports of nonmanufactured goods. It is important to note that the labor figures do not refer to actual persons but to the labor equivalent connected with U.S. exports.

A press release issued by the Department of Commerce on January 29, 1962, contained a statement that a census survey revealed "that approximately 6 million American workers are employed in manufacturing plants which produce for export." This is a correct and valid statement. A total of 6 million workers are employed in plants with 100 or more employees each and with exports of more than $25,000 each, as reported to the Bureau of the Census in its survey of export origin of manufactured goods. The statement above does not say or purport to say that the total production of these 6 million workers is exported.

For those plants in which these 6 million workers are employed as well as for their supply plants and other plants not covered in the Bureau of the Census survey, export business may provide the margin which makes the entire enterprise profitable. Loss of this margin (i.e., loss of export business) would obviously have a definite adverse effect on the plants employing the 6 million workers. This factor is important and should be emphasized.

We must have many more establishments and many more employees involved in export business if we are to achieve the goal of a stronger American economy. Increased exports are vital not only to the profits and employment of the American businessman and American worker, but to the whole national security by enabling us to meet our oversea military and economic commitments while at the same time protecting the soundness of the American dollar.

Senator BUSH. Thank you, sir.

Now, I want to go over to the area redevelopment subject for a moment. You dealt with that. I have here a statement from the Washington Post which appeared December 8, 1961, when they were writing a series of articles concerning the depressed area legislation. This has to do with a shirt factory out in Mountain Home, Ark. The article reports that the Federal Government put up a $160,000 water system. Then it goes on to say what this has meant to the area. But in concluding it makes this statement:

The Mountain Home project and so many others like them are built on shaky foundations of low wages, and antiunion commitments, on the part of a community and heavy public subsidies to unstable industries seeking out low wage and even subservient areas.

Now, Mr. Secretary, do you think that is a fair statement?

Secretary HODGES. Who made it, Mr. Senator?

Senator BUSH. This is made by a staff reporter of the Washington Post named Julius Duscha.

Secretary HODGES. I don't recall seeing the statement. I don't think that is necessarily a true statement because you don't move——

Senator BUSH. The Washington Post has been very favorable to this program.

Secretary HODGES. Of course the Post, like every other paper, makes an error sometimes.

Senator BUSH. But you do not think this is true?

Secretary HODGES. I don't think it is true as a general statement; no, sir.

Senator BUSH. Do you question whether it is true in this case?

Secretary HODGES. I don't know enough about the case. I would be glad to ask Mr. Batt about the case. I would doubt it.

Chairman PATMAN. If you would like to have others accompany you at the table it will be all right.

Senator BUSH. The Secretary may want to look into this privately, I have no objection to that at all, but I do think that it is a matter that is worthy of looking into. I don't think it was the intent of the Congress which passed this bill—and incidentally, I voted for it after some amendments and failure to get through some others. Nevertheless I did vote for it, and I would rather see it succeed than otherwise, I can assure you, but I don't think that this is very good policy, and I don't think that you are going to pick up much of a following for the ARA if that kind of policy is going to be followed. If the Government is going to cooperate with communities to make major pledges to keep unions out and arrangements of that kind, I don't think it is a very healthy thing for the Government to be involved in.

Secretary HODGES. I will say this and I will let Mr. Batt comment further. From the policy point of view of the Government and Department of Commerce on ARA those things are not done. You know by law you cannot transfer a plant. You will find some of these areas which are so-called depressed areas where we are now trying to redevelop you will have some problems, but from our point of view in the Government we don't do any of those things.

Senator BUSH. Mr. Batt, do you want to comment on this? You saw this article?

Mr. BATT. Yes, sir; I saw it. We made some comments on it to the Post. I think it was misinformed. The particular restriction that was put in the act at your urging on outmigration of industry we have not helped finance in any case. This is not a case of outmigrating industry. This is a concern that is already there. It is not a pirated concern.

Senator BUSH. I was not thinking of it as a pirating concern. I am opposed to pirating. And we do have an amendment in the bill. But this is a different question. This is a question of whether a community makes arrangements with a company that comes to settle there that they are going to combine with them in an effort to keep wages down and to keep unions out.

Mr. BATT. Sir, those are the best wages that part of the world has ever seen. I was down there and talked to the people who were working there. There were 300 people there when I was there working in a converted roller-skating rink and various unused store fronts in that little town of Mountain Home. This is the greatest boom that has ever happened to that four-county Ozark area. They are paying wages set by Congress as the minimum. There is nothing stopping the union movement from going in and organizing that plant although it is an open shop at this time.

Senator BUSH. Then this is a misstatement this man has made. There were no arrangements made, no promises or commitments made. Is that what you found?

Mr. BATT. After we heard allegations we checked into it and we found that there were some oral commitments, and I believe they were even reduced to written form but they were thrown out by the court of Arkansas before we got into the act.

Senator BUSH. I am interested in the fact that they did exist and that the intent was to bring about such agreements. In other parts of the country we are trying to maintain the high level that we have gradually acquired here. This is one of the things that is involved in the Secretary's Trade Agreement Act, too. It is very discouraging for us to see the Federal Government through any agency tolerate agreements, whether they be verbal or written, going in exactly the opposite direction.

Mr. BATT. They are paying the legal minimum wage set by Congress in this plant. When the workers have worked long enough to get on a piece rate they are getting a good deal more than the minimum wage. They will have a thousand employees in this area. It is the most cash this area has ever seen. I was convinced after talking to the people there this is the greatest boom they have ever had.

Senator BUSH. I don't regret their increase in prosperity, and I hope they will do well. I do object very strongly to the Government cooperating by the advancing of funds in a situation which involves this type of an agreement. I want to make that very clear. I hope, Mr. Batt, that in the future your agency will examine into such arrangements so that you cannot be a party to promoting that kind of deal.

Mr. BATT. We do, sir. We check every proposal with the National Labor Relations Board and with the Department of Labor to make sure that there are no improper labor relations involved in any effort.

Secretary HODGES. I just want to say again for the record as far as the Government is concerned we have at no time been a party to anything of that character if we knew anything about it.

Chairman PATMAN. Senator Sparkman.

Senator SPARKMAN. Mr. Secretary, I have enjoyed your statement, the part that I have heard, and I have read the rest of it. I think it is one of great encouragement and great optimism.

By the way, with reference to that 6 million figure used about persons employed, I had never thought of that as being an actual count of people that are actively engaged in the export business or in making some particular article that was going to be exported. I thought perhaps the way it was arrived at was by taking our exports of manufactured goods and then determining the number of persons employed in the overall manufacture of those goods.

Secretary HODGES. What is really meant, Senator, and I did not pursue it with Senator Bush because he was going on to another subject—I used to be in the manufacturing business, myself—if you get an extra 5 or 10 percent volume toward the top you can exist and make money. If you lose 5 or 10 percent you are liable to go out of business. The theory of putting this figure of 6 million in was to show that 6 million people at some point or another were with companies which did some exporting so that if you got into the question of whether you would have to bring relief to them or something of that character you might actually lose a company if it lost 10 or 20 percent of its business. We want to show what that was. The figure of 3 million is nearer those who are actually giving their time to exports, but this has a place in the total deliberations if you consider your trade adjustment program later on.

Senator SPARKMAN. Certainly we are going to have to do something in the face of the Common Market, aren't we?

Secretary HODGES. We are or we will be left way behind.

Senator SPARKMAN. Isn't there also a South American trade alliance of some kind?

Secretary HODGES. Yes, sir.

Senator SPARKMAN. Mr. Secretary, I want to commend you and the people of your Department for the vigorous campaign that you have put on in stimulating the sale of American goods abroad. I think the trade missions and all those programs that you are engaged in must have a good result, and I think they have had.

I am delighted that you can come before us today and give this optimistic report. I have no questions, Mr. Chairman.

Chairman PATMAN. Mr. Reuss?

Representative REUSS. Mr. Chairman, I want to join with Senator Sparkman in congratulating the Secretary on the aggressive job he has done already to bring our payments more closely into balance.

However, your generally optimistic tone is tempered, I think, with some pessimism, which is also justified insofar as it can lead to a better result on our part. I would like to explore that with you.

Let us start with your quotation from the President's economic message, reproduced in your report, in which you give his target for bringing our payments into reasonable balance within 2 years. Let us explore just how we are going to do that. I start by affirming my confidence in what you have done and my congratulations for doing as much as you have so far. Would you not agree with the following: The hard core intractable basic part of our balance-of-payments deficit seems to be, judging by the last 3 or 4 years, on the order of $2 to $3 billion a year, that is leaving to one side short-term capital movements, but having particular regard to the net balance if you take into account trade, military expenditures abroad, foreign investment, and foreign aid.

Mr. HODGES. I would.

Representative REUSS. Would it not be a most excellent thing for the realization of this goal of striking a reasonable balance within 2 years if our friends and allies in Western Europe, and particularly the countries of the Common Market, would say something like the following: "In 1947 when there was a dollar gap, we European countries sat down together at Paris for as long as was necessary, and we parceled out the task of bridging the dollar gap and of seeing that the U.S. persistent surplus in payments was rectified." Now, in 1962, the shoe is on the other foot, so the countries of the Common Market plus several others are again going to sit down together and to work out a program whereby the rather persistent $2 to $3 billion U.S. payments deficit on the one hand and the equally persistent Western European $2 to $3 billion payment surplus on the other hand may be brought into balance, first, by greater sharing of the burden of military expenditures by these countries; second, by greater sharing of aid for the underdeveloped regions of the world; and, third, by unreciprocal lowering of tariff barriers and import quotas now preventing the United States from increasing exports to the European area. Would not such a determination on the part of our friends and allies, to sit down and to remain together until a program for bringing that $2 to $3 billion gap were evolved, be a good thing from the standpoint of the United States and from the standpoint of the free world?

Mr. HODGES. Very definitely, Mr. Reuss. You have stated it better than I can. I tried in my own way last summer on two trips to Europe to say just that to them, to the Government and to industry and other groups. I think that is absolutely essential. I happen to have been a part of this program in 1949–51 when we were carrying out the Marshall plan objective. I believe there is an increasing tendency on the part of those countries, even though they are a little tougher traders than we are, and a little more realistic and quite a bit more selfish, I think there is a tendency now to come around a bit. I think they will be buying more military items from us. I think they will be sharing more in the aid. I know they are. I know that France is doing more than the public thinks in some places.

Representative REUSS. In terms of the arithmetic it is a fact, is it not, that they have not attained anything like the resolution I have described to come up with a program which will in fact bridge the gap?

Mr. HODGES. I think that is true, sir.

Representative REUSS. Would you not agree that unless they do so, further efforts by this country by itself, however aggressive and vigorous, are not likely to be able to succeed singlehandedly?

Mr. HODGES. I expect that statement would be true. I would not make it as discouraging as you do. I think that we can do one thing if they don't come to the extent that you and I think they ought to. We have had in the last year or so about a $5 billion surplus trade balance. We ought to be able even to increase that even if we have to keep up our present military and aid commitments because the aid commitments are to other parts of the world rather than Europe now. I think we can add another $1 to $2 billion on our trade surplus, and I think we can pick up several hundred million within 5 years, up to a half billion dollars on our travel.

Representative REUSS. I am with you all the way on that, but isn't it going to be quite difficult to improve the trade surplus in view precisely of the discriminatory external tariff of the Common Market which you have pointed out on page 20 of your report in your example on bookbinding machinery, an example which can be multiplied a hundred times over?

Mr. HODGES. Yes, you are absolutely right on that. We have to be more realistic and we have to see that they come through with that. I hope that the Congress and the administration insists that the nation with whom we make any kind of trade or bargain do away with these many things they have, which make imports to their country more restricted.

Representative REUSS. Now, I share your great belief in and enthusiasm for the President's Trade Expansion Act, I hope that the Congress will validate it. It is a fact, however, is it not, that by and large concessions under the Trade Expansion Act will tend to be reciprocal, thus involving a partial offset at least in terms of expanded imports?

Mr. HODGES. That is right.

Representative REUSS. And that action by Europe and the Common Market in particular on a unilateral, unreciprocal basis at this time of our balance-of-payments difficulties would be enormously helpful to the progress of the free world.

Mr. HODGES. It would, yes, sir.

Representative REUSS. I have one final question. Would it not perhaps be helpful to you of the executive branch in presenting this point of view to our Europen friends and allies if you had some expression of support for that position from the Congress, perhaps in a sentence by this committee in its annual report?

Mr. HODGES. I think it would.

Representative REUSS. I have no further questions.

Chairman PATMAN. Senator Proxmire.

Senator PROXMIRE. In your statement, Mr. Secretary, you say the profit picture is particularly encouraging. You point out that the profits are nearly 20 percent above the low at the trough of the recent downturn. You say that they may be expected to go over $50 billion, you interpolated that in your statement.

Mr. HODGES. Yes, sir.

Senator PROXMIRE. It has been my impression that the profits have been extraordinarily low really over the past few years in comparison for example with the sharp rise in gross national product.

Mr. HODGES. I agree.

Senator PROXMIRE. If you compare profits with gross national product and wages, they are low. Isn't this an important factor in what you talk about in terms of deficiency in investment?

Mr. HODGES. I agree thoroughly.

Senator PROXMIRE. Therefore, while this profit picture is encouraging you would not give the impression that we can be satisfied that it is adequate.

Mr. HODGES. Not at all. I am simply giving it comparatively. I did not try to defend it. I would have said, as you have indicated, that if you go back a decade or more our profit rises percentagewise have been very little as compared to our gross product or our other things that we use as indexes. We have been right around or under 10 percent of our gross national product.

Senator PROXMIRE. It seems to me the figures I have seen compared historically with our American experience and currently with profits abroad, we are way below.

Mr. HODGES. I would think that. That has been true for many years.

Senator PROXMIRE. Now, you discussed the 8-percent tax credit. It seems to me that this could be primarily a cut in the price of equipment and machinery that is purchased. I can't see any other substantial effect to it and it would seem to me that in doing this you would do two things: No. 1, you would encourage plants to increase their capacity. And you may encourage capacity in excess of what a plant would have anyway. It may be excessive capacity and you may be simply borrowing employment from the future. No. 2, you may encourage modernization. But to the extent that you improve automation at an artificially increased rate, isn't it true that you may displace workers in a discouraging way?

Mr. HODGES. That is right. Of course, if you take that position it gets awfully discouraging and I am not discouraged.

Senator PROXMIRE. The reason I ask that is because I understand the business community is not enthusiastic about this and labor does not like it at all.

Mr. HODGES. I believe you will find, sir, when you are as close to it as I am the sentiment on that from the business point of view has changed substantially in the last few months. I think you will find more and more the business community will support this 8 percent. You had a sliding scale, little complications last year, that were introduced. It is much easier now and I find that the machine tool manufacturers are supporting it. I have not seen labor statements recently, but I would be surprised if they fought it.

Senator PROXMIRE. What about argument this would primarily have the effect of increasing capacity or too rapidly displacing workers?

Mr. HODGES. I will be glad to comment on that. Certainly anything you do in the way of expenditure of so many hundred million or billion dollars will increase your capacity. It has to be selective. You have to do it in places where you see a growth situation. You might take in the present steel industry you have got some plants that would run 100 percent two or three shifts, and you have some other plants that might be obsolete and run half the time. When you are talking about this obsolete part or extra capacity, you have to have the newer one in order to compete with the people abroad as well as to keep your prices down here.

Senator PROXMIRE. How does this compare with the systems of depreciation abroad? Are they similar to this in any case?

Mr. HODGES. Yes. Mr. Dillon has said from the Treasury point of view that if and when he brings out this, this spring I hope, his complete program for accelerated depreciation that we would be competitive with most of the major European industrial nations.

Senator PROXMIRE. Competitive in terms of what?

Mr. HODGES. Of the way they handle depreciation.

Senator PROXMIRE. This does not indicate necessarily that they have the same system.

Mr. HODGES. No, not necessarily the same system. They may have and they probably do have more of a choice on the part of the manufacturers. I have heard that they let the manufacturer charge it off in 1 year or 5 years, taking his chance on it, and they get it back by taxing more quickly. Basically they have a more accelerated depreciation than our fixed arbitrary rights that we have had in this country so long.

Senator PROXMIRE. Is it your estimate as a former distinguished and successful businessman before you were Secretary of Commerce that this is a serious disadvantage to us in our competition with countries abroad?

Mr. HODGES. I am sure it is very serious. I will say this: I am ashamed to say it as an American, but our industrial machinery on the whole is outmoded compared with some of the countries we are competing with.

Senator PROXMIRE. You also say residential construction has shown sizable gains in the past year although it is below the peak in 1959. You say you expect some moderate expansion of residential construction. I notice in the table on page 251 of the Economic Report of the President there is a compilation of housing starts since 1929. In the past 12 years or so housing starts have been fairly static. In 1950 there were 1,396,000 housing starts. Last year it was less than that. In fact, it has never been that high since. In view of the increase in population, since 1950, the vast increase in income, I am somewhat concerned that we have not moved along more rapidly in this area. It seems to me one reason, the reason that was suggested by one of the eminent economists who testified this morning, is our monetary policies, our interest rates have increased. They are substantially higher than in 1950. Interest is a very big element in the cost of building a home. It is also something which is pretty much within the control of Government. Don't you feel that a case can be made that we can stimulate construction substantially by a monetary policy that would encourage lower interest rates?

Mr. HODGES. Well, that is somewhat out of my field, Senator Proxmire. I would certainly say that lower interest rates would stimulate it depending on what the Government wants to do in its quarantee. Of course, you have the other side of it. You can't keep your interest rate too low or you will have a great outflow of short- and long-term capital to other countries where interest rates are higher.

Senator PROXMIRE. We have argued, of course, that what they should do is keep short-term interest rates high and long-term rates low, since capital outflow is perforce largely in short terms, where home construction is exclusively influenced by the level of long-term rates.

You talk about the proposal that the individual income tax rates may be temporarily reduced to fight recessions. Now it seem to me that both in this proposal and perhaps also in the depreciation tax credit proposal as well as in the capital improvements proposal, Government spending and public works, that all these may tend to borrow from the future, borrow employment from the future. You cite the tragic loss we have with the people out of work, and I could not agree with you more. It seems to me if we are going to rely on this proposal at a time when we have heavy unemployment even in prosperous and expanding periods all we are going to do is somewhat level off the troughs and peaks but still remain well below the level we should have. This is not the kind of thing I can see moving our economy ahead on a long-term basis as I feel we should.

Secretary HODGES. I think it is primarily an emergency measure, Senator. I don't think it has the element of a long-term constructive point of view. I think it is an essential thing to save us from having further recessions but catch it before it goes too far.

Senator PROXMIRE. If we had had that back in 1958–59 when we had a recession, we had a terrific Government deficit of $12½ billion, this would have dug us a deeper one, $5 billion deeper for the income tax cut alone, perhaps somewhat less. We would have been borrowing from present employment.

Secretary HODGES. That might be true, sir, but I think your question of stimulating people to spend this money that they are going to save from not having to pay their taxes might have stimulated the recovery more quickly.

Senator PROXMIRE. Perhaps it would, but we would have also had the very real fact of reducing our revenues at the time when it worked out that we had a $12½ billion deficit.

Secretary HODGES. That is right.

Senator PROXMIRE. Now on that same page you refer to the 4 percent unemployment figure as being tolerable.

Secretary HODGES. Yes, sir.

Senator PROXMIRE. I want to make sure that is not misunderstood. Mr. Goldberg was extremely emphatic. He said the administration is not satisfied with 4 percent. It wants to go lower. I just hope that that word "tolerable" is not construed by the press or anyone as a difference of opinion within the administration.

Secretary HODGES. I did have the word in my prepared statement but it is expressly qualified. The phrase I used was, "tolerable, if not desirable." I guess the adjective is not too good. What we are trying to say is we must take this a step at a time. If we can reach the 4 percent on unemployment, say, in a year and a half, we would have reached what is known as a target because that will get us on a level from which we can move forward to a lower percentage. Then you have to have the real growth if you get it below that. I meant "tolerable" in the sense of being able to live with it because that is the way we are planning our budget and so forth on that basis. I still think it is too high. But, of course, 4 percent is much to be preferred over our present 6 percent of unemployed.

Senator PROXMIRE. You feel that we can reduce it substantially below that without having inflation?

Secretary HODGE. I do but I do not think you can do it quickly.

Senator PROXMIRE. Now you talk about the guarantee of loans.

Secretary HODGES. Yes, sir.

Senator PROXMIRE. This I realize is going to be in a special area but still don't you take the heart and soul out of the risk in the free enterprise system if the Government is going to go in and guarantee loans? Even if you insure loans only in some limited areas, aren't you constrained to do it in other areas and pretty soon we find that the element of judgment and responsibility that is so important in the free enterprise system and so well diversified by free enterprise just disappears?

Secretary HODGES. You will notice it is simply a study. The reason we are doing that, the reason we are thinking along those lines, Senator Proxmire, is that I feel so strongly and our Department feels so strongly that you must have accelerated investment of a capital nature. If it takes a long-term loan to industries to get that, then almost anything, including the 8 percent, would be helpful to get it because that is the only way you will create jobs. That is the only way you will ever get away from the 4 percent.

Senator PROXMIRE. It is a beautiful system so far as everybody is concerned, but everybody is moving into a dangerous future if they do it. The banker is making a loan at higher rates, but it is Government guaranteed and, therefore, it is equivalent to a Government security. He does not have to worry about the risk so much because if it does not work out the Government is going to take care of him.

Secretary HODGES. We also had a little industrial development association in my State some 3 or 4 years ago that raised several million dollars just from selling stock. The only way you could borrow from that corporation was if the bank turned you down twice. That was the easiest thing they had. The banks would turn it down. You would not have your houses built if you did not have a guarantee on the part of the Government.

There is a new thing, which I have not discussed in here, taking effect in a couple of weeks. For the first time in history the U.S. is going to have an insurance program for guaranteeing political risks on exports abroad. Industrial competitors abroad, Europe particularly, have been doing this for years. It looks a little silly, a little socialistic, but it is good business.

Senator PROXMIRE. Political risks, I can understand.

Secretary HODGES. You are going to do it because of some of these places if you are going to urge more of the people to export.

Senator PROXMIRE. Political risks I understand, that is the only way that it can be done. This other guarantee to me is quite different.

Secretary HODGES. Yes. We may not come out with it. We are just studying it.

Chairman PATMAN. Senator Pell.

Senator PELL. Governor, in connection with Senator Proxmire's query concerning the relative advantage of the proposed depreciation and tax credit system for new machinery can you put in the record a table of how we currently compare with the various Western industrial nations?

Secretary HODGES. Comparative depreciation approach?

Senator PELL. That is right. Are we on an even base with Western industrial nations or are we still behind?

Secretary HODGES. I think it is a good request because sometimes you are taking these things generally and you don't know your facts.

Senator PELL. My recollection is that we still are relatively behind West Germany in this respect.

Secretary HODGES. I was quoting Secretary Dillon on the one thing. I was quoting one nation, where they allowed them to do it very quickly.

(The following was later received for the record:)

Comparison of depreciation deductions, initial and incentive allowances[1] for industrial equipment in leading industrial countries with similar deductions and allowances in the United States under actual and various proposed plans

	Representative tax lives (years)	Depreciation deductions, initial and incentive allowances (percentage of cost of asset)		
		1st year	1st 2 years	1st 5 years
Belgium	8	22.5	45.0	92.5
Canada	10	30.0	44.0	71.4
France	10	25.0	43.8	76.3
West Germany	10	20.0	36.0	67.2
Italy	10	25.0	50.0	100.0
Japan	16	43.4	51.0	68.2
Netherlands	10	26.2	49.6	85.6
Sweden	5	30.0	51.0	100.0
United Kingdom	27	39.0	46.3	64.0
United States:				
Without investment credit and lives equal to current Bulletin F weighted average of 19 years		10.5	19.9	42.7
With lives of—				
15 years		13.3	24.9	51.1
14 years		14.3	26.5	53.7
13 years		15.4	28.4	56.6
12 years		16.7	30.6	59.8
11 years		18.2	33.1	63.0
10 years		20.0	36.0	67.2
With investment credit and lives equal to current Bulletin F weighted average of 19 years[2]		26.5	35.9	58.7
With lives of—				
15 years		29.3	40.9	67.1
14 years		30.3	42.5	69.7
13 years		31.4	44.4	72.6
12 years		32.7	46.6	75.8
11 years		34.2	49.1	79.0
10 years		36.0	52.0	83.2

[1] The deductions and allowances for each of the foreign countries have been computed on the basis that the investment qualifies fully for any special allowances or deductions permitted. The deductions in the United States have been determined under the double declining balance depreciation method, without regard to the limited 1st-year allowances for small business.

[2] For purposes of this table, the proposed 8-percent investment credit has been considered as equivalent to a 16-percent investment allowance. For corporations subject only to the 30-percent normal tax it is equivalent to an incentive allowance of 27 percent. The initial allowance of 20 percent of each year's investment, up to $10,000, is not taken into account because of its relatively small impact.

Source: Treasury Department, Office of Tax Analysis.

Senator PELL. I have one further question in line with Chairman Patman's thought. Does Mr. Batt have any advice as to how we in the States can work with ARA headquarters to speed the processing of applications for ARA assistance, because, recalling the campaign last year, we ran on the theme that this was the panacea for many of our troubles. Conditions have improved but the ARA has not played a substantial role in the recovery when it has occurred. How can the ARA get more involved?

Mr. BATT. Senator, the ARA of course is aiming at the long-term chronic unemployment and not the recovery that has come with the recovery from the cyclical recession. The kinds of projects which we are able to get underway fastest have been the training projects because this has been 100 percent Federal money. One is going, as you know, in Providence for 178 workers and 1 in Pomfret, Conn., 200 workers, and another 1 in Danielson, 1 in Windham County, Conn.; we have 20 projects in training. They were able to be organized in relatively short order. Some have exciting progress there. Secretary Goldberg has talked about them. The greatest activity is in terms of the loans under sections 6, 7, and 8 of the act. This, of course, is not all Government money, this is a very small piece of the Government seed money. The rest of the capital has to be dug up. You also put, and I think very wisely, in the legislation, the provision that we were not just doling out money. We had to originally require that the community organizations organize themselves. In some areas of the country like your State and Senator Bush's State, they were well organized. In other areas of the country they were not organized at all like southern Indiana and eastern Kentucky. These organizations had to be built from nothing and they had to come in with an overall economic development plan.

Senator Pell. To my mind, in my own State the impact of ARA is still disappointing in my mind. I am asking how can we in the State help you make ARA work more effectively.

Mr. Batt. Help your people develop proposals under sections 6, 7 and 8, actual business loans under the act. I think the first bottleneck was the overall development plans. That bottleneck is by way of being broken, in many cases with help from individual Members of Congress. The overall development plans have come in from over 400 areas of the country. We have taken a map of the country. The areas which are in red are eligible for help and the areas which have blue outlines are the ones which have come in with overall development planning. You will notice that Rhode Island is well represented here. Almost every section of the country. There has been an avalanche of local planning which might be of interest to this economic committee such as has never been seen in the country before. If we had them here they would reach to the ceiling.

Senator Pell. Do you feel disappointed in the responsiveness of the States?

Mr. Batt. Some of the States have not come forward as fast as others with their local organizations and with their overall development plans. One State just this week is getting in its first overall governmental plan. As Congress wrote the legislation, they have to precede the approval of any loans.

Senator Pell. To be very specific, I think my own State came forward very early with their plan. It was well organized, as you pointed out. Why is there still such a lag of actual help coming in?

Mr. Batt. I don't know what the status is on actual projects. The projects, of course, have to originate with the community development corps, itself. We will be happy to run down any particular projects. We have about 11 projects which have already gone through the machinery and been approved, worth about $3 million. We have about 103 more projects worth $80 million in the pipeline being developed by local development corporations or being reviewed by ARA or its cooperating agencies.

Senator Pell. This is for the United States as a whole?

Mr. BATT. This is the United States as a whole. To check your State specifically, I will be happy to check on any specific projects. Again the Congress made perfectly clear that the initiative had to come from the community itself.

Senator PELL. Basically, as of now, almost a year after the bill has passed, only $3 million worth of projects have been approved?

Mr. BATT. Let me amend that, sir. Just over 4 months after the money was provided by Congress $3 million dollars has been dispensed.

Senator PELL. I stand corrected.

Mr. BATT. And it is moving at an increasing speed.

Senator PELL. One final query, Mr. Secretary. In connection with the travel service, I was wondering if you would enlarge on that a little bit. You mentioned you have your representatives abroad. How many representatives are there?

Secretary HODGES. Here is what we have. With the appropriations by Congress we have increased very moderately in our organization. We had 12 American positions to be filled, of which 10 are filled. Incidentally, this particular travel service has turned out to have the greatest sex appeal in the Department of Commerce. We had 2,000 applicants for the 37 jobs. It has been a problem of getting organized in the last 6 months, but we now have contracts let with three or four of the leading advertising and public relations firms of the world for certain parts of it. We have on the printing press now all the promotional data of a general institutional nature, "Visit U.S.A., an exciting place to go," that is in seven languages. We have these people out in the seven parts of the world now drumming up general trade for visiting the United States. After about 30 days—about 30 days after you passed the bill and it came to our shop I had a visit from a Swiss executive who said this was a great thing, and if we can do this on a package base and you will help us, get some of your transportation group lined up, Swiss group, he said, "We will send you a thousand people from Switzerland before the year is out."

Senator PELL. Do you have representatives abroad for this travel service?

Secretary HODGES. Yes, in London, Paris, Frankfurt, Tokyo, São Paulo, Mexico City, and Sidney, already.

Senator PELL. As attachés to the embassies?

Secretary HODGES. No; we have a separate travel office. I have looked at three of them myself, in Tokyo, London, and Paris. We go into the travel center where the travel industries are located and take as good a place as we can afford to get and establish with a small staff of three to six people and start displaying and talking and working primarily with booking agents.

Senator PELL. Their job is to promote travel, the job of the consul usually is to discourage travel. How do you get their cooperation?

Secretary HODGES. I think that is somewhat of an old theory. I would agree with you a year or so ago but you can get a visa now within 5 to 30 minutes in most any place. We don't ask the women what their age is for coming to America.

Chairman PATMAN. Senator Bush.

Senator BUSH. Just two small matters. In the first place, I was interested in what Congressman Reuss said to you because I agree very much with him that this business of exploring a broader area of cooperation than is in this trade bill is very desirable and these countries, allies, free countries, that have substantial reserves, international currencies, dollar reserves, and so forth, should be more willing to carry a larger share of the burden that we are carrying as free countries. Senator Fulbright said in his article last October 1 in Foreign Affairs, in effect, that despite our abundant resources we are trying to carry too large a share of the world burden. Now, as to what Congressman Reuss said, that thought is extended substantially in a paper which Congressman Curtis and myself prepared as an addenda to the Boggs committee report on the trade program, and the State Department sent for 20 copies of our statement. They sent for 10 and then 10 more, showing their interest in it. Now, I would like very much to make some copies of that available to the people in your Department who are studying and working on this trade bill.

Secretary HODGES. We will be very happy to have that.

Senator BUSH. May I send you 20 copies and you may see that they get on top of appropriate desks?

Secretary HODGES. I certainly will.

Senator BUSH. What we tried to do in that paper was to deal with some of the problems that are closely related to this whole question of the Trade Agreements Act. I have been a supporter of the Trade Agreements Act as it has come up from year to year and I am just anxious—just as anxious to improve our trade as anybody else. Still I think that there is a question here whether we are ready to go quite as far and as fast as the proposal the President has sent down. I would like your people to study some of the reservations that we submitted in good faith on that very important matter.

Secretary HODGES. All right, sir.

Senator BUSH. In the trade bill there is a provision which says in effect that where we and the Common Market countries control some 80 percent of the world trade in any given category, that tariff barriers may be eliminated entirely. The President is given the authority to go all the way?

Secretary HODGES. That is right.

Senator BUSH. This raises a question in my mind as to whether this would give the President authority to trade off concessions by ourselves on industrial goods in order to secure more concessions for agriculture—for agricultural goods into that area. Have you any thoughts about that? Has that matter been discussed in connection with the trade bill? Is it contemplated that the authority under that 80-percent clause might be used that way?

Secretary HODGES. I have not heard it so discussed, Senator Bush, that you would put one against the other. It would be my understanding that under this so-called dominant supply, the 80-percent matter, that the machinery and so forth would stand on its own feet as compared to their machine. Of course, we do have a very lasting problem of getting our agricultural products into Europe because they are becoming surplus areas also, but it is not the intention of pitting one against the other.

Senator BUSH. Would it be asking too much for an opinion on that from your office as to whether that authority might be used that way?

Secretary HODGES. I will be very glad to find out if anybody knows because there is nothing specific about what the President is going to do. It takes about a 5-year period before he can reduce these items.

Senator BUSH. What would be helpful would be an opinion from your own counsel or one who works on that trade bill, as to whether the authority is so broad that it would permit that type of tradeoff, you see, where we would concede on manufactured goods in order to gain concessions on agricultural products?

Secretary HODGES. We will be glad to submit that.

Senator BUSH. I don't want an opinion whether it is desired or not, only whether the authority is in the bill.

Secretary HODGES. We will be glad to get that, Senator Bush.

Senator BUSH. Thank you very much.

(The following was later received for the record:)

GENERAL COUNSEL OF THE DEPARTMENT OF COMMERCE,
Washington, D.C., February 15, 1962.

Hon. PRESCOTT BUSH,
U.S. Senate, Washington, D.C.

DEAR SENATOR BUSH: This will supplement Secretary Hodges' letter of February 8 acknowledging your letter of February 2 requesting our views regarding the scope of certain authority under the proposed Trade Expansion Act of 1962 and the submission of certain information regarding exports and imports.

Enclosed is copy of my opinion to the Secretary of Commerce, dated February 14, 1962, dealing with section 211(a) of the proposed Trade Expansion Act of 1962 (H.R. 9900), copy of which has also been transmitted to the clerk of the Joint Economic Committee for inclusion in the record.

We will submit the additional material you requested regarding exports and imports as soon as it has been prepared.

Sincerely yours,

ROBERT E. GILES.

U.S. DEPARTMENT OF COMMERCE,
OFFICE OF THE SECRETARY,
February 14, 1962.

U.S. Government memorandum.
To: The Secretary.
From: Robert E. Giles, General Counsel.
Subject: H.R. 9900, Trade Expansion Act of 1962.

This is in response to your request for an opinion as to whether under section 211(a) of the administration's trade expansion bill the President would have the legal authority to grant concessions on imports of industrial goods in return for concessions by the Community on agricultural goods exported from the United States to the Community.

In my opinion, under section 211(a) the President would have such authority; he would not be restricted to exchanging concessions on imports of industrial goods into the United States for concessions on exports from the United States of the same or similar industrial goods. By the same token, the President would have legal authority to grant concessions on imports of agricultural goods in exchange for concessions on exports of U.S. industrial goods. I would point out that the proposed trade expansion bill is in this respect no different from the trade agreements legislation which has been enacted since 1934.

Subsection (a) of section 211 (basic authority) provides: "If the President determines that the United States and the European Economic Community together account for 80 percent or more of the aggregated world export value of all the articles within any category, he may, in carrying out any trade agreement with the European Economic Community under this title, issue proclamations as to articles within such category without regard to the limitation expressed in section 201(b) of this Act."

As presently worded, therefore, subsection (a) only refers to articles within certain categories in respect to which the President would be authorized to proclaim changes in U.S. customs treatment of imports, without being held to the maximum 50-percent reduction limitation set out in section 201(b). Subsection (a) does not, by its terms, refer to or limit the kinds of U.S. export articles in respect to which the President would negotiate and obtain concessions, in exercising authority under section 211. Nor is there any other provision of H.R. 9900 which would require a different conclusion.

This opinion, of course, is strictly limited to the legal aspects involved and is not to be taken as indicating any expression of policy as to the desirability of negotiations of one kind rather than another.

Chairman PATMAN. Any other questions?

Senator PROXMIRE. Yes, I would like to ask Secretary Hodges and also Mr. Batt.

Mr. Batt, you said something about an avalanche of economic planning. That is very interesting. I think it would be very helpful to have some indication of what the economic planning really means in terms of our economy. I think it is most heartening to know, particularly for the areas that are more depressed in our country and have need for knowing where they are going and where their resources are, what resources they can get, and so forth, for doing this. This is a great contribution even if the ARA does nothing else at all.

Secretary HODGES. If they did not even spend a dollar it would be good.

Senator PROXMIRE. It would be fine to have some indication from you, perhaps. I would not expect a study of any length but just some summary in your judgment.

Mr. BATT. We will be very happy to do so. There have been 400 of these areas come in with overall economic development plans. Three hundred have been approved. To accelerate this, we have given preliminary approval, so that the requirements of the act would be met. Then we require them at the end of the year to come in with a more intensive plan. While these are often not sophisticated economic analyses, they do show an acute awareness of their problem. They are not dominated by the "rose colored glasses" approach.

(The following was later received for the record:)

SUPPLEMENTARY STATEMENT OF DEPARTMENT OF COMMERCE TO TESTIMONY ON FEBRUARY 2, 1962, BEFORE JOINT ECONOMIC COMMITTEE

SUMMARY OF LOCAL PLANNING UNDER THE AREA REDEVELOPMENT ACT

The progress of the program to help local areas suffering from excessive unemployment cannot be measured only in terms of the number and amount of loans and grants that are made.

The real strength and opportunity of the area redevelopment legislation lies in the important task it lays out for the local community. The loans and grants act as "seed" money and give an incentive for local people to start thinking about their economic problems, to frame a program of local action, and to organize to carry out this program.

Congress recognized that a recovery program would be meaningless if the local community did not have a voice in area plans and the law and the committee reports are quite specific on how this local expression was to be made a part of the loan and grant procedure. Before a community can qualify for assistance, it must submit for approval by the Secretary of Commerce a carefully thought-out statement of how it intends to proceed on its own overall redevelopment plan.

ARA has provided general instructions for the preparation of these overall plans by local communities, including an outline of the general requirements for setting up a local development organization. The instructions include suggestions for analysis of local business conditions and the natural and human resources upon which a development effort can be built. The instructions also suggest that the community outline as frankly as possible the nature and causes leading to the local economic difficulties. Finally, the local group is asked to put down in sequence the actual steps it will take to modify local conditions, to develop local resources, and to take advantage of the numerous sources of help that are available from the State and Federal Governments. The local group is urged to adopt a local program that is within its own reach and capability.

When the program statement is completed it is sent to the State development agency for endorsement, modification, or suggestions. The State agency forwards the program to the Area Redevelopment Administration where it is checked for internal consistency and conformance with prior instructions. In most cases a preliminary approval is given so that the community can immediately start its redevelopment plan and can begin to share in the loans and grant provisions of the program.

In extending this approval the Secretary, through the Administrator, usually points out additional steps that the community could take or sources of help that possibly are not known to the local group. Very often the community is urged to cooperate with other nearby communities for a joint solution on a common problem. Finally, the community is usually asked to make a more thorough analysis of its problems, taking into account some rather extensive comments proposed by the professional staff of ARA, which is made up of specialists who offer suggestions based on their experience with economic programs in many communities across the country.

Always the community is encouraged in its attempts to find a reasonable solution. This kind of approach is especially important in those cases where the local organizations are inexperienced and are struggling for the first time with their own economic futures on an organized basis. The significance of providing a means of expressing local plans and ambitions is reflected in the viewpoint of the mayor of a western city who recently said: "Even if the Area Redevelopment Administration does not make a single loan or grant, it will have proven worthwhile because of the incentive and stimulation it has given to organized economic planning and programing at local and regional levels."

To date the Area Redevelopment Administration has designated 829 areas and 47 Indian reservations as eligible to participate in the program. Some 33 million people live in these areas. Preliminary overall economic development programs have been received from 420 local areas and we have approved preliminary programs covering 328 areas.

These plans are given reality and vigor through the system of followups and implementation that the Area Redevelopment Administration has instituted. Headquarters staff examines them for potential industrial and commercial loan projects and in situations where a Federal program can be helpful, the particular agency which is in a position to extend assistance is notified. In other instances, where a marketing study or research into a community resource is warranted, technical assistance funds are made available to break the bottlenecks to economic progress. In this way, local programs are given life and meaning.

Senator Proxmire. I know in the northern part of my State, northwestern and northeastern Wisconsin, there has been talk for generations about doing something. At long last they are getting realistic ideas of what they can do. It is very, very helpful, a real contribution.

I might as well discuss these two things together. There is a discussion of the multiplier effect. You cited Carbondale, Ill., where you say a $455,000 Federal loan induced an additional $1.3 million in local and public and private investment and a large number of jobs. Then you go on in the appendix to say that ARA has reserved nearly $30 million for 37 projects, some 17,000 permanent jobs are available. You break it down further and point out, for example, that in Gassville, Ark., with a total of 160,000 roughly of Federal money you get a thousand jobs. That is a job to $160 of loans. It is phenomenal you can get this number of jobs. How firm is this?

Mr. Batt. That is perfectly firm. The relevance there is that we built a waterplant. The plant was built by local people, local capital.

Senator Proxmire. You are not talking about the number of people required to build it?

Mr. Batt. No. Congress made that very clear in the legislation. We are only talking about permanent jobs.

The multiplier effect is fascinating. We had a study made on that first loan we made in southern Illinois of what the multiplier is. We tried to reflect that in the second statement.

Senator PROXMIRE. I would like to see it. I thought the most effective criticism of this bill was that it was peanuts, $395 million was a lot of money. But it could not make any real impact on a $500-billion economy. If this multiplier effect can be substantiated and documented it is mighty persuasive.

Mr. BATT. I think we can do it, not only in what additional jobs we created but also in terms of the savings effected in unemployment and insurance and public assistance, which are very substantial, also.

Senator PROXMIRE. You say you have done that?

Mr. BATT. That was a special study. We shall be happy to furnish that.

(The following was later received for the record:)

ECONOMIC IMPACT OF LOANS IN REDEVELOPMENT AREAS: CASE STUDY OF CARBONDALE, ILL.

By Dr. Robert L. Wrigley, Jr., Office of Planning and Research, Area Redevelopment Administration

As you requested, I have assembled for Mr. Bozman's office some data showing the possible economic implications of ARA's recent $500,000 loan to the Carbondale Industrial Development Corp. of Carbondale, Jackson County, Ill. This loan plus substantial local assistance—financial and otherwise—will enable the Technical Tape Corp. of New Rochelle, N.Y., to open a $1,825,000 plant employing within 3 years about 1,000 persons.

Here is an introductory thought. Workers living within and near the coal mining district of southern Illinois have had to become very mobile in their search for jobs, hence it is quite likely that many of the new jobs in Carbondale will be filled by persons living outside Jackson County. It is also probable that many of the new jobs will be filled by persons not on the unemployed list. These are not significant matters since the new jobs need not necessarily be filled by citizens of Jackson, County; moreover, an employed person taking one of the new jobs will, in most instances, vacate a job that someone else can fill. On the other hand, for purposes of calculation, it is much easier to use Jackson County as a base rather than a broader area. Accordingly, data for Jackson County has been used whenever available.

NEW EMPLOYMENT AND PAYROLLS

In a recent telephone conversation with Mr. Paul D. Cohen, president of Technical Tape Corp., I received this information on employment and payroll for the firm's Carbondale installation.

Number of workers	Average weekly pay	Average yearly pay	Length of work period (weeks)	Total yearly pay
600	$70	$3,640	52	$2,184,000
100	140	7,280	52	728,000
300	70	1,120	16	336,000

The 100 workers receiving the highest pay include company officers, other office staff, supervisors, and maintenance force. Since the product of this firm is used very extensively in packaging during the months prior to Christmas, a force of about 300 temporary workers will be engaged during the months, August through November.

Of the 700 permanent jobs, only about 40 will be filled by persons brought in from outside the territory. Virtually all of the 300 temporary jobs will be filled locally.

What additional employment will this new Carbondale operation bring into that locality? In analyzing the impact of new industry on an area, the U.S. Chamber of Commerce has stated that one new industrial job will create around 1.7 additional jobs. Other authorities have used a ratio of 1:1. Both of these figures appear to be too high for an expansion of the type now underway at Carbondale. In other words, the existing commercial facilities and services in that community are not fully utilized. Then, too, a sizable increase in population is not anticipated. There will be, however, some expansion in secondary employment. Moreover, existing commercial and service activities that are barely able to make ends meet will profit from the new payroll which in the aggregate will be substantially more than the unemployment and welfare payments that now take the place of the payroll.

A ratio of 1:0.4 has been used in this analysis. This is a conservative relationship. In developing this formula, I am using a rounded-out full employment for Technical Tape Corp. of 700 workers. Thus, the additional jobs that Technical Tape might bring to, or create in the area, would total about 280. Some new employment might be attributed to the $336,000 payroll of part-time workers at Technical Tape but no new employment has been claimed in this case.

According to President Cohen of Technical Tape, there is other expansion already planned for Carbondale. Two firms that supply his plant—the Dilly Manufacturing Co. of Fanwood, N.J., and Mastro Plastic Co. of the Bronx, N.Y.—will be opening facilities either in Carbondale or at nearby Crab Orchard Lake. As a rough estimate, these firms will employ together about 75 persons receiving about $70 a week or a total yearly payroll of $273,000. The remaining workers totaling 205 (280–75) would be engaged primarily in retailing, wholesaling, and service activities and, according to the U.S. Labor Department, the average wage for such a diversified group is about $75 weekly. The 205 workers thus would receive a total of $799,500 in wages yearly.

The total job and income picture, therefore, is estimated as follows:

Number of workers	Average weekly pay	Total weeks employed yearly	Total payroll
675	$70	52	$2,457,000
100	140	52	728,000
205	75	52	799,500
300	70	16	336,000
Total			4,320,500

DIRECT COST OF UNEMPLOYMENT

Financial support for the unemployed is a very expensive matter. An eight-county area in southern Illinois, including Jackson County, received benefit payments from the Illinois State unemployment insurance fund totaling $20,278,060 during the 5 years, 1955–59.[1] Payments in Jackson County during this same period came to $2,747,605. For so small an area, this is a heavy drain on the insurance fund which is built up year by year through a payroll tax on all Illinois industries.

Welfare payments are another important factor in the cost picture. Not all welfare payments, which include Federal, State, and local funds, are closely tied to unemployment. Blind persons needing help, for example, are found almost everywhere. Nevertheless, we must bear in mind that people aided under any of the social welfare programs "must be needy, according to the definition of need used in the State."

One official of HEW has suggested that two phases of social welfare—aid to dependent children and general assistance—are rather closely associated with areas of acute unemployment. These programs in the eight counties referred to above came to about $23 million in the 5-year period, 1955–59. For Jackson County the payment was approximately $418,160 during 1960.

SAVINGS IN USE OF UNEMPLOYMENT INSURANCE

New employment created by the growth of Technical Tape Corp. should help reduce the drain on the Illinois unemployment insurance fund.

In Jackson County the benefit payments, according to the Illinois Division of Unemployment Compensation, are currently running between $550,000 and $570,000 yearly with around 500 persons receiving benefits in an average week. The

[1] Franklin, Hamilton, Jackson, Jefferson, Johnson, Perry, Saline, and Williamson.

total persons aided during the year may be several times the figure cited since workers go on and off the list during the year depending on their "benefits" standing. Since the county's latest unemployment figure is 1,650, it is evident that no more than 33 percent of the unemployed, according to the data used, are receiving benefit payments at any one time.

In an earlier paragraph, I noted the creation of some 980 new jobs within 3 years. The effect of this on total benefit payments is extremely difficult to measure. It is suggested, that a rough estimate on the possible reduction of benefit payments might be secured in the following way. Assume, as the figures show, that the new employment will eliminate about 60 percent of the county's unemployment (1,650). Should this happen then it is logical to assume that over the long run about 60 percent of the $560,000 yearly unemployment insurance bill also might be eliminated. This figure comes to an annual savings of $336,000.

POSSIBLE REDUCTION IN WELFARE PAYMENTS

During 1960 some $5,600,000 was distributed as aid to dependent children and general assistance in the eight Illinois counties noted earlier. About 14,000 persons received, on the average, $400 of assistance that year. Now suppose that one-fourth of the 980 new jobholders created by Technical Tape's expansion would be using at least $400 yearly in welfare payments if they did not have the support provided by the new development based on an ARA loan. These 245 workers would require $98,000 in welfare funds every year. Accordingly, I am assuming, and it appears to be a reasonable assumption, that the development of Technical Tape Corp. would cut Jackson County's annual welfare bill of $418,160 by about $98,000 or 23 percent.

EFFECT OF NEW EMPLOYMENT ON PERSONAL INCOME TAX PAYMENTS

Taking several hundred persons off the unemployment rolls where they are costing government at all levels a great deal of money and providing them with constructive jobs, not only raises their own moral and well-being but also generates additional tax revenue. By using standard tables for an average family, I found that jobs, based on the expansion of Technical Tape, should increase Federal income tax revenue by about $226,800 yearly. A sizable increase in State income tax revenue also could be expected.

OTHER LOCAL BENEFITS

Whereas the city of Carbondale has previously paid tax on an unused industrial building, it will now receive $30,000 yearly in rent from Technical Tape.

A going concern of 500–800 workers in a modern $1,825,000 plant will tend to raise property values through the community. A personal property tax on the company as well as new revenue from sales tax should further benefit local government.

SUMMARY PICTURE

The area benefits derived from new expansion based on a $500,000 ARA loan to the Carbondale Industrial Development Corp., as outlined in the preceding paragraphs, include:

980 full-time jobs with an annual payroll of	$3, 984, 500
300 part-time jobs with an annual payroll of	336, 000
Annual savings in unemployment insurance benefit payments	336, 000
Annual savings in welfare payments	98, 000
New personal Federal income tax (yearly)	226, 800
Annual rent for factory building paid to city of Carbondale	30, 000

Additional tax revenues and other economic gains might be estimated and listed in a more comprehensive study of this development. However, the essential elements have been covered, and the results clearly show how the wise investment of a few hundred thousand dollars can alter the fortunes of individual workers from a state of needing public support to a point where they are contributing to Federal and other programs.

Senator PROXMIRE. Mr. Hodges, when you discuss the trade expansion act you say the resulting harships are but a small fraction of the benefits of the reduction in trading barriers to the economy as a whole.

I think I could agree with you if you are talking about two elements, one of which is economic and one of which is not. I can see a benefit which comes from lower prices in the economy because of greater competition and, secondly, a very great political benefit in the strengthening of the free world. I think that is the most important of all.

But I cannot understand when we have a $5 billion favorable balance of trade today how we can allow this to go on for very long if, as Senator Bush indicated a few minutes ago, we can expect to get the free world to share our aid burden a little more. It seems to me if this is done and we move toward a more normal situation we can expect our favorable balance of trade to dwindle to nothing. Under these circumstances I should think that the adverse effect of trade on employment might equal the favorable effects.

Secretary HODGES. I think you could, of course, have easily come to that conclusion, Senator, because you must bring in imports if you are to sell a whole lot of exports. I suppose I am just too enthusiastic about the possibility of what this Nation can do if it gets tooled up to do it and if it gets a selling point of view. We are the lowest industrialized nation in the world in the percentage of the number of manufacturers who participate in exports and in the amount of our gross national product percentagewise that we sell abroad. We have hardly scratched the surface. With all the know-how that we are supposed to have, with all the promotion and with the explosive population all over the world, including us here, I would think that the chance for selling increased quantities regardless of the imports that are coming in are very good indeed. I think that is our job to do. We have not started that.

Senator PROXMIRE. Is it true that, No. 1, our big market has been here, this is where the effective demand is?

Secretary HODGES. That is the reason we have gone to sleep because we have had the market here.

Senator PROXMIRE. No. 2, as these other countries improve their productivity, efficiency, and get more investments and increase their skills, it seems to me the competition would become tougher and they might move to take some of this big market of ours. Also over the long pull when we hope to reduce our foreign aid program which accounts for two-thirds of our favorable trade balance this might make it tough for us.

Secretary HODGES. It will. It will give us difficulty, but the thing that bothers me is that if we let this thing go off and leave us—they are getting more efficient, there is no question about that—but if they close out all of the barriers between them, in 5 to 6 years, then what they do is automatically build up the size of the plants in Germany making aluminum and steel and automobiles and all other things, and we will not have even a chance to get in. So we must bargain with them to see that their external tariff comes down now. If we get on the ball I think we can sell a lot more goods proportionately.

Senator PROXMIRE. You are arguing the negative view as well as the positive that if we don't do it we will lose the advantage we have?

Secretary HODGES. We will either stagnate our exports or they will diminish.

Senator PROXMIRE. Just one more question. In your statement you say the HHFA is giving aid to urban mass transportation and administering an extensive program for aiding investment and operations in the American merchant marine. I suppose not much can be done about the latter, although I have tried to oppose increases in subsidies. I am very concerned about our getting into a brandnew substantial area of Federal subsidy that can grow enormously and if we aid railroads, and I guess this is primarily for railroads, it seems to me there are subsidies to other forms of transportation. If you are going to go ahead and do this isn't this going to become increasingly burdensome to the Federal Government and also destructive of effective private responsibility?

Secretary HODGES. Yes, sir. Just two things, Senator. One is we don't indicate here that we are for subsidies for railroads and so forth. We are not talking that at all. We are simply saying that we are carrying out a program on the merchant marine where subsidies are because that is where Congress determined they wanted it.

Senator PROXMIRE. You gave the same viewpoint it is true on aids to urban mass transportation.

Secretary HODGES. Yes. That is a very necessary thing to be done. I would hope that it be done primarily at the local level with certain Federal assistance but not big in the way you are talking about.

Mr. BATT. Mr. Proxmire, you raised the question of the seed money aspect of an area. I have the results of this study here. This one loan in Carbondale in this coal town—this coal country of southern Illinois was $455,000 in Federal money. For this $455,000 here is what we got. Two and a half million dollars of private investment, $4.3 million of local payrolls every year, and $788,000 of public savings and earnings including a Federal tax revenue estimated at $226,000.

Senator PROXMIRE. Every year?

Mr. BATT. Every year. So with the Federal tax alone we will repay this loan in 2 years, and we are going to get this loan paid back. We put in seed money of $455,000 and we get this as a conservative multiplier effect on this one loan alone. We went into it in depth because it was an interesting case. Two more companies were brought in to supply this branch plant of an eastern concern.

I did want to answer you, if I could, Senator Pell, when you asked about why had we not gotten more into Rhode Island. I don't know the details, but I have this figure. Rhode Island got the second training project in the country. We had three applications for section 6 business expansion loans from Rhode Island, one on October 31 which is now being negotiated—supposed to be a meeting today between CFA and your people in New York. That was Woonsocket. The second came to us on the 26th of December, the day after Christmas. That is now being studied. A third one came to us on the 22d of January. Those are the three we have.

Senator PELL. Thank you very much. I had one further question. I was wondering if the figures are available anywhere as to what the general impact, negative impact of the trade adjustment program would be on the 50 States? You say here that resulting hardships will be but a small fraction of the benefit of the reduction in trade barriers to the economy as a whole, but in order to say that one must know what the hardships will be.

Secretary HODGES. What we are trying to say there is that of the $15 billion now that we import in this country literally two-thirds of it does not affect our people at all, it does not compete with other things we make here. So when you get down to a third, or about $5 billion, why it would not be too rough. I don't know how you would find out exactly the effect, but we are taking a look at it.

Chairman PATMAN. Thank you, Governor Hodges, for your patience and consideration and helpfulness. You have helped us greatly. We appreciate Mr. Batt's being here too. We appreciate your testimony, sir.

Secretary HODGES. Thank you.

Chairman PATMAN. You may enlarge upon your testimony if you decide to include anything that is germane.

Secretary HODGES. Thank you, Mr. Patman. We appreciate it very much.

Chairman PATMAN. Without objection, the committee will stand in recess until Monday morning, February 5, here in this room, at which time we will have a panel of economists on fiscal and monetary policy.

(Whereupon, at 3:30 p.m., the committee recessed, to reconvene on Monday morning, February 5, 1962, at 10 a.m.)

JANUARY 1962 ECONOMIC REPORT OF THE PRESIDENT

MONDAY, FEBRUARY 5, 1962

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

The Joint Economic Committee met, pursaunt to recess, at 10 a.m., in room P-63, the Capitol. Representative Wright Patman, chairman of the committee, presiding.

Present: Representative Patman, Senators Bush, Douglas, Sparkman, and Proxmire; Representatives Reuss, Curtis, Widnall, and Kilburn.

Chairman PATMAN. The committee will please come to order.

This moring we continue the hearings on the Economic Report of the President for 1962.

We have this morning a panel of distinguished economists who will discuss fiscal and monetary policies.

Prof. John G. Gurley, Stanford University, former senior staff member, Brookings Institution, whom we have had the pleasure of having before us before; Prof. Richard A. Musgrave, Princeton University, who has been very helpful to the committee in many ways over the years; Prof. Raymond J. Saulnier, Barnard College, Columbia University, who was a Chairman of President Eisenhower's Council of Economic Advisers.

Dr. Edward M. Bernstein, who has held many high positions in Government, notably in connection with the Bretton Woods Agreement, is unavoidably detained, but will be here soon.

We are extremely glad to have you gentlemen. It is good of you to come, and I believe we will start with Mr. Gurley.

Professor Gurley, we will recognize you, and you can proceed in your own way, sir.

STATEMENT OF PROF. JOHN G. GURLEY, STANFORD UNIVERSITY

Dr. GURLEY. Thank you, Mr. Chairman.

I wish to apologize, to begin with, for not having extra copies of my statement; but it is short.

I am John G. Gurley, a professor of economics at Stanford University.

I very much appreciate the opportunity that you have given me, Mr. Chairman to appear before this committee.

My opening statement will be brief. It will consist mostly of supplementary remarks to a few points discussed in the President's Economic Report on monetary and fiscal polices.

The Econimic Report is correct in stating that fiscal policy has been less restrictive during the present upturn than it was in the recovery of 1958–59. And the report could have included the recovery of 1954–55 in the comparison.

If we consider comparable periods in the three recoveries—that is, three-quarters of upturn following the trough of the business cycle—some interesting comparisons, based on a few simple assumptions, can be made.

For example, it can be shown that, if Federal expenditures for goods and services and Federal net receipts had remained constant in the 1954–55 recovery period, GNP might have risen by almost 16 percent.

This inflationary upsurge would probably have come about because of the growth of autonomous private expenditures that actually occurred during those three quarters of recovery. However, since GNP, in fact, rose by only 8 percent in this period, it means that Federal budget policy applied the brakes to the extent of the difference between the two figures, that is, by 8 percentage points.

In the same way, it can be shown that Federal budget policy cut back the growth rate of GNP during the 1958–59 recovery period by 6 percentage points, somewhat less than the previous upswing.

In 1961, budget policy had, on balance, little if any restrictive effect on the growth of GNP. The reason for this is that the rise in tax receipts during 1961 tended to reduce private expenditures by about the same amount that Federal expenditures rose.

Fiscal policy, therefore, has become less and less restrictive. There is, however, another side to this coin. GNP, whether in current or constant prices, grew by about the same percentage, during three quarters, in all three recovery periods.

Hence, if Federal budget policy has become less and less restrictive, it implies a weakening of private demand, a weakening of that demand which is based on growth prospects of the economy, population increases, and other long-range factors.

Fiscal policy has had to be increasingly lenient in each upswing, in the face of a weakening growth in private demand, to achieve about the same results overall in the three recovery periods.

Monetary policy has also been somewhat less restrictive in this upturn than in previous ones. Short-term rates are substantially below their high points of the 1958–59 recovery; and long-term rates have risen very little in the past three quarters.

This has been the result of fairly light net issues of primary securities, in the form of Government securities, corporate bonds and stocks, mortgages, consumer debt, and the like. These issues in the aggregate amounted to only 10 percent of gross national product in 1961, which is low for an upturn.

In addition, as the Economic Report notes, there has been an unusually large accumulation of liquid assets by the public, mostly claims on financial institutions, including monetary claims.

These two things together mean that consumers, business firms, and Government units have sold large proportions of their primary security issues to financial institutions, which in turn have created large amounts of liquid assets for the public to hold. This process has kept interest rates from rising very much.

The Economic Report says practically nothing about the possible effects of the recent rise in interest rates paid by commercial banks on their time deposits. My feeling is that this will not have much upward pressure on the general level of interest rates, and it might even tend to lower interest rates on the average.

If the extra demand for time deposits is at the expense of the demand for money holdings, checking deposits and currency, then there will develop an excess demand for primary securities, for bonds and other types of primary debt, because commercial banks will have additional excess reserves to demand primary securities, without there being an extra desire by anyone else to sell securities. The excess demand for securities would tend to lower the general level of interest rates.

However, if the additional demand for time deposits is at the expense of the public's demand for primary securities themselves, or for claims on other financial institutions, the extra demand for these securities by commercial banks will be more than offset by an additional supply of securities coming either directly from the public or from financial institutions which have suffered withdrawals of funds. This would tend to raise the general level of interest rates.

But it can be shown that, for every dollar involved, this latter effect is significantly smaller than the former one, so that if the funds going into time deposits come fairly evenly for money balances, primary securities, and claims on other financial institutions, the net effect is very likely to be downward pressure on interest rates generally, or at least little effect one way or the other.

Moreover, if the funds going into time deposits represent an increase in planned saving, further downward pressure will be exerted on interest rates generally.

It might well be that savings and loan associations and other financial institutions will raise their deposit rates. Some already have. One effect of this, however, is to increase the probability that funds flowing into time deposits come from money balances, which earn no interest at all; in which case interest rates on securities would tend to fall.

It is also possible that commercial banks and other lenders will raise interest rates on certain types of loans which are negotiated in monopolistic markets. If so, the likely net effect, considering all the factors I have mentioned is some change in the structure of interests rates, without much if any change in the general average of interest rates.

There is just one place in the report's discussion of monetary and fiscal policies that made me uneasy, and that occurred in the explanation of the concept of the full employment surplus. On page 80 it is stated:

> Generally speaking, one budget program is more expansionary than another if it has a smaller full employment surplus.

It is clear that throughout the discussion of fiscal policy, a surplus budget is considered by the report less expansionary than a deficit budget. And yet there is no simple relationship between the size of the surplus or deficit and the restrictive or expansionary effect of the budget on full employment GNP.

The relationship depends on several other factors, including the level of Government expenditures. Two surpluses, for example, of the same size, may have totally different impacts on the economy if the levels of Government expenditures associated with the surpluses are quite different. A surplus 2 years from now is likely to have a much more expansionary effect at the full-employment income level than would the same amount of surplus today, because by then Government expenditures will be larger.

Of course, if the surpluses are equal, tax receipts would grow by the same amount as Government expenditures. But the rise in tax receipts is likely to reduce private expenditures by less than the amount that Government spending rises. Hence, it is not possible to gage accurately the probable impact of Federal budget policy in fiscal 1963 from the report's comparisons of full employment surpluses on page 82; the discussion here is incomplete and may be highly misleading.

I favor the fiscal policy recommendations in the report to give the President standby authority to vary temporarily the general level of tax rates and to initiate a limited amount of public investments. However, it seems to me that, for purposes of economic stablization, standby authority both to raise and to lower tax rates temporarily from a given base would be superior to the present proposal.

Congress may be more willing to approve a request for a tax-rate reduction to stave off a depression than for a tax-rate increase to fight inflation. If so, from an economist's point of view, it would be important for the President to have standby power to raise taxes temporarily—from an economist's point of view but perhaps not from Congress'.

On the other hand, the report's recommendation on this matter would carry more weight if a President had ever asked Congress for a tax-rate reduction for economic stabilization purposes, and had been refused.

It can also be said that the long list of fiscal actions taken in 1961, as recorded in the Economic Report, impressively suggests that a great deal of flexibility already exists with regard to timing of expenditures, tax refunds, and transfer payments. Nevertheless, despite such considerations, these recommendations, on balance, strike me as good ones.

I wish to conclude by saying that in my opinion this Economic Report wins top prize, with all due respect to its predecessors. The economic analysis in it is first rate and stimulating, and its various points fit together quite nicely. The report not only presents a sharp and full picture of where we have been, but it also presents guideposts and goals for the future growth of our economy.

But, most important of all, the report reflects a genuine concern for improving the welfare of all human beings, whether they are Negroes living in dilapidated houses, the ill with inferior medical care and facilities, children with inadequate educational opportunities, or the unemployed without job prospects.

The report is a most impressive document.

Chairman PATMAN. Thank you, sir.

After we hear from all of you gentlemen, we will ask you questions.

We have as our next witness, Prof. Richard A. Musgrave, of Princeton University.

Professor, you are recognized. You may proceed in your own way, sir.

STATEMENT OF PROF. RICHARD A. MUSGRAVE, PRINCETON UNIVERSITY

Dr. MUSGRAVE. Mr. Chairman, if I may, I would like to summarize my statement and place the fuller statement, with some data, in the record.

Chairman PATMAN. It will be placed into the record at this point, sir, and you may summarize it as you desire.

(Professor Musgrave's prepared statement follows:)

PANEL ON FISCAL AND MONETARY POLICIES—JOINT ECONOMIC COMMITTEE HEARINGS ON ECONOMIC REPORT OF THE PRESIDENT

Testimony by Richard A. Musgrave, professor of economics and public affairs, Princeton University

I find myself in substantial agreement with what the economic report has to say on the role of fiscal policy in the cycle. I wish to underline once more the powerful contribution of the fiscal system to the recent recovery, and to welcome the sharp reduction in the level of surplus at full employment which has occurred over the last year. The President's proposals for increased flexibility in fiscal policy will further increase our ability to forestall serious recessions and has my enthusiastic support. I am somewhat troubled, however, regarding the implications for fiscal policy of a growth-rate target of 4½ percent.

ROLE OF FISCAL POLICY IN THE RECESSION

The leverage exerted by the fiscal system depends upon the level of Government purchases, transfer payments, and tax receipts.[1] Using quarterly data (national income basis, annual rates, seasonally adjusted) I have estimated changing leverage from 57 to 62, as shown in tables 1 to 3 and plotted in the chart. What is important for stabilization policy, we note, is not so much the absolute level of leverage but changes therein. The fiscal system has an expansionary effect over a given period if leverage rises, and it has a restrictive effect if leverage falls. Such changes in fiscal leverage (for all levels of Government combined) are recorded in columns VI and VII of table 2 and are plotted in the chart. Two measures of change are shown,[2] one using an instantaneous multiplier (col. VI of the table, and solid blocks in chart) and one using timelags (col. VIII of the table and striped blocks in chart). The latter concept is superior and is used in table 1. Similar data for the Federal budget only are shown in table 3. Throughout, the recorded leverage includes those changes which result from the operation of built-in flexibility, as well as those which result from discretionary action on tax or expenditure policy.

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[1] This fact is blurred by the report's preoccupation—pp. 79–82—with the level of surplus and deficit. It would have been better, in charts 6 and 7. to record the levels of fiscal leverage—be it in terms of multiplicand or, full multiplier effect—at various levels of income. Such, at least, is the case if we deal with employment aspects. The report's treatment is more appropriate in connection with growth effects.

[2] For the first concept, the estimated leverage (col. V of tables 2 and 3) is calculated to equal 2 (100 percent of purchases plus 70 percent of transfers minus 50 percent of tax yield). The terms in the bracket reflect the various ways in which the budget provides for an initial increase in expenditures. Government purchase are counted fully, while transfers and taxes are discounted so as to exclude the change in disposable income which is not reflected as a change in private expenditure. The total "multiplicand" is then multiplied by 2, the estimated average value of the multiplier.

This view of the matter runs into difficulty if the changes in leverage are to be related to changes in GNP. Since the multiplier effect operates overtime, changes in leverage based upon the instantaneous multiplier do not properly describe the timing aspect. To correct this, the multiplicand (equal to ½ of col. V) was assumed to give rise to a multiplying process equal to 1 in the initial quarter, ½ in the following, ¼ in the next and so forth. The total leverage shown in col. VII is derived in this way, reflecting for each quarter, the multiplicands for five preceeding quarters.

Obviously, this is still a very rough estimate. The values of the coefficients (here set at 7, 5, and 2) will vary over the cycle, and dynamic effects complicate the result. Nevertheless, this index of change is much superior to that provided by considering the change in size of deficit or surplus only. While rising leverage is usually accompanied by falling surplus or rising deficit, this is not a necessary, and frequently not a close association.

Regarding the multiplier of 2, note that the multiplier of $\frac{1}{1-(1-t)c}$ is usually estimated at 2. Using $t=0.25$, this gives $c=\frac{2}{3}$. The multiplier formulation, appropriate for our calculation is $\nless 1/1c$, which gives a value of 3. The figure of 2 is used to be on the conservative side. Since the true multiplier is likely to vary over the cycle, our indexes of change in leverage are only a crude indicator. Note, however. that this objection is greatly reduced for the ratios of table 3, changes in both the private and the public sector being subject to the same multiplier.

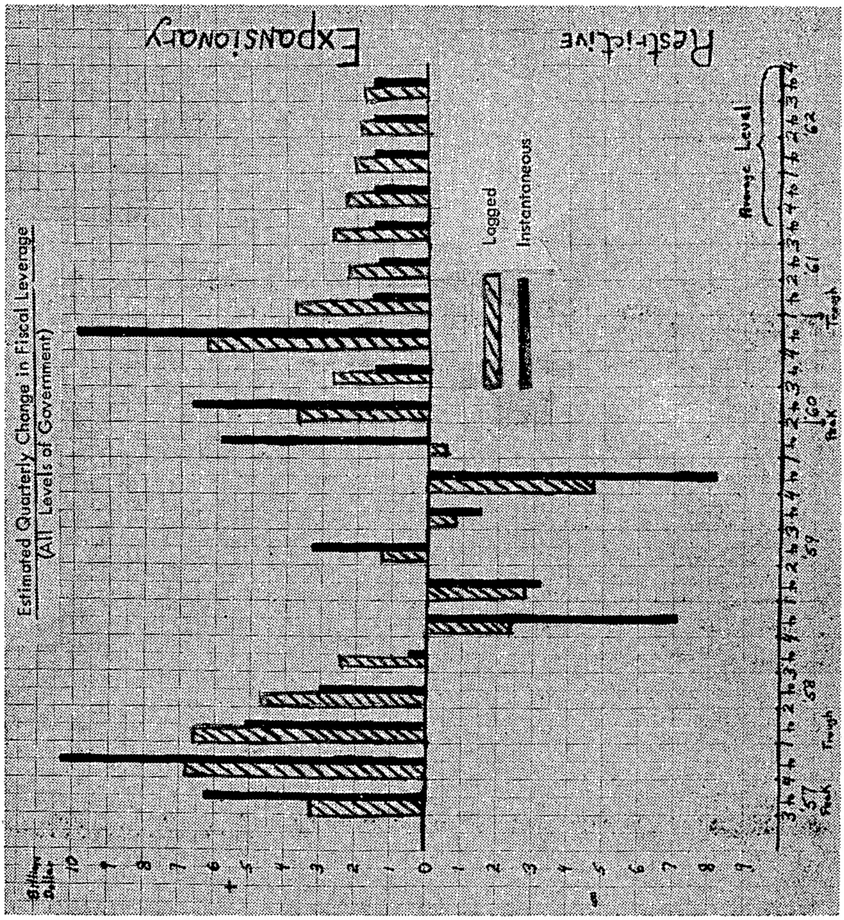
Estimated Quarterly Change in Fiscal Leverage
(All Levels of Government)
Expansionary
Restrictive
Lagged
Instantaneous
Average Level
Peak
Trough
Peak
Trough
'57
'58
'59
'60
'61
'62

TABLE 1.—*Influence of fiscal system in recent cycles*

[Annual rates, seasonally adjusted]

	Peak 1957, 3d quarter to trough 1958, 1st quarter	Trough 1958, 1st quarter to peak 1960, 2d quarter	Peak 1960, 2d quarter to trough 1961, 1st quarter	Trough 1961, 1st quarter to peak 1962, 4th quarter
Change in fiscal leverage [1] (billion dollars):				
Federal	+7.9	−0.9	+7.3	+4.9
State and local	+2.3	+6.0	+5.2	+6.1
All levels	+10.2	+5.1	+12.5	+11.0
Change in GNP (billion dollars)	−15.4	+63.5	−5.6	+79.0
Fiscal policy effect (percent): [2]				
Federal:				
Drop checked by	32		56	
Rise boosted by		−1		7
State and local:				
Drop checked by	13		45	
Rise boosted by		10		7
All levels:				
Drop checked by	40		69	
Rise boosted by		9		12

[1] See tables 2 and 3, cols. VIII, and note 1 in text.
[2] Equals fiscal leverage as a percent of (GNP minus fiscal leverage) i.e., what change in BNP would have been without fiscal change. The partial effects for the 2 levels do not add to the combined effect since nominators differ.

TABLE 2.—*Estimated fiscal leverage, all levels of Government* [1]

[Seasonally adjusted, annual rates; in billion dollars]

Quarter	Purchases I	Transfers II	Tax receipt III	Balance IV	Estimated leverage [2]: Instantaneous: Total V	Estimated leverage [2]: Instantaneous: Change VI	Estimated leverage [2]: Lagged: Total VII	Estimated leverage [2]: Lagged: Change VIII
Peak 1957:								
3d quarter	86.9	28.5	117.4	42.0	96.3		49.1	
4th quarter	87.7	30.0	114.8	−2.9	102.6	+6.3	97.4	+3.3
Trough 1958:								
1st quarter	90.1	31.2	111.0	−10.3	112.9	+10.3	104.3	+6.9
2d quarter	91.9	33.4	112.6	−12.7	118.0	+5.1	110.9	+6.6
3d quarter	94.8	34.1	116.3	−12.5	121.6	+3.0	115.7	+4.8
4th quarter	97.1	34.4	120.9	−10.6	121.5	+.5	118.2	+2.5
1959:								
1st quarter	96.7	33.8	126.3	−4.1	114.4	−7.1	115.9	−2.3
2d quarter	97.5	33.9	131.3	−.1	111.2	−3.2	113.2	−2.7
3d quarter	98.1	34.0	129.3	−2.8	114.5	+3.3	114.4	+1.2
4th quarter	96.5	36.0	130.4	−2.0	113.0	−1.5	113.6	−.8
1960: 1st quarter	96.9	36.0	139.4	6.5	104.8	−8.2	108.9	−4.7
Peak:								
2d quarter	99.6	36.8	140.0	3.5	111.8	+5.9	109.4	−.5
3d quarter	101.9	37.4	138.8	−.5	117.4	+6.7	113.2	+3.8
4th quarter	101.6	38.6	138.3	−1.9	118.9	+1.5	115.8	+2.6
Trough 1961:								
1st quarter	105.0	39.8	136.9	−7.9	128.8	+9.9	121.9	+6.1
2d quarter	107.3	41.2	141.9	−6.6	130.4	+1.6	125.8	+3.9
3d quarter	109.0	42.3	145.4	−6.0	131.8	+1.4	128.1	+2.3
4th quarter	113.0	41.7	[3] 149.0	[3] −5.7	135.4	+3.6	130.7	+2.6
1962: 4th quarter	120.0	44.3	164.0	+.3	138.0	+2.6	133.0	+2.3

[1] Data for 1957 computed from Survey of Current Business, July 1961, p. 17. Data for 1958 from Economic Report of the President, 1961, p. 135, data for 1959 to 1961 from Economic Report of the President, 1962, p. 217.
[2] For explanation, see text, note 1. [3] Estimated.

TABLE 3.—*Estimated fiscal leverage, Federal Government* [1]

[Seasonally adjusted, annual rates; in billion dollars]

Quarter	Purchases I	Transfers II	Tax receipt III	Balance IV	Estimated leverage [2]			
					Instantaneous		Lagged	
					Total V	Change VI	Total VII	Change VIII
Peak 1957:								
3d quarter	50.0	29.9	82.5	2.6	59.4		58.0	
						+3.4		+2.4
4th quarter	49.4	31.2	79.7	−.9	62.8		60.4	
						+9.1		+5.7
Trough 1958:								
1st quarter	50.6	32.9	75.4	−8.1	71.9		66.1	
						+5.2		+5.5
2d quarter	51.8	35.5	76.2	−11.1	77.1		71.6	
						+1.9		+3.8
3d quarter	53.7	36.3	79.2	−10.7	79.0		75.4	
						−1.7		+.8
4th quarter	54.3	37.1	83.2	−8.1	77.3		76.2	
						−6.6		−2.6
1959:								
1st quarter	53.2	36.9	87.4	−2.7	70.7		73.6	
						−2.4		−3.2
2d quarter	53.9	37.2	91.6	.5	68.3		70.4	
						+3.3		+.7
3d quarter	54.1	37.5	89.1	−2.5	71.6		71.1	
						−.7		.0
4th quarter	52.9	39.1	89.6	−2.4	70.9		71.1	
						−10.1		−4.0
1960: 1st quarter	51.8	38.7	97.0	6.5	60.8		66.1	
						+3.5		+.9
Peak:								
2d quarter	52.9	39.6	96.9	4.5	64.3		65.2	
						+4.4		+1.5
3d quarter	54.0	40.2	95.6	1.4	68.7		66.7	
						+.4		+1.1
4th quarter	53.0	41.2	94.6	.4	69.1		67.8	
						+8.4		+4.7
Trough 1961:								
1st quarter	54.7	43.3	92.5	−5.5	77.5		72.5	
						−1.2		+3.0
2d quarter	56.6	44.5	96.8	−4.3	78.7		75.5	
						−.2		+1.2
3d quarter	57.4	45.0	99.3	−3.1	78.5		76.7	
						+1.5		+1.5
4th quarter	59.9	44.4	[3] 102.0	[3] −2.3	80.0		78.2	
						−3.2		−.8
1962: 4th quarter	[3] 63.0	47.0	115.0	+4.4	76.8		77.4	

[1] Date for 1957 to 1960 from Survey of Current Business, July 1961, p. 17. Data for 1961 from Economic Report of the President, January 1962, p. 276. Figures for 1962 are my estimates based on budget figures.
[2] For explanation, see text, note 1.
[3] Estimated.

The results are summarized in table 3. In the downturn from the third quarter of 1957 to the first quarter of 1958 estimated fiscal leverage rose by $10.2 billion, while GNP declined by $15.4 billion. Had fiscal leverage been constant, the estimated decline in GNP would have been $10.2 billion larger, or $25.6 billion. The ratio of 10.2 to 25.6 or 40 percent shows the estimated fraction of potential decline, which was prevented through change in fiscal leverage. For the downturn from the second quarter 1960 to the first quarter of 1961, estimated fiscal leverage rose by $12.5 billion, while GNP declined by $5.6 billion. The fraction of potential decline in GNP prevented was 69 percent. These ratios refer to the leverage of total (Federal, State, and local) budgets combined, the corresponding ratios for the Federal budget alone being 32 and 56 percent. The President was indeed correct when stating that "the Federal budget played its proper role as a powerful instrument for promoting recovery."

As shown in the chart, changes in fiscal leverage were positive (the fiscal system acted as an expansionary force) during both the 1957–58 and 1960–61 downturns. While the expansionary thrust of fiscal leverage was nearly as large in 1957–58 if considered in aboslute terms, it was smaller relative to the strength of the restrictive force in the private sector of the economy. Hence the higher "prevented" ratio for 1960–61. As may be seen from tables 2 and 3, rising purchases and transfers contributed a large share of the gain in leverage in the latest recession, leaving reduction in tax yield of lesser importance. Taking the leverage of $7.3 billion provided by the Federal budget, about 25 percent thereof may be imputed to rising purchases, 45 percent to rising transfers, and 30 percent to reduction in tax yield.

The sharp rise in fiscal leverage from the fourth quarter of 1960 to the first quarter of 1961 deserves special mention, reflecting as it does the speedup of purchases and other antirecession measures taken by the administration. While the Council modestly notes that the upturn would probably have started in the first quarter without this expansionary fiscal force, it has surely been a major factor in providing a vigorous turnaround.

ROLE OF FISCAL POLICY IN THE UPSWING

The role of fiscal policy in recent upswings also appears in table 1. For the 1958–60 upswing as a whole (from the first quarter of 1958 to the second quarter of 1960) fiscal leverage rose by $5 billion, a decline in Federal leverage of $0.9 billion being much outweighed by a rise in State-local leverage. Taking the Federal budget by itself, fiscal restriction may have checked the expansion of GNP to some extent. In addition, money markets tightened and bond yields rose by half a percentage point.

As shown in the chart, fiscal leverage declined—that is, changes in the fiscal system were heavily restrictive—through most of 1959. Fiscal policy thereafter became expansionary and remained significantly so in the quarters preceding and following the peak, but the heavy drain in 1959 had worked its damage on the upswing. While the net effect over the span from trough to peak was nearly neutral, there is danger in looking at so long a span. The damage of the 1959 restriction, in a dynamic economy, could not be repaired by the subsequent expansion.

Compared to this rather discouraging experience, the outlook for the current upswing is much more cheerful. Taking the Federal Government by itself, fiscal leverage is expected to decline in the course of this year; but the decline will be modest (perhaps $3 billion from the fourth quarter of 1961 to the fourth quarter of 1962) and is likely to be more than offset by expansion at the State and local level. As shown in the chart, combined fiscal leverage should continue to expand slightly through each quarter, thus avoiding a repetition of the unfortunate experience of 1959. Taking the entire period from the trough in the first quarter of 1961 to (what we hope, will not as yet be the peak) in the fourth quarter of 1962, the fiscal system may have boosted the rise in GNP by, say, 12 percent. Monetary policy, as well, is faring better as long-term rates, as yet, have risen but slightly. Given this setting there is good reason to hope that the projected surplus (national income accounts basis) for 1963 will be realized.

Another view of the expansionary change in the fiscal structure is obtained by considering what has happened to the level of a potential surplus at a full employment income. The Council, last spring, noted that the existing fiscal structure would produce a surplus, at a full employment level of income, of over $10 billion. The Council now estimates that this potential surplus has shrunk to $6 billion; and this in turn was one of the reasons why the state of budgetary balance moved from a substantial deficit to a rising surplus.

PROPOSALS FOR FISCAL FLEXIBILITY

I do not wish to detract from what has been accomplished, but I should note that stabilization policy, as it were, has been riding the crest of an upward adjustment in the level of Federal expenditures. In the course of 1960–61, Federal purchases rose by $7 billion, and another $3 billion will be added thereto in 1962. These increases were largely in response to rising needs for defense, space exploration, and so forth, factors quite exogenous to stabilization as such. They were called for anyhow, but happened to come at the right time. In the next round, such favorable coincidence may not be present and the problem of antirecession policy may have to be faced explicitly, i.e., creation of leverage by a policy package including substantial tax reduction. It is important that this be kept in mind, lest the recent success lead us to an overly complacent view of what may be expected.

I am delighted, for this reason, that the President has seen fit, building upon recent proposals by the Commission for Money and Credit, to recommend at this time a series of measures designed to take prompt action in the case of future recessions. I am pleased especially with his proposal for flexible income tax adjustment—a proposal which I have advanced at various times before this committee. I believe that the requested authority would greatly increase our ability to maintain high levels of income and employment. At present, monetary policy is the only major means by which quick action may be taken; and monetary ease is not likely to have a significant effect on the level of consumer expenditures, the very component of demand which needs to be strengthened when investment begins to slacken. Moreover, the individual income tax has shown little built-in flexibility, due to the stability of personal income, so that the needed stimulus to consumption will not be forthcoming in an automatic fashion.

I appreciate that the authority to levy taxes and to control the purse strings of Government must be vested with the Congress, and that there should be no weakening of this basic authority; but I believe also that the proposed authority would in no way infringe upon this privilege. I very much hope that these aspects of the matter can be worked out as I believe that passage of the proposed legislation would add greatly toward increasing the stability of our economy. Also, it would strengthen our ability to conduct a stabilization policy favorable to economic growth.

FISCAL ASPECTS OF ECONOMIC GROWTH

I realize that economic growth is to be the subject matter of your next panel, but I insert a few words on its fiscal aspects here. Economists have been pointing out, for some time, that stabilization policy for economic growth should aim to combine a relatively restrictive budget policy with a relatively expansionary monetary policy. While the former is to hold down consumption, the latter is to encourage investment. Thus, resources are to be transferred from consumption to capital formation, thereby increasing the rate of growth. This policy was set forth in the Economic Reports of the preceding administration, and it is again given a prominent place in the statements of the present Council.

This prescription is clearly valid in a "classical" type of economic system—a system, that is, where investment always adjusts itself to match planned saving; or in a "neoclassical" system where such a match may always be achieved by monetary measures. Here a policy of budget surplus combined with monetary ease will result in higher capital formation and more rapid growth. But the formula may backfire in a setting where these assumptions do not always hold; where investment may fall short of planned saving even though it be encouraged by monetary ease. Here the indicated policy may not accentuate economic growth but cause unemployment instead.

The actual world in which we live may, at times, approach the "classical" or "neoclassical" setting, but it is not to be identified with it. It is important, therefore, to realize that the economics of growth policy does not call for a combination of budget surplus and monetary ease; rather, it calls for a combination of greater reliance on fiscal restriction with monetary ease. At times (and there is no law which tells us that such might not be the case for the average year), this greater reliance may mean a lesser deficit, rather than a larger surplus. Putting it differently, the appropriate level of deficit or surplus is that which permits us to achieve the dual objective of full employment, while at the same time devoting on appropriately large share of resources to capital formation. I emphasize this, because in the Economic Report there prevails a somewhat disturbing association of growth policy with the surplus objective. This association may be justified if a highly buoyant view of the longer run economic outlook is taken, but it may mislead the reader who chooses a more cautious appraisal. However, so far this is a point in theory only. The important fact is that fiscal action during the past year has significantly reduced the level of surplus at full employment.

Of course, much depends on how effective policy can be in stimulating a higher rate of capital formation. Economists have not been too optimistic regarding the powers of monetary ease to accomplish this objective, and recent balance-of-payment developments (not withstanding the degree of success achieved in "Operation Nudge") have placed further restraints on the monetary approach. The alternative then is to induce a higher rate of capital formation through public expenditure and/or a tax policy. To the extent that private capital formation is concerned, emphasis is on tax incentives. Now, it may well be that tax incentives can be devicsed (including, if need be, negative taxes or subsi? dies) which are sufficiently powerful to achieve most any desired increaes in the rate of capital formation, but this is besides the point. The real issue is how the incentives can be given without doing more harm than need be to the equity of the tax structure.

The investment credit, which has been proposed by the President and which is now under consideration by the Congress, has much merit on these grounds. It appears to be the most effective way of inducing expansion for a given current revenue loss and least likely to be wasted in benefiting investment which would have occurred anyhow. For these and other reasons, I believe that the credit is a desirable step in the right direction. At the same time, its importance should not be overestimated. Raising the growth rate by 1 percentage point or more is no simple matter. Much more drastic measures than have been contemplated so far may be needed to accomplish this objective, and their cost (in terms of equity in the tax structure, and implications for other phases of public policy) may be more severe than has been realized.

Dr. MUSGRAVE. I join Mr. Gurley in commending the report for its excellent economic analysis and find myself quite sympathetic to the general line of reasoning on fiscal policy. However, I take it my presence here will be more constructive if I try to be critical where I can and thus introduce some additional ideas.

Mr. Gurley is completely correct in pointing out that the level of deficit and surplus is not the appropriate measure of the expansionary or restrictive effect of fiscal policy. And I have tried, in view of this, to develop a somewhat fuller measure thereof.

Now, the expansionary force of budget policy at any one time depends on the level of Government purchases, on the level of transfer payments, and on the level of tax receipts, the first two being related positively and the last one negatively to this expansionary force.

Moreover, if we want to ask ourselves whether, over any period, the budget was an expansionary factor in the cyclical movement, what we ought to look at is not the absolute leverage which was exerted by the budget at any one time, but rather the change in this level.

If the leverage increases over a given period, then, over this period, we can speak of budgetary forces as having been expansionary. If the leverage declines, then, over this period, we would speak of the budgetary forces as having been restrictive. It is this change in leverage that really matters.

I have tried to compute a measure of change in leverage on a quarterly basis, and you will find this plotted in the chart which is in my paper. The striped and solid blocks give two alternative methods of change in fiscal leverage. Without going into the technicalities of computing them, let me say that the striped blocks are the more relevant ones.

Whenever these blocks are above the line, this means that leverage rose and that the budget has been expansionary. For instance, in the first period, which is from the third to the fourth quarter of 1957, the expansionary force of the budgetary factors was approximately $3 billion. In the fourth quarter of 1958 to the first quarter of 1959, it was minus $3 billion. In other words, the budget was restrictive.

The chart shows quite dramatically how the budgetary forces were expansionary in the period from the second half of 1957 to the beginning of 1958, from the peak to the trough, and again in the period from the peak in the second quarter of 1960 to the trough in the first quarter of 1961.

You also see how, in the course of 1959, fiscal forces were very restrictive, as shown by the negative blocks. And you note how, projecting within the context of the budget estimate, the fiscal factor remains expansionary throughout 1962, which seems to say that, fiscally speaking, the prospects for a sustained recovery are very, very much better than they were in 1959.

Similar results are also shown in table 1. Take the period from the peak to the trough in 1957–58, as shown in the first column. During this period I estimate fiscal leverage; that is to say, the positive contribution of fiscal factors to the level of GNP, to have increased by $10 billion. During this period, GNP declined by $15 billion. Thus, if the fiscal leverage had not increased by $10 billion, then in fact GNP would have declined by $25 billion. Ten billion dollars as a percent of $25 billion is 40 percent, which is the fraction of the potential decline in GNP, which was checked by fiscal factors.

You will see that this same fraction, for the decline from the second quarter of 1960 to the first quarter 1961, decline was nearly 70 percent. The fiscal forces of expansion, relative to the drop in GNP, were much more substantial. You will also note that the contribution in the current upswing will be greater than it was in the upswing of 1959.

These ratios at the bottom of the table, to which I have been referring, relate to all levels of government; and these data include whatever change in fiscal leverage came about as a result of built-in flexibility, as well as that which came about as a result of discretionary action. The distinction between these two is not relevant for my purpose.

Thus I agree with the Council that budget policy has behaved pretty well; although I do not quite agree with their way of measuring it.

Now, I think that we should give credit where credit is due, and I do not want to belittle what has been accomplished. But it should be noted that fiscal policy during this upswing, as it were, has been riding the crest of an upward adjustment in Government purchases, for defense, for space programs, and so forth, things which were needed for nonstabilization reasons. Fortunately, it happened to come at the right time. But next time it might not come at the right time. Indeed, as far as additional defense expenditures are concerned, let us hope that they will not be needed. even if they came at the right time. Thus, next time, the problem of fiscal antirecession measures may have to be faced more explicitly; that is to say, by a policy package which includes tax reduction.

This is the explicit, the direct way of doing it, and while it did not prove so necessary last time, it may next time. Therefore I am extremely happy to find that the proposal for flexible tax policy, which was advanced by the Monetary Commission, was incorporated into the President's program.

I am especially happy about this, because I have made the suggestion before this committee on several previous occasions, and I did not expect that it was to become an official policy recommendation within so short a period.

I very much hope that the Congress will find ways in which this authority can be granted without weakening the congressional privilege to control the pursestrings, which privilege should not be weakened; but I do think that ways can be found. If they are, it would greatly help the ability of public policy in the United States to maintain stability.

Finally, let me add a word on the growth aspects of fiscal policy. I realize that this is to be discussed this afternoon, but a word should be said now.

As the Council points out, a stabilization policy appropriate for growth is one which combines relative emphasis on fiscal restriction with a policy of relative monetary ease. This formula had been advocated in the economic reports of the preceding Council, and is a continuation of the same philosophy then advanced.

Now, I think that this formula of relative emphasis on fiscal restriction, combined with monetary ease, is all right; but I am somewhat disturbed by the tendency in the Economic Report to substitute the words "policy of budget surplus combined with monetary ease" for the words "policy of fiscal restriction combined with monetary ease."

In the economics of the matter, the proper term is "fiscal restriction." This fiscal restriction may mean lesser deficit just as well as larger surplus. If you look at this formula for growth in the context of a full-employment policy, which we all want to do, the question whether it implies a larger surplus or a smaller deficit depends altogether on revealing economic conditions. Thus, I wish that, whenever the Council says "monetary ease combined with surplus," it would have added "and/or lesser deficit." I say this because I am not at all sure that for the average year ahead it will be possible to have a full employment economy, while at the same time carrying a surplus.

How far we can go in this direction, of course, depends on how much we can do to stimulate investment. Conceivably, one could think of public policy measures which would be powerful enough to get almost any level of investment which one may want. You simply subsidize investment to whatever point is needed to get the desired result.

But this creates problems of equity in the tax structure, in income distribution, and so forth.

On the whole, I feel that the Council, and not only the Council but public-policy discussion in the United States today is too optimistic with regard to the ease with which it will be possible to increase and sustain the growth rate by 1 or 1½ percentage points. I think that the investment credit proposal is the right sort of thing, going in the right direction, because it is designed to get a maximum effect, investmentwise, with the least revenue loss, and also, which I think is very important, with the least damage to the equity of the tax structure. But I do not feel that this investment credit, as now being considered, is sufficiently powerful to do the whole job. It will just get us a first step in the right direction.

I personally have some hesitations about the commitment of public policy to getting a growth rate of 4 or 4½ percent. The costs of doing this, in terms of social policy, the equity of the tax structure, and other aspects of Government policy, may be much greater than people believe: and I am not quite so convinced that the benefits to be derived are as momentous as is generally felt.

Thank you.

Senator SPARKMAN (presiding). Thank you.

Prof. Saulnier, Barnard College, Columbia University.

I believe we have had the pleasure of having you here before. We welcome your return. Just proceed in your own way.

STATEMENT OF PROF. RAYMOND J. SAULNIER, BARNARD COLLEGE, COLUMBIA UNIVERSITY

Dr. SAULNIER. Mr. Chairman and members of the committee, I have prepared a statement of views, which has been submitted to the committee; and rather than read it in its entirety, Mr. Chairman, I will summarize parts of it, and at points perhaps revert to a reading of the text.

Senator SPARKMAN. You know, of course, that the text in full will be printed in the record.

Dr. SAULNIER. I both know that and appreciate that courtesy of the committee.

(Professor Saulnier's prepared statement follows:)

TESTIMONY OF DR. R. J. SAULNIER, PROFESSOR OF ECONOMICS, BARNARD COLLEGE, COLUMBIA UNIVERSITY, NEW YORK CITY, BEFORE THE JOINT ECONOMIC COMMITTEE OF THE CONGRESS, WASHINGTON, D.C., FEBRUARY 5, 1962

Mr. Chairman, I am grateful to you for this opportunity to give testimony on the economic program of the President for 1962, as set forth in his January 20 Economic Report to the Congress, and on the report which the Council of Economic Advisers made to the President on January 12 covering much the same range of policy questions and certain collateral issues. I shall, as has been suggested, limit my testimony to matters of fiscal and monetary policy and mainly to recommendations that have been made for legislative action.

Let me begin by saying that there are two directions in which economic policy can look. It can look inward to predominantly domestic questions, the level and stability of our economy, its rate of growth, and whether this is fast enough or whether there are significant gaps between our actual performance and what may be estimated to be our full capacity. Until quite recently, economic conditions in the United States have permitted policy to be designed largely with these domestic questions in mind. But some countries have learned from necessity that they must look predominantly outward in economic matters and shape their national policies mainly with their international economic and financial position in mind.

We are still between these two positions, but I believe we are moving rapidly toward the latter. Such reservations as I have about the year-end economic messages are mainly that they have not been fully accommodated to these new circumstances. I feel all the more strongly about this having heard only a few days ago that our international balance-of-payments deficit for 1961 is now estimated at $2.5 billion, which means that there must have been a very large loss in the fourth quarter of the year. Clearly, our economic policies must be quite deliberately designed to help correct this imbalance. The Council has said in its report that domestic policy must be framed "* * * with an eye to the balance-of-payments" (p. 145). I would say that, at this time and until we have accomplished a correction on which we can count, we must frame domestic policies with both eyes on our balance-of-payments.

I want to make it quite clear at the outset that I am not an alarmist about the balance-of-payments. There is nothing in it that we cannot cope with. It all depends on how our policies, public and private, respond to it. What I shall try to do in this testimony, therefore, is to indicate briefly, yet as clearly as I can, what I think our policy responses should be.

Clearly, we need a surplus in the Federal budget. We need this for technical economic reasons. We need it because a deficit balance-of-payments situation requires that we keep costs as low as possible. We need it considering where we are in the business cycle. And we also need a budgetary surplus of meaningful size for reasons of international financial psychology.

I would judge that the necessity of a surplus is not in dispute, though there may be some who still feel that Federal deficits of large amounts are necessary to spur economic growth and, by some means, to help close gaps in the statistical record of our economic performance. But this is a minority view, at least as regards the fiscal 1963 budget. The really important question is whether the budget as proposed gives reasonable assurance of a significant surplus.

I must confess to some doubts on this important point. In the first place, it contemplates a revenue increase of $10.9 billion over what is currently estimated for fiscal 1962. This is a very large increase in receipts; it is substantially larger, for example, than was achieved in fiscal 1956, which is as close to being a cyclically comparable fiscal year as we can find in recent history. An increase of this magnitude could be achieved only with an exceptionally strong economic advance, carrying with it a very sharp increase in corporate profits as well as a large rise in personal income. My 1962 GNP forecast is a bit on the conservative side, I would judge, as forecasts go, but after going through the January issue of Business Cycle Developments I must say that I am not disposed to change it. I doubt, especially, that the corporate profit expectation which is implicit in the official projection of budget receipts is a realistic one.

And there are other features of the budget that raise doubts as to the prospect of its actually being balanced.

First, it very properly asks for an increase in postal revenues, and I hope that the Congress will respond affirmatively to this recommendation by the President. But the $600 million saving contemplated by the postal rate increases might very well be wiped out in large part by pay increases not provided for on the budget's expenditure side. I don't want to judge the budget document incorrectly or unfairly, but we do have to consider all the contingencies quite realistically when we ask ourselves how things are likely actually to turn out. It could very well be that postal rates will have to be increased over what has already been proposed if the Post Office deficit is actually to be wiped out.

Second, the budget contemplates a $468 million reduction in the costs of the Department of Agriculture, although expenditures last year under this Department rose by more than a billion dollars. We must always be prepared for pleasant surprises and possibly even for miracles, but I don't regard the fiscal 1963 budget of the Department of Agriculture as the place to look for them. We all hope that the Congress will this year check the mounting costs of this domestic program; as it stands, it is a weakening influence in our international economic position as well as being a burden on our domestic economy. And I believe that America's farm families desire a program that will move agriculture into a significantly more independent position. The contemplated reduction in the cost of our farm programs reflects only the expected results of legislative proposals that have only just been presented to the Congress. I think you will agree that, all things considered, some doubts about this section of the budget are legitimate.

Third, if the budget outcome should be less favorable than what is officially looked for, and if interest rates move up on the average over the next 18 months, as I expect they will, interest payments on the public debt, which the budget expects will come to $9.4 billion, up by $400 million over fiscal 1962, will rise by an even larger amount.

This is not the place to attempt an item-by-item examination of the budget, but I believe that such an examination would support the doubts I expressed at the outset concerning the prospect of a balance. Certainly if the estimates of receipts should prove to be overly optimistic, and the estimates of expenditures should prove to be too low, the projected $500 million surplus could disappear very quickly. The moral in this is that the Congress should scrutinize appropriations requests with exceptional care. I feel sure that a close scrutiny of them will yield many opportunities for expenditure reductions that will in no way impair the essential, or even the merely desirable, services which the Federal Government provides for the American people.

There is another point with respect to the budget to which I should like to direct the attention of this committee. It is sometimes believed that a budget has no inflationary effect so long as it is balanced. I do not share this view. On the contrary, I believe that the level of expenditures in the budget is vitally important, and particularly the year-to-year changes in that level. In this connection, I would point out that the expenditures proposed in the fiscal 1963 budget exceed those of fiscal 1962 by almost $3.5 billion, and that this follows an increase in Federal spending between fiscal 1961 and fiscal 1962 of about

$7.6 billion. In this 2-year span we will have raised our Federal expenditures, on these proposals, by more than $11 billion. This is a very large increase in any budget, whether balanced or not, and it presents a situation that warrants the closest examination by the Congress. We must all ask ourselves whether this trend is to be extended very far into the future. It is clearly not a trend that is consistent with improvement in our international financial position; quite the opposite. If it does continue, it will have to be supported by a substantial increase in taxation.

Let me turn now to monetary policy. I would judge from the documents before us that there is broad satisfaction with Federal Reserve policy this last year. Free reserves have been held constant at a plus $500 million; the demand deposit component of the money supply has increased by $6 billion (which roughly offsets the $7 billion decrease which preceded the 1960–61 recession); and interest rates have been at what I would say are roughly appropriate levels.

Borrowing costs have been moving up for the last 6 months or so, and will probably continue to rise; certainly they will if the economic assumptions underlying the budget are borne out in events. In this context, there may be some temptation to resist rising interest rates. This would be a serious mistake, in my judgment. I hope, especially, that any efforts to counteract a rising interest rate trend by authorizing increased amounts of Federal funds to be loaned at rates below market levels will be defeated. Quite apart from other undesirable effects, an expansion of such programs would ruin any chance of balancing the budget at present tax rates.

The general shape of the monetary policy response called for by our balance-of-payments deficit is clear. I must confess, however, to some confusion on what the President desires of monetary policy in 1962. I judge from the economic message that he expects the projected budget surplus to clear the road for an expansionist monetary policy. Of course, things might work this way if the budget were, in fact, balanced with a substantial surplus and the balance-of-payments deficit were to be safely corrected. But if a substantial budgetary surplus is not attained, monetary policy might have to be restrictionist, and then we would have the worst of both worlds: A Federal budgetary deficit that would complicate our balance-of-payments situation; and a monetary policy which would restrict domestic economic growth. This is another reason for making quite sure that we have a surplus in the Federal budget.

The President concluded his discussion of this subject by pointing out that monetary policy in 1962 would require "continued ingenuity in technique and flexibility in emphasis." I think I agree with this, but I would be happier if the President had said that in 1962, with a good recovery underway, monetary policy should be quite studiously directed toward helping to achieve the significant improvement in our balance-of-payments position which we very much need.

I cannot leave this subject of monetary policy without commenting on that section of the President's message to the Congress having to do with the proposals of the Commission on Money and Credit.

I am sure that it is wise to set up the interagency study groups to which the President alludes. There is much work for them to do, and ample opportunities for making constructive recommendations. But I must register my dismay at the President's proposal to amend the Federal Reserve Act to make the term of office of the Chairman of the Board of Governors of the Federal Reserve System coterminous with the 4-year term of the Presidency. The present arrangement is, as the President has described it, "accidental and inadvertent" (p. 22) but this is not to say that it isn't a good arrangement. Some of the best arrangements we have are accidental and inadvertent.

The principle that should guide us in these matters is that our central banking system should be in the hands of men who are both technically competent and who will perform their vitally important duties without reference to political considerations. I believe the present arrangement affords greater assurance of achieving these ends than would the arrangement which the President desires. Under our system of government, the President heads a political party and he is pledged to give effect to a political program adopted in a party convention. How could a nonpolitical administration of our central banking functions be maintained under a system which would virtually guarantee a change in the Chairmanship with every change in the Presidency and would time this change so as to occur in the atmosphere of our most partisan political discussion.

Speaking quite respectfully, I must say that this would be a very great mistake.

I should like to turn now to a different but related question, namely, to that part of the Council's report in which they state that "The general guide for non-inflationary wage behavior is that the rate of increase in wage rates (including fringe benefits) in each industry be equal to the trend rate of overall productivity increase." (p. 189) This has such overriding importance that it is futile to discuss monetary and fiscal policy without reference to it.

As the Council points out, wage policy based on the guideline they propose would promise a rough stability of price levels. In the past, I have favored this guideline myself. It would have been a vast improvement over our actual experience, in which wage advances typically outran economywide productivity gains by substantial margins. But I believe that in the present international context what we need is not merely a stability of price levels but significant price reductions. The right guideline at this time is one under which wage advances would be kept well within the limits of productivity improvements, not made to equal those improvements. This would leave room for significant price reductions, which are precisely what we need to improve our international competitive capability.

When I was in Europe last summer I got the impression that wage rates and unit production costs there might rise so fast that we would find in them at least a partial solution to our problem of staying competitive in international markets. But this requires that we keep our own affairs strictly in order, and I must say that I have seen very little since I came home to support the hope that we will do so. The recent settlement of an electrician's strike in New York City by granting $4.96 an hour for a 5-hour day (better than a 10-percent increase over previous hourly rates) and apparently guaranteeing a 6th hour at $7.44 an hour (well over a 10-percent increase in overtime pay) is so completely unsuited to our national needs as to be almost unbelievable. I do not like to see Government intervening in the settlement of industrial disputes, but it does seem to me that this would have been a good one in which to have taken a hand. Surely we must all understand that this is not a pattern, not even the shadow of a pattern, that we can safely follow as a nation in matters of wages and hours of work.

I think it is also clear that we must adopt a very different attitude toward the introduction of methods that will make our industries more efficient if we are to respond as we should to the changed international economic position in which we find ourselves. We have had some bad experiences in New York City recently on these matters also. I refer to the resistance to automated equipment on our subway system.

The President's Commission on these matters seems to have ended with a divided and inconclusive report. I urge as strongly as I can that the Joint Economic Committee put wage policy, policy on hours of work, and policy toward the introduction of labor-saving methods high on its agenda for 1962. I would suggest special hearings on this range of subjects.

Finally, I should like to comment briefly on the suggestions which have been made in the President's message for additional discretionary authority to be lodged in the Office of the President to help stabilize the economy.

I like the proposal which would give the President authority to extend unemployment compensation benefits for an additional 13 weeks when, during a recession period, exhaustion of benefit rights mounts to unusually high levels. I am far from sure, however, that this extension of benefits should be made automatic and contingent upon reaching a 5-percent unemployment level. I would rather see it made altogether discretionary with the President, though he will of course, wish to have appropriate and flexible quantitative guidelines to follow in the administration of his authority.

I like the proposal because we have had two experiences with a temporary extension of unemployment compensation benefits and the system has worked well. It is my idea of the near-perfect counter-recession measure. It does not prevent recessions, to be sure, but it softens their impact and it gives assistance to those most in need of it. I hope to see this proposal, with appropriate revisions, enacted into law.

I am by no means persuaded, however, that the proposal which would permit an increase of Presidential initiative in individual income tax changes is a wise one. I am less concerned about that part of the recommended legislation under which the President would make proposals to the Congress that would take effect 30 days later, unless rejected by a joint resolution, than I am about that part which would give the President the right to make temporary tax reduc-

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tions when the Congress is not in session, with extensions subject to congressional veto. From a purely administrative point of view, I don't see how this could fail but produce much confusion. And I also have doubts about the proposal on more strictly economic grounds. Unlike the unemployment compensation proposal, we have had no experience with tax reduction as an antirecession measure. I do not regard the tax reduction in 1954, which accompanied a substantial drop in Federal expenditures made possible by the ending of war in Korea, as a concluisve test of the need for, or the efficacy of, individual income tax reduction in this connection. And, as we know, recovery from recession was accomplished in 1958 and again in 1961 without recourse to personal income tax reduction. There were influential voices calling for tax reduction in 1958 and again in 1961, and it should be instructive to note that these were heard even after there were signs of a recovery to come and in some cases even after recovery had already started. It is not easy to withhold one's hand in such situations, but there are times when it is best to do so. I am afraid that the proposed legislation would invite situations in which taxes would be reduced when it was not really timely or beneficial to do so.

Finally, I am opposed to the request for standby authority under which the President would be authorized to increase Federal expenditures on capital improvements up to as much as $2 billion. The guidelines proposed are altogether too loose, it seems to me, but apart from that, I would object to the proposal on the grounds that it is not needed and that it is unlikely, in any case, to be effective as an antirecession measure.

This is another matter on which we have had a good deal of experience. I would say that that experience teaches two lessons. The first is that there is a good deal of leeway for increasing construction expenditures under our present arrangements, which normally authorize the obligation of funds substantially above the amounts normally scheduled for expenditure. The second is that increases in expenditures intended to counter recession normally do not become effective until well after a recovery is underway. I would much rather see us committed to a steady level of capital improvements, wisely selected for their national benefit, and pitched at just as high a level as our resources will reasonably permit. For various reasons, I do not like off-again on-again programs of capital improvements. I think our economy and our public interest are benefited more by steady, assured, public construction programs. I think we would be better off to continue with our present arrangements.

I offer these as my suggestions for public and private policy responses suitable to our present international economic and financial position.

Thank you very much.

Dr. SAULNIER. Let me say, first, Mr. Chairman, that I appreciate very much the opportunity to return to this chamber and before this committee.

I will limit my testimony, as has been suggested, to matters having to do with monetary and fiscal policy, though I should like, in the course of my remarks, to refer briefly to the Council's suggestions on the question of wage policy, because I think that this is basic to a full consideration of monetary and fiscal policy.

I begin, Mr. Chairman, by pointing out, perhaps generalizing a bit too much, but primarily to bring out a point which I think is of major importance to our country at this time, that economic policy can look either predominately inward to domestic questions or predominately outward to international questions.

Let me say, Mr. Chairman, that such reservations as I have about the proposals that have been made by the President, and by the report made by the Council, reflect primarily my feeling that at this time the program is inadequately attuned to the international economic and financial position of the United States today.

I have felt this way about matters for some time, and, as I have indicated in my proposed statement, I have felt all the more strongly about it since I heard that the deficit in our international balance of payments for the year 1961 is now estimated at $2½ billion, which means, of course, that there must have been a very large deficit in the fourth quarter of the year.

I want to make it quite clear that I do not take an alarmist view with respect to the balance of payments. This is a situation which has developed because of some very right and proper things which our Government has done in the international field. Unfortunately, however, it has been aggravated by what I would regard as some wrong domestic policies.

I feel, Mr. Chairman, that the real problem that confronts us today, from a policy viewpoint, is how we respond, in the broad strategy of our economic policy, to this international economic and financial situation. And I want, therefore to outline what I believe are the proper responses at this time.

Now, clearly, the first response indicated is a surplus in the Federal budget.

The budget that has been presented by the administration projects a budget surplus for the fiscal year 1963.

I must confess to some doubts on this important point. I have spelled these out in my statement, Mr. Chairman, and I shall not do so here, except, in summary, to say that I am a little concerned that the estimates of revenue on which the budget surplus is premised are, I am afraid, a bit on the optimistic side. I should say over-optimistic.

I would point out also that there are some matters on the expenditure side that may prove to be troublesome. The budget contemplates that the deficit in the Post Office Department will be eliminated by an increase in postal rates.

I am very hopeful that the Congress will respond affirmatively to a proposal for increased rates which will put our Post Office Department on a self-supporting basis. I have never felt that the Post Office Department of this country was an area within which we ought to be running a large deficit. A deficit that runs well over a half a billion dollars a year and threatens to reach a billion dollars a year seems to me entirely indefensible.

I am afraid, however, that the postal rate increases that have been suggested may prove to be insufficient to eliminate that deficit, if what I read about moves for higher pay in the Post Office Department should be responded to affirmatively by the Congress.

I am not commenting here, Mr. Chairman, on the merits of Post Office pay increases. I am simply saying that the Post Office Department is not an area of our Government in which we ought to be operating at a very large deficit, and I fear that unless the rates are increased by more than has actually been requested in the President's budget it may prove to be exactly that.

Second, I see that the budget contemplates a reduction of nearly a half a billion dollars in the expenditures of the Department of Agriculture.

I have said, I trust the committee will not think facetiously, that while we can all hope for pleasant surprises and maybe even for miracles, the budget of the Department of Agriculture is not the place to look for them.

That budget has involved higher and higher expenditures year after year. I would point out that the increase in expenditures last year was close to a billion dollars.

It may be that we are to be treated now to a reversal of that trend. I hope so, and I think that this would be met with favor by our farm families.

It will require, however, a very deep revision, a very profound revision, in our approach to farm policy.

Finally, I must say I am a little concerned that the budget may have underestimated expenditures for interest on the public debt. Certainly if it proves to be a deficit budget rather than a surplus budget, as I think there is danger that it may, and if, as I expect they will, interest rates rise in the period ahead, we may find that the increased expenditures for interest may prove to be insufficient.

Here I think it is well to point out again—I think this is something that the citizens of our country now and then lose sight of—that expenditures in the budget for interest on the public debt stand now just under $10 billion a year.

Now, Mr. Chairman, there is another aspect of the budget to which I would like to refer briefly; and that concerns the level of Federal expenditures.

Much discussion of the budget and its effect on our economy runs in terms of whether there is a surplus or a deficit. I do not say that this is unimportant. It is important. But it is also important to consider the level of Federal expenditures; and in particular the changes in that level from year to year.

And I would point out that the expenditures proposed in the fiscal 1963 budget exceed those of fiscal 1962 by almost $3½ billion, and that this follows an increase in Federal spending between fiscal 1961 and 1962 of about $7.6 billion. In other words, in this 2-year span we have raised our Federal expenditures by more than $11 billion.

This is a very large increase in any budget, balanced or not, and it presents a situation that warrants the closest attention by the Congress. We must all ask ourselves whether this trend is to be extended very far into the future.

It is clearly not a trend that is consistent with improvement in our international economic position. Quite the opposite. If it does continue, it will have to be supported by a substantial increase in taxation.

Now let me turn to monetary policy.

Here I would judge that the administration seems broadly satisfied with money policy this year. I share that view. I think the policy has been pretty well attuned to our international economic and financial needs, as well as serving our domestic interests.

I must say, however, Mr. Chairman—and here I will just summarize my statement very briefly—I have some reservations about the statement in the President's Report in which he said that monetary policy in 1962 would require "continued ingenuity in technique and flexibility in emphasis."

I think I agree with this; though I am not entirely sure what it means. But I would be happier if the President had said that in 1962, with a good recovery under way, monetary policy would be quite studiously directed toward helping to achieve the significant improvement in our balance-of-payments position which we very much need.

Now, on the proposals that have been made for actions growing out of the report of the Commission on Money and Credit, I should like to say, Mr. Chairman, that I think it would be very wise to set up the interagency groups that the President proposes to go forward with.

I must, indeed, register my dismay at the President's proposal to amend the Federal Reserve Act to make the term of office of the Chairman of the Board of Governors of the Federal Reserve System coterminous with the 4-year term of the Presidency. The present arrangement is as the President has described it, "accidental and inadvertent." But this is not to say that it is not a good arrangement. Some of the best arrangements we have are accidental and inadvertent, but have proved, in the test of time, to be good ones.

The principle that should guide us, it seems to me, in these matters is that our central banking system should be in the hands of men who are both technically competent and who will perform their vitally important duties without reference to political considerations.

I believe the present arrangement affords greater assurance of achieving these ends than would the arrangement which the President desires. Under our system of Government, the President heads a political party, and he is pledged to give effect to a political program, adopted in a party convention. How could a nonpolitical administration of our central banking functions be maintained under a system which would virtually guarantee a change in the chairmanship with every change in the Presidency and would time this change so as to occur in the atmosphere of our most partisan political discussion?

Speaking quite respectfully, I must say that this would be, in my judgment, a very great mistake.

I will turn now, Mr. Chairman, if I may, to the question that is brought up in the Council's report having to do with wage policy.

They have stated a general guide for noninflationary wage policy, or wage behavior, which is the familiar proposition that wage increases are noninflationary if they are in line with overall productivity increases.

I have favored this guideline myself in the past. I agree wholly with the Council's analysis of it.

I feel, however, that in the present international context what we need is not merely stability of price levels, which this policy would give some assurance of producing, but a significant reduction in prices.

The right guideline at this time is one under which wage advances would be kept well within the limits of productivity improvements, not made to equal those improvements. This would leave room for significant price reductions, which are precisely what we need to improve our international competitive capability.

I have then commented in my statement on my own experiences, Mr. Chairman, when I was in Europe last summer and the experiences that I had all around the world in the course of a long trip which my wife and I took during last year. I have pointed out that it seemed to me when I was in Europe that increases in wage rates there and possibly some slowing down in the rate of their productivity improvement might give us in the United States, a chance if we keep our own affairs in order to significantly improve our competitive position. And I think that opportunity still exists. But I must say that since I have returned home I have not seen very much to give me comfort that we will in fact do this.

I have referred in my testimony to the settlement of the electricians' strike in New York City by granting $4.96 an hour for a 5-hour day, which is better than a 10-percent increase, and apparently guaranteeing a sixth hour at $7.44 an hour, also a 10-percent increase, and have described this as so completely unsuited to our national needs at this time as to be almost unbelievable.

I do not like to see Government intervening in the settlement of industrial disputes, but it does seem to me that this would have been a good one in which to have taken a hand.

Surely we must all understand that this is not a pattern, not even the shadow of a pattern, that we can safely follow as a Nation in matters of hours and wages.

I should like to suggest, Mr. Chairman, that I think this matter of wage advances, productivity improvements, and hours of work are so important that I should like to see this committee put them very high on its agenda for the year 1962.

I gather that the President's Commission appointed to consider these questions has submitted an inconclusive report. And I would take it, also a divided report. This is unfortunate. This seems to me to be the kind of question which should be before this committee, and I strongly urge that you consider special hearings on it in the coming year.

Finally, Mr. Chairman, I should like to comment on the suggestions that have been made to give discretionary authority to the President—to extend the period of unemployment compensation, change individual income tax rates, and increase expenditures on Federal public works.

Let me speak first of the proposal to extend the period of unemployment compensation. I like this proposal. I am far from sure, however, that an extension of benefits should be made automatic upon reaching a 5-percent unemployment level. I would rather see it made altogether discretionary with the President; though he will, of course, wish to have appropriate nonstatutory guidelines to follow.

This is a proposal with which we have had experience. It has worked well. It is my idea of the near-perfect counter-recessionary measure.

I am by no means persuaded, however, that the proposal which would permit Presidential initiative in individual income tax changes is a wise one.

I am less concerned about that part of the recommended legislation under which the President would make recommendations to the Congress that would take effect 30 days later, unless rejected by a joint resolution, than I am about that part which would give the President the right to make temporary tax reductions, when the Congress is not in session, with extensions subject to congressional veto.

From a purely administrative point of view, I do not see how this could fail but produce much confusion; and I also have doubts about the proposal on more strictly economic grounds.

Unlike the unemployment compensation proposal, we have had no experience with tax reduction as an antirecession measure. I do not regard the tax reduction in 1954, which accompanied a substantial drop in Federal expenditures made possible by the ending of war in Korea, as a conclusive test of the need for, or the efficacy of, individual income tax reduction for counterrecessionary purposes.

And, as we know, recovery from recession was accomplished in 1958 and again in 1961 without recourse to personal income tax reduction. There were influential voices calling for tax reduction in 1958 and again in 1961, and it should be instructive to note that these were heard even after there were signs of a recovery to come, and in some cases even after recovery had already started.

It is not easy to withhold one's hand in such situations, but there are times when it is best to do so. I am afraid that the proposed legislation would invite situations in which taxes would be reduced when it was not really timely or beneficial to do so.

I strongly feel, as I have stated on earlier occasions before this committee, Mr. Chairman, that I should like if possible to see tax reduction saved for situations in which they can be used to make significant improvements in the structure of our tax system and lasting reductions in the tax burden, not employed during recession in what could very well be ineffective ways.

Finally, I also have, Mr. Chairman, reservations about the proposal to give the President standby authority to increase Federal expenditures on capital improvements up to as much as $2 billion. The guidelines proposed are altogether too loose, it seems to me, but apart from that, I would object to the proposal on the grounds that it is not needed and that it is unlikely to be truly effective as an antirecession measure.

This is another matter on which we have had a good deal of experience. I would say that that experience teaches two lessons. The first is that there is a good deal of leeway for increasing construction expenditures under our present arrangements. The second is that increases in expenditures intended to counter recession normally do not become effective until well after a recovery is underway.

I would much rather see us committed to a steady level of capital improvements, wisely selected for their national benefit, and pitched at just as high a level as our resources will reasonably permit.

For various reasons, I do not like off-again, on-again construction programs. I think our economy and our public interest are benefited most by steady, assured public construction programs. I think we would be better off, Mr. Chairman, to continue under our present arrangements.

I offer these as my suggestions for public and private policy responses suitable to our present international economic and financial position.

May I just add one word, that I do like, Mr. Chairman, the proposal that has been made for an investment tax credit. It is only an oversight that accounts for it not having been noted in my prepared statement.

Thank you very much, sir.

Senator SPARKMAN. Thank you very much, Dr. Saulnier.

Dr. Edward M. Bernstein, Bernstein & Associates.

Doctor, we are glad to have you with us, and you may proceed as you see fit.

You understand, of course, that your paper will be printed in full.

STATEMENT BY DR. EDWARD M. BERNSTEIN, EMB (LTD.) RESEARCH ECONOMISTS, WASHINGTON, D.C.

Dr. BERNSTEIN. Mr. Chairman, I have a truncated version of this paper which I might read, which might be helpful, and will highlight the points in any case.

Senator SPARKMAN. Very well, sir.

(Mr. Bernstein's prepared paper follows:)

STATEMENT OF EDWARD M. BERNSTEIN, EMB (LTD.) RESEARCH ECONOMISTS, ON TWO BASIC PROBLEMS OF THE U.S. ECONOMY

The U.S. economy has made a satisfactory recovery from the mild recession of 1960–61. The real test of the strength of the economy, however, will come in 1962 and 1963. In 1954–57, nearly three-fourths of the increase in industrial production and in the gross national product at constant prices, and in 1958–59 more than four-fifths of the increase, occurred in the first 12 months of the expansion. Unless we do substantially better in 1962 and 1963 than in the two previous cycles, the level of unemployment will remain excessively high, even at the peak of business activity; and production will not reach the levels that would be justified by our economic potential. To achieve the objectives of the Employment Act of 1946, we must solve two basic problems: first, restoring the U.S. balance of payments; and second, accelerating the growth of the U.S. economy.

I. BALANCE-OF-PAYMENTS DEFICIT

The United States is confronted with a difficult balance-of-payments problem. This is not a problem on the fringe of the economy, important only to bankers and economists. The balance-of-payments deficit is closely related to the basic problems of the economy, the excessive level of unemployment and the inadequate rate of growth. The strengthening of the U.S. balance of payments would contribute directly to an increase in employment and it would facilitate the taking of other measures to encourage the expansion and growth of production.

The balance-of-payments deficit of the United States was $3.9 billion in 1960 and about $2.5 billion in 1961. If the balance-of-payments deficit were eliminated by increasing U.S. exports relative to imports, there would be a significant increase in production and employment in this country. One of the reasons why the unemployment rate was higher at the peak of the expansion in 1960 than in 1957 is that net exports of goods and services were at an annual rate of $6 billion (1.37 percent of the gross national product) in the first quarter of 1957 and at an annual rate of $1.8 billion (0.39 percent of the gross national product) in the first quarter of 1960. If net exports had been as high, relative to the gross national product, the rate of unemployment in February 1960 would have been about the same as in 1957—that is, 4 percent.

Capital movements and the deficit

A considerable part of the balance-of-payments deficit is attributable to the outflow of U.S. funds for short-term investment abroad. For the 2 years 1960 and 1961, the recorded and unrecorded outflow of such funds is estimated at about $4.8 billion. The point has been made that the method of presenting the U.S. balance of payments is asymmetrical, that it includes as a payment the outflow of private U.S. short-term funds but does not include as a receipt the inflow of foreign private funds.[1] According to this view, the United States should not be too much concerned with its overall balance of payments, if it can restore its basic payments position; that is, a balance on commercial trade, other services, private long-term capital, and Government expenditures and aid.

While it is important to distinguish the factors that cause the payments deficit. it would be a mistake to ignore the short-term capital movements. The Commerce Department statement of the balance of payments is designed to show the effect of our foreign receipts and expenditures on our reserve position. For this purpose, it regards the net payments position as equal to the change in U.S. holdings of gold and convertible currencies and the change in U.S. short-term and liquid liabilities to foreigners. This is asymmetrical, because short-term banking assets and liabilities are treated differently. The distinction is justi-

[1] In this connection, it should be noted that the claims of U.S. banks on foreigners increased by about $2 billion in 1960 and 1961.

fied and is based on a definition of reserves similar to that in the Articles of Agreement of the International Monetary Fund.[2]

There are some points regarding U.S. private short-term capital outflow that must be emphasized. First, an important financial center like the United States should regard a reasonable outflow of short-term funds as part of the function it performs in financing international trade and payments in all parts of the world. Second, an abnormal outflow of short-term funds and the conversion of dollars into gold can be limited by interest rate policy. Even if one were willing to overlook the effect of short-term capital movements on U.S. short-term and liquid liabilities to foreigners, it is impossible to disregard the steady reduction of the U.S. gold reserves which has amounted to $6 billion in the past 4 years.

Interest rates and capital movements

We must solve our payments problem in two ways: First, by reducing the outflow of short-term funds; second, by strengthening our basic balance of payments. The outflow of funds is affected by interest rates in the United States and in other important financial centers. In the past few years, differences in short-term interest rates have generally become larger, with money market rates higher in a number of European countries than in the United States. As many Western European countries have a strong payments position, with large reserves and convertible currencies, the higher rates induce a movement of funds from the United States for interest arbitrage. The United States can no longer maintain short-term interest rates substantially below those in Western Europe.

Since 1958, interest rates in the United States have risen considerably. Some critics of the Federal Reserve say this is due to a tight money policy. The facts do not bear this out. The availability of credit in the United States, as measured by the free reserves of member banks, has been easier from 1959 to the present than in the corresponding phases of the cycle in 1957 and 1958. On a daily average basis, free reserves in June 1957 were minus $508 million (member bank borrowings $1,005 million, excess reserves $496 million). In January 1960, when interest rates were highest, free reserves were minus $361 million (member bank borrowings $905 million, excess reserves $544 million). In May 1958, free reserves (the highest monthly level in the recession) were $547 million. In January 1961, the last month of the previous recession, free reserves were $696 million.

Short-term interest rates were 2¼ to 2¾ percent in 1960–61, not because the Federal Reserve provided less free reserves than in the past, but because other basic factors are causing higher short-term interest rates. One factor is the greater attractiveness of foreign money markets. U.S. corporations that held $23.5 billion in U.S. Government securities in the fourth quarter of 1959 held only $18.4 billion in the third quarter of 1961. Another factor is the widespread view that the upward trend of long-term interest rates has come to an end. We may be on a new plateau of interest rates with moderate cyclical fluctuations. Under such conditions, differences between short-term and long-term interest rates will not be as large as formerly and money market rates cannot fall to 1 percent as they did in earlier recessions.

The Federal Reserve authorities and the Treasury wanted short-term rates to stay up in order to minimize the impact on international capital movements. In my opinion, they could not have brought down short-term rates significantly without extreme measures. If the Federal Reserve had increased bank reserves by another $400 million, the effect on interest rates would have been minimal because the outflow of short-term funds would have been that much larger.

Role of fiscal and credit policy

The importance of short-term capital movements in our balance of payments requires a clearer understanding of different aspects our our financial policy. A budget deficit in a period of recession has a large effect on aggregate demand, but only a small effect on the balance of payments. A budget deficit of $6 billion may increase the gross national product by the same amount or more. It will increase imports by about $200 million—say, 3 percent of the increase in the gross national product. On the other hand, the forcing down of short-term interest rates by a very large increase in reserve credit can lead to a capital outflow

[2] The Fund agreement states: "A member's monetary reserves shall be calculated by deducting from its central holdings (of gold and convertible currencies) the currency liabilities to the treasuries, central banks, stabilization funds, or similar fiscal agencies * * * together with similar liabilities to other official institutions and other banks in the territories of members * * *" (art. XIX(e)).

of as much as $2 billion. We can afford a budget deficit in a recession, when the cyclical conjucture is favorable to the U.S. balance of payments. We cannot afford excessively low short-term interest rates, even in recession, because our balance of payments is too sensitive to capital movements.

This does not mean that the role of credit policy in the business cycle has been seriously hampered. There is a good deal that the monetary authorities can do to restrain inflation during a boom and to encourage recovery during a recession through a flexible credit policy. That policy cannot ignore what is happening in foreign money markets. It is a great step forward to have the leading industrial countries consult in the Organization for Economic Cooperation and Development. No country need give up the right to an independent monetary policy; but all must apply their policies within reasonable limits. That means that a country cannot resort to very low-interest rates in a recession because of the effect on its own balance of payments or to very high interest rates in a boom because of the effect on the balance of payments of other countries.

Flexible monetary policy is and will remain an important and effective instrument for achieving economic objectives. It will have to be supplemented by other measures to guide the economy and to keep the balance of payments in order. Countries can still have moderately low money rates in a recession and moderately high rates in an expansion or in a period of payments difficulties. This will permit large capital movements in response to interest rate differentials; but they can be financed, if they reach massive proportions, through the supplementary resources being provided for this purpose through the International Monetary Fund.

Basic balance of payments

Although short-term capital movements have been a large factor in our payments deficits, the fact is that our basic balance of payments is too weak. The pressure on our balance of payments arises to a considerable extent from the enormous burden imposed on us by our political commitments abroad. Our military expenditures, our military aid, our economic aid and long-term investment are essential for the freedom of the Western World. We cannot reduce our commitments, but it would help if our strong and prosperous allies in Western Europe would assume a greater share of the common burden of defense and aid. This would ease the U.S. balance-of-payments problem, but it cannot solve it.

The fact is we must restore our balance of payments. This is not a responsibility any country can shift to others. We must improve our overall balance of payments by $2.5 billion a year. It will help to strengthen our balance of payments if a more favorable environment is created for world trade. The key to this is the lowering of trade barriers in the Common Market against industrial and agricultural imports. The Common Market owes the rest of the world a unilateral reduction in its tariffs and other restrictions to offset the adverse effect of the greater preferences to its members and to the associated states in Africa. Beyond that, there should be a reciprocal reduction of tariffs in the Common Market, in the United States, and in other industrial countries to increase world trade and to broaden the markets of the low-income countries.

A better environment for world trade will create an opportunity to increase our exports. To succeed, the United States must be able to supply export goods on a competitive basis. We weakened our competitive position in the heavy goods industries by letting our prices rise at a time when the great industrial countries of Europe were expanding their capacity to produce and export. We must now make a special effort to hold down our prices and costs. The Annual Report of the Council of Economic Advisers has a useful discussion of the guideposts for noninflationary wage and price behavior.

"The general guide for noninflationary wage behavior is that the rate of increase in wage rates (including fringe benefits) in each industry be equal to the trend rate of overall productivity increase. General acceptance of this guide would maintain stability of labor cost per unit of output for the economy as a whole—though not, of course, for individual industries.

"The general guide for noninflationary price behavior calls for price reduction if the industry's rate of productivity increase exceeds the overall rate—this would mean declining unit labor costs; it calls for an appropriate increase in price if the opposite relationship prevails; and it calls for stable prices if the two rates of productivity increase are equal."

The Council gives four modifications to these general principles to encourage the adjustment of jobs to the labor supply and of capital to the needs of industry. Unfortunately, the Council does not discuss the wage and price policy necessitated by our large and persistent balance-of-payments deficit. The proper policy for the United States at this time is to have wage rates rise somewhat less than productivity in the export-import industries and to have prices of export-import goods fall partly with the increase in productivity. Unless labor unions and industrial corporations are prepared to accept this wage and price policy until our payments position is restored, the payments deficits will weaken our economy and prevent us from maintaining a high level of production and employment.

II. STRENGTHENING THE DOMESTIC ECONOMY

The economy of this country has failed to realize the potential of which it is capable. The rate of economic growth in the past 10 years has been inadequate. The simplest proof of this is that the economy has not expanded enough to provide jobs for our growing labor force. In each successive cycle, the rate of unemployment at the peak of expansion has been greater than in the preceding cycle. In each successive recession, the recovery from unemployment has been slower and the number of persons unemployed for long periods of time has become larger.

In one sense, this is a cyclical problem. It is necessary to explain why the expansion phase of the cycle does not last long enough or rise high enough to enable the economy to reach an acceptable level of employment—say, with an unemployment rate down to 4 percent at the peak of the cycle. In another sense, this is a problem of long-term growth. Obviously, if employment would increase at the same rate as the labor force, then with the same increase in productivity per man-hour, the growth in total output would be greater. And if the increase in employment were relatively greater in the high output industries, the average increase in productivity per man-hour would also increase.

Output of durable goods industries

The principal reason for the unsatisfactory performance of the economy is to be found in the relative decline in the demand for the output of the durable goods industries. The decline in relative demand has been pervasive—in our export markets and in our domestic markets; for consumer durable goods, for business equipment, and for defense materiel. Final domestic purchases of durable goods by consumers, producers, and Government have tended to be a much smaller proportion of the gross national product since 1950–52. No other major sector of the economy has shown such a small, and a declining, rate of growth as the durable goods industries in which the United States is commonly thought to have greater comparative advantages than in other industrial sectors.

Industrial production, durable manufactures, and business equipment, 1952–61

[Federal Reserve index, 1957=100]

Year	Industrial production	Durable manufactures	Business equipment
1952	83.8	85.1	89.4
1953	90.8	96.0	91.8
1954	85.4	85.0	80.8
1955	96.0	97.9	87.2
1956	99.3	100.0	99.4
1957	100.0	100.0	100.0
1958	92.9	86.8	85.2
1959	104.9	101.5	99.6
1960	108.0	104.3	104.7
1961	109.1	103.1	105.0
1961 increase over 1952 (percent)	30.1	21.1	17.4

An examination of the Federal Reserve index of industrial production and some of its constituent series will show the extent to which the rate of growth has declined in the past 10 years. The slower growth is marked in durable goods and particularly in business equipment. While any comparison between 1952 and 1961 is subject to the qualification that the 2 years were not in the same phase of the business cycle, the results would not be different if a comparison were made between 1952 and 1959, when the cyclical situation was similar. From 1952 to 1961, industrial production increased by 30.1 percent. The increase in durable goods manufactures in the same period was 21.1 percent, and the increase in the production of business equipment was only 17.4 percent. Machinery and equipment, therefore, are one sector, and a key sector, in which the lag in output has held back the growth of the entire economy.

Investment in producers' durable equipment

The inadequate growth in the output of business equipment is directly attributable to the fact that investment in producers' durable equipment has failed to keep pace with the growth of the economy as a whole. In dollar value, expenditures on producers' durable equipment reached a peak in 1957, when they amounted to $28.5 billion. Between 1951 and 1961, the largest proportion of aggregate expenditures going into investment in producers' durable equipment was in 1956, when it was 6.49 percent of the gross national product. The ratio, in current dollars, has declined steadily since then and it was 4.95 percent of the gross national product in 1961. As prices of equipment goods have risen more in recent years than the price level of output as a whole, the ratio of investment in producers' durable equipment to the gross national product in constant dollars fell to 4.72 percent in 1961. At the peak of the expansion in the second quarter of 1960, the volume of investment in producers' durable equipment was 8 percent lower than in the fourth quarter of 1956, the peak of the previous cycle, nearly 4 years earlier.

Gross national product and investment in producers' durable equipment, 1952–61

Year	Billion dollars		Ratio, percent	
	GNP	Equipment	Current dollars	Constant dollars
1951	329.0	21.3	6.47	6.44
1952	347.0	21.3	6.14	6.15
1953	365.4	22.3	6.10	6.10
1954	363.1	20.8	5.73	5.73
1955	397.5	23.1	5.81	5.73
1956	419.2	27.2	6.49	6.24
1957	442.8	28.5	6.44	6.02
1958	444.5	23.1	5.20	4.83
1959	482.8	25.9	5.36	4.97
1960	504.4	27.5	5.45	5.14
1961	521.2	25.8	4.95	4.72

An increase of investment in machinery and equipment would contribute to the solution of both the cyclical problem of increasing production and employment and to the longer run problem of accelerating growth in productivity and in total output. An increase in investment would stimulate a general expansion in the economy. As the equipment industries are the high output industries, an increase in the proportion of the gross national product devoted to such investment would raise the average output per worker. And as the newly equipped industries would produce more efficiently, they would be better able to compete in world markets. One reason, although not the only reason, why production has been growing faster in Europe than in the United States is that their industries were thoroughly reequipped and modernized in the course of the past decade. If American industry could be induced to increase its investment in new equipment, the U.S. economy would be strengthened and its growth would be accelerated.

Increasing investment in machinery and equipment

The considerations that determine new investment are exceedingly complex. The factors that must be taken into account are the prospective demand for output, the prices at which the goods can be sold, and the costs at which they can be produced. Even when there is no expectation of a substantial increase in demand, old equipment is replaced by new when the technical efficiency is so much greater than the labor, capital and other costs of producing with the new equipment are less than the out-of-pocket costs of producing with the old equipment. This may be put simply in these broad terms: it pays to undertake investment in new equipment when the gross annual investment return (the cash flow) is greater than the gross annual investment cost (interest and depreciation).

Economic policy is concerned with encouraging investment both through a rise in the investment return and a fall in the investment cost. Measures to increase aggregate demand have the effect of increasing the investment return from new equipment. Measures can also be taken to reduce the gross annual investment cost of new equipment. One way is through lower long-term interest rates. There are differences of opinion as to the effectiveness of lower interest rates, under given conditions of demand for output, in stimulating new investment. In any case, it is not feasible to reduce interest rates at this time. There are other ways, and more effective ways, of reducing the gross annual investment cost. The proposals for encouraging investment through a tax credit or through accelerated depreciation can be analyzed in terms of reducing the price of capital equipment and the gross annual investment cost.

If an 8-percent tax credit is given for investment in machinery and equipment, the effect of the credit is to reduce the cost to the investing firm of any machinery and equipment qualifying for the credit by 8 percent. Given the rate of interest and the schedule of depreciation, the gross annual investment cost will be reduced proportionately. The effectiveness of such a measure can be seen from a comparison of this reduction in gross annual investment cost with that resulting from a reduction in interest rates. A tax credit of 8 percent would have the same effect on gross annual investment cost as a reduction of interest rates from 5 percent to 2 percent for equipment with a 5-year life, from 5 percent to 3 percent for equipment with a 10-year life, and from 5 percent to 4 percent for equipment with a 20-year life. This can be seen by reducing by 8 percent the gross annual investment cost for the three classes of equipment at a 5-percent interest rate in the table below and finding the lower interest rate with an equivalent gross annual investment cost.

Gross annual investment cost as percent of price of capital equipment

Interest rate	Annual cost of interest and depreciation for equipment of—[1]		
	5-year life	10-year life	20-year life
2 percent	21.22	11.13	6.12
3 percent	21.84	11.72	6.72
4 percent	22.46	12.44	7.36
5 percent	23.10	12.95	8.02
6 percent	23.74	13.59	8.72

[1] Depreciation is calculated on a sinking-fund (compound interest) basis.

Source: E. M. Bernstein, "Wage Rates, Investment, and Employment," Journal of Political Economy April 1939, p. 230.

Accelerated depreciation is another means of reducing the gross annual investment cost of machinery and equipment. If a firm investing in new equipment with an expected life of 20 years can accelerate the depreciation charges for this equipment, the capital cost will be returned in a shorter period and the true annual investment cost will be reduced. A firm saves payment of income taxes now on the accelerated portion of the depreciation; it will pay income taxes later on an equivalent amount. At a 52 percent income tax and 5 percent interest, if depreciation is accelerated from 20 to 10 years, the present value of the reduced taxpayments in the early period would be equal to 21.08 percent of the cost of the equipment. The present value of the additional income taxes to be paid in the last 10 years to offset the accelerated depreciation would be equal to 12.94 percent of the cost of the equipment. Thus, by accelerating depreciation from 20 to 10 years, the gross annual investment cost is reduced by 8.14 percent.

Present value of accelerated depreciation[1]

[Percent of original cost]

Normal length of life	Depreciation accelerated to—		
	5 years	10 years	15 years
20 years	13.26	8.14	3.76
15 years	9.50	4.38	
10 years	5.12		
	Percent of original cost written off		
	25 percent	50 percent	
20 years	4.49	8.99	
15 years	3.56	7.11	
10 years	2.46	4.93	
5 years	1.19	2.37	

1 Based on the assumption of an income tax rate of 52 percent and an interest rate of 5 percent to find the present value of future payments.

Some discussions of accelerated depreciation propose the immediate writeoff of a major portion of the cost of the equipment, the remainder being charged to depreciation according to the standard schedule. Actually, the present value of such a method of accelerating depreciation is not very large. If 25 percent of the cost of equipment were written off at once, and the remaining 75 percent were depreciated over 20 years, the present value of the accelerated depreciation, at a 52 percent income tax and 5 percent interest, would be equal to 4.49 percent of the cost of the equipment. If 50 percent of the cost were written off at once, and the remaining half were depreciated over 20 years, the present value of the accelerated depreciation would be equal to 8.99 percent of the original cost.

While the present value of the benefit of accelerated depreciation is not significantly different for acceleration from 20 years to 10 years or for a 50 percent writeoff on 20-year equipment than for an 8 percent tax credit, the effect on the finances of the Treasury is quite different. Accelerating depreciation from 20 years to 10 years would decrease tax revenues in the first 10 years and increase tax revenues in the last 10 years of the life of the equipment. On a continuous basis, the Treasury's tax revenues would be lower for the first 15 years of the plan and higher thereafter. It should be noted, however, that the decreased revenues because of the accelerated depreciation would be less than the decreased revenues because of the tax credit until the fourth year and that on a cumulative basis, total tax revenues would decrease more with the tax credit than with accelerated depreciation until the sixth year. On the whole, the revenue aspects of accelerating depreciation from 20 years to 10 years are more favorable for the Treasury than an 8 percent tax credit. On the other hand, a 50 percent writeoff for depreciation of equipment with a 20-year life would reduce tax revenues more than an 8 percent tax credit until the 14th year. The cumulative decrease over this period would be more than twice as much for a 50 percent writeoff than for an 8 percent tax credit.

The effect on the inducement to invest of these three alternative methods of reducing the gross annual investment cost is much the same. It is difficult to believe that their immediate impact on Treasury finance and on corporate finance is as significant as is sometimes assumed. On the whole, business firms may be better able to adjust their financing to a different rate of cash flow after taxes, the present value being the same, than the Treasury can adjust its financing to an increased deficit in the next few years combined with an increased surplus in the later future. Furthermore, the tax credit for investment in machinery and equipment should not preclude realistic revision of depreciation schedules. If Congress enacts such a tax credit, it would still be desirable for the Internal Revenue Service to revise the guides to depreciation to make them more suitable to the conditions of a world in which technical innovation is extremely rapid. Our economy has plenty of resources for providing U.S. industry with the most modern equipment. The best hope of increasing production and employment and of accelerating the growth of the U.S. economy is by encouraging more investment in machinery and equipment.

Dr. BERNSTEIN. The U.S. economy has made a satisfactory recovery from the mild recession of 1960–61. The real test of the strength of the economy, however, will come in 1962 and 1963. To achieve the objectives of the Employment Act of 1946, we must solve two basic problems: first, restoring the U.S. balance of payments; and second, accelerating the growth of the U.S. economy.

1. BALANCE-OF-PAYMENTS DEFICIT

The balance-of-payments deficit of the United States was $3.9 billion in 1960 and about $2.5 billion in 1961. If the balance-of-payments deficit were eliminated by increasing U.S. exports relative to imports, there would be a significant increase in production and employment in this country. One reason why the unemployment rate was higher at the peak of the expansion in 1960 than in 1957 is that the payments position deteriorated. If net exports had been as high, relative to the gross national product, the rate of unemployment in February 1960, would have been about the same as in 1957—that is, 4 percent.

A considerable part of the balance-of-payments deficit is attributable to the outflow of U.S. funds for short-term investment abroad. For the 2 years 1960 and 1961, the recorded and unrecorded outflow of such funds is estimated at about $4.8 billion. The point has been made that the method of presenting the U.S. balance of payments is asymmetrical, that it includes as a payment the outflow of private U.S. short-term funds but does not include as a receipt the inflow of foreign private funds. According to this view, the United States should not be too much concerned with its overall balance of payments, if it can restore its basic payments position—that is, a balance on commercial trade, other services, private long-term capital, and Government expenditures and aid.

While it is important to distinguish the factors that cause the payments deficit, it would be a mistake to ignore the short-term capital movements. First, an important financial center like the United States should regard a reasonable outflow of short-term funds as part of the function it performs in financing international trade and payments in all parts of the world. Second, an abnormal outflow of short-term funds and the conversion of dollars into gold can be limited by interest rate policy. Even if one were willing to overlook the effect of short-term capital movements on U.S. short-term and liquid liabilities to foreigners, it is impossible to disregard the steady reduction of the U.S. gold reserves which has amounted to $6 billion in the past 4 years.

We must solve our payments problem in two ways: first, by reducing the outflow of short-term funds; second, by strengthening our basic balance of payments. The outflow of funds is affected by interest rates in the United States and in other important financial centers. In the past few years, differences in short-term interest rates have generally become larger, with money market rates higher in a number of European countries than in the United States. As many Western European countries have a strong payments position, with large reserves and convertible currencies, the higher rates induce a movement of funds from the United States for interest arbitrage. The United States can no longer maintain short-term interest rates substantially below those in Western Europe.

Since 1958, interest rates in the United States have risen considerably. Despite this, the availability of credit in the United States, as measured by the free reserves of member banks, has been easier from 1959 to the present than in the corresponding phases of the cycle in 1957 and 1958. Short-term interest rates were 2¼ to 2¾ percent in 1960–61, not because the Federal Reserve provided less free reserves than in the past, but because other basic factors are causing higher short-term interest rates. One factor is the greater attractiveness of foreign money markets. Another factor is the widespread view that the upward trend of long-term interest rates has come to an end. Under such conditions, differences between short-term and long-term interest rates will not be as large as formerly and money market rates cannot fall to 1 percent as they did in earlier recessions.

The importance of short-term capital movements in our balance of payments requires a clearer understanding of different aspects of our financial policy. A budget deficit in a period of recession has a large effect on aggregate demand, but only a small effect on the balance of payments. A budget deficit of $6 billion may increase the gross national product by the same amount or more. It will increase imports by about $200 million—say, 3 percent of the increase in the gross national product. On the other hand, the forcing down of short-term interest rates by a very large increase in reserve credit can lead to a capital outflow of as much as $2 billion. We can afford a budget deficit in a recession, when the cyclical conjuncture is favorable to the U.S. balance of payments. We cannot afford excessively low short-term interest rates, even in recession, because our balance of payments is too sensitive to capital movements.

This does not mean that the role of credit policy in the business cycle has been seriously hampered. There is a good deal that the monetary authorities can do to restrain inflation during a boom and to encourage recovery during a recession through a flexible credit policy. That policy cannot ignore what is happening in foreign money markets. It is a great step forward to have the leading industrial countries consult in the Organization for Economic Cooperation and Development. No country need give up the right to an independent monetary policy; but all must apply their policies within reasonable limits. Countries can still have moderately low money rates in a recession and moderately high rates in an expansion or in a period of payments difficulties. This will permit capital movements in response to interest rate differentials; but they can be financed, if they reach massive proportions, through the supplementary resources being provided for this purpose through the International Monetary Fund.

Although short-term capital movements have been a large factor in our payments deficits, the fact is that our basic balance of payments is too weak. The pressure on our balance of payments arises to a considerable extent from the enormous burden imposed on us by our political commitments abroad. Our military expenditures, our military aid, our economic aid and long-term investment are essential for the freedom of the Western World. We cannot reduce our commitments, but it would help if our strong and prosperous allies in Western Europe would assume a greater share of the common burden of defense and aid. This would ease the U.S. balance-of-payments problem, but it cannot solve it.

The fact is we must restore our balance of payments. This is not a responsibility any country can shift to others. We must improve our overall balance of payments by $2.5 billion a year. Much the greater part of this will have to come from an increase in exports relative to imports. It will help to strengthen our balance of payments if a more favorable environment is created for world trade. The key to this is the lowering of trade barriers in the Common Market against industrial and agricultural imports. The Common Market owes the rest of the world a unilateral reduction in its tariffs and other restrictions to offset the adverse effect of the greater preferences to its members and to the associated states in Africa. Beyond that, there should be a reciprocal reduction of tariffs in the Common Market, in the United States, and in other industrial countries to increase world trade and to broaden the markets of the low-income countries.

A better environment for world trade will create an opportunity to increase our exports. To succeed, the United States must be able to to supply export goods on a competitive basis. We weakened our competitive position in the heavy goods industries by letting our prices rise at a time when the great industrial countries of Europe were expanding their capacity to produce and export. We must now make a special effort to hold down our prices and costs. The Annual Report of the Council of Economic Advisers has a useful discussion of the guideposts for noninflationary wage and price behavior. Unfortunately, the Council does not discuss the wage and price policy necessitated by our large and persistent balance of payments deficit. The proper policy for the United States at this time is to have wage rates rise somewhat less than productivity in the export-import industries and to have prices of export-import goods fall partly with the increase in productivity. Unless labor unions and industrial corporations are prepared to accept this wage and price policy until our payments position is restored, the persistent payments deficits will weaken our economy and prevent us from maintaining a high level of production and employment.

II. STRENGTHENING THE DOMESTIC ECONOMY

The economy of this country has failed to realize the potential of which it is capable. The rate of economic growth in the past 10 years has been inadequate. The simplest proof of this is that the economy has not expanded enough to provide jobs for our growing labor force. In each successive cycle, the rate of unemployment at the peak of expansion has been greater than in the preceding cycle. In each successive recession, the recovery from unemployment has been slower and the number of persons unemployed for long periods of time has become larger.

The principal reason for the unsatisfactory performance of the economy is to be found in the relative decline in the demand for the output of the durable goods industries. The decline in relative demand has been pervasive—in our export markets and in our domestic markets. Final domestic purchases of durable goods by consumers, producers, and Government have tended to be a much smaller proportion of the gross national product since 1950–52. No other major sector of the economy has shown such a small rate of growth as the durable goods industries in which the United States is commonly thought to have greater comparative advantages than in other industrial sectors.

From 1952 to 1961, industrial production increased by 30.1 percent. The increase in durable goods manufactures in the same period was 21.1 percent, and the increase in the production of business equipment was only 17.4 percent. Machinery and equipment, therefore, are one sector, and a key sector, in which the lag in output has held back the growth of the entire economy. The inadequate growth in the output of business equipment is directly attributable to the fact that investment in producers' durable equipment has failed to keep pace with the growth of the economy as a whole. In dollar value, expenditures on producers' durable equipment reached a peak in 1957, when they amounted to $28.5 billion. Between 1951 and 1961, the proportion of aggregate expenditures going into investment in producers' durable equipment fell from 6.47 to 4.95 percent of the gross national product. At the peak of the expansion in the second quarter of 1960, the volume of investment in producers' durable equipment was 8 percent lower than in the fourth quarter of 1956, the peak of the previous cycle, nearly 4 years earlier.

An increase of investment in machinery and equipment would contribute to the solution of both the cyclical problem of increasing production and employment and to the longer run problem of accelerating growth in productivity and in total output. An increase in investment would stimulate a general expansion in the economy. As the equipment industries are the high output industries, an increase in the proportion of the gross national product devoted to such investment would raise the average output per worker. And as the newly equipped industries would produce more efficiently, they would be better able to compete in world markets. If American industry could be induced to increase its investment in new equipment, the U.S. economy would be strengthened and its growth would be accelerated.

The considerations that determine new investment are exceedingly complex. The factors that must be taken into account are the prospective demand for output, the prices at which the goods can be sold, and the costs at which they can be produced. Even when there is no expectation of a substantial increase in demand, old equipment is replaced by new when the technical efficiency is so much greater that the labor, capital and other costs of producing with the new equipment are less than the out-of-pocket costs of producing with the old equipment. This may be put simply in these broad terms: It pays to undertake investment in new equipment when the gross annual investment return (the cash flow) is greater than the gross annual investment cost (interest and depreciation).

Economic policy is concerned with encouraging investment both through a rise in the investment return and a fall in the investment cost. Measures to increase aggregate demand have the effect of increasing the investment return from new equipment. Measures can also be taken to reduce the gross annual investment cost of new equipment. One way is through lower long-term interest rates. There are differences of opinion as to the effectiveness of lower interest rates, under given conditions of demand for output, in stimulating new investment. In any case, it is not feasible to reduce interest rates at this time. There are other ways, and more effective ways, of reducing the gross annual investment cost. The proposals for encouraging investment through a tax credit or through accelerated depreciation can be analyzed in terms of reducing the price of capital equipment and the gross annual investment cost.

If an 8-percent tax credit is given for investment in machinery and equipment, the effect of the credit is to reduce the cost to the investing firm of any machinery and equipment qualifying for the credit. A tax credit of 8 percent would have the same effect on gross annual investment cost as a reduction of interest rates from 5 percent to 2 percent for equipment with a 5-year life, from 5 percent to 3 percent for equipment with a 10-year life, and from 5 percent to 4 percent for equipment with a 20-year life. It is a much more powerful instrument than a reduction in interest rates.

Accelerated depreciation is another means of reducing the gross annual investment cost of machinery and equipment. If a firm investing in new equipment with an expected life of 20 years can accelerate the depreciation allowances for this equipment, it will save payment of income taxes now on the accelerated portion of the depreciation. It will pay income taxes later on an equivalent amount. At a 50-percent income tax rate, and 5-percent interest, the reduction in gross annual investment cost in accelerating depreciation from 20 years to 10 years is equal to 7.5 percent of the cost of the equipment. If depreciation is accelerated from 20 years to 5 years, the reduction in gross annual investment cost is equal to 17.23 percent of the cost of the equipment.

It is apparent that both a tax credit and accelerated depreciation would have a great effect in reducing the gross annual investment cost on new equipment. Public policy on these alternatives must take into consideration their impact on tax revenues and corporate finances. If Congress enacts a tax credit for investment in machinery and equipment, it would still be desirable to revise depreciation allowances to make them more suitable to the conditions of a world in which technical innovation is extremely rapid. Our economy has plenty of resources for providing U.S. industry with the most modern equipment. The best hope of increasing production and employment and accelerating the growth of the U.S. economy is by encouraging such investment.

Senator SPARKMAN. Thank you very much, Dr. Bernstein.

That completes the presentation of the papers for the panel, I believe.

I shall ask only a very few questions and then pass it on to other members of the committee.

Let me ask this question generally. I was not here for all of the papers. Mr. Gurley completed his paper before I came in.

Is there approval by all members of the panel of the 8-percent investment feature that was referred to by Dr. Bernstein and by Dr. Saulnier? Do the others agree with them with reference to that?

Dr. GURLEY. Senator Sparkman, I did not mention it in the statement that I gave, but I do.

Senator SPARKMAN. You do concur?

Dr. GURLEY. Yes.

Senator SPARKMAN. Dr. Musgrave, do you?

Dr. MUSGRAVE. Yes.

Senator SPARKMAN. Now, there was one other thing, the idea that Dr. Bernstein concluded on—more rapid depreciation. Are all of you agreed on that, as a principle?

Dr. MUSGRAVE. No.

Dr. SAULNIER. I am, sir, favorable disposed toward the reexamination of depreciation arrangements that is now going forward at the Treasury. I hope this eventuates in a significant liberalization of our depreciation regulations.

It is important, however, to remember that there is a difference between the depreciation allowance that is stated in the regulations and what has in effect been allowed in the course of day-to-day adjudications of these questions by the Internal Revenue examiners.

I get the impression, Mr. Chairman, that our depreciation policies have been significantly liberalized in the course of day-to-day adjustments by Internal Revenue examiners and are substantially more liberal than one would infer from a look at—what is it?—Bulletin 720, the bulletin on depreciation.

However, I would like to see a further liberalization.

Senator SPARKMAN. Yes, Doctor?

Dr. MUSGRAVE. May I add a word to this, Mr. Chairman?

The basic principle of the mater ought to be, and I think the Treasury has been right in taking this view, that we should have those depreciation provisions which give us the proper definition of income. This is a matter of properly defining profits for tax purposes. To do this, we ought to have depreciation which corresponds to the useful life of the asset.

Now I am quite in favor of going over the present depreciation schedules to see whether they are still suitable, to make adjustments where needed, where obsolescence has proved more rapid, where the nature of the machinery has changed; to make these changes, in some cases down, and where need be, up.

We should think of the depreciation schedule as giving a proper definition of income. We should not think of it as an investment incentive. Otherwise, we get completely fouled up in this basic question of defining taxable income.

When it comes to giving an investment incentive, I think that the depreciation approach is distinctly inferior to the credit approach. It is inferior on equity grounds. It is much inferior in terms of the bang you get for a buck.

So I disagree with what I take to be Mr. Bernstein's view, and Mr. Saulnier's view, that depreciation adjustments should be used for incentive purpose.

They should be connected to correspond to the useful life, and the rest should be alone through the credit approach.

Dr. BERNSTEIN. Mr. Chairman, perhaps I should clarify what I said, here. I am in favor of tax credits for investment. I have no objection to the use of accelerated depreciation.

It does not seem to me that what is involved here is a question of principle. What is involved here is a question of effectiveness and a question of the impact on tax revenues and on corporate finance.

The notion that one cannot use the two methods so that they have an equal effect is not correct. I have tried my best to show that you can determine the impact of accelerated depreciation in much the same way as a tax credit. It is true that the impact on corporate finance and on Treasury finance is not the same for the two methods.

For example, let us just take the figures of what would happen if you had an accelerated depreciation. Suppose that you accelerated depreciation from 20 years to 10 years. That is really a very modest acceleration of depreciation. In that case what happens is something along this line. You would have a reduction in taxpayments in the first 10 years that would be equivalent, in present value, to 19.3 percent of the cost of the equipment. On the other hand, in the last 10 years, for the same equipment, the firm would be restoring taxpayments, present value, by 11.85 percent of the cost of the equipment. The present value of such accelerated depreciation is almost the same as an 8-percent tax credit.

Now what I think Mr. Musgrave means is that for the Treasury to forgo this 19 percent in the first period of accelerated depreciation is too big a burden on the Treasury.

That is the point.

Was that the point?

Dr. MUSGRAVE. Yes. As the Treasury data presented with the earlier tax message show, increase in the rate of return, or the equivalent interest-rate reduction, which you obtain by forgoing a certain amount of revenue within a given time period, will be much greater under the credit approach than for spending the same money on speeding up depreciation.

The basic reason for this is that both are the same insofar as their effect on the flow of funds, is concerned. But as far as the effect on the rate of return is concerned, the depreciation speedup increases the rate of return only via the interest saving which results by pushing tax liabilities to the future. Cost reduction through the investment credit, on the contrary, is an outright gain to the taxpayer.

Dr. BERNSTEIN. Mr. Chairman, I think we do have to bear in mind that it has this effect on the revenues of the Government. I think it is also necessary to consider the other side, the fact that the accelerated depreciation has the effect of increasing the retained cash flow of corporations and making it easier for them to finance themselves.

Now as I do not think there is really any serious problem of corporate finance, of raising money for equipment, I do think that we could put more emphasis on the tax credit as the proper way, while recognizing that a revision of scheduled depreciation rates is desirable to take account of the greater rate of obsolescence in the modern economy, which is being done by the Internal Revenue Service.

Representative REUSS (presiding). Senator Bush?

Senator BUSH. Sorry, gentlemen, that I did not get here to hear all the papers. I am glad to welcome my old friend, Mr. Saulnier, back to the scene.

I would like to ask you: You truncated your paper all right, Dr. Bernstein; so I had a little difficulty following you. But I just would like to ask you if you would comment again on this matter of accelerated depreciation. Do I take it you favor the 8-percent tax credit that has been proposed?

Dr. BERNSTEIN. I favor that in any case.

Senator BUSH. You favor that in any case. And so far as the move for accelerated depreciation——

Dr. BERNSTEIN. I have no objection in principle to stimulating investment through accelerated depreciation. I do not believe that this must distort corporate bookkeeping. That does not disturb me at all.

Senator BUSH. In your thinking about our need to expand our plant and equipment, which you touched on here, do you not think that, or do you think that, accelerated depreciation with greater leeway would stimulate the investment?

Dr. BERNSTEIN. Senator, both methods would stimulate it, and, in fact, the difference in stimulus between, let us say, an 8-percent tax credit and accelerating depreciation from 20 years to 10 years is negligible. They both would have exactly the same effect, as I look at it.

The significant difference between them is that one of them may have an adverse effect on Treasury finance. The other one facilitates corporate finance. That is to say, the tax credit has an adverse effect on Treasury finance, because the Treasury has to forgo a good deal of tax collection in the first 10 years of rapid acceleration, you see. It gets some of the money back normally in the last 10 years, but in the meantime it has to do a lot of financing.

Now it seems to me that this is not a matter of principle. I find this to be a matter of convenience in practice. I really do not understand why we should object to giving this subsidy in one form and not in another. All subsidies, so to speak, break the normal relationship between cost and price.

Even with accelerated depreciation, corporations that are alert to their problem will keep their books to take account of the fact that they are getting this benefit over a 10-year period for equipment that lasts 20 years.

I am disturbed, however, by the fact that in allowing such a rate of accelerated depreciation the Treasury would have to give up tax revenues having a present value, in the first 10 years, equivalent to about 19 percent of the investment cost. It would get back, you see, in the latter 10 years, something now equivalent to 11 percent.

Of course, the nominal depreciation allowances are equal in both cases. But I brought them down to present values—you see what I mean, Senator?—to give us the real comparison.

Senator BUSH. You sense that the business community is sort of adjusted to thinking of this 8-percent tax credit? At first I saw no enthusiasm in the business community for it; but latterly I have not seen very much objection.

Dr. BERNSTEIN. I do not see why they should, Senator, because the plain fact is that if we start with the assumption that a corporation is thoroughly capable of financing itself in the market, it gets less, by a hair, but still less, by having accelerated depreciation from 20 years to 10 years than it gets from having a tax credit of 8 percent. True, even more rapid depreciation than in the illustration I used would give them a little more benefit.

Senator BUSH. Dr. Saulnier, did you want to comment on that?

Dr. SAULNIER. Just to say, Mr. Chairman, that my impression of the reactions to this of the business community is that they have been interested for a long time in a liberalization and updating of depreciation policies and the investment credit was at first regarded as a competitior for depreciation reform.

Now suddenly, perhaps even inadvertently, we find that it is not a competitor at all, but a companion, and that we may have both depreciation liberalization and investment credit which should be a very powerful stimulus for investment. And if it is something which jointly can be afforded under our present revenue situation, I would be among the last, I think, to object.

Senator BUSH. Sort of a "bird in the hand is worth two in the bush" theory?

Dr. SAULNIER. Yes, but now we may have two birds, in the same bush.

Senator BUSH. Dr. Bernstein, I was very much interested in your comments about the balance-of-payments situation, and your emphasis upon the real necessity in this business, if we are to increase our exports, which we must, is to increase our competitive position, and to not give out the signal at all that increases in productivity can be passed on in increased wage rates, but rather to emphasize very strongly that there must be great restraint in that field because of the already disadvantageous margin we have with the other free countries of the world in respect to wage rates and unit labor costs and all factors involving wage payments.

Certainly there should be effort made, and I think this administration should conduct more of an educational campaign along this line, that what we need to do is to get our prices down; and as we do increase productivity, to pass this along to not only wage increases, but also with greater emphasis on the buying public, both at home and abroad, and on corporations being allowed to accumulate reserves that will warrant plant expansion and modernization and so forth.

I think you made a very good point on that, and I wish this would receive a lot more attention.

I do not think I have any other questions. I am sorry I missed these other papers, Mr. Chairman.

Representative REUSS. Dr. Saulnier, in your paper you say, speaking of the recent electricians wage strike in New York:

I do not like to see government intervening in a settlement of industrial disputes, but it does seem to me that this would have been a good one in which to have taken a hand.

By "taking a hand," I assume you mean that this would have been a good dispute or potential dispute in which the Government, through the Secretary of Labor, the Council of Economic Advisers, some ad hoc board, or whatever, would have attempted to apply the wage-price canons, such as are listed in the Economic Report of the President, or canons somewhat like them, to this specific electricians situation. Is that what you had in mind?

Dr. SAULNIER. Well, there are, of course, different ways in which the Government can take a hand in these matters. They have taken a hand recently in a good many industrial disputes. In some cases it has been merely to indicate to the parties involved what seem to be right policy.

And here we are not talking about a small thing, Mr. Reuss, as you know and, I know, appreciate. We are talking about a case in which a union of electricians in New York City first proposed an arrangement under which, as I recall, they would have a 20-hour week.

We may sometime in this fine country of ours get to the point where we can have a 20-hour week. I hope so, and the sooner we get there, the better.

But I am saying, with all of the force and sincerity that I can, Congressman Reuss, that this is not the time for that. And if I may just extend that remark for a moment, this dispute was finally settled with an arrangement for a 25-hour week, at close to $5 an hour, plus another hour at close to $8 an hour.

Now frankly I do not know how the Government should have intervened in this. What did happen, in fact, was that the President, after it was all over, stated his regrets. I think this was right. It is regrettable. But I would like to think that it might have been possible to have stated this earlier, to have brought to bear on this question a greater force of public opinion and perhaps to have avoided this outcome.

It was not a question of getting an ordinary wage increase. The level of wages in this case was high to begin with, but what was given was a 10-percent increase.

Now the Council of Economic Advisers tells us that these things should be geared to overall productivity improvements. I do not know where in the world industry, overall, has been achieving 10-percent productivity improvements. Certainly not in the United States.

Representative REUSS. In your statement just now, that you would have favored some method of bringing to bear on this dispute the force of public opinion, informed public opinion, you sound very much as I have been sounding for some years when I have urged this upon both the prior administration and this one. However, I recall that when I and several other members sponsored legislation to permit and encourage the executive branch to do that in cases involving the national interest, you opposed such legislation. Have you changed your mind?

Dr. SAULNIER. No, Congressman Reuss, I have not changed my mind on that. This is a question of means for accomplishing an end. What I had in mind, in saying that it would have been well to bring to bear a stronger statement of the public interest in this question, I had reference to more informal approaches than I think were contemplated in your legislation.

Representative REUSS. You did mention the force of public opinion.

Dr. SAULNIER. Yes.

Representative REUSS. And you will have an informed public opinion only if you do analyze the impact of a given wage or price proposal on the public interest. As I recall, you were not in sympathy with that approach. I would welcome it.

Dr. SAULNIER. I was not in sympathy with your proposal, as you know, and I tried to state my views fully and objectively on it. I thought that it would carry our Federal Government too far into the whole business of the settlement of wage disputes and in the determination of prices as well.

Representative REUSS. Let me ask you this question: The Electricians' dispute in New York involved solely the wages and hours within the New York building trades area, did it not?

Dr. SAULNIER. That is my understanding of it, sir.

Representative REUSS. It was not a national dispute, as a steel wage negotiation can become a national dispute?

Dr. SAULNIER. That is correct, sir. And furthermore, if I may add, the agreement was with only, as I understand it, part of the contracting group that employs the services of electricians.

Representative REUSS. Furthermore, the dispute involved electricians who work on buildings and construction existing and underway, and has only a somewhat remote connection with our export trade and our balance of payments. Is that not so?

Dr. SAULNIER. Congressman Reuss, let me say quite respectfully that I think that is not the case. If you are in the export business, you will probably occupy space in an office building in New York. You will pay a rent. You will find that that rent is adjusted to the cost of construction of that building. The cost of construction of that building will be affected by the cost of construction labor, which, as you know, is very high relative to other types of labor.

So the costs of operating businesses all across the board, domestic and export, are affected.

I think this is an important point, and one that seems to be sometimes lost sight of. We are inclined, perhaps, to say that this was just a local New York incident, and can be ignored on that ground. I do not regard it that way. Furthermore, it seems to me to be setting, possibly, a pattern—I would hope not—that could have broader effect through the country.

Representative REUSS. I was not suggesting that we ignore it. I was simply pointing out that this was not a nationwide wage dispute, but initially, at least, a local wage dispute, and secondly, that it was a wage dispute in an industry, which, whatever may be said of its indirect connection with our export trade, was not an industry in which men are engaged directly in making goods for distribution abroad.

Dr. SAULNIER. Yes, Congressman Reuss; and what I am saying is that it was a local dispute with national interest.

Representative REUSS. Surely; which leads me to my final question.

Since you did not seem to take kindly to the suggestions made in recent years that the Federal Government attempt to focus an informed public opinion on wage-price disputes in industries where the national interest was concerned, what would be your criteria for intervention in a specific case? This Electricians' dispute seems to me to be of lesser national interest, though I agree it is of some national interest, than a dispute in the case in steel, let us say.

Dr. SAULNIER. I would agree, Congressman, that it is of lesser national interest than steel. My point is that it was an egregiously wrong policy, totally and completely unsuited to our national needs.

After all, can we really afford to go on a 25-hour week?

Senator BUSH. Afford what?

Dr. SAULNIER. To go on a 25-hour week? Is this what we should be doing at this time?

I have just returned, Congressman, from a trip around the world, which included a number of months spent in the Soviet Union, and in other of the Soviet bloc states; and I come back full of concern over our international position. I can tell you that the people with whom we are competing in the world today, both in peaceful trade and, unhappily, in the area of international politics, are working very hard. They are not working 20 hours a week. They are working long hours. I wish we could afford it; but we cannot.

Representative REUSS. These electricians were not working 20-hour weeks. They were simply being paid a very high hourly wage for the number of hours they did work. Is that not so?

Dr. SAULNIER. This is, in many cases, a means of raising the average hourly rate of wages. That is correct.

Representative REUSS. And to summarize—I see my time is about up—your criterion for intervention by the Federal Government, in order to mold an informed public opinion in the wage-price area, would be based upon what you conceive to be the outrageousness of the request, rather than the essentiality of the industry?

Dr. SAULNIER. Well, you know, Congressman, I am rather an eclectic in these matters. I think that a wage settlement that is very much out of bounds is something on which we all, as citizens, should speak out; equally with an universe, inflationary wage settlement, even if it is not as high, in an industry that has great national import. I would not want to have to choose between these. I think we have to play these things pretty much by ear, and make our decisions as we go along in the light of the circumstances as they develop.

I am not friendly toward intervention by the Federal Government in labor disputes. On the other hand, we have had that intervention. And here we seem to have had a case boiling up on the sidelines, and, so far as I know, nothing was said about it until after it was all over.

And if it was appropriate to speak about it after it was over, it might have been appropriate to say a word while it was being shaped up.

Representative REUSS. Thank you very much.

Mr. Widnall?

Representative WIDNALL. Do any of you members of the panel have any comparative figures addressed to the tax rate credit and the depreciation allowance as it pertains to the economy of West Germany, Italy, Japan, Switzerland, and England?

We hear time and again disparaging remarks about our rates of growth as compared to those countries. Now, it seems to me that a great deal of this has been made possible by their depreciation allowances and by their tax credits; at least from what I have read.

Do you have any comparative figures on this?

Dr. MUSGRAVE. I think that I could get them for you, if I may.

Generally speaking, the depreciation rates in most European countries are faster, and of course, there are some countries such as the Netherlands and especially Sweden, where depreciation is used as a countercyclical device to be turned on and off as conditions require.

In some instances, as for instance in the case of Germany, these tax provisions have been helpful. But I think they also have been handled in a way which made them very wasteful and inequitable, and gave rise to wealth and income-distribution effects which are undesirable.

We should try very hard to adjust our tax structure, so as to be helpful in this respect. But maybe we can do it better and more efficiently than they did. (The material referred to was not received at the time the hearings were printed. When received it will be made a part of the committee files.)

Representative WIDNALL. Professor Musgrave, I agree with what you said on that. But when we have so much emphasis placed on comparative growth rates in the past few years, I would like to know honestly the reason for it, whether or not a good deal of it was not due to the encouragement that was given taxwise, and also by depreciation allowances. Have we failed as miserably as we are told we have failed, growthwise?

Dr. MUSGRAVE. I think that we should do more by tax policy than we have done. But I think—and this comes back to the close of my initial remarks—that we have gone a bit haywire on this game of comparing growth rates. As I said, it is perfectly obvious and inevitable that an economy such as the Soviet Union, being at the state of economic development in which it finds itself, will grow more rapidly than we. I think it is altogether foolish to invite a competition in comparing growth rates, where we are, by the nature of the case, bound not to win.

In many of these cases, such as the Japanese economy, and the Western European economies, you have very distinct situations. In Japan you have the case of an economy possessing on the one side vast labor resources which can be drawn out of the most primitive kind of employment, and on the other over the technical know-how which makes it possible to put them into modern employment. The only effective restraint, so far as I can see, for Japan to have a growth rate of 20 percent or more, is the balance of payment problem. It is a case which is entirely incomparable to ours.

Similarly, the case of the Soviet Union, with still very large unused resources, with low per capita income, on the average still low productivity of labor, is a case which cannot be compared. The case of Germany, which had to reconstruct its economy from a destroyed wartime state of affairs, introducing all modern equipment, having a very large labor influx—again this is an abnormal situation.

Europe, having gained the benefits of the increased efficiency of the Common Market, will continue to grow very fast for some time. This, of course, is very fine, but I think we have been going much too far in saying that something is wrong with our economy if we cannot go as fast as they.

I think we can go a little faster than we have. But I would say that if we have a policy of being efficient and progressive in industry, of maintaining high employment, we will grow at a reasonably rapid rate.

I don't believe in the idea that in Africa and in southeast Asia, people sit around and every morning wait to read a bulletin on what is our growth rate and what is the Soviet growth rate and accordingly vote on whether they want to go Soviet or free economy.

From the foreign policy point of view, if we are going to be willing to divert a large part of our growth increment into increased economic aid all the world over, if we are going to step up our growth rate and say, "All right, some sizable fraction of this increment we will give to the world in economic aid"—then faster growth will help. But if more rapid growth simply means that everybody has three ice boxes instead of two, and that we become more efficient and make it more difficult for less-developed countries to compete with us in world markets, then the faster growth might do more harm than good. Growth in GNP is not the only thing the world looks at.

Dr. Bernstein. May I add a word in reply to this question, very briefly?

The rate of economic growth in continental Europe has been greater than in the United States. The proportion of the gross national product invested in continental Europe is higher than in the United States. That higher proportion of investment is due to two factors. First, they had a big deficiency of investment because of their war destruction. The second is that on an average Europeans use more capital per unit of output than we do. Strangely, while we use more capital per unit of labor, they need both more labor and more capital to produce a unit of goods.

Now, the increase in production in Europe has been exceptionally large, partly because they have been catching up. It seems to me that their rate of growth and production will slow down.

As Professor Musgrave says, it is impossible to conceive of a people as enterprising, as intelligent, as innovating as those of Western Europe, knowing so much about technical methods of production, not catching up with us as time goes on.

The real test, then, of our productivity, is not whether we are growing as fast as other countries. The real test is this: Is our economy growing enough to provide the growing labor force with the jobs that they are seeking?

If we have a rate of growth in the United States of 3 percent per annum, even if it is steady, but the number of people looking for jobs is growing more rapidly, and there is increasing unemployment, we are not going fast enough.

That is the real test. We do not have to catch up with anyone else's rate of growth; but we have to grow enough to satisfy our own economic requirements.

Representative WIDNALL. Professor Musgrave, could you furnish for the record some comparative figures with respect to those countries, as to the tax credits and depreciation allowances?

Dr. MUSGROVE. Yes, sir, I will be glad to do so. (The material referred to was not received at the time the hearings were printed. When received it will be made a part of the committee files.)

Representative WIDNALL. Dr. Bernstein, I was particularly interested in what you said about the Council not discussing the wage-and-price policy necessitated by our large and persistent balance-of-payments deficit.

It seems to me that you underscored this by saying:

> Unless labor unions and industrial corporations are prepared to accept the wage-and-price policy until our payments position is restored, the payments deficit will weaken our economy and prevent us from maintaining a high level of production and employment.

From that, I assume that inherent in that statement is the fact that we have really been on a merry-go-round over a period of years and that if we are going to live out our life expectancy in a democracy, we are going to have to live for more than the next 24 hours, which a lot of people have been doing in both business and in labor.

The attitude too often has been, "Get as much as you can while the getting is good." And we cannot afford to do this any more, with the type of competition we have throughout the free world.

I think, Dr. Saulnier, in your remarks, too, there was inherent also the same implications.

Now, I have a quote from your remarks, Dr. Saulnier. On page 6, where you said:

> It is clearly not a trend that is consistent with improvement in our international financial position.

This refers to the large growth in Federal spending.

> If it does continue, it will have to be supported by a substantial increase in taxation.

In testimony that was given last week, it was shown that in the increase of a million jobs that had been lost during the recession, over 35 percent of those jobs were picked up through Federal, State, and municipal employment.

Do you think that is too high a proposition to be borne discretely by the economy as we continue? This will inevitably lead to everybody being employed by the Federal Government or local and municipal government.

Dr. SAULNIER. Just offhand, Mr. Widnall, it strikes me as a high percentage. I would have expected that the employment increase in the cyclical industries would have been the most important.

Representative WIDNALL. That was in the testimony of Secretary Goldberg before this committee.

Dr. SAULNIER. That is interesting. I must look at that. It does surprise me.

Representative WIDNALL. May I just ask one more question?

Doesn't the large increase in foreclosures, both FHA and VA—and the VA I believe 3 weeks ago suspended payments on redemption of these mortgages—indicate that the picture in the economy is not as rosy as the President indicated in his report; and, secondly, doesn't the marked increase in failures of small businesses also provide a warning sign?

Dr. SAULNIER. Mr. Widnall, I am inclined to think that the expectations concerning the growth of the economy which underlie the budget estimates are a bit on the optimistic side. I hope that it turns out that way. It would be a wonderful thing for us if this were to come to pass.

But I have some doubts about this, and I think, accordingly, that our policies should be designed just as expertly as possible to help bring this happy result about.

Now, about foreclosures: This is a very interesting point.

You will observe, as I can see you have, Congressman Widnall, that the curve of foreclosures has been rising steadily and rather rapidly. Foreclosures are still small relative to the total exposure of our mortgage insurance system, but they are becoming more frequent.

I do not think, Congressman Widnall, that this represents only a cyclical effect, or a condition of business; it may represent also the results of an excessive liberalization of credit terms. These, in my judgment, has tended to encourage people to take on commitments in connection with the purchase of a house that are a bit more than they can carry over the long run, even when employed.

I feel that this is a point that ought to be of very great interest to this committee. And if I may do so, sir, I would like to suggest that you make a special point of looking into this.

I am, as you know, a great admirer of our Federal home mortgage insurance and guarantee systems. I think they have done wonderful things in promoting homeownership in our country. But it is possible to undermine them by an excessive liberalization of terms. I hope what we are seeing is not the beginning of the effect of such an excessive liberalization but it could be. This is something for the committee, I think, to look into.

Dr. GURLEY. May I add a general comment to your question, Mr. Widnall?

I share your suspicion that things are not quite as rosy as the report makes them out to be. Gross national product in the last three recoveries has increased by about the same percentage in each of the last three recoveries, the 1954–55 recovery, the 1958–59, and the recent one—considering three quarters of upturns from the trough.

Now, Federal budget policy has become increasingly more lenient in each of these recovery periods. And by that I mean Federal Government expenditures have increased relative to tax receipts by a larger amount in each of these recovery periods.

Now, this certainly suggests that as Federal budget policies become more and more lenient, and yet the overall effect has been exactly the same on total demand and spending, private demand has been weakening in each of these recovery periods.

And I think that this has definitely been so, and I think there is a weakening all along the line of private demand, not only in housing, not only in equipment, but all through the private sector of the economy.

This suggests that some sort of a tax adjustment, the 8 percent tax credit, something along these lines, should certainly be made. It is urgent, in order to provide stimulation.

Dr. BERNSTEIN. Our economy has expanded just about as much in this expansion so far as in every other. There is no reason for being especially happy about that. Three-fourths of the expansion in a cycle generally occurs in the first year of expansion. If we do not do better in 1962 and 1963 than was done in previous expansions in the second and third year after recovery, we are not going to have a very good situation. We have to do much better, therefore, than we did in the past.

To my mind, the key to this is what Professor Gurley said. The best hope of getting a good expansion is to get an increase in private investment, particularly private investment in producers' durable equipment. The tax credit is to my mind an essential part of a program to get the kind of expansion in 1962–63 that this economy needs.

I would not be overly optimistic unless we get something like that to go with the normal forces of expansion.

Representative REUSS. Senator Proxmire?

Senator PROXMIRE. In view of the fact that every member of the panel except Professor Musgrave has commented on that question—and it is a very interesting one—I get the impression from Professor Saulnier, Professor Gurley, and Professor Bernstein, that you three gentlemen feel that we will not get the GNP predicted by the President and the Council of Economic Advisers, at least without the tax credit.

Dr. BERNSTEIN. That is correct.

Senator PROXMIRE. Professor Musgrave, would you concur in that and make it unanimous?

Dr. MUSGRAVE. Their prediction involves the tax credit.

Senator PROXMIRE. I understand it does, yes.

Dr. MUSGRAVE. I hate to overestimate the importance of the tax credit. The tax credit, in the short run, might stimulate the rate of investment by $2 billion.

Senator PROXMIRE. It is my understanding that along with Dr. Brown you are one of the two authors of the tax credit. It is interesting to observe this modesty.

Dr. MUSGRAVE. I had some interest in it, but I do not look at the credit as an employment-creating policy in the short run. I feel that the credit should be looked at as a policy which, against the background of a full employment economy, will help us to shift resources from consumption into capital formation, thereby helping us to increase capacity output, to raise the ability of the economy to produce.

The credit has the nice side effect, in the short run, of helping the employment situation. But it is not an employment-creation program. It is a program which should help our economy to get into shape to grow more rapidly, provided that the rest of the fiscal policy is such as to hold the aggregate demand sufficiently high to keep us at a high level of employment.

So I think that there is hope that in calendar 1962, we will reach the levels which are projected. The budgetary picture for 1963 depends largely on the profits and incomes in calendar 1962, and here I am optimistic. As to calendar 1963, I share my colleagues' views that we should not be to sanguine about the longer run.

If I may, I would like to come back for a moment to a point which Mr. Saulnier made, a point which, if I understand it correctly, I very much disagree with. This is the proposition that, since we did have a recovery in 1959, and in 1961, things were fine, and more strenuous measures were not needed.

After all, the recovery of 1959 came late and was weak. The recessions were very wasteful. While I would agree with Mr. Saulnier in not wanting make-work projects on the expenditure side, I think that it would have been extremely beneficial in both of these cases, if we had had the flexible tax device.

As to the last recession, even if a tax cut had been introduced as late as spring of 1961, a tax cut amounting to, let us say, an annual amount of about $10 billion, and had been kept in effect for 6 months——

Senator PROXMIRE. By the flexible tax device, you are talking about the temporary cut in personal income tax? You say $10 billion annually for 6 months?

Dr. MUSGRAVE. At an annual rate of $10 billion for, say, 6 months. I do not see Mr. Saulnier's point that, because eventually we had a recovery, this is proof that there was no need for doing anything more.

Dr. SAULNIER. Are you really talking about 1961?

Dr. MUSGRAVE. Preferably, it should have come earlier, say, in May 1960.

Dr. SAULNIER. That is quite a difference.

Dr. MUSGRAVE. It not having come in 1960, it would still have been a help in spring 1961. But preferably it should have come in middle 1960.

Dr. SAULNIER. This is one of the interesting points about this kind of question. You see, Professor Musgrave can be not quite sure whether it should have been 1961 or May 1960.

Dr. MUSGRAVE. I would have preferred 1960.

Dr. SAULNIER. You would prefer May 1960?

Dr. MUSGRAVE. Yes.

Dr. SAULNIER. This is a complex question, and I would doubt that we would have time this morning to resolve it, but I must say that I have grave doubts about the wisdom of having made a $10 billion annual cut in our tax revenues on individual income tax accounts in May 1960.

I would just like to emphasize that. I have very grave doubts on that.

Senator PROXMIRE. Professor Gurley, you said something very interesting to me:

> There is no simple relationship between the size of the surplus or deficit and the restrictive or expansionary effect of the budget on full employment GNP.

And you differentiated between different kinds of surplus. I presume you are not talking about the administrative budget. You are talking about the budget on income and product account, the cash budget?

Dr. GURLEY. I was thinking of the budget on income and product account.

Senator PROXMIRE. And you did not make the same point I understand Professor Musgrave made, that it is the matter of the timing of the surplus. His point, as I understand it, was how rapidly you are moving from a deficit situation to a surplus situation, rather than the absolute size at a given time of the surplus or deficit. Was your point the same?

Dr. GURLEY. We perhaps were making slightly different points. But on the crucial overlap, we both made the point that it is not only the size of the surplus or the size of the deficit, but also the level of Government expenditure, and in fact Professor Saulnier made exactly the same point. That is, if there are two surpluses of exactly the same size, but one of them is associated with a much higher level of Government expenditure, that one will tend to be much more expansionary than the one associated with the lower level.

Senator PROXMIRE. Before Professor Musgrave replies I would like to say that is a very interesting observation, because this is the position taken in the OECD report, as you will recall, a few weeks ago. And I specifically asked Dr. Heller about this, with the notion in mind that if we could have an inspection enforced arms control, for example, and reduce our Government spending by $20 billion or some very large figure, and reduce our taxes, too, I said: "Would this necessarily tend to contract the economy?" In my hope, it would not. And it was Professor Heller's contention it would not necessarily do so, too.

I take it from what you say that this would tend to have a contracting effect, and a serious contracting effect, on the economy even if the budget were balanced. Is that correct?

Dr. GURLEY. Yes. That is exactly right. If there is a balanced budget in both cases, or a given size of surplus in both cases, if you drop to a much lower level of expenditures, that will certainly have a contracting effect.

Senator PROXMIRE. I do not want to misquote Dr. Heller. Perhaps I did. I think Dr. Heller's position was that the economy would not necessarily be in a serious economic recession or depression under these circumstances. There might be other things that could be done.

Dr. GURLEY. He was no doubt thinking of adjusting tax rates in order to raise private demand by enough to take up the slack.

Senator PROXMIRE. Do you feel that you can move ahead, some people might call it responsibly, by balancing your spending with taxing and then increasing both spending and taxing as the OECD seemed to suggest, disregarding the notion of whether more Government spending is morally correct or not? I am inclined to be opposed to it, as you may be, but just as a technical economic point, if we spend more and tax more, you say that this will have an expansionary effect on the economy; it would tend to promote economic growth?

Dr. GURLEY. Well, it depends. First of all, it would have an expansionary effect just from the standpoint of raising aggregate demand. Whether it has a good longrun effect in promoting growth certainly depends on the type of expenditures that we are talking about.

Given the very best type of Government investment expenditures to promote growth and taxes that do not interfere with private expenditures in the investment field, then, yes, we have both things working for us, increasing aggregate demand and a composition of expenditures that would be growth promoting.

It is very possible to do this.

Senator PROXMIRE. Professor Musgrave?

Dr. MUSGRAVE. There is an important difference, depending on whether we think of how the policy affects the level of aggregate demand, or of how it affects capacity output. When it comes to effects on the level of aggregate amount, I think there is no question but that an increase in Government expenditures of $20 billion, matched with a tax increase of $20 billion, a balanced increase, will be expansionary, and a balanced reduction will be restrictive To avoid restriction with an expenditure cut of $20 billion, you might have to cut taxes by, say, $25 to $27 billion, to give some order of magnitude. To remain even, aggregate demandwise.

On the other hand, and I think Professor Heller would agree with this—it may well be that in cutting Government purchases for defense by $20 billion, while at the same time doing things to maintain full employment, we could raise the full employment-capacity growth of our economy, because we would have more resources available for capital formation, public and private, and so forth.

But as far as effects in demand and employment are concerned, a balanced reduction in the budget would certainly be restrictive.

Senator PROXMIRE. Then I just wanted to button this up before I asked Dr. Saulnier to comment.

Two points on this: You are talking about resource using government spending and not transfer payments? In other words, a simple increase in social security balanced by an increase in social security tax—would that have the same effect?

Dr. MUSGRAVE. For all purposes you could assume that it would not.

Senator PROXMIRE. And in the second place, would there be a tendency for prices to rise? Would you have to have a corresponding tighter monetary policy to keep the prices from rising under these circumstances?

Dr. MUSGRAVE. Under which circumstances, sir?

Senator PROXMIRE. Of rising spending and rising taxing. The assumption has always been made before this committee, at least to my limited experience, that the main fiscal problem in regard to prices is whether you have a balanced budget or not. Now, you are raising another point and a very interesting one, and that is that as you expand spending and expand taxing at the same time, you are going to increase growth, and you also increase the pressure driving up prices.

Dr. MUSGRAVE. If you are close to a high employment level, you certainly will. If you have a lot of slack in the economy, relatively little. The closer you are to high employment, the more you run the risk of doing this.

Dr. BERNSTEIN. In any case, I think if you increase the social security taxes, and other aspects of income distribution per unit of output are not reduced correspondingly, you are going to have a rise in costs per unit of output and a tendency for prices to rise.

If you increase social security taxes, that means that the increase in all other incomes per unit of output must be restrained, as production increases, to that same extent. If it is not, prices will rise.

We cannot answer the question whether increases in social security prices will raise prices unless we know whether it will be accompanied by a restraint on wages, profits, and other forms of income simultaneously. If it has no effect on the other forms of income, it is going to raise prices.

Senator PROXMIRE. Dr. Saulnier wanted to comment.

Dr. SAULNIER. Just to observe, Senator Proxmire, that I think the conclusions we reach by comparing the effects in, as we say, aggregative terms of an increase in expenditures and a simultaneous increase in taxes, or conversely a reduction in expenditures and a reduction in taxes can be very wrong. The arithmetic here is too simple. It works out all right in a simple arithmetical model, but in our world the transfer of resources is so difficult and the leakages, as we say, are so great, that big changes of this kind could have, if carried out in a short period, tremendously disturbing effects through our economy.

I must say that if I were Chairman of the Council of Economic Advisers, and somebody told me that we were going to have a reduction of $20 billion Federal expenditures and a tax reduction of $20 billion, I would urge that it be phased out very carefully and I would feel that we might still have some very rough water to go through before it was over.

This is a place, it seems to me, Senator Proxmire, where what we call aggregative economics, and especially when put in simple arithmetical terms and applied to the short run, can lead us to wrong policy conclusions.

Representative REUSS. I have a quorum call, and I would like to get in one question to Mr. Bernstein, if you would bear with me.

Dr. Berstein, I would like to ask a question about our basic balance of payments and methods of preparing our deficit.

You say, and I certainly agree with you, that Western Europe should assume a much greater share of the burden of defense and aid, and also that the Common Market owes the rest of the world a unilateral approach in its tariffs and restrictions. I agree with that.

If those things are so, isn't it really our friends and allies in Western Europe that have got to do some hard thinking and acting on repairing the U.S. balance-of-payments deficit?

I completely agree with you that we must keep our prices competitive, and particularly our export prices. But assuming we do that, do we not, in order to bridge this $2½ billion basic annual gap, need that kind of response by our friends and allies in Western Europe?

Dr. BERNSTEIN. I think definitely if they would use more of their resources for aid and more of their resources for defense, even if we did not reduce our own, you see, even if we kept up our level of aid and our level of defense, the whole market for our export products would be improved. That is one aspect of it.

The second aspect, of course, is that if they proceed to reduce the accessibility of the rest of the world to this largest of all importing markets, the Common Market, then of course it is going to cause more trouble for us.

I think there is understanding in Europe that they owe us, owe the whole world, a unilateral reduction. The United Kingdom has made a public statement to the effect that if it joins the Common Market, it would favor a unilateral reduction of 20 percent.

Representative REUSS. But these things have not yet happened, and it is important that they do happen?

Dr. BERNSTEIN. The parts on aid and defense are to some extent happening already. They are going along slowly, not as I would like. The point on the Common Market has happened a little bit. They have already given some reduction.

Representative REUSS. But not nearly enough?

Dr. BERNSTEIN. Not nearly enough. That is the point. It is not nearly keeping pace with what I would regard as the restrictive effect of the broadening preferences as they move ahead to wipe out the tariffs within the Common Market.

Representative REUSS. In case there are obtuse Europeans who may be reading this transcript, what you mean, then, is that the Europeans are supposed to get together in the field of trade, aid, and military defense, and do a substantial part of the job of bridging our balance-of-payments gap. Is that so?

Dr. BERNSTEIN. Congressman, having discussed the expense in aid, this would ease the U.S. balance-of-payments problem, but it cannot solve it. That is because it would create an environment in which the absorption of our exports would be greater; but we would still have to be able to export on a competitive basis. That we must do.

They must create the environment. We must take advantage of it.

Representative REUSS. The environment, however, they create by taking a larger part of the burden of defense and aid. That is what you say, isn't it?

Dr. BERNSTEIN. That is right.

Representative REUSS. Then they must go on, you further say, unilaterally to lower their tariff walls. And our contribution to this gap bridging lies in the kind of attention to our cost-price structure which you talk about; namely, we had better not have an inflation here, or we will rob ourselves of the fruit of this.

But still, it is up to Europe to bridge the $2½ billion gap?

Dr. BERNSTEIN. I do not think that would be the right way to put it. It is up to Europe to create conditions in which aggregate demand for our export goods, if the goods were available at competitive prices, could be absorbed.

Now, if the Europeans in fact hold down their own expenditures for defense, for aid, and so forth, and their own absorption of their own output for domestic consumption and investment is not really large enough, they are going to have surpluses, and they are going to pile up reserves. This is a technique for providing that.

Now, even if they did that, the consequences of it for our balance of payments would still depend upon our costs. Maybe the British, maybe the Canadians, maybe the Japanese, all of whom, by the way, have balance-of-payments problems along with us, maybe they would capture that market if they are more successful in holding down their costs.

Representative REUSS. Surely. But I want to emphasize again that throughout our colloquy, here, it has been my assumption that we do what we say we should do, namely, avoid inflation here, and particularly keep our export prices competitive; but if we do that, if we adopt the spartan life, here, we still need, in order to bridge this $2½ billion gap, the type of performance by our European friends which we have been talking about. Is that correct?

Dr. BERNSTEIN. That is right.

Representative REUSS. I understand.

Senator PROXMIRE. Dr. Saulnier has to leave for an appointment. I would appreciate it if I could ask Dr. Bernstein, Professor Gurely, and Professor Musgrave a few more questions.

So, Dr. Saulnier, you are excused, and thank you very much.

Dr. SAULNIER. Thank you very much, Senator.

Senator PROXMIRE. I would like to ask Professor Musgrave: What effect will this tax credit on investment together with a substantial increase in depreciation allowances, or shortening of the life of depreciating assets, have on tax equities?

In my understanding, you are an outstanding expert in this field. You have published a work indicating that the taxes, local, State, and Federal taxes, now may be more regressive than most of us think, or at least a little less progressive than has been generally represented. I am very concerned about this, and I think it is as important an aspect as the effect on growth, and so forth.

I am wondering what your opinion is, then, on the effect of this inequity?

Dr. MUSGRAVE. I heartily agree, Senator, that the equity of the tax structure is one important aspect of the tax policy. Of course, it is not the only one. There are other effects on the economy, too.

Senator PROXMIRE. We have not discussed this at all, however. We have discussed the other aspects of it exclusively.

Dr. MUSGRAVE. If we give special incentives, if we introduce special incentives into the income tax, this by its very nature will give special treatment to special groups. We have to sacrifice some loss in equity, as it were, for the gain which we hope to get in terms of economic growth. We have to pay a price.

Senator PROXMIRE. But how about relating this as a matter of practical politics and balance to the proposals which the President made along with the tax credit, for so-called loophole plugging measures, including dropping the dividend credit and that kind of thing, withholding of dividends and interest?

Dr. MUSGRAVE. Giving the investment credit will increase the net rate of return to investors, which is precisely the way you want to get your effect. Therefore, it will improve the position of people receiving dividend income and receiving capital gains in corporations.

It is also correct that the repeal of the dividend credit and exclusion would place a burden on these groups. So you might say from this point of view, that say you would trade increased taxation by repeal of the dividend credit and exclusion, against reduced taxation by way of the investment credit, and the gain would be such so as to improve incentives.

Discontinuing capital gains for depreciated assets works in that direction. The proposal for source withholding on interest and dividend income would again affect recipients of capital income, but to a considerable extent in the lower- and middle-income groups and not only in the high-income groups.

I do not know how the package as a whole would work out by way of income brackets. It might be fairly neutral. But the main principle is that you would trade an efficient device, we hope, in terms of the investment credit, for the less appropriate devices of the dividend credit and exclusion, which have little merit on equity grounds, in my judgment.

Senator PROXMIRE. Will you compare this tax credit in terms of revenue with a comparable drop simply in the corporation income tax.

I am a little concerned with the income tax erosion effect of these exemptions and credits and so forth. You get one, and it may be justified by itself. This gave rise to another. And this is one of the great weaknesses and difficulties of our whole personal income tax structure. Incentives by simply lowering the rate itself appeals to me logically and from the standpoint of equity.

Dr. MUSGRAVE. It would be perfectly correct to say that, in terms of equity, in the sense of equal treatment of all people receiving a profit income, the reduction in the tax rate would be better than the credit.

But, a $1.8 billion reduction in the corporate tax rate, meaning, let us say, a reduction by 3 or 4 percentage points, would be very much less effective in giving investment incentives.

The obvious reason is that the reduction in the corporate rate across the board would increase the profitability of old and new capital. And the bulk of it would go to increasing the profitability of old capital. To the extent to which you do this, you do not gain insofar as the profitability of new investment is concerned. And this is what matters for the incentive.

What the credit does, and similarly what accelerated depreciation on new investment does, is to focus the entire revenue loss at the margin where the new investment occurs, and therefore it will be more potent as an incentive measure. But you "buy" this at a cost in terms of equity.

Senator PROXMIRE. Well, there is a further equity cost I would like to touch on, because Mr. Bernstein, it seems to me, brought it out in his testimony, too.

You talk about the tax credit in terms of a lesser loss of immediate revenue to the Federal Government as compared to a comparable increase in depreciation incentives.

Dr. BERNSTEIN. From 20 to 10 years.

Senator PROXMIRE. Right. Now, why would not the present value of cash to a corporation—and I would say especially a small corporation, which has great difficulty raising cash in the market, be just as great for the corporation as the present value of cash to Government from the tax credit? In fact, I would think that from the standpoint of economic incentive in the system—and I am chairman of the Small Business Subcommittee, and that is why I am so conscious of this—particularly from the standpoint of small business, this tax credit would be far less attractive than a comparable drop of the kind you describe, in depreciation, which would give small business substantially more cash now and for the next several years. This is especially true with a rapidly growing corporation.

Dr. BERNSTEIN. Let us take a look at this both in cash value and in actual sums as it accrues over a 10-year period.

Suppose that the Government says it will give an 8-percent tax credit; and then, on an investment of $100,000, a corporation has $8,000 more than it would have ever had if it had undertaken the same investment without the tax credit. And the Government has $8,000 less than it would otherwise have had.

Now, suppose that the corporation, instead, gets an accelerated depreciation from 20 years to 10; and the tax rate is 50 percent. That means that the corporation, instead of setting aside five units, $5,000 on a straight line basis for depreciation each year, now sets aside $10,000. That is the second $5,000 which it sets aside, which is not subject to Federal income tax. It would have been under ordinary circumstances. And at that 50-percent rate the corporation saves $2,500 the first year, and $2,500 each additional year to the end of the 10th year.

In gross amount this accumulates up to $25,000 in the period.

Dr. MUSGRAVE. I think we miss a point if we do not look at the dynamics of a growing economy.

Dr. BERNSTEIN. I think if we do, we have the same thing about the 8 percent. We have to keep raising that, too.

Let me finish it this way, Dick, and then, if you had any great objection to my way of analyzing it, you go right ahead, and I will listen very carefully.

In this 10-year period this company saves $25,000 gross, accumulated $2,500 a year for this period. The Government gives up the opportunity of getting that $2,500 in tax revenue; or $25,000, in tax revenue, rather.

It is true that in a flat economy we would get that money back in the second period. And what would happen is that once you reached that $25,000 per $100,000 investment, the Government loses in the 10-year period it would remain flat. Thereafter, in fact, the Government would have no difference in revenue.

In a growing economy, we would have to make adjustments for that, but so we would for the 8-percent tax credit, too.

Senator PROXMIRE. Just at this point, then: There are two things. One is the problem of the growing economy, in which accelerated depreciation represents a larger revenue loss than tax credit. The other, as I understand it, is the effective interest-free loan the Government is giving. You are giving $25,000 as compared with the old depreciation amount, with no interest.

Dr. BERNSTEIN. Now, even without a growing economy, this problem of handling the Government's finances for the next 10 years—and that is problem enough—involves in effect giving to this corporation an interest-free loan which requires from $2,500 per $100,000 the first year to $25,000 in the 10th year. That interest-free loan is accompanied by the fact that the Government's revenues are less than they would otherwise have been.

I make the point that actually when we put this all down on a cash basis, that 10-year loan turns out to be worth roughly $7,500. That is what its cash value is. It is not really larger. It is actually less than cash value, than the 8-percent credit.

I did mention that there are corporations that might find their financial position makes this a very attractive thing for them to have, much more attractive than even a larger credit. They do not find finance as acceptable to them as they would like.

Senator PROXMIRE. Once again I will interrupt to say these are the smaller corporations; is that right?

Dr. BERNSTEIN. That may be. And I say that as to considerations of equity, if I may read from the last paragraph one sentence, I make this proposition:

Public policy on these alternatives must take into consideration their impact on tax revenues and corporate finances.

I do believe that there are cases, legitimate cases, in which corporations, choosing what is best for them, would prefer this accelerated depreciation. I think some of the large corporations that have no difficulty in getting finance underestimate the relative benefits they would get from the tax credit as against the investment in machinery and equipment.

Now, one last word about this growth business. Let us not exaggerate the role of growth in this analysis in a growing economy.

We have not had any increase so far in the type of investment goods that are being covered by this in quite a number of years. There has not been any rapid growth in purchases of producers' durable equipment.

One of the points I tried to make is that it has been awfully flat, and that in fact in real terms, allowing for price changes, it was actually 8 percent less in the second quarter of 1960 than it was in the fourth quarter of 1956.

Now, I hope we do get growth, Dick, but I think this analysis can be done almost as well without complicating it on the growth side.

Senator PROXMIRE. I am well aware of the fact, of course, that the small corporation, if it is very small, pays the 30-percent rather than the 52-percent rate with the 22-percent surtax. Now you go ahead.

Dr. MUSGRAVE. Let me introduce two distinctions which we need in the picture.

One is that the effect, the favorable effect, of these measures on investment can come about in two ways. It can come about because corporations will be getting more internally available funds. Therefore, if they could not have gone to the market, now they have the money, and they can invest it.

Also, there will be a favorable effect on investment, because profitability is increased, because the rate of return on capital is increased.

In the case of accelerated depreciation——

Senator PROXMIRE. I see; because the tax is less.

Dr. MUSGRAVE. Yes; because the tax is less.

Now, we know very little about investment behavior, but probably both of these factors are in there. Investment will respond favorably to having more internal funds, and it will also respond to having a higher net rate of tax. There are these two aspects.

Dr. BERNSTEIN. That applies both to the accelerated depreciation and the tax rates.

Dr. MUSGRAVE. Correct. When it comes to accelerated depreciation, we have to make a distinction between accelerated depreciation which would be given to old and new investment alike, and accelerated depreciation, which would be given only for new investment.

The Senator's point requiring the small firm I believe, relates to the case of giving accelerated depreciation to old and new investment alike; because then, the firm can get the relief simply on its old investment; whereas if you give the accelerated depreciation only on new investment, then the credit and accelerated depreciation are the same thing. In both cases, the investor, as it were, gets a matching grant, but only if he has something to match with.

In order to have the advantage of giving the benefit to small business, which does not have the funds to meet this matching grant condition, you would have to go to accelerated depreciation across the board. But if you do this then the profitablility effect would be very much less; it would be as in the case of a rate cut, which would apply to profits from both old and new capital.

So if you give a great deal of weight to this consideration of the small company that cannot match, then you have to give the relief on all investment, including the old one, and your profitability effect is very much less.

In discussing the problem of the revenue comparison, which Mr. Bernstein had in mind, he was thinking of giving accelerated depreciation on new investment only.

So I think, Senator Proxmire, that it is very important to decide—and this is an empirical question—how much weight should be given to this concern for the small corporation that cannot do the matching, as against how much weight should be given to using your given revenue loss so as to buy the greatest gain in profitability.

Senator PROXMIRE. Do you advocate across the board accelerated depreciation for old and new? You say Dr. Bernstein advocates it for new only. And you advocate it for both old and new?

Dr. MUSGRAVE. No.

Senator PROXMIRE. If you do not, then there is a real discrimination, it seems to me, against the small firm, which tends to buy all the equipment.

Dr. MUSGRAVE. I am saying as far as your concern with the small corporation is concerned, Dr. Bernstein's plane is as bad as mine. His accelerated depreciation on new investment is of as little help for the small company as is my credit on new investment. So what you really need is across the board measures.

Dr. BERNSTEIN. Mr. Senator, I did not invent this accelerated depreciation. I merely compared its effects with the tax credit. I would like to continue what the effects would be along the lines you asked.

Suppose a corporation paying a rate of 50 percent income tax invests in every single year $100,000 for 10 years.

Notice, now, what its retained cash flow effect would be by the tax credits and the accelerated depreciation. You get a tax credit in every single year of $8,000. So at the end of the fifth year you have $40,000 in accumulated tax revenue. You save $2,500 the first year, $5,500 the second, up to $12,500 the fifth year, through the accredited depreciation. This adds up to $37,500. So that in fact it is only in the sixth year that a corporation would find that its retained cash is greater.

Senator PROXMIRE. That was a big jump. Why would you not find out immediately in the first year?

Dr. BERNSTEIN. In the first year, Senator, this company increased its investment $100,000. The Government by the tax credit would have given it back $8,000. Suppose it had an option. If it elected to have an accelerated depreciation, in which 20-year equipment is depreciated in 10, then the depreciation now becomes $10,000 a year, instead of $5,000.

Senator PROXMIRE. I see.

Dr. BERNSTEIN. So that $5,000 extra depreciation—it saves $2,500 in taxes, and that is what its increased cash flow is.

The second year it again invests, you see.

Senator PROXMIRE. Your position is that it is only in the sixth year that the tax credit——

Dr. BERNSTEIN. Gives less cash. It gives more cash up to the seventh year. If it is all done——

I am giving you a special case. I am giving you a 20-year depreciation, brought down to 10. If we made it 20 years brought down to 5, we would get a different result.

My real argument, here, Senator, is that I have not, as Professor Musgrave has, great moral principles at stake in whether we use a technique for encouraging investment by acting on the depreciation allowance year by year on the new investment, or through a tax credit.

I am not disturbed that the accounts of corporations reporting their income will somehow be less precise than they have been. In my opinion we have not had proper reflection of true corporate profits for 15 or 20 years, because of the accounting systems that we require by Internal Revenue in a period of unstable prices. So I am not worried about that.

I am worried about two different questions. First, the stimulus that each would give, and second, what would be the effect on corporate finance, and what would be the effect on Treasury finance? I think we have to take these things into consideration.

I am now indicating that I think in fact corporations have in the past felt the tax credit was not doing as much as they wanted. Of course, if they meant to get an enormous acceleration depreciation, down to, say 20 years, brought down to 5 years, they may be right.

I am thinking of one that had equivalent cash value, and they do not get any more cash through the accelerated depreciation than they do through the tax credit.

Dr. MUSGRAVE. I still believe that my position is superior on both moral and immoral grounds.

I am willing to discard the moral grounds.

On the other grounds I would make two points. As far as the flow of funds is concerned, the same revenue loss to the Treasury, by definition, will give the same gain to corporations, be it through the credit or depreciation. As far as the profitability effect is concerned, one's conclusions will depend on the time horizon and on what one assumes about the growth of the economy.

If one takes a constant investment assumption, we might find that in order to get a given profitability effect, the annual revenue loss to the Treasury, under the credit, will be less, up to about 9 years, and more after that.

If we take a growth rate of investment of about 3 or 4 percent, the breakeven point, the year to which the credit for the same profitability effect will be cheaper to the Treasury, will be about 10 years, and the annual costs will be the same after that.

Senator PROXMIRE. At a growth of 3 percent?

Dr. MUSGRAVE. Three or four percent.

Cary Brown in his paper at the New York Economic Association meetings worked these figures out. Thus, with a limited revenue loss to the Treasury, there is a considerable advantage, in terms of the profitability effect, in the credit approach. However, I recognize Senator Proxmire's point: What about the small companies which have no funds? For them, the crux of the problem is not to tie to new investment, not to make a matching grant, but to give outright relief, which they get on their depreciation of old investment.

Senator PROXMIRE. Of course, I cannot see any reason why this would not stimulate buying and selling of older equipment, increase that kind of activity, which might have some good effect.

Dr. BERNSTEIN. I think it improves the tone of the economy generally.

May I ask you a question, Senator, by turnaround?

Why do you want to take a matter as important to the economy of the United States as the choice of tax credit, or accelerated depreciation, and say that a major consideration in the choice of one or the other method is its impact on the cash position of small businesses? Wouldn't it really be much better, considering the magnitudes we are dealing with, to choose the best method for the U.S. economy, and then, if this has inadequate effects for small corporations as compared to big, choose some method of financing which will let them take advantage of the better investment opportunities open to them?

Senator PROXMIRE. Let me say that the reason that I asked the question is exactly because I elicited this kind of response from you. You are on record now implying that if this tax credit passes, we should at least look around to see what we can do to balance the payments to small business. So you and Dr. Musgrave are on record as indicating the real advantage of this tax credit is for large business as compared to small business. It is a real contribution to public policy. We have to keep this in mind.

Votes pro and con the tax credit may be based on a very close balance, between favorable and unfavorable considerations. The small versus large business consideration might tip the balance.

Dr. MUSGRAVE. If you were to give a reduction of the corporate rate for small firms, you could give them the advantage which they would receive from applying depreciation across the board, and you could do it for little revenue cost.

Senator PROXMIRE. In other words, you turn around the ordinary regular tax and surtax?

Dr. MUSGRAVE. Keeping a proper notch arangement, one could make an adjustment so as to reduce the burden on the small companies.

Senator PROXMIRE. One balancing suggestion might be the proposal made by Senator Fulbright to have a 22 percent normal tax on corporations and a 30 percent surtax, instead of vice versa.

Just one other question.

I apologize for keeping you gentlemen so long.

Dr. Bernstein, in your statement—and I would appreciate it very much if Professor Gurley and Professor Musgrave would also give me the benefit of their wisdom on this —you say something that has puzzled me a great deal.

You say:

> We must increase our exports relative to our imports by $2.5 billion a year.

At the present time we have a $5 billion favorable balance of credit, as I understand it. This would give us a $7½ billion favorable balance of trade.

You in your colloquy with Congressman Reuss tended to agree that it might be proper for European counties and Japan, as they can do so, to help relieve some of this burden in foreign aid.

I am wondering how we can possibly expect to maintain a $7½ billion favorable balance of trade for very long without great capital export of one kind or another by this country either private or Government; and it seems to me that we are looking at this strictly and exclusively and unfortunately from our viewpoint alone, and not from the viewpoint of the other countries, which are therefore going to have a $7½ billion adverse balance of trade.

Dr. BERNSTEIN. Well, no, Senator, it is not quite as bad as that; though I think you have indicated why a little more precision helps in starting these things.

It is essential for us to have an improvement in our receipts relative to our payments of $2½ billion a year to bring our payments in order. Unless there could be a substantial change in other items in the balance of payments, which does not seem to me to be very likely, this will have to be done by increasing our exports relative to our imports.

Now, it is always true that there are balance-of-payments surpluses that match our balance-of-payments deficits.

Senator PROXMIRE. I am talking about trade; not payments.

Dr. BERNSTEIN. I know. But you see, we can have a surplus on our trade—we can increase our trade surplus, as we have an overall deficit—because there are countries that have a surplus in their overall payments, and therefore they can afford to see their imports rise relative to their exports.

We need not worry about the trade balance as such. The trade balance is an element which, when proper, is sufficient to bring the overall payments position into balance.

Senator PROXMIRE. Yes, but, Dr. Bernstein, you are going to increase the trade balance by 50 percent at a time when it is so favorable to us, at a time when we recognize that many countries are increasing their productivity, are getting into the trade market a great deal more. We are talking about trade versus aid, and we are doing all we can to encourage every nation we aid to balance their trade as much as possible. We should recognize that the reason we have an adverse balance of payments with a $5 billion favorable balance of trade is something quite artificial and quite temporary, with our foreign trade and troops abroad, and that kind of thing.

Dr. BERNSTEIN. I am sorry, Senator, to have to differ with you on this.

Senator PROXMIRE. I wish you would say why.

Dr. BERNSTEIN. First, the statement that we have a very favorable trade balance is a qualitative statement. If what you mean by favorable is an excess of exports over imports, then the word favorable does not mean we have a suitable trade balance. A proper trade balance for us is one which is sufficient to offset the deficit that in the other aspects of our balance of payments—on service account, on Government account, on long-term private investments.

Therefore our trade balance is by no means very favorable. On the contrary, I would say given the environment in which we are living, our trade balance is not good enough.

Now, that is the first thing.

Senator PROXMIRE. If I could interrupt just at this first point, my argument is that we have this $5 billion balance of trade because we have a foreign-aid program, because we have troops abroad. And if we expect to reduce these problems, at least relatively—and most Members of the Congress hope to do so; that is, get other countries into the act a little more——

Dr. BERNSTEIN. Suppose you keep our Government expenditures overseas flat from now on. Our aid remains exactly the same. Our troop expenditures remain exactly the same. But military expenditures rise on the Continent of Europe, and aid increases from the others. The significance of that for our balance of payment will be that it will create a broader market for us in which to export goods—defense equipment to Europe and other goods to countries getting aid. It will not change the need for us to increase our exports relative to our imports.

Senator PROXMIRE. But we will assume we have to continue our present foreign aid program, and continue our present troops abroad program.

Dr. BERNSTEIN. I would say this: that for the period which is relevant to our balance of payments, given the problem we have, the period in which we must restore our position is relatively short. That is to say, we have got to be thinking in terms of setting this in order in a year or two, at most. For that period, Senator, no one can foresee significant changes on the nontrade side.

Senator PROXMIRE. You see, what I am thinking about are countries like Japan, with an unfavorable balance of trade with regard to us that is serious and which is looking to China. This is a very difficult problem for her. Also, it is different for European countries, which it would seem to me are going to be looking for bigger markets and be opposed to worsening their position of trade more.

You made your position very clear, and it is very eloquent and persuasive.

Dr. BERNSTEIN. Senator, let me put it this way. It is not easy to increase exports by $2½ billion relative to imports. There are other countries that are going to fight just as hard to do the same thing. They include the United Kingdom, Canada, and Japan, to mention only very large countries.

On the other hand, there is capacity within the world to absorb an increase of our exports relative to imports without upsetting the general pattern of world payments; a strong pattern of world payments. That is what I wanted to get across.

There are countries with surpluses who are now using these surpluses to build up reserves and they can absorb the impact of a rise in our exports relative to our imports to that extent.

Senator PROXMIRE. I would like to say to Professor Gurley that I am also somewhat impressed by Gardiner Means' testimony, that it was probably a very fine and healthy thing for us that we have lost as much gold as we have over the past 15 years. If we had not, we would have had a very much more difficult situation internationally between 1946 and the present time. Having 70 percent of the gold in this country is not a good situation.

Dr. BERNSTEIN. I am glad we lost it, but I hope we stop.

Senator PROXMIRE. Professor Gurley, do you want to comment on that? I thought you might have an observation.

Dr. GURLEY. The only observation I have is that there should be more action on more fronts than perhaps Dr. Bernstein would have it.

I would like to see action not only for stimulating exports relative to imports, or trade balance, but also for reducing our military expenditures abroad and our purchases of long-term claims of various sorts.

Senator PROXMIRE. Thank you very much.

Professor Musgrave?

Dr. MUSGRAVE. I think in similar terms. I have fear that the economic report may be too optimistic about the balance of payment problem. This is a problem which is not going to be overcome very easily, as you suggest. The further strengthening of the rest of the free world economies which is fine, is going to make matters more difficult.

And I am somewhat fearful that we will have the tail wagging the dog; that we may end up with a $2½ billion balance of payment problem, keeping a $600 billion economy from being fully employed; and that we should think about developing policy means which will permit us to have high employment, which will not necessarily be helpful on balance of payment grounds, and at the same time meet our balance of payment problems.

In other words, we may have more policy objectives than we have tools to meet them. We may need to develop new ways of dealing with the balance of payments problem. Some influence over capital exports to highly developed countries is one of the things we may have to think about.

Senator PROXMIRE. Thank you very, very much, gentlemen. I deeply apologize that I kept you so long, but I just could not resist the opportunity.

I want to ask, at the request of the staff, Dr. Bernstein to answer for the record: What is your position on the payment of a differential by the Treasury to foreign central reserve banks?

Dr. BERNSTEIN. What is that again?

If you will give me the question, I will put it into the record.

(The following was later received for the record:)

The short-term rate of interest has an important effect on the attitude of foreign central banks toward holding U.S. dollar claims rather than converting dollars into gold. The Treasury has said in the past that it would consider issuing special obligations payable to foreign official institutions bearing a higher rate of interest than the market yield on Treasury bills. As these obligations would be issued outside the market and would not be transferable in the market, there would be a justification for offering a higher return. Actually, the Treasury has sold securities directly to several foreign official institutions, but the interest rates have not been higher than market rates. The Treasury sold $46.3 million of 3-month certificates of indebtedness, denominated in Swiss francs, bearing interest at 1¼ percent per annum. The Treasury sold $25 million of 3-month certificates of indebtedness, denominated in Italian lire, bearing interest at 2.70 percent per annum. This was the average rate for Treasury bills at the preceding weekly auction. The Treasury sold $450 million of 3-month Treasury bills to the United Kingdom, the proceeds of a transaction with the International Monetary Fund, at the average rate for Treasury bills at the preceding weekly auction. The Treasury has sold obligations to other foreign official institutions outside the market. Details of these transactions will be announced, no doubt, in the usual course of publication of Treasury data. There is reason for believing that the interest rates on such securities have been no higher than market rates.

Senator PROXMIRE. Thank you, gentlemen, very, very much. It has been most enlightening to me.

The committee will resume at 2 o'clock.

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

AFTER RECESS

Chairman PATMAN. The committee will please come to order.

We have with us this afternoon a panel of economists on "Investment and Growth." Dr. Gerhard Colm, with the National Planning Association, Washington, D.C., Prof. Raymond W. Goldsmith, Yale University, Prof. Daniel Hamberg, University of Buffalo, and Dr. Leon H. Keyserling, Conference on Economic Progress, Washington, D.C.

We are very glad to have you, gentlemen.

I assume that we will start with Dr. Colm. I assume that is the order in which it was understood the witnesses would appear.

We will first hear from each one and then the members will ask questions of the panel. Any material that any one of you desire to insert in connection with your remarks you may, anything that is germane to the matter under discussion.

STATEMENT OF DR. GERHARD COLM, NATIONAL PLANNING ASSOCIATION, WASHINGTON, D.C.

Dr. COLM. Thank you.

Chairman PATMAN. Dr. Colm, you may proceed in your own way.

Dr. COLM. I have a prepared statement, but if you will bear with some incomplete sentences, I would rather speak without the manuscript and offer my prepared testimony for the record. That way I believe I can save some time.

Chairman PATMAN. You may insert your testimony at this point in the record and summarize or elaborate on it any way that you desire, sir.

Dr. COLM. Thank you.

(The statement referred to follows:)

STATEMENT BY GERHARD COLM[1] ON INVESTMENT AND GROWTH, PREPARED FOR THE PANEL DISCUSSION BEFORE THE JOINT ECONOMIC COMMITTEE

ECONOMIC GROWTH AS AN OBJECTIVE

The American economy has grown in terms of GNP (in constant prices) at an annual rate of 3.5 percent from 1947 to 1960. President Kennedy, in the Economic Report of January 1962, has stated: "Increasing our growth rate to 4½ percent a year lies within the range of our capabilities during the 1960's." The Economic Report presents the reasoning of the President and the Council of Economic Advisers why they believe that an increase in the rate of growth should be an objective of vital importance for the United States.

I welcome the President's and the Council's emphasis on economic growth as an objective and I am glad that the joint committee has endorsed the emphasis by dedicating one of their panels to this topic.

The emphasis on growth is important because only an economy of rising production and productivity can support the foreign economic policy of the United States which is called for in the present world situation. The United States

[1] Chief Economist, National Planning Association. The views expressed do not necessarily reflect those of the NPA.

has joined with the other 19 members nations of the OECD in setting a 50-percent increase in total production within a decade as a target for the Western World. The Council speaks of the U.S. ability "to meet, and even to exceed this target." Only the increase in productivity implied in such a rate of growth wil make it possible to solve the U.S. balance-of-payments problems without resort to restrictive policies which would run counter to major policy objectives. Only such a rate of growth would produce the tax revenues on the Federal, State, and local levels which will be needed to meet the many tasks such as providing for adequate education, health, and research, rebuilding cities and rural communities, conquering poverty at home, and supporting development abroad. Economic growth is the only source providing a painless increase in tax revenues.

Furthermore, an economy without adequate vigor of expansion will at best bump from recession to recession with rising unemployment even at the peaks. Anticyclical monetary and fiscal policies are likely to prove mere palliatives unless supported by longer run promotion of economic growth.

While I agree that a growth rate of 4 to 4½ percent is a desirable objective, I also agree that a more rapid rate of growth is desirable for periods of recovery from a recession or for emergency periods. However, a considerably higher rate as a long-term goal might bring us into conflict with other objectives of policy such as stabilization. I hope this committee will endorse the President's target for increased economic growth.

There are good reasons for expecting a continuing recovery movement which is likely to carry us through the rest of the year. There is much less agreement whether this recovery movement left to its own momentum will head into a prolonged period of economic growth, into another period of near stagnation, or even into a renewed recession. The President and the Council believe that with the policies recommended in the report, it is assumed that the recovery will not lead into a renewed recession but into a satisfactory rate of growth. I assume the committee, in formulating the topic for this panel, wanted the witnesses to examine the measures proposed to promote economic growth, with particular emphasis on the problem of investments.

PROMOTION OF ECONOMIC GROWTH BY EXPANSION OF DEMAND AND INVESTMENT

In order to ascertain what measures are likely to promote an increased rate of economic growth, it is first necessary to determine what obstacles may have stood in the way of a higher rate of growth in the past.

The Council's report answers this question with desirable clarity. "Faster economic growth in the United States requires, above all, an expansion of demand, to take up existing slack and to match future increases in capacity. Unless demand is adequate to buy potential output, the growth of potential is neither an urgent problem nor a promising possibility. Full utilization will itself contribute to growth of capacity" (p. 108). This is the beginning of the chapter on economic growth, and to make sure that this most important point is not forgetten, it is restated in the "Conclusion" (p. 142): "Capacity to produce is not an end in itself, but an instrument for the satisfaction of needs and the discharge of responsibilities. The needs will go unfilled and the responsibilities unmet to the extent that growing productive power runs to waste in idle machines and unemployed men."

I agree with this basic position of the Council. Nothing discourages an increase in investments and future growth as much as idle capacity; nothing stimulates investments as much as a high rate of operation and the expectation of expanding markets. Needless to say that aggregate demand includes not only consumer demand, but also business demands for new producers' goods, and Government demand. The Council recognizes "the budget, the tax system, control of the supply of money and credit" as the main policy instruments for assuring an adequate and not excessive increase in aggregate demand. I entirely agree with this basic position. The question remains to be asked, however, whether the budget, tax, and monetary policies of the administration are likely to support over the years the needed increase in aggregate demand. While the principle is stated with admirable clarity the consequences, especially for budget and tax policy are not spelled out in detail. The freedom to adapt monetary policy to the requirements of domestic economic growth is limited by balance-of-payments considerations. This places an additional responsibility on budget, lending, and tax policy to support an increase in aggregate demand which is in line with, but not in excess of, the growth objectives.

The Council's report presents a very interesting estimate illustrating the production and employment targets which must be reached in order to reduce unemployment to 4 percent by 1963. This intermediate goal requires an increase in private nonagricultural employment by 4.6 million over a 2-year period. We never had any such increase before except under the special circumstances of the beginning and the end of the Second World War, and in spite of a healthy recovery in production, until December 1961, very little progress has been made toward the 1963 target. I am not sure that foreseeable developments in the private economy and proposed budget and monetary policies give us assurance that the Council's intermediate target will be reached by 1963. As the committee had a special panel on fiscal and monetary policy this morning, I will not go into this topic.

While the increase in demand is a necessary and primary condition, it is not the only condition for increased economic growth over a longer period of time. The report recognizes that long-term increase in economic growth depends on increased investments, investments not only in plant and equipment but of equal importance, investments in research, in education, training, and health. Programs in these areas are justified because they add to human welfare but also because they contribute to productivity and thereby promote economic growth. These investments in human capital contribute to growth and become more feasible by growth. Just as growth creates markets, incomes, profits, and thereby facilitates the financing of business investments, growth also results in higher tax yields and the means for financing increasing public investments in human capital.

The Economic Report presents "illustrative" estimates of total production ($825 billion in 1961 prices), employment, and productivity in 1970 compared with 1960. I welcome the fact that the report complies with the letter and spirit of the Employment Act in presenting estimates of the level of production and employment needed to accomplish the objectives of the act. However, the report does not spell out the role of consumption, investments, and Government in such a needed increase in production and employment.

If I have any criticism of this report then it is that there is a gap between the excellent analysis and the rather general proposals for implementation. There is no quantitative estimate of the role which private business and the Government should play in achieving the desired increase in production. I believe that the time has passed when Government operations could be planned from one year to the next. Most corporations have adopted long-term investment programs and this practice has greatly contributed not only to the stability of corporate investments but also probably has increased the shock resistance of the economy as a whole. Both for efficiency in Government programs and for promoting steady economic growth, it appears imperative to relate long-range budget planning to the objectives of economic growth.

In this connection, it would be of great importance if a long-term Federal budget outlook were presented which included expenditures under existing legislation, under recommended legislation and also, possibly with alternatives, under programs which are under consideration and may result in future recommendations.

Adequate aggregate demand and adequate Government investments in human capital are essential conditions for promoting private business investments. Nevertheless, the administration proposes not to rely exclusively on the incentives for increased business investments which result from these factors. It proposes to create an additional incentive for modernization and expansion by the investment tax incentive proposal and by more liberal depreciation allowances. One could say, "let us wait with the adoption of such additional incentives until we have observed what the effect of rising demand and a rising ratio of business operation will be." If we were only concerned with increasing the rate of growth one might well favor such a policy of "wait and see." However, a more rapid modernization of our productive plant and equipment is imperative in order to promote the international competitiveness of American industry. As accelerated investments are useful for both increasing the rate of economic growth and improving our export position, I hope that this committee will urge the legislative committees and Congress as a whole to adopt these tax proposals. However, it cannot be emphasized enough that an investment incentive can be effective only if technological advances are made and adopted and if skills are developed and if a continuing increase in effective demand is realized. Promotion of technological advances and of their prompt adoption is a necessity in the present situation even though it must be recognized that such advances in turn require additional public and private provisions for retraining and other measures for mitigating the impact of rapid technological change on the labor force. These are the essential conditions for expanding investment and an increased rate of growth. The investment incentive, taken by itself, would be ineffective and result in a substantial loss of revenue without compensating gain.

PROMOTION OF ECONOMIC GROWTH BY INCREASE IN SAVING

The basic argument in the Economic Report is that economic growth has been held back by lack of adequate increase in aggregate demand in recent years. This view is in contrast with an explanation given by others that investment and growth were impeded by inadequate saving. The latter view has been attributed to Simon Kuznets, one of the most knowledgeable experts on matters of economic development. As reference was made to his book in the invitation for this panel, I will briefly discuss the position Kuznets has taken in his monumental work "Capital in the American Economy: Its Formation and Financing." (National Bureau of Economic Research. Princeton University Press, 1961.) Kuznets states as his basic conviction: "In a society such as ours, the basic decisions that determine capital formation are those made by households, business units, and governments, in the disposition of their income between current expenditures and savings" (p. 391). In contrast with the rather dogmatic statement which I have quoted, I personally believe that adequate financing is a condition of economic growth but not its primary determinant and moving force. Kuznets admits the possibility that capital formation and economic growth were held back over the long-term by limited investment opportunities rather than by limited savings. However, he personally leans toward the conclusion that capital formation was held down by the limitation on savings, particularly as a result of the rapid pace of emulative consumption and the heavy income and inheritance taxation (p. 388). However, Kuznets states this opinion only as a reasonable impression and as a suggestion for further exploration.

Kuznet's position is not necessarily in conflict with the opinions expressed in the Economic Report because he has been analyzing the long trend of the past and taking a long look into the future. He might regard the lack of aggregate demand as an explanation of the recent decline in growth as a prolonged cyclical phenomenon. The belief that the increased rate of growth after full employment has been reached may require an increase in the ratio of saving at some future time is expressed also in the Economic Report. The report especially considers that a budget surplus at full employment may be desirable, to help to finance the formation of capital.

It is not impossible that at some future time a rapid increase in capital investment may require measures to stimulate an increase in the ratio of saving. As a matter of fact, there are nations where this condition exists today. For the United States there is no conclusive evidence which suggests that a general lack of saving has held down capital formation and economic growth in recent years. On the contrary; it is my opinion that the greatest brake on business investments has been the existence of idle or underutilized resources in our economy. Therefore, for the immediate future, our first task is to put all our resources to work.

With respect to the more distant future, I admit that I am not sure. Obviously, productive capacity must be increased at a faster rate if the increase in production is to be raised. Over the long run, technological advances have made it possible that somewhat reduced dollar outlays for capital investments were needed to increase output by $1. This increase in the efficiency of capital was in part due to the fact that more equipment could be packed into a given plant, thus reducing the relative high outlays for factory buildings. If these trends of the past should be resumed, it is possible that an unchanged ratio of capital formation and saving to total production will be compatible with a higher rate of growth in production. Actually our own estimates suggest that a relatively small increase in the ratio of business investments to total production would be needed for the desired increase in the rate of growth. In an age of continuing technological revolution, it cannot be assumed that while everything else changes the capital-output ratio of the economy remains constant. It appears more likely that this ratio will decline rather than rise (at least as long as we do not capitalize the investment in education and research in our accounts). Nevertheless, the statistical bases for these statements are everything but firm which applies both for Kuznets' and my conclusions. Therefore, I doubt that it would be wise now to determine future tax and other policies with a view to promote savings at the cost of consumption. I personally welcome an increase in the rate of saving of families because a sizable nest egg adds to the feeling of security of individuals. I also welcome the rise in pension and welfare funds which have become such an important part in our national savings. I believe, however, that it is misleading to regard a lack of saving as a primary obstacle to an increased rate of growth in the past or the foreseeable future and to suggest that a policy designed to stimulate saving would be the best way to promote economic growth.

Under conditions as they exist or are likely to develop in the foreseeable future in the United States, I doubt especially that increasing tax revenue in excess of Government expenditures would be a useful device to create compulsory saving for financing an increase in business investment. This particular suggestion of the Economic Report is not offered as a rationale for the proposed budget surplus in the fiscal year 1963 and has little relevance for the report's basic approach to the immediate task of promoting economic growth.

Dr. Colm. Mr. Chairman, President Kennedy has stated in the economic report that we could achieve a rate of growth of 4.5 percent, which compares with about 3.5 percent for the average of the years 1947 to 1960. I have in my prepared statement three pages of why I think the increase in the rate of growth is a very desirable objective. First I intended to omit this because I thought it was self-understood. However, I was here this morning and listened to the discussion when one of my good friends and colleagues said we shouldn't put too much emphasis on growth. Therefore, with your permission, I change my mind and say why I think that this is a very vital objective of American policy.

I think it is a vital objective for both domestic and international reasons. Mr. Chairman, I submit there are a lot of things to do in the United States. We have to do much more in research, education; we have a tremendous job of urban renewal. We still have poverty in spite of the so-called affluent society. These things require larger private and Government expenditures. I don't think there would be much likelihood that we will make needed progress on these programs unless we grow. We have to obtain more revenue in order to finance all of these domestic and international objectives. We know there is only one source for additional taxes which is not painful and that is economic growth. That is the only painless source for additional taxation. But also internationally, I submit that growth is a very important objective.

I agree with what Richard Musgrave said this morning that we should not engage in a statistical race either with the Soviet Union or Japan or Western Germany because conditions are very different. However, unless we succeed in making full use of our potential, I don't see that we can arouse much enthusiasm for our political, economic, and social system. I want to be quite clear that I do not recommend any effort of matching the 8 to 10 percent rate of growth that some other countries have achieved for a number of years each year. But I think that the objective stated by the President of 4½ percent is one which takes account of our international and domestic needs, which is in line with the commitment the OECD countries have made jointly last November, and also is not a rate of growth which would necessitate such heroic methods as coming into conflict with other objectives, for instance price stability. So I propose that the 4½ percent annual rate of growth is a very reasonable goal once we have achieved high employment. I guess what the joint committee wanted in asking for this particular panel was a discussion of the likelihood that some such increase in the rate of growth could be achieved, and how we judge the policies which are recommended in the light of this objective.

I entirely agree with the point made in the economic report that one of the reasons for the inadequate rate of growth in the past is that we had repeated recessions. We had four recessions in the short postwar period. From that might be concluded that all we need do is adopt anticyclical policies and measures, and several are recommended by the President. I think, indeed, it would be most desirable, having more flexibility—more flexible tax and more flexible expenditures policies, although I think that there might be some discussion of how this flexibility could be best achieved. But besides that, I feel it is more important that public policy and private endeavor operate so that we achieve sustained growth and need not act after we have gone into a recession. Anticyclical actions often become effective too late. The economic report I think rightly emphasizes as a main condition for sustained economic growth that we should have an adequate expansion in aggregate demand. The report analyzes the reasons for inadequate growth largely in terms of inadequate expansion of aggregate demand in the past.

Mr. Chairman, there was some discussion this morning about the adequacy of the budget and monetary policy to achieve that adequate expansion of demand. I think particularly in light of the balance-of-payments position the first emphasis has to be on budget policy in this respect. The Economic Report characterizes the 1963 budget as slightly restraining. I think that term is used. I believe the 1963 budget has a slight expansionary effect. It was quite correctly pointed out this morning by, I think, almost everybody on the panel, that whether there is a surplus or deficit is not the essential criterion, as long as expenditures go up. Even a faster rise in revenue may not result in a net deflationary effect. Whether the budget is sufficiently expansionary, I do not know. Personally, about 2 months ago, I published an estimate that the 1963 budget would end up with a $2 billion deficit in the conventional budget. From my study of the budget document I am not entirely convinced that I should revise that estimate. At least, I don't do it at the present time. I will wait awhile for that.

Monetary policy was also discussed this morning, but I would like to mention that I am afraid that the threat of the balance-of-payments situation is somewhat used as a club over the monetary policy. While there are restraints, I think the time is too early to switch over to a tight money policy.

Mr. Chairman, I want to bring to your attention that there is an indication in the Economic Report which says that if we are to achieve a 4-percent rate of unemployment, which is not regarded as a desirable target but as a kind of interim goal, if we are to achieve this very modest goal by 1963, we have to add 4.8 million to the jobs in private nonagricultural employment. So far we have made some progress toward this objective, namely to the extent of, I believe, 600,000. Mr. Chairman, I submit that this is a rather disturbing performance, at a time when we had a very healthy recovery, in comparison with other recoveries. But the progress toward anything which, very modestly, could be called an adequate employment level, that progress is very poor. We have moved $600,000 toward an objective of 4.8 million. This, in my opinion, indicates that more needs to be done in order to achieve our objective in the foreseeable future. The Economic Report puts, I think, very good and entirely accurate emphasis on the need for expansion of adequate demand in accordance with the expansion of the productive potential. However, the report is not specific in showing that under the proposed budget and monetary policy the increase in aggregate demand will be adequate to reach this 1963 objective.

The report quite correctly does not only emphasize adequate demand, but also very properly emphasizes that for the long-run economic growth very important are investments in which we have private and public programs, but particularly public programs and responsibilities.

The report also correctly emphasizes that for increased economic growth we need more private plant and equipment. Nobody would question that. But there are rather vague allusions to the proposition that in order to achieve the higher rate of growth we have to divert into plant and equipment, resources which with an increase in the ratio of capital investments, private capital investments, to gross national product. The report fails, in my opinion, to guarantee these relationships. There is a very desirable illustrative table which shows that by 1970 with full employment we should reach, I think, $825 billion, in 1961 prices, and it shows what employment and productivity would be under those conditions. But there is no estimate of the role which the public sector and the private sector—investment, consumption and so on would play—in reaching this objective. In stating goals, I think, the report comes closer than any previous report in complying with the spirit and the letter of the Employment Act. I think not enough can be said in praise of that fact. However, I feel it is only a first step, and further steps have to be taken in order to make these goals meaningful as a guide for policy.

Mr. Chairman, I do believe that in order to step up economic growth to 4.5 percent an increase in the ratio of capital investment to GNP is needed. Through the years 1950 to 1960 we had nonagricultural investment in plant and equipment of 8.6 to 8.7 percent of total GNP. Our computations indicate that we need a ratio of about 9.6 percent, which is increase by 1 percent, in order to achieve a rate of growth of 4 to 4½ percent. This is substantial, but it is not as much as I think one can read into the qualitative statements made by the Council, and certainly not those made by other people. The President in his report and the Council recommend two measures for stepping up the rate of private investment, namely a more liberal depreciation schedule, which primarily is justified on other grounds but which would also support growth, and, second, an investment tax credit. I cannot go into this in detail, because I want to stay within 20 minutes, but let me only give you my recommendations on this.

I am personally very much in favor, first, that our schedule F be brought up to date, which means a liberalization of depreciation. We have a more speedy process of obsolescence in the modern technological age, and I think the schedule F should reflect that.

I am also in favor of the investment credit because it would further the technological advance and thereby also support the higher rate of growth. But I make this recommendation only with two qualifications: One, any measure for supporting a higher rate of business investment is futile unless the first requirement of growth is met—namely, adequate demand expansion. Speeding up capital investment is futile without seeing that outlets are created, and aggregate demand includes private consumption, business investments, and Government. Without adequate outlets it would only give us a short-term upturn leading to an early collapse of such a temporary upswing. Only if the two measures go together could I be in favor of policies designed to step up investments.

Secondly, if we were only concerned with economic growth I might take the position, Mr. Chairman, of "let's wait and see." If we have adequate demand, we know that alone will stimulate investments and will generate more savings. It might work out without a special tax incentive.

I am, however, not in favor of a wait-and-see policy because the same measure has another objective, namely improving our competitive international situation, and there we cannot wait. I know the risk involved; I know that the two measures combined mean a loss of revenue of something like $3 to $3.5 billion, even though some loss may be recovered, but it would be more than a $3 billion net loss. If we don't expand adequate demand that increase in productivity capacity will not be utilized, and we will have losses in revenue without compensating gains. But I think that if combined with these other policies, with increases in adequate demand, with investment in social overhead costs, research, education, training, in combination with those other measures, I think it could serve both purposes, namely supporting increased economic growth and also supporting our competitive situation.

Mr. Chairman, I have in my prepared statement a discussion of Professor Kuznet's book which allegedly came to the conclusion that the bottleneck for economic growth is a lack of saving, partly due to emulative consumption, as he calls it, and partly due to the income and estate taxes. I went into that because your executive director, in inviting me for this panel, called my attention to this book.

Since my time is up, I will not go into details of Kuznet's book. I only like to say that Kuznet really doesn't offer that as a definite conclusion from his study. He only says that is an "impression" which he offers as a spur for more research work. So, Mr. Chairman, I will stop at this point.

Thank you.

Chairman PATMAN. Thank you, Dr. Colm.

Professor Goldsmith, we would like to hear from you at this time.

STATEMENT OF RAYMOND W. GOLDSMITH, PROFESSOR OF ECONOMICS, YALE UNIVERSITY

Mr. GOLDSMITH. In contrast to Mr. Colm's policy statement, mine is very academic. If you want to find anything out about my policy views, you will have to ask me. The statement is too long to be read in full. I would, therefore, suggest that you insert the full statement, and I read you parts of it.

Chairman PATMAN. It will be inserted in the record at this point. Then you can comment on it, if you please, Professor.

(The statement refered to follows):

STATEMENT OF RAYMOND W. GOLDSMITH, PROFESSOR OF ECONOMICS, YALE UNIVERSITY, BEFORE THE JOINT ECONOMIC COMMITTEE

Regretfully but unavoidably I must begin with apologies, traceable in part to the chairman's kindness in allowing members of the panel to select in their statements any aspect of the broad subject of investment and growth which they regard as important and on which, I suppose, they are least incompetent to deal. I have taken advantage of this license to select three topics which, though I regard them as important and as relevant to your committee's inquiry, are not likely to be popular. I also regret that due to the short time available and the pressure of other obligations, I have not been able to avail myself of the privilege of preparing a paper for the record that would amplify and document the obiter dicta, as the lawyers say, to which I shall often have to limit myself in this statement. I shall, of course, be glad to remedy these deficiencies as far as possible in answers to your questions.

My first duty, as I see it, is to give you a sketch of the trend in capital formation in the United States as background for discussion. This will be dull, I fear; but not too contentious, I hope. I shall then try to impress upon you that the relations between investment and growth are much more complicated, both as problems of analysis and of policy, than they are often presented; and that the answers are much more uncertain than popular discussion would lead one to believe. This may be unwelcome, I fear, because by casting doubts on some cherished presumed home truths, I shall seem to act as the devil's advocate. Finally, I shall argue that we know altogether too little about the facts to make confident predictions, or to prescribe with assurance policies in the field of investment and its effect on growth. I shall, therefore, plead—and this will be doubly unpopular because it costs money—for the collection and analysis of facts and figures not now available that may increase our understanding of the relationships between the level and structure of current investment and the stock of capital on the one hand and the many factors determining economic growth on the other.

In reviewing the long-term trend of capital formation in the United States it may be best to concentrate on one problem that seems to have attracted considerable attention recently; the alleged sharp fall in the ratio of capital formation to national product, i.e., the decline in the share of current output devoted to increasing national wealth.

The measurement of capital formation, particularly if a figure net of capital consumption is wanted, is one of the most difficult subjects in economics, both conceptually and statistically. This is not the place, nor is there the time, to enter into discussion of the numerous technical problems involved; or to try to reconcile the differences among the various estimates which are substantial. You will see immediately, however, that these nasty problems cannot be swept under the rug entirely.

The first table which you have before you presents some of the basic data, while the chart shows four sets each of estimates of the ratio of net and gross capital formation to national product, probably the simplest summary measure of the importance of capital formation in an economy. Most of these figures have been taken from one source, Professor Kuznets' recent basic study of "Capital in the American Economy," in order to avoid the complications inherent in using the results of different estimating procedures.

TABLE I.—*The share of capital formation in gross national product*

[In percent]

A. CURRENT PRICES

	Excluding consumer durables			Consumer durables			Total		
	Gross capital formation	Capital consumer allowance	Net capital formation	Gross capital formation	Capital consumer allowance	Net capital formation	Gross capital formation	Capital consumer allowance	Net capital formation
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
(1) 1869–78	20.3	8.0	12.3						
(2) 1879–88	20.6	8.7	11.8						
(3) 1889–98	23.1	10.7	12.5						
(4) 1899–1908	22.8	10.5	12.4	6.3	5.0	1.3	29.1	15.5	13.6
(5) 1909–18	20.9	11.5	9.4	7.1	6.3	.8	28.0	17.8	10.2
(6) 1919–28	22.0	11.3	10.8	9.2	7.4	1.8	31.2	18.7	12.5
(7) 1929–38	15.5	13.4	2.1	8.0	8.2	−.2	23.5	21.6	1.9
(8) 1939–48	17.1	13.2	3.9	7.7	6.0	1.7	24.8	19.2	5.6
(9) 1946–55	21.9	14.2	7.7	9.1	6.3	2.8	31.0	20.5	10.5

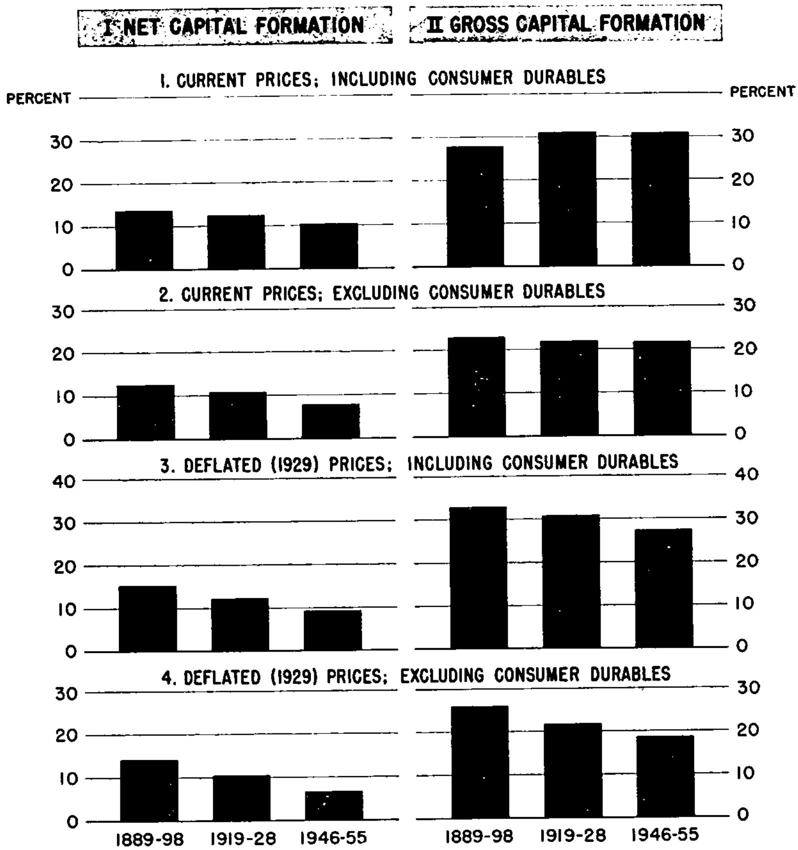
B. DEFLATED (1929) PRICES

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
(1) 1869–78	23.4	9.5	13.9						
(2) 1879–88	22.9	9.8	13.1						
(3) 1889–98	26.0	12.1	14.0						
(4) 1899–1908	24.2	11.3	12.9	7.7	6.2	1.5	31.9	17.5	14.4
(5) 1909–18	22.6	12.3	10.3	8.0	6.9	1.1	30.6	19.2	11.4
(6) 1919–28	21.9	11.5	10.4	9.1	7.3	1.8	31.0	18.8	12.2
(7) 1929–38	14.4	12.6	1.8	8.9	8.2	.7	23.3	20.8	2.5
(8) 1939–48	15.9	12.1	3.7	8.8	7.0	1.8	24.7	19.1	5.6
(9) 1946–55	18.8	12.2	6.6	8.8	6.1	2.7	27.6	18.3	9.3

Source: Cols. 1–3, S. Kuznets, "Capital in the American Economy," pp. 92, 95. Cols. 4–6, based on R. W. Goldsmith, "The National Wealth of the U.S. in the Postwar Period and a Study of Saving in the U.S.," vol. I.

CHART I

VARIANT ESTIMATES OF THE SHARE OF CAPITAL FORMATION IN GROSS NATIONAL PRODUCT 1889-98; 1919-28; AND 1946-55



If you look at the left bottom panel of the chart you may indeed share the alarm many reviewers of Professor Kuznets' book have shown. The proportion of our national product used to increase our net stock of capital seems to have declined from approximately 14 percent in the 1890's to 10½ percent in the 1920's and to a mere 6½ percent in the decade following World War II. These three periods have been selected because they are sufficiently distant from each other to reflect long-term changes; because they are not directly affected by the two world wars or the great depression; and because their position in the long swings is reasonably similar. (The series unfortunately end with 1955, but figures for the 1950's probably would not be much different from those shown for 1946–55.) This result is reached by excluding consumer durables from the stock of durable assets, and by adjusting both capital expenditures and national product to the price level of 1920. If you now direct your attention to the left top panel, a variant of the share of capital formation in national product which I regard as more appropriate for some purposes because it includes consumer durables and is based on actual (undeflated) values, you will receive quite a different impression. The ratio of net capital formation to national product shows only a slight and fairly regular downward trend from about 13½ percent in the 1890's to 10½ percent in the postwar period. The decline in the capital formation ratio between the 1920's and the 1950's thus is not unprecedented either in direction or size, and this is true irrespective of the variant of the ratio you may choose to select. There is, therefore, no need to invoke explanatory factors specific to the postwar period.

Should you choose to disregard capital consumption and use the figures for gross capital formation shown in the right half of the chart, you would find a substantial decline in the capital formation ratio only if you excluded consumer durables and preferred deflated figures. The three other variants of the capital formation ratio show either a modest decline between the 1890's and the 1950's; or, if consumer durables are included and actual values are used, even a small increase. Use of gross figures, while for many purposes less appropriate than those of net ratios, is not wholly unjustified. If a measure of the additions to capacity to produce is wanted, something between the gross and net ratios may be the most appropriate figure.

So much about the bare figures. Let me add, although there is no time to explain this opinion, that I am inclined to doubt the existence of a significant decline in the share of capital formation in national product over the past generation. It is possible that the capital consumption allowances in the estimates I have used here overstate the decline in the ratio of net to gross capital formation, among other reasons because of the apparent failure to take account of the acceleration in the rate of quality improvement in many types of durable goods.

II

It is not, however, the movements of capital formation, in absolute figures or as a percent of national product, in which we are primarily interested, but the relation of capital formation to economic growth. Let us again begin with the actual data for the United States.

Table II permits you to compare the ratio of net capital formation with the rate of growth of real national product per head for decadal periods between 1869 and 1955. The main impression you will probably receive from this comparison is the absence in the historical record of a clear-cut, steady relationship between the intensity of capital formation (the ratio of capital formation to national product) and the rapidity of economic growth (the rate of increase in output per head). The rate of growth of output (and income) per head was about the same in the 1890's and the 1950's—approximately 2 percent per year—although the share of capital formation was lower in the more recent period, spectacularly so if you accept the variant excluding consumer durables and using deflated figures. On the other hand, both the capital formation ratio and the growth rate were very low in the 1930's, while the growth rate was very high but the capital formation rate very low during the 1940's. To complete the possibilities we also have one example of an average ratio of capital formation associated with a low rate of growth (the decade ending 1918) and one of relatively high rates for both capital formation and growth in output per head (the decade ending 1908).

TABLE II.—*Rate of growth and capital formation ratio*

Decade ending—	Rate of growth (percent per year) [1]			Capital formation ratio (percent) [2]	
	Gross national product (1)	Population (2)	Gross national product (per head) (3)	Including consumer durables (4)	Excluding consumer durables (5)
1888	4.5	2.3	2.3	(13.0)	11.8
1898	3.8	2.0	1.8	(13.7)	12.5
1908	4.4	1.9	2.5	13.6	12.4
1918	2.7	1.5	1.2	10.2	9.4
1928	3.7	1.6	2.1	12.5	10.8
1938	−.2	.8	−1.0	1.9	2.1
1948	4.3	1.2	3.1	5.6	3.9
1955	3.8	1.7	2.1	10.5	7.7

[1] Based on 3-year averages (estimates of Simon Kuznets for col. 1) centered on last year of current and preceding decade.
[2] From table I, pt. A.

Similar comparison can also be made between the capital formation ratio, as the presumed casual factor, and various measures of productivity; e.g., output per man-hour or output per unit of input of all types of resources (labor, capital, and land). While the exact result of such comparisons depends on the measure of productivity used and the author of the estimates, the results are likely to be even more disappointing than those of the comparison of capital formation ratios and growth of national output per head just presented. Decadal changes in productivity seem to be little and irregularly affected by differences in the capital formation ratio.

The fact that the rate of growth of output per head was approximately the same in the 15 postwar years as during the first three decades of this or the last three decades of the 19th century, although the capital formation ratio was lower, is more than an historical curiosity. It points to a basic change which appears to have taken place in the American economy and which is reflected in what economists call the aggregate production function; i.e., the form of the relation between the volume of inputs of capital, land, and labor and the volume of output of goods and services, a subject to which your distinguished member, the senior Senator from Illinois, has made such outstanding contributions when he was still one of ours.

While the inputs of capital and labor alone could account for most of the increase in output up to the 1920's this is no longer true. The statistics indicate that a given percentage increase in the input of both capital and labor now produces a more than proportionate increase in output. The economy as a whole works under increasing returns, and this extra return can be attributed to technological progress, to use one vague word for a congeries of many and diverse factors that are extremely difficult to disentangle. Recent intensive investigations (e.g., by Professor Kendrick of the National Bureau of Economic Research, Professor Solow of Massachusetts Institute of Technology, and Mr. Denison of CED) agree that the majority of the observed increase in output is attributable to technological change. If these findings stand up under further intensive examination—and there is now no indication that they will not—they cannot be ignored in an assessment of the decline in the aggregate ratio of capital formation to national product, whatever its exact size may ultimately be determined to be. If the national production function is of a form that involves an increase in output higher than the increase in the input of either capital and labor, then the capital formation ratio may decline without bringing about a decline in the rate of growth of output per head. Indeed, if technological progress is rapid enough, a declining capital formation ratio is compatible with a rising rate of growth.

Technical progress, although often originating in an individual's brain and requiring no implements beyond pencil and paper, is not altogether separable from capital investment. It generally take tangible durable assets—machinery and structures—to embody technical progress. This, however, does not mean that the more rapid technical progress the more new capital is needed, particularly in relation to output. It depends on the character and intensity of technical progress whether the same rate of growth requires an increasing, unchanged, or even a declining capital formation ratio. Since technical progress is as a rule embodied in machinery rather than in the other components of capital formation (structures, inventories, monetary metals, and foreign claims)—and modern technology seems to tend more and more in this direction—the volume of gross and net investment in machinery and equipment and its relation to national product may be more pertinent in studying the relations between investment and growth than the aggregate of all forms of capital formation. It is therefore relevant that the share of "producer durables" in national product has not declined at all over the past century on a net basis, whether measured in current or deflated prices, and has considerably increased in proportion to total capital formation.

I certainly do not want to argue that no systematic relationship has existed in the United States during the past century between capital formaion and economic growth even in the long run. (There is an evident positive relation over the business cycle not visible in the figures I am using here.) Nor do I wish to assert that such a relation could not be shown to exist and could not be measured if more advanced statistical techniques were brought to bear on the data—including the obvious introduction of a lag between the dates of capital expenditures and of increase in output—or if the century were broken up into other than decennial periods; e.g., into full cycle averages. The fact remains, however, that the historical record does not disclose an obvious, regular unchanging association between the intensity of capital formation and the rate of economic growth. Economic growth is dependent on "* * * the interaction of * * * the advance of knowledge, the improved skills of the working population, and the rise in capital per worker * * *" as the Economic Report correctly stresses. On this empirical basis the burden of proof would seem to be on those who claim that an increase in the ratio of capital formation, beyond its apparent trend line, over one or more full business cycles will in and of itself—and these are the key words—lead promptly to an acceleration in economic growth; i.e., an increase in the rate of growth of real national product per head. If there is such an association the increase in the capital formation ratio required for a substantial increase in the rate of growth, say by one-half of 1 percent a year, is probably considerably larger than is often imagined, and is large enough to require far-reaching changes in our financial and business organization.

III

Since the United States is not an island (in Donne's sense), nor the American economy a phenomenon sui generis, I now ought to review the evidence on the relation between capital formation and economic growth that other economically advanced countries provide. There is neither the time to do this, rewarding as it might be; nor are there data comparable in length and detail to those at hand in the United States. The best I can do, therefore, is to quote to you a few sentences from the conclusions of what is so far the most intensive statistical exploration of this problem. Here is what Professor Kuznets says:[1]

"* * * while capital formation proportions did rise with the secular rise in per capita income in some countries * * * the rise ended fairly early, while per capita income continued to grow at substantial rates; and in others * * * a significant rise in the national capital formation proportions did not begin until after several decales of vigorous growth of * * * per capita product * * *."

"* * * the different levels of national capital formation proportions were not associated with differences in per capita income * * *. Nor was there any close similarity among countries either in the average level of their capital formation—output ratios * * *; or in the movement of these * * * ratios."

And now for the crucial statement:

"At some danger of exaggerating, one might say that the rather simple relations assumed in much economic analysis—close association between levels of income and savings proportions and between capital formation proportions and the rate of growth—are not confirmed by the long-term records."

"Our findings * * * suggest that the savings-income capital-growth relations have been far too variable * * * to retain much usefulness as guides in either analysis or policy."

All I can add is that the investigations which I have made myself on the relation of capital formation and economic growth in industrial countries are in agreement with Professor Kuznets' conclusions that I have just read to you. As in the case of the United States there is some tenuous association between the intensity of capital formation and the rate of economic growth, particularly when very large noncyclical changes are involved. The association is much too irregular in fact and too uncertain in its causal mechanism to permit this simple prescription: If more economic growth is wanted, all that is needed is to increase the ratio of expenditures on durable goods to total national product.

IV

That we cannot now say with a reasonable degree of confidence much that is relevant about the relations of investment and economic growth—or, for that matter saving and economic growth—that is not so vague as to lose all value as a guide to policy, does not mean that we never will. It means, however, that a determined effort will be needed, first, to collect and marshal data that are relevant to the problem; and, then, to analyze them in such a way that the results can have practical application. In view of the limitations of time and competence I shall have to restrict my suggestions to one fairly specific project in this broad field, one only but perhaps one of critical importance. This is the need for an inventory of the national wealth of the United States.

[1] Economic Development and Cultural Change, IX, 4 II (July 1961), pp. 55–56.

Every business, and some governmental organizations too, have in addition to an income account, a balance sheet which reflects assets and liabilities at the beginning and end of the year. No balance sheet is available on a consistent and detailed basis for the United States as a whole, or for the economic sectors or regions which make up our economy, except possibly for agriculture.

We are thus unable to answer questions such as: How is the national wealth of the United States divided among the States? Among industries? Among the main sectors of the economy? What proportion of equipment in the United States, or in Texas, or in the textile industry is older than 10, 20, or 50 years? What is the share of automatic and semiautomatic equipment in different industries and different regions? What proportion of plant and equipment—for the United States as a whole, for any industry—was not utilized during last year? Does the value of fixed capital per man or per unit of output in a given industry differ as between establishments in different States, or establishments of different size? How rapidly are certain types of equipment actually retired—sold or scrapped—or relegated to standby use, in different industries? How much of plant and equipment now in use was acquired new or secondhand? Does the ratio between new and hand-me-down equipment differ among industries; between large and small firms; among different parts of the country? What is the value of the main subsoil assets in the different States? How does the value of governmental structures and equipment in the various States compare to their tax receipts, their expenditures, and the income of their citizens? Is the relation between the value of fixed capital and output in a given industry dependent on the size of the establishment, on the age of the equipment, on the location of the plant, on other factors?

In other words, in an economy characterized by the importance of industrial plant and equipment we hardly know anything, in reasonable detail and with reasonable precision, about how much of the different types of equipment we have, in what shape it is, and how it is utilized.

Without this information it is hardly possible to assess the contribution of the stock of capital to output; to estimate future capital requirements for replacement or expansion; to evaluate the trend toward automation and hence the reduction in labor requirements per unit of capital employed and of output; to formulate intelligently policies regarding depreciation and depletion; to anticipate the possible impact of thermonuclear attack on the national wealth; and, last not least, to evaluate the role of capital in the economic growth of the postwar period and in the expected growth over the next decade or two.

This is not the place to discuss how such an inventory is best organized, and set up in a way which will permit the data to be kept up to date once the basic benchmark figures are secured. All I should like to do is to bespeak your interest and assistance in this enterprise. This is a fairly large undertaking, as statistical or economic projects go. It is also a complex enterprise that would involve many agencies of the Federal Government as well as some organizations outside of it. For these reasons careful preparation and planning is essential. The suggestion that has emerged from preliminary discussions is to organize a small group—provided financing can be found—that would within about 1 year develop, with the help of several committees of experts for the main sectors of the economy, a reasonably detailed operational outline for an inventory of national wealth, which could then be submitted for action to the appropriate agencies of the Federal Government and the Congress.

V

Let me sum up, then, a presentation that already has been all too summary.

The decline in the share of investment in national product between the postwar period and earlier phases of our economic history is considerably smaller than is often assumed. Indeed when allowance is made for capital formation by the Government and in the form of consumer durables, two categories often omitted without good reason; when the calculations are made in current prices which appear to be more relevant for this comparison; and when attention is directed toward the addition to productive capacity embodied in capital formation rather than to its accounting magnitude, it may well be doubted that an economically significant decline has actually occurred between, say, the first 30 years of this century and the postwar period. If there has been a decline, it is quite likely not of larger proportion than that observed between the last quarter of the 19th and the first quarter of the 20th century and may reflect a long-term trend in the American economy rather than a sudden and abnormal change starting with the great depression.

Investment, in the sense of expenditures on durable reproducible assets, is an important factor in determining the rate of economic growth as measured by real national product per head. In the long run, investment in excess of replacement of capital used up is even an indispensable factor in economic growth. Investment alone, however—and this may be more important to stress than the self-evident truth of the preceding sentences—is not the only determinant of economic growth. It may not even be the most important single cause of growth; and may be matched or outranked in its contribution to growth by technological progress and scientific advance and education as its proximate causes, by improvements in the quality and health of the labor force; and sometimes even by psychological factors difficult to measure. These are subjects on which, I presume, some of the other members of the panel will have something to say.

Furthermore, and this must be stressed because it is more important for policy formation and less evident than the complementary rather than predominant role of investment in economic growth, the measurable relationships between investment and growth, embodied in the capital-output ratio or similar measures, far from providing a stable and reliable basis of economic forecasting and planning, change in the short as well as in the long run; differ widely among and within sectors of the economy; and show substantial variations among countries. What is more, we are as yet far from understanding the reasons for many of the observed changes and differences.

Finally, what we actually know with reasonable confidence and in reasonable detail about volume and structure of capital formation, of the Nation's stock of capital, and on their interrelations with the main and measurable factors of economic growth is quite insufficient as a basis for intelligent policy formation. A major effort toward improving our statistical knowledge and our analytical understanding of this entire field is one of the most urgent tasks for cooperative research among the Federal Government, the economic profession and business.

Mr. Goldsmith. Regretfully but unavoidably I must begin with apologies, traceable in part to the chairman's kindness in allowing members of the panel to select in their statements any aspect of the broad subject of investment and growth which they regard as important and on which, I suppose, they are least incompetent to deal. I have taken advantage of this license to select three topics which, though I regard them as important and as relevant to your committee's inquiry, are not likely to be popular. I also regret that due to the short time available and the pressure of other obligations, I have not been able to avail myself of the privilege of preparing a paper for the record that would amplify and document the obiter dicta, as the lawyers say, to which I shall often have to limit myself in this statement. I shall, of course, be glad to remedy these deficiencies as far as possible in answers to your questions.

In reviewing the long-term trend of capital formation in the United States it may be best to concentrate on one problem that seems to have attracted considerable attention recently: the alleged sharp fall in the ratio of capital formation to national product, i.e., the decline in the share of current output devoted to increasing national wealth.

The measurement of capital formation, particularly if a figure net of capital consumption is wanted, is one of the most difficult subjects in economics, both conceptually and statistically. This is not the place, nor is there the time, to enter into discussion of the numerous technical problems involved; or to try to reconcile the differences among the various estimates which are substantial. You will see immediately, however, that these nasty problems cannot be swept under the rug entirely.

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If you look at the left bottom panel of the chart you may indeed share the alarm many reviewers of Professor Kuznets' book have shown. The proportion of our national product used to increase our net stock of capital seems to have declined from approximately 14 percent in the 1890's to 10½ percent in the 1920's and to a mere 6½ percent in the decade following World War II. This result is reached by excluding consumer durables from the stock of durable assets, and by adjusting both capital expenditures and national product to the price level of 1929. If you now direct your attention to the left top panel, a variant of the share of capital formation in national product which I regard as more appropriate for some purposes because it includes consumer durables and is based on actual (undeflated) values, you will receive quite a different impression. The ratio of net capital formation to national product shows only a slight and fairly regular downward trend from about 13½ percent in the 1890's to 10½ percent in the postwar period. The decline in the capital formation ratio between the 1920's and the 1950's thus is not unprecedented either in direction or size, and this is true irrespective of the variant of the ratio you may choose to select. There is, therefore, no need to invoke explanatory factors specific to the postwar period. If you look at the right-hand side, which is based on gross capital expenditures, there is no decline at all, or even a slight increase. I discuss that briefly in my text.

It is not however, the movements of capital formation, in absolute figures or as a percent of national product, in which we are primarily interested, but the relation of capital formation to economic growth. Let us again begin with the actual data for the United States.

Table II permits you to compare the ratio of net capital formation with the rate of growth of real national product per head for decadal periods between 1869 and 1955. The main impression you will probably receive from this comparison is the absence in the historical record of a clear-cut, steady relationship between the intensity of capital formation (the ratio of capital formation to national product) and the rapidity of economic growth (the rate of increase in output per head). The rate of growth of output (and income) per head was about the same in the 1890's and the 1950's—approximately 2 percent per year—although the share of capital formation was lower in the more recent period, spectacularly so if you accept the variant excluding consumer durables and using deflated figures.

The fact that the rate of growth of output per head was approximately the same in the 15 postwar years as during the first three decades of this or the last three decades of the 19th century, although the capital formation ratio was lower is more than an historical curiosity. It points to a basic change which appears to have taken place in the American economy, and which is reflected in what economists call the aggregate production function, i.e., the form of the relation between the volume of inputs of capital, land and labor and the volume of output of goods and services, a subject to which your distinguished member the senior Senator from Illinois has made such outstanding contributions when he was still one of ours.

While the inputs of capital and labor alone could account for most of the increase in output up to the 1920's this is no longer true. The statistics indicate that a given percentage increase in the input of both capital and labor and land now produces a more than proportionate increase in output. The economy as a whole works under increasing returns, and this extra return can be attributed to technological progress to use one vague word for a congeries of many and diverse factors that are extremely difficult to disentagle. If the national production function is of a form that involves an increase in output higher than the increase in the input of either capital and labor, then the capital formation ratio may decline without bringing about a decline in the rate of growth of output per head. Indeed if technological progress is rapid enough a declining capital formation ratio is compatible with a rising rate of growth.

I certainly do not want to argue that no systematic relationship has existed in the United States during the past century between capital formation and economic growth even in the long run. The fact remains, however, that the historical record does not disclose an obvious, regular unchanging association between the intensity of capital formation and the rate of economic growth. Economic growth is dependent on—

> * * * the interaction of * * * the advance of knowledge, the improved skills of the working population, and the rise in capital per worker * * *

as the Economic Report correctly stresses. On this empirical basis the burden of proof would seem to be on those who claim that an increase in the ratio of capital formation, beyond its apparent trend line, over one or more full business cycles will in and of itself—and these are the key words—lead promptly to an acceleration in economic growth, i.e., an increase in the rate of growth of real national product per head. If there is such an association the increase in the capital formation ratio required for a substantial increase in the rate of growth—say by one-half of 1 percent a year—is probably considerably larger than is often imagined, and is large enough to require far-reaching changes in our financial and business organization.

Since the United States is not an island (in Donne's sense), nor the American economy a phenomenon sui generis, I now ought to review the evidence on the relation between capital formation and economic growth that other economically advanced countries provide. There is neither the time to do this, rewarding as it might be; nor are there data comparable in length and detail to those at hand in the United States. The best I can do, therefore, is to quote to you a few sentences from the conclusions of what is so far the most intensive statistical exploration of this problem. Here is what Professor Kuznets says ("Economic Development and Cultural Change," IX, 4 II (July 1961), pp. 55–56):

> * * * while capital formation proportions did rise with the secular rise in per capita income in some countries * * * the rise ended fairly early, while per capita income continued to grow at substantial rates; and in others * * * a significant rise in the national capital formation proportions did not begin until after several decades of vigorous growth of * * * per capita products * * *.
>
> * * * the different levels of national capital formation proportions were not

associated with differences in per capita income * * *. Nor was there any close similarity among countries either in the average level of their capital formation—output ratios * * *; or in the movement of these * * * ratios.

And now for the crucial statement:

At some danger of exaggerating, one might say that the rather simple relations assumed in much economic analysis—close association between levels of income and savings proportions and between capital formation proportions and the rate of growth—are not confirmed by the long-term records.

Our findings * * * suggest that the savings-income capital growth relations have been far too variable * * * to retain much usefulness as guides in either analysis or policy.

All I can add is that the investigations which I have made myself on the relation of capital formation and economic growth in industrial countries are in agreement with Professor Kuznets' conclusions that I have just read to you. As in the case of the United States there is some tenuous association between the intensity of capital formation and the rate of economic growth, particularly when very large non-cyclical changes are involved. The association is much too irregular in fact and too uncertain in its causal mechanism to permit this simple prescription: If more economic growth is wanted, all that is needed is to increase the ratio of expenditures on durable goods to total national product.

That we cannot now say with a reasonable degree of confidence much that is relevant about the relations of investment and economic growth—or, for that matter saving and economic growth—that is not so vague as to lose all value as a guide to policy, does not mean that we never will. It means, however, that a determined effort will be needed, first, to collect and marshal data that are relevant to the problem; and, then, to analyze them in such a way that the results can have practical application. In view of the limitations of time and competence I shall have to restrict my suggestions to one fairly specific project in this broad field, the only but perhaps one of critical importance. This is the need for an inventory of the national wealth of the United States.

We are thus unable to answer questions such as: How is the national wealth of the United States divided among the States? Among industries? Among the main sectors of the economy? What proportion of equipment in the United States, or in Texas, or in the textile industry is older than 10, 20, or 50 years? What is the share of automatic and semiautomatic equipment in different industries and different regions? What proportion of plant and equipment—for the United States as a whole, for any industry—was not utilized during last year? Does the value of fixed capital per man or per unit of output in a given industry differ as between establishments in different States, or establishments of different size? How rapidly are certain types of equipment actually retired, sold or scrapped, or relegated to standby use in different industries? How much of plant and equipment now in use was acquired new or second hand? Does the ratio between new and hand-me-down equipment differ among industries; between large and small firms, among different parts of the country? What is the value of the main subsoil assets in the different States? How does the value of governmental structures and equipment in the various States compare to their tax receipts, their expenditures, and the income of their citizens? Is the relation between the value of fixed capital and output in a given industry dependent on the size of the establishment, on the age of the equipment, on the location of the plant, on other factors?

In other words, in an economy characterized by the importance of industrial plant and equipment we hardly know anything, in reasonable detail and with reasonable precision, about how much of the different types of equipment we have, in what shape it is, and how it is utilized.

Without this information it is hardly possible to assess the contribution of the stock of capital to output; to estimate future capital requirements for replacement or expansion; to evaluate the trend toward automation and hence the reduction in labor requirements per unit of capital employed and of output; to formulate intelligently policies regarding depreciation and depletion; to anticipate the possible impact of thermonuclear attack on the national wealth; and, last but not least, to evaluate the role of capital in the economic growth of the postwar period and in the expected growth over the next decade or two.

This is not the place to discuss how such an inventory is best organized and set up in a way which will permit the data to be kept up to date once the basic benchmark figures are secured. All I should like to do is to bespeak your interest and assistance in this enterprise. This is a fairly large undertaking, as statistical or economic projects go. It is also a complex enterprise that would involve many agencies of the Federal Government as well as some organizations outside of it. For these reasons careful preparation and planning is essential. The suggestion that has emerged from preliminary discussions is to organize a small group—provided financing can be found—that would within about 1 year develop, with the help of several committees of experts for the main sectors of the economy, a reasonably detailed operational outline for an inventory of national wealth, which could then be submitted for action to the appropriate agencies of the Federal Government and the Congress.

Let me sum up, then, a presentation that already has been all too summary.

The decline in the share of investment in national product between the postwar period and earlier phases of our economic history is considerably smaller than is often assumed. If there has been a decline, it is quite likely not of larger proportion than that observed between the last quarter of the 19th and the first quarter of the 20th century and may reflect a long-term trend in the American economy rather than a sudden and abnormal change starting with the great depression.

Investment, in the sense of expenditures on durable reproducible assets, is an important factor in determining the rate of economic growth. In the long run, investment in excess of replacement of capital used up is even an indispensable factor in economic growth. Investment alone, however—and this may be more important to stress than the self-evident truth of the preceding sentences—is not the only determinant of economic growth. It may not even be the most important single cause of growth; and may be matched or outranked in its contribution to growth by technological progress and scientific advance and education as its proximate causes, by improvements in the quality and health of the labor force; and sometimes even by psychological factors.

Furthermore, and this must be stressed because it is more important for policy formation and less evident than the complementary rather than predominant role of investment in economic growth, the measurable relationships between investment and growth, embodied in the capital-output ratio or similar measures, far from providing a stable and reliable basis of economic forecasting and planning, change in the short as well as in the long run; differ widely among and within sectors of the economy; and show substantial variations among countries.

Finally, what we actually know with reasonable confidence and in reasonable detail about volume and structure of capital formation, of the Nation's stock of capital, and on their interrelations with the main and measurable factors of economic growth is quite insufficient as a basis for intelligent policy formation. A major effort toward improving our statistical knowledge and our analytical understanding of this entire field is one of the most urgent tasks for cooperative research among the Federal Government, the economic profession and business.

Thank you.

Chairman PATMAN. Thank you, sir.

Professor Hamberg, we would like to hear from you, sir.

STATEMENT OF DR. DANIEL HAMBERG, UNIVERSITY OF BUFFALO

Dr. HAMBERG. Thank you, Mr. Chairman. I should like to take the cue from Professor Goldsmith and read excerpts from my paper, in the interest of timesaving; my full paper can be inserted in the record.

Also, perhaps following an acute failing of the academician, my paper is primarily analytical. I should like to request the committee's indulgence to read along with me to help us over certain little symbols.

(Dr. Hamberg's prepared statement follows:)

INVESTMENT AND ECONOMIC GROWTH [1]

(By D. Hamberg, University of Buffalo)

Episodically, the question whether our economy is faced with secular inflation or secular stagnation seems to recur. Years of rapid growth, excess demand, and inflation have, starting in 1957, given way to an extended period of alarmingly slow economic growth, deficient demand, and growing unemployment. As has happened before, the specter of secular inflation has been replaced by the specter of secular stagnation. Recent events have started many wondering whether our economy is saving too much—at least relative to the investment outlets available in the private sector of the economy. I shall address myself specifically to the sources of the recent slowdown in the growth of the U.S. economy at a later point in this paper. At this juncture, I should like to present an adaptation of a set of tools, familiar to economists, which is designed to provide the basis for approximate answers to the above question. Too often, efforts to determine whether our economy is saving too much, or too little, are marked by vagueness, simple extrapolations of past ratios, polemics, or a combination of all three. Generally, the difficulties seem to be associated with an inability to say something concrete about potential (private) investment outlets. It is this gap which the model presented below is meant to fill—in a rough way.

[1] Paper presented to the Joint Economic Committee, Congress of the United States, in connection with its hearings on "Investment and Growth," Feb. 5, 1962.

Saving versus investment outlets in a growing economy

We begin by defining a natural, or ceiling, growth rate. The natural rate of growth is that growth rate which, in the presence of full employment, is permitted by the growth in the labor force and the rate of technological progress (measured in terms of advances in output per worker). It is thus the maximum, potential growth rate the economy can achieve, given the rates of growth in labor force and productivity. It is this growth rate that provides the basis for estimating capital requirements or investment outlets in the private sector of the economy (with certain qualifications set forth below).

Specifically, the natural growth rate is a ceiling growth rate whose capital requirements are, at a given rate of interest, set by the combined growth in labor force and production techniques. For example, assume that a 1.5 percent annual growth in the labor force and a 2 percent annual growth in output per worker determine a potential growth in national income of (approximately) 3.5 percent a year. If the (marginal) capital-output ratio is 3, then the demand for capital will approximate 10.5 percent of national income. Algebraically, this proposition may be written as:

$$\frac{\Delta Y}{Y_n}\times\frac{\Delta K}{\Delta Y}=\frac{\Delta K}{Y_n}=\frac{I}{Y_n} \qquad (1)$$

where $\Delta Y/Y_n$ represents the natural (percentage) rate of growth of national income and output, as determined by the growth rates in labor force and productivity; $\Delta K/\Delta Y$ represents the marginal capital-output ratio, where ΔK stands for the increase in capital stock, or net investment, I; thus this ratio defines the increment in capital stock or net investment needed to produce an increment in output, at a given rate of interest.

With one possible exception, equation (1) gives the long-run demand for capital, at a given interest rate, in complete or exhaustive fashion. Ultimately, there are only three sources of demand for capital: (1) to equip a growing labor force at a given capital-labor ratio; (2) to provide for the implementation of new techniques; and (3) to provide additional capital per head of working population and hence per unit of output in response to a fall in (long-term) interest rates.[3] Thus it will be seen that a variation in labor force growth, or technological progress as it affects the growth in labor productivity, as well as the value of the capital coefficient, or changes in the rate of interest as these effect this coefficient will alter the capital requirements associated with the natural growth rate. From the small and very slow changes in the capital-output ratio (at full employment) over long periods of time, it appears that the assumption of constancy in this ratio for periods of 5 years or so will serve as a fairly good approximation to reality.

One possible source of investment demand not covered by the above analysis derives from shifts in the composition of the national product in favor of industries with capital-output ratios larger than those of the industries from which demand has shifted. However, on the one hand, this factor can work both ways; that is, shifts in the composition of output can move in favor of industries with capital coefficients smaller than those of the lagging industries. On the other hand, in principle this factor can be handled in the above model by viewing the capital-output ratio as a kind of weighted average for the private sector as a whole.

In opposition, as it were, to the natural growth rate, we have one which, with a given capital-output ratio, will fulfill the standard equilibrium condition of

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[3] If it be asked what has happened to the demand for additional capital originating in the need to produce, simply, a larger output, along the lines usually expressed by the acceleration principle, the answer is that the first source of demand listed above is concealed in the acceleration principle. To say that the demand for capital is a function of the level of output assumes that the labor force is growing fast enough to produce the output at given interest rates and techniques of production. Therefore, the acceleration principle (or incremental output) is not an additional source of demand for capital over and above the three sources listed above; it is simply a variant of (1) above.

equating planned saving and investment. Given the saving ratio, S/Y, and the capital coefficient, $\Delta K/\Delta Y$, we can write:

$$\frac{\Delta Y}{Y}\times\frac{\Delta K}{\Delta Y}=\frac{S}{Y} \tag{2}$$

or

$$\frac{\Delta K}{Y}=\frac{S}{Y} \tag{3}$$

or since by definition $\Delta K=I$,

$$\frac{I}{Y}=\frac{S}{Y} \tag{4}$$

Thus it is that the rate of income growth, $\Delta Y/Y$, in (2) is with the given saving and capital-output ratios an equilibrium growth rate in the sense of equating planned saving and investment. This growth rate may also be called the full-capacity growth rate, because in equalizing planned saving and investment its realization assures that aggregate demand will grow apace with the growth in productive capacity (incremental capital stock) originating in the net investment associated with it.

We now have before us a tool for rendering (rough) judgments about whether an economy is saving and investing too little or too much, whether, in other words, it is faced with secular exhilaration or secular stagnation. From equation (4) we find that associated with equilibrium or full capacity growth is a certain rate of capital accumulation or net investment. From equation (1) we find that associated with the natural, or ceiling, or full employment (because in the nature of it, the natural growth rate assures full employment of the growing labor force and those tending to be released from production through advances in productivity) growth rate is a certain rate of demand for capital. If the ratio I/Y exceeds the ratio I/Y_n, the economy is indeed saving and investing too much, relative, that is, to the capital requirements of longrun growth.

Persistence of this condition over long periods implies that the economy's secular capital requirements are inadequate to its secular saving propensities. Unless either the saving coefficient is lowered and/or the growth in labor force or productivity are speeded up, the economy will display the characteristics of secular stagnation.

In like manner if I/Y is less than I/Y_n, the economy is saving and investing too little—relative to the secular capital requirements of a growing labor force and advancing technology. The demand for capital originating in these growth factors will outrun the rate of capital accumulation associated with full-capacity growth; a condition of excess demand is implied, as is a condition of secular exhilaration. As society chooses, this condition may be dealt with either by raising the saving coefficient and/or reducing the rates of labor force growth and technological advance.[3]

Adjustments of the natural to the warranted growth rate

With some justification, it may be (and has been) argued that the foregoing distinction between the natural and equilibrium growth rates is somewhat overdrawn. For example, when the equilibrium growth rate starts to press against the growth ceiling and threatens to rise above if persistently (so that I/Y exceeds

[3] This same analysis may be conducted in terms of comparisons of the equilibrium or full capacity growth rate with the natural or full employment growth rate. For disparities between the investment ratio I/Y and I/Y_n imply corresponding disparities between these two growth rates. For example, an excess of I/Y over I/Y_n implies, from equations (1) and (2), an excess of the full capacity growth rate over the full employment growth rate (since the capital coefficient is the same in both equations). Hence, in these circumstances, investment will tend to be excessive in the sense that productive capacity will grow faster than output, and eventually excess capacity will appear in sufficient amount as to either retard growth or bring about an actual downturn in production and employment.

I/Y_n), the implied labor shortages and rising wage rates may tend to raise the growth ceiling a bit. This might come about through a rise in the labor-force participation rate, as women, say, enter the labor force in increasing numbers; or the lure of relatively high wages might attract a stream of workers from low productivity sectors (like agriculture) to high productivity ones (in industry); both of these factors have been characteristic of U.S. economic development for many years, the latter particularly since the erection of the prohibitive immigration barriers in 1920 (immigration, incidentally, was also a source of alleviation of labor shortages in the 19th century in this country). In similar fashion, persistent labor shortages might also act as a spur to the introduction of laborsaving inventions and thus raise the productivity growth rate.[4] Similar, but opposite, adjustments in the ceiling growth rate might be made in response to conditions prevailing when the ceiling growth rate is persistently above the equilibrium one (and I/Y_n exceeds I/Y).

To a limited degree, there is a certain amount of truth in this argument, and we would accept it (with the reservation noted in footnote 4) as a minor qualification of the analysis of equations (1) to (4)—but no more. It is perfectly obvious from the experience of the underdeveloped countries, in the form of secular inflation and mounting unemployment, that the natural or full employment growth rate will adjust downward to the equilibrium one only to a small extent, if at all; it is possible, in other words, to save and invest too little relative to the capital requirements of economic growth, at least for long periods of time. In the same way, it is possible to save and invest too much in highly developed economies, relative that is to the capital requirements of long-run growth of these economies. Although there were other forces at work, I do believe that just this phenomenon underlay the great depressions of the 1870's, the 1890's, and the 1930's, and I think most students of the business cycle would concur.

Another objection to the model set forth in equations (1) to (4) that might be raised is that it suffers from the crucial failing of separating the advances in productivity of the natural growth rate from the saving and investment activities of the equilibruim growth rate. Since investment is the vehicle for introducing technological change, the natural growth rate should follow the equilibrium growth rate up and down with changes in S/Y and I/Y. In one form or another this kind of argument has been heard increasingly of late, and there have been many proposals for raising S/Y and I/Y in order to raise the (natural?) rate of U.S. economic growth. Because this is such an important question, and because I believe this policy prescription to be filled with pitfalls, I want to devote a number of pages to an examination of this matter.

Investment and technological progress

I want now to present a simple model that makes technological change avowedly a function of investment. The point of this model is to demonstrate that, despite this assumption, the rate of technological progress and the natural growth rate are nevertheless independent of the proportion of the national income devoted to investment, I/Y. Other more complicated models could be adduced to show the same thing, so that on this important point, at least, the virtue of great simplicity is not a mixed blessing.

First, let us write a saving equation:

$$S_1 = sY_1 \qquad (5)$$

where s is the long-run average and marginal propensity to save, $S/Y = \triangle S/\triangle Y$, and in accordance with usual assumptions (and factual information) is posited as positive and less than one in numerical value. As earlier, Y stands for national income, and the numerical subscripts refer to time periods.

Next, let us write an investment equation:

$$I_1 = B(Y_1 - Y_2) \qquad (6)$$

where the coefficient B is the long-run average and marginal capital-output ratio,

[4] In a country such as the United States, where labor has persistently tended to be the scarce resource, this last result is problematical. When labor costs loom large among production costs, as they do in the industrialized countries (in the United States wage and salary costs have approximated some 30 percent of value of manufacturing product, while interest costs have approximately 2 percent), the pressure to economize on labor is fairly continuous, and the stream of laborsaving inventions and innovations is likely to be little affected by limited changes in relative factor prices.

$K/Y = \Delta K/\Delta Y$, and again in accordance with usual assumptions (and factual information) is posited as greater than one in numerical value. This equation, a form of the so-called acceleration principle, says that investment is a function of an increase in output, since with full capacity operations an increase in output requires an increase in capital stock, with the capital-output ratio defining the increment in capital stock needed to produce the increased production. Since we are dealing with growth problems, the assumption of full-capacity operations is proper and fitting.

Equations (5) and (6) bear a family resemblance to equation (2) and may be solved for the equilibrium growth rate that will equate planned saving and investment. In fact, if equation (2) is divided through by the capital coefficient, $\Delta K/\Delta Y$, the equilibrium growth rate thus obtained would be the one yielded by equations (5) and (6). And as we have seen from equations (2)–(4), this growth rate equates planned saving and investment.

Now let us introduce the equation that explicitly makes technological progress and hence the natural growth rate dependent on capital accumulation or investment:

$$\frac{Y_1 - Y_2}{Y_1} = a + b\left(\frac{\Delta K_1}{K_1}\right) \tag{7}$$

For convenience (only), we may assume the labor force constant; hence the (natural) growth rate on the left-hand side of (7) refers to growth in productivity as well as growth in total output. The second term in (7) (where $0 < b < 1$) indicates that output and productivity growth are a positive, but nonproportional, function of the percentage rate of growth in the capital stock. Nonproportionality arises from the first term a (>0), which is introduced into (7) in recognition of the fact that some technological change can take place without capital accumulation (or investment), as in the case of improvements in productivity stemming from purely organizational and managerial improvements. Improvements in plant layout and inventory control practices are just two instances of the latter.

Before proceeding, let us rewrite equation (6) in its equivalent form:

$$\frac{I_1}{Y_1} = \frac{K}{Y} \times \frac{Y_1 - Y_2}{Y_1} \tag{6.1}$$

or

$$\frac{Y_1 - Y_2}{Y_1} = \frac{I_1}{Y_1}\frac{K}{Y} \tag{6.2}$$

It can now be shown that in longterm equilibrium the percentage rate of growth of output and productivity will equal the percentage rate of growth in capital stock (i.e., in equation (7) $\Delta Y/Y = \Delta K/K$), and that the growth rates of both capital and output (and productivity) will equal $a/1-b$. In other words, in longrun equilibrium the rate of growth of output and productivity (as well as the capital stock) will be independent of the investment ratio, I/Y.

Let us begin by postulating (for example) in equation (7) that $\Delta Y/Y > \Delta K/K$. Then Y/K is rising and K/Y is falling over time. From (6.1) it would appear that I/Y should therefore commence falling. But (6.2) shows that $\Delta Y/Y$ is not independent of K/Y; in fact, a decline K/Y results in a more than proportionate increase in $\Delta Y/Y$ (equation (2) also shows this), so that in (6.1 I/Y will rise, because the rise in $\Delta Y/Y$ will more than offset the fall in K/Y. Hence in (7) $\Delta K/K$ will rise.[5]

But apparently from equation (7) the rise in $\Delta K/K$ will induce a rise in $\Delta Y/Y$. However, from the form of (7), the rise in $\Delta Y/Y$ will be less than proportional to the rise in $\Delta K/K$. Hence we can conclude that as long as $\Delta Y/Y$ exceeds $\Delta K/K$, the latter will rise (faster than $\Delta Y/Y$) until it catches up to and equals $\Delta Y/Y$. At this point, equation (6.1) informs us, I/Y will cease rising,

[5] In case it is not obvious that $\Delta K/K$ is an increasing function of I/Y:

$$\frac{\Delta K}{K} = \frac{K/Y}{\Delta K/Y}$$

or since, by definition, $\Delta K = I$,

$$\frac{\Delta K}{K} = \frac{I/Y}{K/Y}$$

This expression also shows, directly, that $\Delta K/K$ varies inversely with K/Y.

so that longterm equilibrium growth will have been reached at which $\Delta K/K = \Delta Y/Y$. Mutatis mutandis, the same line of reasoning tells us that in the event $\Delta Y/Y$ is less than $\Delta K/K$, both will decline until they are equal.

This being the case, the longrun equilibrium growth rate of capital, output and productivity can be determined by substituting in equation (7) $\Delta Y/Y$ for $\Delta K/K$ to arrive at the growth rate $a/1-b$. Thus the equilibrium and, in this model, the natural growth rate turns out to rest only on the values of the parameters of equation (7) and thus to be independent of the investment-income ratio, I/Y.

Explanation of independence of the natural growth rate from I/Y

Let me try to make some sense of this important result, particularly that part of it that, in effect, makes the rate of technical progress associated with the natural growth rate independent of I/Y. To say that investment or capital formation is a vehicle for putting technical change into effect is to imply, at heart, that the advances in technology associated with investment are a function of the age distribution or average age of the capital stock. That is to say, for any given rate of invention, the lower the average age of the capital stock, the more up to date the average level of technology will be, because more of the capital stock will embody the most recent inventions, even though none of the individual technologies may have been changed. It would seem that the higher the investment-income ratio, I/Y, and therefore the higher the percentage rate of capital accumulation, the lower will be the age distribution of the capital stock. But under natural growth conditions this last would be a false conclusion.

The fact of the matter is that under conditions of natural exponential (i.e., compound interest or constant percentage) growth, the age distribution or average age of capital stock is constant. All vintages of the capital stock will grow at the same proportionate rate (e.g., the rate given above from equation (7)); therefore, the proportion of the capital stock from the oldest to the newest vintages is constant over time. Under conditions of natural exponential growth the only factors that determine the age distribution of the capital stock are the rate of growth itself and the rate of depreciation (in both cases the relationship is, not surprisingly, an inverse one).

If the economy has been growing over a long period at a percentage rate that is less than the natural rate (as given by the rate of technological progress, and the rate of labor force growth as well in reality), then the mean age of the capital stock will be above the mean that would prevail under natural growth conditions. Hence, by raising the actual growth rate, say through acceleration of the rate of capital accumulation, the average level of technology can be raised, because in these circumstances the mean age of the capital stock can be progressively reduced until it reaches the level set by the natural or full employment rate of growth. This result can be seen in the previous analysis of the establishment of the natural rate of growth in equation (7). When the rate of growth of output and productivity ($\Delta Y/Y$) was below the natural rate, we found that on the way up to this rate, the proportional rate of capital accumulation ($\Delta K/K$) got successively larger, implying a declining age distribution of the capital stock and hence a progressive shifting of weights in favor of capital embodying the most recent inventions.

Once the natural rate of growth and minimum mean age of the capital stock have been reached, then the way to speed up technological change is, again, not surprisingly, to raise the flow of inventions (e.g., by more research). With a given age distribution, an accelerated rate of invention means that each vintage of capital stock will be better than it would have been at a slower rate of invention, so that the average level of technology will be better.

Another alternative is to lower the economic life of capital goods by raising the rate of depreciation, thereby lowering the average age of the capital stock and raising the average level of technology. But unless we are willing to lower the economic lifetime of capital goods progressively toward zero (on the face of it, economic nonsense), this alternative is of the one-shot variety.

Growth levels or paths versus rates of growth

Thus far we have been talking about rates of growth. In particular, we have found that the natural rate of growth is independent of the proportion of national income devoted to saving and investment. To show that the economic world portrayed by our models is not completely topsy-turvy, however, we may also note some characteristics of these models with respect to levels of capital stock, output, and technology at different saving-investment ratios.

(1) At all times, before and after the natural growth rate is reached, the level of capital stock will be higher, the higher is the investment-income ratio, I/Y. For a given output, investment or incremental capital stock will be higher, the higher is the ratio I/Y; therefore, for all outputs, the stock of capital will vary directly with this ratio.

(2) Since output varies directly with capital stock, the level of output will also vary directly with the ratio I/Y.

These strictures mean, in effect, that although the natural growth rate is independent of I/Y, the natural growth path will be higher, the higher is I/Y. This growth path may be likened to the base (or principal) of the compound interest formula, and the natural growth rate to the rate of interest of this formula. With a given interest rate (or percentage rate of growth), the larger will be the numerical value of any compounded future sum, the larger is the base or principal. This same point may be made by reference to a ratio chart containing two parallel and positively sloped straight lines, one higher than the other. These two lines are, in effect, growth paths; being parallel, they display the same percentage rates of growth, but the numerical values of the dependent variable (measured on the vertical axis of the ratio chart) at any point on the higher line will obviously be larger than the value of the same variable at the corresponding point (straight down) on the lower line. So it is that whether we measure capital or output on the vertical axis of such a chart, with two economies having the same natural growth rate, the one with the higher ratio I/Y will grow along a (parallel) line above the other. The more heavily investing economy will thus have more capital stock and be richer in terms of income and output than the other.

(3) Fortunately or unfortunately, no such blanket assertions can be made about the average level of technology. To begin with, we have seen that the average level of technology can be raised, if at all, only if an economy has been growing at a rate for long periods of time below its natural rate of growth. Only in these circumstances can the average level of technology be raised—because a higher rate of growth of captial stock will mean a declining average age of this stock.

Now whether a higher investment-output ratio will effect this higher rate of growth depends on the view we take of the workings of the economic system and its growth tendencies. This dilemma is illustrated by the two previous models: equations (1)–(4) and equations (5)–(7). The latter model indicates that in longrun equilibrium what we have called the natural and the equilibrium growth rates automatically merge to become one (the natural) growth rate. And this growth rate, we have seen, is independent of the ratio I/Y. That is to say, once a fixed investment-output ratio is established, and altogether irrespective of its value, the growth rate of the economy will tend toward the natural rate. So if the rate of economic growth has been below the natural rate, the average level of technology will rise toward the level associated with the natural growth rate as a matter of course—to repeat, no matter where the ratio I/Y is set.

If, on the other hand, the model of the economy represented by equations (1)–(4) is taken to be a closer image of the growth mechanism, then we imply that there may be no such automatic merging or equalizing tendencies between the equilibrium and natural growth rates. And if the economy has been growing at a rate equal to the equilibrium one, and this is below the natural growth rate, then from equations (2)–(4) it is apparent that a rise in the ratio I/Y will raise the growth rate of output and capital stock; in the process, the average level of technology will be raised as the age distribution of the capital stock is reduced by the higher (proportional) rate of capital accumulation.

Sources of recent stagnation in the U.S. economy

I should like to conclude this paper with a few observations on the sources of recent stagnation in the U.S. economy. Can we adduce an excess of the equilibrium over the natural growth; i.e., an excess of private saving and investment over longrun capital requirements, in explanation of the low rate of economic growth since 1957? This is a possibility, but I believe that it is not yet necessary to look for this kind of explanation.

Instead, I think the explanation lies in fiscal and monetary policies that have been crippling our upswings and causing them to die aborning. In the case of fiscal policy, especially, I think it is fair to say that we may have purchased stability at the expense of economic growth. We have become quite proud of the capacity of our economy to limit downswings to rather minor recessions, and we point to our powerful automatic stabilizers as perhaps the chief reason for this new-found stability. These economic gyroscopes consist of the more than proportionate decline in taxes when the national income and product decline, thereby holding up after-tax incomes and thus spending in the face of falling production and employment; bolstering the automatic stabilizing effects of taxes have also been the automatic increases in outlays for unemployment compensation. On the other side of the budget, we have found Government purchases of goods and services displaying remarkable stability during recessions in the face of sharply falling tax receipts, thereby helping strongly to maintain total spending, private and public, as production contracts.

What we have failed to realize, however, is that our automatic stabilizers, functioning as good gyroscopes should, stabilize in both directions—upward and downward. With our progressive tax structure, taxes also rise more than proportionately during periods of economic expansion, thereby causing after-tax incomes and thus private spending to rise less than proportionately in the face of expanding production; these deflationary effects are reinforced by the decline in outlays for unemployment compensation as unemployment drops. At the same time, for various reasons, mostly shortsighted, Government spending (Federal particularly) has also been held stable in the face of sharply rising tax revenues, thus reinforcing the retardation in the growth of total spending as the national output rises.

The significance of this fiscal behavior is that large chunks of incremental income are removed from the stream of private expenditures in the form of taxes without being offset by increments in Government spending. Hence, since 1957, total spending has tended to lag badly behind rising production, leading to unintended inventory accumulation, excess capacity, and therefore too slow a rise in business capital expenditures, particularly, but also consumer spending as well.

If I may, I should like to rephrase the above a bit more precisely in the parlance of economics. What we now have is a very high marginal propensity to tax, i.e., ratio of tax change to income change, $\triangle T/\triangle Y$. A high marginal propensity to tax, like a high marginal propensity to save, means a small national-income multiplier; thus the multiplier effects of exogenous increases in private and Government spending on the national income and product are smaller than they would be with a smaller marginal tax ratio, $\triangle T/\triangle Y$. At the same time, we have been experiencing relatively small rises in multiplicands, in the form of certain components of private investment (like residential construction) and, especially, Government spending. The result has been slow growth in the "product," viz, the national product.[6]

The upward stabilizing effects of the high marginal propensity to tax went unnoticed before 1957 for two main reasons. One is that for war and postwar reasons the multiplicand(s) in the multiplier formula were expanding rapidly before this. In the aftermath of World War II were the huge demands for capital originating in the backlogs that built up during the great depression and then during World War II. Before these backlogs were exhausted, the outbreak of the Korean war produced a large increase in Government spending and another large increase in investment spending in defense-connected industries. Abetted by the continued boom in residential through 1957, the enormous automobile year in 1955, the subsequent capital-goods boom of 1955–56, and the Suez export boom of 1956–57, plus the temporary spurt in Federal spending in the second quarter of 1957, these war and postwar stimuli were enough, evidently, to conceal the effects of the declining multiplier until the middle of 1957. (Incidentally, were it not for the strictly fortuitous export boom in late 1956 and early 1957, plus the apparently fortuitous spurt in Federal spending in the second quarter of 1957, I think it is clear from the appearance of increasing excess capacity in a number of industries that the contraction that began in the late summer of 1957 would have started almost a year earlier.)

I use the word "declining" next to the multiplier above advisedly. For my second, though subsidiary reason, why the effects of the high marginal tax went unnoticed before 1957 is that the marginal propensity to tax has undoubtedly

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[6] The same point could be expressed in terms of the model contained in equations (1)–(4). On the right-hand side of equation (2), the expression t-g could be added, where $t=\triangle T/\triangle Y$ and $g=\triangle G/\triangle Y$, G standing for Government purchases of goods and services. What we have said in the text above implies that t-g rises sharply during upswings in the national income, thereby raising the equilibrium growth rate sharply, too, pushing the latter above the natural growth rate, i.e., raising I/Y dramatically above I/Y_n.

been rising steadily through the post-World War II years. The reason, of course, lies in the heavily progressive tax structure at the Federal level of Government. As households and to a lesser extent, business firms, move up the income ladder with an expanding economy, and thus into successively higher tax brackets, the incremental total tax bite accompanying successive increments in the national income gets progressively larger. Since little was done to offset this on the expenditures side of the Federal ledger, the damping or retardiing effects on U.S. economic growth of this fiscal behavior were bound to grow progressively strong.

If the foregoing analysis is correct, it is clear that, unless the people of the United States are prepared to undertake large increases in Government spending, to offset the retarding or stabilizing effects of the large marginal tax bite, the time has come to consider seriously some sharp reductions in income taxes. However, I would emphasize the proviso. Frankly, I belong to the group that believes we have been starving the public sector and that there is room for vast increases in Federal spending before these needs are filled, and I speak of defense as well as civilian needs.

For the above reasons, I personally am glad to see the large increases in Federal spending that the Kennedy administration has been undertaking and advocating. For I look forward not only to a badly needed stimulus to our economy, offsetting (I hope enough) the retarding effects of the high marginal tax bite, but also filling some of our needs in the public sector.[7]

Dr. Hamberg. Episodically, the question whether our economy is faced with secular inflation or secular stagnation seems to recur. Years of rapid growth, excess demand, and inflation have, starting in 1957, given way to an extended period of alarmingly slow economic growth, deficient demand, and growing unemployment. As has happened before, the specter of secular inflation has been replaced by the specter of secular stagnation. Recent events have started many wondering whether our economy is saving too much—at least relative to the investment outlets available in the private sector of the economy. I shall address myself specifically to the sources of the recent slowdown in the growth of the U.S. economy at a later point in this paper. At this juncture, I should like to present an adaptation of a set of tools, familiar to economists, which is designed to provide the basis for approximate answers to the above question. I should also like to use the same tool as a kind of takeoff to analyze another problem that I think bears heavily on the remarks of Professor Goldsmith, namely, the relation between investments intensity, investment-output ratio, if you like, and economic growth generally and technical change particularly.

Let me begin by defining a natural, or ceiling, growth rate.

The natural rate of growth is that growth rate which, in the presence of full employment, is permitted by the growth in the labor force and the rate of technological progress (measured in terms of advances in output per worker). It is thus the maximum, potential growth rate the economy can achieve, given the rates of growth in labor force and productivity. It is this growth rate that provides the basis for estimating capital requirements or investment outlets in the private sector of the economy (with certain qualifications set forth below), and so enables us in a crude and rough way to at least ask the right questions with regard to whether the economy is saving or investing too little or too much.

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[7] To a lesser extent, part of the blame for the recent stagnation must be placed at the feet of the Federal Reserve System for its insistence on fighting inflation by means of tight money policies long after it became clear that inflation was a thing of the past. Because tight money policies work with particular effect on investment spending, it is clear that these policies have abetted fiscal policy in retarding our economic growth. But this point has been so worked over in the literature that it hardly needs further elaboration from me.

Specifically, the natural growth rate is a ceiling growth rate whose capital requirements are, at a given rate of interest, set by the combined growth in labor force and production techniques. For example, assume that a 1.5-percent annual growth in the labor force and a 2-percent annual growth in output per worker determine a potential growth in national income of (approximately) 3.5 percent a year. If the (marginal) capital-output ratio is 3, then the demand for capital will approximate 10.5 percent of national income.

Senator DOUGLAS. When you speak of this marginal capital-output ratio, do you mean you have to have a simple increase of 3 percent in capital?

Dr. HAMBERG. An increase of $3 worth of capital stock to produce $1 worth of additional output.

Senator DOUGLAS. Reducing both to dollar terms?

Dr. HAMBERG. Yes.

Algebraically, the proposition is presented in equation (1), where we multiply the percentage rate of growth, the percentage natural growth rate, by the capital-output ratio, and you see that it works out that we obtain the ratio of investment to national income that will be associated with this maximum natural growth rate. And "natural," incidentally, may be interpreted as being independent of saving and investment ratios.

The delta K, incidentally, for later reference, equals net investment; the increment in capital stock is by definition investment I.

I will resume.

In opposition, as it were, to the natural growth rate, we have one which, with a given capital-output ratio, will fulfill the standard equilibrium condition of equating planned saving and investment. Given the saving ratio of S/Y, and the capital coefficient of delta K over delta Y, then equations 2, 3, and 4 tell us that a given growth rate, delta Y/Y, will lead to equality of investment and savings. So this growth rate that equates planned saving and investment, an important concept for later reference, is called the equilibrium growth rate, one that equates planned saving and planned investment, where, in effect, the delta Y/Y is the unknown, so to speak, and we are getting that growth rate which will yield an I/Y equal to S/Y in (4).

We now have before us a tool for rendering (rough) judgments about whether an economy is saving and investing too little or too much, whether, in other words, it is faced with secular exhilaration of secular stagnation. From equation (4) we find that associated with equilibrium growth is a certain rate of capital accumulation or net investment. From equation (1) we find that associated with the natural, or ceiling, or full employment—because in the nature of it, the natural growth rate assures full employment of the growing labor force and those tending to be released from production through advances in productivity—growth rate is a certain rate of demand for capital. If I/Y exceeds the ration of I/Y_n, that is, if the rate of investment associated with equilibrium growth exceeds the ratio of investment to national income that the economy needs to implement its growth ceiling, then the economy is indeed saving and investing too much, relative, that is, to the capital requirements of long-run growth. Persistence of this condition over long periods implies that the economy's secular capital requirements are inadequate to its secular saving propensities. Unless either the saving coefficient is lowered and/or the growth in labor force or productivity are speeded up, the economy will display the characteristics of secular stagnation.

In like manner, if I/Y is less than I/Y_N, the economy is saving and investing too little—relative to the secular capital requirements of a growing labor force and advancing technology. The demand for capital originating in these growth factors will outrun the rate of capital accumulation associated with equilibrium growth; a condition of excess demand is implied, as is a condition of secular exhilaration. As society chooses, this condition may be dealt with either by raising the saving coefficient and/or reducing the rates of labor force growth and technological advance.

Let me consider an objection raised to the model set forth in equations 1 through 4, namely that it suffers from the crucial failing of separating advances in productivity of the natural growth rate from the saving and investment activities of the equilibrium growth rate. Since investment is the vehicle for introducing technological change, the natural growth rate should follow the equilibrium growth rate up and down with changes in S/Y and I/Y. In one form or another this kind of argument has been heard increasingly of late, and there have been many proposals for raising S/Y and I/Y in order to raise the (natural?) rate of U.S. economic growth. Because this is such an important question, and because I believe this policy prescription to be filled with pitfalls, I want to devote a number of pages to an examination of this matter.

Let me consider the relation specifically between investment and technological change.

I want now to present a simple model that makes technological change avowedly a function of investment. The point of this model is to demonstrate that, despite this assumption, the rate of technological progress and the natural growth rate are nevertheless independent of the proportion of the national income devoted to investment, I/Y. Other more complicated models could be adduced to show the same thing, so that on this important point, at least, the virtue of great simplicity is not a mixed blessing.

First, I present a saving equation that says saving is some fraction of national income. Then I present an investment equation in which investments is stated to be some proportion of a change in national income. This second equation (6), this investment equation, is a form of the so-called acceleration principle that says in effect that in order to have an increase in output, there has to be an increment in capital stock or investment, and the coefficient B, which is the capital-output ratio I referred to earlier, defines how much additional capital stock is needed to produce the increment in output given in the brackets, and so defines the amount of investment associated with the growth in the brackets. Equations (5) and (6) bear a family resemblance to equation (2) and may be solved for the equilibrium growth rate that will equate planned saving and investment. In fact, if equation (2) is divided through by the capital coefficient, delta K/delta Y, the equilibrium growth rate thus obtained would be the one yielded by equations (5) and (6). And as we have seen from equations (2)-(4), this growth rate equates planned saving and investment.

Now let us introduce the equation that explicitly makes technological progress and hence the natural growth rate dependent on capital accumulation or investment: Here we have equation (7) that says, in effect, the percentage rate of growth is equal to some constant, plus a proportion of the percentage rate of growth in capital stock, the rate of capital accumulation.

This relation is a nonproportional one due to the insertion of that constant *a*. The constant is simply designed to show that there is some technical change which really does not need capital formation, for example organizational improvements and managerial improvements. such as improved methods of inventory control and plant layout. These clearly are forms of technical change which do not need capital formation to bring them about. This means, then, and this is rather important for the behavior of my system, that the percent rate of growth on the left-hand side of (7) is positively related to capital formation but nonproportionately so. That is, an increase in the capital stock of X percent will result in an increase in output of less than X percent. Incidentally, for convenience only, we can assume the labor force constant and, hence, Y, output, can also stand for output per man and thus productivity. Therefore, with this assumption, I can use the left-hand side of equation (7) to refer both to the percentage rate of growth of output and output per man that is related to capital accumulation.

Let me skip now to the middle or a quarter down on page 10.

Let us begin by postulating, for example, in equation (7), that the percent rate of growth of output exceeds the percent rate of growth of capital stock; this means, then, that the capital-output ratio is falling. Output is growing faster than capital. Consequently, the ratio of capital to output is falling over time.

If you look down to footnote 4 for convenience, it turns out that the percentage rate of capital accumulation, delta K/K, is inversely related to the capital-output ratio. So if the capital-output ratio falls, this means that delta K/K in equation (7) rises. But apparently from equation (7), delta Y/Y will also rise, the percentage rate of growth of output and productivity, but less than proportionately. So we can conclude that as long as the percentage rate of growth in output exceeds the percentage rate of growth in capital stock, delta K/K, the latter will rise—faster than the percentage rate of growth of output—until it catches up to and equals the percentage rate of growth of ouput. We could show a similar result if we posited at the outset that delta K/K in equation 7 exceeded the percentage rate of growth of output on the left-hand side. So what we have arrived at is a notion that in equilibrium, the percentage rate of growth in output and capital stock will be equal. This being the case, the long run equilibrium growth rate of capital, output and productivity can be determined by substituting in equation 7 on the right-hand side delta Y/Y for delta K/K, and if we rearrange terms, we find out that delta Y/Y and delta K/K turn out to grow at the growth rate given by the parameters of that equation, namely $a/1\text{-}b$. The point of this is, then, that in equilibrium, the equilibrium growth rate and in this model, the natural growth rate turns out to rest only on the values of the parameters of equation (7) and thus to be independent of the investment-income ratio.

Let me try to make some sense out of this important result, particularly that part of it that, in effect, makes the rate of technical progress associated with the natural growth rate independent of I/Y. This may be the most important thing I have to say in this paper.

To say that investment or capital formation is a vehicle for putting technical change into effect is to imply, at heart, that the advances in technology associated with investment are a function of the age distribution or average age of the capital stock. That is to say, for any given rate of invention, the lower the average age of the capital stock, the more up to date the average level of technology will be, because more of the capital stock will embody the most recent inventions, even though none of the individual technologies may have been changed. It would seem that the higher the investment-income ratio, I/Y, and therefore the higher the percentage rate of capital accumulation, the lower will be the age distribution of the capital stock. But under natural growth conditions this last would be a false conclusion.

The fact of the matter is that under conditions of natural exponential (i.e., compound interest or constant percentage) growth, the age distribution or average age of capital stock is constant. All vintages of the capital stock will grow at the same proportionate rate (e. g., the rate given above from equation (7)); therefore, the proportion of the capital stock from the oldest to the newest vintages is constant over time. Under conditions of natural exponential growth the only factors that determine the age distribution of the capital stock are the rate of growth itself and the rate of depreciation (in both cases the relationship is, not surprisingly, an inverse one).

If the economy has been growing over a long period at a percentage rate that is less than the natural rate (as given by the rate of technological progress, and the rate of labor force growth as well in reality), then the mean age of the capital stock will be above the mean that would prevail under natural growth conditions. Hence, by raising the actual growth rate, say through acceleration of the rate of capital accumulation, the average level of technology can be raised, because in these circumstances the mean age of the capital stock can be progressively reduced until it reaches the level set by the natural or full employment rate of growth. This result can be seen in the previous analysis of the establishment of the natural rate of growth in equation (7). When the rate of growth of output and productivity (delta Y/Y) was below the natural rate, we found that on the way up to this rate, the proportional rate of capital accumulation (delta K/K) got successively larger, impying a declining age distribution of the capital stock and hence a progressive shifting of weights in favor of capital embodying the most recent inventions.

Once the natural rate of growth and minimum mean age of the capital stock have been reached, then the way to speed up technological change is, again not surprisingly, to raise the flow of inventions (e.g., by more research). With a given age distribution, an accelerated rate of invention means that each vintage of capital stock will be better than it would have been at a slower rate of invention, so that the average level of technology will be better.

Another alternative is to lower the economic life of capital goods by raising the rate of depreciation, thereby lowering the average age of the capital stock and raising the average level of technology. But unless we are willing to lower the economic lifetime of capital goods progressively toward zero (on the face of it, economic nonsense), this alternative is of the one shot variety. (If we raised the depreciation rate to one, we would raise the ratio of investment to income upward toward one in the whole economy.)

Thus far we have been talking about rates of growth. In particular, we have found that the natural rate of growth is independent of the proportion of national income devoted to saving and investment. To show that the economic world portrayed by our models is not completely topsy-turvy, however, we may also note some characteristics of these models with respect to levels of capital stock, output, and technology at different saving-investment ratios.

(1) At all times, before and after the natural growth rate is reached, the level of capital stock will be higher, the higher is the investment-income ratio, I/Y. For a given output, investment or incremental capital stock will be higher, the higher is the ratio I/Y; therefore, for all outputs, the stock of capital will vary directly with this ratio.

(2) Since output varies directly with capital stock, the level of output will also vary directly with the ratio I/Y.

These strictures mean, in effect, that although the natural growth rate is independent of I/Y, the natural growth path will be higher, the higher is I/Y. This growth path may be likened to the base (or principal) of the compound interest formula, and the natural growth rate to the rate of interest of this formula.

If you have a higher base, clearly, with any compound rate of interest rate of growth, you will wind up with more capital stock and more output at any given time in the future than if you started with a lower base in just the same manner that you arrived at a larger future sum when your principal is larger than when it is smaller for any given compound rate of interest.

Fortunately or unfortunately, no such blanket assertions can be made about the average level of technology. To begin with, we have seen that the average level of technology can be raised, if at all, only if an economy has been growing at a rate for long periods of time below its natural rate of growth. Only in these circumstances can the average level of technology be raised—because a higher rate of growth of capital stock will mean a declining average age of this stock.

Now whether a higher investment-output ratio will effect this higher rate of growth depends on the view we take of the workings of the economic system and its growth tendencies. This dilemma is illustrated by the two previous models: equations (1)–(4) and equations (5)–(7). The latter model indicates that in long-run equilibrium what we have called the natural and the equilibrium growth rates automatically merge to become one (the natural) growth rate. And this growth rate, we have seen, is independent of the ratio I/Y. That is to say, once a fixed investment-output ratio is established, and altogether irrespective of its value, the growth rate of the economy will tend toward the natural rate. So if the rate of economic growth has been below the natural rate, the average level of technology will rise toward the level associated with the natural growth rate as a matter of course—to repeat, no matter where the ratio I/Y is set.

If on the other hand, the model of the economy represented by equations (1)–(4) is taken to be a closer image of the growth mechanism, then we imply that there may be no such automatic merging or equalizing tendencies between the equilibrium and natural growth rates. And if the economy has been growing at a rate equal to the equilibrium one, and this is below the natural growth rate, then from equations (2)–(4) it is apparent that a rise in the ratio I/Y will raise the growth rate of output and capital stock; in the process, the average level of technology will be raised as the age distribution of the capital stock is reduced by the higher (proportional) rate of capital accumulation.

Thank you.

Chairman PATMAN. Thank you, sir.

Doctor Keyserling, we would like to hear from you.

STATEMENT OF LEON H. KEYSERLING, CONSULTING ECONOMIST, AND PRESIDENT, CONFERENCE ON ECONOMIC PROGRESS, WASHINGTON, D.C.

Mr. KEYSERLING. I would like to insert my full prepared statement into the record, if I may, with my charts, Mr. Chairman.

Chairman PATMAN. Without objection, that will be done.

(The statement referred to follows:)

TESTIMONY OF LEON H. KEYSERLING,[1] JOINT ECONOMIC COMMITTEE HEARINGS ON PRESIDENT'S ECONOMIC REPORT, RE INVESTMENT AND GROWTH

Mr. Chairman and members of the committee, I appreciate this opportunity to discuss the problem of investment and growth, with particular reference to the treatment of this subject in the January 1962 Economic Report of the President and Annual Report of the Council of Economic Advisers.

As there is no substantial conflict between these two documents, I shall for purposes of simplification refer to them jointly as "the reports." And in order not to distract you with details, whenever I refer to materials in either of these two documents, I shall not specify in which of the two the materials appear nor on what page, except in special instances where it may be helpful or necessary to do so.

I appreciate and applaud the great emphasis which the reports place upon an adequate rate of economic growth, and upon the important role of investment in sustaining this rate of growth. I welcome also the reports' recognition that this investment must be both private and public and must include investment not only in plant and equipment and science and technology but also in our human resources.

But this recital of these elements in growth does not get us very far, although it is a good first step. I am concerned that the reports, as I read them, do not contain a sufficiently comprehensive analysis as to why our growth rate averaged so dismally low during the past 9 years, nor as to how the operations of the economy and the relationships within it need to be readjusted in order to improve this record in future. Correspondingly, in my judgment, the reports do not contain a sufficiently comprehensive growth program, either quantitative or qualitative; and some of the policy recommendations seem to move in the wrong direction because of the gaps in the analysis. This is especially true with respect to the business investment analysis, and with respect to the proposal to provide an 8-percent tax credit against tax for investment in depreciable machinery and equipment.

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[1] Former Chairman, Council of Economic Advisers. Consulting economist and attorney; president, Conference on Economic Progress.

I focus attention upon this 8-percent tax credit because it is really the most significant and proximate of the reports' recommendations dealing with the growth problem. Later on in my testimony, I shall further disclose why this is so. The reports' recommendations for standby powers in the tax and public works fields, to deal with future recessions, are further removed from the context of the immediate economic situation. Moreover, I believe that long-range programs to restore and maintain the maximum health of our economy as it goes along should be accorded more weight than countercyclical weapons. This seems desirable for a variety of reasons, including the reason that such long-range and positive policies offer a stronger approach to avoiding recessions than attempting to counteract them when they threaten. The main question we should ask now is not what to do when the next recession threatens, but rather how we can now commence to unite our short-range and long-range efforts to restore and maintain a maximum level of economic performance under the Employment Act. Indeed, I fear that the stress upon standby powers, in the framework of the reports, intimates that we are further out of the woods now than I think to be the case.

The reports' proposals for strengthening unemployment compensation, and for training or retraining workers, are desirable. But they are hardly debatable, and do not raise very large issues of national economic policy.

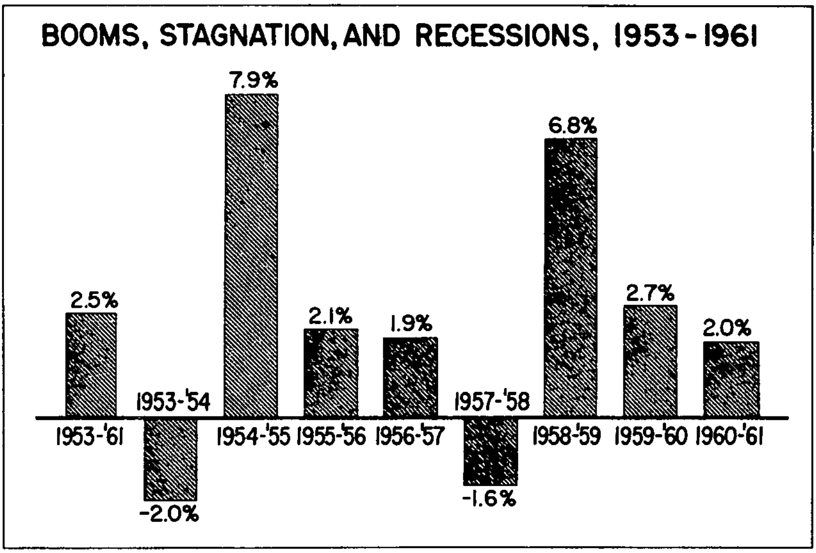
Let me now turn to why we have had such a dismally low rate of economic growth during the past 9 years. For an examination of this question is the inescapable first step toward delineating sensible corrective policies for the future. I shall undertake this analysis of the past 9 years by means of propositions briefly stated, in order to keep within the time limitation. I have some charts, which I shall offer for the record, to amplify and fortify this summary analysis.

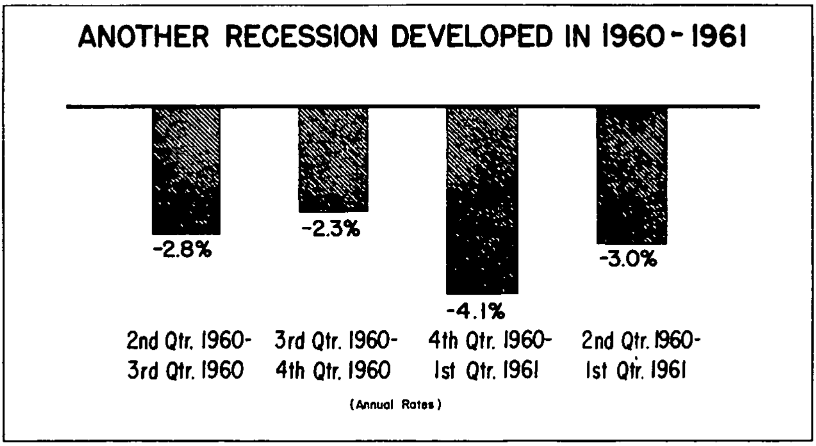
First, the average annual growth rate of only about 2½ percent during the past 9 years was not due primarily to a deficient rate of growth in the labor force or in productivity, the two main factors in our potentials for economic growth. To illustrate, if the labor force had grown only in the neighborhood of 1 percent a year, and productivity only 1½ percent a year, the 2½ percent average annual rate of economic growth would have utilized the growth in the labor force and in productivity, and would not have resulted in the extremely serious chronic rise in idle manpower and plant which I have been forecasting before this committee and elsewhere for so many years. Manifestly, the chronic rise in idle manpower and plant has meant that the labor force and productivity have grown more rapidly than their actual utilization.

I offer at this point charts 1 through 5, which portray the low and irregular growth rate, the chronic rise in idle manpower and plant, and the national economic losses suffered in consequence, during the period 1953–61.

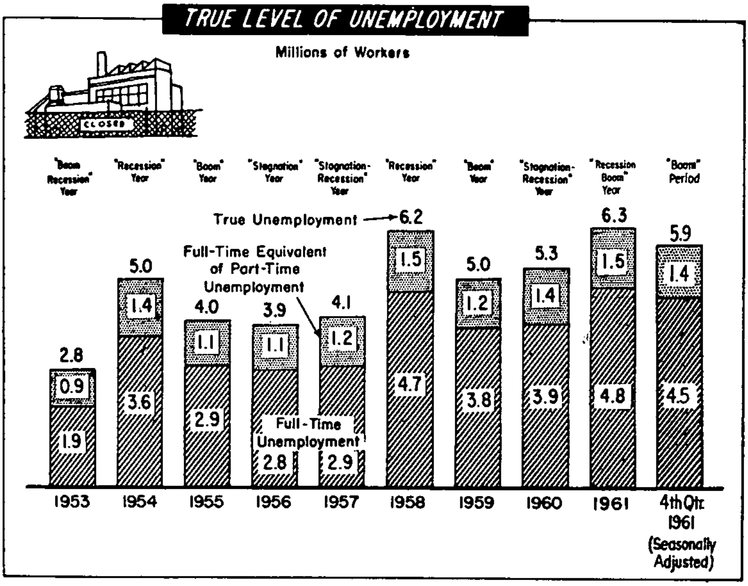
GROWTH RATES, U.S. ECONOMY, 1953-1961

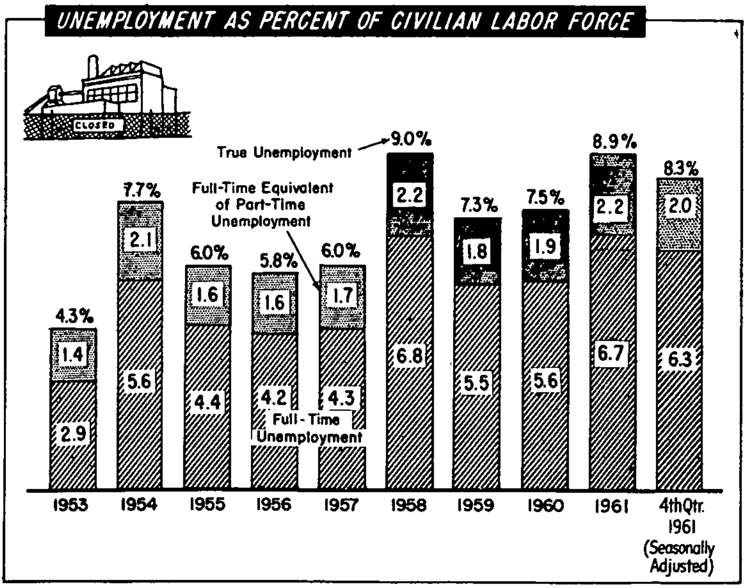
Average Annual Rates of Change in Gross National Product
In Uniform 1960 Dollars

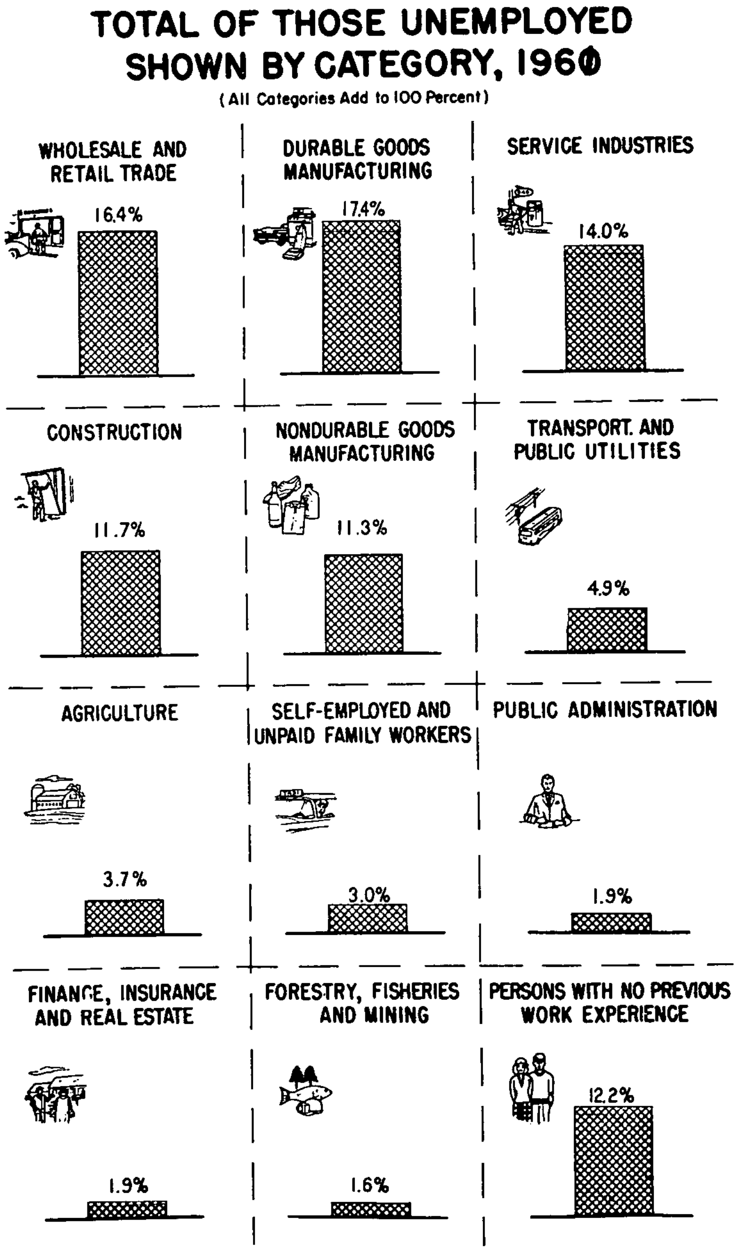




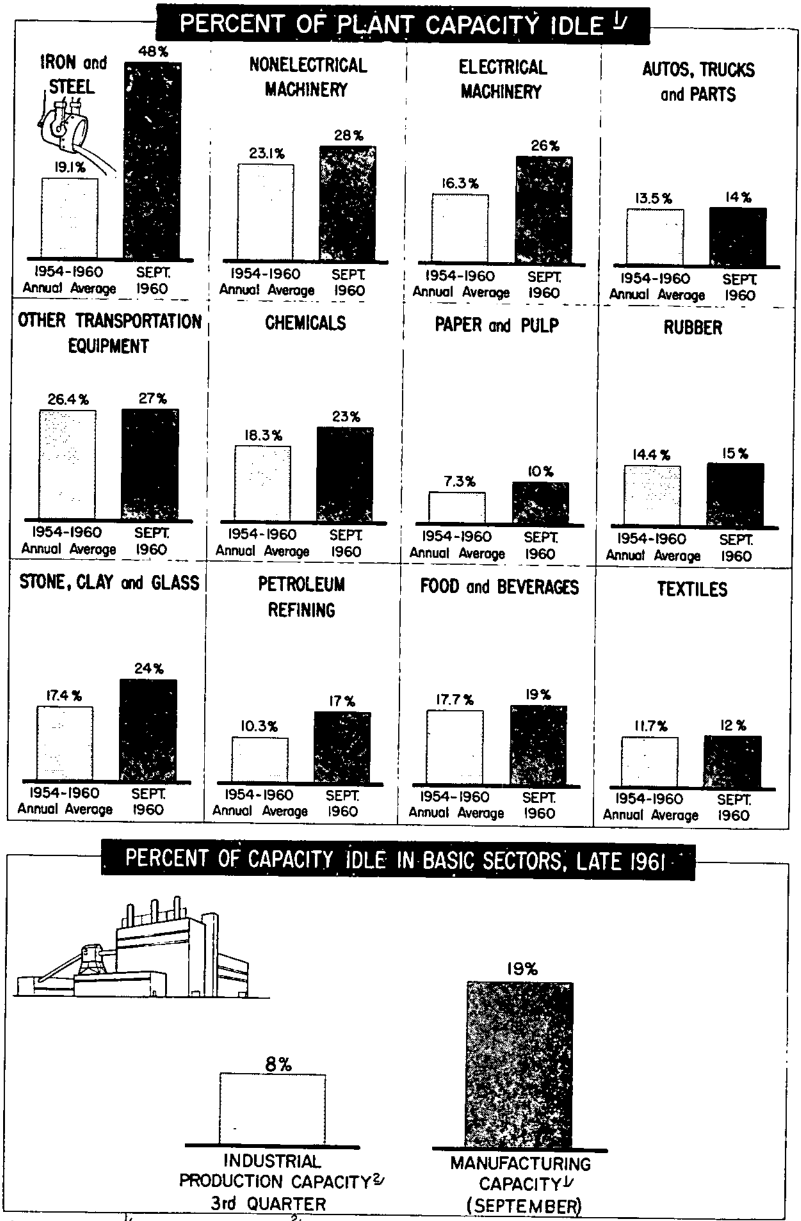
THE CHRONIC RISE OF IDLE MANPOWER






TOTAL OF THOSE UNEMPLOYED
SHOWN BY CATEGORY, 1960
(All Categories Add to 100 Percent)
WHOLESALE AND RETAIL TRADE
16.4%
DURABLE GOODS MANUFACTURING
17.4%
SERVICE INDUSTRIES
14.0%
CONSTRUCTION
11.7%
NONDURABLE GOODS MANUFACTURING
11.3%
TRANSPORT. AND PUBLIC UTILITIES
4.9%
AGRICULTURE
3.7%
SELF-EMPLOYED AND UNPAID FAMILY WORKERS
3.0%
PUBLIC ADMINISTRATION
1.9%
FINANCE, INSURANCE AND REAL ESTATE
1.9%
FORESTRY, FISHERIES AND MINING
1.6%
PERSONS WITH NO PREVIOUS WORK EXPERIENCE
12.2%

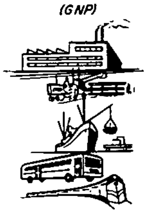
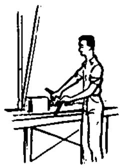
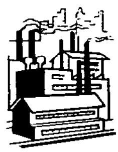
THE GROWING VOLUME OF IDLE PLANT AND MACHINES—1954-1961



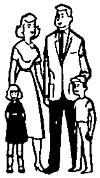
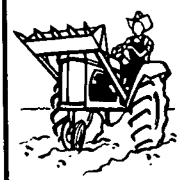
Source of Basic Data: 1/ McGraw Hill Annual Surveys; 2/ University of Pennsylvania, Econometric Research Unit.

LARGE NATIONAL ECONOMIC DEFICITS DURING 9-YEAR PERIOD 1953-1961

Dollar Items in 1960 Dollars

TOTAL NATIONAL PRODUCTION *(GNP)*	*MAN YEARS OF EMPLOYMENT*	*PRIVATE BUSINESS INVESTMENT* *(Incl. Net Foreign)*	*PRIVATE AND PUBLIC CONSUMPTION* 1/
			
$344 Billion Too Low	22.4 Million Too Low	$90 Billion Too Low	$254 Billion Too Low

...THESE HAVE LED TO LARGE LOSSES TO ALL ECONOMIC GROUPS

AVERAGE FAMILY INCOME *(Multiple Person Families)*	*FARM OPERATORS' NET INCOME*	*WAGES AND SALARIES*	*UNINCORPORATED BUSINESS AND PROFESSIONAL INCOME*
			
$5,750 Too Low	$55 Billion Too Low	$228 Billion Too Low	$18 Billion Too Low

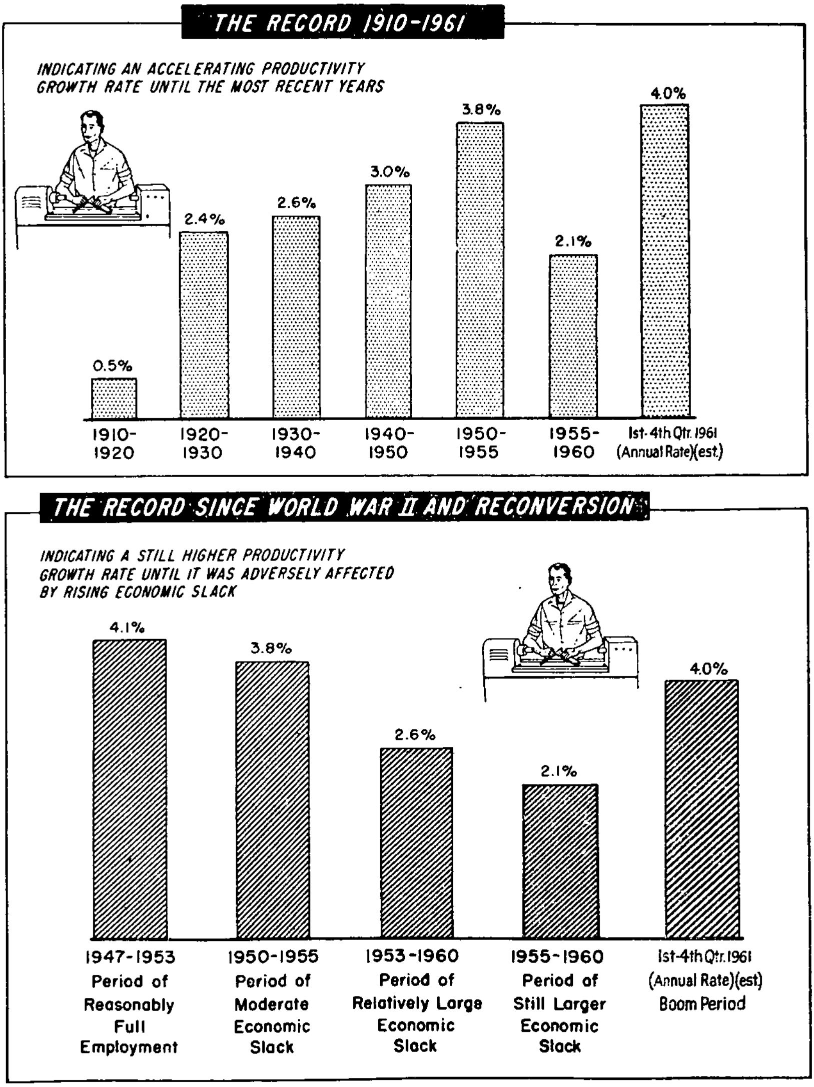
1/ Includes personal consumption expenditures plus government (Federal, state, and local) expenditures (220 and 34, respectively)

Second, it is also true that both the labor force and productivity would have grown considerably faster, if we had maintained reasonably full utilization of our productive power in being from year to year. Indeed, this is admitted at many points in the reports. The almost absolute failure of the civilian labor force to grow from December 1960 to December 1961 is a dramatic illustration of the depressing effect on the labor force of large economic slack, even allowing for the substantial growth in the Armed Forces. And with respect to productivity growth, while the rate of productivity growth averaged much too low during the past 9 years, the more nearly correct way to state this problem is that the large amount of economic slack and the low rate of economic growth impacted adversely upon productivity growth, rather than to say that the low rate of productivity growth was an autonomous or initiating factor in the unsatisfactory economic performance. In other words, the unsatisfactory rate of productivity growth must be explained primarily, not in technological terms, but rather in terms of the economic disequilibriums during the 9 years under review.

Chart 6 indicates, I think rather conclusively, the tendency of productivity growth to accelerate in the long-term under the impact of the new technology, and to be extremely sensitive to the extent of utilization of our productive resources in being. To state this in another way, the chart indicates that, even with no more plant and equipment and technology than we actually had in being during the past 9 years, the productivity growth rate would have averaged much higher if the actual rate of utilization had clung close to maximum utilization. Very recent productivity figures reinforce this conclusion.

TRENDS IN OUTPUT PER MAN-HOUR -OR PRODUCTIVITY-1910-1961

Average Annual Rate of Productivity Growth
for the Entire Private Economy



Note: Based on U.S. Department of Labor estimates, relating to man-hours worked.

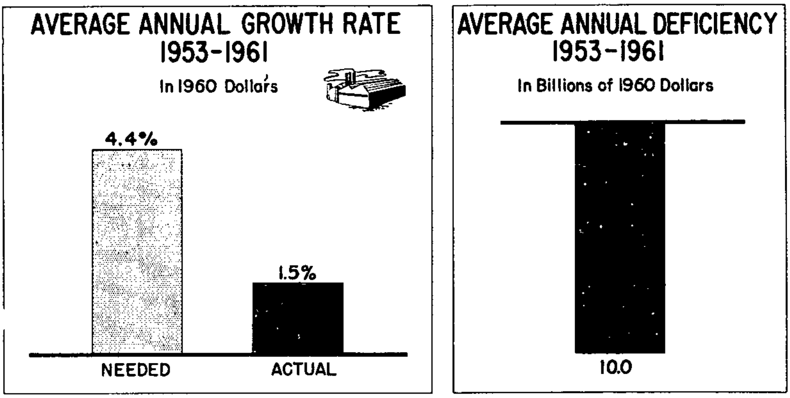
Third, while much of the unsatisfactory productivity record is to be explained on the ground of insufficient utlization, it is of course true that our productivity growth potential during the 9 years under review would have been enlarged, by higher absolute levels of investment in plant and equipment and technology. It is also true, for the 9-year period as a whole, that this absolute level of investment was too low. But why was it too low? This is indeed the central question.

Fourth, careful observation of the economy in action demonstrates clearly why the rate of business investment was too low in absolute terms, for the 9-year period as a whole. It was not because either the tax treatment of investors or other factors such as price-wage-cost relations militated against a sufficiently high level of profits and investment in producers' goods at any time when the ultimate demand for products in the form of private consumer expenditures and public outlays for goods and services at all levels of government were high enough to make reasonably full utilization of plant and equipment and technology in-being. Entirely to the contrary: whenever this ultimate demand was adequate or indeed not glaringly deficient, expansion of plant and equipment through the investment process raced so far ahead of the expansion of ultimate demand that the economy got badly out of balance. Recessions consequently followed.

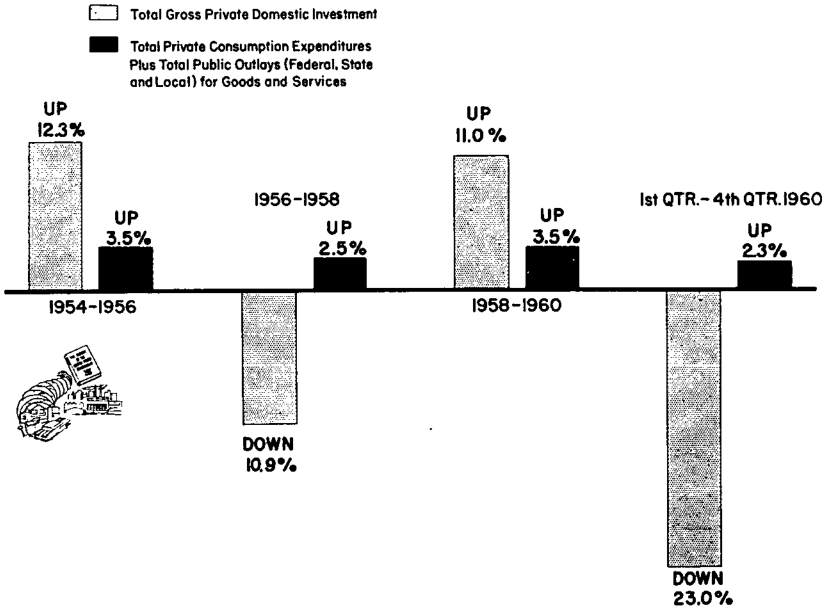
I now offer chart 7, which shows that, for the period 1953–61 as a whole, there was an annual average deficiency in private domestic investment of about $10 billion, measured in 1960 dollars. But the chart also knows how, during the boom periods 1954–56 and 1958–60, total private domestic investment grew several times as fast as private and public demand for ultimate products. The contrast was even more striking if one singles out private investment in plant and equipment. The chart also shows how these investment binges generated very severe downturns in business investment—thus contributing to the general economic recessions—when it became abundantly clear to the business managers that they were confronted by a condition of extremely overexpanded productive facilities relative to the actual and foreseeable levels of ultimate demand.

Chart 8 shows, how, during the period 1953–61 as a whole, both gross private domestic investment, and investment in producers' durable equipment, fluctuated much more extremely than did the gross national product. This, in conjunction with what I have already said, illustrates that, if we could overcome the tendency of the demand for ultimate products to lag so far behind the expansion of producer facilities during boom periods, this would help to iron out the course of business investment, iron out the course of the gross national product, and thereby result in a more adequate average rate of overall economic growth and much lower levels of idle plant and manpower.

GROSS PRIVATE DOMESTIC INVESTMENT WAS DEFICIENT DURING 1953-'61 AS A WHOLE



BUT AT TIMES INVESTMENT FAR OUTRAN CONSUMPTION; THIS LED TO RECESSIONS AND CORRECTIVE INVESTMENT SHRINKAGE



AVERAGE ANNUAL RATES OF CHANGE, 1960 DOLLARS

FLUCTUATIONS IN GNP AND IN TYPES OF INVESTMENT, 1953-1961

(Quarterly Data, Seasonally Adjusted Annual Rates)

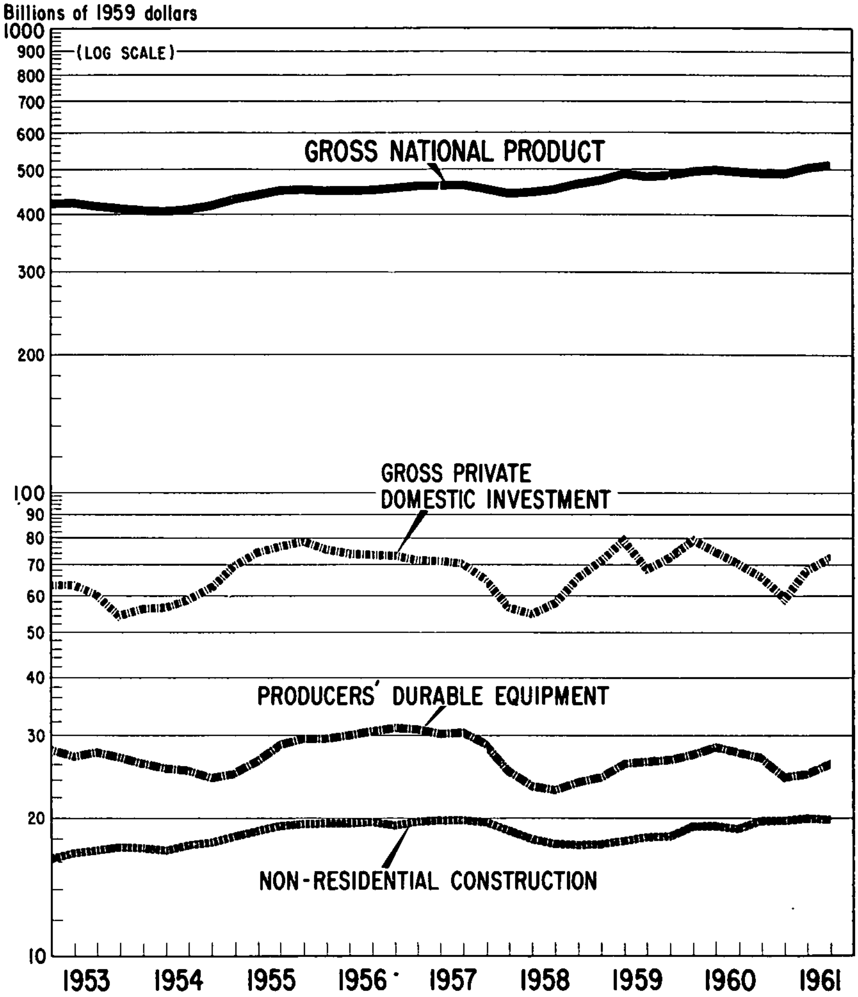
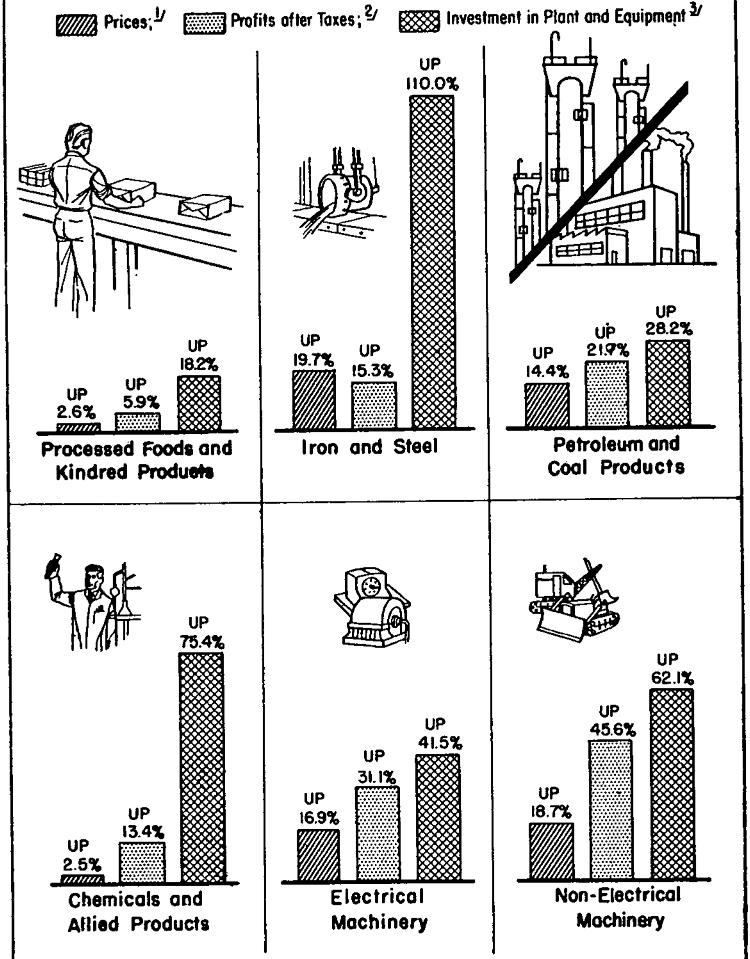


Chart 9 illustrates how, during the period preceding the 1957–58 recession—from which we have not fully recovered—price and profit increases yielded phenomenal expansions of plant and equipment. As I have said, these far outran the demand for ultimate products. This chart, of course, makes the point that business investors in the main need no special tax concessions or other types of more favorable treatment than they have been receiving, in order to enjoy all of the funds and incentives required for the highest rate of expansion of investment in plant and equipment consistent with the growth rate in the demand for ultimate products.

PRICES AND PROFITS ENCOURAGE VERY HIGH INVESTMENT UNTIL CONSUMPTION DEFICIENCY PUNCTURES THE BOOM

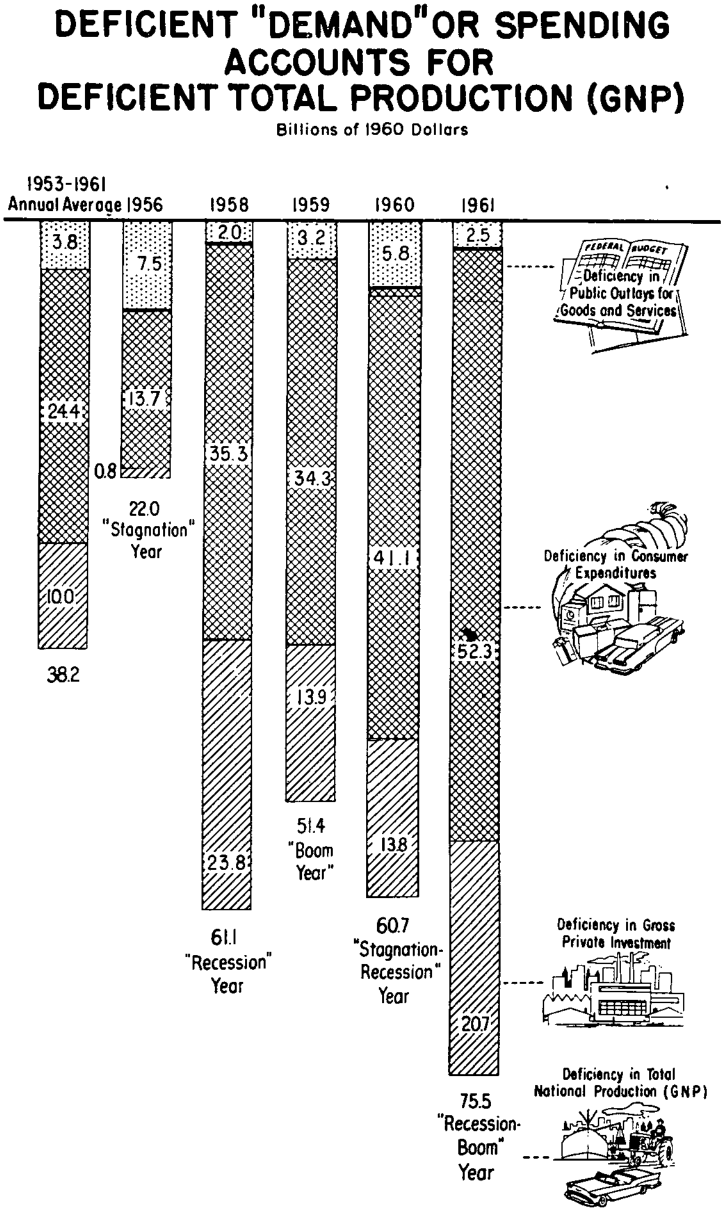
The Investment Boom Before the 1957-1958 Recession

First Three Quarters 1955 - First Three Quarters 1957



1/ Bureau of Labor Statistics, (U S. Dept. of Labor), Commodity Wholesale Price Indexes
2/ Securities and Exchange Commission, Profit Estimates.
3/ Securities and Exchange Commission estimates of expenditures for plant and equipment.

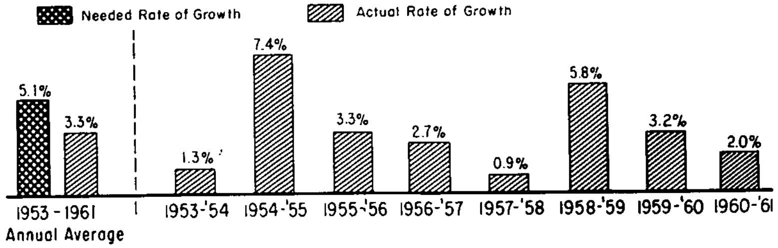
Chart 10, which is in the nature of a summary chart, shows my computation of the deficiencies in the main sectors of the economy during the period 1953–61. The fact that this chart shows some deficiency in business investment even during the boom year 1959 does not negate the proposition that investment during the boom years was too high relative to ultimate demand. The chart merely indicates that, even during these boom years, we could have had a higher absolute level of investment, on a healthier basis, if the much larger deficiencies in ultimate demand had been overcome—in other words, if the gross national product had been running at a level approximating maximum employment and production. Further, a large part of the deficiency in gross private investment in the boom years was in housing construction, not in producers' facilities.



Fifth, while the deficiency in private investment during the period under review was a reaction to the deficiencies in the demand for ultimate products, the deficiencies in this ultimate demand were caused by errors in private and public economic policies. Chart 11 illustrates in detail how the deficient growth rate in private consumer spending was not due primarily to an excessive rate of consumer saving, but rather to serious deficiencies in consumer incomes, made up mostly of deficiencies in wages and salaries and in farm proprietors' net income. Since all of my analysis is in terms of uniform dollars or real purchasing power, it does not vitiate my analyiss to observe that, if prices had increased less, lower rates of increases in money wages might have been consistent with a sufficient expansion of real consumer purchasing power.

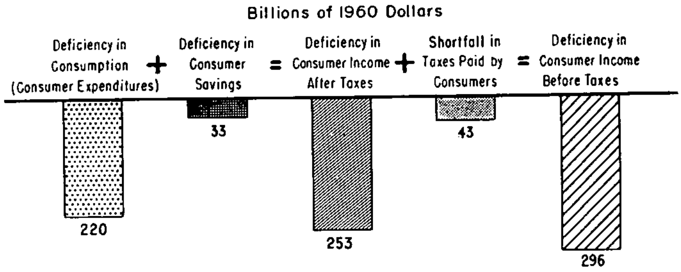
DEFICIENT RATE OF GROWTH IN PRIVATE CONSUMER SPENDING, 1953-1961

Rates of Change in 1960 Dollars



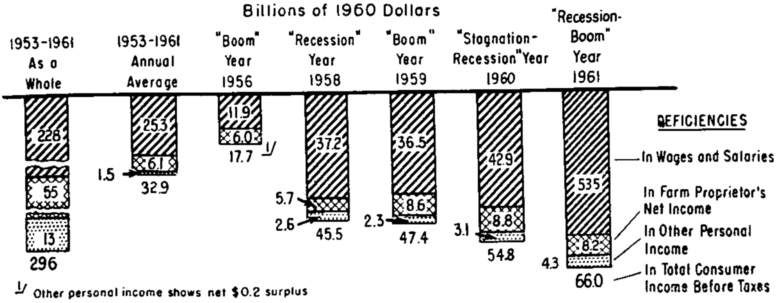
$220 BILLION CONSUMPTION DEFICIENCY, 1953-1961 AS A WHOLE, REFLECTED EVEN LARGER CONSUMER INCOME DEFICIENCY

Billions of 1960 Dollars



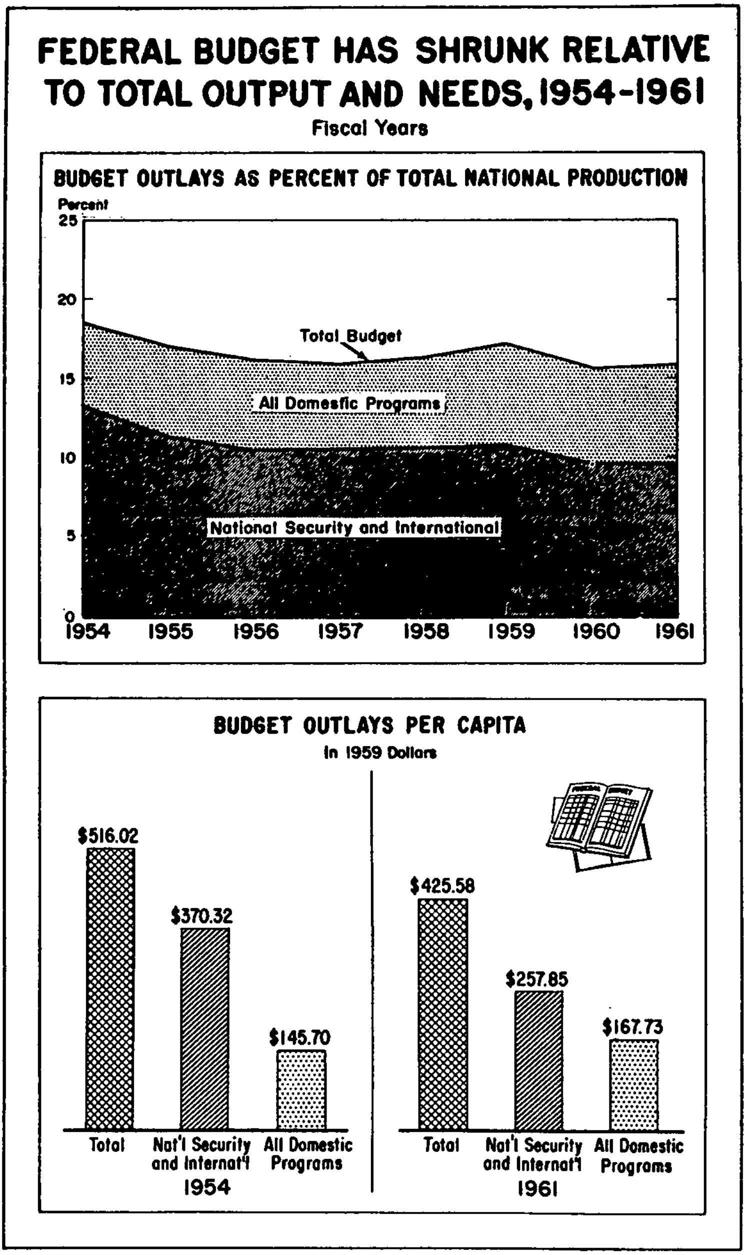
DEFICIENCIES IN WAGES AND SALARIES AND IN FARM INCOME ACCOUNT FOR MOST OF TOTAL CONSUMER INCOME DEFICIENCY

Billions of 1960 Dollars



Sixth, the deficiency in public outlays was due mainly to deficiencies in the Federal budget, as State and local outlays, and increases in State and local debts, grew at an extraordinarily rapid rate.

Chart 12 indicates how the Federal budget declined as a percentage of gross national product, and on a per capita basis, comparing fiscal 1961 with fiscal 1954, measured in uniform 1959 dollars.



Seventh, it should be added at this point that, just as our economic difficulties during the past 9 years have not been due primarily to technological obstacles, neither have they been due primarily to deficiencies in the skill or education or aptitudes of workers. To be sure, programs of training and education are always desirable in the course of progress. But it is a grievous error to explain massive unemployment, which has been due predominantly to the economic maladjustments just described, as being due in large measure to shortcomings in our human material.

Eighth, it is easy to capsule the main public and private economic policies which have destroyed the economic equilibrium during the past 9 years. Federal spending has been too restrictive. Planned surpluses in the Federal budget, devised improperly in times of high economic slack, have become actual budget deficits as the economy has reacted unfavorably to spending and tax programs based upon planned surpluses at the wrong time. Planned deficits at the right time, expressing the priority of our commitment to maximum production and employment, would have offered the only real prospect of a balanced budget in the long run. The tight money policy and rising interest rates repressed private consumption and public investment, but did relatively little to restrain the inordinate business investment booms, which were financed mainly out of the price structure and largely out of retained earnings. All kinds of special tax concessions in early 1957, allegedly to encourage investment when we already had so much idle plant capacity, accentuated these distortions. Public policies which deflated farm income, insufficiently expanded social security and other welfare programs, and held down housing, all contributed to the deficiencies in consumer incomes and spending. Despite much agitation to the contrary, prices and profits and investments in the key areas where the so-called inflationary problem centered far outran wage rate increases, and the pressure of Government pronouncements was designed to encourage rather than to combat these trends.

All of this analysis really points to the central conclusion that our greatest default has been our failure to expand private consumer spending and public investment sufficiently to equate with the growing productive power in-being, and the even greater productive potential, which have resulted from the actual processes of business investment and the thrust of the new technology and automation. This should not be surprising. Few economic generalizations are valid, but this one is certainly valid: Except under conditions of actual war or rapidly stepped-up mobilization or demobilization, the core of our economic difficulties at least throughout this century has been the failure to achieve this adequate expansion of ultimate demand. This happened in the twenties under a stable price level, when the advancing technology was not adequately translated into higher money incomes for wage earners and farmers, nor into enough demand in the form of public programs, as has been so ably developed by Senator Douglas in his great book on the subject. But it is surprising that, when the past 9 years have so thoroughly corroborated what we should have known all along, we now find a reversion to economic ideas and policies which substantially discard the new increment of experience and resort once again to the old errors which have done us so much damage.

Mr. Chairman and members of the committee, the quantifications and analyses which I have offered may be right or wrong in detail. We are all subject to human error. But this is not the main point. The main point is that I have sought to make the kind of analyses of needed levels of employment, production, and purchasing power, in their overall and component relationships, and to correlate these with policy analysis in a manner explicitly required by the Employment Act of 1946. Perhaps others can do this better than I have done it. But unless this effort is systematicaly made, all of the glowing words and academic tours de force with respect to increasing our economic growth and getting rid of our huge idleness of manpower and plant will continue to spend themselves in vain.

Turning now to the President's Economic Report and the Annual Report of the Council of Economic Advisers, I submit regretfully that reading them line by line will reveal no comprehensive and satisfactory analyses of this sort. I grant that the reports are replete with general statements that we have suffered from a deficiency in demand, usually accompanied by the observation that this has been a deficiency in the demand for ultimate products relative to our productive capacity in being. But despite this observation, perhaps the most concrete and forceful and specific recommendation is that we attempt to expedite the rate of economic growth by providing special tax incentives to investors in plant and equipment.

Aside from the many reasons which I have already given why this approach seems to me so unrelated to our problems as they actually confront us, I should like to attempt to dispose of some of the other arguments advanced in favor of this tax bonanza plan.

It is admitted by the reports that we can achieve a 3½ percent average annual growth rate, presumably through the maintenance of economic equilibrium. But then it is argued that a higher growth rate than 3½ percent depends upon accelerating the rate of productivity growth through accelerating the rate of business investment growth in producers' facilities, and indeed lifting the ratio of private investment in plant and equipment to GNP to a ratio far above that averaged in recent years. Then it is said that the special tax concession is essential to this purpose.

But the reports offer not even a scintilla of specific analysis, tending to show either as to the past or in future that those programs which would promote an adequate level of demand for ultimate products would not yield an adequate level of business investment in producers' facilities, without these tax bonanzas. If the reports had probed this problem carefully and reached conclusions different from mine, I would give them a good deal of weight. But no such analyses is attempted. Indeed, the general emphasis which the reports place upon ultimate demand suggests that the tax proposal was arrived at independently and tacked on to an analyses which the proposal does not fit.

It is true that, assuming reasonably full use of resources and growth in the labor force determined mainly by population growth, the rate at which our economy can grow from year to year will depend on the rate of productivity growth, which in turn depends substantially upon the rate of business investment in producers' facilities. If we want overall economic growth at a 6 or 8 percent annual rate, we need a higher rate of growth in productivity and in such business investment than if we are satisfied with an overall economic growth rate of 4 or 5 percent. This is obvious. But the Council of Economic Advisers and others commit a very serious technical and practical error when they jump from this truism to the conclusion that a fully employed economy growing at 6 or 8 percent a year requires a higher ratio of business investment in plant and equipment to gross national product than a fully employed economy growing at the rate of 4 or 5 percent a year. Whatever the overall growth target may be, if it is to be sustainable, the ratio of business investment to ultimate demand depends upon the technological question of how much investment produces how much goods to be taken up by ultimate demand. To illustrate, if a 10-percent increase in investment adds more than 10 percent to productive capabilities, as I believe likely in view of the new technology, then a 10 percent increase in investment needs to be matched by a more than 10-percent increase in ultimate demand. Under these circumstances, an increase in the ratio of investment to total gross national product will merely produce a frequent run of general recessions due to relative overbuilding, and the long-term consequence of this—even as during the past 9 years—will be a deficiency in investment growth, productivity growth, technological growth, and overall economic growth. In other words, a 6 or 8 percent economy requires more investment than a 4 or 5 percent economy, but it also requires more ultimate demand, and I have seen no attempt to show why the higher overall growth rate requires a higher ratio of investment in producers' goods to GNP, assuming sustainable ratios at maximum employment under either growth rate.

The reports appear to have made no attempt to analyze in quantitative terms what would be a sustainable and therefore desirable relationship between the growth of investment in producers' facilities and the growth of ultimate demand. Instead, the reports tend to support without due qualification the widely held idea that the higher the ratio of investment to consumpion, the higher will be the rate of economic growth. To test this idea, I ask this question: What would happen in the American economy if investment in producers' facilities rose to 30 percent of gross national product?

Notice should also be taken of the use of correlations which do not lead to the conclusions which they are designed to support. The reports, or the Council of Economic Advisers elsewhere, have called attention to the fact that the ratio of investment in plant and equipment to gross national product was higher in the late 1940's than during the past 9 years, and that the rate of economic growth was also higher during this earlier period. But this correlation overlooks the point that, in the immediately postwar years, an entirely different composition of gross national product was needed than the composition needed in the more recent years. A pattern suitable to transition from war to peace is by definition nonsustainable. Further, we have no clear evidence that the 1946–48 investment boom was sustainable; indeed, we got into a sharp recession in 1949, and we do not know definitively what would have happened but for the outbreak of the Korean war in mid-1950. In any event, even if the ratio of investment to gross national product has averaged too low during the past 9 years as a whole, there is no reason to conclude that it might not average higher in the years ahead without the proposed tax concessions, if the economy maintains reasonably full use of its resources.

A second illustration of incorrect attempts at analogy is involved in the frequent citation that such economies as Japan, Germany, and some others have had a higher growth rate than we have had in recent years, and that this has been accompanied by a much higher ratio of investment to gross national product.

But the comparisons are not valid, because if we had been bombed out to the extent that Japan and Germany were, we could have sustained for a few years a phenomenally high ratio of investment in capital goods to gross national product.

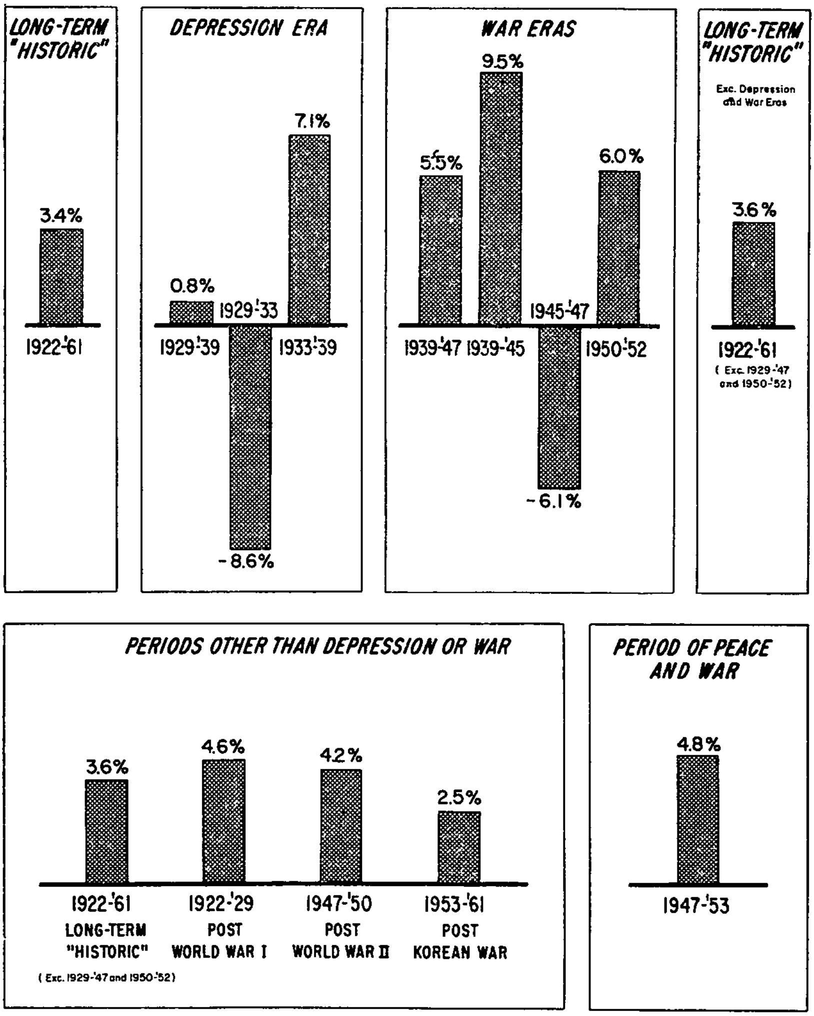
I believe that there is need to issue a word of warning against a wide range of international comparisons which are now in vogue on this whole question of the investment-consumption relationship. Manifestly, an underdeveloped country like India, or a relatively underdeveloped country like Israel, needs to strive for what in our case would be a nonsustainably high ratio of investment to gross national product. In order to achieve this, these countries must vigorously restrain personal consumption. But this does not mean that these countries now have a sustainable pattern of growth; it merely means that they are undergoing a rapid transformation from one kind of economy to another kind. Similarly, the ratio of investment in capital goods to gross national product in the Soviet Union during recent years has little bearing upon the desirable ratio here, although of course the high rate of overall economic growth in the Soviet Union does have some bearing upon how high a rate of overall economic growth we should seek to achieve in the United States. And even the Soviets, in the years ahead, will utilize a larger part of their total national product to lift their consumer living standards. As to countries like France and Italy, which recently have been growing at a faster overall rate than the United States, these countries have needed a higher ratio of investment to gross national product because they had been and still are so far behind us in the process of general industrialization. But none of the other countries I have referred to have countenanced a ratio of investment to ultimate demand which is nonsustainable in the sense of yielding recurrent recessions and high idleness of plant and manpower. Our real problem, therefre, is to find for ourselves a ratio between investment and gross national product which offers fair promise of utilizing our own resources fully and steadily. These relationships we must forge out of pragmatic analysis of our own economy, not out of superficial analogies with other economies.

Then it is said that we need a higher ratio of business investment in producer facilities to gross national product, and special tax concessions toward this end, in order to reduce our real costs, and thus to improve our competitive position overseas. There is no time here to analyze all of the issues related to our competitive position overseas and our balance-of-payments position. Suffice it to say here that, even assuming that we want to improve our competitive position, and granting fully that we are all in favor of more rapid advances in technology and productivity, the surest pathway to these objectives is the improvement rather than the impairment of a sustainable relationship between productive capabilities and ultimate demand.

I have already pointed out that, whether we want to drive for a 4 percent or a 5 or 6 percent overall growth rate, this has very litle bearing upon what constitutes a sustainable ratio between business investment in producer facilities and ultimate demand. Thus, the Council of Economic Advisers seems to me in error when it suggests that a 3½ percent rate of overall growth might be looked upon as "normal," and as consistent with maintenance of maximum employment and production once achieved, while at the same time the Council suggests that attaining the 4.3 percent average annual growth rate in our productive potentials and the 4.9 percent average annual growth rate in gross national product (allowing for the current economic slack) which are set as targets between now and 1970 would require a new admixture of investment and consumption to be achieved with the aid of special tax concessions to investors. Aside from offering no analysis to support this conclusion, the Council's assumption that a 3½ percent overall growth rate is "normal," and that a higher growth rate requires higher priority to business investment, seems to me not justified by historic observation. Chart 13 shows that the American economy, in periods other than depression or war since 1922, has registered annual overall growth rates well in excess of 4 percent or even in excess of 4½ percent, except when we had very large economic slack. The most recent figures on productivity advance, referred to by the Council, my previous chart depicting productivity trends, and the most likely foreseeable trends in the labor force, indicate that the lowest rate of overall economic growth consistent with sustained maximum employment and production after it is achieved would not be less than the growth targets set by the Council. Collaterally, the Council's use of the 3½-percent figure leads to various other aberrations of analysis and policy.

GROWTH RATES, U.S. ECONOMY, 1922-1961

Average Annual Rates of Change in Gross National Product
In Uniform 1960 Dollars



I would have no objection, through special tax concessions and otherwise, to encourage a rate of investment consistent with a 5 or 6 percent gross national product growth rate, if at the same time we took measures to promote an expansion of ultimate private and public demand consistent with a 5 or 6 percent gross national product growth rate. The trouble with the reports is that, in terms of specific programs and policies (though not in terms of general language) they are to a substantial degree bulls on investment and bears on private consumption and public investment and this merely repeats the errors of recent years.

The relative bearishness on demand for ultimate products, as a matter of actual program and policy, is apparent in the reports. The avowed endeavor to increase the ratio of business investment in producer facilities to ultimate demand is but one evidence of this. Another evidence is that, while the reports speak fulsomely of the need for public investment in our human resources, the new budget indicates a very picayune additional allowance for these purposes on net balance, compared not only with the actual need in these areas but also with the requirements for economic restoration and economic growth. The monetary policy, as the chairman of this committee has observed, is far too stringent, and I wish there were time for me to discuss this at greater length. The entire analysis of the price-wage problem in the reports shows a worthy concern about inflation, but does not in my judgment get to the heart of its real causes in recent years. And while wages are analyzed as a cost factor to business, there appears to be no quantitative analysis either of wage deficiencies in the past or of wage needs in the future as a factor in consumption. Nor is there adequate proposed expansion of nonbudget Federal programs which add to the expansion of consumption, such as social security, especially for the aged. And, finally, while the reports give full support to the modern theory of using the Federal budget as a balance wheel in the economy at large, the hard fact remains that the new budget proposes a $1.8 billion surplus in the consolidated cash budget, and a $4.4 billion surplus in the Federal sector of the national income accounts, during a fiscal year when the reports admit that we shall suffer from serious economic slack.

Coming back to the reports' specific proposal to make available an 8-percent tax credit for investment in depreciable machinery and equipment, these questions may be asked: Even if this tax credit is not genuinely needed, may it not be of some utility, on the ground that the economy admittedly needs some further stimulation and that practically any kind of lightening of the tax burden at any point has some stimulative effect? In addition, may it not be argued that this proposed tax credit would not result in direct loss of revenue to the Federal Government, because it is accompanied by offsetting proposals to close some specified tax loopholes?

Granted that practically any kind of tax concession has some stimulative effect, we are confronted with a practical situation where the desire to balance the Federal budget, whether right or wrong, is manifestly holding public outlays below the level of some of the most important priorities of our needs. This desire for a balanced budget is also holding the general tax level at rates which many economists, including me, believe too high in that these rates would yield a very large budget surplus long before maximum employment and production are attained. Under these circumstances, it is not enough to say that the tax credit proposal would have some stimulative effect. The point I would stress most emphatically is that the several billion dollars of direct loss of revenues to the Government which the tax concession would entail would be infinitely more valuable to the economy if taken in the form of other types of tax abatement, such as reducing the effective tax take on low income consumers, or in the form of increased expenditures for very high priorities for national needs. The condition of the Federal budget leaves no room to squander potential tax revenue to the tune of several billion dollars, when there would be so many effective ways of using this potential revenue. In the context of this argument, the proposal to close tax loopholes really has nothing to do with the case. Whether tax loopholes are closed or not, the principle still applies that tax concessions should be directed to where they will do the most good.

Further, even while conceding that the proposed tax concession to investment might have some immediate stimulative effect, I still maintain that it would be highly unwise economic policy, quite apart from immediate considerations of the Federal budget. In the short run, it is certainly undesirable to offer such tax concessions for the expansion of producer facilities, at a time when these facilities are still in large oversupply relative to ultimate demand, and when the main inhibiting factor against business investment expansion is the concern which appears to me legitimate that ultimate demand will not expand sufficiently to justify such additional investment. Thus the tax concession is untimely in terms of the immediate economic situation. And from the long-range viewpoint, the tax concession would aggravate rather than moderate the established tendency of investment in producer facilities to outrun ultimate demand when and if the economy is operating near maximum employment and production and thus exerting real pressure upon available productive facilities. In effect, the tax concession would misplace the stimulative effect in the short run and in the long run would generate economic disequilibrium and therefore be depressive and work against economic growth.

In this broader perspective, the undesirability of the 8-percent tax concession proposal looms very large, because it is symbolic of a more general misplacement of emphasis in dealing with our economic problems in their entirety. Nor are the amounts involved small. The difference between several billion dollars applied toward these tax concessions as against several billion dollars applied in more wholesome ways comes to an aggregate net effect which I submit to be of very large and lasting economic significance.

Before closing my discussion of investment and economic growth, I should like to comment upon the monumental study recently completed by the distinguished economist, Simon Kuznets, entitled "Capital in the American Economy." This study has been used, in some quarters, to support the thesis that the U.S. economy has suffered from a long-term deficiency in savings, that this in turn has worked against an adequate long-term level of private investment in the means of production, and that this in turn has worked against an adequate long-term rate of economic growth.

It is impossible in short space to evaluate thoroughly the Kuznets study. In brief, while it is an invaluable gathering of useful data, I do not believe that its description of what happened in the long run is accompanied by comparable analysis of why the economy behaved as it did, that is, by equilibrium analyses. To say that savings and investment were deficient in the long run, even if true, does not reveal the reasons for these deficiencies, nor examine whether these longrun deficiencies may not have been the result of deficiencies in ultimate demand which caused savings and investment, to behave in an erratic fashion, swinging between periods of excess and periods of deficiency. In other words, the Kuznets volume, if the thesis ascribed to it in some quarters is validly ascribed, suffers from the same shortcomings as the essentially similar thesis, with respect to the past 9 years, which I have appraised in detail. I would prefer to assume, however, not that Kuznets is in error, but rather that he is credited with conclusions which he has not reached.

Moreover, the Kuznets study, in its very long-range focus, does not attempt in large measure the analysis of the successive shorter range or cyclical variations in the economy which add up to the very long range performance, and which cyclical variations must be examined very carefully if one seeks to draw policy conclusions from the very long-range analysis. Indeed, Kuznets is very wary of drawing policy conclusions.

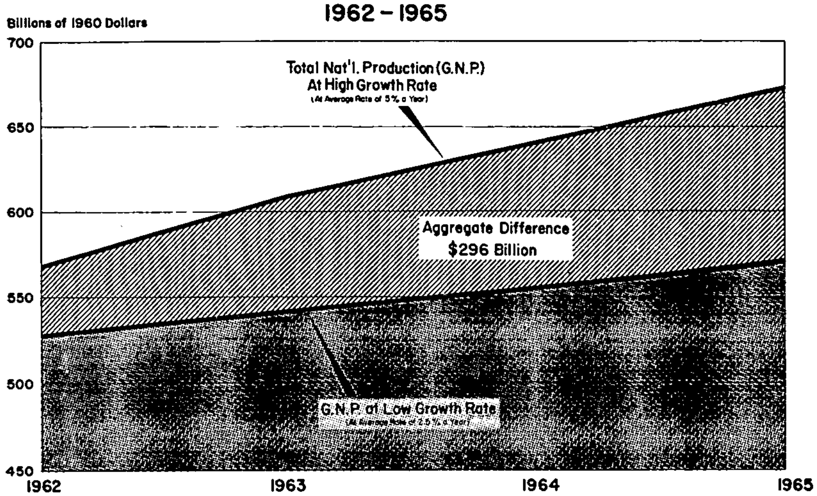
In any event, the Kuznets volume hardly touches upon the record during the most recent years, and not at all upon the current economic situation, and these periods are probably much more relevant to current policy issues than the very long range trends or the distant past. And I would venture the strong guess that Dr. Kuznets, careful scholar that he is, would be the last to argue that his book can provide important guidelines as to whether an 8-percent tax credit now to stimulate investment in producer facilities would be wise or unwise. Citation of authority may be incorrect. We should always remember who it was that Shakespeare said could cite Scripture for his purposes.

In conclusion, I believe that the reports miss the mark on some policy fronts not only because they do not thoroughly analyze the quantitative relationships bearing upon the very poor performance during the past 9 years, but also because they do not adequately project in quantitative relationships the needed levels of economic activity and their main components for the years ahead as guides to our national economic policies. The goals are stated in a rather random, incomplete, and unintegrated manner, and the recommended policies are not welded carefully to these goals. For example, the chapter on economic growth in the advisers' report calls attention to our deficiencies in health and education and housing, but it makes no attempt to state what our long-range programs in these human investment areas should be in terms of human needs and national economic equilibrium. Most surprising of all, the chapter on economic growth contains no significant recognition that the main problem of economic growth, in the American context, is to maintain economic equilibrium. Instead, this chapter merely cites an impressive list of factors in economic growth, much as they might be cited in a textbook written for all time but not geared to what needs to be done, and in what proportions, at any given time.

I submit, for the record, charts 14 through 17, in which I attempt to quantify our tasks in the immediate future and in the years ahead. These balanced portrayals of economic growth objectives represent in coverage and method what I think the reports should contain. My quantifications may be in error, but in the substantial absence of such qualifications I can find no impressive nor even adequate growth program in the reports now before this committee.

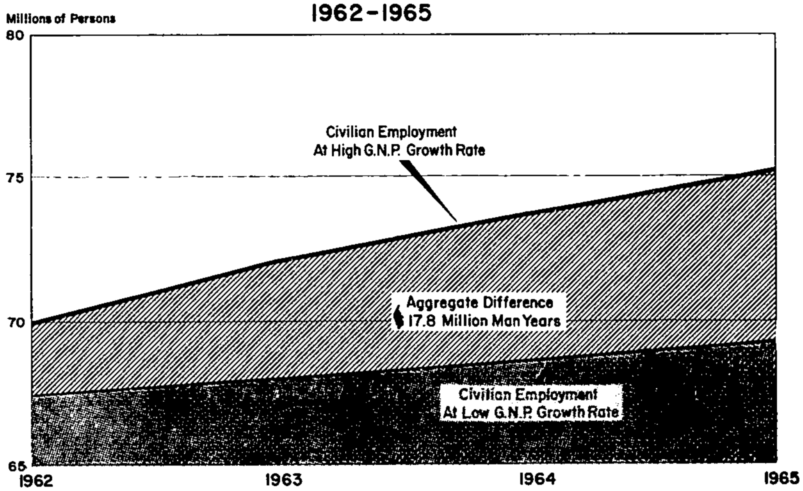
BENEFITS OF HIGH GROWTH RATE IN TERMS OF PRODUCTION

1962 - 1965



BENEFITS OF HIGH GROWTH RATE IN TERMS OF EMPLOYMENT

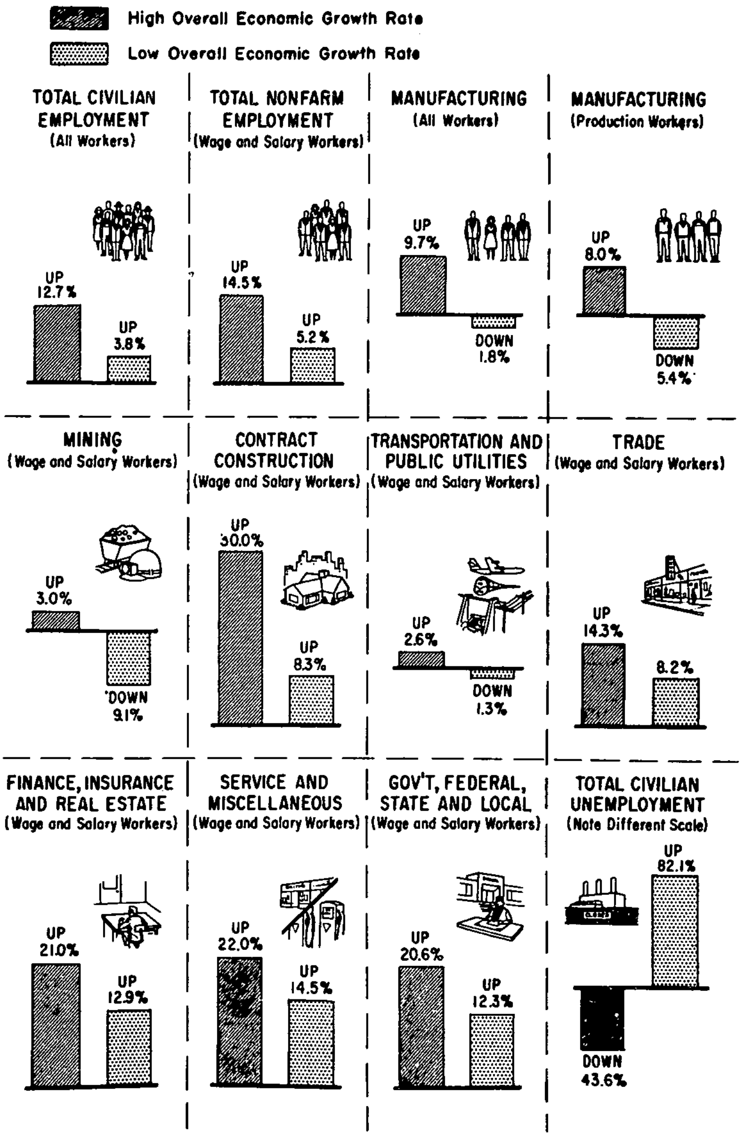
1962-1965



NOTE: 1961 is used as the projection base year for this chart.

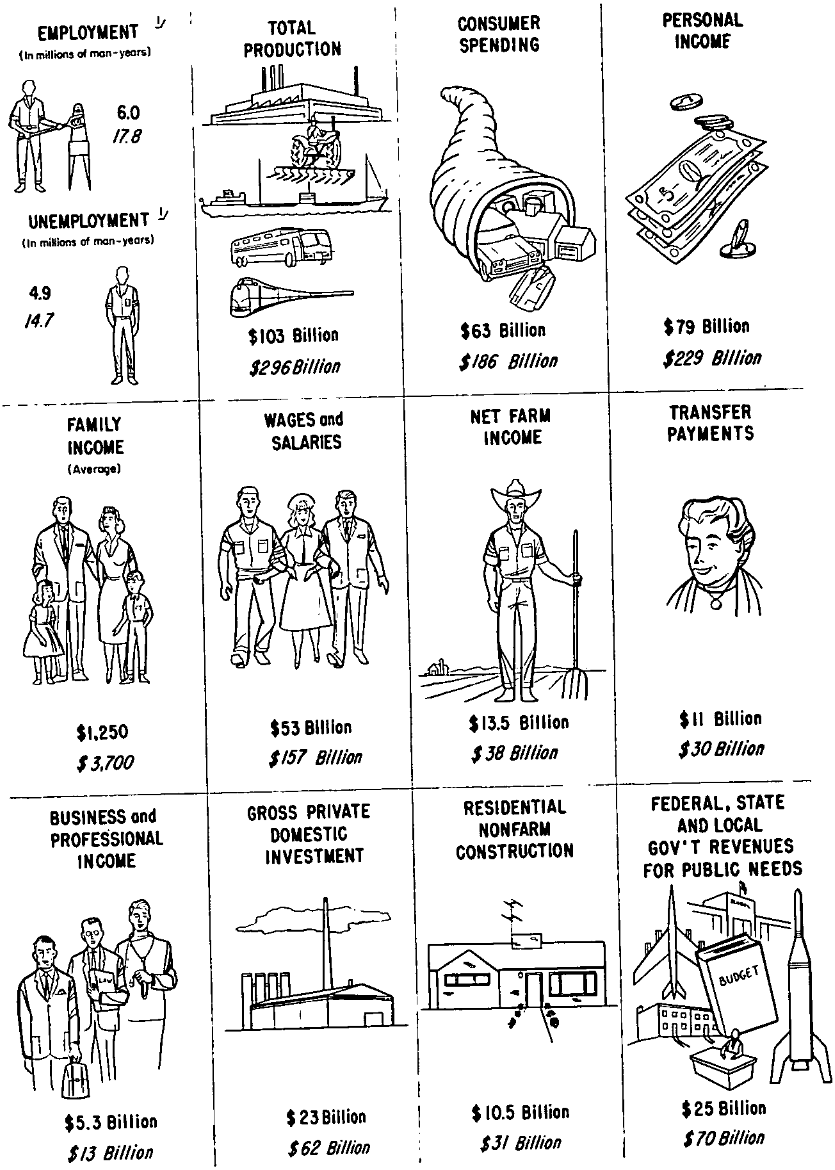
ALTERNATE EMPLOYMENT TRENDS, 1960-'65, AT HIGH & LOW OVERALL GROWTH RATES

Index: 1960=100



DIFFERENCES IN RESULTS OF HIGH AND LOW OVERALL GROWTH RATES, 1962-1965

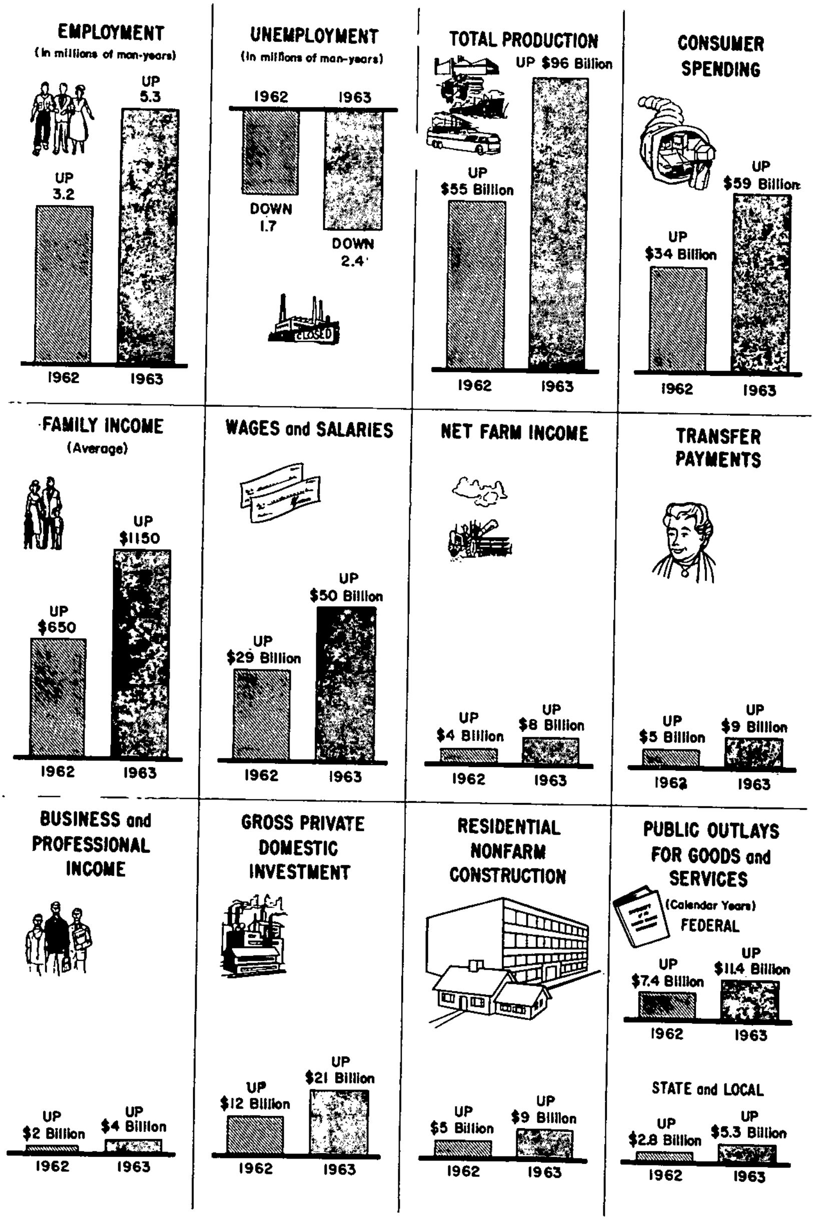
Bold Face - Difference in 1965; *Italics - Difference for four year period as a whole*
Dollar figures in 1960 dollars



1/ High growth rate would draw more persons into the labor market than low growth rate.

GOALS FOR 1962 AND 1963, CONSISTENT WITH LONG-RANGE GOALS THROUGH 1965

1962 and 1963 Goals Compared with Estimated 1961
Dollar Figures in 1960 Dollars



I am sorry that I have been so critical, for I am entirely in sympathy with the aims of the administration. In many respects, I believe that the reports now before you represent a substantial advance over earlier reports. Their general tone is progressive, candid, and farsighted. They do not hestitate to state the tasks of responsible government. I have a high personal regard, and a high professional respect, for the three members of the present Council of Economic Advisers. I realize fully, from my own experience, that the advisers are bounded by many limitations not of their own making, and that they are not at liberty to say all that they may believe nor to advocate precisely and fully all that they may think desirable. The public service is both an asset and a liability to the individual engaged in it. These comments go double with respect to the President of the United States, whose problems, both domestic and international, both substantive and political, would be so close to unbearable if the bearer were not so strong.

Yet I cannot avoid the conviction, especially in the light of the nature and failings of the economic upturn in process since early 1961, that unless we alter our course and profoundly reshape our economic thought and action—and here this committee of the Congress can be of immense help—we shall register an economic growth rate during the next few years not appreciably better than the average since 1953. If this should happen, in view of the new technology and the rapid growth in the labor force, our idleness of plant and manpower in the years ahead would average very much higher than in recent years. Our domestic defaults would worsen; our international position would become critical indeed. Therefore, I feel that some of us must assume the unpleasant task of being sincerely critical, even if we cannot be sure that we are correct.

Mr. KEYSERLING. I would like to proceed now to summarize my statement, if I may.

Chairman PATMAN. You may proceed as you desire, sir.

Mr. KEYSERLING. First of all, Mr. Chairman and members of the committee, I have some impression that most of what the other three witnesses have said supports what I am going to say. But frankly, I did not fully grasp part of what they said. And as I think they will understand what I say better, I will have to let them check whether I am right in supposing that they support what I have to say.

I want to quote again before the committee what the German poet said, "My worthy friend, gray are all theories, and green alone life's golden tree."

I think the task we have before us is to look at the American economy in action, and, on the basis of empirical observation of what has been happening, try to derive a set of national economic policies which will given us a better economic growth rate than we have had. This is perfectly consistent with admitting that there are many things which economists do not know, and some things which they will never know. But nonetheless, all policy must be based upon feeling that one is sufficiently confident of his analysis to proceed on that basis.

The very first point I want to make, based upon this growth chart (chart 1) with which you are familiar, is that the low average growth rate of the American economy during the period since 1953 has not been due substantially to an insufficient growth in the labor force or an insufficient growth in productivity. This can be demonstrated simply, and it provides a guide to the basic problem of a workable relationship between investment and consumption as this bears upon economic growth.

A very simple formula is this: If the labor force had grown annually by 1 percent, and productivity had grown annually by 1½ percent, on the average, the economic growth potential would have been 2½ percent. And since the actual growth of the economy, 1953–61, averaged 2½ percent, we would not, on this assumption, have had the chronically increasing idleness of manpower and plant which we in fact have had. Therefore, it necessarily follows that the growth in the labor force and in productivity have on the average been much higher than the actual growth of the economy.

Further, if one observes the actual growth rate in the economy, varying from a 2-percent decline in 1 year (1954–55), to a 7.9-percent rise the next year, to a 2.1-percent rise the next year, to a 1.6-percent drop 2 years later, and to a 6.8-percent rise the next year, it is manifest that neither the growth rate in the labor force nor the growth rate in productivity has been anywhere near that erratic. So proposition No. 1 is that there must be some other explanation than the labor force and productivity of why the economy grew so slowly during 1953–61 as a whole.

This is perfectly consistent with the proposition that, while the labor force and productivity combined grew more rapidly than the economy, the slow growth in the economy had an inhibiting effect upon the growth in the labor force and the growth in productivity. The best example of the inhibiting effect upon the growth of the labor force is that, from a year ago until now, the civilian labor force has actually declined. The only possible explanation of this is the inhibiting effect of high unemployment for long periods of time.

Secondly, it is equally clear, and even more important from the viewpoint of the productivity problem and the investment—consumption relationship, that actual productivity growth, as distinguished from growth in the technological productivity potential, is greatly affected by the actual condition of the economy. I think it would be a safe generalization, as to the past 9 years, to say that the low growth rate of the economy adversely affected productivity, rather than to say that the unsatisfactory growth rate in productivity adversely affected the growth rate of the economy. This is indicated by this chart (chart 6) which shows a gradual acceleration in the rate of productivity growth over the decades based upon the advancing technology, but a very sharp adverse reaction of productivity growth to a low rate of economic growth. For example, from 1950 to 1955, we seem to have had a productivity growth rate averaging annually close to 4 percent. But the rate declined to about 2 percent during 1955–60, when the rate of economic growth was very low, and the annual productivity growth rate seems to be in the neighborhood of 4 percent, during the current economic upturn which is pulling productivity upward. This principle is demonstrated even more clearly in the lower half of the chart.

The question this really leads to is: What, then, has been the reason for the low economic growth rate? I submit that the central reason for the low economic growth rate is that, recurrently in the boom or upturn periods, the economy got out of balance and economic equilibrium was destroyed. If we can discern the main reasons why, during these boom periods, the equilibrium was destroyed and the economy moved downward, we will have discerned how better to stabilize the economic growth rate. And better stabilization of the economic growth rate will in itself, because of what I have already said about the labor force and productivity, yield an economic growth rate of 4 to 5 percent a year, which is in the nature of what the President's Economic Report is shooting at.

Succinctly, my analysis is that the equilibrium was destroyed in each instance because investment in plant and equipment got our productive capabilities in-being far ahead of the ultimate demand represented by the composite of private consumer outlays and Government outlays at all levels. This, to me, is extremely clear from analysis of the successive booms and downturns during this period.

Let me say, in this context, that very long-range historical analysis proves relatively little, because if you take a long enough period of time, everything "balances out." If I drink too much beer and eat too much, and then get put in the hospital and eat and drink very little, my average intake during the whole period of time may be very low. But it is nonetheless true that the short-term excesses produced the short-term trouble and the low average in the longer run. Thus, what happened between 1850 and 1953 is infinitely less relevant analytically and empirically to the problem we have to deal with now than a shorter term analysis of what has happened between 1953 and 1961.

I am sorry to say that I cannot find anywhere, and I say this regretfully, I cannot find anywhere in the report of the Council of Economic Advisers any sustained attempt at a really careful quantitative interrelationship or equilibrium analysis of why we have had the trouble we have experienced in the immense American economy during the past 9 years. And without this kind of analysis, we have no sufficient basis for the formulation of policies for the future. I submit that some of the main policies presented to you, particularly the 8-percent tax credit, reflect this lack of analysis and would, indeed, repeat the very imbalances, the very disequilibriating forces, which we have suffered.

I am inclined to think, and he will have to correct me if I am wrong, that when my friend, Dr. Colm, says that he is for this tax proposal only if we take other measures which we are not now taking to stimulate ultimate demand, he is really saying that in the context of the program now being proposed this tax proposal would accentuate and exacerbate the very imbalances on the side of investments that we have had in the recent past. In the short run, the tax credit would be a futility, because we now have so much excess plant capacity, and in the longer run the tax credit would increase the unstabilizing factors which we have had in the recent past.

This chart (chart 8) shows how, during 1953–61, investment in producers' durable equipment has swung up and down much more rapidly than GNP. That is a well-known thing, and I will run over it very rapidly.

Another chart (chart 7), subject to further study, shows how, during two important boom periods, business investment ran far ahead of demand for ultimate products. This in turn led to very severe downswings in business investment as it responded to the fact of excess capacities.

I also have a chart here (chart 9) which I think tends to show that one of the most axiomatic and self-evident facts in the American economy is that, in any period when ultimate demand is high enough to support a high growth rate in business investment, business in general lacks neither the funds nor the incentives nor the retained earnings nor the tax treatment which will induce that high level of business investment. In fact, our real problem is to prevent business investments from becoming relatively too high during these types of periods. I have studied recent reports of this committee which I think tend in the same direction.

In the framework of this analysis, we are now called upon to evaluate two main aspects of the administration's program: (1) A proposal to accelerate the increase in investment in plant and equipment through an 8-percent tax credit; and (2) a budget which, if you look at it in real economic impact terms rather than in conventional budgetary terms, really proposes a surplus ranging between $1.8 and $4.4 billion. I maintain that this combination of stimulating business investments and repressing ultimate demand is a substantial repetition of the mistakes which I tried to advise committees of in early 1957. I am rather surprised that this mistake is being made by people trying to learn, on the basis of experience, and trying to vindicate their own criticisms of those who had preceded them.

The main argument advanced for the tax credit proposal runs about like this: If you have more investment in plant and equipment, productivity will grow faster; if productivity grows faster, the economy will grow faster; and therefore, if you have a higher ratio of business investment to the whole national product (GNP), the economy will grow faster. This argument neglects the obvious point that, whether you aim for an economic growth rate of 2 percent, 4 percent, 6 percent, or higher, this has very little to do—in the perspective of the highly developed U.S. economy—with the appropriate ratio of the growth in investment in plant and equipment to the rate of economic growth. This is because the rate of economic growth, to be sustainable, must reflect a ratio of plant and equipment investment to the total size of the economy which expands productive power pro tanto with the expansion of ultimate demand. In other words, if a 10-percent increase in business investment causes productive power to rise by 15 or 20 percent, which I think is very likely under the conditions of the new technology, then you need a 15- or 20-percent increase in ultimate demand to sustain a 10-percent increase in such investment; and in that event, you need a falling ratio of investment to the total size of the economy, regardless of what size economic growth rate you want.

Thus, if we want to aim for a much higher economic growth rate, we must intensify our efforts to get a higher growth rate in both business investment and ultimate demand. But the statement that, to get a higher economic growth rate, we need a higher investment ratio to GNP is clearly a non sequitus. Such a policy would merely lead to more frequent recessions, and thus would average less investment and less productivity in the longer run.

For the same reasons, the argument that we have to expand investment faster than consumption, in order to lower our competitive costs so that we can sell more goods overseas, and that therefore we should support an investment tax credit which otherwise we would oppose, is completely beside the point. We can lower our competitive costs only if we reduce real costs, and we can reduce real costs only if we get more investment in the longer run, and we can get more investment in the longer run only if we maintain economic equilibrium. If we force investment out of line with ultimate demand, so that we average only a 2.5 economic growth rate during the period of the next 4 or 5 years, we will get a lower rate of investment in a 2½-percent economy than we would get on the basis of a 5-percent economy. Thus, in my view, the tax credit to stimulate investment would be self-defeating.

So I suggest that this committee, as I know it will, give careful attention to the problem of economic equilibrium. It is perfectly true that, if we wanted to have a 9- or 10-percent rate of economic growth, we would have to give carefully selective tax concessions to industry, and we would also have to do many things to stimulate ultimate demand which are not now being contemplated. But within the framework of a 4- or 5-percent growth rate objective, the tax credit proposal seems entirely erroneous. And may I say that use by the Council of Economic Advisors of a 3½-percent growth rate figure to arrive at conclusions about the need to stimulate investment through this tax credit seems to be entirely out of line. No analysis can show any period in American history since the turn of the century where a 3½ percent growth rate supported anything like reasonably full use of resources. This seems to me a forced argument to provide support for a tax proposal arrived at independently. Therefore, I suggest that, if we examine the equilibrium problem, and make balanced projections ahead as the Employment Act intends, we will find no rational basis at all for a composite of tax and budget policies which seems to me to be extremely disequilibriating and not to be in consonance with what we are trying to do as a Nation and a people.

Thank you very much.

Chairman PATMAN. Thank you very much, Dr. Keyserling.

Senator DOUGLAS. I would like first to have the panel turn to page 128 of the report of the Council. Many years ago I attempted to study the quantitative relationships between changes in the available quantity of capital, the man-years of labor, and the physical output in manufacturing, and found that historically, output grows from one-quarter to one-third of the difference between the ratio of the increase of capital and the ratio of the increase of labor.

In other words, the ultimate that occurred was from 1 to 1¼ between the labor and the capital curve.

It was surprising that they found this result in the British Commonwealth. Then when we took not years as observations but industries within that area for observations, there was further corroboration of our findings. Curiously enough, the share of the product which went to labor-capital seemed to be not far from the share which you would expect under this arrangement. If you look at the chart on page 128, however, and address one's attention primarily to the period of 1940 on, you will see there that output grows much more rapidly than physical capital in the stock of plant and equipment.

It is obvious that if these production values were true throughout the early 1900's, they certainly were not true from 1940 through 1960.

I assume what happened was improvement in technology and the improvement in the quality of both labor and capital.

Dr. Goldsmith, have you a comment on that?

Mr. GOLDSMITH. You are correct, Senator. Up to the 1920's, when you made these studies, the increase in the volume of capital and of labor could explain fairly accurately the increase in output. But this isn't correct any more for the postwar period.

Studies that have been made by various authors, show that the increase in output is larger than the increase in input, whichever way you figure them and however you combine them, this means that, to use a vague term, technical progress has become a more important element in the increase in output. There is another factor of importance, the change in product mix.

There has been apparently, although it may be a little early to say so definitely, a change in the aggregate production function. This, of course, is of very great importance for this problem. As I tried to point out in the statement, if this change is permanent, and we have no reason to assume that it will not be, then we can have the same rate of growth, with a smaller investment-output ratio than we could have had in the 1920's or before.

Dr. COLM. Elaborating further, I think there are three factors involved in the postwar period. One is the change in the relationship between plant and equipment. We are packing much more equipment into the same shell. The shell is very expensive, with a very high capital-output ratio. The equipment has a lower ratio.

So there is a changing mixture in plant and equipment which I think is one of the factors. Second, there seems to be a resumption of the long-term trend toward increase of productivity of capital because of technology.

This is not shown in this chart because it does not go back to the 1920's. It does not refer that far back.

It is very clear that our technology is not only labor saving but also capital saving. This is particularly true if you include also the inventory, which is not in this chart.

Third, as has been referred to, there is a different product mix. We have in the manufacturing industry 40 percent of current investment in private plant, and equipment, but only 33 percent of employment. In the trade, service, and all those groups which are now expanding much more than manufacturing, there is 25 percent of all capital investment and 57 percent of employment. We have here a higher output relative to the capital investment.

I think these three factors explain the change. I would say that I do not know so well about plant and equipment, but certainly the other two factors are likely to continue so that the continuation of this trend shall be assumed for projections.

If I may add this difference in the capital-output ratio in manufacting and trade and services, in my opinion, also explains part of the difference in the capital to GNP ratio between the United States and Western Europe, for instance, and certainly Soviet Russia and Japan.

Senator DOUGLAS. Would you place any importance on any improvement in the quality of labor?

Dr. COLM. Greatly, Senator. I know all the recent studies show the great importance of increases in education for economic growth.

Senator DOUGLAS. Is a consequence of what you are saying that production can be increased and growth stimulated, not merely by more investment and more capital but also by the speeding up of worthwhile inventions, research, improvement in health, improvement in education, and so forth?

Dr. COLM. Senator, I think if you put it in quantitative terms, increased technology is, I think, the greatest stimulus that can be provided to economic growth.

We have this tremendous reservoir of research, broadly speaking, in the defense area. Anything which speeds up the flow of research from the defense area into the general economy would be greatly of help in support of economic growth.

Senator DOUGLAS. Research is dependent upon education?

Dr. COLM. Yes.

Senator DOUGLAS. You cannot put a bushman in a business laboratory.

Dr. Hamberg, do you wish to make any comments on that?

Dr. HAMBERG. Well, if I have to guess at the behavior of this chart, I would suggest that the main explanation stems from a factor I talked about in my statement, namely, that in recent years, although there may still be a lot of outdated equipment, we have had substantial modernization of the capital stock.

We have had high rates, fairly high rates, of investment, perhaps irregularly, since World War II, and clearly this new capital, while it was not necessarily net investment, was new gross investment, tended to incorporate at least the latest techniques existent at the time of investment.

So, by guess would be that this decline in the average age of the capital stock which took place, I think, in postwar years would explain—and the resulting higher level of technology incorporated in that capital stock would tend to explain—this relationship between output and capital stock in the diagram.

In effect, I am suggesting that capital stock is more efficient today than it was. That seems to me a quite reasonable assumption.

It is for the economy as a whole, and I would guess, perhaps, for the manufacturing industry in particular.

Mr. KEYSERLING. I have two interrelated comments. The first is that I have become convinced, in correlating various aspects of the economy in recent years, that there has been an increasing productivity of capital, which means that each dollar of new capital investment results in more than a dollar of increased product.

I do not think there is any other explanation of the fact that, while the CEA's observation is true that the ratio of capital investments to GNP has been rather low over the past few years by some historic standards, there has nonetheless been a terrific increase in unused plant and manpower. This strongly indicates an increased productivity of capital.

This increased productivity of capital accentuates the relative problem of expanding ultimate demand enough to keep up with the capital investment trends.

I have a second point. Even if I am wrong on the above, even if we assume that the investment in plant and equipment during the past 9 years should have averaged higher in ratio to GNP, the question still remains as to why it did not average higher.

I think if we had prevented the excesses, the extreme excesses, which such investment showed in the boom periods, and had leveled off such investment at a more sustainable rate of growth through more accent upon stimulating ultimate demand during those excess periods, the capital investment relative to GNP might have averaged higher over the 9-year period as a whole.

In any event, such investment would have averaged a higher ratio if a higher ratio were sustainable, and if a higher ratio were not sustainable, it would be a tremendous disadvantage to have a higher ratio.

So, any way you look at it, whichever hypothesis you take, I think you come to the same ultimate conclusion.

Senator DOUGLAS. If we took 1945 rather than 1940, because of the peculiar war situation, the physical amount of capital did not increase, but there were the second and third shifts, with full utilization.

I haven't too much time left but there is one question I would like to raise. It is frequently said that if you increase production, you must also increase the mass purchasing power to absorb the products which are turned out. I would like to raise this question:

If we had more competition, would we not have a reduction in cost per unit and a fall in interest rates so that even if the total money stock did not rise there would be an increase in the quantity demanded at lower prices and, therefore, the economy would not get out of equilibrium?

If this is so, then is not the difficulty created, because of arrangements which make it difficult to reduce prices or to allow interest rates to fall?

Does anyone want to reply to that?

We only have 1 more minute.

Mr. KEYSERLING. I would say that I think the Senator is right. If we had perfect competition or classic equilibrium, we could achieve a stable growth rate at a lower price level. But since we do not have perfect competition, policy must be exerted at the points where the disequilibriums appear. Some of the policies now proposed seem to me to be addressed to the wrong points.

Senator DOUGLAS. Anyone else?

Dr. HAMBERG. It seems to me you ought to push that a little further. For example, it seems to me if you are going to assume these flexible prices, that would not be enough, from the point of view of market structure.

For example, if we tended to have excess capacity, and if interest rates were flexible, then they might fall and cause a substitution of capital for labor and the excess capacity could be eliminated that way, provided, however, we could assume that there was no limit, no lower floor, on acceptable rates of return that would follow upon the higher ratios of capital labor and also that interest rates could be brought down indefinitely.

It seems to me regardless of the state of competition that there are floors both to acceptable yields, rates of return on capital, and interest rates that would exist independent of the state of competition and, in effect, suggest that even if you had pure competition the problem could not be solved, and certainly not over long periods, indefinitely.

So, we are back to aggregate demand in some sense.

Senator DOUGLAS. Aggregate money demand?

Dr. HAMBERG. Yes, to keep the capital-labor ratios from rising indefinitely.

Senator DOUGLAS. Or the possibility of stabilization of rates?

Dr. HAMBERG. Either way. I am not sure that that isn't putting the emphasis in the wrong place. Even if you have flexible interest rates, the chances are they are flexible downward only to a point.

There are administrative costs, risk premiums, and so forth. I think also that there are minimum acceptable profit rates of return, and I do not think, therefore, there is unlimited flexibility regardless of the degree of competition.

There is a limit to these.

Senator DOUGLAS. Mr. Curtis.

Representative CURTIS. First, Mr. Chairman, I want to apologize to the committee for not being a better attendant, but it seem this year they have sort of unloaded on the Ways and Means Committee and we do not have too much time.

The second point is purely procedural. I was thinking as some of these rather lengthy papers were presented here, and, of course, they have to be paraphrased, whether or not it would not be more gracious to the witnesses and also more productive if those papers were made available to the members ahead of time. Sometimes we can read them ahead and in that way we would be able to interrogate a little better.

On the other hand. it does impose a burden on the witnesses to have papers earlier. But I make that as a point because these papers will be in the record, but I certainly have not had a chance to read them. So my interrogation will be limited to what has been brought out in the oral testimony.

One thing that I wanted to emphasize were the suggestions made by Dr. Goldsmith, with which I, as a layman, am so much in accord with, the recommendation that we get more data in this area.

Your concluding statement is, "Finally, what we actually know with reasonable confidence and reasonable detail about volume and structure of capital formation, of the Nation's stock of capital, and on interrelations, with the main and measurable factors of economic growth, is quite insufficient as a basis for intelligent policy formation."

The details which you spelled out in your paper, sir, are areas that we need to go into. I feel very deeply that this is correct. Our Subcommittee on Economic Statistics, in my judgment, might well go into that. So that leads me into the question that I would like to pose to the panel.

Everything has been predicated on economic growth without any definition of economic growth. I presume the only definition used is this differential that exists in gross national product. At least, that was the basis, I believe, for the statements that the economy was stagnant, as one said, with recent slowdowns in growth, and so on.

It strikes me that gross national product, although a very helpful economic factor, was never set up to measure meaningful economic growth.

May I ask first, if the panel agrees that that is a very limited tool in measuring economic growth, and, if it is, what other factors we should look to in order to discuss what we are talking about here, which is economic growth?

Dr. Colm?

Dr. Colm. Mr. Curtis, I am very glad you raised this question. First, let me say increase in economic growth is not necessarily increase in the economic welfare. These are two different concepts. After having said that, I would say that economic growth, what we really mean by it, is an increase in total production of goods and services.

Representative Curtis. That would be, then, the gross national product.

Dr. Colm. The gross national product comes closest to it. There are a few things wrong with the GNP. One is, I think it includes a small amount of duplication because of the depreciation, and, second, it does not give adequate weight to new products.

So I would say GNP is not a perfect tool. But for all practical purposes of policy consideration, I would say it is good enough.

If I may add one proviso, for many purposes you want to consider GNP per capita.

Representative Curtis. Let me add a few other items that I think are not included, which, to me, are very important. One is the housewives time. That is not in GNP, is it?

Dr. Colm. No.

Representative Curtis. Let me list some, because I want to get the discussion going.

The measure of governmental goods and services is rather an arbitrary measure, as I understand it. The increased leisure time, which comes out in the do-it-yourself is not listed. It would strike me that increased productivity probably would show a preliminary decrease in gross national product unless other factors came in because it would tend to result in more leisure time.

There are so many areas that seem to me to relate to meaningful economic growth.

There is one other item: Economic errors, which loom frequently quite large, or replacement. For instance, here are railroads, in effect, being replaced in transportation by the private automobile. Those things relate to what I would say is meaningful economic growth.

I think that by using the GNP, although I do not want to be misunderstood—I think it is the most important statistic we have—when we cut it off there and just talk, as I understood the panel, all of them, were talking in terms of economic growth, it is as if that were an accurate and adequate measure.

It is really the adequacy of the measure about which I am raising the question.

Dr. Colm. Mr. Curtis, I think every point you made is well taken. We do not include the work of the housewife, but we could, and for some countries it has been done. I had the opportunity in December to look at economic conditions in an African country where the nonmonetary items are about one-third of the whole GNP. The services performed for their own use (e.g., building lists) have to be taken into account. But as a general rule, I would say that we include such item if the inclusion would not lead to greater errors than their exclusion.

Granting everything you said, Mr. Curtis, and also granting that more work should be done in improving our national accounts, granting all that, I do not think we are misled by using GNP in real terms as a broad indication of change in total production and using it for policy considerations.

Representative CURTIS. Dr. Goldsmith?

Dr. GOLDSMITH. I would agree with that, particularly if you are thinking of the short-run period, up to a decade or two. These arguments, these points that you made, which are very well taken, are much more important when we make long-term comparisons in one country or when we compare one country with another. In those cases we must be very careful to preserve a reasonable degree of invariance; for instance, to use the famous example we tell our students, we must not make the national income go up because a man marries his cook.

But these are really technical points which the experts can handle. I hope that some of these points you mentioned will be taken into account as our national accounts are further improved.

Leisure time is a little bit different. There we come back to the fact as Dr. Colm said correctly, that national product is not a welfare measure. We measure the value of output. Leisure time enters into the comparison between output and input. It would be relevant if you wanted to measure productivity. The do-it-yourself activities, on the other hand, again, are correctly a part of output, and there should be an allowance made for what you do to improve your house or your garden, and so forth.

These are technical problems and I am quite sure that in the course of time they will be handled. But for shorter term comparisons and for the economic policy problems that you face from one year to another or from one cycle to another, they do not detract from the value of GNP.

Another more important factor is the allowance for price change. Of course, when we make comparisons over time, even a limited period of time, we must make some allowance for the change in prices. It is probably true that the present methods have overstated the price rise and, hence, understated the increase in real product. This is a problem very well known to the specialists.

Representative CURTIS. Here is the reason that I raised the question: I think in my judgment this is highly inadequate because it has led many economists, as Dr. Keyserling has, to regard our economy as having slowed down by that standard. But by the other standard of automation, being so rapid that they really developed a new term for an old phenomenon, this is very inadequate measuring. For example, 30 percent of the goods and services now on the market were unavailable 5 years ago.

There is an economy that is growing in my judgment in a very meaningful way. But this tremendous innovation that is occurring apparently is not reflected in this particular statistic.

I think it is in error to suggest that we have a stagnant or a slowed-down economy when this kind of phenomena is occurring.

Dr. GOLDSMITH. No, this is not correct. The fact that there are new products is not ignored in calculating GNP. The new products, of course, are in. The only point you can make is a very technical one, that these new products are not put in at the right prices, compared to the previously available products. There has been a good deal of professional discussion about that. That may make a small difference. Let us put it this way, that if we now figure the rate of growth was 2.4 percent, perhaps, this might be 2.5 or 2.6, if a more adequate allowance for new products were made.

Representative CURTIS. I think you are missing my point. I am saying that as far as the citizens are concerned, and as far as the ability of the economy to produce, and its flexibility, which means a tougher economy, when you have this rapid innovation we are really talking about something that is economic growth, but apparently the GNP, for some reason or other, does not give it that weight.

Let me relate to another thing, which is quite clear. In any war, as a matter of fact, you take the same gross national product starting out before World War II, at 100, actually, and in 5 years of war it becomes 213. That is not real economic growth.

That is military goods which are largely expended, and we all know that. I think there are other somewhat subjective tests that can be applied which illustrate the really grave limitations of GNP as a method of measuring where our economy is going and whether or not it has this flexibility and toughness which it seems to me the automation that has occurred, the innovations that exist, show to be a fact.

Dr. HAMBERG. Congressman, even if you were correct, this problem would have applied to periods in the past. There is nothing new. There would be nothing new about this, and it would still be true.

Representative CURTIS. I have not much time, but let me pose this and then we shall come back to it. Suppose you had a really stagnant economy where there was no innovation, the goods and services remained the same, a blacksmith still could be a blacksmith, your styles were not going out because of automation, and new skills coming in.

How would an economy like that show up? It could show, I daresay, in increases in GNP. And then, on the other hand, take an economy that is rapidly growing. Take the economies that existed after World War II, Russia, Germany, Britain, France, and Japan, industrial economies which had their war plant badly damaged, and replace it and see what happened in those in measuring GNP.

Dr. HAMBERG. I am sure that most of us would agree in a technical sense to that, but my point is that the change in product mix over time, perhaps as a result of new product innovations, and the like, still isn't new and has existed as long as economic growth has occurred and our measurements of it have existed, and it would still remain that the problem which has been bothering us in the last few years is that however we measure the GNP we are still growing, obviously, more slowly than our potential would permit.

Representative CURTIS. I think I have been misconstrued. My point is that I do not think even fixing GNP up to plug these inadequacies would catch what we are really talking about in meaningful economic growth.

It comes into that area when I use the word "meaningful," because then it becomes somewhat subjective.

My time is up.

Representative REUSS. Dr. Colm, is it the thesis of your paper that for greater growth this country needed greater demand, and the way to get greater demand was by monetary and fiscal policy, and that as between the two sets of policies, monetary and fiscal, you said freedom to adapt monetary policy to requirements of domestic economic growth is limited by balance-of-payments considerations?

I have two questions to ask in connection with that. First, does monetary or fiscal policy need to be limited very much by balance-of-payments considerations, if they are based upon sound domestic economic principles of striving for maximum production without inflation?

I say that in view of the fact that our balance-of-payments deficit which we are worrying about, quite properly, is on the order of $3 billion a year.

In the context of a $570 billion economy, I hope you will agree with my general proposition that given sound domestic monetary and fiscal policies, the balance of payments need not distract us very much.

Dr. Colm. I agree with you. It is difficult to measure the impact of differential in interest rates on capital movements. Quite frankly, I do not know. I do not believe anybody really knows how much differential in short-term interest rates accounts for the movements of capital from one country to another if all the other factors remain the same.

The current analyses are not conclusive because we are living in a period of turmoil with so many things happening, and you never know exactly what was the effect of the interest rate.

I still would say that particularly with respect to the shortrun interest rate and the precarious balance-of-payments position, I think our freedom of action is somewhat limited in the monetary field.

This by no means comes to the conclusion that we have to depress the $550 billion economy in order to squeeze $3 billion more out that we need in additional net exports.

This would be, as you suggest, outright silly. I mean the economy is too big for that. But I think it does put a greater burden on fiscal policy for achieving what, under other conditions, we could do by a more equal consideration of fiscal and monetary policy.

Representative Reuss. Let me then address to you my second point, addressed particularly to your statement that if we have to yield a bit on demand-creating power, let us yield, you suggest, on monetary policy rather than on fiscal policy.

Dr. Colm. Short term.

Representative Reuss. Well, I do not know that you quite said short term. Let us assume for the purposes of this discussion that we are going to so skew our interest rate policies that that we are going to see that the maximum possible interest rate increase or lack of decrease is on the short side. Let us assume that.

But I gather you believe there is an even greater constraint in the monetary field than in the fiscal field. I am not trying to put words in your mouth.

Dr. Colm. I think that is true. I did no go into this in my statement, because monetary policies were supposed to be all settled this morning. I do feel we could go perhaps a little further in the operations of the Federal Reserve.

They have belatedly accepted the advice which you gave the Ways and Means Committee some time ago. But I think it could have been done a little bit more than by the present "nudging" operation. Certainly, I do not think this is the situation for an overall tight money policy.

Representative REUSS. My second question is this: Is it really valid—and here I am talking more about a political and psychological judgment than an economic judgment—that monetary ease is going to put us into greater balance-of-payments trouble than fiscal ease?

Let us look at the realities. Monetary ease, in the premises, can be applied by only one person, Mr. Martin, head of the Federal Reserve Board. Fiscal ease is mainly applied by the Congress, which is now under a Democratic majority.

Is it not part of the ideology or even the mythology of those European central bankers and financial men, who, by their ability to command gold, are the persons capable of putting us in real balance-of-payments difficulties, is it not part of their ideology or mythology, that what Mr. Martin does is likely to be sound and what the Democratic Congress does is likely to be unsound? Therefore, don't you have to give some psychological and political weight to the economic judgment you make, and may it not well be that there is no choice, really, in terms of the balance of payments, as between adequate fiscal policy and adequate monetary policy?

Dr. COLM. I do not think it is quite right that the monetary policy is entirely up to the Chairman of the Federal Reserve Board.

I think there has developed close cooperation between the Treasury and the Federal Reserve, and I do not think there is much difference of opinion at the present time.

I also think that the Federal Reserve has been somewhat responsive to suggestions coming from the President, quite contrary to previous experience.

Nevertheless, I do feel, as you say, that fiscal policy has greater leeway under present economic and fiscal conditions.

Representative REUSS. Mr. Keyserling, in the very short time that is left me, could you state the effect of your critical analysis of present growth policy in terms of what you would recommend for 1962 in the next fiscal year by way of fiscal and monetary policy?

You have said that you would not enact the 8-percent tax credit, for example. What additions to the spending side of the budget would you think are correct, and what greater monetary ease than at present would you think is indicated?

Mr. KEYSERLING. Well, first of all, I think that many economists in recent years have committed a great default in their degree of abandonment of quantitative interrelationship analysis. I think all of our economic problems are subject to examination and treatment in terms of how our resources are actually working and what their relationships are.

So my first basic concern is not that the Economic Reports arrive at a different policy result from what I arrive at, but rather that they, in terms of their own policy results, make no sufficient quantitative analysis of the economy in action to show why they get where they do on the policy front.

You get a feeling that somebody decided on some policies, and then somebody else writes some analyses, and then somebody puts both in the same book. I think, in answer to your question, that if one made this kind of quantitative analysis that I am talking about (as we did during wartime, as we do whenever we realize we are really put to it to use our real wealth as a nation), we would arrive at the conclusion (within wide bands) that the Congress ought to give greater consideration to the stimulation of ultimate demand and less consideration to bonanzas designed to provide direct stimuli to business investment, not on the ground that both investment ad ultimate demand are not important, but on the ground that this approach would provide better balance.

I think any comprehensive quantitative analysis would pull us in this direction. You ask what this would mean for specific policy.

I think it would mean, first, a complete abandonment of this 8-percent tax credit bonanza, and even if the Federal budget were now in the position where we wanted to forgo tax revenues, it would be much better to forgo them to stimulate low-income-family consumption, or to stimulate residential construction which relates so closely to the problems of compensating for the new technology and the national needs.

I can think of 10 ways, within the province of the Congress, to use this several billion dollars more effectively than the 8-percent tax credit, from the viewpoint of economic equilibrium and growth.

Quite aside from the 8-percent bonanza, I submit that we should provide far more stimuli to the expansion of ultimate demand, both private consumption and public outlays.

I think every quantitative economic analysis is pointing the needle to the American economy and the Congress that we have hardly commenced to respond to the magnitudes of the technological thrust.

We are in danger of being confronted with an even more gigantic idleness of plant and manpower within a few years. This is the worst recovery we have had since World War I in terms of how far it still leaves us from full employment, by far the worst, even without allowing for the peculiarities in the figures which show no growth in the labor force since a year ago.

Within a few years, unless we wake up and get moving, we will be threatened with 50-percent more idleness of plant and manpower than we now have.

Therefore, we need a tremendous expansion of consumption. It seems to me that it is in the discretion of the Congress and not for me to decide whether we want to take this out in more public spending, or whether we want to take it out in the right kind of tax reduction, or whether we want to take it out in a liberalized monetary policy. I feel sure we need all three of these approaches.

It appears that the CEA has given its set of quantified perspectives to Business Week. But why were these perspectives not contained in the reports under the Employment Act? This is part of the responsibility defined under the Employment Act. Then we would have an official qualification of needed goals and interrelationships. Then, as a matter of policy, the Congress would be able to decide on the basis of what are really the priorities of public policy.

I think Congressman Curtis is right, that we have many considerations beyond purely quantitative economic growth—whether a nation wants more defense, more schools, lower tax reductions on low-income families. But we should be enabled to make these choices within an environment of quantification which would enable us to do it sensibly rather than flying blind.

I have just one other comment on monetary and fiscal policy. I think the response of your earlier question, Congressman Reuss, is that the balance-of-payments problem has been misused to turn our economic policies upside down, just as the inflationary scare was used a few years ago.

Some economists and others are pontificating that the balance-of-payments problem imposes restrictions on this and that. But they have come forward with no satisfactory analysis of needed trade adjustments, of national economic quantifications.

I think Senator Proxmire has done a great job, although I do not agree with all of his conclusions. But he is correct in challenging some of these sanctimonious pronouncements that the old economic formulas are right just because the fellow next to him has uttered them.

I happen to think that you are utterly right, Congressman Reuss, more right than many of the economists, to the effect that whatever policies would increase the real wealth of the United States by maximizing our production and maximizing our employment, whatever policies would reduce real costs by using our resources more efficiently, would be the greatest step we could take to improve our balance-of-payments position, our competitive position overseas, and everything that goes with these objectives.

Instead of this, we are treated to a rationalization of avoidance of these problems, on the ground that we have a balance-of-payments problem. I wish there were time here for me to discuss this balance-of-payments problem more fully and analytically, as I have grave fears that we are letting it carry us far away from a correct or even safe course.

Representative REUSS (presiding). Senator Proxmire.

Dr. HAMBERG. I had in an appendix I put in after my paper was mimeographed some comments on the recent sources of slow economic growth. I would like to mention them briefly in connection with Congressman Reuss' question and Mr. Keyserling's reply.

It is my impression that we may be in, I think, the very real and present danger of having achieved stability at the expense of economic growth.

We have talked a great deal about the resiliency of the economy during contractions, particularly because of automatic stabilizers in the form of tax behavior, the larger than proportionate reduction in taxes, as income falls, holding up spending and so forth, as well as unemployment compensation.

I think what we fail to realize is that these automatic stabilizers work both ways. They not only stabilize contractions but they retard economic growth. I think in addition we have failed to realize that our progressive tax structure is such that we have taken increasingly large chunks of income out of the expenditure stream and so retarded growth.

On the other side of the budget picture, Federal spending particularly has remained more or less static, until very recently. That has stabilized greatly the downswings. But, again, in view of the big marginal tax bite during upswings, we have absorbed increases in income without offsetting increases in Government spending.

I think, therefore, we have one of the great retarding factors of our economic growth in this fiscal behavior.

If you ask why this did not show up in earlier periods, when we had the same kind of tax structure, say since 1945, my answer would be that in the past we had a combination of large increases in Federal spending at one time or another, and also big increases in investment spending that were related to the backlogs from the war and prewar years. Once these were overcome, these exogenous increases in spending, private and public, have not kept pace with the marginal tax bite that has actually grown larger over the years because of our progressive tax structure.

We have moved into higher and higher levels of tax brackets with a rise in the gross national product and income.

In recent years we have exhausted most of these backlogs in the private sector. Government spending has held more or less unchanged in the last 4 or 5 years. I am thinking of the period from 1957, for example. Meanwhile this tax bite keeps rising.

I am convinced that at this point we have to make a decision with regard to fiscal policy of either having rapid, large increases in Government spending or reducing taxes. Else we are inviting a heavy retarding force into the economy.

I, myself, have my own preferences. I think there is enough spending to be done in the public sector to warrant increases in Government spending to offset the greatly increased marginal tax bite. But that is neither here nor there.

The point is, to come back to our balance-of-payments and interest problem, if things remain fairly unchanged (and I think the Kennedy administration may be changing this) let us say, had remained status quo ante as of the spring or summer of 1961, let us say, the pressure was on to try to lower interest rates as an offset to the deflationary or retarding effects on the fiscal side.

On the other hand, if we had either, and this is a public judgment, a value judgment. if we had either the reduction in taxes to reduce the marginal tax bite or the increases in Government spending to offset the marginal tax bite, then I think the easy monetary policy, the efforts to reduce interest rates, could have been largely dispensed with.

That is, I am suggesting that if we had a more stimulating fiscal policy, whichever form it took, tax reductions or increases in spending, you would have a much more rapid rate of growth, and aggregate demand.

I think if we look at the behavior of certain components in the balance of payments, for example, we would find that perhaps without changing interest rates, the situation would improve.

For example, it occurs to me that when the present recovery took place in this country, a lot of funds that were leaving the U.S. stock market suddenly came back with a rush. I would suspect that less capital exports from the United States to abroad (private capital exports) would take place because with a higher rate of growth there would be more investment opportunities, and this balance-of-payments problem would be greatly reduced by a reversal in these movements of capital.

Representative REUSS. Thank you.

Mr. Proxmire.

Senator PROXMIRE. I would like to tell Dr. Colm that I was here this morning, I think practically all morning, but I missed the assertion by a member of the panel or of the committee downgrading the importance of growth.

I understood you to say at the end of your statement that there was some dispute on the importance of growth. It seemed to me there was none, none that I could catch. I would add to your notion of the importance of growth to taxes and revenue, its importance to employment, but especially to our very survival, growth is fundamentally important if we are going to have the military strength we will need in the future.

You characterized the budget as expansionary. On page 82, of the Joint Economic Report, there is a chart showing the national income accounts basis of the budget as it would be in fiscal 1963.

I take it, from the testimony we have had before, that this is a better measure of the administrative budget, of the impact of the Federal spending and taxing in the economy. If so, far from being expansionary, the budget would tend to contract the economy. It would run a surplus of about 2.5 billion in the first half of the fiscal year and in the last half over $6 billion, surplus that is, and unless you put very, very great weight, as was put this morning, but even greater weight perhaps than was put then, on the fact that we are spending more and taxing more, to draw your conclusions that this is expansionary, it would seem to me that this could be characterized as a budget which might be viewed as not expansionary, and in fact to be somewhat restraining.

Dr. COLM. Senator, my point that this budget is slightly expansionary was based on the expenditure developments.

To the extent that receipts increase because of higher tax rates, they are more restraining than increases which are the automatic result of rising incomes.

Senator PROXMIRE. Why would they be more restraining if they are the result of higher income, more taxes coming from higher incomes?

Dr. COLM. If our incomes increase, Senator; for example, somebody's income of $10,000 goes to $20,000, but he does not get the full $20,000 because he gets into a higher tax bracket and of the increase he gets only, let us say, $5,000. He is still $5,000 better off than before and can spend $5,000 more.

But if the increase in tax revenues is due to increased rates and he has only $10,000 but has to pay $1,000 more by taxes because rates have increased, then he has only $9,000 left for spending.

So all I am saying is that an increase in receipts due to increased incomes limits the increase in spending ability but does not reduce the spending ability. The increase in expenditures, as we professionally say, has a higher multiplier than the negative multiplier of the increase in tax receipts resulting from rising incomes.

Senator, you assumed that I thought that the national income sector account is a better measurement than the conventional budget. I agree. But I do not think it is a better measurement than what we call the consolidated cash budget.

I do not believe that the $4 billion surplus is really a good measurement of the effect of the budget because this concept excludes loans.

Senator PROXMIRE. On the other hand, if I can interrupt for a moment, isn't it also true that the income accounts budget does measure accruals which can have an immediate impact on the economy and perhaps an impact significant or more significant than when the money is actually spent, when the commitment is made, the men are hired, and so forth.

Dr. COLM. Absolutely right. In that respect, that concept is superior. But where I criticize the concept is as it is said in the budget document somewhere that loans do not directly affect incomes. That is literally true.

However, when the Small Business Administration, for example, gives a loan for financing a small business enterprise, so they can buy more equipment, of course that affects the economy almost exactly as if that had been an outright subsidy.

The Economic Report only says, "Let's consider the effects of loans in another chapter than the effects of expenditures." That is all right. But if you only analyze the budget in terms of the sector accounts, then you eliminate all loans. Transactions in existing assets should, of course, be eliminated in either case.

If the Government buys land, we have only a change in assets, making a change in the liquidity. But the effect of loans, in my opinion, is not so different from the effects of expenditures.

This is a rather technical thing. I am pretty much alone in the profession, I know. Since the sector account shows a bigger surplus, I think I have a hunch why it has become more popular in recent years. But on the merits of the thing, I think that loans should not be eliminated from the analysis of the budget.

Senator PROXMIRE. You seem to emphasize or you go along with the 4½-percent-a-year growth objective and seem to agree that this is highly approved, I understand.

Dr. COLM. Absolutely.

Senator PROXMIRE. In connection with that, I am looking in your paper and your presentation of how you go about achieving this. You seem to put so much emphasis on increasing the size of the budget, itself, rather than whether it is in balance or not.

That is, running a deficit you seem to feel is perhaps secondary as compared with increasing the size of the budget, or the activity of government.

I am wondering, since we have a much bigger budget now than we had in the 1920's, in relation to gross national product; is that correct?

Dr. HAMBERG. No, not that one.

Senator PROXMIRE. I am talking about the 1920's. There was a period in the war, of course, when we had a far bigger budget in relation to GNP.

Well, my point is this, in view of the fact that we had a smaller Federal budget in relation to GNP in the twenties, and the growth was about the same then as it has been on the average over the past 10 years, what confidence can we in Congress place in the notion that a simply expanded budget will have an expansionary effect on the economy?

Dr. COLM. The budget is now, I think, 18 percent of the gross national product. What I have in mind as long term does not necessarily mean an increase in the Federal budget.

Senator PROXMIRE. Let me interrupt at this point because I want to clarify what you mean by the budget. Transfer payments, it seems to me, have such an important effect, and if you include transfer payments they have increased so greatly in the last 10 years, and, of course, they did not have them, so to speak, in the 1920's——

Dr. COLM. That is included in the 18 percent.

Senator PROXMIRE. They are included?

Dr. COLM. Yes.

Senator PROXMIRE. It is my understanding transfer payments are about 6½ percent of GNP. Without transfer payments, the budget is about 15½ of GNP. If you included those it is closer to 22 percent.

Dr. COLM. I think it is probably close to 20 percent, but I never can remember figures too accurately. But, Senator, let me try to answer your question in very specific terms.

I think what is needed is the long-term assurance that we are making full use of available manpower and investment. One way of doing that is going ahead with those programs which are really of highest priority for the Nation. This is important in the international field and also very important in the domestic field.

I will give you one example. It has been estimated that if we do everything that needs to be done in urban renewal and rural renewal, that we would need to invest, by private and public funds, substantially more than a trillion dollars over a 15- or 20-year period.

According to estimates done by our staff, it might require additional expenditures for a longer period of about three and a half percent of the gross national product, in addition to what we are spending for those purposes now.

Most of that is private outlays, but the private outlays will not go ahead unless the Federal Government gives some leadership.

For instance, the Federal Government will authorize the establishment of metropolitan development authorities, doing something about the placement of bonds, which would then be self-financing through increased real estate taxes, through increased yields from mass transportation, and so on.

I am giving this as an example to illustrate that I think some long-range programs are needed which would not fully affect the Federal budget, though there might be some minor effect on it. Such a program would mainly operate through the combination of private expenditures and such semipublic expenditures as could properly be loan financed.

Senator PROXMIRE. It seems to me that there are certain things the Government can do that are essential for growth. Education is one very important element, at whatever level of government.

Research may be another one. But when you say that, while I agree on that I want to get at this concept with which the whole panel this morning seemed to agree, and perhaps the whole panel here would concur, and I just cannot find the facts to corroborate it, that a larger budget, per se, is favorable to growth, will promote growth.

What I referred to a moment ago in our discussion of the comparative size of the budget and GNP were Federal payments as a percentage of gross national product, and these include budget expenditures, in 1938 was 8.2 percent, the estimate for this year is about 20 percent, 19.8, the percentage of gross national product.

That is quite an enormous difference. All during the 1950's they varied from about 20.1 percent in 1952, down to about 18 percent in that period. It has not seemed to give us results.

Dr. HAMBERG. But, Senator, that is because of this point I raised earlier. It is only in recent years that it has not seemed to give these results. I would say that the reason is when we come out of these contractions we have such an enormous Federal tax bite, given the present structure, and the level of GNP that we are at now.

We are further up the tax structure in rate terms than we were in the past. On the other hand, since 1957 or so there has been very little change, until recently, in Government spending.

So this has been a terrific deflationary force on the economy. We have had huge tax bites diverting income from the expenditure stream, on the one hand, and no offsets in the form of incremental Government spending or some great burst of private spending, investment spending.

Senator PROXMIRE. It has been the general assumption that it was the deficit that seemed to help the economy expand. Economists take the position now that it does not matter whether we have a deficit or not. It is the growth of the budget.

Dr. HAMBERG. That is right.

Senator PROXMIRE. You are talking about the offsetting taxes?

Dr. HAMBERG. Here is a case in point, Senator: If a budget deficit were so stimulating, then a $12 billion deficit in 1959 would have given a great boost to the economy, and the deficit in the 1930's would have given a great boost to the economy. They did not. If deficits per se are stimulating, you cannot explain depressions or recessions in the presence of deficits.

Senator PROXMIRE. My argument is that I have to be shown, not I have to be convinced, that either a deficit or a big budget spending and taxing together is very expansionary. It may be, but I have not seen the statistics to show it.

Dr. HAMBERG. Here is the reasoning, Senator: An increase in taxes will have deflationary effects. It takes income out of circulation. An increase in Government spending has stimulating effects.

On most agreeable assumptions you can show that the deflationary effects from the increase in taxes, are smaller than the stimulating effects from the increase in Government spending.

If you increase both simultaneously, even in a balanced way, you will still get a net increase in total spending.

This is the argument. The details of the argument get a little involved. But that is essentially the argument.

Senator PROXMIRE. This is what happens. I see my time is up.

Did you want to make a comment?

Mr. KEYSERLING. I am surprised at some of the things that my colleagues seem to be saying, because I thought they had a strong commitment to modern fiscal policy. I agree that, if we have a balanced budget, it may be true that if the budget is 20 percent of the national economy it will stimulate growth more than if it is 18 percent on the ground that we are stabilizing a sector of the economy at 20 percent rather than 18. But to jump from this to the argument that, if the President increases the budget, taking an arbitrary figure, $3 billion above last year's budget and balances the budget, that this is as stimulatory as if he left the budget $3 billion lower and ran an $8 billion deficit, is, in my opinion, entirely wrong.

Dr. HAMBERG. No one said that.

Mr. KEYSERLING. I may have misunderstood the impact of some of the responses just made by my colleagues.

I think it is categorically true that, whether you do it by increased spending or by decreased taxes, a large budgetary deficit is stimulative to the economy. And when there is such tremendous slack of plant and manpower as we have now, I think this would be a highly desirable national policy, especially if we are going to continue to have a tight money policy. I do not think that economists should duck this issue or speak softly on it.

Senator PROXMIRE. Senator Pell?

Senator PELL. I apologize for not having been here for the full presentation. I was particularly interested in the discussion of the investments in and supports as opposed to GNP. Having followed this somewhat in the last few years, I wonder if we don't put too much emphasis on gross national product, as opposed to the importance of added investment, and from the viewpoint of the growth of the country, not the peoples' welfare but the growth of the country, the important thing is in net investments each year. I wonder if you might enlarge on that a little bit?

I have asked several times before if there is any way of seeing whether our rate of investment has gone up in the last 12 months or whether it is remaining static, and each time I am told that there is no way to determine that. Would you comment on that, too?

Dr. GOLDSMITH. In my statement, I tried to put the importance of investment for growth in reasonable context. I tried to show that while investment, either gross or net, is, particularly in the long run, one of the important factors of economic growth, it is by no means the end-all, since you cannot establish an easy and simple relationship between the volume of either gross or net investment and the rate of economic growth, particularly not if you deal in broad aggregates. It makes a great deal of difference what type of capital expenditures is involved.

Take another point which has been made. Possibly you can say that the most crucial part of investment is what we call producer durables, equipment rather than structures or inventories or net foreign balances. That part, it happens, has not declined in proportion of gross national product, if you go back to 1929, 1900, or 1880.

I would like to get across the idea that things are rarely what they seem, to use an old quotation. It isn't as simple as if once you put in a billion dollars more investment you get out a well-known increase in the rate of growth on which you can rely.

Senator PELL. But to answer the question specifically, and I have read your testimony, do you consider the rate of growth relatively more important or the rate of investments?

Dr. GOLDSMITH. The rate of growth, absolutely.

Senator PELL. You would consider that more important than the rate of investment?

Dr. GOLDSMITH. Yes. The rate of investment is one of the factors determining the rate of growth. There may be situations in which the rate of investment in brick and mortar is the most important single factor. Such periods have existed, and you can even find countries, in which it is free today. The rate of investment is only one of several factors of growth.

Senator PELL. The other question I had was, Has there been any change in the rate of investment over the past 12 months?

Dr. GOLDSMITH. Well, of course there has been.

Senator PELL. Would you have the statistics on that?

Dr. GOLDSMITH. The people whom you have before you must. The short-time analysts, to which I unfortunately do not belong, must have been able to answer that, beacuse there are quarterly figures on the rate of investment.

Dr. COLM. It is at page 248.

Dr. GOLDSMITH. That is correct. Then refer to business expenditures. You have seasonally adjusted rates and you have also the total gross private domestic investment, on page 107.

Dr. COLM. That is too much influence by inventories.

Dr. GOLDSMITH. There is elaborate literature on the cyclical relationship, I did not go into, on investment and changes in GNP. There is, of course, substantial correlation. Over the cycle, in periods in which the investment goes up considerably, there is also the tendency for GNP to go up considerably. I would be astonished if there hadn't been an increase in the rate of investment, compared to GNP, in the last couple of quarters, compared to the preceeding three or four quarters.

Senator PROXMIRE. Mr. Curtis.

Representative CURTIS. I am going to try to get back to this growth thing if I can. I am afraid I have been misunderstood. It seems to me that when we talk of growth in terms of GNP, we are talking about economic activity. Activity actually being nowhere, as in a war period, or at least with most of the activity wasted, does not go into capital investment. It does not make the country stronger afterward. It might, but I am referring to the actual end product. It seems to me that we have to go beyond economic activity, and the rate of change in that, in order to determine whether we have had meaningful growth. I don't know how to do it, but I cannot understand why, Dr. Goldsmith, you insist on a simple GNP indicator. In fact, I thought your paper was so good, in pointing out the necessity for breaking down this capital investment so we understood what we are talking about. It seemed to be related directly to what I have been trying to talk about, which is trying to determine what we are talking about when we say "economic activity." Is it really meaningful growth or is it just jumping up and down?

Dr. GOLDSMITH. In all the GNP figures we use, we have to accept the valuation of the market. I happen to feel—I hope none of the representatives of their industries resent it—that a lot of the expenditures on TV are waste, and possibly those on liquor. But this is my personal judgment. There are people who like TV a great deal and who like liquor a great deal, and are willing to pay for it.

Representative CURTIS. I can see that. I don't want to get into consumer choice, because I happen to have the same reaction, but I think it is a great system that permits these people to, in effect, cast their economic vote; I am talking about a real economic mistake. One that comes to my mind is when Russia invested heavily in building hydroelectric plants, only to find that they were so far away from the source of using the power they abandoned them to build steamplants. In fact, some they abandoned right in the middle. That is only an illustration. I am sure we have made some major economic mistakes. Or when we see the tearing up of some railroad tracks or streetcar tracks, it is not that a mistake necessarily has been made, but certainly we have shifted to the private automobiles. The net result to the society is in what kind of transportation they have. That is the economic growth. I think we have to subtract from that the actual obsolescence that has occurred. Those are the kinds of things I am thinking of, more than I am thinking of this consumers choice.

Dr. GOLDSMITH. This is quite correct. In principle, we make allowance in the depreciation that we allow for normal obsolescence and for the normal mistakes. We assume that capital investments will have a certain life. Sometimes we may overestimate it and sometimes underestimate it. There has been a good deal of technical discussion on how you best handle this problem, and whether you should make separate allowances for unanticipated changes that result in capital losses. In principle, however, if the depreciation allowances are set right so that they include the correct amount of obsolescence, this is taken care of.

You also raise another question about production during war. This again depends on what sort of general concept of output you want to use. There are people, Professor Kuznets has been one of them at some time, who regarded those as unproducts, to use an Orwellian term. I don't happen to agree with that. You can make a philosophical argument that if we had not produced these armaments we would not have survived the war. Secondly, you can say that military expenditures are paid for exactly the same way as the police. You here get into an argument about value judgments.

Representative CURTIS. I think we have to. I think any attempt to avoid it is wrong. Let me get back to one thing because you hit on a subject that I have done some work in, and this is the depreciation schedule. Ways and Means has been wrestling with that for years. The point I have been trying to drive home is that we never have updated our tax schedules to the economic fact of obsolescence. Our schedules are largely based upon when equipment wears out. Some equipment in this rapidly moving technological economy, this I think is real growth, will wear out in a year or 2 years, which have an actual life of 15 or 20. Those are the very indicators to me that far from a stagnant economy or one that is not growing rapidly show us that we are dealing with a rapidly growing economy which gross national product is not showing to us.

Dr. HAMBERG. But unemployment is, Mr. Curtis.

Representative CURTIS. Unemployment is, too, I will tell you, yes, because where is it? In the unskilled, semiskilled, high school dropouts, and rapid technological advancement cutting down on the jobs that unskilled and semiskilled labor can use. The other area you find it in is obsolete skills.

Dr. HAMBERG. Do you think things have suddenly changed so radically between 1950 and 1960 as regards these skills, or 1955?

Representative CURTIS. Yes. I think your rate has increased considerably.

Dr. HAMBERG. The rate of what?

Representative CURTIS. The rate of innovation, the rate of new goods, new services, new techniques.

Dr. HAMBERG. Do you think in 3 years or so this thing is of such magnitude as to explain all this unemployment?

Representative CURTIS. Yes, and I think I can prove it to you by calling to your attention the rapid suburbanization that has gone on, the influx, and this has all occurred in the past 10 years, which has meant so much in the area of communications and transportation and power. Yes, I think you can just look around and see how this whole society is being changed in that regard.

Mr. KEYSERLING. I think we have a problem of definition here, and I am less inclined to argue with you than to say that you have raised a real question. But I think it can be clarified by definition. First of all, the difference between the increase in investment and the increase in national product is really very simple. Investment is not something that has any value in itself. In other words, factories have no value in themselves. You could put 100 percent of your annual effort into the building of factories. Factories are designed to produce something that is used. Therefore, the factories are one measure of our ability to produce. The gross national product is a measure of what we are actually producing, or turning out for use. Use alone is ultimately significant. This is, of course, subject to the observation that our gross national product may be divided into components that subjectively many people may think have less value than others. We may be producing too much tinsel and not producing enough defense, and this, too, is a matter of national policy, to try to identify priorities.

There is another basic distinction between investment and national product. If investments are rising and national product is not rising correspondingly, you may, for a time, be increasing your power to produce. But the inevitable consequence, under our kind of system, of having investment rising and GNP not rising corespondingly, is that there will be very sharp cutbacks in investment, because nobody is going to keep on investing when the can't dispose of the product. The point I am making is that, unless we have an equilibrium relationship between our gross national product and our investment, we are not going to get the steady and strong growth in investment which is a strong source of our power to produce. This is exactly what has happened during the past 9 years. We have had too low a level of investment in the long run, but we have had this not because of lack of finance, not because of unsatisfactory tax treatment, not because businessmen haven't initiative, but because as prudent business managers, when they are in oversupply, they cut back.

Representative CURTIS. I have been very much impressed with some of the panels' papers which point out, though, that capital investments can and have become more efficient. I particularly see it when, as they call it, we put money in for structure, which is power, communications, and transportation. I would add a third thing, the general education of the public. Let's take the productivity of a doctor. The fact that people know more about health themselves means that the mother can call up the doctor and in 2 minutes find out what to do about the child, and the doctor, in turn, can use the highways and so can the patient, and so on. So as a result of all of this, we have a tremendous increase in productivity. I am sure that the same thing applies to our manual sector. I am just pointing to one area. But it does seem to me quite logical that capital investment should become more efficient when worker productivity increases. I can follow some of that argument and I think there is a lot of merit to it. Incidentally, my time is up but I did want to say it is most unusual to find myself on the same conclusions in some of your points, Dr. Keyserling, particularly on this so-called 8 percent.

Mr. KEYSERLING. I think you have been on my side all along. I just haven't expressed myself clearly enough for you to realize it.

Representative CURTIS. No; I am afraid we are in fundamental disagreement on important factors. But at least as far as some immediate legislation is concerned, we are on the same side.

Thank you.

Senator PROXMIRE. Before I continue my questioning, I would like to ask the panel if they know of any study at all, apropos of Mr. Hamberg's reaction to Congressman Curtis' question, any study which shows that there is a substantially more rapid technological change or automation in the last 2 or 3 years than there was before? I would like to say that there is at least the token study, a very limited study, on the other side saying there wasn't a change, and the study made by the staff of this committee showing that there hasn't been a rapid change. Do you know of any study which would show the contrary?

Dr. HAMBERG. No; I think that is the most amazing thing about the so-called technological revolution, that it doesn't show it up at all in the productivity today.

Dr. GOLDSMITH. The most amazing thing about economic research is that we haven't had a large-scale study about the cause or the causes of productivity in the last 10 or 20 years.

Dr. HAMBERG. I think——

Senator PROXMIRE. Now let me go ahead with Dr. Colm.

You said you wanted to comment. I would like to ask you briefly to comment for the record, Dr. Colm, on the Kuznet study. I was interested in that. That has been quoted a great deal in the Wall Street Journal and a number of others and other sources, quoting it as an indication as to the efficiency of investment. I noticed that you seemed to challenge the conclusion of the Kuznet study. There are certain factors that have been presented to a subcommittee of this committee that seemed quite persuasive. One is that profits have dropped sharply in relationship to gross national product, compared to wages and other factors.

Dr. HAMBERG. Over what period?

Senator PROXMIRE. Over the past 30 years, the past 60 years, and the past 16 years, is that correct?

Dr. HAMBERG. Slight, maybe.

Senator PROXMIRE. Well, the drop is in the order of a drop—I am trying to get the precise figures of about one-half of what they were as a percentage of the gross national product.

Dr. GOLDSMITH. For self-employment to employment in factories, this would also show as a statistic in decline in profits. One must not take these figures at their face value but you must go behind them.

Senator PROXMIRE. That is a good explanation. I am not saying that there isn't an explanation for it. I am saying that this has been offered.

Dr. HAMBERG. It is a statistical illusion.

Dr. GOLDSMITH. A statistical shift that has no intrinsic meaning. Before you say anything, you must adjust for shifts.

Senator PROXMIRE. Well, that is right, but it seems to me that the burden of proof is on you gentlemen who say this had no meaning. The statistics are there, and if you are going to say they have no meaning, it seems to me they would take some kind of substantial study to show why they have no meaning, why there has been this shift.

Dr. HAMBERG. There has been such a study, by a fellow named Budd, formerly at Yale, now at Penn State, who has done a long-term study of income shares. Allowing for all these shifts within the economy, it does come out with a very slight downward trend or decline, anyway, a very slight decline, in the profit shares, but hardly nothing like the magnitude of 50 percent or anything near that.

Senator PROXMIRE. Doesn't this depend on a judgment on his part?

Dr. HAMBERG. He made certain adjustments for the kind of things that Dr. Goldsmith was talking about. For example, the way we keep the accounts in the Government sector, the value of Government production equals Government wages; there is no capital in the Government sector on the basis of our present accounting setup. If the Government product rises as a proportion of the gross national product, then you have a big increase in the wage shares. But it is strictly an illusion because of the way we treat the Government product account versus the private sector accounts where we have other payments. Similarly with agriculture, or any other line of self-employment. If a man moves from self-employment, you would normally count all his earnings under self-employment as a kind of profit, but we noted for years before we made any adjustments that you should allow for a wage share in this income. If you make these kinds of adjustments, then you find the so-called rise in the share of the compensation of employees in the GNP accounts is a statistical illusion. If you adjust it for these shifts, you get a negligible rise.

Senator PROXMIRE. It strikes me this adjustment would be exceedingly difficult.

Dr. HAMBERG. Yes. You have to make certain assumptions and guesses and so forth. But the guesses are very reasonable, and the adjusted figures are much more accurate than the unadjusted ones.

Senator PROXMIRE. What you are saying is that before, when there was much more self-employment, that the so-called profits were really kind of a wage compensation.

Dr. HAMBERG. Exactly, and if you break down that so-called profiting income into its shares, and then carry these up to the present, you find that the labor share, as opposed to the compensation of employees in the GNP accounts, hasn't risen very much.

Senator PROXMIRE. Dr. Colm, do you want to comment?

Thank you very much, I appreciate that.

Dr. COLM. I agree entirely with this, and I think one could say that over the long-term trend, after all statistical adjustments have been made, there is a very slight increase in the ratio wages and salaries and a very slight decline in the ratio of profits. However, if we think of funds available for financing investments, we also have to consider depreciation allowances, which have been rising over the same period so that the funds available for investment had not declined. Furthermore, since we are talking about Kuznets, contrary to what was reported in the papers, he has really not dealt with that problem directly in his book. He only raises that question at the end of the book. He said he had an "impression," that there is a ceiling for growth from the saving side. He makes that statement in order to suggest a study which he had not done in his book. So I don't think that really Kuznets should be quoted as an authority for saying that saving is the really limiting factor.

However, Senator, we are talking about the future, and I would say, as I said before, there is some need to increase the ratio of capital investments to gross national product. It is entirely possible that the saving to finance such additional investments will be generated by the process, itself. We know if there are ample markets, more sales, more profits, and more depreciation allowances, more funds accrue. It might be possible that at some future time we may run into a scarcity of saving. I admit to an agnostic position on that on the basis of what studies I could make. Here I am talking about something in the distant future, after we have reached full employment, after investments have gone up relative to that higher level of activity. I only say, Senator, that I don't see in the present situation any indication which would suggest, that there is a basis for recommending to Congress that measures be adopted to stimulate saving in contrast to other disposals of incomes. I am personally in favor of high savings. I am glad that households have the opportunity to put more aside, and I am glad that the welfare and pension funds are investing more and more. I also favor the revision of income taxes because I think some of these 91-percent rates are provocative. They don't mean a thing. They make everybody mad and are used for purposes of speeches, but they are not used for actual tax collections, except by some people who do not employ the right tax lawyers. But I do not believe that we should rearrange our taxes for the purpose of stimulating more savings at this time.

Senator PROXMIRE. Dr. Goldsmith, how did you compute this chart? I think it is a fascinating chart and it is most instructive. You have this as a percent, the share of gross capital formation as a percentage of gross national product. Why should there be such a difference when it is deflated, or is there much difference?

Dr. GOLDSMITH. Yes, there is a considerable difference. This results from the fact——

Senator PROXMIRE. They are percentages and they are both the same, one being 1929 prices and one the current prices?

Dr. GOLDSMITH. Yes, sir. The numerator and denominator are both in the same prices, in one case present and the other 1929 prices. In the usual indices which we have to apply, the price of capital gains have gone up more than the price of consumption goods, which of course, constitute four-fifths of the gross national products. This has meant that the ratio of capital formation to gross national product has declined more, if you take the 1929 prices, than it has in current prices. In a ratio like this, I think current prices are more relevant, and they are particularly more relevant if you look at the whole problem as one of resource allocation. If you ask the question in the form of which part of the resources of any 1 year is set aside and devoted not to current consumption but to capital formation, then I feel the ratio which uses current values both for the numerator and the denominator is the more relevant one.

Dr. COLM. May I add a footnote to this? There is one additional reason why it is better to compute the ratio in current prices rather than in inflated prices. In the whole area of capital goods, particularly construction of plants but also machinery and equipment, we really don't have any good price index. I have great doubts in the validity of the price indices that are actually used for that area.

Dr. GOLDSMITH. I quite agree. I have the impression that we overstate the relative increase in capital gains prices, and there may not have been this shift. So even if we look at it from the output side, for which theoretically the deflated figure is appropriate, we might not get as sharp a decline as we get if we use the present statistics.

Senator PROXMIRE. I have one more brief question. Why do you include consumer durables as a more significant measure? It would seem to me on the contrary that the net capital information, excluding consumer durables, makes more sense, because this as I understand it, is the increase in the capacity of the economy that enables it to grow, that increases its growth potential. Is that correct?

Dr. GOLDSMITH. That is entirely correct. You can take a consistent position by saying that what you want to measure is the addition to the stock of tangible assets which, in the future, gives off services. Then, of course, you must include consumer durables. Many people do not ride the railroad anymore but use their personal car. Why should I include the railroad coaches in capital formation but not the cars which substitute for the coaches? A good deal of consumer durables perform exactly the same function as producer durables. Moreover, what we call the nonconsumer durables includes a great deal the productivity, of which is very doubtful. They include Coney Island.

Senator PROXMIRE. Coney Island is included how?

Dr. GOLDSMITH. The big wheel at Coney Island is in plant and equipment.

Senator PROXMIRE. I can see these rare exceptions, but it would seem to me that fundamentally the more desirable and useful measure of the potentiality of the economy would be in our investment in net capital formation exclusive of consumer goods.

Dr. GOLDSMITH. I think you might construct some such concept. For instance, the present figures include homes. Why should they be included but the automobiles, refrigerators and so forth excluded? You finally get to a very technological concept, and it is really difficult to see where you stop and where you draw the dividing line. I think a clear dividing line can be drawn between commodities that give off all their services in the period of account, and you think do not.

Senator PROXMIRE. You see, what I am driving at is that there is sort of a moral or puritan feeling on the part of many Americans and there is also a good solid military feeling as we look at the Soviet Union, which is concentrating an enormous amount of its production into net capital formation, exclusive of consumer durables, and, therefore, is forcing its rate of growth and is challenging us. There is a feeling that perhaps we ought to be doing something of the kind so that our capacity to stay ahead of the Soviet Union potentially can continue. Why do you shake your head?

Dr. GOLDSMITH. That is a value judgment. If you want to adapt yourself to the garrison state and the electorate so votes, that is one thing.

Senator PROXMIRE. No, no. I am here as a Senator and I am concerned with policies, as a U.S. Senator, with defense. We have to make valued judgments. That is our job. I am not talking about a garrison state, I want to keep this from a garrison state.

Dr. GOLDSMITH. If you feel you have to spend more on defense, by all means——

Senator PROXMIRE. I am not talking about defense. I am talking about our steel capacity. I am talking about our capacity in all the indices that contribute to our defense, shipbuilding, aircraft building, the electronics industry, the missile capacity and so forth.

Mr. KEYSERLING. I think that the ratios of capital expenditures to GNP in the underdeveloped or lesser developed countries, such as the Soviet Union, are being completely misused for purposes of interpretation here in the United States. Let's illustrate, and I will take purely illustrative figures that make the point whether these figures are right or not. Let us suppose that the Soviet Union is putting 40 percent of its gross national product into what you call fundamental capital investment. They are still challenged with and solving the problem of utilizing the product turned out by that 40-percent ratio. In other words, they wouldn't continue putting 40 percent of their GUNP into capital equipment if 10 percent or 15 percent of the capital equipment that they created remained idle. This is just waste, under any kind of economic system. So they are meeting this problem of equilibrium and full employment, in that they are maintaining a ratio between their capital investment and other utilizations which maintains their economy in balance. But the U.S. economy is not in the same stance as the Russian economy. We have not been, as the Russians have been for many years, undergoing a rapid transformation from an agrarian economy to an industrial economy. What would happen if we put 40 percent of our GNP into capital investment? We would find, instead of 10 percent of our economy remaining idle, 40 or 50 percent remaining idle. In other words, we have to get a ratio of capital investment to ultimate take which maintains the economy in balance. We seem to have been getting, during the past boom periods, a ratio of investment too high, as made obvious by the chronically increasing idleness of plant and manpower. You don't answer this problem by saying that we would be stronger if we had more capital investment.

Senator PROXMIRE. Just to reply briefly to that point, or go on briefly from that point. My position is that as we increase our capacity to produce the weapons of defense, whether we use them fully and produce the steel we need for automobiles, the homes, the highways, and so forth, we should use them as fully as possible—I agree it is a waste if we assume there is not going to be a terrific necessity suddenly to find ourselves—as we increase this capacity, it seems to me we do continue to maintain the advantage we have over the Soviet Union, which is, I think, the most significant advantage or one of the most significant advantages, which is that we have a more powerful, productive economic system. The reason we won World War II as early as we did, as decisively as we did, was that we were the industrial arsenal of democracy. We were able to produce a vast amount of planes, the tremendous number of ships, and so forth, so quickly. Having this capital ability to do this, because of capital investment, is a military asset and shouldn't be undervalued, although I can go along all the way with you on your assertion that we have to think in terms of our using the investment that we make.

Mr. KEYSERLING. I am willing to go along with you that, in the face of the world situation, let's say it would be a national asset to have even more steel capacity and even more chemical capacity, even if it isn't being used. Let's admit that for the purposes of the discussion, though I think full use would be still better. I still have the question that, unless we are going to create the kind of a society where the government arbitrarily and through increasing the Federal budget to $200 billion a year (which wouldn't be as much as we did during World War II on a price adjusted basis), unless we have a society where the government built and owned more and more plants, we have the practical problem of how are we going to get this increased steel capacity and this increased chemical capacity and this increased oil capacity unless the market economy provides the markets which induce expansion.

Senator PROXMIRE. I will not argue that. I think that is right.

Dr. GOLDSMITH. I happen to have worked at the War Production Board during World War II and to have made the same argument then. I once even published an article in a military journal which made exactly that argument. But from what little I know, it is a completely different situation now. Everybody now says—the military people—that the next war will be fought with the equipment on hand the first day. It is an antiquated notion, it seems to me, that after the war has started, you can start up and convert. I used to say before World War II, that one of our great military assets was the automobile industry because this was an immense convertible resource. You could go along for years using it not for what it was originally built, but using it for military production. That turned out to be correct. This, from all I know and all I read, is not any more the case. This argument, I think, is World War II and not world war III.

Senator PROXMIRE. Dr. Goldsmith, you shared this viewpoint earlier. Let me tell you that I think all we can say about the future is we don't know, we can't predict. We may, conceivably, as the President has indicated, as our shift in military spending has indicated, have a series of so-called conventional, and perhaps not. It seems unlikely. I will agree. But it certainly isn't impossible. It is conceivable that we might have a great and substantial need for more of this industrial capacity for military reasons. I think it is unlikely. I would share that, of course, if we assume that we are going to have a doomsday, there is almost nothing we can do about it, I suppose?

Dr. GOLDSMITH. I would agree that if you feel you need more military equipment, by all means step up the budget for them and build the plants for them. Certainly, that is a military and political judgment. All I want to say is that this has very little to do with what we have been discussing here.

Senator PROXMIRE. Let me get back to your statement as quickly as possible. I won't detain you gentlemen much longer. You have been very, very patient. This is the longest session we have had and we have some long ones. In your statement about the need for securing statistical information, I am chairman of the Subcommittee on Statistics of this committee, and I am extremely interested in that. I would like to learn from you how we could get this information as cheaply or I should say at lowest cost possible, information that is most immediately appropriate and pertinent. Say, for example, the relationship to the investment tax credit. If you could let us know about this, I think we might be able to secure the funds we need to make the statistical studies as rapidly as possible. As you know, these funds are very limited. We have been increasing our statistical program a great deal and we are way ahead of any other country, statistically. At least that is what we are told.

Dr. GOLDSMITH. There has been some discussion about this within the Government and also outside of it. The preliminary conclusion is, as I indicated in the text, that it is so complicated a problem that we need sort of an intermediate stage where you have a relatively small group working out the full plan. If the committee is interested I shall be very glad to give you some of the documents that have been prepared in that line. We now feel that we cannot immediately work out an operational plan, but we need about a year of serious and hard work, with the help of committees and so forth, to do so. However, we haven't yet managed to get the money. It is a relatively small amount of money, say $50,000 to $100,000, that is required for this exploratory phase, compared to the money needed for actually doing the larger job.

Senator PROXMIRE. I have one final question and I will address this to Mr. Keyserling.

Did I understand you to say that investments, per se, has no, underlining "no," emphatically no, relationship to growth?

Mr. KEYSERLING. I didn't say that at all.

Senator PROXMIRE. That more investments relative to consumption is meaningless?

Mr. KEYSERLING. No.

Senator PROXMIRE. I jotted this down as you were speaking. I tried to get it accurately.

Mr. KEYSERLING. No, sir, what I said was that it was palpably obvious that, everything else being equal, if 40 percent of your economy went into investment, we would get more of a potential for growth than if 20 percent went into investment, for the very simple reason that investment creates technology. But everything else is not equal. The additional factor is that, by the same token, we might say that if 100 percent of your economy went into investment, we would be still better off. Therefore, we get back to the question of what is the highest sustainable ratio of investment to consumption, to provide continuing motivation for investment in a rational, mixed economy like the American economy.

In short, my position is that, for the last 9 years as a whole, the absolute level of investment has been far too low. In fact, I compute that there has been a deficit of about $10 billion a year. But investment has been too low not because we didn't have tax incentives, not because we didn't have borrowable funds, not because the companies didn't have the means of investing, but because in the boom periods they overexpanded relative to ultimate take, and then, as they saw their excess capacities rising, they cut back sharply on investment. Therefore, the way to get, during the next 5 years, a higher growth in investment than we have had, more expansion of capital equipment, a more rapid expansion of technology, is to provide reasonable use through economic equilibrium. I say all the impirical evidence indicates that such economic equilibrium would yield a 5-percent growth rate, including roughly a 5-percent growth rate in investments.

If we want to go on from there to say that we are in the kind of a world situation where we need a 9-percent economic growth rate, under forced draft, as we had during the war, then we would have to adopt an entirely new complex of policies. I am not against investment. I am merely saying that, as we see that the inhibiting factor on investment has been the repeated shortfalls in the markets for the products of investment, we can't help the investor by giving him more bonanzas to indulge in repeated hectic booms which lead to overcapacity. Instead, we must promote the adequate demand for products which will keep the economy in balance. I say we have a problem of economic equilibrium.

Whether this ultimate demand should be more guns or more butter, more space exploration or more schools, or how much more of all of these things, is an entirely separate question of our national values and priorities.

Senator PROXMIRE. I do have one further question, if you don't mind, on a subject which developed this morning.

This is an immediate policy question. The investment credit proposal, it seems to me, has equity consequences which are significant. It was denied by Mr. Bernstein that they are significant, but I think there is some significance.

In other words, if we pass the investment credit, we tend to provide a reduction in taxes for investors who have large incomes anyway, and to distort the equity aspects.

On the other hand, I said this was a package offered by the President, and he proposed the investment credit together with the elimination of the dividend credit.

Would you say that this is a fair balance? I know you oppose the investment credit, but would you say that in terms of equity that this is seemingly a fairly rough balance?

Mr. KEYSERLING. No, I do not think so at all. I do not think so at all. Furthermore, I think I can answer this in 1 minute.

The genius of the American economy, as a highly productive economy, is that equity and economic sense come very close to each other. In other words, it is really true, because we are such a productive economy, that what is good for most of the people is good for everybody, as against an underdeveloped economy where you have to severely repress consumption to stimulate investment, like India and some other economies. Therefore, this tax credit proposal is way off balance, because it squanders several billion dollars of tax revenues which could be applied immensely more effectively at other points in the economy.

Therefore, it is not only inequitable but economically undesirable.

Senator PROXMIRE. I was not arguing about the merits of it. I am generally opposed to the idea. But I was wondering about the equity balance.

I can see that it tends to take something away from the investor and gives something to him, too.

Do you want to comment?

Dr. COLM. I do not want to join the argument, but I only want to say that you should not assume that if the rest of us are silent that we agree with the last remark Mr. Keyserling made.

I think in every incentive factor is an element of inequity. We always, in a growing economy, have to balance some inequities with the benefits which are expected as result of the incentive.

The question is, Is it worth what you are accomplishing? Therefore, I do not think the equity question can be entirely disassociated from the question whether there is need, whether there is some usefulness in the device.

Recognizing inequities and recognizing the purpose for which the device is proposed, I just come out on the other side, without denying the correctness of the argument. I am weighing how strong one is against the other.

Mr. KEYSERLING. I also said it was not merely a matter of individual equities; what is good for the whole economy is the supreme equity, so to speak.

I do not fully understand what you say, Dr. Colm, because you said earlier that you had very strong reservations as to whether this tax credit proposal was desirable unless we did a variety of other things to maintain economic equilibrium.

I do not want to press you in any way, but do you think that the net balance of the steps that are being taken to expand ultimate demand through the budget and otherwise are adequate as against either the current situation or the increased effect which this tax concession might have upon business investments?

Would you, yourself, arrive at these same conclusions?

Dr. COLM. If I may answer Mr. Keyserling's question, my answer is that it is a matter of the tense that you are using. When you ask are such measures now being taken, that means already underway, then my answer is unfortunately, "No." But I thought this hearing has the purpose of discussing to get some guidance or some help for the committee's recommendations for future policy.

All I am saying is if the committee recommends that there should be the appropriate monetary and fiscal policy and so on, then I also think the committee should recommend this investment tax credit.

Mr. KEYSERLING. Well, I do not object to that. In other words, if Dr. Colm made his own tableau of the kind of budget policy he thought would be desirable as a counterpart to this stimulus to business investment, I think he and I would agree 100 percent. But I think that this would be so different from the current budget policy that he would reach with me the conclusions that, assuming the current budget policy, or an even tighter one, this tax investment credit would throw things further out of balance.

I do not think Dr. Colm and I are really in disagreement.

Senator PROXMIRE. I want to conclude now not by asking a question but by putting into the record something I would like to call to Mr. Colm's attention, page 44 of the Federal Reserve Bulletin for January. It shows that the free reserves may be something of an illusion. The latest figures show that the Central Reserve Bank, New York, $65 million minus free reserves; Chicago $1 million plus free reserves; reserve of city banks, minus 27, and only the country banks with free reserves of $434 million.

All of it is in the country banks. As I understand it, the Government fund, the Federal fund, in which banks can invest from reserves, is a very imperfect instrument, particularly for country banks.

It requires small banks to make long-distance phone calls for small temporary investments. There are many reasons why they do not take advantage of it. Also, it is a matter now of counting vault cash.

So when we put all of these things together, we can see the notion that we are maintaining easy credit because of an appearance of free reserves is subject to this kind of valuation.

Dr. COLM. I entirely agree with that. One should not take the aggregate but should separate the country banks and the city banks.

Senator PROXMIRE. I want to thank you gentlemen again very, very much. We have detained you much too long.

The committee will meet tomorrow at 10 o'clock.

(Whereupon, at 5:30 p.m., the joint committee recessed, to reconvene at 10 a.m., Tuesday, February 6, 1962.)

JANUARY 1962 ECONOMIC REPORT OF THE PRESIDENT

TUESDAY, FEBRUARY 6, 1962

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

The Joint Economic Committee met, pursuant to recess in room P-63, the Capitol, Representative Wright Patman (chairman of the committee) presiding.

Present: Representative Patman; Senators Douglas, Proxmire, Bush, and Javits; Representatives Reuss and Griffiths.

Chairman PATMAN. The committee will please come to order.

This morning we will hear two distinguished economists discuss the Economic Report of the President.

Prof. Theodore W. Schultz, of the University of Chicago, was to be the third man on the panel this morning, but unfortunately Professor Schultz reports that he is ill and cannot be with us.

We have Prof. Alvin H. Hansen, who hardly needs any introduction—Professor Emeritus at Harvard University and now visiting professor at Yale.

We also have another distinguished Yale professor, Prof. Henry C. Wallich, whom we have had the pleasure of hearing several times before. Professor Wallich was a member of President Eisenhower's Council of Economic Advisers.

Suppose you go first, Professor Hansen, and after you have concluded, the committee will ask you questions.

STATEMENT OF PROF. ALVIN H. HANSEN, PROFESSOR OF ECONOMICS, YALE UNIVERSITY

Dr. HANSEN. Mr. Chairman, my remarks will be brief.

First, with respect to the antirecession measures, I shall concern myself here only with one of these—the anticyclical adjustment of the income tax rate. I heartily approve the proposal to grant the President standby authority to cut the rates. Indeed, I should like to go further.

I should like to incorporate into our built-in stabilizers a system of formula flexibility under which income tax rates would automatically be adjusted to offset the cycle. The President should, however, have the power to veto such automatic adjustments if in his judgment and that of his advisers, special circumstances so warrant. As is well known, this procedure has long been advocated by many economists.

But now I come to the essence of what I wish to say. We need not wait for the President's legislative innovation, which I fear may be coming only after prolonged discussion and debate. We are not entirely helpless in this matter, even without any new legislation. In all recent recessions we began to talk about a tax cut after we were already well into the recession. And it always ended up in mere talk. We have never developed a program.

I should like to urge upon the Joint Economic Committee a report expressing firm approval of an antirecession tax cut as a regular procedure. This would, it seems to me, be a significant forward step.

Three things are needed by way of preparation. First an announcement by the President at an early date that he intends, at the first sign of next recession, to ask Congress to enact a temporary tax cut.

It should be understood that the request is not a special case. It should be made quite clear that the administration has adopted this device as regular procedure, so that the country would come to look upon a cyclical tax adjustment as a normal process, just as we have long been accustomed to accept cyclical adjustments of monetary ease and restraint.

Secondly, we need a careful study, designed to reach a firm consensus on the precise point of time in the cycle when the tax reduction ought to go into effect. If time is wasted on debating the appropriate time of action, it may well be too late. A certain degree of quasi-automaticity could be achieved if general prior agreement could be reached on the matter of timing.

Thirdly, we need to reach a firm prior consensus on the amount of the tax cut. Should it be the full 5 percentage points? My answer would be "Yes." For a temporary tax cut covering only 6 months, I doubt that this would be excessive, but this is a matter that requires further study.

I come now to the second section of my comments, the matter of growth projections, based on (*a*) growth in the labor force and (*b*) the rate of productivity increase. I heartily welcome the section in the Council's report which gives us a full employment projection of GNP for the year 1963. I should like to see in future reports an extension to include perhaps 4 years. To be sure, the further one peers into the future the less dependable the projection becomes. But such projections are nonetheless useful, and they should be revised from year to year. Such projections, imperfect though they be, can help very much to gain perspective, to see where we have been, where we are, and where we are tending in relation to the required rate of growth needed to insure full employment. Such projections serve as guideposts from which to measure current performance. With this measuring rod before us, we can begin to think dynamically about the economy. Without it, we are likely to take a static view—a view which makes us satisfied if we merely equal past performances.

We are always noting "records," so-called, in terms of previous peaks. Yet in a growing, dynamic economy such records are quite meaningless. Holding a static view of the economy we persistently misjudge the flow of events. The fiscal 1963 budget, for example, is said to set a record of spending unprecedented in history. Yet, in fact, in any meaningful sense, it sets no record at all. As a percent of the relevant GNP—and I have taken there a conservative estimate as I read the business forecasters—the 1963 budget is smaller than the Eisenhower budget of 1955. The figures are as follows: 15.9 percent for the 1963 budget, against 16.9 for the 1955 budget.

Budgetary restraint in the years following the 1955 budget was partly responsible for the increasing slack from 1956 on. Had the Federal outlays on goods and services, in real terms, increased proportionally as much as State and local outlays from 1955 to 1960, Federal purchases would have stood $16.7 billion above the level actually reached. Equally disappointing is the record of private investment. Had private investment increased in proportion to the potential full employment growth curve, capital outlays would have stood at $88.8 billion in 1960, or $16 billion more than the $72.7 billion actually achieved. From a static point of view, both private investment and Federal outlays in goods and services seem large. From a dynamic point of view, their contribution to growth was seriously inadequate.

It has sometimes been suggested that we overestimate the slack in our system by including in the labor force groups that are really unemployable. This touches closely on the question of structural unemployment. The structurally unemployed are workers who live in ghost towns, workers who have been squeezed out by automation. It includes those who have no skills, teenagers who have no work experience, et cetera. And I could add on considerably in this category.

All these, it is said, are not really a part of the labor force, and when we include them we exaggerate the slack in the economy. Before we fix upon on employment goal consistent with price stability and international balance, the structural unemployed and the unemployables should, according to this line of reasoning, be segregated out first.

On this matter I agree with the investigations of the Council and the staff report of the Joint Economic Committee that the forces making for structural unemployment have not changed substantially since 1957, and that much of what is now regarded as structural unemployment would quickly vanish once job opportunities become more plentiful. Yet it must be recognized that the factors that cause structural unemployment are constantly at work. And if aggregate demand is deficient over a prolonged period, structural unemployment accumulates. It accumulated during the great depression, when it was widely believed that a very large part of the unemployed were in fact unemployable. The war, however, proved this not to be the case.

Western Europe has relatively little structural unemployment. The reason is twofold: (1) Job opportunities are plentiful, and (2) structural unemployment is continually being weeded out by means of well organized and continually operating programs of retraining and relocation. This is especially true in England and the Scandinavian countries. While adequate demand is a necessary condition for the cure of structural unemployment, it is not a sufficient condition.

Finally, I should like to say a brief word about inflation and the balance of payments. It is often said that if an expansionist policy had been pursued in the late fifties, this would have produced serious inflation. Consider in this connection the much discussed inflationary period, 1955–57. Now the plain fact is (and I am glad the Council made note of this in their report) that this inflationary episode was limited largely to one sector of the economy, namely, durable manufactured goods, metals and metal products, machinery and motive products, and the like. In this area there was indeed a sharp rise of about 7 percent per year from 1955 to 1957.

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In the rest of the economy, however, the price increase was less than 1.5 percent per year, an extraordinarily low figure for the prosperity phase of the cycle viewed against the historical background.

At this point I should like to interject a comment.

The Phillips curve analysis, which has become popular in recent years, makes inflation a function of the rate of unemployment, but it covers up the impact of the business cycle. In the 19th century, prices rose in the prosperity phase of the cycle and fell in the depression phase. Nowadays, prices rise in the prosperity phase and remain stable in the recession phase. The prosperity phase induces price increases, because the recovery spurt far exceeds the normal growth rate. If we hope to achieve greater price stability, we must do a better job of ironing out the cycle.

Returning to the 1955–57 episode, there was in 1955–57 no overall excess of demand. In the economy as a whole, excess capacity was rapidly developing, and unemployment was increasing. In the durable manufactured goods area capacity was no doubt strained in some sectors for a brief period. This situation was favorable for the exercise of market power on the one side to maintain profit margins, on the other side to press for wage increases. Had these industries faced sharp foreign competition as they have during recent years, the record might well have been quite different. But we had not yet reached the time when currencies were again convertible, and the United States was still a sheltered market.

The economy as a whole was operating at low capacity and therefore at high unit cost. Expanding output would have put our industries in a stronger competitive condition preparatory to the day when currencies again became convertible.

The so-called classical medicine, under modern conditions, can neither cure the cost-push problem nor the balance-of-payments problem. The classical medicine, namely, semi-depression and a considerable margin of unemployment, was indeed more or less effective in reducing costs under the classical conditions of 19th century free competition. But it will not work in an oligopolistic and highly organized society. Deflation is no longer an effective means to reduce cost. Quite the contrary. It is precisely in slack periods that business presses for higher protective tariffs. It is precisely in slack periods that labor engages in restrictive practices, and demands shorter hours to spread the work. In our kind of society there is no escape. The wage-price push has to be met headon, whether times are good or bad.

There is, however, good reason to believe that this problem can best be managed under fairly high employment conditions when high-capacity output yields low unit costs and satisfactory profit margins. We can stand up against foreign competition much better when business and employment conditions are good. And there is probably no better weapon with which to police the price-wage spiral than foreign competition.

For these reasons I strongly disagree with those who hold the view that the way to solve our balance-of-payments problem is to apply the classical medicine. This is not the way out. Indeed, this road, long pursued, would sink us deeper and deeper into the mire of inefficiency and high unit costs. Unless our industry is running at fairly high capacity, we shall not be able to compete successfully.

In view of what I have said, it is indeed surprising that we have held our own as well as we have in world markets. Our trade surplus remains high. The large increase in our international deficit in the 3 years 1958–60 was not due to any drastic change in our trade situation. The deficit was due basically to capital movements—first a large outflow of long-term capital, and in 1960 a large outflow of "hot" money. The rapid expansion going on in Europe, the emergence of mass markets, booming prosperity in contrast to our semistagnation—all this, once general convertibility was restored, was the cause of the long-term capital outflow which ushered in the exceptionally large deficits of 1958–59, the cumulative effect of which prepared the way for the flight of "hot" money in 1960.

It was not excessive prosperity in the United States that was causing our unusual deficits. We were enjoying no such prosperity; quite the contrary. And confronted with a new experience, we applied the 19th century remedy, thereby pushing the economy down still further. The more depressed the American economy, the more did American capital flow out into more promising fields, while Europe found American investment outlets unattractive. The big deficit of 1958 was primarily caused by a large outflow of long-term capital.

As far as "hot" money is concerned—the gold score—there is good reason to believe that the International Monetary Fund, by enlisting the collaboration of the central banks and treasuries, in all the leading Western nations, has got this matter reasonably well under control. That the great Western nations are prepared to spend many billions of dollars in defense, without doing what is necessary to defend their currencies, is simply beyond credibility. I think we can safely assume that we and our allies are not that silly. We have the financial ability and ingenuity to forestall any probable future gold speculation. I could myself wish, however, that we could scotch this gold speculation right at the source by persuading all countries to do what we have already done, namely, make it illegal for any citizen to acquire and hold gold except for industrial purposes.

That is all, Mr. Chairman.

Chairman PATMAN. Thank you, sir.

Professor Wallich, we would like to hear from you. You may proceed in your own way, sir.

STATEMENT OF PROF. HENRY C. WALLICH, YALE UNIVERSITY

Dr. WALLICH. If I may, Mr. Chairman, I would like to summarize my statement.

Chairman PATMAN. You may insert your statement at this point and summarize it as you desire.

Dr. WALLICH. Thank you very much.

(Professor Wallich's prepared statement follows:)

STATEMENT OF PROFESSOR HENRY C. WALLICH ON THE ECONOMIC REPORT OF THE PRESIDENT AND THE ANNUAL REPORT OF THE COUNCIL OF ECONOMIC ADVISERS

The most important part of the 1962 Economic Report, from the viewpoint of economic analysis, is the report to the President by the Council of Economic Advisers. The Council has produced an extremely stimulating document.

Academic economists will be particularly interested in the use made of the full employment surplus concept, and in the relationship between the rate of capacity at which the economy is operating and the profit level of corporations. With the goals that the Council sets forth in the areas of economic growth, price stability and balance-of-payments equilibrium, I find myself in broad agreement, although I might differ in emphasis. These elements of agreement I would like to stress, because on a number of particular points I feel that questions need to be raised about the Council's approach. These questions are evoked by the report's tendency to set impressive goals and then to propose actions that may fall far short of attaining these goals.

THE ECONOMIC OUTLOOK

The premises on which the Council bases its expectations of continued strong expansion need to be closely examined. The last three recoveries exhibit characteristic features which may throw light on the further progress of the economy. Typically, a change from inventory cutting to inventory building has sparked the earliest phase of recovery. Housing, stimulated by easy money, has then tended to carry it forward. Rising Government expenditures added push in 1958, as they did in 1961. Eventually, inventory building and housing slackened off, and further expansion of consumption and production was stimulated principally by a rise in business capital spending.

This cyclical pattern has tended to repeat itself in 1961. Inventory building came in early, and further impulses can be expected from this source during the first half of this year. Housing picked up, too, although the rise remained moderate because interest returns never fell very significantly. Government expenditures have supplied a powerful push, but will rise much more slowly after midyear. The early expansive forces, in other words, once more are likely to lose momentum. The burden of carrying forward the expansion will then fall upon plant and equipment spending. So far, surveys of business spending intentions give little evidence that strong increases are planned. The Council's analysis seems to rest on the belief that the most promising way to encourage an upward revision of capital spending plans is to push up Government expenditures rapidly in order to narrow the capacity gap. I doubt, however, that a rapid expansion up to midyear will lead businessmen to take for granted that the rise will continue at that rate, if they see little to justify that assumption. A slower and more sustained increase in Government spending might have produced more sustainable expansion.

BUDGET ESTIMATES

Because of the uncertainties surrounding the second-half outlook, the $570 billion GNP estimate must be considered optimistic. The same must be said of the revenue estimate based upon it, even if the GNP estimate should be confirmed. The anticipated level of corporate tax revenues assumes that corporate profits will come very close to 10 percent of GNP, which they did for the last time in 1956.

On the other hand, the assumed expansion of GNP and revenues is in line with the expansions that began in 1954 and 1958. There is no strong reason to believe that the structure of the economy has weakened in the meantime. The GNP estimate that was made for 1959, of $473 billion, was also widely regarded as optimistic. Nevertheless, the GNP actually realized turned out to be $483 billion. During a period of recovery, then as now, a reasonably optimistic estimate is appropriate. In the event that the expansion should be weak and the estimate fail to be realized, the inflationary dangers will be less and a small budget deficit may be appropriate.

THE FULL EMPLOYMENT SURPLUS

The concept of a full employment surplus, which the Council elaborates statistically, has its ancestry in the proposals made by the Committee for Economic Development in 1947. The CED at that time recommended that tax rates and expenditures be so set as to produce a surplus when the economy operates at full capacity. Subsequent increases in expenditures not covered by the natural growth of revenues were to be offset by higher tax rates. This concept of "incremental balancing" of expenditures and revenues fell far short of realization during the early 1950's. For a while, in fact, it looked as if it would be impossible to balance the budget with the existing revenue and expenditure structure. It was a notable achievement that the budget was brought back into line so that a few small surpluses were in fact realized.

By 1960, however, the relative structure of revenues and expenditures had so altered as to make the full employment surplus quite large. This was confirmed by a study undertaken by David Lusher, of the Council of Economic Advisers, early in 1960. While the strong fiscal and monetary restraints that operated during that year were helpful in controlling the balance-of-payments deficits and reducing pressure on the dollar, they probably weakened the expansion and shortened its duration.

Experience in computing the full employment surplus suggests, however, that its measurement is unlikely to be as exact as the Council's report seems to indicate. The level of revenues depends heavily on corporate profits. These have been trending downward during the 1950's. A projection of full employment revenues based on past performance may well exceed what could be realized under today's conditions.

Again this surmise it has been argued that the lag in corporate profits reflects principally the lower rate of capacity utilization in successive cycles. It has been suggested that corporations have sought to meet this by lowering their break-even point so that at full capacity operation the share of profits in the GNP would be higher than formerly. Such evidence as there is, however, seems to be confined principally to the steel industry. For the economy generally, a lower profit rate seems entirely plausible in view of the disinflationary climate, the rise in foreign competition, and the strong efforts made to hold the price line by governmental suasion.

BUDGET OUTLOOK

With the recent rise in Government expenditures, the full employment surplus clearly has been much reduced. Members of the administration have stated that they find the present posture "comfortable." Hereafter, increases in expenditures must not exceed increases in revenues if this posture is to be preserved. Unfortunately the budget statement still does not provide a usable projection of expenditure commitments already on the books and reasonably to be expected. The general impression conveyed by the budget is that the built-in momentum of existing programs will absorb for some years most of the expected growth in revenues. If that impression is correct, there is little room for either further expenditure programs or a tax cut.

When one contemplates the $11 billion increase in expenditures from fiscal years 1961–63, one cannot help feeling that a great deal of money has been spent for very limited purposes. The great bulk has gone for defense and space projects, and I do not presume to argue against them. The remainder, however, has been scattered over a wide variety of purposes, with agriculture one of the principal beneficiaries. It is not at all clear how much has really been accomplished by what might be called the buckshot approach. The experience seems to confirm that it is not easy for the Federal Government to meet particular needs without generating a considerable volume of deadweight expenditures.

TAX CUT AND PUBLIC WORKS AUTHORITY FOR THE PRESIDENT

The Economic Report gives details on the powers sought by the President to cut taxes temporarily and to increase public works in case of recession. In principle, I strongly support the tax authority. Nevertheless, reaction to the proposal thus far seems to show that its legislative prospects are not bright.

Under the circumstances, I would suggest the following alternative. The Congress might see its way to deciding what kind of tax cut would be appropriate in case of recession. This could be done by holding hearings and by declaring the intention of the Congress, perhaps by way of joint resolution. If and when the need for a tax cut should arise, the President could make the proposal and the Congress could quickly respond by voting or rejecting it. This procedure would cut short the legislative processes that would have to be initiated if all the problems involved in a tax cut had to be studied and discussed at the time when it ought to be made. Past experience suggests that a tax cut can be blocked by lack of agreement over the kind of cut that would be appropriate, whether it should stimulate primarily consumption or investment,, whether it should involve a permanent reform of the tax structure or only a temporary reduction in rates, together with a host of other conflicting considerations. If advance agreement could be attained on what to do, the decision whether and when to do it could be made more easily. Effective countercyclical tax policy would then become possible even without discretionary powers for the President.

PUBLIC WORKS AUTHORITY

Past experience with public works in recessions gives only limited hope that they can be developed into an effective stabilization tool. Certainly many projects can be accelerated. This is often possible by administrative decision, as the actions listed in the Council's report demonstrate. Public works on a larger scale have shown themselves to be too slow in operation. In a short recession, they are likely to come too late. In many cases they will not be easy to terminate once jobs and vested interests have been created. It would be unfortunate if the difficulties that seem to stand in the way of tax-cut authority should cause public works to become the primary antirecession tool.

GROWTH

The Council's report properly stresses the importance of a high rate of growth. The report also suggests that a rate of over 4.5 percent will be attainable at some time in the future. This improvement over past performance however would not be the result of the policy measures proposed by the Council. It would result predominately from a more rapid increase in the labor force to be expected as the 1960's advance. It is indeed fortunate that demographic developments permit us to look forward to this. But these developments hardly constitute a deliberate growth policy.

Among the true growth policies in the report, the principal one is the investment tax credit. I believe this is a good device. I am particularly impressed by the Council's statement that the rate of return on a 10-year investment that would yield 10 percent per annum in the absence of the credit would be raised by the credit by one-third. The amount of $1.5 billion, however, is very small when contrasted with the American economy's total gross private investment, which is of the order of $80 billion. Moreover, the revenue lost by the tax cut is to be made up by a series of tax measures some of which will be adverse to capital formation, because a good part of the additional taxes would come out of income saved rather than out of income consumed. Obviously no one could argue that recipients of interest and dividends should not pay their taxes. But it is necessary to realize that unfortunately some of the Nation's homes and some of its plant and equipment were financed with money that really belonged to the U.S. Treasury. A substitute for this money must be found before we can hope to increase total investment. Taxation of mutual savings institutions, of cooperatives, the removal of the dividend credit, the tightening of capital gains treatment will all reduce the volume of investable funds. Whether desirable in themselves or not—and I certainly support some if not all of these actions—the impact as far as economic growth is concerned will be negative and will eat into the benefits that the tax credit may yield.

Of the remaining growth oriented proposals in the report, most are relatively minor. Aid for education would indeed be important, but the legislative outlook does not appear good. In view of all this, it is difficult to avoid the conclusion that we have not yet come to grips with the real problem of raising economic growth.

BALANCE OF PAYMENTS

The Council is to be commended for the very serious attention that it gives to the balance of payments. The constraint that the payments deficit imposes upon American economic policy is apparent everywhere in the report. The decision to balance the budget clearly has been determined in large measure by balance-of-payments considerations.

Nevertheless, the report still seems overly optimistic with respect to the balance-of-payments outlook. The President states that the problem should be solved within 2 years, and the Council says that measures taken and proposed will in time lead to sustainable balance. In support of this judgment the Council cites the improvement in the balance of payments in 1961, which is indeed striking in both the basic and the short-term capital accounts. Unfortunately, most of the improvement occurred during the first half of the year when the economy was still operating at low levels. In the fourth quarter the situation deteriorated materially. One has to apply arithmetic, however, to the Council's quarterly and annual figures to discover this in the report.

With rising prosperity in 1962, a substantial increase in imports must be expected. Exports can be expected to rise too, but probably by a much smaller amount. The initial developments resulting from the Common Market will not be favorable. Under these circumstances the search for further measures to reduce the balance-of-payments deficit must continue relentlessly. If we do not succeed in this endeavor, we face the danger—I do not say the probability—of renewed heavy pressure on the dollar. A large outflow of gold may make it necessary to raise interest rates drastically. The shadow of this contingency falls alarmingly upon the prospect for continued cyclical expansion.

Among the measures urgently needed are those embodied in the President's reciprocal trade proposal. Continued access to the Common Market must be secured. If the President's trade proposals are accepted, there is excellent hope that the net result of foreign reciprocal trade will lead to a great expansion of American exports and imports. It must be realized, however, that this is a defensive operation, economically speaking. The United States is threatened with a loss of some of its markets. By adopting the President's program we can forestall this loss. Whether we are likely to improve the balance of payments beyond what it would have been in the absence of the Common Market is much more uncertain.

GUIDELINE FOR WAGES AND PRICES

In its detailed statement on guidelines for private wage and price action, the Council elaborates and improves upon previous efforts at public suasion by this and the previous administration. It takes a cautious, and I believe, appropriate further step toward the evolution of a wage policy. This is a move which, in one form or another, several European countries have already taken or are in the process of taking. The Council properly stresses that overall productivity gains, rather than gains in each industry, define the available margin for non-inflationary wage increases. The Council also stresses the need for price cuts in industries whose productivity gains exceed the national average, where profit margins would widen in the absence of price cuts.

The quantitative guidelines proposed by the Council are vague, however. Productivity measurement admittedly is in its infancy. Nevertheless, it is hard to see why the Council should present a table in which the range of productivity gains extends from 1.9 percent to 3.5 percent. It is equally difficult to understand why the Council eliminates the public sector from this table. If the public sector were included, average productivity gains would be significantly less.

It would have been possible to pinpoint more precisely the most appropriate single guideline. If Government is to be excluded, perhaps because it is subject to very special circumstances, the same should apply to agriculture, where productivity in recent years has advanced exceptionally rapidly thanks to high price supports and the pressures of acreage restriction. Manufacturing alone certainly is not a fair guideline, since it accounts for less than one-third of the nonagricultural labor force. This points to productivity gains in the private economy excluding agriculture as the most meaningful guide. It seems not inappropriate to disregard the relatively slow growth of productivity before the war and to concentrate on the productivity gains since the war which, for the period 1947 to 1960, has been 2.4 percent. This figure accords roughly with that cited by the President in his economic message early last year, in which he said that productivity per worker had increased by 2 percent on average. Two percent per worker is not far from 2.4 percent per man-hour, allowing for the shortening of the workweek.

Unless the Council pinpoints a much narrower range and preferably a round figure as a guideline, such as 2 percent per worker, there is a serious danger that the guidelines may work mischief. There will be a strong temptation to pick on a figure like 3.5 percent, however irrelevant, which would perpetuate a rate of wage increase incompatible with price stability. Furthermore, by suggesting that low wages should advance beyond the guidelines, the Council invites acceleration of wage movements in certain areas. Much as removal of inequities is to be desired, it is not helpful to speed this development at a time when a general appeal is made for wage restraint. All this creates the prospect that in actual wage bargaining, the maximum in effect may become the minimum.

A similar comment must unfortunately be made also on the announced proposal to raise the civil service pay scale. Such increase is to be desired for many reasons. Few who have worked in Washington would begrudge its loyal and devoted public servants a more adequate rate of pay. But the moral force of an appeal for private wage restraint is not strengthened by simultaneously raising the pay in the public sector.

As an alternative to the Council's proposal, I would suggest that the Government pinpoint a single rate as a voluntary guideline. For some time at least, until the balance-of-payments crisis has passed, labor and business should be urged not to exceed it. There is no need to urge that wage increases should go at least up to this level. Stated in this way, there would be little danger that the maximum would become the minimum. With present and foreseeable unemployment, there is little danger also that significant labor shortages would develop if such a guideline were observed. While this line, as well as the Council's, would tend to freeze labor's share in the national income, that share is now high by historical standards. Insofar as there is unfairness in any guideline, it would at present be directed more nearly toward capital than toward labor, provided the price level remains stable.

With the aid of increased understanding on the part of the public, of labor, and of business, further enhanced by the effect of foreign competition, there is hope that such a guideline can slow the wage price spiral. An essential condition, however, is that Government pursue appropriate fiscal and monetary policies. Public suasion and guidelines are a supplement to responsible financial policies, not a substitute. It would be a great misfortune if the view should gain ground that the establishment of voluntary guidelines for the private sector exonerates the Government from pursuing proper fiscal and monetary policies.

It would be a great misfortune, likewise, if the guidelines should become anything but voluntary. They are a means to help the free market work as it should, not a step toward abrogating it. Guidelines must not become a prelude to wage and price control.

I would urge one further step. The existence of cost-push inflation is generally believed to result from the existence of market power on the part of strong unions and strong companies. Accordingly, it would be possible to reduce cost-push pressure by reducing market power. To accomplish this, it would be necessary to reduce the size both of the large unions and of the large companies. Proposals along these lines are frequently rejected on the grounds that they are not only very difficult to implement, but that they would hurt productivity. I personally share the fear that productivity might suffer, and that would be a high price to pay. But in fact there is little conclusive evidence to prove the case either way. It might be a worthwhile endeavor to undertake a study of the matter. The study would try to discover whether a reduction in the size of the largest corporations would indeed hurt productivity. If objective evidence should turn up that this is not the case, there would still remain very strong practical difficulties in the way of accomplishing anything worthwhile. But an enlightened public opinion can accomplish many things. There is every reason why we should seek to enlighten ourselves and the public on this central question.

Dr. WALLICH. I would like to say first of all that it is a great pleasure to be testifying side by side with my old teacher, Professor Hansen. Most of the economics I know, I learned from him, and I hope that he will feel that I have learned my lessons.

I think the Council has turned out a most interesting document. One reads this with real intellectual excitement. I find myself in broad agreement with the goals set forth. I find particularly attractive the generous goal of broadening equality of opportunity. I might differ in emphasis on some points.

Where I have serious questions about the report is that after setting forth these fine goals, the measures proposed seem to fall far short of attaining them.

Let me begin with the cyclical outlook. We have now experienced several postwar cycles, and they seem to fall pretty much into a pattern. This does not mean it will always be that way.

At the beginning, we get a strong kicker from inventory building. Last winter, that is, in the first quarter of 1961, we had inventory cutting of $4 billion. That has been reversed, and we are now going, or were going in the fourth quarter, to $4.5 billion accumulation.

In other words, $8.5 billion were added to GNP simply by this turnabout in inventories.

Then, historically, we found that housing comes in as a strong expansionary factor, thanks to lower interest rates. This has not happened to the same degree in the recent recession, because interest rates never came down very far.

Government spending continues as an expansionary factor throughout most recessions, certainly in 1958–59, and in the last one. But these forces tend to peter out, and something has to fill the gap.

Now, typically, this should be plant and equipment spending. As the economy rises, we go toward high-capacity operation, and business feels the need to enlarge capacity.

I do not, in the present situation, see very much to suggest that plant equipment spending is going to expand sharply. The surveys—McGraw-Hill, Commerce, SEC—are not particularly promising.

If I interpret the Council correctly, it seems to feel that the way to pry loose an increase in plant and equipment spending is to push up the GNP fast, through a sharp increase in Government spending, and then hope that higher plant equipment will carry the economy from there.

But what has happened in the recent expansion is that Government spending went up sharply and now is going to level off. In other words, the expanding forces will be diminished quite pronouncedly. Businessmen know this as well as everybody else. They read the statistics. And they may not be inclined to upgrade their plant and equipment plans just because expenditures were pushed up so fast in fiscal 1962. I think a slower and more sustained movement of Government expenditures might have given us better assurance that we would have a sustained expansion in this cycle.

As for the GNP and budget estimates for 1963, I cannot help feeling that they are quite optimistic. Even if we should reach $570 billion GNP, that will not assure that we will get $93 billion of revenue. That depends very much on corporate profits, which are the wheelhorse of the revenue system.

Corporate profits have been trending downward all through the 1950's. The last time they reached 10 percent of GNP was in 1956. They may well disappoint us.

At this point, the Council brings in a very interesting concept, the full employment surplus. This was developed in 1947 by the Committee for Economic Development. They even pinpointed a figure. They thought that at high employment we should have a surplus of $3 billion. I think they talked in terms of the administrative budget; not the income and product account budget.

The Council has found in its report that the present full employment surplus is considerably bigger. This is no surprise, because in February 1960, the then Council of Economic Advisers had a staff study by Mr. David Cusher, which showed that indeed the surplus had become quite large.

Basically I think it is an achievement that from a structural deficit, you might say, a full employment deficit, as I fear we had at some points during the 1950's, we did get to a position where, at full employment, we could look forward to surplus.

Senator BUSH. Mr. Chairman, could I ask a question, just for definition?

I do not quite understand this language, "full employment surplus." Would you define what they mean by that?

Dr. WALLICH. Yes, Senator Bush. The Council makes an assumption as to what constitutes full employment, that is, 4 percent unemployment. I personally would not go along with any figure. I think with proper measures we could get below that. But at 4 percent, they then estimate what would be the GNP. And having estimated the GNP at 4-percent unemployment, they estimate what would be the revenues.

Now this is indeed a rather uncertain procedure. We do not know whether a 4-percent unemployment figure would really translate into this precise GNP, and we certainly do not know whether this precise GNP would translate into a particular revenue figure.

For instance, the rates that are applied in order to convert corporate profits and personal income into tax revenues differ during a period of expansion and a period of level movement of the economy. If we merely fall short by 1 percent of GNP in the level of corporate profits, if instead of being 56.5, as is here estimated, profits should be 1 percent of GNP less, which would put them at $51 billion, there would be a tremendous hole, of course, in the budget and in the full employment surplus.

So I think an exercise like this, while it is very valuable in conveying a general impression, has to be taken with a grain of statistical sait.

Senator BUSH. Thank you.

Dr. WALLICH. Now I would like to say one more thing about the budget outlook. I said already that because of the optimistic character of the GNP estimate, and the optimistic character of the revenue estimate derived from that, the budget revenues are clearly on the optimistic side.

Perhaps that is not so bad, after all. If the economy should falter, inflationary pressures would be less and the budget deficit would be less dangerous, and it may even be appropriate to stimulate the economy.

But when I look at the content of the budget expenditures that are listed here, and in the budget message, I see that we have had a great increase in 2 years, about $11 billion. And I ask myself: How much better off are the American people for spending this $11 billion in the budget?

Most of it went for defense and space, and I would not presume to argue about that. That is not an economist's job. But the rest was spread broadcast over a number of diverse functions. The principal gainer was agriculture, last year, that is, in fiscal 1962, with a $1.2 billion increase; and small increases were spread all across the board.

It seems to suggest that the Government, in making some useful and desirable expenditures, finds itself automatically generating a lot of other expenditures that are perhaps less useful and less necessary. There is an inevitable tendency to generate deadweight expenditures along with the good; and that puts a kind of discount on those expenditures that one would regard as desirable.

Next I would like to turn to the very dramatic requests for tax-cut authority and public works authority.

In principle, I am all in favor of the tax-cut authority. In fact, as a technician, I feel compelled to go beyond this. I think we should not cut for 6 months. I think we should cut for 1 or 2 months. And we should not cut 5 percent. We should cut 100 percent. We should suspend personal income tax collection for a very brief time. This would inject a solid dose of purchasing power for a short time. There is no question that this cut would be reversed very soon. There is no danger that a temporary cut might become temporarily permanent, like so many features in our revenue system. And after 1 or 2 months, we would go back to the old rates, and we would have done as much in that period as under this proposal we might do over a year, assuming that the 6-month cut would be extended for another 6 months or so, which seems rather likely to me.

As a practical man, I have to realize that these proposals stand little chance of adoption, and I would like to suggest the following alternative:

The Congress might see fit to deliberate on the kind of tax cut that is desirable—hold hearings; having reached agreement, have a joint resolution proclaiming the desirable form of tax cut, whatever it is, 5 percent or larger. Then if and when an emergency should arise, the President might propose and the Congress could quickly vote yes or no.

Now, we have the experience of 1958. There was a long debate about whether there should be a tax cut or not. It got stymied over the issue whether it should be a tax cut to favor investment with a permanent reform element, or whether it should be a quickie to stimulate the consumer. It took several months to argue about this and it ended up with an agreement that nothing would be done. The recession passed, and we had no tax cut. I would fear that this would repeat itself unless some advance agreement is reached on what to do if the situation should arise. That is what I would like to propose.

About the public works authority I am less enthusiastic. If we have learned anything in these repeated recessions, it is that public works come in too late to help. They tend to come after the economy has already turned up. They are very hard to stop. Once jobs have been created, it is very hard to fire people again. So the transitory tends to become permanent. I hope that we will not go to the public works authority just because, perhaps, it is more feasible, and discard the tax route, which I think is generally recognized to be the more effective and better device.

On the issue of growth, the Council very properly stresses the importance of growth. And indeed, there has been no dearth of discussion. But when one looks at the proposals they make, one finds that the principal reason why the Council hopes that we can hit a 4.5 percent rate sometime during the 1960's is that way back in the 1940's a larger number of children were born who will now enter the labor force. Now, this fact we have known for 20 years or so. This is not a new growth policy.

Among the constructive new measures that have been proposed, the most important one is the tax credit. Granting that there are a lot of questions associated with it, I still think that to the economist, this is an attractive device, particularly as it has now been reformulated by the Ways and Means Committee.

I am impressed by the Council's calculation that this credit raises the rate of return on a 10-year investment project that yields 10 percent, by one-third. Now, that is a pretty substantial inducement to a businessman.

On the other hand, I see that this $1.5 or $1.8 billion investment tax credit is to be recouped by a lot of so-called loophole closings. Most of these loopholes are perfectly legitimate tax provisions properly enacted by the Congress. They are not loopholes in the proper sense of the word. But most of these "loophole" closings unfortunately hit income that would go into saving and investment instead of hitting income that would go into consumption. This is in the nature of the thing. The so-called loopholes are principally in the upper brackets, and that is where the saving principally is.

I am in favor, obviously, of people paying their taxes on interest and dividends. I am in favor of taxing savings and loan associations and cooperatives. But I am aware that this is going to reduce the savings available for housing, for plant and equipment. We are not going to accelerate the rate of growth by removing the financing that is needed for housing and plant and equipment.

Therefore, I come to the reluctant conclusion that the tax proposals tend to take away with one hand what they seem to be giving with the other, although perhaps it is not a quantitative equivalence.

Next, the balance of payments. The Council I think is to be commended for the very serious attention that it gives throughout to the importance of the balance of payments. I think it is pretty obvious that the principal reason for presenting a balanced budget, even an optimistically balanced one, is the balance of payments. But the estimates of the outlook strikes me as on the extremely optimistic side.

We have had an improvement in 1961. This the Council correctly points out. Most of this improvement came in the first half, however, when we were close to the bottom of the recession. Since then, business has expanded; demand for imports has expanded; imports have gone up. And in the fourth quarter, as was well known at the time this was written, and is known in greater detail now, we had a very sizable deficit.

I do not, therefore, understand the statement that the measures taken, or still to be taken, will produce sustainable balance, or the statement in the President's own report that in 2 years we ought to reach a reasonable balance. I fear that we face a much more difficult task.

The National Foreign Trade Council has already projected a $3 billion deficit for 1962, in other words, a bigger deficit, unless we get some special payments again of the kind that we had from Germany and other countries last year.

It is in this context, I think, that one must view the President's reciprocal trade proposal. I think this is a bold and fine proposal. It deserves strong support.

One must realize, however, that it is basically a defensive operation. The Common Market, in the absence of proper action, is going to cut down our exports, or at least cut them down relative to what they would otherwise have been. What we hope to do by getting the better of the bargaining under this trade proposal is to undo this damage. This is in a sense a holding operation. It will not be necessarily a net gain. It will be an avoidance of damage. We cannot, therefore, rely on this trade proposal to straighten out the balance of payments. The trade proposal serves to avoid the damage that in its absence might result to the balance of payments.

I would like to wind up on the subject of the guidelines for wages and prices.

The Council is edging toward what has been called a wage policy. In previous economic reports, more cautious hints in that direction were thrown out. The Council deserves credit for finally having named members. The Council also deserves credit for emphasizing the need for price cuts to match the wage restraint that it suggests.

Unfortunately, the Council's numbers, the rates of productivity gain, are quite vague. On page 186 of the Economic Report, they present the crucial table. The productivity gains cited here run from a low of 1.9 percent per year to a high of 3.5 percent.

It seems to me that this is an invitation to a competent bargaining union to pinpoint the 3.5 percent and say, "That is what we ought to get, and that is the minimum."

If one looks at the table more closely, I think one discovers that the most central and plausible figure to use is 2.4 percent. The reason is this: The table eliminates, first of all, Government. If they had included productivity gains in Government, they would have got lower figures throughout; and I do not see why Government should have been excluded.

Taking only the private economy, the figures are influenced by the abnormal gains in agricultural productivity since the war. These have been produced by the farm support prices and acreage restrictions. The farmer, being under restriction, has poured more fertilizer on a smaller acreage and has come through with a wonderful production record. This has been abnormal and should not be counted as a part of the long-term productivity record.

That leaves us with so-called nonagriculture. I would rule out manufacturing alone, because that is just a very small sector, less than one-third, of the total private sector. I would take the whole of nonagriculture. I would then take the whole of the postwar period. And that comes out at 2.4 percent.

This is very close to the figure that the President mentioned in his economic message earlier in 1961. He said that productivity per worker had grown by 2 percent. That is a good round figure. The Council counts productivity not per worker, but per man-hour. Two percent per worker is pretty close to 2.4 percent per man-hour, because of the shortening of the workweek.

I very much wish the Council had gone back to its 2 percent per worker, instead of putting up this wide range.

I fear that the way the guidelines are qualified, furthermore, will have the effect of making the maximum the minium. In effect, the Council encourages business and labor to find exceptions, and particularly encourages low-wage unions to ask for more than the average.

Obviously, a removal of inequities is highly to be desired. Nobody could quarrel with that. But a time when one is trying to restrain wage increases voluntarily is not the best time to stress the removal of inequities.

Finally, I hope that these guidelines and the emphasis on voluntary restraint do not mean that the Government hereafter is going to feel itself exempt from the need of practicing restraint in its own budgetary and credit policies. That would be very unfortunate.

I agree with my teacher, Professor Hansen, that given the kind of inflation with which we are faced, a cost-push inflation, fiscal and monetary restraints are not sufficient. I still think they are necessary. If they are relaxed, then no kind of voluntary or other restraint on wages and prices is going to do any good. We need them both.

And so these guidelines should not absolve the Government from continuing to do its proper job in anticyclical budget policy, surpluses in booms, deficits in recessions, and the right kind of credit policy.

And I would urge one further step. We seem to be agreed that cost-push inflation has been the principal cause of recent inflations. That means market power. There has been market power in the big unions, market power in the big companies.

One way of dealing with this would be to remove that market power by reducing the size of the companies and reducing the size of the unions.

Now, proposals of that kind are generally rejected on the grounds that they would hurt productivity, quite aside from being very difficult to implement, of course.

I share the fear that productivity might be injured if large companies were reduced in size and large unions were reduced in size. But we have contrary evidence. We have Mr. Romney's American Motors, which seems to be able to turn in a perfectly good profit, being a relatively small company in their industry. And I submit that the statistical evidence here is not conclusive.

We ought at least to study very seriously whether the present scale of bigness in industry and labor is really necessary to attain our present level of productivity. If it is not, the obvious steps follow immediately. This is a central question, and I hope that we can enlighten ourselves on it.

Thank you very much, Mr. Chairman.

Chairman PATMAN. Thank you very much, Mr. Wallich.

Mr, Reuss, you are recognized to interrogate our distinguished witnesses, if you desire to do so.

Representative REUSS. Mr. Wallich, I would like to discuss the balance-of-payments section with you, in which you point out that we have by no means solved our balance-of-payments deficit problem, and that the annual deficit, on the order of $3 billion, which we have had by and large for the last 4 years, seems likely to continue in 1962. And then you say:

Under these circumstances, the search for further measures to reduce the balance-of-payments deficit must continue relentlessly.

Well, let us continue relentlessly right now. And I bear in mind that you contributed, in an article in Harvard Business Review, for example, a set of recommendations on what we ought to do about our balance-of-payments deficits. Many of the recommendations made by you and others, I am happy to say, have been followed and have prevented, I believe, the situation from becoming worse.

However, as I see the situation, we have done domestically about everything that you and other wise men have recommended we do, and we still have a $2 to $3 billion basic deficit.

I, therefore, ask you, as long as we are pursuing relentlessly the search for a solution, if the most feasible solution is not for the strong countries of Western Europe, which are running a surplus which is almost a precise counterpart of our deficit, to get together, as they have done in the past, notably in Paris in 1947, in the Committee for European Economic Cooperation, and work out a plan and program for lowering their surplus by $2 or $3 billion a year, and wiping out our deficit by a corresponding $2 or $3 billion a year, by a combination of paying a greater share of the burden of defense, contributing more to the development of underdeveloped areas, and unilaterally lowering their tariff barriers and undoing their quotas, so that we may expect more.

Is that not the royal road to balance-of-payments solvency?

Dr. WALLICH. Well, Congressman Reuss, except for an effort to increase our own productivity and to keep our own price and wage level in line——

Representative REUSS. We must, of course, do that.

Dr. WALLICH. I would put your solution at the top of the list. However, I do not know any feasible way of achieving it other than by slow, patient, prodding negotiation. This has been going on for years, and I hope further progress can be made. I do not expect any miracles. Prepayments of debt simply mean using up our reserves.

Representative REUSS. I do not want to seem ungrateful for the prepayments that have occurred, but are they not essentially almost as deceptive as, let us say, the action of certain big banks in the 1930 depression, who would quickly lend some assets to a shaky smaller bank the day before the bank examiner came around, to make it look a little better? The prepayment of debts does not alter in any fundamental way, does it, our balance-of-payments difficulties?

Dr. WALLICH. That is my impression, too. This is almost the same as if we were borrowing abroad. It is simply a using up of reserves. What we need is a structural improvement.

If we can get this greater burden sharing on military and foreign aid account, that is fine. I think this effort should go on continually.

I doubt very much that we can accomplish enough that way. I doubt that we can, so to speak, say to our creditors: "Look, we have come to the end of the rope. We don't know what else we are going to do. So now you must do something for us."

I think that this might add some hundreds of millions of dollars to the solution of the problem. I doubt very much that it will give us $2 or $3 billion.

Representative REUSS. I am disturbed to hear you say that, because neither you nor anybody else has been able to tell me how we are going to do it.

Of course, we need to keep our own price level stable. We need to expand our productivity, particularly in the export fields, and we can just take that as a datum for all our discussion on it. Having done all that, however, we still are faced, it seems to me, with an intractable $2 to $3 billion annual deficit. Unless you or some other thoughtful person can show me how we are going to bridge that gap, I would disagree with your conclusion that slow, quiet, modest nudging methods are going to work. I think that what is indicated is the kind of cosmic appeal which set the Marshall plan in motion, for example, and that if we continue with these modest, hat-in-hand, "Give us a few million dollars" approaches, we are going to be in very serious trouble.

I would like your comments on that.

Dr. WALLICH. I think we have not yet exhausted the range of possible action.

First, if we could really make the wage and price guidelines stick, I think we would have taken a very large step forward. Wages in France and Germany are advancing very rapidly—11 percent, I believe, in Germany last year. And if we can just slow our rate of price advance, or perhaps even cut prices a little, it will help us a lot.

Second, I think we have not exhausted the possibilities of an export drive. The British after the last war really went after exports in an organized way. They established joint advertising for small firms, joint sales facilities. They had a dollar export council that told individual firms just how to go about exporting and cracking the American market.

This I think we have not yet done very effectively, though I recognize there is some action in that area. I do not know whether our export credit insurance scheme is of a magnitude that will really help. The Germans run billions and billions of dollars through their scheme. I doubt that ours is going to build up in the foreseeable future to anything like that.

And finally, I think it is not beyond what the GATT permits to have some aid to the export industries in the form of accelerated depreciation, for instance, that would enable industries that export to get better equipment and cut their prices.

Now, here are just three proposals that come to mind. I am sure there are many others.

Representative REUSS. Do you not think it would be a sensible procedure for the free world to pull itself together and ask itself in quantitative terms how much of the $3 billion gap this proposed accelerated export drive is likely to redress? I should think, by and large, it would be rather on the middling side. And how much, then, has to be redressed by aid sharing, military defense sharing, and unilateral tariff lowering?

Would you disagree with my assertion that the great preponderance of the gap has to be accomplished not by anything we can do unilaterally, but by what Europe has to do, or that it is not going to be redressed?

Dr. WALLICH. I agree with you, Congressman Reuss, that we should keep after our friends in Europe. And if you feel that a great, cosmic approach would be the helpful way, rather than the slow, diplomatic one, I am not one to judge this.

But I remember what happened in Vienna when we wanted to negotiate some rather modest standby loans for the IMF. It turned out that we could count on a great deal less cooperativeness than we had hoped. And I fear the same thing would happen if we now made this approach.

Representative REUSS. Vienna was not really very cosmic, and you also, I am sure, remember what happened at Bonn in November 1960.

You were along on that noble-spirited, but ill-fated venture, of a very uncosmic character, I think you got out of town all right, but you certainly did not bring home much help, did you? I, of course, intend no reflection on you and Secretary Anderson, who I felt was a much maligned man.

Dr. WALLICH. I appreciate your temperate comment on that expedition, but it was precisely that experience which in part leads me to think that the effort of trying to throw the burden on the other side is not too helpful.

We are still regarded as the great rich country that has been rather generous, not to say loose, in its financial practices. They think we ought to do the job and not they.

Representative REUSS. I appreciate your views, though I do disagree with you.

Thank you, Mr. Chairman.

Chairman PATMAN. Senator Bush?

Senator BUSH. I incline to agree very much with Mr. Reuss' thinking on this subject. And I think the visitation to Europe of Mr. Anderson and Mr. Dillon and Dr. Wallich, who went with them, did result in making an impression on them for the first time that we considered that we had a serious problem here. And it resulted eventually in a prepayment last year of some $650 million of debt.

Now, I agree with your interpretation of that, and with Dr. Wallich's interpretation. But it is $650 million, and for that particular year it reduced our deficit from the previous figure of upward of $3 billion down to $2½ billion. So I am not going to sneeze at that kind of a reduction.

Nevertheless, I certainly agree that this is a one-shot injection, and, as Dr. Wallich says, it is in a sense a borrowing type of operation and not at all a corrective one to the real causes of our problem, here.

Now, Dr. Wallich, I note your firm endorsement of the President's trade proposal, and I think we are all agreed that if we can increase our exports substantially and widen our balance of trade surplus, this would be a great help. But you testified about 2 months ago before a subcommittee of this committee that, as I recall it, certainly in the early stages of this deal, that was then projected, although we had not seen it, imports were likely to rise more rapidly than exports, particularly if we were enjoying an upswing in our own economy and our GNP was increasing, and that this would further aggravate rather than help the balance-of-payments problem, because it would narrow the surplus in balance of trade.

You recall that statement?

Now do you still feel this might be the result for the first year or two of such agreement?

Dr. WALLICH. I do feel, Senator Bush, that in the period ahead, imports will rise, yes; and this is likely to make the deficit worse. I am hopeful that in the tariff bargaining we will be able to improve our position, for several reasons.

One is that on the whole, our tariffs seem to be a little lower than theirs. If both sides cut by an equal percentage, theirs ought to come down a little more than ours; although this is not so for each product, and it may differ very substantially from product to product, in fact.

Second, I think we can count on some heritage of legacy of good will from the past. In the post-war period we made and received concessions, but many of the concessions we received tended to be nullified by quota restrictions. We often did not get their full benefit. I am hopeful that we could conduct a kind of bargaining that would, without too many concessions on our part, bring in substantial concessions.

Now, it is quite clear that we have to make some concessions, but it is also clear that we cannot cut deeply into vital industries. The peril point and the escape clause will remain in being, although with a somewhat different meaning; and we will have trade adjustment. I hope that will mean in many cases that the same industry will produce its old products in a more efficient way and will be able to compete, rather than that people will get out of that industry and let a flood of imports come in.

Senator BUSH. Well, this is a very hopeful statement which you make, I must say, Dr. Wallich.

The President has indicated, and it is in the bill, that the most favored nations policy would continue under this new plan. This means, of course, that if we make tariff adjustments downward with the Common Market, these same adjustments will be available to all trading nations who trade with the United States.

But do you not think it would be appropriate for us to insist that the Common Market countries, like ourselves, all working together in the interest of preserving a free world—that the most favored nations policy should be adopted by them as well as ourselves?

Dr. WALLICH. Yes, sir, I think that is really quite essential. We will make these concessions worldwide; Japan, for instance, will get the benefit of the concessions we make to Europe.

Senator BUSH. I noticed in the Washington Post in recent days two articles about Japan, written by Alfred Friendly, who is out in Tokyo. The first one is entitled "Japan Mystified by U.S. Policy," and the second one is headlined, "Second Fiddle Trade Role Feared by Japan."

In other words, they fear they are going to get left out of this thing. And then the headline on the top of the succeeding page: "Japanese Fear Desertion by United States Following Talk with Inner Six."

Our Attorney General is out there. He is supposed to be on a good will mission, I presume. I hope he will give the Japanese assurance that we do not intend to desert them. And I hope that we can somehow provide in this trade bill that the most favored nations policy must be adopted by the Common Market Six if we enter into agreements with the Common Market Six.

I do not think it is fair, frankly, for them to just run a little mutual protective society at this time, which is the basic purpose originally of the Common Market Six, which was to promote trade within those countries and to raise tariff barriers without.

But in view of our very serious balance-of-payments problem, I think it is the most serious overriding issue we have in our whole picture. It does seem to me that we are justified in calling upon them to be more cooperative along the lines that Mr. Reuss has suggested, particularly, I think, along the lines of recognizing that they, too, have a free world responsibility toward the countries of Latin America, and of Japan and the Far Eastern countries, which are struggling hard in this cold war in defense of the free way of life.

What these other countries are doing is very important to the Common Market countries, which are right under the gun, so to speak.

Well, I did not mean to make a speech, but your comments inspired me to say something along that line.

Chairman PATMAN. Before yielding to Senator Proxmire, I would like to get Professor Hansen's view on present-day problems and trends, and I wonder, Professor, if you are disturbed or alarmed about them.

I will be more specific. In the last few years, the trend has been for people to move to the cities, to leave the country, some for an obvious reason—necessity. It appears that in a few years from now most of our people will be in a few large cities.

The community life is drying up in many of our fine communities throughout this Nation, in smaller towns and smaller cities, and everything seems to be moving to the big cities.

Now, of course, the older people, a lot of them, move to the cities because they can get better services there, such as hospital and medical care, and other people move for reasons of economic necessity.

Now, then, the smaller towns have an awfully difficult time. The pitiful thing about it is that most of the businesses in the small towns are owned by absentee owners. And the seed corn money that would normally stay there and pass around among the people from one person to another from 25 to 50 times during the course of a year just leaves overnight.

The facts show that about 50 percent of the business profits of America move into two centers, New York and Chicago—50 percent of the business profits of America.

Well, that means that they are being taken away from other parts of the United States.

And I just wonder if you consider it a healthy trend or an unhealthy trend; if you believe it creates problems; and if so, what do you think ought to be done about it. We would appreciate your consideration.

Dr. HANSEN. Well, I think you have asked a very, very general question.

Chairman PATMAN. Yes, sir, I have. But I consider it a very important one.

Dr. HANSEN. I suppose my answer in the first place would be that this trend to the urban communities, appears to be an inevitable tendency growing very largely out of the fact that we are experiencing this enormous increase in agricultural productivity, so that instead of having 80 to 90 percent of our population engaged in raising food, as we did a hundred years ago, we have now reached a point where it is only 8 percent of the population. We have almost reached the point where, so to speak, we have complete automation in agriculture, with nobody engaged in producing food any more.

This is certainly an economic fact, and this is I think the basic reason why our population is moving into the cities.

So that I should say that the thing to do is to recognize this movement and to realize that more and more our problems are urban problems, and consequently, I should very much favor establishing a Department of Urban Affairs.

We have this tremendous growth of urban areas, with a larger and larger percentage of people in our cities, and this creates problems of community living which we have not begun really to tackle. This is the big problem.

As far as the domestic problems are concerned, this is the big problem. And I do not see any chance of reversing the trend of population movement. I think we will have to tackle this problem of how to meet our urban problems, transmit and all the other problems that are involved.

I think we are going to have a very tough time to meet these problems, and we have not begun to scratch the surface yet.

Chairman PATMAN. Thank you, sir.

Senator Proxmire, you are recognized.

Senator PROXMIRE. Thank you very much, Mr. Chairman.

I want to apologize to Professor Hansen for not being here earlier. I was testifying in the House on the milk resolution.

I recall sitting at your feet at Harvard, Professor Hansen. The last time I saw you, I think you were giving me an oral examination for my Ph. D., and you were asking the questions. This time I am. Unfortunately, the sad difference is that you were able to vote me a grade, but I cannot do the same for you.

My first question refers to the little exchange we had, when you criticized my dissent to the Economic Report last year in a letter to the New York Times.

Now, in your statement, you support the temporary tax cut proposed. I would like to ask if you think the proposal framed by the President is adequate, since it is a $5 billion tax cut in a $550 billion economy, and it is limited to 6 months at a $10 billion annual rate. Do you think that this, together with the public works proposal, in your judgment, as probably the outstanding expert on business cycles in the world, will do the job?

Dr. HANSEN. Well, Senator Proxmire, that I think is a very difficult question to answer in terms of figures.

Five billion dollars, if extended as Henry was suggesting, to a 12-month period, is $10 billion, and then the $2 billion of public works is, after all, a considerable amount, in view of the fact that the declines that we have had in our recessions in the postwar period have not been of the character that we had in the 1930's, for example, and this is a very considerable offset. And if this offset comes early in the recession period, then I think it might do the job.

I do not know how one can really answer that question beforehand. But I would like to start with this. I think this is enough to start on.

Senator PROXMIRE. In terms of our historical experience, though, as you know, we ran deficits that averaged 4 percent of the gross national product in the 1930's. This President's proposed tax cut would be a 2-percent addition to whatever deficit we might have, and it is limited to 6 months, by law. Therefore I wonder if it would be adequate. If it is not adequate, then are we not in a position of continuing this pretty much indefinitely, without any adequate historical experience to support the view that we can move our way out of a recession or depression by the deficit route?

Dr. HANSEN. Well, my feeling is that in the 1930's, if we had really hit the thing on the head when it came, we would not have needed such a terrific deficit. The thing had accumulated so.

Recently I found Lord Keynes had recommended a deficit of $5 billion that looked rather big in a period when the gross national product was only about $60 billion; but in terms of the present gross national product, that would be $40 billion.

Senator PROXMIRE. That is my point.

Dr. HANSEN. But this was at the bottom of the depression, when we had already gotten down to that terrifically low level. If we had hit it right on the head, we would not have had the decline, either in investment outlays or in consumption outlays that we had, and a very much smaller deficit would have done the job.

Senator PROXMIRE. Did we not hit it on the head in terms of an enormous deficit, an automatic kind of a deficit, in relation to our gross national product? The equivalent would be an average deficit for 10 years at $20 billion a year, would it not? We never did come out of the depression.

Dr. HANSEN. This is true, but it is because of the prolonged downward cumulative process.

Now, I would say that if we had really hit that depression on the head at the beginning, the magnitude of the deficit, contrived deficit, would have brought expansion countering the decline in investment immediately, and we could have gotten by with very much less than the figure that you suggest, which I think is based on the cumulative downswing.

In addition to that, I think the factors making for a depression at that time were extraordinarily powerful, and I do not believe we are facing such powerful recessional influences as we did at that time. So that at that time we probably would have needed a much larger contrived deficit than we would need at the present time.

It may very well be that you are right that these figures are not large enough. I would be inclined to entertain that view. But I think it is tremendously important than we do hit this next recession, and not allow it to develop as we have all the other recessions we have had in the postwar period.

And this figure of $5 billion, extended to another $5 billion in the 12 months, and then the $2 billion of public works, might be enough to do it. I would not be prepared to say that it surely would be enough.

Senator PROXMIRE. You see the position this puts us in. It might be enough to do it. For 6 months it is a $7½ billion deficit. The experience we had in 1959 was with a $12½ billion deficit.

We are considering a proposition that would increase greatly the burden of the national debt on a basis that is the burden of the national debt in some things that seem to be economically questionable in view of our experience, because we never did come out of the depression of the 1930's by this route.

Dr. HANSEN. Well, of course, that needs long discussion to really answer that question.

You may be quite right that it would be wiser to make it $10 billion for 6 months.

Senator PROXMIRE. I want to make it clear that I am not advocating the $10 billion.

Dr. HANSEN. It might very well be so.

Senator PROXMIRE. I am not advocating that. I am just saying that this kind of method for overcoming the depression may not be satisfactory.

Now we get on to the next point you make. Why do you think it might be advantageous to have a 4-year guideline, instead of 1 year?

Dr. HANSEN. Yes, I just mentioned four, because I would like to extend it into the future.

Senator PROXMIRE. I think it is a very interesting and constructive proposal, but it seems to me in view of the state of development of the economic art or science, to try to look into that clouded crystal ball for 4 years would put the advisers on the spot quite seriously.

Dr. HANSEN. No, I do not think so. The required rate of growth is not some fictitious figure. It is based on the growth in the labor force, which one can calculate quite well in 4 years. That part is pretty definite. And it is based on the increase in productivity.

Now, to be sure, while the trend increase in productivity can be estimated fairly definitely, you cannot estimate it from year to year. That fluctuates quite a little. And here is the one element that is uncertain.

But that makes no difference from the standpoint of getting a perspective. And that is the real purpose of the projection into several years. And there is one element here that I think is very solidly based on statistics; namely, the increase in the labor force.

Senator PROXMIRE. You say that the budget is now smaller in relationship to the gross national product, or will be, in 1963, than it was in 1955. And you are talking about the administrative budget. If you add transfer payments, I find that the budget will be bigger by 1 percent.

In other words, in 1963, the budget, if you add the 6.5 percent for transfer payments, projecting roughly, would be 22.4 percent of the gross national product, as compared with 21.4 in 1955. So that this would be bigger. And it seems to me this is a better measure than excluding transfer payments.

Dr. HANSEN. I agree. The only point I am making here is that one can in a meaningful way appraise the size of a budget by relating it to the gross national product.

If you wanted to relate it to the national income accounts budget, that is quite all right, and that might well show that this budget was larger, indeed, han the national accounts budget in 1955.

But the only point that I am making here is that I feel that we mislead ourselves, and we just cannot make correct decisions if we are thinking statistically about our economy.

Talking about records being made—what does a record mean? It has no meaning except in terms of a dynamic society, measured against the prospect of growth.

Senator PROXMIRE. In terms of the static versus dynamic view of the economy, it is interesting and very refreshingly frank, I guess, that you express disappointment that the Federal purchases are not bigger, that we do not have a bigger Government, bigger activity on the part of the Federal Government.

It seems to me, however, that in view of the fact, as I have indicated, that there is an increase in the relationship of the national accounts budget to the gross national product—it seems to me an irrefutable truism that the bigger the Government is, the less the freedom of the people involved. As Government goes from 20 to 25 to 30 percent, obviously it takes more of the income of people in taxes, and you have less freedom to spend your money.

Isn't this something to be concerned about on the moral level, perhaps, other than the economic technique of trying to stimulate growth?

Dr. HANSEN. Well, take the matter of the size of the budget. If you take the Government outlays of goods and services in real terms, correcting for price changes, they did not grow a bit from 1955 to 1960. In fact, there was some decline in the Government purchases, Federal Government purchases of goods and services. There was also a slight decline in private investment from 1955 to 1960, in real terms. And the whole gain in gross national product in real terms in that period was in State and local outlays and in private consumption.

Private consumption was stimulated by transfer payments in part and in part by consumer credit. But the whole gain in real terms in GNP came in State and local government outlays and in consumer outlays. The Federal Government outlays on goods and services did not increase at all, but declined a little, in that 5-year period.

And I would say we must think of the use of all the resources. The Government outlays ought to be decided in terms of social priorities. What is the best use of our resources? And in those terms, the budgets should be made and taxes should be adjusted then to that budget in a manner that would contribute to full employment.

That leaves, then, the rest of the productive resources for the private areas that you were concerned with. And surely the proper thing, the logical thing, the rational thing, is to try to decide Government expenditures in terms of social priorities, what society needs.

Senator PROXMIRE. I think that is a very logical and very persuasive answer, except that it seems to me that given the social priorities, it leaves out the fact that the individual has less discretion over his income than he had before.

And you throw in something else that makes my point even more emphatic, and that is to emphasize that the State and local governments have grown even more rapidly in relation to the gross national product. So the tendency of all government to impinge on the American citizen and take a larger and larger share of his income seems to be growing.

I would not for a minute discount your analysis. I think you are right. But I say there is something else we have to consider at the same time, along with social priorities.

Dr. HANSEN. Well, the private citizen—I would say the things he wants government to do for him are just as important as the things he wants to buy in the market. And you are not denying the private citizen his choice by voting public budgets.

Senator PROXMIRE. Ah. Here is the point. The things the government does for him are of a different nature in terms of his initiative and volition. He is a part of the collective mass that votes, but he has no individual choice.

Dr. HANSEN. No individual choice. But in modern times, if we are going to leave everything to the market, especially with the growth of communities, your individual choice would not be worth very much.

Chairman PATMAN. Senator Javits?

Senator JAVITS. I would like to ask both professors a question. They are equally eminent and seem to have a common finding, which I think is very important.

Professor Hansen, you say in your statement—and I, too, did not have an opportunity to hear it orally, because we had to confirm a new Comptroller of the Currency and had a few questions for him.

You say:

> From a static point of view, both private investment and Federal outlays, the goods and services seem large. From the dynamic point of view, their contribution to growth was seriously inadequate.

And Professor Wallich says, at page 8:

> In view of all this, it is difficult to avoid the conclusion that we have not yet come to grips with the real problem of raising economic growth.

I take it, therefore, though you do not use the same words, that you both agree that we have talked a lot about growth, and the economic advisers have written a lot about growth, but they have not yet recommended what needs to be done to really attain measurable growth; and though Professor Wallich likes the investment tax credit, he points out it is a billion and a half against $80 billion, which is the aggregate investment in plant and equipment, et cetera.

Now, could you gentlemen therefore tell us, in your own way, what you would like to see the Council of Economic Advisers recommend, or perhaps what some of us could recommend, which would really contribute to growth, as you both seem to feel that the recommendations made are inadequate?

Dr. HANSEN. Well, I would like to begin by referring to Mr. Wallich's suggestion about agriculture.

The U.S. Government has for a period of I suppose now about 100 years been putting in a lot of money in agricultural research. This I think is the basic reason for the increase in productivity in agriculture: The research over all these years that the Federal Government has been putting into agriculture.

This is one way to stimulate growth. We are doing much more in research now, technological research, than before, but we could do still more.

But I think fundamentally we would have had greater growth since 1955 if we had had two things, larger outlays in real terms in private investment, and larger outlays in real terms in Federal Government outlays on things that do promote growth, like education, investment in natural resources, and in research.

These are the two things, in my judgment, that promote growth, namely, large private investment outlays, large Federal outlays, on the things that tend to promote growth. And that covers a wide range of Federal outlays.

That would be my answer.

I might add that you could not expect any large rate of growth in the United States when in real terms private investment and Federal outlays in goods and services did not rise. And that is what happened.

Dr. WALLICH. I agree with Professor Hansen on the great importance of private investment outlays in growth, plant and equipment. I think those have been inadequate. They are far below what they are as a percentage of GNP in countries like Europe and Japan.

I think there are many Federal expenditures that would be helpful, such as for instance education, which I would like to see, and natural resources.

At the same time, I think I said on page 5 of my testimony that I am disenchanted with what we got by increasing Federal expenditures by $11 billion in the administrative budget over 2 years. That ought to have helped us get a lot of growth, but it does not seem to have done a great deal for us. What has come of it? Not even a program for education.

So I feel that the principal burden has to continue to rest on private investment.

There are, however, some other things we can do.

One is to run a surplus in the Federal budget, which is a form of saving. This saving is fed back into private investment by repayment of public debt, which enables the banks to lend more, and enables private investors to lend more. Then we can have more investment.

The difficulty is to get these savings channeled into investment. Suppose banks get their Government debt repaid. What causes them to lend to a private firm?

To expand private demand for loans calls for tax reform, and it calls for an appropriate monetary policy; as easy as the circumstances of the balance of payments and the inflationary pressures would permit.

This would be my prescription: Some good Federal expenditures, but principal emphasis on private plant and equipment, aided by tax reform, Federal surpluses, and appropriate monetary policy.

Senator JAVITS. Now I would like to address a question to each of you on what you have just said.

Dr. HANSEN. Senator Javits, could I make just a comment on that, first?

On this matter of a Federal surplus, if you once, by whatever factors that accidentally came into play, reached full employment, then of course Federal surplus is necessary in order to have balance in the system. And then you can use these funds, as Henry suggests, for investment.

But if we start now with the idea that now we are going to get growth by developing a surplus, and so therefore let us now proceed to cut expenditures or to raise taxes—that is not the way to get growth.

Senator JAVITS. Now, Professor Hansen, you have mentioned agriculture and its expansion and productivity. Therefore would you regard the President's proposals to restrict agricultural productivity as being counterproductive in terms of growth?

Dr. HANSEN. I would be in favor of the income payments plan for agriculture. I would drop the price controls completely and let us have a world price for agricultural products. And instead of letting farmers completely go bankrupt, I would use the income payment system.

Senator JAVITS. So that you would favor continued high production and utilizing the agricultural products as food for peace?

Dr. HANSEN. Yes. I would say that one of the most important things we could do would be to scrap the price controls completely and introduce the income payments.

Senator JAVITS. Therefore you do not look with satisfaction at the present proposals of a farm policy which is based essentially on even more sharply curtailed production?

Dr. HANSEN. No; I personally do not.

Senator PROXMIRE. I would like to ask Dr. Hansen whether or not he has had a chance to study the President's program as set forth, for instance, in the food and agriculture document I hold here in my hand.

Dr. HANSEN. All I know is what I have been reading in the New York Times.

Senator PROXMIRE. I suggest there are other sources that are a little more comprehensive on this particular subject.

I would like to say this is not a restrictive program in any sense. There is no reduction in research. It certainly is a complete misstatement to say the President has asked to restrict the productivity of our farmers. As far as the production is concerned, there is a very, very carefully worked out program to see that we make the most abundant use of our food production, here in America and abroad. And far from reducing the so-called food-for-peace program, in this excellent document, which has been painstakingly prepared by the Secretary of Agriculture's food and agriculture program for the 1960's, there is assurance of how the food-for-peace program is going to be expanded and the way it is going to be expanded and the very great dimensions of this expansion, as pointed out. A very large proportion of the foreign aid program is financed through the American farmer and charged to the American farmer in the budget because of programs like Public Law 480.

Dr. HANSEN. Could I comment on that, Senator Proxmire?

Senator PROXMIRE. I wish you would.

Dr. HANSEN. I did not state that I was opposed to any part of the program which continues research and increasing productivity. My answer simply was that I would favor scrapping of the price controls.

Senator PROXMIRE. I understand. I will get to that next.

Dr. HANSEN. So I was not criticizing the program on the grounds that you are now discussing.

Senator PROXMIRE. Would you favor what used to be called the Brannon plan?

Dr. HANSEN. That is correct.

Senator PROXMIRE. In other words, you recognize that farm income is inadequate?

Dr. HANSEN. That is right.

Senator PROXMIRE. That it is only half of the income people have off the farm and the hours are longer, the investment is greater, the risk is greater and efficiency has increased faster.

Dr. HANSEN. Yes.

Senator PROXMIRE. Now, first, in general, all other Americans, virtually all other Americans, with some exceptions, get their income in the marketplace. Secondly, the farmers represent a constantly diminishing proportion of the population. If you have him produce as much as he can and throw it on the market, under the Brannon plan, as I understand, and get whatever price it will bring, and then make up the difference in compensatory payment, will this not mean he is going to have a colossal overproduction, because people are not going to consume much more food in this country? We consume almost exactly the same amount as we did 30 years ago. The price may go down very low. And, therefore, this compensatory payment would have to be a very large proportion of the farmer's income. Thus he would become dependent, as a small minority, on the other 90 percent of the population to make up this difference through taxes, a grim prospect for the farmer.

Dr. HANSEN. I see no particular difference. He is dependent upon the country now for his income.

Senator PROXMIRE. Oh, yes. I disagree with the present system completely. I think it ought to be scrapped, too. But I just want to suggest one other thing.

With every other industry or economic factor we have a limitation on production, whether in labor, in manufacturing, whether it is the merchant who refuses to sell below a price generally that will give him cost plus his particular expenses and a small profit. This is true within the professions. It is true generally.

Now, if the farmer is not enabled, with some cooperation from Government, which can be very minimal, to limit his production to what he can sell at a fair price, it seems to me we are going to disadvantage him.

I am not asking for the usual kind of price supports. I just say: Isn't it possible to say how much we can usefully, constructively use of our food production, and then permit the farmer to produce his share of this, so that he can limit his production the way the American Motors or Ford Motors or General Motors does, instead of putting him in a position where he has to run his assembly line, so to speak, 24 hours a day, 52 weeks out of the year, and produce food which one way or the other is not going to be able to be sold? Isn't that a very wasteful thing to be able to do, to operate under the system you propose, or the system we use now?

Dr. HANSEN. The problem, of course, is an extraordinarily difficult one. There are no easy answers here, at all. But I would be inclined to think that if we removed the price controls and supported the farmer with income payments, this system would gradually lead, over time, better than the present system is able to, to an equilibrium position.

I do not know how soon that might come, but you would be in a stronger position to move over to an equilibrium position in agriculture if the prices were not rigorously controlled, if you allowed them to seek the world market price.

And I do also agree there would be a larger consumption. And the consumer would get a tremendous benefit out of the low prices.

Senator PROXMIRE. I think that is true. The consumer gets a tremendous benefit now. The fact is, as you know, the only reason that the cost of living was stable last year was because food was the only element in it that dropped.

Dr. HANSEN. I fully agree. I have pointed out elsewhere that we talk about all the subsidy to farmers, and as a matter of fact, the farmers are contributing more in productivity than any other section of the community, and even with the subsidy we have been getting our food prices cheap relative to other commodities.

Senator PROXMIRE. I am delighted to hear you say that.

Senator JAVITS. And now, Professor Wallich, can I ask you a question about private investment?

Both of you agree that there is inadequate private investment. You have pointed out that the tax system somewhat inhibits private investment, and of course there are many variables in that, including the capital gains tax.

But I would like to ask you whether there are any economic factors that inhibit private investment. For example, do you think the climate in this country in labor-management relations is such as to encourage or inhibit private investment?

Dr. WALLICH. Well, I think one can certainly trace a good many instances of investment restraint to this. One can also, I think, trace some instances on the opposite side. For instance, there is the fact that wage pressure creates a certain amount of investment that tends to reduce the use of the labor force.

But basically, I am sorry to say that I think the stance of labor is not conducive to increased investment and increased growth. As long as the policies of the Nation aimed chiefly toward evening up the distribution of income, the policies of labor, moving in on profits and cutting them down were appropriate.

But in a country that wants maximum growth rather than maximum equality of income, it is unfortunately true that a certain amount in inequality of income must be tolerated.

In the long run, labor will be better off by allowing business an adequate rate of profit and letting it invest more. That will raise productivity faster; then wages can go up faster.

The present policy of labor, I fear, is defeating labor's own interest. Labor seems to want to restrict all actions that would give business a chance to get funds for more investment. In doing so they restrict the growth of productivity and ultimately the growth of wages.

Senator JAVITS. Professor Hansen, may I ask—because I would love to have your comment; and I only have a minute—what you would think of the sidewise movement of labor, which I have been urging for labor itself at labor union meetings and conventions, into profit sharing and stockownership? Would that meet the point which Professor Wallich has just raised? That is, a sidewise movement away from Sam Gompers' famous word "more," and profit participation through stockownership and profit participation plans?

Dr. HANSEN. Well, this is a proposal which is really a very old one, and there has been a good deal of experimentation with it. I think over time in past history the record has not been too favorable.

Now, this grows out of the fact that you have profits and you have losses in business; and profits are all right, but the losses side is not so good.

Now, it may be that we have reached a situation in our economy where, well, the profits are certainly far more stable and we do not have such terrific depressions as we used to have in the 19th century. And we have collective bargaining, under which these profit-sharing schemes can be controlled in a way that was not true in the earlier days, when these schemes failed.

So I would not be unsympathetic with your suggestion. I think under present conditions, it might very well work.

Senator JAVITS. May I have permission to get Professor Wallich's comment, Mr. Chairman?

Dr. WALLICH. I think if this is not the ideal, it is certainly the most feasible way of reconciling the interest of labor with the need for greater capital accumulation. In that way, the recent automobile industry contracts point a hopeful way.

But I share Professor Hansen's concern. What happens when profits go down? Does that, then, lead to added wage demands to make up for the loss of dividends?

And very broadly, I have this concern: If, for instance, one were to propose that part of undistributed profits be shared by labor, this would lead to a substantial increase in labor's ownership interest in industry. It would not take very long before labor would become a very powerful factor in management. Union members would yield proxies to the union. The union would vote these stocks. They would certainly be on the boards of directors.

I would recommend in that care that labor unions be treated like registered investment companies, namely, that they would not be in a position to vote stock.

Senator JAVITS. I thank the gentlemen very much.

Dr. HANSEN. Senator Javits, on this point, I would like to direct the committee's attention to that chart in the Council's report showing the movement of profit margins in relation to the gross national product. I think that is a very significant chart, showing that the decline in profit margin relates a great deal to the fact of inadequate demand.

If you could have adequate demand and full utilization capacity, the squeeze on profit margins would largely disappear.

Chairman PATMAN. Mrs. Griffiths?

Representative GRIFFITHS. I would like to ask Professor Wallich: What effect do you think the investment tax credit will have on prices? Do you think that the overall effect will be to make prices more competitive?

Dr. WALLICH. I think so, Representative Griffiths. It will if it has any effect at all. The effect I think is going to be favorable, but not very large. It will lead to an increase in equipment purchases, and in that way is likely to lead to greater productivity and perhaps lower prices or less high prices.

In that respect, it is in a sense preferable to accelerated depreciation. There, the danger exists that it will lead to a change in cost accounting, with higher depreciation being charged into unit cost, leading, then, to the possibility of higher prices.

Representative GRIFFITHS. In your judgment, generally, will the effect of the tax bill, if it is enacted as proposed, be to reduce housing?

Dr. WALLICH. Well, I think it will increase plant and equipment expenditure. Now, I do not think one needs to expect an absolute reduction in housing; although it might happen.

There may be effects on both sides. Certainly the taxation of some of the sources of housing finance, like the savings and loan associations, will be a minus. On the other hand, if the tax credit leads to higher investment, since the administration thinks that it will increase investment by more than the $1.5 or $1.8 billion of the credit itself, then the national income will rise, and we will get closer to high capacity operation, and over the years we will grow more rapidly.

So in absolute terms, I think housing will probably benefit, even though relative to plant and equipment expenditure housing may be getting a little less.

I must add that I think very many factors in our financial system channel resources into housing, and not nearly enough help to channel resources into plan and equipment.

Representative GRIFFITHS. In your judgment, would the longrun effect of a closing of the tax havens adversely affect our balance of payments, or improve them?

Dr. WALLICH. In the long run I think it would adversely affect them. By "tax haven," we mean broadly all foreign operations where the tax situation is more favorable, and not just the, let us say, Bermuda kind of operation. On that I would have no judgment, and I do not know if it is quantitatively large.

But in the long run, over, say, 10 years or 15 years, I think foreign investment, particularly direct investment by corporations, builds up a stream of income that exceeds the outgo.

It is like a family putting money in the bank. After a while, they get more in interest than they are putting in in annual payments. And because profits on direct investment tend to be rather high, this turnabout comes much more rapidly than it would come in the case of a family putting money into the bank. In fact, in the aggregate, of course, this favorable constellation, receipts being larger than expenditures, already prevails.

Representative GRIFFITHS. On your statement you point out, regarding the tax bill and regarding the matter of the taxing of savings and loans, that you would support some if not all of these actions. Would you care to say which you would not?

Dr. WALLICH. I feel particularly skeptical about the 4-percent dividend credit removal.

I do not for two reasons. First, it concerns me to see a source of saving removed. It is not a condition where as in the case of the savings and loans associations, somebody is paying practically no tax at all.

And certainly it concerns me that in 1 year the administration is proposing to remove what one might call "gimmick" from the tax structure and introduce another "gimmick"; namely, the investment tax credit.

Now, it is not going to be very encouraging to business to see how easy it apparently is to remove that kind of thing from the tax structure. It means that the life expectancy of the investment tax credit may also be very short and that it may be thrown out of the law after a few years.

Representative GRIFFITHS. I have raised some question about this, and I think once it is in it will be permanent. But thank you very much for your views.

Senator DOUGLAS. I want to apologize to the witnesses for not being able to come earlier in the session.

I have had a chance to look hastily over the papers. I would like to ask this general question and perhaps make a further statement.

In 1958 I urged a temporary tax cut as a means of offsetting the decline in the reduction in employment which was then setting in. This, of course, was not accepted. I was therefore pleased that the

President recommends an anticyclical adjustment of the income tax rate. In general I approve of this, but there are certain problems connected with it that I think we should go into.

The first question I would like to raise is this: Once the cut goes into effect, will it not be very hard, as a matter of fact, to restore the original rate?

I would like to ask the opinion of Dr. Hansen and Dr. Wallich.

Dr. HANSEN. The understanding is that you would automatically go back to the old tax rate after 6 months; so that the tax cut is per se a temporary tax, and it would require new legislation, as it would now, to cut the basic rate.

Senator DOUGLAS. It could be continued, could it not, by decision of the President, or decision of the Congress? It is always easy to lower taxes and hard to increase them. And the question I want to raise is whether the pressures which this would engender in a business community and the general public would be such as to make it very difficult to restore the original tax. And would it not always be claimed that by restoring the original tax you are choking off recovery?

Dr. HANSEN. For that reason, I would prefer the antomatic device, by which the thing is adjusted according to a statistical series and not by a decision of the President. I would prefer the automatic device, so that no decisions are being made at all.

Senator DOUGLAS. And what criteria would you use in determining this? an index of production? gross national product? relative to volume of unemployment? the price level?

Dr. HANSEN. I think production and unemployment indexes.

Senator DOUGLAS. And would you develop a wage system for these two?

Dr. HANSEN. Yes; I think in all of these matters we cannot hope to reach perfection, but I think the unemployment index and production index would be quite satisfactory guides.

Senator DOUGLAS. You would not include the price index?

Dr. HANSEN. I would not; no.

Senator DOUGLAS. So that you could get decisions as automatically as an automatic computer will determine the velocity of missiles?

Dr. HANSEN. Yes. In the course of events, things might happen so that we would need deliberate action. But this automatic device would minimize the need for deliberate action as against the situation that we have now.

But I would not sit by and allow these automatic movements to bring us into a state that we all would agree was not a sound one. We should act then. But we have to act now. And I think the calls for action would be less under this automatic system than it is now.

Senator DOUGLAS. Dr. Wallich?

Dr. WALLICH. I agree strongly, Senator Douglas, that there is a tendency for temporary tax cuts to become permanent. We have the corporate tax rates that are temporary since Korea. We have various excises in the same catgory.

For that reason, if it were at all feasible—and I hesitate to believe it is—I would prefer something in the nature of a tax holiday for a very short period, 1 month or at the outside 2 months, reducing rates not by one-quarter but perhaps by one-half, or better by 100 percent.

Senator DOUGLAS. That I think was Mr. Yntema's suggestion in 1958, in the Vice President's report.

Dr. WALLICH. Yes. We have always had this suggestion. And I think it has the great virtue of overcoming the problem that you raised, because it seems pretty clear that this cut would have to be reversed.

Now, it is true that there is some doubt about the effectiveness of a quickie windfall of that kind. But I should think that that is a matter of a few percentage points, and not a matter of all or nothing.

Now, if I may address myself to the triggers of the automatic system discussed by Professor Hansen: With due respect to what he said, and to the possible virtues of the scheme, I am impressed by two facts.

First, the behavior of the unemployment index in the recent recession—one had a feeling that things were obviously getting better, but the rate would not come down. People then begin to wonder whether something was wrong with the statistics. And while I think the unemployment statistics are good and honest, nevertheless, it seems clear that the trigger can become mischievous.

The other fact is the particular safeguards that the Council has written into the public works standby authority.

Now, you will notice that some very complicated timing schedules had to be put in here in order to show that in each of the postwar recessions this particular trigger mechanism would have gone off at the right time, would have authorized the President to take action, and would not have been counterproductive.

It is hard for me to believe that in future recessions things will always work out quite that way, and that a mechanism of that kind will not play tricks on us.

Senator DOUGLAS. Well, I take it that both of you will agree that in the use of a tax cut during the period of recession—and your differences are perhaps in matters of amounts and mechanism rather than on the principle itself; is that correct?

Dr. HANSEN. I would like to say with respect to this complete cessation of tax for 2 months, I would feel that that would decidedly reduce the consumption expenditures that would be induced. I doubt that it would be very effective, for that reason.

And on the other matter that Henry was discussing, it is quite true that the statistical guideposts that the Council has set up for the public works might not work perfectly in every recession; but I come back to my point that it works far better than what we are doing now. You may need decisions, but you do not need as many decisions as you now need.

Senator DOUGLAS. Does anyone else have any questions?

Senator BUSH. Yes, just one, if I may, Mr. Chairman.

Senator DOUGLAS. I came in late. I did not realize that you had not had a chance.

Senator BUSH. I have questioned, and I am on my second round.

On this automatic tax cut, this thought has occurred to me, Professor Wallich. I particularly address this to you. If we are running along with a budget surplus of $2 or $3 billion a year for several years, and then we suddenly run into a recession of substantial proportions, I can see where we might immediately cut taxes. While it would increase the deficit that was probably going to come anyway, we would have been having surpluses, and the inflationary effect of a deficit might not be very important at that time; whereas if we had been running along with deficits, and then we come to a recession, and then we put in a big automatic tax cut and cut $5 billion, $4 or $5 billion, and add that to the deficit, and in view of the fact that under those circumstances it is most likely that the financing of this deficit would have to be done through the banking system, which would add substantially to the money supply—my question is: Would not the inflationary effects of this type of operation to some extent, if not the whole extent, offset the desirable consequences of a tax cut?

Dr. WALLICH. I think, Senator Bush, this is a very real danger, because we have experience with it. All through the 1930's, we built up a very large money supply, partly through capital imports, partly through deficits. Then we added tremendously to this during the war, and came out with a great monetary overhang.

We know from that experience that an excess of money supply built up in recessions or under periods where prices do not rise because of controls can come to life and can become very inflationary later on.

So if we had been building up liquidity rapidly as a result of bank-financed deficits and then struck a recession and were faced with the problem of whether to create another large bank-financed deficit, we would have to take that very seriously into consideration. I would say that would be a limitation on the size of the deficit, particularly if the balance of payments is weak.

Now, one possible way of coping with the dilemma is to provide for the sound financing of deficits. I would like to see conversion of some short-term debt into long-term debt.

In the present recession, that has not been done. There was a reason for it. The authorities wanted to keep the short-term rate relatively high, for balance-of-payments reasons. It seemed convenient to throw a lot of short-term debt into the market.

But from the point of view of making sure that we are not building up inflationary fuel that will come to life in future expansions, we have to watch that short-term debt buildup.

Senator PROXMIRE. I would like to ask, Dr. Hansen, on another subject: You mentioned investment and research, as I understand it, as the principal ingredients in growth. Are you not too modest about your own profession? Unless you would include, somehow, research as education or investment?

Dr HANSEN. I mentioned education, and investment in natural resources, and so on.

Actually, when one compares our situation with Europe, investment in Europe includes public investment, which is a very large part of the European investment. So this makes a very big difference, comparing European investments to our investment.

Senator PROXMIRE. I am delighted to see your comparisons on structural unemployment in Western Europe. It is a real contribution. I agree with you wholeheartedly on structural unemployment.

Dr. HANSEN. On that point consider our definition of "unemployment" and the English definition of "unemployment." Whether the English used our method or their method does not make very much difference. If they use our method, the figures are practically the same despite the fact that they do not include (as we do) the youngsters who are looking for work but have never had a job. In our system we have 20 percent of our teenagers who are unemployed. In contrast their teenagers get jobs readily.

Senator PROXMIRE. And what you are saying is——

Dr. HANSEN. Is that they have similar problems of rapid automation. But demand is high, job opportunities are plentiful, but in spite of that, they are not suffering from a runaway inflation, and they have virtually full employment in the Western European countries. They have of course had moderate price increases.

Senator PROXMIRE. Now, you talk about the impact of foreign competition on the wage spiral. I think this is the most important of all, really, that it does promote stable prices. But isn't the effect of this quite limited? That is, it will not apply to services, obviously, many services. It will not apply to transportation, except, to limited extent, for cars. It will not apply to medical costs and so forth.

Dr. HANSEN. You are quite right. Again I would like to emphasize the point that when people talk about inflation they forget that the only period after the Korean war in which we had any important rise in prices was in 1955–57. And it was limited to a certain area. The Council points that out quite rightly. I am glad to see that, because it has been overlooked by most people. There was very little price rise in the economy as a whole. It was concentrated in the area of durable manufactured goods and related fields.

But that relates to wholesale prices. You are quite right as to the services.

Let us assume that wholesale prices are stabilized. We will then have to assume that the Consumer Price Index will rise, because of the continued rise of the service index. The service index is bound to rise so long as money incomes are rising, in line with increase in productivity, because there is no improvement in productivity to speak of in the service area, or relatively little; so that we have to expect a rise in consumer prices if we have stability in the wholesale price index.

The foreign competition does not affect that area. You are quite right.

It affects, however, just the area where we got the wholesale price rise in 1955–57. I come back to that as a very important point.

I very much disagree with people who talk about inflation in this country without defining what it is they are talking about and what period they are talking about and what area of the economy they are talking about.

We had a price rise in the general economy in the boom of 1955–57, which was considerably less than the average price rise we had had in business cycles from 1894 on to 1929, omitting the World Wars. In nine cycles, the increase in prices was about 3.5 percent. And outside of the metal industry, the rise in price in the 1955–57 boom was less than 2 percent per year.

Senator PROXMIRE. I would like to ask Professor Wallich could you give us your opinion of the difference, to the extent we can evaluate them at all, between promoting expansion by increasing Government spending and taxing in a balanced way, on the one hand, as compared with doing so by the deficit route on the other?

The OECD, for instance, had a kind of a shocking recommendation—shocking to me—that you can do it by balancing your budget, by just having greater Government spending and taxing, too.

Dr. WALLICH. I think it can be done both ways, Senator Proxmire. The way of the deficit I would judge to be something like two to three times more effective per dollar than the other.

Senator PROXMIRE. On what basis do you arrive at that conclusion?

Dr. WALLICH. That becomes a very technical matter, of course. The so-called multiplier of Government expenditure is of the order of 2.2 to 2.3 or maybe larger. That multiplier disappears when expenditures are offset by taxes.

There is something that used to be called the balanced budget multiplier, and some of us had a colloquy in the academic journals on it during the middle 1940's.

It is by no means universally accepted, nor can one expect it to work accurately in the short run. All one can say is that an increase in both taxes and expenditures is expansionary, but that it is less expansionary than an increase in expenditures alone. That is pretty certain. The ratio of 2 or 3 to 1 that I have given is pretty much guesswork.

Senator PROXMIRE. Then I can conclude rather quickly.

I would like to make sure, Professor Wallich, of your position. It is a little ambiguous.

You discuss public works, and you indicate that you can see there are disadvantages in it Do you favor it, or do you oppose it? It is not clear to me.

Dr. WALLICH. I find it a hard thing to decide. If there were a reasonable chance, in the course of a few years, of working out some form of tax cut mechanism, whether that be by Presidential authority or by some kind of prior agreement at which the Congress might arrive, to which we would then go back when the situation arose—I would say we ought to stick to that, and leave variation in expenditures to what can be done by administrative means. These are not small. The highway program has been accelerated; procurement, Air Force, Atomic Energy, GSA, can be accelerated, and order placement can be accelerated. There is something of this kind already in existence.

Senator PROXMIRE. Isn't that acceleration awfully limited? It seems to me that the acceleration the President was able to secure in 1961, at least as totaled up, was a small fraction of 1 percent of the gross national product.

Dr. WALLICH. Yes. Indeed, that would mean $5 billion. That would be a very large acceleration, would it not?

Senator PROXMIRE. I beg your pardon. I should say it was in the order, as I recall, of less than a half a billion

Dr. WALLICH. Yes. I would think that what the President was able to do at that time was very limited; partly, I suppose, because some of the possibilities had been exhausted by his predecessor, and in general what the two administrations could do together was very limited.

But I think we have learned that public works are not the right way to get out of a recession. Only if we were completely hopeless about the tax cut route would I say that we should resign ourselves and take what is very much a second best. It would certainly be better than nothing.

Senator PROXMIRE. Now, why this investment tax credit? Why not key the tax privilege to marginal buying? I thought that was the original administration proposal; because you are losing an awful lot of revenue in order to get, it seems to me, a relatively modest amount of additional buying.

Originally, as I understand it, they were going to simply provide the tax privilege for that increase in buying. This would encourage growth, provide for the small businesses that are moving ahead. Why isn't that preferable?

Dr. WALLICH. I have always thought that that had a great deal to recommend it.

The objection that has been raised to it is that it affects only a limited range of industries. Industries have their expansion cycles, and there are those who just completed their cycle. They would not benefit.

It has been argued also that the proposal is very hard to handle technically. It would raise accounting and tax enforcement problems. And I think there is probably a good deal to that criticism.

Now, given the almost universal skepticism that seems to have developed to this proposal outside the Treasury, I no longer thought it helpful to press for it. I think the sustitute that is proposed now is a perfectly good thing.

Senator PROXMIRE. Just a couple more things. One: You suggest taxation of mutual savings institutions and cooperatives. And you say if you want to give up any of these, you would give up the dividend credit. You would just as soon have them retain that.

Now, it seems to me that you are applying economic perfectionism possibly and forgetting the equity aspect of this. To ask the Congress to tax co-ops and to let the investors go, it seems to me, is pretty difficult to justify on the basis of equity.

Dr. WALLICH. Certainly there are real problems here, as always when one talks about taxing people in the lower brackets and the upper income brackets.

Now, the dividend credit is designed to remedy what has been called double taxation. Whether or not it is double taxation depends upon whether corporations really absorb the corporate income tax, or whether they manage to shift it to include the tax.

Senator PROXMIRE. They do both, generally, do they not? Utilities undoubtedly pass on all of it, because they are permitted to earn after taxes a rate of return. Monopolies, oligopolies, are inclined to do the same. Over time, the tendency is to pass it on.

Dr. WALLICH. I believe that is the picture, a mixed picture. When I was studying with Professor Hansen, there seemed to be more of a tendency to believe that it would be largely passed on. Today there seems to be more of a tendency to think that a good share is absorbed. Now, if a good share is absorbed, then there is some degree of double taxation.

In the case of the cooperatives, if I understand it correctly, only one level is sought to be taxed. Either the cooperative is a business enterprise, or the farmer, the member, is a recipient of income; whereas if the cooperative were to convert itself into a corporation, if I understand it correctly, then two levels of taxation would go into effect, that on the corporation and that on the recipient of dividends.

Senator PROXMIRE. But the proposal is to tax income as included to the individual, and not as the income received. Is that not correct?

Dr. WALLICH. That is how I understand the proposal. But in that case it is taxed at only one level, is it not? It is not taxed like corporate income. It is taxed at the individual level, if I understand the proposal right.

Senator PROXMIRE. That is right.

Now, just one other point.

I am delighted to see you stress that this new extended trade program of the President is primarily a defensive operation, economically speaking. Not only is it useful in stabilizing prices, but I think if we expect to increase our favorable balance of trade of $5 billion, we are being unrealistic. When you consider the fact that other economies are recovering, and they also want a balance of trade, they are deficient now with trade deficits by this $5 billion. We do hope to reduce, relatively at least, our foreign aid program, and military commitments perhaps. If we do so, it is going to be exceedingly hard to maintain this balance of trade that we have that is so favorable now.

Therefore I think to stress the defensive merit is absolutely right, and I am delighted to see you do it. It is a very real contribution.

Dr. WALLICH. Thank you.

Senator DOUGLAS. Thank you, gentlemen, very much.

We meet tomorrow morning in this same room, and in the afternoon as well; in the morning with representatives of management, when the representatives of the National Association of Manufacturers, the chamber of commerce, and the CED will testify, and then the representative of the CIO.

(Whereupon, at 12:20 p.m., the committee was recessed to reconvene at 10 a.m., Wednesday, February 7, 1962.)

JANUARY 1962 ECONOMIC REPORT OF THE PRESIDENT

WEDNESDAY, FEBRUARY 7, 1962

Congress of the United States,
Joint Economic Committee,
Washington, D.C.

The Joint Economic Committee met, pursuant to recess, in room P-63, the Capitol, Representative Wright Patman, chairman of the committee, presiding.

Present: Representative Patman; Senators Douglas, Proxmire, Pell and Javits; Representatives Reuss, Griffiths and Curtis.

Chairman Patman. The committee will come to order.

This morning we continue hearings on the January 1962 Economic Report of the President. We have this morning a panel of distinguished economists representing several national business organizations.

Mr. Theodore O. Yntema of the Committee for Economic Development, who is also vice president of the Ford Motor Co.; Mr. Herbert Stein, research director of CED; Mr. Emerson P. Schmidt, chief economic consultant for the Chamber of Commerce of the United States; and Mr. George D. Hagedorn, director of research for the National Manufacturers Association.

Mr. Yntema, I would like to hear from you, sir, and you may be recognized at this time and proceed in your own way.

STATEMENT OF THEODORE O. YNTEMA, CHAIRMAN OF THE RESEARCH AND POLICY COMMITTEE OF THE COMMITTEE FOR ECONOMIC DEVELOPMENT, ACCOMPANIED BY HERBERT STEIN, RESEARCH DIRECTOR, CED

Mr. Yntema. My name is Theodore O. Yntema. I am chairman of the research and policy committee of CED. I am accompanied by Mr. Herbert Stein, the research director of CED.

I am pleased to appear before you in response to your invitation to the Committee for Economic Development to comment on the Economic Report of the President.

In my business capacity I am an official of Ford Motor Co., but this morning I am not speaking for Ford Motor Co. or for myself. In my statement I am presenting as accurately as I can the views of the research and policy committee of CED. I shall be relying largely on a recent policy statement of our committee, fiscal and monetary policy for high employment, copies of which have been supplied to you.

The Economic Report is a long document, filled with useful information and analysis on a wide variety of subjects. I cannot claim to have analyzed it thoroughly in the 2 weeks since its publication.

In the short time available to me today I cannot comment on all the aspects of the report that even a first study shows to be worthy of mention. Therefore, I shall concentrate on a few subjects that seem of major importance.

We find the Economic Report to be in general agreement with our broad philosophy of the use of fiscal and monetary policy to achieve high employment and economic stability that we have expressed in our recent statement and in a series of earlier statements going back to 1947. This agreement includes:

(*a*) Looking at the budget surplus as it would be under conditions of high employment, as a guide to budget policy;

(*b*) Setting expenditure programs and tax rates so they would yield a moderate surplus at high employment;

(*c*) Accepting actual departures from this target surplus, below in recession and above in boom, that result from automatic responses of tax yields and expenditures, as beneficial stabilizing influences on the economy;

(*d*) Accompanying this budget policy with a strong flexible use of monetary policy;

(*e*) Being prepared, in some circumstances, to take further discretionary action in the budget, notably temporary tax reduction in recessions.

Also we have recommended, as the Economic Report does, that the national income budget, rather than the cash or the administrative budget, should be used in measuring overall budget policy.

I think that what is becoming national agreement on these aspects of policy represents real progress. I would, however, call attention to some important matters within this framework on which we have a different position from that of the Economic Report or which we believe to have been neglected.

First, this general description of budget policy leaves open the question of how big this moderate target, high employment surplus, should be. On this point there would seem to be two possible courses.

One is that we should select some target that seems to be consistent on the average with high employment and hold that target constant over a period of years.

The other is that we should estimate each year what particular target for the next year is most likely to be consistent with high employment in the foreseeable circumstances of the next year. We, in CED, have chosen the first course.

This course would at least prevent the budget from being a positive unstabilizing force, as it has been on occasions in the past. In view of the difficulties of economic forecasting and the political pressures that operate on the budgetary process, we do not believe it is possible to do better than this. We have suggested that the target surplus at high employment should be somewhere between $3 and $7 billion.

The administration's budget policy seems to follow the second course, of annual decision. The high employment surplus proposed for fiscal 1963 is justified, both in the budget message and in the Economic Report, on the ground that a smaller surplus would be inflationary and a larger surplus would choke off the recovery. The Economic Report presents no evidence in support of this conclusion.

It is worth noting that the administration's budget is estimated by the Council of Economic Advisers to have a high employment surplus running at the rate of $10 billion a year in the first half of calendar 1963. This is higher, even in relation to the size of the economy, than in any previous period of high employment since the unusual conditions of 1948.

Moreover this surplus would be accompanied by higher interest rates than at any earlier time in the postwar period. It may be that the Council has overestimated what the GNP and national income would be at high employment, in which case the size of the high employment surplus implicit in the budget is also overestimated. It is possible, too, that the Council may be overestimating the tax yields and underestimating the expenditures that will occur at high employment GNP.

But if the Council's estimates are correct the question of whether the contemplated budget and monetary policy will permit us to get and keep high employment needs further examination.

However my main point is not to question the budget for this particular year. My main point is to stress the need for a consistent policy not too dependent on yearly forecasts or too exposed to political pressures.

Second, I would emphasize a matter that concerns us greatly. These hearings are probably the last moment at which Congress will consider the budget as a whole. Whether or not the budget target proposed by the administration is the correct one, there is no reliable machinery in the Congress that will make the overall results conform either to the administration's target or to some other target consciously chosen by the Congress.

The various taxing and appropriating committees of the Congress are already going their separate ways, making the unrelated decisions that will finally determine the budget. We won't even know the net result of all this until a month after Congress goes home. To carry out the purposeful budget policy on which there is growing agreement, more effective machinery in the Congress is needed.

Third, our position on the timing and order of discretionary antirecession action differs from that presented in the Economic Report. The report proposes that the President be authorized to increase certain Government expenditures whenever the unemployment rate has risen by 1 percentage point and has risen in 3 out of 4 or 4 out of 6 consecutive months.

The report also proposes that the President be authorized to make a temporary tax cut, subject to congressional veto, in circumstances that are not quantitatively specified.

The signal authorizing expenditure increases would have gone off early in each of the postwar recessions. In the first three of these recessions the signal would have sounded when unemployment was below 5 percent; in 1953–54 recession unemployment would still have been below 4 percent.

We do not concur in the policy of increasing expenditures on the basis of so slight a rise of unemployment and certainly not before temporary tax reduction is in effect.

We believe that temporary tax reduction is to be preferred to expenditure increase as an antirecession measure. The tax reduction is more likely to take effect quickly and less likely to contribute to unnecessary longrun growth of Government spending.

We believe that tax reduction and, if used at all, expenditure increase are called for only in a serious recession. In such a recession the costs and dangers of inaction are large and the risks of doing too much and causing inflation are small because the economy is far below its potential output.

To invoke strong measures in a mild and ill-defined situation would increase risks of inflation unnecessarily and would weaken the discipline that the free market exercises against excessive price and wage increases.

We cannot tell whether the formula suggested in the Economic Report would have given the right signals or not in the postwar period without knowing more than we do about the size and timing of the effects of the proposed action. Even if it is possible, with hindsight, to devise a formula that would have given the correct signals in the postwar period, this formula may well give wrong signals in the future.

The Economic Report says that—

> Even if the criteria were to give a false signal in the future—for example, if unemployment were to rise because of a major strike—the President simply need not invoke the authority.

But of course the difficult problem always is to know in advance whether the signal is false.

Fourth, we agree with the administration on the importance of being better prepared than we now are to make a temporary tax cut in a recession. On this point our committee said:

> The essential condition for use of a temporary tax cut as an antirecession instrument is that the Executive, the Congress, and the public at large should understand the functions that such a cut would be intended to serve, the circumstances in which it would be appropriate, and the distinction between such a cut and basic, permanent revision of the tax structure.

This condition is more important than any parliamentary device. Without such understanding, parliamentary arrangements to make temporary tax reduction easier will be neither desirable nor obtainable. In any case, national discussion of the President's suggestion that he be given authority to make a temporary tax cut, subject to congressional veto, will be educational and useful.

In our statement we noted that such a proposal as has just been made by the President raises questions of the distribution of power between the President and Congress. We said:

> What is desirable is not to tip the balance of power between the President and the Congress but to obtain a prompt decision. An alternative way of doing this would be to provide that the President's proposal to change the tax rates should take effect only if approved, as in the case of ordinary legislation, by a majority of each House but to amend the congressional rules so that a proposal for a temporary tax reduction, within limits of duration and character specified by previous law, should come up for a vote without amendment in each House within a reasonable period of time—such as 60 days.

Fifth, we are greatly concerned about the long-run growth of the Federal budget. The Economic Report estimates that with constant rates and structure the yield of the Federal revenue system at high employment is rising at a rate of $6 billion a year.

Whether or not this is the correct figure, clearly the correct figure is large. Some combination of expenditure increases or tax-rate reductions will be needed to prevent the surplus from becoming too large. On this question the Economic Report says:

> Undoubtedly much of the reduction in the full employment surplus should be channeled directly to private purchasing power.

Understanding by this that tax rates should be reduced, not temporarily but permanently, we fully agree. But we would point out that, while this undoubtedly should happen, it undoubtedly has not happened. The surplus requiring reduction does not appear, because it is absorbed in higher expenditures before the question of tax reduction can be raised. The tax-rate reduction that will be permitted by the growth of the economy is always just around the corner. As we say in our policy statement:

> In fact, there is a tendency for tax rates to be regarded as given and for expenditures to rise as the revenue from the constant tax rates grows. That is, there is a bias in the system favoring higher expenditures rather than lower taxes, without consideration of the relative merits. We consider it important, in the program we recommend, to emphasize that in the absence of compelling reason for particular expenditure increases, tax reduction is more appropriate than expenditure increase in keeping a stable relation between revenues and expenditures.

Sixth, while we welcome the attention given by the Economic Report to the movements of wages, we believe that there are at least two important additional things to be said.

The Economic Report treats the unemployment problem essentially as a problem of getting an adequate amount of total demand through getting an adequate amount of money expenditures. The wage problem is regarded as important basically because of its relation to inflation, although a connection to unemployment through the balance of payments is recognized.

We would state the problem differently. The demand that gives employment is a real demand, not a money demand. The real demand depends equally upon money expenditures and upon wage rates. Correct behavior of wage rates is as important to the maintenance of high employment as is the correct behavior of money expenditures. In fact, the excessive rise of wage rates has at least as much role in explaining the unemployment of recent years as does the inadequate growth of demand.

A more difficult question is what to do about the problem once it is recognized. We are not sure that appeals for responsibility in the exercise of power are sufficient. The Economic Report discusses the role of competition in product markets as a limitation on power to raise prices. It is now urgently necessary to turn attention to the state of competition in labor markets.

In a policy statement issued in 1958 our committee, considering possible steps to be taken if we have a persistent general tendency to inflation and unemployment, said:

> The search for means to strengthen competition would have to be pursued without favor in business markets as well as in labor markets. But it is only a recognition that we live in the 1950's—not in the 1890's or 1920's—to say that the main problem lies in labor markets. There are several reasons for this.
>
> In most industries, except public utilities subject to regulation, there are several—often a great many—firms competing with each other, whereas single unions covering an entire industry or market are common.

Moreover, labor costs are much larger than profit margins. The potential contribution of excessive wage increases to inflation is therefore greater. Most important, we have a long-established public policy in favor of competition in business. The laws and machinery to implement this policy have been in effect for a long time, and in our view, have had a great deal to do with the growth of our economy and the improvement in our standards of living. There have been repeated national studies to see how these policies might be more effective. As a consequence we not only have substantial business competition; we also keep exploring the route by which we can preserve or strengthen it.

But we do not have even the beginnings of a public philosophy about the proper limits to the powers of labor organizations in an economy basically organized on the principle of competition. Our laws tend to deny the existence of the problem, as if saying that labor is not a commodity changes the facts that labor is the main economic resource and that wage rates are the main element in costs and therefore in prices. And recent investigations of unions have not focussed on this central issue of their effects on wage rates and inflation.

The problem of the proper limits to the character and extent of union power in a competitive, democratic, free society is one that urgently needs objective public discussion.

We recommend that the basic laws of the country be reviewed to see whether they permit labor organizations to have a degree of economic power which is not in the public interest.

Chairman PATMAN. Thank you, sir.

Now, our next witness will be Mr. Emerson P. Schmidt, who is with the Chamber of Commerce of the United States.

Mr. Schmidt, we are glad to have you here, and you may proceed in your own way.

STATEMENT OF EMERSON P. SCHMIDT, ECONOMIC CONSULTANT FOR THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA

Mr. SCHMIDT. I will summarize my statement. I have a slightly corrected copy which I will give to the recording secretary.

Chairman PATMAN. That may be done.

Mr. SCHMIDT. Like Mr. Yntema, I had only a short time to complete this lengthy report, so obviously I can comment only on certain points.

On the whole I think it is a good report. In many respects it is better than the average since the Employment Act was passed. Having said that, what I am going to say is by and large critical, but I hope that this does not overshadow the fact that I think, on the whole, it is a very good report.

On the business outlook, I think the Council's projection is roughly in line with what we have from other sources, although it may be a bit on the high side, and particularly projected profits for calendar 1962 may be somewhat high. If I had to guess, I would say that the 1963 budget will not be balanced, based on what we know now, but these things do change.

In regard to the budget analysis, I think that there is a tremendous improvement in both the Economic Report and the budget report. I think it is partly due to the work of his committee, the Proxmire Committee on Economic Statistics, and particularly the document which was put out just about the same week that the Economic Report was put out.

For that I think your committee deserves a great deal of credit. But now we are confronted really with what you might say are four kinds of budgets.

We have the ordinary conventional budget, which shows about $93 billion, and this unfortunately gets practically all of the play and all of the publicity and actually the budget is not at that level.

Rather, it is at a level of something like $117 billion, if it on a cash basis. If you go at the matter in the way in which the Federal budget is an economic document—which was prepared by Roy Moor for the Proxmire committee—you will find (p. 5) that the totals are much more staggering than that.

I have a little table there taken from his study showing that for 1960, total receipts for the Federal Government will be $127 billion, for expenditures, about $130 billion. Of course, these figures do not add in the State and local expenditures, and if you were to add in the entire Government sector of our economy, we would have close to $200 billion of cash flowing to Government treasuries. So it is roughly 40 percent of our GNP for 1960. This is scarcely a basis for the frequent charge of "public squalor in the midst of private affluence."

I would hope that this committee, in its report, can have something to say to remove what is the undue emphasis on the conventional budget and put more emphasis on the cash budget, and particularly the work that was done by Senator Proxmire's subcommittee.

Now there are tremendously large programs in the making and a great many so-called unmet public needs. But I think that much of the argument for this expansion rests on purely imaginary needs or false analysis, and in many cases on very unsound—what I would call economic cost accounting.

These are rather serious charges and I have here a pretty good documentation of some of the evidence. Needless to say, this does not apply only to the Central Government, but it also applies to the State and local governments at times, although you probably get a little bit more for your money at the levels of government closer to the people.

George Stigler has pointed ou that some years ago the State boards of education began to set down rules for the certification of teachers. This led to a deterioration of teachers, due to the fact that they excluded, to a large degree, a very large number of highly qualified potential teachers, namely, those who were liberal arts graduates in the colleges with majors in the fields of physics, chemistry, biology, mathematics, and languages, by demanding unnecessary pedagogical courses on the part of these teachers for our public schools.

Conversely, they have imposed a set of course requirements in pedagogical philosophy and methodology at the expense of the subject matter in the sciences, the humanities, and languages.

They have imposed tenure systems which make it virtually impossible to terminate incompetent teachers and they have tolerated automatic raises in pay through a minimum salary schedule which has promoted mediocrity in the profession by becoming a maximum salary schedule.

So a few years ago the Federal Government moved into this area in order to stimulate more learning and studying in the sciences and languages and so on to help correct the defects caused by intervention at the State level.

Now we hear a great deal about the crisis for education and many other fields. But just a week or 2 weeks ago the chairman of the House Education and Labor Committee said that he is going to follow a "go slow" policy on further intervention in education because actually nobody knows what the Federal Government is already doing in this area.

Apparently there are some 40 programs spending about $2 billion on this, and Congresswoman Edith Green reinforced that view at the same time.

I think there is a great need, and I think that this confirms what Mr. Yntema was saying about testing the usefulness of Government programs.

It is always possible, of course, to point to some benefit from Government spending, but this is in no sense a justification for such spending. Government spending always absorbs private resources and you ought to have a test. I have the test here on page 8 to the effect that no unit of any resource should be used for one purpose or in one place if it would produce more value in some other purpose or place.

In a free and efficient economy the economic resources are allocated by free consumer choice in such a way as to equalize the additional returns to society of additional outlays among all of their productive uses.

Stated another way, the maximum efficiency of our economy as a whole has not been achieved so long as it is possible to shift resources from one use to another, if such a shift results in the gain in total satisfaction.

Last year's Economic Report stated this principle very clearly, but I do not think that it helped to implement it very effectively.

Your own subcommittee, Mr. Chairman, back in January of 1958, issued a similar statement of fiscal policy entitled "Federal Expenditure Policies for Economic Growth and Stability"; this is one of the best statements I have ever seen in print on how to apply this principle to the Government sector.

But you also have to add a few other points. Since most Government activities escape taxation, you have to test this balancing principle in terms of the values lost by moving resources from the private sector, where they would be taxed, into the Government activity, where they are essentially tax free.

Now if State and local governments taxed all Government facilities like they do other property, if this were done, this would facilitate better resource allocation. It would certainly be better economic cost accounting.

You also have to add in the losses and the failures or other uneconomic uses in the public sector in order to get full and adequate cost accounting.

The Economic Report is almost completely silent on this matter. I found only one statement—on page 136—where it discusses the problem of water resources where it tries to apply this cost accounting type of principle.

For this it is to be commended, but this theme should run, it seems to me, through the whole report.

The interest rate, by offering to finance Government loans at submarket interest rates, can never meet the total demand. Anything that is underpriced tends to get overused. In the case of the REA you have the 2-percent interest rate. This is part loan and part gift. All you have to do to see how significant this principle is, is to ask yourself, what would be the demand for capital if you could get a perpetual loan at a zero interest rate? Now, that is admittedly an extreme, but I think that it brings the issue into focus.

The Economic Report states, on page 140, that the Government "facilitates homebuilding." There is no evidence that this is true and I have on page 10 some very interesting figures on a couple of years in the 1920's and a couple of years in the 1950's, both following a period of war, and both of them prosperous periods. Yet, in terms of the proportion of personal consumption expenditures, the housing expenditures, in spite of the fabulous intervention by Government in housing, were no larger in the mid-1950's than they were in the 1920's.

Housing starts were actually lower in the mid-1950's per million of GNP at constant prices, in fact, 60 percent lower then they were in the decade of the 1920's—that is, the 1925–26 period.

Housing starts per thousand population were higher in 1925–26 than they were in 1955 and 1956. I only give this as an illustration of the kind of analysis that I think the Council and your committee ought to make in judging and evaluating its Government programs. It is so easy to think that we, the Government, spend money that does some good.

It undoubtedly does, but it does not do the amount of good that is indicated by the dollar figures. Every existing and every proposed Government program ought to be tested by this kind of an approach.

Now, coming to the contracyclical points that are mentioned in the President's and the Council's reports, I am not at all certain that we need additional contracyclical weapons. The so-called recovery measures are listed as applied in 1961, and there is a failure to distinguish between those which were anticyclical, although being listed as promotive of employment, and those which were neutral and those which were proemployment in their impact.

These Government programs are not costless, and they may have merely absorbed resources from elsewhere, and therefore make no net contribution, and they may be mere transfer payments or income redistribution without making any net contribution to the activity.

So you find, for example, farm price-support increases, and increases in the minimum wage are listed as recovery measures. But we have certainly no evidence that that is on that side and all of the evidence I have seen is on the opposite side.

In fact, the Federal budget as an economic document, prepared by the Proxmire subcommittee, points out that nowhere in the budget or in any Government document is there any analysis of the quantitative impact of these several programs.

Yet the Economic Report states quite categorically, on page 59, that—

> A careful appraisal of the direct and indirect effects of increased Federal activity indicates that it was a major force—probably the principal driving force—of the recovery of 1961.

Now, since these two Government documents quoted here were published within less than a week of each other in January, what is the citizen supposed to believe?

As a matter of fact, in January of 1961, the Bureau of the Budget made a close examination of the antirecession weapons actually employed in the 1957–58 recession, and came to these conclusions:

1. The fiscal actions of the Government which gave the biggest boost to the economy in 1958 were the "built-in stabilizers," such as automatic decreases in income tax revenues and automatic increases in unemployment benefits which took effect under existing law without the need for policy action by either the executive branch or the Congress.

2. Many of the deliberate countercyclical actions, including some of the largest in terms of expenditures, made a small contribution in relation to their budgetary cost or were poorly timed.

So here you have a purely contradictory conclusion to that which the Council has advanced for 1961, and I see no evidence in this report to justify this rather categorical statement. As a matter of fact, I do not think it is correct.

To some extent the Council's report, and I hate to use a word that has come to be something of a swear word, "too Keynesian" in its orientation, in the sense of overpreoccupation with aggregate demand and insufficient attention to the maladjustments and roadblocks and distortions in the economy, which I deal with a little bit later.

For example, the report says:

Unemployment of 4 percent is a modest goal, but it must be emphasized that it is a goal which should be achievable by stabilization policy alone.

Well, I am not at all sure that that is true. If you have a basic maladjustment such as uneconomic wage rates, or other difficulties in foreign exchange rates or foreign currencies, you cannot solve this by stabilization policy alone.

Now, on to proposed tax cuts. We are very skeptical about this kind of an idea. To some extent there is danger in striving for utopia, lest we suffer even more from the imposed remedies for the problems than we suffer from the problems themselves.

Other than the great benefits from improved understanding of contracyclical monetary and credit policies, I am not at all sure there is much evidence that we have learned very much about how to handle the business cycle. The current reliance on the flexibility of revenues under the graduated income tax, and the effect of this, is already on the plus side.

Furthermore, the cut that is recommended by the President is a pretty modest cut. Sometimes a modest amount or marginal amount will tip the scales, but I am not at all sure that something like 2½ percent of personal income tax rebate would be much of a factor in shifting the economy from a downturn toward an upturn.

If this deficit were to be created deliberately in this way and financed by the banking system, it would apply some additional leverage. But then you come to the fact that you would have additional liquidity in the economy and probably would have more inflationary pressures when the next recovery comes about.

There is also some danger in getting the country to look to tax flexibility, discretionary tax flexibility, as a contra-cyclical weapon because it may open the door to fiscal irresponsibility.

Deficit financing could become a permanent way of life, and this is important for internal reasons, but also for balance-of-payments reasons. We certainly know that governments elsewhere have floundered on this particular point.

It is also possible, although I am not sure that this is correct, that if the President announces a tax cut and we get a lot of publicity on this, which would be the equivalent of saying we are in a recession or faced with a serious cutback, that this might encourage spending timidity on the part of businessmen and on the part of consumers. So we are not at all sure that a tax cut would have the right psychological effect.

I think that Dr. Arthur F. Burns thinks that it ought to be a tax cut without a terminal date for this very reason, whereas Henry Wallich, who is equally competent in this field, recommended in 1958, I think, a tax cut of 2 months.

I think most economists would say a tax cut for 2 months or a tax holiday, as they called it, for 2 months would be ineffective. Whether this would really have any effect as an impact, I do not know.

Then there is the constitutional question of whether you people, you Members of Congress, ought to hand this power over to the Executive, although I would certainly agree that tax flexibility is preferable to additional standby public works spending program.

We know that in 1958, and again in 1960 and 1961, public works, highway spending, and many others, were accelerated without any particular additional authority based on any standby power to invoke additional public works spending. I am not going into this very fully. We have done this in a number of our publications, particularly a little pamphlet we put out several years ago entitled "The Economic Lessons of Postwar Recessions."

On the matter of Federal control of unemployment compensation, I think it is not generally realized the degree to which the States have improved unemployment compensation systems. Originally, for example, there was a waiting period of from 2 to 4 weeks. I think that now no State has a waiting period in excess of 1 week and some have no waiting period at all.

The duration originally in most States was something on the order of 15 or 16 weeks. Today, practically no State has less than half a year, and the bulk of the employees are in States now in which the duration of unemployment compensation is in excess of or at least equal to half a year.

The benefit level has gone up twice as fast as the cost of living since the mid-1930's. It is a question of what you really want to do with unemployment compensation. I think that first you need to know what the States really have done and this ought to be accomplished in a way that would bring all of the relevant facts together, excluding the part-time unemployment from the averages so that you have valid figures.

Employers and employer organizations have almost consistently supported the unilateral financing of unemployment compensation, partly because it was felt that to some extent through experience rating, the employers would provide steadier jobs.

Now, if you convert unemployment compensation into something else, as a contra-cyclical weapon, I think questions are going to be raised whether this unilateral financing by employers ought to continue. Maybe the workers ought to have taxes withheld from them for that "rainy day."

So, there are a great many questions that need to be considered before this committee endorses this kind of a program.

Now, coming to the question of employment and unemployment, I think the report is a little weak in that it does not recognize that there are a lot of factors besides so-called aggregate demand that affect the Government level of employment.

In my statement, I have added three possible sources of unemployment—legislated unemployment, administrated unemployment and union-generated unemployment.

The business climate is very important. The rate of profit formation is important. The retained earnings are important. The expectation of profits is a dynamic factor.

Coming to the question of wage rates, the Council does not really relate the unemployment problem to the wage rate problem. They march right up to it on page 176, where they show that the wage rate of blue-collar workers has gone up faster than the rate of other workers in manufacturing. But the other workers have outpaced the blue-collar workers in the rate at which manufacturers have employed them.

I have a very interesting table, which is based on some charts in "The London Economist." If you look at the right-hand side, you will see that the mainly unorganized workers increased in employment between 1945 and 1960 by nearly 12 million. From 1955 to 1960, the increase was nearly 4 million.

The mainly organized, as against the unorganized, from 1945 to 1960 increased about 1 million, and from 1955 to 1960 declined by 1 million.

Now, the Economist drew no conclusions, and certainly no one will say that the upward wage pressures on the part of unions is the exclusive cause of this remarkable shift in the expansion of employment between the mainly organized and the mainly unorganized. But I suspect that there is a clear-cut relation. This also has been verified by the OEEC study, which was published in May of last spring and from which we quote at considerable length.

So we end up here by making a plea—although we did not compare notes with Mr. Yntema—for applying, or trying to apply, more of the free market in the labor market than we have done.

This, I think, is the great defect of the Economic Report. Although, strangely enough, it marches, again, right up to this point on page 189. If you use its wage tests, I think that you would say that in the case of the steel industry this year, there should be no wage increase at all.

I think that if we do not look at these questions of the level of wages, we are not going to solve the unemployment problem, and we are not going to solve the balance-of-payments problem.

In fact, there are some pretty bad statements in the report. For instance, on page 14, it says that:

> In the long run, the competitive position of U.S. industry depends on a sustained and rapid advance in productivity.

Now, this is not true. France has had a very rapid rate of productivity in the last decade and yet it was forced to devalue its currency. A rapid rise in productivity obviously is on the plus side; but if we allow our costs in money terms to accelerate relative to those with which we are competing abroad, we will not improve our net export position.

So I end my statement with a plea to do something with this labor problem. And I predict that Congress will be forced into the adoption of a coercive national wage policy, if we do not make the labor market work.

(The prepared statement of Emerson P. Schmidt follows:)

TESTIMONY OF EMERSON P. SCHMIDT, ECONOMIC CONSULTANT FOR THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA, ON THE PRESIDENT'S ECONOMIC REPORT BEFORE THE JOINT ECONOMIC COMMITTEE

The opportunity to evaluate the President's Economic Report and that of the Council of Economic Advisers is welcomed.

The reports are well written and highly useful. As in the past, they contain much helpful economic analysis. The appendix carries excellent historical statistical material (nearly 100 pages), much going back to 1939 and even 1929; useful tabular material is found also in the text of the two reports (nearly 200 additional pages).

Having said that, any further comment in order to be most constructive should be critical, but, hopefully, helpful. Whether it is advisable to have two reports, one from the Presildent and one from the Council, is questionable. The economist is most useful when he adheres to economic analysis. For the sake of brevity, some of the comments are not as fully developed as they could be if more space and time permitted. First, what of the report's projections for the year ahead.

THE BUSINESS AND ECONOMIC OUTLOOK

While projecting the prospective developments of GNP, national income and employment is always hazardous, both the Government and businessmen must look ahead in order to plan and conduct their affairs.

The Economic Report's projections for 1962 and early 1963 are roughly in line with those from other sources, although they may be on the high side. Projected corporate profits may be too high in terms of rising costs and growing competition.

The recovery from the mild 1960–61 recession (beginning in February 1961) to the end of the year shows a rise of about $41 billion in GNP from the first to the final quarter—$542 billion rate estimated in the last quarter and $521 billion for the calendar year, although this is an increase of only $17 billion from 1960 to 1961. For the second quarter of 1962 a rate of $565 to $570 billion GNP is expected; but since $570 billion is expected for the year, this would suggest relatively slower growth in the last half of calendar 1962. Because of the fear of a steel strike and inevitable inventory accumulation before the strike or a settlement, it seems most likely that the last half of 1962 will be less buoyant that the first half, just as in 1959. In fact, this strike situation could precipitate another dip in 1962 as in 1959. Artificial stimulants to inventory accumulation do not make for solid progress.

Factors making for a high level boom are not clearly visible. All Government sectors are expected to absorb and pay out more funds. The automobile industry looks promising. Total construction may reach a new annual high of about $60 billion, but little, if any, above the yearend rate of 1961. (This rate was already reached in November–December 1961.) The deficit in our international balance of payments probably was at a $4 to $5 billion rate in the fourth quarter of 1961, and is expected to be more stubborn in 1962 than in 1961; this could require monetary and credit restraint, which in turn could slow down the economy.

In spite of the public advice to union officials on restraint of demands regarding wage-fringe costs, featherbedding and compressed workweeks, they are not likely to be responsive to the pleadings; nor is it clear how seriously the administration means what it says, as evidenced by its silence before the cost-raising demands of Local No. 3 of the Electrical Workers Union in New York in early 1962 were forced on the consumer. The labor situation in 1962, too, may call for credit restraint in order to restrain costs and inflation.

Plant and equipment expenditures should rise moderately; if consumer spending and other market demands firm up, projected expenditures may rise somewhat more than now indicated. Currently, paperbound orders, a good short-run barometer, are very strong.

In short, this picture, while suggesting improvement in early 1962, does not provide assurance that the administration's targets for 1962 as a whole will be attained or that the 1963 budget will generate a surplus.

THE BUDGET

The proposed budget for fiscal 1963 reflects the strong tendency for expenditures to rise up to income. Administrative budget receipts are expected to rise from $82 to $93 billion; projected expenditures are $92.5 billion, leaving a thin, tenuous projected surplus of $500 million. But this surplus will depend upon a large rise in economic activity to generate the extra $10 billion of tax revenue, and a firm congressional and administration determination to resist unbalancing increases in appropriations and expenditures, reducing agricultural outlays and cutting the postal deficit. The request to Congress to raise the Government's legal debt ceiling to $308 billion, while partly explainable on short-run or seasonal grounds, has suggested to some observers that the administration actually does not expect the economic levels to be attained, or expenditures to be destrained, or both, particularly since the new debt ceiling is to extend through fiscal 1963.

The budget shows little effort to restrain expenditures; many new programs are proposed, usually with a modest first-year budget impact. Few significant reductions are proposed. Only $200 million, for example, are allocated to civilian pay reform for 1963; once the wage question is opened, does anyone believe that this will be the ceiling?

Whenever the administration or the Congress makes such a change or devises new programs, the citizen should be given the complete impact, on a full-year basis. When new programs are launched, furthermore, the congressional authorization committees as well as the appropriation committees should show enough self-discipline and fiscal responsibility to spell out, case by case, the probable costs over a period of years as the program grows, expands, and becomes more costly. Only by taking some such steps can the Congress and the taxpayers have any clue as to what they are buying—whether the public benefits will equal the costs. One congressional subcommittee put the matter this way:

"We need to know where the cost of present plans and activities may take us not simply through the next fiscal year, but for several years ahead.

"A 12-month budget reveals only the tip of the fiscal iceberg * * *. Cost estimates, to be meaningful, must be based on the full expected lifetime of programs.

"Longer term budgetary projections do not imply a change in the present system of presenting a budget to the Congress each year, and voting appropriations on an annual basis. Nor is the aim to make in 1962 decisions that can only be made in 1966. It is to take greater account of the consequences in 1966 of the budgetary decisions which must be made in 1962."

A Member of Congress should be as prudent in voting authorizations and appropriations as he is in his own family, business, or professional affairs. Unless he is willing to look ahead, case by case, he is not performing the role of a statesman.

Confusing budgets

The form in which the budget is presented on B day each January is unsatisfactory. The administrative budget receives nearly all the emphasis by members of the Government, of the press, and, therefore, of the taxpayer. But the administrative budget is becoming progressively less meaningful and valid; the Government certainly should minimize the chances of misleading the citizens.

In fiscal 1963 the National Government does not expect to collect only $93 billion from the taxpayer as most of the publicity implies; a more accurate figure on collections would be $117 billion. This represents the difference between the conventional or administrative budget, which is given wide publicity, and the consolidated cash budget; the latter is not only more relevant for economic analysis, but also comes much nearer to reporting the facts as to tax levies upon and collections from the public. Here is a difference of $24 billion, or more than 25 percent in excess of the conventional budget figure.

"In a seemingly bipartisan fashion over the prior 15 years," one economist has said, "every year or two, programs and categories of expenditures have been 'moved out' of the administrative budget. For example, the Highway Act of

1956 set up a separate trust fund for highway-related excise taxes and for the grants to States. These receipts and expenditures had both been included in the administrative budget previously. Beginning in 1948, tax refunds have been netted out of tax receipts instead of showing up as a major category of budget expenditures."

Many other cases could be cited. Furthermore, most of the excluded items have been growing rapidly, thus aggravating the spread between the administrative and cash budgets.

There is a further reason why the Joint Economic Committee should take a firm position on this matter: its January 16, 1962, release of the 185-page report "The Federal Budget as an Economic Document," by Roy E. Moor. This important study, for which Senator Proxmire's Subcommitee on Economic Statistics deserves credit, shows further how misleading the administrative and even the cash budgets are in terms of size, as shown by the following for 1960 (and for 1962–63 the disparity may be even worse):

[Billions of dollars]

	Receipts	Expenditures
Administrative budget	77.8	76.6
Cash consolidated budget	95.1	94.3
Actual totals	126.8	129.7

In addition to these three types of accounting, the recent Economic Report and the budget also carry economic and budget reporting on the National Government sector in terms of the national income accounts. This may have use in analyzing the economic impact of the Central Government on the economy; but it parallels more closely the cash than the conventional budget. (For a short description see Economic Report, p. 77, and Budget in Brief, fiscal 1963.)

Each of these four different methods of accounting for Government receipts and expenditures has its purposes and uses. Yet, four methods may be too many and too confusing. Primary stress should be placed by the Government and the citizen on the cash consolidated budget, with some modifications to take account of whatever may be useful in the national-income accounts and more of the many other fruitful suggestions made in "The Federal Budget As An Economic Document" (op. cit.) than was true this year.

The latter report (including TVA, Post Office, etc.) carries comprehensive tables including detailed breakdowns on total cash receipts of the National Government ($126.8 billion) and of expenditures ($129.7 billion) for calendar year 1960 (pp. 33 and 79, respectively), some 65 to 70 percent above the widely publicized administrative budget. We have no such total figures for fiscal 1962 or 1963 although the Budget of U.S. Government for fiscal 1963 carries a special table on "Public Enterprise Funds." For those concerned with big government, the growth of the welfare state, or U.S. collective spending, this type of tabulation is the most comprehensive and useful. (These data, of course, exclude State and local government expenditures, which in 1960 amounted to over $50 billion, and perhaps nearly $60 billion if assembled on the basis discussed in this paragraph.) These figures are much larger than any amounts published in any budget or in any other Government source; in fact, there is no one place in the Government accounts where any combined summaries of them can be readily found; monthly, quarterly or annually.

Thus, governments accounted for close to $200 billion of cash spending annually (roughly 40 percent of our GNP in 1960), scarcely a basis for the frequent charge of "public squalor in the midst of private affluence."

The Joint Economic Committee, when it comes to prepare its report, might well consider a recommendation that both the Council of Economic Advisers and the Bureau of the Budget stress in their next reports the cash budget and more of the approach and data as suggested in "The Federal Budget As An Economic Document," although this year's reports make important steps in this direction.

LARGER EXISTING AND MORE NEW PROGRAMS

The President's messages and the Economic Report recommend expansion in nearly all current National Government activities and the creation of many new ones. Legitimate or proper basic functions of government, of course, should be expected to expand roughly with the growth of the economy and the population. But even allowing for any such proper growth, the expansions recommended call for additional greatly enlarged public payrolls and enlarged Central Government activities.

Imaginary needs

Much of argument for this expansion rests on purely imaginary public needs, or false analysis or unsound economic cost accounting. These are serious charges against government, and anyone making them should try to provide some evidence to support the charges; this is done, in part, in what follows. Additional evidence may be secured from our publication "The Goals of Economic Policy" and the forthcoming "The Criteria for Government Spending."

Needless to say, perhaps, these charges do not apply exclusively to the National Government; for example, Prof. George J. Stigler of the University of Chicago has contended that State boards of education have adopted policies relating to teacher certification to lower the quality of the education of our children. Admittedly, local school boards have at times abused their powers, for example, by appointing favorite nephews or nieces to teaching positions. But State education boards have done much worse:

(1) They have virtually excluded from teaching a large number of highly qualified potential teachers; namely, the qualified liberal arts graduates with college majors in physics, chemistry, biology, mathematics, and languages, by demanding unnecessary pedagogical courses.

2. Conversely they have imposed a set of course requirements in pedagogical philosophy and methodology at the expense of subject matter in the sciences, the humanities, and languages.

(3) They have imposed tenure systems which make it virtually impossible to terminate incompetent teachers.

(4) They have tolerated automatic raises in pay through a minimum salary schedule which has promoted mediocrity in the profession by becoming a maximum salary schedule.

To try to help to make up for these deficiencies the National Government stepped in several years ago to encourage stress on the neglected subjects; but, based on past experience, its programs will inevitably suffer from hardening of the arteries and in time will be found to be misdirected. Governments rarely keep pace with change. Many decades ago the National Government began to subsidize vocational education; yet, now we are told, and correctly, that we are greatly short of the type of skills neded most and new training programs are proposed. Why did these U.S. Treasury-aided programs do so badly? The President recommends now three different programs financed in whole or in part by the Central Government (Economic Report, pp. 24, 25, and 94). In 1961 the depressed area law allocated funds for retraining. Furthermore, the Economic Report repeats the request for large sums for additional public and higher education and an intensive program to reduce adult illiteracy.

Evidently the steps already taken, reaching back over many years, are viewed as never adequate; cries of crisis are heard. All this disjointed effort seems headless and largely misdirected. In fact, the chairman of the House Education and Labor Committee on January 23 announced a slowup on most of the education aid bills until a congressional study could determine how much waste there is in existing programs. He said that there are some 40 different Federal agencies spending some $2 billion on education. Several agencies refused to reveal facts and figures on their educational activities. Congresswoman Edith Green at the same time said that she didn't think a single Government official, or anyone else, knows what the educational program actually is and this in turn makes it impossible for any Member of Congress to know what is being done. If these charges coming from Members of Congress are valid, how can the Congress act intelligently on the numerous new proposals for new programs or for program acceleration?

Testing Government programs

It is possible, of course, to point to some benefit from Government spending; but this is in no sense a justification for such spending. Government programs absorb private resources.

No unit of any resource should be used for one purpose or in one place, if it would produce more values in some other purpose or place. In a free and efficient economy, economic resources are allocated by free consumer choice in such a way as to equalize the additional returns to society of additional outlays among all of their productive end uses. That is, the individual allocates his dollars of income among the competing uses so as to maximize satisfaction of his tastes and desires and well-being.

Stated in another way, maximum efficiency of our economy as a whole has not been achieved so long as it is possible to shift resources from one use to another if such a shift results in a gain in total satisfaction.

The President's Economic Report of 1960 stressed that this principle of efficient utilization of resources applies with equal force to the Government sector of our society.

"The public use of funds, whether to continue established programs or to initiate new ones, must be justified on the ground that it makes a larger contribution to well-being and economic strength than could be made by their private use. The entire range of Federal spending must be continuously under review, with this criterion in mind * * *."

This principle also is in conformity with the report of the Subcommittee on Fiscal Policy of the Joint Economic Committee, "Federal Expenditure Policies for Economic Growth and Stability" (January 1958), which is one of the best brief statements of the goal.

Since Government programs escape taxation, the foregoing tests of the value of Government activity to the citizen or to society, must in addition allow for the taxes which would have been paid had the resources remained in the private sector of the economy. If State and local government taxed Government facilities like private property, this would facilitate accurate comparisons. Losses through default, failure, or other uneconomic use of resources also must be added in to arrive at a full evaluation; many Government ventures and programs fail and are charged off. Without such economic cost accounting, valid economic comparisons and contrasts as to private against Government spending cannot be made honestly or intelligently.

That the Council's Economic Report should be largely silent on this type of testing is inexplicable. In its analysis of water supply, the Economic Report is on the right track when it states that scarcities may be due to the failure to use the price system effectively,

"To treat a costly commodity as if it were free only encourages excessive use * * *. The burdens of scarcity on the economy cannot be entirely eliminated by using scarce capital to augment the supply of scarce water. But the burden can be minimized by a proper balance between investments in increased supply on the one hand, and price increases to eliminate inefficient use on the other" (p. 136).

While this is not complete economic cost analysis, it is a meritorious step in the correct direction for which the Council deserves commendation.

Let us examine another possible source of false analysis or unsound economic cost accounting: the interest rate. Interest is the price of loan funds. They have a supply price. Government, by financing its own or private (REA for example) activities at submarket rates, has persistent difficulty in meeting the demand. The reason is obvious. Government production of electric power, for example, almost inevitably leads to recurring shortages simply because the energy is underpriced; this underpricing is made possible by escape from taxation, by subsidies, and by the uneconomic use of capital made available at submarket interest rates. College loans, REA loans (2 percent while the Treasury, the taxpayer, must pay nearly double that for long-term financing), housing loans, etc., are all examples of policies which add to the size of the U.S. Treasury operations and burdens upon the taxpayer. Submarket Government loans are part loan and part gift. Such loans are a drag on normal economic growth. Anything which is underpriced tends toward overuse. The vast new Government (subsidized) electric power program is not analyzed in terms of accurate economic cost or need; it should be forced to prove its case.

The charge that those who urge this type of analysis are indifferent to public welfare, while easy to make, is not true. Let us examine housing needs, for example, since the 1920's.

Housing supply

The Economic Report claims that "the Government facilitates homebuilding" (p. 140); although innumerable devices and agencies are referred to, there is no proof furnished that Government has increased the housing supply. In fact, it is doubtful, as shown below, even though Government intervention has altered its nature and ownership.

The Economic Report assumes as in housing, usually without searching for evidence, that Government intervention has been a stimulant to growth and recovery. In order to show how effective Government policies have been one would need to know, however, what would have happened in their absence.

Great credit is taken, as noted above, by Government for stimulating new housing starts and residential investment. But in several years in the mid-1920's, say 1925 and 1926, new nonfarm residential private construction outlays were 6.98 and 6.75 percent, respectively, of total personal consumption expenditures; in 1955 and 1956 the figures were 7.28 and 6.54 percent, respectively—no major change. (Both pairs of years followed a war and were periods of prosperity.) In the years 1955 and 1956, housing starts were only about 3 per $1 million of GNP as against over 5 in 1925 and 1926 (1954 prices); this shows a 60-percent better performance in the earlier Government-unassisted period, relative to the mid-1950's, as shown by the table. In terms of population, housing starts were actually higher in 1925–26 than in 1955–56 (right column).

Housing starts—Federal aid

Year	Nonfarm housing starts (thousands)	Housing starts per million dollars GNP (1954 prices)	Housing starts per thousand population
1925	937	5.79	8.09
1926	849	4.97	7.23
1955	1,329	3.38	8.04
1956	1,118	2.78	6.65

Possibly these few figures do not prove anything conclusively; but they do suggest that the enormous amount of costly Government effort and allied private effort (hearings, surveys, reports, legislation, and appropriations and the establishment of housing agencies and programs—dozens of programs—and the large number of private meetings, trips to Washington by builders, contractors, mortgage fund suppliers, etc.) may have been largely wasted, or at least, this question may be worth looking into.

Every existing and proposed Government program should be put to the economic test: Are the benefits worth the cost? If not, could the resources be used more productively by private business or private families?

Perhaps the special interest congressional committees cannot be expected to do the badly needed evaluation job; but the Joint Economic Committee, having no legislative responsibility, should be free to examine total Government activity and case by case help to set up criteria for determining merit and priorities.

CONTRACYCLICAL POLICIES

Both the President's and the Council's reports take credit for the recovery in 1961, but provide no proof that this is so.

Certainly sustained high level use of our human and other resources is of the utmost importance. Yet, little dent was made on the problem of unemployment. Even though the noninstitutional civilian labor force showed virtually no rise from December 1960 to December 1961 (only 10,000), unemployment stood over 6 percent last December, which was only marginally below a year earlier, although some improvement should occur in the first half of 1962. In the face of the rise of GNP in 1961 one would look for a sharp analysis in the Economic Reports of the reason lying behind the failures in the field of employment and unemployment; no adequate analysis is to be found anywhere in the reports, as shown below. In fact, the so-called recovery measures listed and applied in 1961 fail to distinguish between the measures which are antiemployment, neutral, and proemployment, in their impact. Government programs are not costless; they may merely absorb resources from elsewhere; they may be mere transfer payments or income redistribution without making any net contribution to total activity or well-being. Thus, for example, under the recovery programs are listed increased farm supports and increases in the minimum wage (pp. 5–6 and 97 ff.); any such increases may be income to some, but are also costs to others, and the latter always has disemployment effects.

The Federal budget as an economic document, previously mentioned, lists (as does the Economic Report) some dozen steps which the President took shortly after inauguration and 7 other recommended steps in 1961 calling for congressional action; but this report states that not 1 of the 13 will ever be adequately, if at all, examined in any Budget document. It also states that "The noteworthy aspect of these proposals in terms of this study is that virtually no information is available about how these policies will influence budget totals *or the economy*" (p. 132; emphasis supplied).

The report then goes on:

"The significant aspect of these actions, from the standpoint of this study, is that not one of them ever will be examined in any budget document."

Yet, on the contrary, the Economic Report states rather categorically: "A careful appraisal of the direct and indirect effects of increased Federal activity indicates that it was a major force—probably the principle driving force—of the recovery of 1961" (p. 59).

Since the two Government documents quoted here were published within less than a week of each other (January 1962), what is the citizen supposed to conclude?

In January 1961 the Bureau of the Budget made a close examination of the antirecession spending steps taken in 1957–58 and came to these conclusions:

(1) "The fiscal actions of the Government which gave the biggest boost to the economy in 1958 were the 'builtin stabilizers,' such as automatic decreases in income tax revenues and automatic increases in unemployment benefits which took effect under existing law without the need for policy action by either the executive branch or the Congress.

(2) "Many of the deliberate countercyclical actions, including some of the largest in terms of expenditures, made a small contribution in relation to their budgetary cost or were poorly timed" ("Federal Fiscal Behavior During the Recession of 1957–58," Jan. 13, 1961).

The Federal budget as an economic document may be viewed as essentially a plea for the elimination or at least the reduction of guesswork and special pleading and drawing dubious conclusions from insufficient evidence or no evidence. It has led to almost no general public discussion. It merits much greater attention than it has received.

Nevertheless it, along with part of the Economic Report, may be too Keynesian in its orientation, in the sense of over preoccupation with aggregates, and inefficient attention to maladjustments and roadblocks and distortions in the economy.

The Economic Report states, "Unemployment of 4 percent is a modest goal, but it must be emphasized that it is a goal which should be achievable by stabilization policy alone" (p. 48).

In spite of the size of the Government sector in our economy, some 80 percent of production is still dependent upon the private sector. By making the free market work effectively, human well-being is maximized. Government is peripheral at best, and a roadblock at worst; yet, Government is essential and by concentrating on a few essentials such as monetary policy and fiscal responsibility it makes its maximum contribution. Nevertheless, more and more Government intervention is proposed. Probably no Member of Congress is satisfied with the results of its agriculture policy for example, which promotes a large misallocation of human and other resources and places a large burden on the taxpayer and the consumer. It damages our international balance-of-payments position. Formerly we suffered from some social and economic evils; now we suffer from the remedies for them.

NEWLY PROPOSED CONTRACYCLICAL POLICIES

The Economic Report now proposes three new countracyclical steps:

(1) Standby tax reduction authority;

(2) Standby authority to accelerate and initiate public works spending; and

(3) Imposition of central control of our unemployment compensation systems.

It will be possible here only to raise some questions about each of the proposals.

Standby tax cutting authority.

Perhaps more should and can be done to mitigate recessions, in spite of the mildness and brevity of the four postwar recessions. But there is danger in striving for utopia, lest we suffer even more from the imposed remedies for our problems than we suffer from the problems themselves. Other than the great benefits from improved understanding of contracyclical monetary and credit policies, there is little evidence that we have learned much. Current heavy reliance on income taxes in the existing tax structure to finance Government spending, undoubtedly already has a contracyclical impact. There is no clear evidence that standby Executive authority to cut taxes is needed, although all careful scholars regard it as superior to special ad hoc public works programs. Both in the 1958 and the 1961 recessions, many competent scholars, politicians, and others urged tax cuts; but cuts were resisted by the White House and by key congressional committee leaders. Both such tax cuts and ad hoc public works programs would require a forecast of future business, an underdeveloped art.

In 1961, personal income amounted to $417 billion and individual income taxes amounted to $41 billion or about 10 percent of total personal income. The President asks authority to cut the income tax rates across the board by not more than 5 percentage points. Even at the maximum proposed cut, this would reduce the tax take by only $10 billion for a full year which would amount to about 2.5 percent of total personal income.

This would amount to only a few cents for the average worker per day and, by itself, would certainly not be a very potent antirecession weapon. A larger cut would intensify problems discussed below.

If this would augment the Treasury deficit and the deficit were financed by bank credit, some additional economic leverage would become operative. But, in this case, the resultant increased financial liquidity would tend to remain in the economy and thus become the basis for inflation, particularly during the next recovery and boom. In this context, some experts have said that discretionary tax changing power should also include tax raising in order not to overload monetary policy as an anticyclical weapon.

Once the Congress and the public come to accept taxcutting and deficit financing as devices for creating expansion, the door would be open for more fiscal irresponsibility. Deficit financing might become a permanent way of life—a matter that is not only important for internal reasons but also for balance-of-payments reasons. Many erstwhile stable Governments have floundered on this one.

It is also possible that, if in the midst of a recession, the President suddenly cuts taxes for recession reasons, this could create offsetting spending timidity on the part of both business and consumers. If confidence is sustained that public policy will act promptly and effectively, this problem would not arise. But we have no assurance as of now, particularly if serious breakdown occurred, that the execution of such standby taxcutting authority would achieve its purpose.

In addition, there is an important constitutional question involved. The constitution extends the power to levy taxes and appropriate funds to the Congress and not to the President. While appeals to constitutionality have lost some of their potency, as we look around the rest of the world where the rule of law and constitutional safeguards are held in light esteem, the United States of America should not depart lightly from constitutional safeguards.

Standby public works spending

The President's request for standby authority to accelerate and initiate up to $2 billion of public works spending seems unnecessary in the light of what was done in late 1960 and in 1961 in the form of accelerating post office, highway, and other construction without any additional congressional authority. In 1961 out of total construction of $57.5 billion, more than $17 billion was public and of this latter figure a very large proportion was either direct Federal construction or federally influenced, such as highways, hospitals, local sewer and water facilities, and many others.

It seems somewhat strange that in the light of the foregoing and the almost unanimous conclusion of business cycle students that public works are not suited as a cure for recessions, particularly mild and short recessions, that this authority should be requested.

Nearly every student who has closely examined the use of public works as a contracyclical weapon has found it an awkward and largely unsuited weapon for this purpose. Furthermore, it is not likely that the Congress would like to stand idly by while the administration operators at the public works control levers try to provide more jobs through more public works. While the President's request as of this year is limited to $2 billion in pratcice we might get some multiple of that figure including congressional authorizations and appropriations for public works which are not easily turned on and off to fit neatly in some valley of recession.

This discussion of these two contracyclical weapons does not pretend to exhaust the subject; in our report "Economic Lessons of Postwar Recessions," we discussed both of these questions much more fully, with reference to the literature and authorities.

Federal control of unemployment compensation

In the name of economic stability the Economic Report urges Congress to impose new Federal controls on the relatively autonomous State programs of unemployment compensation. He also requests Congress to establish a permanent national program of extended unemployment compensation for unemployed workers who use up their benefit rights under the regular State programs. Both parts of this double-decker system are to be financed by higher taxes on employers.

Over the decades so many people have argued that the States have not updated their unemployment compensation laws that many people have come to believe this to be a fact. Actually, the contrary is the case. Average UC benefits have increased nearly twice as rapidly as the Consumer Price Index since 1939. UC benefits have increased more rapidly than net spendable wages. Waiting periods have been reduced from the original 2 to 4 weeks to 1 week or less in all of the States. The size of covered firms has dropped steadily from those with eight or more employees (the 1935 national law requirement) to four or more and nearly half the States cover firms with fewer than four employees.

About 45 States with approximately 90 percent of the Nation's covered workers pay benefits for a half year or more to workers with substantial work history and the majority of workers in most of the States are eligible for the maximum duration. Too little is known about these great changes that have occurred since the States originally adopted the "model" laws in the 1930's.

Now pressure is to be brought on the States to increase still further unemployment compensation, primarily to provide the National Government with another more powerful contracyclical weapon—a purpose which played no role in the mid-1930's when these laws were adopted, although this does not demonstrate that no change should be made.

Unemployment compensation is financed by payroll taxes levied against the employer. Businessmen and business organizations have supported this unilateral financing partly because they believed that it gave management a strong incentive to rearrange and adjust its affairs so as to provide steadier jobs. There is much evidence that incentive financing (experience rating) in State laws promoted steadier employment. The proposed changes will weaken seriously this extra employer incentive to stabilize employment.

However if unemployment compensation is now to be converted into a more massive contracyclical weapon by Federal coercive action as to benefit levels, duration, higher payroll taxes, and a higher wage base on which to levy the tax, this raises the question of the advisability of the continuation of the unilateral financing by employers. Questions will be raised inevitably as to whether employees, through payroll deduction, should not bear the added cost. But, if so, this might further impair the effectiveness of the experience rating in encouraging employers to provide steadier jobs.

Still higher benefits have a cost. Even more important, it must be noted that payroll taxes levied on employers raise the cost of putting workers on the payroll and therefore are bound to have disemployment effects, particularly as they go higher and higher (along with other payroll taxes and fringe costs). If benefit levels keep rising, they may also encourage some workers to take advantage of the "paid leisure."

Undoubtedly the increase in transfer payments has had some cushioning affect during recessions. The Economic Report refers to these as "automatic stabilizers"; a more accurate term would be "economic snubbers" or "economic cushions." The Economic Report of the Council also states that "Government transfer payments to individuals are held down when unemployment declines" (p. 64). The question may be raised whether this is accurate. Transfer payments have increased from about $1 billion in 1929 and $2.5 billion in 1939 to a rate of over $33 billion in late 1961. Yet since the end of World War II transfer payments have declined significantly only in one year, 1951, and climbed steadily since then, more than doubling since 1950. This matter is mentioned only because there seems to be a tendency in the Economic Report to exaggerate the aggregate contracyclical behavior of transfer payments.

We should not assume, of course, that existing economic stabilization tools and institutions are perfect or good for all time. Better and more timely statistics and better economic intelligence generally, may improve the performance of the weapons we now have; for example, about two-thirds of the GNP recession declines since World War II have been inventory recessions. Perhaps here we could do better. Flexible monetary policy must at times mean credit restraint; but the pressure for continuous credit ease could pave the way for recession. Furthermore, if there are basic maladjustments in the economy, which lead to a corrective pause or recession, it is not obvious that more powerful fiscal and public works weapons would be on the plus side, unless we somehow reduce mistakes and maladjustments.

EMPLOYMENT, UNEMPLOYMENT, PRODUCTIVITY, WAGES, AND PRICES

The Economic Report expresses concern over the level of unemployment, the rate of economic growth and inflation, both currently and in recent years. While recognizing that the unemployment may be marginally due to structural deficiencies, its primary stress is on inadequate aggregate demand, or the output gap. If this emphasis is wrong, but allowed to stand, we may drift toward more Government spending and Treasury deficits, not on their merits but because we have misdiagnosed the problems. What follows is intended to fill what may be an analysis gap about the so-called output gap.

In our testimony before the Joint Economic Committee's Subcommittee on Economic Statistics (see hearings, Dec. 19, 1961) we suggested that there may be more to the structural unemployment thesis than is commonly recognized by the Council of Economic Advisers. Although the subcommittee had prepared for it a Bureau of Labor Statistics report ("Unemployment: Terminology, Measurement, and Analysis, 1961") which listed several dozen types or causes of unemployment, we suggested that it might be important to add three more causes of unemployment: (1) legislated unemployment, (2) administrated unemployment, and (3) union-generated unemployment.

Adequate employment opportunities depend heavily on new investment, research and new product development, on the jobmaking climate and the cost of labor. The expectation of profits is the dynamic factor. Net corporate profits have remained relatively stagnant for the last decade; allowing for the deterioration of the dollar they have declined by about 25 percent since the beginning of 1950. They have declined per dollar of sales and as a share in the national income. In the economic expansion from 1950 to 1960, in current dollar profits showed no rise, while compensation of employees rose by 91 percent and national income by 72 percent and GNP by 77 percent.

The rise in payroll taxes and wage-fringe costs have made it progressively more difficult to put men on the payroll. U.S. depreciation policies have been among the most backward of all the industrialized nations. Dr. Simon Kuznets, in his seventh and final report on savings and capital formation, concludes that investment outlets have risen much faster than our rate of savings and investment; he was not beguiled by the apparent short-run excess capacity which is always apparent during recessions, just as excess labor is evident at such times.

The investor and businessman operates within a political and economic climate as he sees it. Congress has steadily subjected business decisionmaking to a growing volume of rules and regulations and a growing volume of paperwork. All major and many minor business decisions now must be made in a constrictive straitjacket of Government-imposed rules, regulations, court decisions, and congressional laws. Some 80 to 100 bills are pending before various congressional committees which would further circumscribe the freedom of business decisionmaking and a number of these are endorsed in the Economic Report.

A vast complex of rules and regulations have been evolved by administrative agencies which are too often conflicting, shifting and changing, difficult to understand, and costly to comply with—creating administrative unemployment. Many small businessmen find it impossible to compete in this world of bewilderment.

A private enterprise system has much durability, but the spirit of enterprise cannot thrive under a climate which keeps lowering the ceiling and closing in the walls which impair dynamic and aggressive venturing.

The Economic Report is rightly concerned about lagging employment; but it shows little awareness of the nature of the need for a favorable jobmaking climate. Virtually all discussion of this problem runs in terms of education, training, and retraining for would-be jobholders; there is little discussion of the role of self-employment or of the jobmaker. The wage motive will cause a man to take a job, if the profit motive first creates the job. We need entrepreneurial motivation and management training, but the latter should not be a burden to the taxpayer.

The report discusses free collective bargaining without defining the term. The right to strike is commonly assumed to be the ultimate weapon of the union official. But this is wrong. The ultimate weapon is actual or potential coercion and violence which is general in bargaining and strike situations. Employers and workers anxious to keep on working know this to be true. The promptness with which employers now close down an operation when a strike occurs, is due to their knowledge that any attempt to keep operating would only invite violence.

In the report's last chapter (p. 167 ff.) there is extensive discussion of the topics listed at the head of this section—employment, unemployment, productivity, wages, and prices. Much of the analysis is acute and highly relevant, but it still misses the mark.

The law of costs

The law of costs, while alluded to, is not adequately analyzed in terms of employment and international balance-of-payments problems.

The goal is stated to be stable overall prices, without any reference to a preference for a slowly falling average price level if we are to improve our balance of payments and broaden purchasing power at home.

There is no recognition, with possibly one minor exception, that the price of labor has any relevance to employment.

One of the oldest and most respected economic laws (as well established as other components of the laws of supply and demand) states that under competition the price of a commodity tends to equal its costs. Prof. Edward H. Chamberlin, of Harvard University, one of the closest students of the free market put the matter this way:

"* * * It is fundamental to distinguish between the labor market and the product market, but it is also common to place far too much emphasis on the distinction. As markets they are clearly not the same: the former deals with the purchase and sale of labor services, the latter with the purchase and sale of the company's product. The link between them, however, is simple and vital—that the buyer in the first market and the seller in the second are one and the same; viz, the entrepeneur. Another way to state the relationship is that the entrepeneur buys labor in the first market for the obvious purpose of reselling it, incorporated into a product, in the second. The economic law which links the two markets, the 'law of cost,' is as venerable and respectable among economists as the more famous 'law of supply and demand.' In simplest form it states that the price of a commodity tends to equal its cost of production * * *" (U.S. Chamber of Commerce, "Inflation, Unions, and Wage Policy," p. 26).

While Chamberlin was concerned primarily with inflation and the impact of union organizations, the Economic Report is concerned both with inflation and unemployment (ch. 4). Yet it is remarkable that there is no stress on the fact that labor as a factor of production is a cost-input, which inevitably will be minimized by management insofar as it is possible to substitute less costly inputs. The Economic Report identifies innumerable ways and means of intensifying competition in the goods market; this is another way of saying, in the face of the well-established law of costs, that maximum pressures are to be generated upon employers to get their costs down. Since labor costs are the chief costs of production, outweighing all other costs combined several times over, the pressures on management to minimize the use of labor are heightening. Undoubtedly in terms of efficiency this is just as it should be; but if concern about unemployment and more growth is expressed, adequate attention should be paid to the cost of putting labor on the payroll; yet in this context the Economic Report reflects a serious gap.

In discussing rents and costs of housing, the Economic Report does identify correctly the long-run cost levels with changing construction costs, property taxes, and interest rates (p. 170); but it fails to carry this "lesson" into its discussion of unemployment, although there is some recognition of the relations between costs and prices, or average price levels—but not unemployment.

Again and again, the Economic Report comes up to the law of costs as related to unemployment, but it never quite nails the point. Thus it points out that "Although aggregate salaries in manufacturing have risen twice as rapidly as aggregate wages, annual disbursements per worker for salaried workers increased at an average rate of only 3.8 percent a year during the period 1947–61, while disbursements per production worker increased at a rate of 4.9 percent. At the same time, the number of salaried workers was increasing at a rate of 3.7 percent a year, and the number of production workers declining at a rate of 0.5 percent" (p. 176).

That such wage pressures may cause artificial mechanization rates and cause unemployment among blue-collar workers and slow down growth, which noted, is not explored at all.

The Economist (London) last autumn published a series of charts breaking down employment growth in the United States into two groups; namely (1) mainly nonunionized and (2) mainly unionized. We dug up the data on which these charts must have been based and present them for your consideration. If we are concerned with unemployment, it will be noticed that from 1945 to 1960, the mainly nonunionized areas of our economy showed an employment increase of about 12 million, while the mainly unionized sectors increased by less than 1 million workers. In the period 1955–60 the comparative growth rates are even more striking.

Changes in employment

[Thousands of employees]

	1945	1955	1960	1945–60	1955–60
Mainly unorganized:					
Government	5,944	6,914	8,456	+2,512	+1,542
Services and miscellaneous	4,011	5,916	6,637	+2,626	+721
Trade	7,522	10,846	11,643	+4,121	+797
Finance, insurance, and real estate	1,428	2,219	2,485	+1,057	+266
Manufacturing (nonproduction)	2,438	3,502	4,073	+1,635	+571
Total change				11,951	3,897
Mainly organized:					
Manufacturing (production)	12,864	13,061	12,263	−601	−798
Contract construction	1,132	2,759	2,771	+1,639	+12
Mining	826	777	664	−162	−113
Transportation and utilities	3,872	4,062	3,902	+30	−160
Total change				+906	−1,059

Source: Bureau of Labor Statistics.

The Economist drew no conclusions. Certainly no one would attribute this significant differential growth exclusively or perhaps mainly to the union influence, but it merits thoughtful consideration. It may have relevance for the oversimplified dichotomy: structural versus aggregate demand unemployment or the "output gap."

Nor should anything said here be interpreted as antiworker (who isn't a worker?) or as opposition to the freedom of the worker to join a union. A union has many useful functions to perform, particularly in the areas of communication. The very concept of the dignity of man, which we all cherish, involves his open opportunity to air his grievances, to express his feelings, and participate in many decisions. Two-way communication is urgent. Unions which are free from compulsory membership and renounce any use of force or coercion, can perform highly essential services. If these primitive weapons were renounced or effectively outlawed, collective bargaining would cease largely to be any problem to the administration, the Congress, or to the country in terms of employment, inflation, or balance-of-payments problems.

These problems of legislated, administrative, and union-generated unemployment, are not confined to the United States. But most foreign nations have a natural discipline working on the minds and emotions of union officials via those nations' heavy dependence upon exports, in order to earn the foreign exchange to pay for essential imports. We have no such natural discipline. In Sweden, for example, there is general rejoicing when the top union federation official comes from an industry which is heavily involved in exports. This is true in most of the European countries and helps to promote efficiency, cost control, and relative price stability. A number of the European countries rely on as much as one-third or two-fifths for their income by earning exchange through exports.

As the Common Market matures, a part of this automatic and natural discipline will be lost; this could play into our hands but will not cure our unemployment problem or our basic international payments deficit.

Because the Economic Report reflects some, possibly serious, omissions here, let us look abroad.

The leaders in Europe are so aware of the wage problem that the Council of OEEC (now OECD, of which the United States is now a member) requested a group of independent experts to study the problem of rising prices, growth, and employment, and report its findings. In May 1961, the report, "The Problem of Rising Prices" (489 pp., Paris), of the group of distinguished economists (William Fellner, professor of economics, Yale University; Milton Gilbert, director of economics and statistics, OEEC; Bent Hansen, professor and director, the National Institute of Economic Research, Konjunktur institutet, Stockholm; Richard Kahn, professor of economics, Cambridge University; Friedrich Lutz, professor of economics, Zurich University; Pieter de Wolff, professor of econometrics and director of the Central Planning Bureau, The Hague), was published.

All members of the group were agreed that excessive wage increases (wage and fringe increases) secured through negotiation have been a significant factor in the upward movement of prices (p. 55). The report places no faith in public exhortation as a wage policy.

The majority agreed that stabilization authorities (meaning Government) must have a wage policy if the several goals of growth, high employment, and reasonable price stability are to be achieved. This recommendation is fraught with much more significant implications for the survival of human freedom than is commonly assumed by those who are intrigued by the naive notion that, say, a Government responsive to "labor" will control "labor," in the national interest. The majority rejected the idea of "restoring competition in the labor market as unrealistic" (p. 57). But from this latter view two members, who had long residence in the United States, dissented.

Since the Economic Report discusses the role of market power, it is of some significance to note that all members of the OEEC study group agreed that business monopoly, administered prices, and monopoly in the goods market were not significant factors in the wage-price spiral, a conclusion also reached in our earlier studies: "The Mechanics of Inflation and Administered Prices and Inflation." (This, however, is in no way any endorsement of monopoly or price fixing.) Prof. George J. Stigler, after a careful and critical examination of the hearings and reports of the Senate Subcommittee on Antitrust and Monopoly of the Committee on the Judiciary beginning in 1957, states that—"The attribution of inflation to monopoly power of enterprises is therefore lacking as a theoretical national and an empirical basis."

Dr. Stigler concludes his critical examinations by saying that the subcommittee's—"* * * chief results were to popularize the erroneous belief that there is an important phenomenon called administered prices, and that if such prices existed they would have something to do with inflation." "Administered Prices and Oligopolistic Inflation," the Journal of Business, University of Chicago, January 1962.

The two dissenters in the OEEC group from the idea of a compulsory national wage policy (Fellner and Lutz) concluded that wherever "the bargaining attitudes" create a lasting conflict between key policy goals the solution must run in terms of cutting down "the size and functions of the organizational units on both sides of the bargaining table" (p. 64). The dispersal and diffusion of undue power is in the long run tradition of American history. The two dissenters make good sense.

That the United States of America is drifting toward a position of Government-coerced "national wage policy" is obvious. The pressures of inflation and international imbalance of payments together are forcing us in this direction; as the incompatability of unlimited market power in the hands of union officials and low unemployment and the integrity of the dollar, is made clear by unfolding events, the drift toward Government coercion will be furthered.

But there is another way out.

England is facing this issue today; in spite of its serious balance-of-payments problems and uneconomic practices in many respects, the unions are striking and pressuring their demands. The Council on Prices Productivity and Income appointed by the United Kingdom in 1957 to wrestle with this problem, in its first report in 1958, said:

"We must revert at this point to the suggestion that from time to time a percentage figure should be announced by which average money wages could increase during the year without damage to the national interest. We are conscious of the attractiveness of this proposal, offering as it does the hope of establishing a link between the rate of wage increases and the growth in overall productivity. There are, however, serious practical objections to it. There would always be industries in which there were good reasons for the advance in wages to exceed the average; others in which much less good reasons for it to do so could be thought up; very few in which the case for lagging behind the average would be readily conceded."

Then applying these findings the Council stated:

"There would thus be a real danger that the prescribed average would always become a minimum, and the process of wage inflation therefore built into the system. This is apart from the point already made that such a procedure seems to involve too definite an endorsement of the doctrine that in a progressive community the general level of prices should never be permitted or encouraged to fall as an alternative to a rise in money income."

We are told by the Economic Report that we "must rely on the good sense and public spirit of our business and labor leaders to hold the line on the price level in 1962" (p. 17). But the Council states that it is "* * * undesirable that they should bargain implicitly *about the general price level*" (p. 188, italics supplied).

At best, such a pair of advisory statements in the same volume are confusing, not only to students but also to business executives and union officials; at worst, they are in contradiction with each other.

But more important there is an implication of market power on the part of business and union officials, that they should not try to maximize their returns, and having this power they should behave responsibly. The union literature and sales talk is replete with the self-admission of market power in demanding and getting wage settlements; there is no such comparable management admission of the power to set prices, or to make any particular prices stick under the restraints and constraints of the power of the consumer to pick and choose, foreign and domestic competition, availability of substitutes, etc. Those who are dedicated to the free competitive market believe that this is the way the price system should work.

The purpose of collective bargaining is to destroy competition in the labor market; while much consideration has been given to the application of antitrust legislation to unions, little progress has been made. But does it seem reasonable for government to convey market power to unions in the labor market, and then expect them not to use that power? This is precisely the situation which the country now faces; even though it is not squarely acknowledged in the Economic Report, it is implicitly acknowledged there.

RELIANCE ON MARKET FORCES

We have, unfortunately, no objective criteria to apply to wage determination through collective bargaining. It is doubtful that we ever will—any more than we can have general guides for the future for price changes of a company or of an industry, in spite of the Economic Report's extensive but contradicting discussion of the matter.

In searching for some criteria for wage determination, Dr. Winfield W. Riefler, then Assistant to the Chairman, Board of Governors of the Federal Reserve System (in an address July 21, 1959, entitled "Inflation—Enemy of Growth") stated:

"* * * I would hope that the benefits of rising productivity and growth were broadly distributed in three general directions and not overweighted in any one: (*a*) in the direction of wage and incomes advanced to the working force to encourage mobility and the ready availability of needed skills and talents at points of innovation; (*b*) in the direction of lower prices promotive of broader and expanded markets for those end products where productivity has lowered real costs; and (*c*) in the direction of sufficient profit encouragement to those who innovate successfully to stimulate initiative in management planning for growth. In other words, I would favor a situation where the efficiencies of growth were reflected in falling, not rising, unit costs * * *."

This is quite clearly a plea for making the free market function effectively in the broad general interest and letting the market forces distribute the gains of productivity among all groups and sectors of society. Even the New York Times, in an editorial, after the 116-day steel strike of 1959, took this same position: "* * * It should be left to the competition and the price system to determine how the income flowing from the process of turning raw materials into finished goods should be distributed* * *" (December 5, 1959).

Prof. Walter D. Fackler, of the University of Chicago, came to a similar conclusion before a joint session of the American Statistical Association and the American Economic Association (December 30, 1959, Proceedings of the former). This, in fact, is the process whereby, over the decades throughout most of our history, we have spread real purchasing power to all groups and raised our scale of living to the world's highest levels. And it does not involve stagnant real income for workers; it provides rising real purchasing power for them—as it should.

This approach is in marked contrast to the Economic Report where it states, "It is desirable that labor and management should bargain explicitly about the distribution of the income of particular firms and industries" (p. 188). Under such a doctrine the outcome depends on relative power and weapons to make demands stick. This will not lead to optimum allocation of resources or equity. Only if all sides renounced force and violence could this be sound.

But union monopoly, compulsory unionism, and the use of force, violence, and coercion must be eliminated if genuine and balanced collective bargaining based on discussion and persuasion is to be restored. The renunciation of the use of force is not unknown. For example, under the long leadership of President William D. Mahon, the Streetcar Workers' International Union adhered to the policy that all disputes not resolved by negotiation be settled by voluntary arbitration. It is better to disperse and diffuse undue concentrations of power (as we have done quite effectively, even if not perfectly, in the product markets through antitrust laws and the growth of competition through science, research, and technology) than it is to try to regulate them. What is the proper guide for settling a wage claim?

1. Without minimizing the key role of proper monetary, credit, and fiscal policies to help maintain sustained prosperity and high employment, the question may be raised whether a general wage increase should be granted by an employer as a result of collective bargaining in a competitive and dynamic economy, except when such an increase is necessary to hold and recruit an adequate supply of individual workers for the establishment. If an employer has difficulty in securing enough manpower, this suggests that the remuneration is inadequate; if he has more applicants for jobs than there are openings or has no difficulties in securing adequate help, this suggests that his offering rates are adequate or more than adequate.

In spite of the questionable analysis and contradictory assertions of the Economic Report, its "general guide" for wage behavior (p. 189) says almost the same thing as the paragraph above. In fact, its four tests of wage adjustments would seem to mean that in the case of the steel industry, for example, there should be no general wage increase in 1962. Yet, elsewhere it calls for wage increases in industry a whole equal to the rise in general productivity.

2. Proper wage and salary administration in the individual establishment, in addition to the standard set forth in the penultimate paragraph above, may in addition provide for individual payment adjustments in response to improved skill, better performance, etc.

3. Furthermore, wage adjustments from time to time to maintain morale, reduce turnover, and reward cooperative teamwork may be good personnel policy and sound business practice.

Such wage policies in a highly competitive economy, complemented by noninflationary credit and fiscal policies, would help distribute productivity gains over the years and would lead to a stable or a slowly falling general price level and improved values. This would benefit all consumers, including workers as consumers, farmers, as well as those who have retired and those who are living on fixed and lagging incomes. It is the one way to spread "purchasing power" in the broadest possible way. It would provide an automatic, steady increase in real income for the gainfully occupied, as well as others. And if European and other countries continue paying wages in excess of productivity, it would solve our international balance-of-payment problems within 2 years or less.

It is difficult to escape the conclusion that regardless of the conflicting diagnoses and prescriptions and the apparent contradictions in the Economic Report and the claims of union officials, the forces of supply and demand—that is, the free play of market forces—should determine wage rates and wage levels.

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Collective bargaining, if devoid of force and compulsion, would come close to achieving this goal.

Perhaps the report is not sufficiently concerned with inflation; it does not recommend the amendment of the Employment Act of 1946 to include among its goals the integrity of the dollar. Such an amendment would provide Government officials and citizens a precise congressionally determined target or benchmark along with "maximum employment, production, and purchasing power."

What has been said of wages applies with equal strength to the goods market. Competition in the goods market should be enforced and relied upon to pass on the benefits of technical progress and cost reductions to employees and others as consumers. Only if we have strong competition in the goods market, and it is widely known that it is substantially effective, can we expect adequate public support for the foregoing wage policies.

The Economic Report states that, "In the long run, the competitive position of U.S. industry depends on a sustained and rapid advance in productivity" (p. 14).

This is not correct; France has had a very rapid rate of productivity advance in the last decade, yet it was forced to devalue its currency. A rapid rise in productivity obviously is on the plus side; but if we allow our costs in money terms to accelerate, relative to those with which we are competing, we will not improve our net export position.

CONCLUSIONS

The idea of Government setting a target for annual wage increases is fraught with inflationary dangers, furthering our balance-of-payments difficulties and is in basic conflict with the requirements of a dynamic changing economy.

Government should examine its own responsibility for unemployment in terms of an improved jobmaking climate, tax reform, labor legislation including minimum wage fixing at rates as high as $4 and $5 per hour, frustrating and excessive bureau and administrative controls and its encouragement of unemployment-creating union power.

Freer international trade with concessions by foreign nations at least equal to ours, would improve human well-being. But we must control our costs better than foreign nations do. Unless Government takes prompt steps to reduce the undue market power of union officials, we will unwillingly and unwittingly be driven into authoritarian action. The Economic Report is aware of the dilemma but has no medicine for the malady except exhortation.

There is no adequate reason to believe that the Government needs vast new contracyclical programs. Tax reforms with lower corporate and individual rates and depreciation liberalization are urgent. A mere tax credit for investment is a loophole in the sense of not being available to all; it is a subsidy which general taxpayers should resent.

Government expenditures have been getting out of hand; there is too little attempt made to measure public benefits against tax costs.

The constant rise of Government outlays and intervention is heavily motivated by a view that the citizen does not know what is good for him—he is viewed as incompetent and ignorant; therefore Government must take his money away from him and decide how it is to be spent, and surround him with a vast and bulging bureaucracy to help him or make him come to sound decisions.

Government benefits should be calculated on the basis of all economic costs, including market interest rates, taxes foregone, depreciation of depreciable assets, and so forth.

A shift in the Economic Report and the Bureau of the Budget away from the administrative budget and toward highlighting the cash consolidated budget should be accelerated, although some progress has been made this year.

Sound policy can rest only on full information. The Government should make it as easy as possible for the concerned persons to understand the costs of Government, the expenditures by function and activities; nothing should be left to guesswork.

The foregoing critical comments on the Economic Report, it is hoped, are constructive and should not be interpreted as a failure to acknowledge much valuable material and analysis in it.

Chairman PATMAN. Thank you, Mr. Schmidt.

Mr. Hagedorn, the director of research for the National Association of Manufacturers, is the next witness.

STATEMENT OF GEORGE G. HAGEDORN, DIRECTOR OF RESEARCH OF THE NATIONAL ASSOCIATION OF MANUFACTURERS

Mr. HAGEDORN. I would like to ask you to include my complete prepared statement in the record, and permit me to summarize.

Chairman PATMAN. That will be done, and you gentlemen may insert any mater that is germane in your statement when you go over your transcript.

(Mr. Hagedorn's prepared statement follows:)

STATEMENT OF GEORGE G. HAGEDORN, DIRECTOR OF RESEARCH, NATIONAL ASSOCIATION OF MANUFACTURERS

The reports of the President and his Council of Economic Advisers contain many useful contributions toward an understanding of the economic issues confronting the Nation. The factual information presented, and the analytical insights contained in the text, provide the raw material for a penetrating appraisal of the economic state of the Nation.

Unfortunately, the reports do not follow the full implications of these materials in drawing their final conclusions and stating their recommendations. My major criticism is that the policy recommendations display a reluctance to attack the basic economic problems of the Nation at their sources, which are clearly revealed by the facts. Instead of correcting the things that are wrong, these reports seem to prefer programs for offsetting their effects by Government action of various kinds. The emphasis on the Federal budget as a tool of economic action reflects this preference.

Nevertheless, the reports of the President and his Council do perform a public service in drawing attention to certain serious current economic difficulties. Among these are: the international balance-of-payments deficit, the need for a higher level of investment to support economic growth, and the damaging effects of wage increases in excess of productivity gains. Although I will have some criticisms to make of the treatment given these subjects, their recognition as pressing problems is a helpful step forward.

The comments which follow are, as you will see, based mainly on the data and analyses contained in the reports themselves. I will seek to draw out certain conclusions which, although clearly inherent in these materials, seem to have been incompletely recognized in the discussion.

Reports of this character are understandably a combination of economic analysis and statements of political philosophy. In the latter connection, I will, in what follows, raise questions in regard to the generally "pragmatic" approach advocated in the Council's report. One gets the impression that expediency, rather than principle, should be our guide. Is this the philosophy the Nation wishes to follow in defining the role of Government in our life?

WAGE, PRICE, AND PROFIT TRENDS

If the materials on wage, price, and profit trends contained in the Council's report are assembled, the following picture emerges:

(1) There has been a persistent tendency in the recent past for the compensation of employees to increase faster than their productivity. Between 1957 and 1961, in nonagricultural industries, average hourly compensation increased at an annual rate of 4 percent, whereas average hourly output increased at an annual rate of only 2.5 percent. (See p. 175 of the Council's report.)

The gap between increases in compensation and increases in productivity represents an increase in the unit cost of production.

(2) The recent past has not been a period of inflationary price rises. There has been some upward creep in the Consumer Price Index due mainly to the service element. But the wholesale price of industrial products has shown practically no change since 1958. In the words of the Council's report (p. 172): "Since mid-1958 there has been stability on the average in the prices of commodities at wholesale and retail, with a continuing upward trend in consumer service prices."

(3) There has been an increasing squeeze on profits during the past decade. Despite the cyclical rise during 1961, corporate profits after tax for that year were only 4.5 percent of gross national product. The only postwar year in which

this percentage was lower was the recession year 1958. If we take three successive 4-year periods, the record has been as follows:

Period—	*Profits as percent of GNP*
1950 through 1953	6.0
1954 through 1957	5.2
1958 through 1961	4.5

NOTE.—The year-by-year record of profits in relation to gross national product is presented in the table at the end of this statement.

These three sets of facts, taken together, are a key to understanding recent economic conditions in the United States. Labor costs have moved persistently upward. However, market conditions have made it impossible for business to pass these higher costs on in the form of higher prices. The result has been a gradually tightening squeeze on profits.

The general sluggishness of the American economy during the past 5 years is, to an important degree, explicable in these terms. Profits are, after all, the driving force for business activity and business expansion. When costs encroach upon profits, marginal activities which might otherwise have been carried on are eliminated. Plans for expansion which might otherwise have been attractive are abandoned.

The Council's report recognizes the squeeze on business profits, but seems to regard it as a *result*, rather than a *cause*, of the underutilization of our national productive capacity. This is strange, in the light of the obvious importance of profits as a directive force in our kind of economy. Also it is a fact, as stated in the Council's report (p. 55), that: "The share of corporate profits in GNP moves closely with the measures of capital utilization, although *it swings somewhat earlier*." (Emphasis added). One would assume that the measure which moved earlier was the cause and the measure which moved later was the result.

The persistence of unemployment at a rate higher than 5 percent since 1957 is a natural result of increases in labor cost which could not be recovered from the customer. It reflects the elimination of marginal employment opportunities which business might otherwise have offered. Further, these cost increases have placed a premium on the types of capital investment which eliminate the need for labor and have discouraged the types of investment which open up new jobs.

The NAM has recently presented its views on the unemployment situation in detail to this committee's Subcommittee on Economic Statistics. For that reason I will refrain from dwelling further on this aspect of the subject.

Incidentally, the wage-price-profit record which has been cited should lay to rest the charge that price increases based on the market power of business are an important source of inflation. In recent years business has not even had sufficient market power to recover its higher costs, much less to raise prices on its own initiative. Even-handed admonitions to both business and labor to exercise restraint, so as to avoid inflation, ignore this obvious fact.

IS DEMAND THE KEY?

A persistent theme which runs through the Council's report is that expansion of demand is the key to both economic growth and high employment. Thus, at one point (p. 68): "The objective of stabilization policies is * * * to keep overall demand in step with the basic production potential of the economy." Later (p. 108): "Faster economic growth in the United States requires, above all, an expansion of demand * * *."

This is a serious misdirection of emphasis. We are suffering in this country from a relationship between costs and prices which depresses the level of economic activity. To describe this situation in terms of "inadequate demand" is not very helpful.

THE INTERNATIONAL BALANCE OF PAYMENTS

The problem of our international balance of payments is of course closely related to the trend in costs and prices in this country. The Council of Economic Advisers has performed a useful service in bringing this problem before the public. In general, their discussion is quite informative. However, I believe they have understated the seriousness of the situation and exaggerated the degree of progress which has been made in solving it.

As the Council states forthrightly (p. 155): "In the new environment of the 1960's the United States cannot continue deficits of the size of the late 1950's."

This is certainly true. But the improvement which the Council's figures show in the "balance on basic accounts" in 1960 and 1961 is hardly cause for concluding that we are moving toward a solution of the problem.

The "balance on basic accounts" omits from the deficit as usually stated the effects of movements of short-term capital out of this country. The large volume of such movements in 1960 and 1961 is one of the alarming aspects of our balance-of-payments position. It is largely the effect of the attraction of higher interest rates abroad, which is a factor restraining our own freedom in respect to interest rates at home.

Our exports depend on economic conditions abroad, and our imports depend on economic conditions in this country. It can hardly be a cause for much satisfaction if we have reduced our "basic" deficit in 1960 and 1961 as a result of the fact that trends in economic activity have not been as favorable here as in many of the other countries with which we trade.

The Council's figures show that, with improving business conditions, our merchandise trade surplus declined during the second and third quarters of 1961. Complete data for the fourth quarter are not yet available to show the full extent of this trend. If the projected improvement in our domestic economy occurs during 1962, there is the possibility of a further decline in our merchandise trade surplus. Thus the outlook for our balance-of-payments position is not a reassuring one.

The balance-of-payments problem has many aspects, but the competitiveness of our products is of central importance. Not much that we do to expand our foreign trade can be very effective if our goods are not priced competitively. As the Council recognizes (p. 167): " * * * price remains at the heart of the matter." However, there is a danger that prices, partly because of the restraint imposed by foreign competition, will not rise but that costs will nevertheless continue to go up. This would result in a further squeeze on profits and an abandonment of some marginal activities in this country to foreign competitors. Thus stability in our price indexes should not be regarded as evidence that we are successfully meeting the problem of foreign competition.

WAGES AND PRODUCTIVITY

Past increases in labor costs have, as indicated, played an important role in creating our present economic problems. For this reason an examination of the relationship between wages and productivity can help in establishing a public understanding of the problem. The Council's discussion of this issue is to be welcomed as a constructive contribution.

In general, I believe that the relationship of productivity and wages is a highly useful tool for broad-gage economic analysis. It is of much more limited usefulness as a tool for the actual conduct of collective bargaining.

The "general guide for noninflationary wage behavior" which the report offers (p. 189) is that "the rate of increase in wage rates (including fringe benefits) in each industry be equal to the trend rate of overall productivity increase." This is an advance over previous discussions which had sometimes left the public with the impression that the relevant guide to wage settlements was the rate of productivity gain in the particular plant or company concerned. It has too often been thought that a noninflationary wage settlement was one which did not lead to a unit-cost increase or price increase for the product of the company or industry involved. The Council's report should help to correct this misconception.

The report lists a number of exceptions to its general rule. It is well to study these carefully, since our economy cannot be put into a straitjacket of uniform formulas. Such special factors as the supply and demand for the particular kind of labor involved, and the pattern of demand for the industry's product, must be taken into account.

One of the specific modifications of its general guidepost which are listed by the Council reads as follows (p. 189):

"Wage rate increases would fall short of the general guide rate in an industry which could not provide jobs for its entire labor force even in times of generally full employment; or in which wage rates are exceptionally high compared with the range of wages earned elsewhere by similar labor, because the bargaining position of workers has been especially strong."

This is interesting because the situation which it describes resembles that which obtains in many of the highly unionized basic industries of the country.

Although the number of nonagricultural wage and salary workers increased by over a million between 1957–61, there was an actual decline in manufacturing, mining, construction, and transportation. On the other hand, substantial gains in employment occurred in the trade and service fields. It is precisely in the highly unionized basic industries that we hear protests against declines in employment and demands for various measures to improve employment security.

It is also true that in a number of basic industries aggressive unionism has in the past led to exceptionally rapid increases in wage rates. Thus, on both the counts mentioned in the Council statement quoted above, wage rate increases in the basic highly unionized segment of our economy should be somewhat below the norm suggested for the economy as a whole. It seems somewhat optimistic to expect that the aggressive unions in these industries would permit such a development to occur. Their members have the same stake as everyone else in maintaining the conditions for noninflationary economic growth.

The Council's general discussion of the subject may be taken as depicting, in broad strokes at least, the type of relationship which ought to hold between wages and productivity. It is in fact the kind of relationship which would prevail if wages were set by supply and demand conditions in a competitive labor market, given a background of monetary policy geared to price stability. It is not the kind of result we have achieved in the past and it is questionable whether we can achieve it when a preponderance of power rests on the labor side in wage bargaining. The solution must be sought in bringing about a better balance, with no excess of power on either side.

There is a danger that the figures on productivity growth named in the Council's report will become the minimum rather than the average for future wage settlements. Reasons can always be found for shading them upward in particular cases. The unions are likely to resist equally valid reasons for shading them downward.

BUSINESS INVESTMENT AND ECONOMIC GROWTH

While I have to dissent from some of the policy recommendations in the Council's chapter on "Economic Growth," it is nevertheless a constructive discussion of the factors which determine the rate of growth. Especially gratifying is the recognition (p. 132) that a high rate of investment "* * * is a major requirement for accelerated economic growth." Economists have of course always recognized that the accumulation of capital is essential to the continued economic development of a nation. However, in recent years this problem has too often been brushed aside on the ground, apparently, that it will somehow take care of itself. The Council's report brings the rate of investment back into focus as a matter for national concern.

The report is also to be commended for its attitude that the average growth rate achieved in the past is not "an immutable natural constant" (p. 111). Practically speaking, there are no limits on the degree to which additional capital formation can accelerate our future growth rate. There is no need to fear that additional accumulation of capital will simply lead to excess capacity since we could not grow fast enough to use it.

The fact is, however, that instead of exceeding past rates of capital formation we have been falling well behind them. This has recently been well documented in a study on "Capital in the American Economy" by Dr. Simon Kuznets, of the National Bureau of Economic Research. I recommend that volume highly to your committee and its staff.

Dr. Kuznets' computations indicate that when periods long enough to eliminate cyclical fluctuations are considered, gross capital formation has remained at approximately 20 percent of gross national product ever since 1869. In other words, a nearly constant proportion of national output has, over the long run, been invested in gross additions to inventories and plant and equipment.

This constant relationship is not a new discovery, and it has sometimes led to a false feeling of assurance that all is well with our rate of capital formation. But, as Dr. Kuznets points out, the rate at which we use up capital has become much greater than in the past. An increasing proportion of our annual investment must go to replacing the part of our capital that is used up currently.

Dr. Kuznets brings out the startling fact that whereas in an earlier phase of our history it took only $1.70 of gross investment to leave a net addition of $1 to our stock of capital, in recent years it has required $3 of gross investment to do so.

As a result, the ratio of net capital formation to net national product has fallen drastically below earlier levels. The ratio fell from 14.6 percent in 1869–88, and 11.2 percent in 1909–28, to only 7 percent in the post-World War II period, 1946–55. Despite the growth of our per capita national income, we are saving a much smaller fraction of it to provide net additions to our stock of capital.

Accumulation of technical knowledge is, of course, an important source of economic progress. But, in the words of Dr. Kuznets: "One persistent bottleneck in the use of knowledge in economic production has been the scarcity of the resources for the production of capital goods needed for the application of new knowledge. Furthermore, since efficient production requires some minimum of capital goods per worker, the growth of population and the labor force requires accumulation of more capital."[1]

The decline in the rate of accumulation of capital must be explained in terms of the factors affecting saving. "In a society such as ours, the basic decisions that determine capital formation are those made by households, business units, and governments in the disposition of their income between current expenditures and savings."[1]

Government action has its chief effect on the savings rate, and hence on the rate of economic growth, through taxation. The main hope of increasing the rate of economic growth in the future lies in reducing the barrier to capital formation imposed by present tax rates and tax practices.

This is implicitly recognized in the administration's proposal to increase business investment through an 8-percent tax credit. The Council's report argues that (p. 132): "The investment tax credit will increase by some $1.5 billion the flow of cash available for investment under conditions anticipated for 1962." But this is part of a package which would make up this revenue loss by other provisions. It is difficult to see how giving $1.5 billion with one hand, and taking the same amount away with the other, could increase the flow of savings available for investment. The chief result of the proposed investment credit would be to distort the patterns of capital formation, rather than to increase them in amount.

The investment credit is inadequate in magnitude, and wrong in character, for achieving the rates of economic growth which are attainable in the future. What is needed is not a new tax stimulant to business investment, but a removal of the existing tax barriers. A practical plan for accomplishing this will be presented later.

THE PRAGMATIC APPROACH

In discussing the question of the division of responsibilities between the public and private sectors, the Council makes the following statement (p. 139): "That issue cannot be settled by the invocation of historical ratios any more than it should be settled by abstract argument. If our economy is to use its productive resources in reasonable accordance with a consensus as to national priorities, we must face the question of public versus private expenditures pragmatically, in terms of intrinsic merits and costs, not in terms of fixed preconceptions."

This is a disturbing statement. It seems to say that in defining the limits of action by the Federal Government we should not be guided by fixed philosophical principles; that past practices and traditional concepts are alike irrelevant. Instead we should consider the various proposals which may be advanced for new forms of Federal activity, one by one, each on its own merits, and without ever looking at the whole pattern in perspective. It is as though we were urged to plan a journey one step at a time, rather than in terms of the destination to which it would lead.

The benefits from a proposed program of Government spending are usually concentrated on a limited group and hence are clearly visible. The benefits which would be derived from allowing taxpayers to spend the money themselves are diffused and not specifically predictable. Thus the pragmatic approach to decisions of this type gives all the advantage to a decision in favor of Government spending.

I do not mean to carp at the Council's choice of words and would not bring this to your attention if it were not that the pragmatic approach pervades a great deal of the report. As a result the Council's recommendations in a number of sections strike this reader as a rag bag of miscellaneous proposals for Gov-

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[1] Both quotes from Simon Kuznets, "Capital in the American Economy," Princeton University Press, 1961, p. 391.

ernment intervention rather than as a program carefully designed to meet the specific problems revealed by economic analysis. Thus, it is conceded that the current unemployment problem is not to any important degree a matter of structural unemployment. Nevertheless a whole series of programs are suggested for rescuing the alleged "victims of progress." Despite the recognition in the report that the level of education of our population has been dramatically raised in the past, it advocates a number of measures for new forms of Federal intervention in this field.

Surely we need something better than this concept of a pragmatic approach, to guide us in defining the role of Government.

CONCLUSIONS AND RECOMMENDATIONS

Discussions of the economic state of the Nation inevitably concentrate on the unsatisfactory aspects of our economic situation rather than on the areas in which all is going well. This is as it should be, since there is no point in wasting time on self-congratulation when we know that we can and should be doing better. Still, we should not allow ourselves to be misled by this emphasis on problems and failures to a belief that the current situation calls for desperate emergency remedies. It calls rather for a calm analysis of why and how our present economic problems have arisen, and the devising of measures logically designed for dealing with them.

I would suggest that there are two central problems in which economic policymakers should be concentrating. They are:

1. *Increases in labor costs which under present market conditions, cannot be passed on in higher prices.*—The consequent reduction in profit margins means that certain marginal business operations which might otherwise be attractive are simply not undertaken. The underutilization of our national productive resources in the period since 1957 is mainly due to this situation.

(In order that there be no misunderstanding, it should be emphasized that the solution should not be sought in creating conditions which would make it possible to pass the increased costs on in higher prices. This would be to use inflation as the cure for unemployment. Even if this were desirable, it is simply not feasible, given the present U.S. balance-of-payments position.)

2. *A reduction below historical levels in the rate of net capital accumulation in our economy, due mainly to the impact of our present tax system on business and personal saving.*—This has created a bottleneck to the long-range growth of our national productive potential.

The solution to the first of these problems must be sought on many fronts. In part the problem is a carryover from bad practices which developed in the early postwar period when wage increases could be passed on and therefore did not create unemployment. We neither can nor want to re-create the conditions of that era. Better general understanding of the damaging effects of labor-cost increases will be helpful in correcting this difficulty. The administration's attitude, as expressed in the reports under review, is a contribution to that end.

In addition, some means must be found for redressing the balance of power in collective bargaining. There is a preponderance of power on the labor side. The clearest evidence of this is the continuation of increases in labor cost even in a period when unemployment has remained above acceptable levels.

On the second problem, the inadequate rate of net capital accumulation, I am able to be more definite. What is clearly needed is a thoroughgoing overhaul of our Federal tax system at the points where it specifically acts as a barrier to saving and capital formation. These are:

1. Steeply graduated individual tax rates.
2. Excessive top rate of corporate tax.
3. Unrealistic length of lives and classification of depreciable property.
4. Taxing of gains on transfers from one investment to another, and destructive rates of estate and gift taxes. Both of these are burdens on capital directly rather than on income.

Fortunately, there is now before Congress a carefully spelled-out practical tax measure for dealing with these four barriers to economic growth. It is embodied in the identical bills H.R. 2030 and H.R. 2031, now before the House Ways and Means Committee and popularly known as the Herlong-Baker bills. I recommend this proposed legislation as the most constructive measures this Congress could pass.

Profit record—1947 to 1961

(Dollars in billions)

Year	GNP	Profits before tax	Profits after tax	Profits as a percent of GNP	
				Before tax	After tax
1947	$234.3	$29.5	$18.2	12.6	7.8
1948	259.4	33.0	20.5	12.7	7.9
1949	258.1	26.4	16.0	10.2	6.2
1950	284.6	40.6	22.8	14.3	8.0
1951	329.0	42.2	19.7	12.8	6.0
1952	347.0	36.7	17.2	10.6	5.0
1953	365.4	38.3	18.1	10.5	5.0
1954	363.1	34.1	16.8	9.4	4.6
1955	397.5	44.9	23.0	11.3	5.8
1956	419.2	44.7	23.5	10.7	5.6
1957	442.8	43.2	22.3	9.8	5.0
1958	444.5	37.4	18.8	8.4	4.2
1959	482.8	46.8	23.7	9.7	4.9
1960	504.4	45.0	22.7	8.9	4.5
1961	521.2	46.1	23.3	8.8	4.5

Source: Economic Report of the President, January 1962. Tables B-1, p. 207; B-62, p. 279.

Mr. HAGEDORN. I would like to proceed then by summarizing briefly the comments we have to make on the Economic Report of the President and the report of his Council of Economic Advisers.

I agree with Mr. Schmidt that this is on the whole a very good report. It contains a large amount of factual material that is extremely helpful in appraising the current state of the economy and examining the real nature of the problem that is before us. Not only is the factual material good, but I would say also that in the text there are many insights that are also helpful in studying the economic condition of the country.

Unfortunately, I have the same feeling that Mr. Schmidt does, that the Council doesn't quite, in the end, tie it altogether. They don't quite face all of the implications that are clear in their own analysis.

It seems to me that the fundamental place to start appraising the state of the Nation at this time is with the analysis of prices, wages, and profits. The Council, of course, has gone into this subject in great detail and provided a great deal of material on it. And drawing on that material, we can see, first, that in the recent past wages have gone up faster than productivity.

Wage costs per hour in the period 1957 to 1961, according to the Council's figures, have gone up at a rate of about 4 percent a year; whereas output per man-hour has gone up at only about 2½ percent a year. In the period prior to 1957 the gap was wider than that. But the gap still continues with the result that unit labor costs have been rising.

Now, when we look at the price picture, we find that the period since 1958 has not in particular been a period of inflationary price rises. There has been some upward pressure in the Consumer Price Index largely because of the service element. But, as the Council report itself states, prices of commodities have not increased since about the middle of 1958.

So, we have this relationship—an increase in unit labor costs with no increase in prices.

In other words, the situation has been such that market conditions have prevented producers from passing on their higher costs to the customers.

Now, we would conclude that there must have been a squeeze on profits resulting from that situation. And when we turn to the profit figures and relate them to the size of the economy, we see that has indeed occurred.

Attached to the end of my prepared statement there is a summary table relating profits after taxes to gross national product. If you will look down the last column of that table, you will see that there has been almost a persistent decline in this ratio in the postwar period. There is a decline from the levels of 6, 7, or 8 percent in the early postwar years down to between 4 and 5 percent in more recent years.

In 1961, profits as a percent of GNP were 4½ percent. That is the lowest figure, with the exception of the recession year, 1958, that we have recorded in the postwar period.

Now, of course, I am not giving you this information on profit trends with the intention of making a plea that you should feel sorry for the people who earn profits. It is not a plea for sympathy at all; but rather the point is that profits are the driving force and it is the expectation of profits that causes people to carry on productive activities and to expand their productive facilities.

If the opportunity for profit is curtailed, there is less economic activity and less expansion. I think that fundamental situation is important. Cost increases continue in a period when they could not be passed on in the marketplace to the customer, this encroaching on profits, and therefore putting a sort of weight on the whole economy that prevents it from really attaining a level that we could consider satisfactory, and really moving ahead.

Now, as I said, and as Mr. Schmidt mentioned, the Council recognizes all of these things. They have a chart showing the reduction in profits and yet they don't quite face the implication of it.

Their discussion of profits rather creates the implication that profits or the decline in profits in relation to gross national product is a result of the decline in the rate of utilization of our capacity rather than a cause of it. Now, that seems to ignore the whole rôle of profits as the central driving force in the private sector of our economy.

Then, too, there is the emphasis on demand that runs all through the Council's Economic Report. This seems to me to evade the real issue here. If the problem is one of a distortion in the relationship between costs and prices, then to say that we need more demand is to misread the whole situation entirely.

The insufficiency of demand explanation of why we have unemployment now and why we have had a retardation of growth is, at the best I could say, a misplacement of emphasis. But I think we can go beyond that, and say it is completely misleading.

Of course, where you have a situation, where costs are encroaching upon profits because prices cannot rise to take care of the higher costs, just discussing it as an abstract problem, there can be two ways to handle it. You could take the pressure off the top and let prices rise, so again you would have a satisfactory margin, or you could reduce the pressure on costs from beneath. Now, as a theoretical point, you have those two choices.

However, in the present state of affairs, to choose the first one, that is, to take steps to cause prices to rise so that profits would be better and therefore more people would be employed and expansion would be accelerated, is a rather impractical step and a very dangerous one in the light of our balance-of-payments situation. What such a step would amount to is to decide that we prefer to have inflation in the country rather than accept unemployment.

That choice may have been before us in some periods in the past, but it is now now a real option in the light of the balance-of-payments condition of this country. We would price ourselves out of more markets by choosing the inflationary solution to unemployment. I think, in the long run, trying to pursue such pattern would lead to disaster.

Well let me drop that subject for the moment and go on to what I think is the other major problem before the country.

The Council in its analysis, I think, quite helpfully divides the discussion into a chapter on the current underutilization of resources in the country, how that should be dealt with, and what causes it, and the question of long-range growth in the actual potential rate of the country.

Now, what is the chief determinate of the longrun growth rate in the country? I believe it is the rate of investment in new physical assets. It is certainly true that the quality of our population, the skills of our labor force, and the education of our people, and the development of new technology has an important role in the growth of our economy.

But, the bottleneck comes in the fact that you need money, and you need physical investment to carry out new technologies that are devised to make use of the new skills. I believe that Mr. Kuznets' book "Capital In American Economy," with which I believe the committee is familiar, since it has been mentioned in your literature, presents a very illuminating discussion on what has been happening in this country.

It is, of course, a very long perspective of our economic situation. It reveals the fact that the rate of accumulation of capital has declined rather drastically over our history. We hadn't fully realized it up to the time that Mr. Kuznets' book was published.

If we look at figures on what is called gross capital formation, that is, the gross acquisition of plant and equipment and inventories and the other forms of capital, it seems to have stayed at roughly the same percentage of our gross national product as far back as the Civil War, or back as far as we have statistics.

It has remained about 20 percent of GNP. But this is the gross figure and it does not reflect the net addition to our stock of capital in this country. From it we have to deduct the current using up of capital through depreciation, loss by accident, and so forth. The fact revealed in Mr. Kuznets' analysis is that this rate of capital consumption has grown much faster than the rate of gross capital formation in the last 90 years. Proportionately, we need to devote a much larger percentage of our gross additions to capital just to replace what is currently being used up in the way of capital consumption.

I think Mr. Kuznets' figures show that in the late 1800's, it took $1.70 of new capital to give you $1 of net addition to the capital stock of the country. That is the 70 cents would be used to replace the current using up of capital. Now, it takes $3 of gross capital formation to provide $1 of net addition to the capital resources of the country. Our failure to realize fully this has misled us in the past. But, when capital consumption is taken into account, it can be seen that our current rates of net capital formation are substantially below those in the historic past of the country.

Now, what determines the rate of capital formation? It is the savings habits of the people. Capital, in essence, is what we save out of our current production. Again in Mr. Kuznets' analysis, the chief reason for a reduction in our rate of saving over this long historical perspective has been the growth in the Federal expenditures and in Federal taxations, taking away from the people the amounts that they would otherwise save. So if we are to improve our long-term perspectives in this country, the chief means we have of approaching that problem is through a reduction of the tax burden on the country.

This is implicitly recognized by the Council's analysis when they suggest that the proposed 8-percent investment credit would be a way, using their words, to stimulate the growth of capital in the country. And it would provide, they estimate, an additional $1.5 billion in cash flow for the creation of new capital.

The National Association of Manufacturers, however, believes that this is not the way to approach that problem. In the first place, the proposal is part of a package which would give 1½ billion with one hand and take it away in various other forms and various other aspects of the tax system with the other hand. In effect, leaving no net addition to cash, it is hard to see how that could increase the rate of saving in the country.

Also, even deeper than that, our people in the National Association of Manufacturers feel that if the tax system, with its high rates and with other incentive features of the tax system, has been a barrier to saving and capital formation, we shouldn't try to relieve that situation by adding another gadget that would offset the bad effects of other parts of the tax system.

We should deal with the parts of the tax system that have this bad effect. In other words, we should remove the hurdles rather than giving the runner a stimulant so he can jump over the hurdles.

Now, these are the two problems on which I believe that attention should be concentrated at this time. The first is the encroachment of rising labor costs upon profits which control the rate of growth in the economy, and has resulted in an underutilization of our resources and unemployment in the present period. The second problem is the present high tax rates which siphon off capital needed for investment.

The Council has a discussion of the relationship between productivity and wages, which of course is one approach in dealing with this first problem of restraining the growth of labor costs so that they would not continue to have this repressive effect on the economic activity. On the whole, I think that that discussion in the Council's report is a very helpful and useful analysis of this complicated problem, and I think that it adds some new points that haven't been sufficiently analyzed and understood in the past.

For example, the point that insofar as productivity is used as a guide to wage determination, it should be the productivity of the economy generally rater than the productivity of the particular plant or company concerned. This has been misunderstood in the past, and I think it is helpful to have it set forth rather clearly in the Council's statement.

Also, the Council recognizes that you cannot tie the whole wage structure of the country to one rigid formula. And it recognizes that there must be exceptions in many cases and that you must either shape upward or downward the general rule in applying productivity to a particular case, depending on conditions in the labor market in that industry, and also conditions in the market for the product of that industry.

The conclusion I come to, however, after contemplating this material, is that the relationship between wages and productivity is a highly useful tool for economic analysis, for people like your committee and like us sitting at this table to understand what is happening in the economy. I am much more doubtful as to the extent to which it is a practical tool for operating on the ground, so to speak, in the actual conduct of collective bargaining.

First, realize particularly we have to recognize many exceptions. And having done so, in a particular case, the exceptions tend to swallow up the general rule. And I certainly agree that these exceptions should be fully recognized, and you can't apply a general rule rigidly, but the danger is that when this general rule has been announced, it will become a minimum in wage negotiations rather than the average.

Reasons can always be thought of for shading it upward, but where you have strong and aggressive unions, it is extremely unlikely that they could be persuaded that there were convincing reasons for shading it downward.

But, above all, I think that we can accept the picture of the relationship between wages and productivity given in the Council's report as in broad gage terms—at least a picture of the relationship that ought to hold in our economy.

The fact is that the relationship hasn't held in the past and I am rather doubtful as to whether merely outlining this picture is going to be sufficient to cause things to work out that way in the future. In the past, wage increases have been substantially higher than the growth in productivity and the cause of this, I believe, I would analyze in the same terms as Mr. Schmidt. It has been partly the result of Government action, for example, in the minimum wage field, and it is partly the result of the very strong power of industrywide unions being able to exert much more bargaining power than the industry people who sit opposite them across the bargaining table.

This is a question to which I cannot find any easy answer: "How you are going to equalize the bargaining power so you will get a more rational relationship between the growth in productivity and the growth of wages in the future negotiations?"

I would concur with the CED policy that was included in the last page of Mr. Yntema's statement, that this is certainly something that should concern us deeply, and we should be seeking the solution to it.

On the question of the long-range growth and how to provide more capital for long-range growth, I would say that there is a practical way of handling this, in the long run, by reducing the tax burden so that people will have more income to save and will be able to provide a greater rate of capital accumulation in the future. That is the Herlong-Baker approach, the bills introduced by Representatives Herlong and Baker, which are now before the House Ways and Means Committeee.

In essence they provide for a reduction in taxes and elimination of some of the features of the tax system which are most restrictive to the accumulation of capital by allocating the increase in revenues which results from economic growth to that purpose, rather than simply allowing it to be taken in increased Government expenditures in the future.

That, Mr. Chairman, is a summary of my statement.

Chairman PATMAN. Thank you very much, sir.

Mr. YNTEMA. I would like to ask you one question, please, sir.

You mention about the power of the President, as proposed, to reduce taxes. Would you be in favor, under certain conditions, with certain limitations and restrictions, of permitting balancing of the budget—in the event Congress has adjourned leaving an unbalanced budget—by providing the President with power to increase taxes?

Mr. YNTEM. Mr. Chairman, speaking for the Committee for Economic Development, I think their view is that the really important thing is to have this understood, and that the particular mechanisms by which you do it are something for the Congress and the President to debate. We do not have a firm opinion one way or the other as to how it should be done.

Chairman PATMAN. I know, but if you are in favor of giving the President the power to reduce taxes, would you not be in favor of giving the President the power to increase them in certain cases?

Mr. YNTEMA. I do not think the committee has a position on that.

Mr. SCHMIDT. I think that is a very good question, Mr. Chairman, and I alluded to it in my statement. I think logically you almost would have to say the administration should have the power, because the Congress may not be in session.

Chairman PATMAN. Particularly if the Congress were to adjourn leaving an unbalanced budget when times are good.

Mr. SCHMIDT. Or if the situation is such that it generates an unduly big surplus, perhaps taxes ought to go up; although I am not in favor of this; I think you people ought to decide these things, and not the President. But I think if you were going to favor discretionary tax cutting power, you would logically have to think about this point you are raising.

Chairman PATMAN. What do you think about that, Mr. Hagedorn?

Mr. HAGEDORN. The NAM would be, I think, opposed to giving the President discretionary power in either direction.

Chairman PATMAN. In either direction?

Mr. HAGEDORN. Yes, sir.

Chairman PATMAN. Let me ask you another question, sir.

With reference to the administration's budget for fiscal 1963, do I understand that your analysis leads to the conclusion that either planned spending is too low or the tax receipts will be too high?

Mr. YNTEMA. Mr. Chairman, of course, I am speaking for myself. The committee has not taken any position with respect to the 1963 budget.

My own question is whether or not the estimate of GNP and the estimate of the receipts and expenditures are correct. If you assume them to be correct, I think there is a real question whether the full employment budget surplus may not be too high. But this is based on the assumptions of the Council, with which I am not sure I am in complete concurrence.

Chairman PATMAN. You say that Congress has no reliable machinery to insure that the budget will hit the administration's target, or any other target.

Do you have any suggestion for improving this situation?

Mr. YNTEMA. May I read from our statement on fiscal and monetary policy?

> We have previously suggested that relations between expenditures and revenues and the effects of the size of the budget on growth should be considered by a Joint Budget Policy Conference that would include several members of the leadership and majority and minority representations from the appropriations and revenue committees. This group, which should be fairly small, would meet periodically during the course of a session to consider revenue-expenditure problems. Its major function would be the study of current fiscal policy and the long-run effects of the budget. * * * A useful precedent for such a Joint Conference in a closely related field is the Joint Committee on Internal Revenue Taxation.

Our point is that there ought to be some mechanism for continuous review as matters develop in the Congress.

Chairman PATMAN. Mr. Reuss?

Representative REUSS. I want to congratulate all three organizations represented here today, organizations which in one way or the other represent the business community, for your thoughtfulness, fair-mindedness, and obvious desire to help this committee. I am really greatly encouraged by the general measure of agreement which you gentlemen have displayed with the goals and outlines presented by the President's Economic Report this year.

I say that with full awareness of points on which you disagree, for your critical appraisals are very helpful to this committee. But I want to start right out by expressing my gratitude to you there.

I am going to use the rest of my time questioning some of your assertions.

Mr. Hagedorn, you deduced from the recently published study by Dr. Kuznets, that there does not seem to have been enough saving and capital formation in recent years to fulfill the growing needs of the economy. And on the last page of your report, you suggest the easing up in rates on estate and gift taxes, as one method, I take it, of providing more available capital for investment.

Mr. HAGEDORN. That is right.

Representative REUSS. Elsewhere in your presentation, you have quite rightly, I think, asked for the evolution of general philosophical principles to govern economic decisions, and I think that is a good idea.

I would ask you: What do you think is a sound philosophical principle governing our estate and gift tax rates?

I will confine it to that, because it is in a sense one aspect of the problem. Obviously, if you had no estate or gift taxes, you would have a greater volume of private savings and, therefore, presumably more funds for investment in bricks, mortar, machinery, and other forms of capital.

I take it you do not suggest that we abolish the gift and estate taxes, any more than I would suggest that we make their rates 100 percent; but what advice can you give us on a general philosophy of rate structure?

Mr. HAGEDORN. Well, since you have asked for a general philosophy, I will answer your question in philosophical terms.

If we had a pattern in this country of wealth accumulation and the passing of that wealth down through generations, which resulted in a continual accumulation of wealth in certain families, so that the same families came to own more and more of the country's wealth, I would say then we had the wrong kind of estate and gift tax system. If that were the case we would have to have an estate and gift tax system that would prevent the development of classes into which people were placed by their birth; so that there was a continuous accumulation and certain classes would get richer in each generation and therefore be able to save even more in that generation, and the in the next generation have an even larger percentage of the wealth of the country.

If that was the result of our systems of estate and gift taxation, I would say it was wrong; that we should place a greater burden on estates and gifts.

Since we do not see that happening, then we must recognize that the estate and gift taxes are a burden on the capital of the country. They deplete the capital of the country. They do in either case, but they might be justified in the former case.

Now, that is a very broad philosophical principle. And just how you would apply that in a detailed statistical study of how high the estate and gift tax rate ought to be, I do not know.

But what we do see in the country is not such an accumulation, not the continuous development of certain families, in which each generation acquires a larger percentage share of the wealth of the country. That has not been happening.

So as a practical matter, we can be assured that we do not have to worry about that question.

Representative REUSS. Thank you.

In your statement, Mr. Hagedorn, you give the profits as a percentage of GNP for the last 12 years, showing that the percentage has been declining.

Mr. HAGEDORN. That is an abstract from the longer table at the end.

Representative REUSS. Do you have a table which shows what has happened, not just to profits, but to depreciation reserves over that period?

It seems to me if you are talking about the amount of funds available for capital investment, you would have to include those, too, would you not?

Mr. HAGEDORN. Well, that information is available for gross capital investment, but it is in no sense part of the incentive that causes people to undertake business operations.

The point in the discussion where this table was introduced was that the decline in rate of profit has reduced the incentive in the economy, the factor that leads to expansion and leads to full utilization of our resources. That was the point that was being made, where these figures were cited.

Now, the merely getting your money back as you use up your capital is in no sense an incentive to go out and invest.

Representative REUSS. It does, however, provide the wherewithal to go and do them if you somehow have the incentive, does it not?

Mr. HAGEDORN. Well, at best it provides you with the money to replace your equipment and your plant as it wears out.

Now, in many cases it is not even sufficient for that, because of the accounting methods that are traditionally used, based on historical cost rather than the current cost of replacing the real value.

Representative REUSS. But in any case, you do not have available a similar comparison, which would include depreciation and depletion allowances as well as profits?

Mr. HAGEDORN. I believe the Council has a table. I do not know whether I can put my finger on it right at this moment.

Representative REUSS. I will ask the staff to see if they can find it for me. Thank you.

(The material referred to follows:)

Sources and uses of corporate funds, 1950–61 [1]

[Billions of dollars]

Source or use of funds	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961 [2]
Total uses	36.5	36.8	27.3	28.2	24.0	45.1	39.5	37.8	31.5	45.2	39.1	42.1
Plant and equipment outlays	16.9	21.6	22.4	23.9	22.4	24.2	29.9	32.7	26.4	27.7	30.8	30.4
Inventories (book value)	9.8	9.8	1.3	1.8	−1.6	6.7	7.6	2.1	−2.4	5.7	3.0	2.2
Customer net receivables [3]	5.0	2.0	3.1	.7	2.4	6.4	3.3	2.1	2.9	5.5	5.5	4.8
Cash and U.S. Government securities	4.5	2.8	.1	1.8	(4)	5.0	−4.3	−.3	2.6	3.6	−3.1	1.5
Other assets	.3	.6	.4	(4)	.8	2.8	3.0	1.3	1.9	2.7	2.9	3.2
Total sources	35.4	36.9	28.1	30.0	22.4	44.8	42.4	40.1	35.7	48.0	41.4	44.4
Internal sources	20.8	19.0	17.8	19.7	19.8	26.6	27.8	28.0	26.0	30.6	30.3	32.1
Retained profits and depletion allowances	13.0	10.0	7.4	7.9	6.3	10.9	10.5	8.9	5.7	9.1	7.4	[5] 7.7
Depreciation and amortization allowances	7.8	9.0	10.4	11.8	13.5	15.7	17.3	19.1	20.3	21.5	22.9	24.4
External sources	14.6	17.9	10.3	10.3	2.6	18.2	14.6	12.2	9.8	17.4	11.1	12.3
Federal income tax liability	7.3	4.3	−3.1	.6	−3.1	3.8	−1.7	−2.2	−2.5	2.4	−1.5	(4)
Other liabilities	1.0	1.9	2.4	2.2	.4	2.1	3.0	2.1	1.8	2.0	1.5	1.2
Bank loans and mortgage loans	2.6	5.4	3.1	.4	−.6	5.4	5.4	1.7	1.1	5.2	3.1	1.7
Net new issues	3.7	6.3	7.9	7.1	5.9	6.9	7.9	10.6	9.4	7.8	8.0	9.4
Discrepancy (uses less sources)	1.1	−.1	−.8	−1.8	1.6	.3	−2.9	−2.3	−4.2	−2.8	−2.3	−2.2

[1] Excludes banks and insurance companies.
[2] Preliminary estimates.
[3] Receivables are net of payables, which are therefore not shown separately.
[4] Less than $50,000,000.
[5] Preliminary estimate by Council of Economic Advisers.

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

Mr. Schmidt, I want to express my complete concurrence with what you have to say about education, and particularly the process by which State education boards have given a misplaced emphasis on unnecessary pedagogy, courses in educational psychology, educational philosophy, et cetera, at the expense of basic excellence in philosophy, psychology, the sciences, languages, and mathematics. I am delighted to see this set out so clearly here, and I would leave this thought with you.

You represent a very powerful organization, organized in almost every large community in the country, and certainly in every State. There is not really very much that the Joint Economic Committee or the Congress can do about State educational requirements, or that it should do. However, I would hope that the chambers of commerce, which are your constituent organizations, could do something, particularly at the State levels, where in all the 50 States you are well organized and know how to present matters to State legislatures.

I do not believe—I do not say this disparagingly—that you have so far done anything in this vein. Is that correct?

Mr. SCHMIDT. I believe Montgomery County, here in Maryland, has just adopted a merit salary scale. I think it is the largest school system, or the second largest, in the entire United States which has done this. It has tried to put the salary scale on a merit basis rather than this annual or biennial wage increase, regardless of competence or achievement of teachers, and so on. So there is a little movement, there, that I think is in the right direction.

Representative REUSS. My question was whether the chambers of commerce at the State level had presented to the various State legislatures the views here expressed, particularly in points 1 and 2 of your presentation, that State teacher certification procedures should be amended and improved to emphasize the subject matter and to deemphasize unnecessary pedagogical courses.

Mr. SCHMIDT. Well, a great deal has been done. I do not happen to have any quantitative evidence that I could lay on the table here today, but we have an educational department in our headquarters here devoted exclusively to this kind of problem, the promotion of better administration, schools, teachers' salaries, and so on.

I think we have organized somewhere between 1,000 and 2,000 committees at the local level, of businessmen and professional men, who are concerned with upgrading the school systems. I know they have had an impact. How to quantify that is a little difficult.

Representative REUSS. I want to commend you and your organization on it and express the hope that throughout the country your local committees will address themselves to whatever the certification methods are in their State, and if, as is so very frequently the case, there is an undue emphasis on unnecessary pedagogy at the expense of subject matter, they do what they can to make that view known.

Chairman PATMAN. Senator Proxmire?

Senator PROXMIRE. Mr. Yntema, your name has been prominent in so many respects, and you have done such a fine type job that I have been wondering how you pronounce your name.

Mr. YNTEMA. Yntema.

Senator PROXMIRE. Mr. Yntema, in your statement, you say, as your item (c):

> Accepting actual departures from this target surplus, below in recession and above in boom, that result from automatic responses of tax yields and expenditures, has beneficial stabilizing influences on the economy.

It was a little bit difficult for me to determine by what followed whether you would view the present budget, in view of the increase in the GNP—as meeting this particular criterion.

Mr. YNTEMA. The 1963 budget?

Senator PROXMIRE. That is correct.

Mr. YNTEMA. Well, this criterion would be better, anyway, if you simply leave the tax receipts and expenditures programs alone.

The question with respect to the budget is whether the target surplus and high employment is appropriate. And I would say the 1963 budget, as far as we can tell, is approximately within the range that we would consider appropriate.

Senator PROXMIRE. It seems to me there are a couple of things to to consider. One is the actual amount of unemployment, and so forth, that you have at the end of the fiscal year projected. The other is the direction in which the economy is moving.

In view of the fact that there is expectation that we will be expanding at a rapid rate compared with our historical experience, during the coming year, I wonder if you would regard this very slight surplus, almost negligible, as adequate to contain the inflationary forces that might develop.

Mr. YNTEMA. Well, we have to distinguish as to the actual surplus that occurs and the economic conditions. In a depression, for example, we run a deficit. In the first half of 1963, at the annual rate, the surplus would be about $10 billion.

Senator PROXMIRE. What surplus are you talking about? You are not talking about the administrative surplus?

Mr. YNTEMA. I am talking about the surplus on the national income account.

Senator PROXMIRE. Where do they indicate that?

In that chart I do not get a $10 billion surplus. Maybe I misinterpreted this.

The first half of the year, there is about a $2 billion annual rate surplus, and then the last half of the fiscal year a $6 billion annual rate surplus; because at the bottom it says—

Seasonally adjusted annual rates, data for half year.

To aggregate the surplus here, it seems to me, would be wrong. You have to average it. It would be a surplus of about $4 billion.

Mr. YNTEMA. I am sorry. What I was talking about was the first half of 1963. And the total is about $8 billion. That is the last part on the right side of the chart.

Senator PROXMIRE. That bar looks to me like about $6 billion.

Mr. YNTEMA. The scale for that, you see, is $5 billion and $10 billion, and this runs a little short of $10 billion.

Mr. SCHMIDT. That is including the actual plus the full employment.

Mr. YNTEMA. What I am talking about is the surplus if we have full employment.

Senator PROXMIRE. Then it is under different conditions than the actual.

Mr. SCHMIDT. Than the one that is projected.

Mr. YNTEMA. But what we suggest is that this is what we ought to look at in the budget policy, what kind of surplus we would have if we had a high level of employment.

Senator PROXMIRE. I very much appreciate your stress on the income accounts, rather than on the administrative budget. I think there is no question that that seems to be better.

Then you say in (*d*)—

Accompanying this budget policy with a strong, flexible use of monetary policy.

Would you regard the policy we have presently and have had over the past few months as meeting this criterion?

Mr. YNTEMA. I think it is probably as strong and flexible as you could have in the circumstances. I think the circumstances are somewhat unfortunate. This is the last point we make in this document, that there is an underlying problem with respect to the underlying pressure in wage.

If we did not have any cost push in the economy, we could have, of course, a more liberal monetary policy, a more expansive monetary policy. And this ties in with the balance-of-payments problem.

Senator PROXMIRE. Well, the balance-of-payments problem is one that we have constantly had before this committee. This is the first time I have had this tied in with the cost push, which I consider to be a little distinct and different from the monetary effect, because as I understand the monetary impact, it is a demand impact on aggregate demand. The cost push is something that is exerted independently or purports to be somewhat independent.

Mr. YNTEMA. What I am saying is that the existence of the balance-of-payments problem puts a limit on what you can do with monetary policy, because if you have a more liberal monetary policy, easier credit and lower interest rates, this is likely to complicate our balance-of-payments situation.

Senator PROXMIRE. Now, the usual interpretation has been a little more direct, that if our interest rates are too low, we have an exodus of short-term capital, which takes advantage of higher rates abroad, moves abroad and this aggravates our unfavorable balance of payments. We try to contend that the Federal Reserve should do a lot more than it has done in keeping long-term rates high and the short-term rates lower.

Mr. YNTEMA. Senator, let me go back a minute. What I am saying is that I think the cost push is at the heart of our balance-of-payments problem. Now, of course, there are other outside factors that have brought this about—such as a very rapid rate of growth abroad. The future of our balance-of-payments problem is going to be tied, of course, to how our price level behaves. And the balance-of-payments problem does set practical limits on the ease of monetary policy. We could have an easier monetary policy if it were not for the balance-of-payments pressure.

Senator PROXMIRE. I see. Now I understand the point you are making.

Now, you say—and this is at the bottom of your first paragraph—

> If the Council's estimates are correct, the question of whether the contemplated budget and monetary policy will permit us to get and keep high employment needs further examination.

Does this mean the budget may be too restrictive?

Mr. YNTEMA. We think it possibly may be; although it comes very close to what we think is appropriate. And as another caveat, we have some doubt about the estimate of potential GNP in these circumstances.

Senator PROXMIRE. You overestimate the GNP and underestimate the Government expenditures?

Mr. YNTEMA. Yes. That is possible. That is two questions. But given the assumptions, then I would say there is a possible question here as to whether the surplus may be too big. I am not sure the assumptions are correct, however.

Senator PROXMIRE. You think expenditures may increase?

Mr. YNTEMA. More than indicated. And the GNP may be too high. So that my guess is that the budget is probably in the ball park as far as our general conditions that we set forth are concerned.

Senator PROXMIRE. You say:

> To carry out the purposeful budget policy on which there is growing agreement, more effective machinery in the Congress is needed.

Well, the President has already asked us to give up I think an awful lot, and I am just wondering how much we can turn over to him. If we seek to give him the discretionary power over public works spending—as I understand, the thrust of your suggestion here is that the machinery is too slow in Congress, and the specific proposals when you reduce this to specifics is always in the direction, it seems to me, of congressional surrender of power.

Mr. YNTEMA. That is not our intention. All we suggest is that there be a continuing joint conference with respect to these matters.

No, it is not our intention that the Congress surrender power to the President.

Senator PROXMIRE. In connection with that, are you saying, that:

> What is desired is not to tip the balance of power between the President and the Congress but to obtain a prompt decision. An alternative way of doing this would be to provide that the President's proposal to change the tax rates should take effect only if approved, as in the case of ordinary legislation, by a majority of each House—

and so forth.

Would you suggest this as a preferable alternative to the President's proposal that we act to give him the power, the discretion, to reduce taxes?

Mr. YNTEMA. Our position is that the most important thing is that there be some way of getting this done. We do not think it is necessary to delegate the power to the President. This would be an alternative that would be perfectly satisfactory.

Senator PROXMIRE. It is pretty important that CED then takes the position that it is not necessary for the Congress to give up this power; that if they arrange some kind of an understanding on the kind of tax cut, for example, and let Congress decide whether to reduce taxes or not, you feel that would meet the objective?

Mr. YNTEMA. Yes.

Senator PROXMIRE. And you prefer it?

Mr. YNTEMA. We have not provided anything definite. The important thing is that some arrangement be made so that it can be done. And we think this is something for the Congress to decide.

Senator PROXMIRE. Well, your first clause indicates that you would prefer this. You say, "What is desired is not."

Mr. YNTEMA. That is correct.

Senator PROXMIRE. And what the President is asking does tend somewhat toward determining the balance of power between the President and Congress.

Mr. YNTEMA. I think that is correct. And we suggest this as a possible means of accomplishing this. I do not think it is necessary to delegate the power to the President. We think it is necessary to have some arrangement such as this, so that there will not be interminable debate and amendment when the proposal comes before the Congress.

Senator PROXMIRE. Now, you say:

We are greatly concerned about the longrun growth of the budget.

This is refreshing. We have had prominent economists in the last couple of days here, who argued that the long-term growth of the budget is desirable to expand the economy and to promote growth, and they follow the OECD recommendation, with which you are familiar, which also recommends that the increased taxing and spending together, even with a balanced budget, promises growth.

I disagree with this viewpoint. Maybe it is just a kind of an instinct and hope. I am hoping to get some substantial economic support for my position, but most of the economists seem to disagree, and feel if we are going to grow we have to think in terms of a constantly bigger budget, and that the budget should at least keep pace with the GNP and maybe move a little ahead of the GNP if we are going to expand.

You express the opposite viewpoint. I would like you to document it.

Mr. YNTEMA. I would agree entirely. Suppose, for example, we should have peace in the world and you should do away with military expenditures. We could grow more rapidly. There would be more resources for capital investment. The Government is not the only agency that can spend. The families could spend. I could rather spend my own money for things I want than to have someone else decide what is to be spent. I do not think there is any basis in this.

Senator PROXMIRE. I think that is right. But we had as prominent and as middle-of-the-road and conservative an economist as Professor Wallich, who was one of President Eisenhower's economic advisers, who told us yesterday that there is a mathematical relationship between the expansionary effect of (*a*) running a deficit, which of course tends to be inflationary and expansionary, and (*b*) just having a bigger budget. He claimed that, as I understand or recall, it was something like 2½ times, in relationship to the amount involved, as expansionary to run a deficit as to increase Government spending and taxing together. But they have the effect of pushing the economy ahead, of promoting growth, of increasing expansion.

Mr. YNTEMA. If the Government spends more than it takes in, this obviously puts money into the spending stream.

Senator PROXMIRE. Right.

Mr. YNTEMA. And this would be appropriate in a depression, of course. But if the budget were half as big as it is, you still get this effect if the taxes are less than expenditures.

But it seems to me that the growth in the economy ought not to be tied, is not in fact, tied to the size of the budget. The budgetary expenditures ought to be made for things that we need. When we need national defense, we ought to spend for it. When we need roads, we ought to spend for it. When we need education, we ought to spend for it. But this ought to be determined on the basis of these needs and whether the money kept by individuals can be spent better——

Senator PROXMIRE. I agree with you on that, but what I am speaking of is the technical economic fact. And whether it is right or wrong, whether I agree or disagree, I want to know what the facts actually show. Even though it shows the economy will expand more rapidly, I may still reject it for the very reasons you give. But I would like to know what the facts are; economically, whether there is any sound economic reason to expect that we can move ahead faster with a budget that taxes more and spends more.

Mr. YNTEMA. No, I would say that it would be less. The growth in the economy does not come from what the Government does. Some of it does, for example, in the case of expenditures on research.

Senator PROXMIRE. And education?

Mr. YNTEMA. And on education. But most of the growth in the economy comes from the expansion of capital in private business, finding better ways to do things. And the less the Government absorbs, the more there is to do this in the private economy.

Senator PROXMIRE. My time is just about up. I would like to ask one more brief question. You discuss the wage rates, and you say:

Correct behavior of wage rates is as important to the maintenance of high employment as is the correct behavior of money expenditures.

I like the way you phrase that. I am a little disinclined to approve your ultimate conclusion. Is it not possible that wage rates could be too low for effective demand, that is, so low that it is difficult for the workers to have the purchasing power to buy what they produce? And if so, can you give me any historical situation in which this would maintain?

Mr. YNTEMA. I think that from 1929 to 1932 we knew a good deal less about these problems than we do today. There was a view that all that was necessary to cut wages. There was no recognition of the fact that we needed an increase in money expenditures. And all we are saying is that these two things must be considered together. We are not going to solve the problems of the country just by cutting wages without any reference to expenditures. These are two factors that must be considered together. If you allow wage rates to rise higher than productivity in the country, you are going to squeeze profits, and what you will have will be a rise in prices and unemployment.

I would favor a rise in wages a little less than the rise in general productivity, for two reasons: It relieves our balance-of-payments problem; and, second, it gives the people fixed incomes to share in the profits of the country.

Senator PROXMIRE. At lower prices?

Mr. YNTEMA. That is right.

Senator PROXMIRE. But is there not a longrun tendency, where you have a moderate inflation from year to year, for people to look forward and be a little more optimistic?

Mr. YNTEMA. No; in the late 1920's, for example, the wholesale price tended to go down during the course of the boom. I am not favoring deflation of 3 or 4 percent a year. But you can have 1-percent decline a year. I think this would be a healthy thing. All it means is that the increases in productivity, instead of going all into money wage rates, will go partly into lower prices.

Senator PROXMIRE. My time is up, Mr. Chairman.

Chariman PATMAN. Senator Pell?

Senator PELL. I have a question on the subject of the relationship of capital investment to gross national product.

I would like to direct this question to Mr. Hagedorn: Does he have any ideas how to increase the rate of capital investment in our economy other than the approach presently being followed?

Mr. HAGEDORN. Well I would say in seeking an approach to increase the rate of investment in our economy, if we are to be consistent with our general philosophy of relying on free markets to allocate the resources of the country, and relying on the free decisions of our people, as to how much of their income they want to save and how much they want to invest, then the proper approach is to reduce the tax burden, which leaves them a larger portion of their income with which they can make that kind of a decision, rather than to add some particular feature to the Government tax program, which is an attempt to nudge them, which is, in essence, an interference with the market processes.

Senator PELL. To further elaborate on Senator Proxmire's point, would it not be equally effective to lower taxes and raise wages? It would appear that such a policy would increase the amount of money available for investment.

Mr. HAGEDORN. Raising wage rates would not increase incomes in the country. It would result in an amount of unemployment which would further cut into the total amount of income. A few people would receive larger incomes.

Senator PELL. You do not believe by raising wage rates we would produce unemployment, do you?

Mr. HAGEDORN. Yes, sir.

Senator PELL. The raising of wages per se tends to produce unemployment. Is that right?

Mr. HAGEDORN. Raising wage rates, where market conditions are such that they have to be absorbed out of profits, does tend to reduce employment levels in the country. Yes, Senator.

Senator PELL. I am not an economist, but I would tend to differ with that.

But going back to my basic point, as to how to increase investment in plant, the Western European countries went through the experience of having their plants devastated by war. We have not gone through that experience, thank God. We are trying to encourage investment through tax credits. Do you see any other means besides that?

Mr. HAGEDORN. Well I think there is an approach on both sides of the capital problem, both the supply of capital and the demand for capital. And this relates to both the two major points that I brought up in my prepared statement. One is that there has been an encroachment on profits by increases in wages, thereby decreasing the incentive for expansion.

And the other major point is covered with the reduction in the supply of capital through our present tax system below what the supply of capital has been historically.

Now I think we will increase the rate of capital accumulation insofar as we cure the problem on both sides, increase the incentive on the side of demand for capital and increase the supply of capital by reducing the tax bill.

Senator PELL. Which do you feel is more productive, the depreciation approach, or the tax credit approach, if you had to choose between them?

Mr. HAGEDORN. I believe that the aproach that will have the most effect on the rate of accumulation of capital is a systematic approach for reducing the tax burden at all the points at which it impinges on savings in capital formation; the high rates as well as the unrealistic depreciation rates.

Senator PELL. I understand you believe that all taxes should be reduced, but which is more effective, in your opinion, the credit or the depreciation approach, to get new machinery, new plant?

Mr. HAGEDORN. I believe that depreciation should be increased, simply because it is an unrealistic measurement of the rate at which capital is used up.

Senator PELL. But between the two, which is more effective in producing new plant?

Mr. HAGEDORN. In the long run, I believe the depreciation approach would be more a factor in providing capital for the growth of plant in the country.

Senator PELL. You mean increased depreciation allowances would produce more new machinery than a tax credit?

Mr. HAGEDORN. A reduction in the allotted time allowed to write off an asset.

Senator PELL. You do not think it would simply be passed on in profits with no new incentive to buy new machinery, as there is with the credit?

Mr. HAGEDORN. I do not think it would be a bad thing if that were used, to some degree, to relieve the squeeze on profits.

Senator PELL. But it still would not produce the desired result, would it?

Mr. HAGEDORN. If it were included in profits, surely. Profits are, to a large extent, the source of capital for the purchase of new equipment and new plant.

Senator PELL. Thank you. No further questions.

Chairman PATMAN. Senator Javits?

Senator JAVITS. I have not had an opportunity to hear the gentlemen, but I do have a couple of questions, and if they will forgive me if they are out of context, I will be very grateful to them.

Could I have the view of Mr. Yntema and—I gather it is Mr. Hagedorn who has been testifying on the attitude toward the President's trade proposals and how that fits into the general economic appraisal which they are making.

Mr. YNTEMA. Senator, we have a subcommittee of our research and policy committee studying that, and we hope to have the statement out soon, but I cannot speak for the committee at this time, because they have not made a statement on the subject.

Senator JAVITS. This is the committee headed by Dr. Emilio Collado?

Mr. YNTEMA. That is correct.

Senator JAVITS. Would you give us your view on that, Mr. Hagedorn?

Mr. HAGEDORN. Senator, I have to say that the National Association of Manufacturers does not attempt to speak for its members on the question of tariff protection. We have a wide diversity of interest and a wide diversity of views among our members, and it has been decided that we will take no position on the question of tariff protection.

Senator JAVITS. The other question I had of each of you is that the economic advisers have given us what they call guidelines with respect to what ought or ought not to be wage increases. And has there been any formulation of policy by CED or by the NAM as to that question? The guideline subject has been very much discussed here in terms of the internal discipline which should be the rule in labor-management negotiations. Are you gentlemen familiar with the guideline point? Could we get your view on that, Mr. Yntema?

Mr. YNTEMA. We have not gone into it in as much detail as the Council has. I would say in general our ideas would coincide with those of the Council, perhaps, with, however, the exception that the Council says where there is the power to get more, let them get it. We are much more concerned, however, with the stucture of labor and its powers in the economy and the question of whether these guidelines are going to be achieved. Our real concern is whether or not these will be achieved within the present structures and patterns of behavior that we have.

Senator JAVITS. But you do favor the type of guidelines that are laid down in this report?

Mr. YNTEMA. Yes. What we said, for example, in our statement on defense against inflation in 1958, was that—

> Wage rates on the average should rise as fast as total national output per man-hour, which has been between 2 and 3 percent a year.

Our real concern is how to keep wages from running ahead faster than that.

Senator JAVITS. I am trying to find this page where the guidelines are set forth.

Mr. SCHMIDT. 189.

Senator JAVITS. Thank you.

Mr. YNTEMA. It starts on page 185.

Senator JAVITS. At the top of page 189, you will notice that also they have a guideline for price behavior. Would you have any comment on that?

> The general guide for noninflationary price behavior calls for price reduction if the industry's rate of productivity increase exceeds the overall rate.

Mr. YNTEMA. Well, as a general statement, I think that is appropriate. I mean there may be special circumstances. It is a question of what the starting point is. And the question also whether it is an expanding industry, that needs to attract resources into it.

The same kind of modifications made with respect to wages would apply to this general statement. But in general where there is rapidly increasing productivity and wages do not eat this all up, prices will come down and should come down.

Senator JAVITS. Now, do you believe—Mr. Hagedorn, do you want to comment on this?

Mr. HAGEDORN. Well, in general I agree with what Mr. Yntema has said. This is a helpful picture of, broadly speaking, the way the economy ought to work. If you take it as a broad gage and do not try to apply it too rigidly, I think it is a good description of the general relationship between prices, productivity, and wages.

Senator JAVITS. Let us take in the present steel situation, gentlemen, where we are right up against the issue. Would these guidelines require a modification, a very material modification, in the position of the respective parties in the negotiations for a steel contract?

Mr. HAGEDORN. May I make a comment, Senator?

In the discussion on page 189, after laying down the general guideline, the Council lists some exceptions, particular situations in which the settlements ought to be either higher or lower.

I would call your attention to item 2 on page 189:

> Wage rate increases would fail short of the general guide rate in an industry which could not provide jobs for its entire labor force even in times of generally full employment; or in which wage rates are exceptionally high compared with the range of wages earned elsewhere by similar labor, because the bargaining position of workers has been especially strong.

What this suggests is that in the basic industries of the country, including the steel industry, the wage rate increases should be somewhat below the norm established by the guideline.

Before you came in, Mr. Schmidt produced a very interesting table on trends in employment in the country. It showed that in the highly organized sectors of our economy we have had very little growth in employment over the long run, and in fact some decline in recent years.

So, according to the employment criterion laid down in this statement by the Council, wage rate increases should be somewhat less than the average productivity increase. And also in those areas where they have strong unions, past wage rate increases have put those people somewhat ahead in wage levels, somewhat ahead of the national norm.

Senator JAVITS. Do your organizations favor, in a given wage negotiation, an effort on the part of management to negotiate with a view toward a price decrease as one of the elements in the negotiation? In other words, is the negotiation between management and labor to be conducted solely on the ground that management is seeing that more profit is made by the enterprise and labor is seeing that more wages and salaries are paid? And if the public interest comes in there, in terms of lower prices, who asserts it?

May we have your observation on that?

Mr. YNTEMA. If we had a lesser increase in wages, prices would go down automatically. Competition would take care of that. And we would be very happy to have this result.

Senator JAVITS. In other words, you really have no way in which there can be a calculated policy in this regard. It simply depends upon the interplay of economic forces, the forces of competition, as they condition the labor-management negotiations. We have no way in this country in which a public interest in price reduction, for example, can be asserted except by the interplay of these economic forces?

Mr. YNTEMA. Yes, but you control the interplay of them. You have an antitrust policy, for example, which I think has been very effective. And if I may say so, speaking for myself, I think this is the way that we ought to control, in a free enterprise-free market economy. That is, we ought to set up the structures and the processes so that we get the proper kind of behavior of the parties in an economic bargain. And this is our concern about the labor problems today.

Senator JAVITS. In other words, that there is a weighting on the one side which does not allow the economic process to operate in a normal way? Is that your feeling?

Mr. YNTEMA. Yes; we said that in greater detail in the testimony.

Senator JAVITS. Now I would like to ask just one other question of both groups, if I may.

What do you gentlemen think of the future of profit sharing and stockownership as a way in which to bring about a sidewise movement in the desire of labor to get a greater share of the avails of our productivity, rather than the upward movement which has characterized our postwar history, where the increases have been in wages and salaries?

Mr. YNTEMA. Senator, that has not been discussed by the CED. We do not have any view on that subject.

Senator JAVITS. Would you care to give us a personal view? I do not want to compel you to do that, at all.

Mr. YNTEMA. And I do not want to speak for Ford Motor Co. when I answer this.

We did make an offer, for example, in the company, which involved some increase in stockownership. We like to see our employees buy stock. We have arrangements by which they can do this.

Whether this should take exactly the form of profit sharing or whether there should be some other arrangement, such as we have, I think is an open question that should be examined in the particular circumstances.

Might I ask the indulgence of the committee? I came here on the assumption that we would be heard seriatim, and I would like to have permission to leave to catch a plane, if I may be excused.

Senator PROXMIRE. We will be through, I think within the next 10 or 15 minutes.

Senator JAVITS. Can I get the answer of Mr. Hagedorn to the profit-sharing question? Then I am through.

Senator PROXMIRE. Would you like to leave now?

Mr. YNTEMA. I ought to leave very soon. It is almost an hour's trip out there.

Senator PROXMIRE. Yes; you are wise to allow at least an hour to make it.

Senator JAVITS. Would you answer that question on profit sharing?

Mr. HAGEDORN. I cannot cite any policy of the National Association of Manufacturers on that. I will, if you wish, give you a personal impression, which is a rather noncommittal one.

My personal feeling is that if, in a particular situation, the workers of a company and the company wish to install a profit-sharing plan, there is no reason in principle that anybody should object. It is one way of sharing the proceeds of the business; because, whether you have what is called profit sharing or not, under any arrangement there is a sharing of what is received for the productivity of the business between the employees and the owners of the company. That is the very nature of the thing. There can be different arrangements for deciding how the sharing will take place.

The usual arrangement is on a contractual basis. People are hired at fixed rates, and that is their compensation. The company in effect takes what is left and takes its risks of that amount being adequate to cover all other costs and earn a profit.

Now, that can be modified to have part of the compensation of the employees on a fixed basis, part of it to be contingent on the success or failure of the company.

Now, there are advantages and disadvantages both from the employees' point of view and from the management's point of view to such an arrangement.

Senator JAVITS. Thank you.

Mr. Schmidt, I am sorry I did not ask you these questions. I did not realize you were here separately for the chamber of commerce. Would you care to make any comment on these matters?

Mr. SCHMIDT. I was very much interested in your leaning toward a lower price level. This is exatcly the thrust of my testimony. The last five or eight pages is devoted exclusively to this possibilty. And I think the Council really arrogates to itself an objective which certainly deserves to be challenged. It says:

The desired objective is a stable price level.

Certainly we want stability in the sense of avoiding irregularity. But I would perfer a slightly falling price level, so slowly that people are not quite aware of it; a half percent a year, or a percent per year. And in that way, you actually increase purchasing power, because all the foundations, the hospitals, that have to rely on income, or perhaps endowment funds—the farmers, the retired people, will be cut in on the market in that way.

So instead of raising wages greatly to enlarge purchasing power, when you raise wages unduly you cut down purchasing power in the aggregate, and you also have this balance of payments problem.

So I think we really ought to give very serious consideration to public policies, which would encourage a slowly falling price level.

Senator JAVITS. I was not thinking so much in a generalized way as of a case where it was divided in economic terms.

Senator PROXMIRE. I think Mr. Yntema is going to have to leave, and Mr. Stein is going to stay to answer questions pertaining to this testimony.

Mr. YNTEMA. If there is any question you have——

Senator PROXMIRE. If you can stay for a couple of minutes, I would like to ask one question.

You place so much stress, near the end of your testimony, on wages and on what apparently appears in your view to be an unfortunate impact on the whole structual economic system, because of labor power. I wonder if there is any study showing the divergence between profit and wages, of the kind that you stressed here.

Professors Goldsmith and Hamberg, who were here yesterday and are eminent economists, deny vehemently that there is any such shift. They quote a study made by a man named Budd, now at Penn State, who was at Yale University, who has made a careful study, and he says that any shift toward lower profits is because we now have fewer people who are working independently in business and fewer people are self-employed, and allowing for that, the wage-profit relationship has been very stationary over the last 50 years.

I wonder if you gentlemen, in view of the seriousness of this position that you take, Mr. Yntema, and your reliance only on the facts, can show any study that supports your contentions here.

Mr. YNTEMA. There are two questions here. I do not think that you can determine this by just reference to the share of labor and the share of capital in the product of industry. I think it is a question of how this works out; because if wage rates go up, prices will go up. This is what is happening in recent years.

Senator PROXMIRE. I know you are in a hurry, but wouldn't you want to correct that and say: if wage costs go up? Certainly if wage rates go up prices do not have to go up.

Mr. YNTEMA. But if wage rates go up more rapidly than productivity, then wage costs per hour will go up.

In the last few years we have had a rather substantial unemployment. Prices have not gone up.

We have watched this process take place, and we are deeply concerned about it.

Now, there is room for adjustment in this matter. This is one of the projects, I think, that the Committee for Economic Development may devote a great deal of its time to. We are having a meeting, the end of February, to discuss whether or not this is something on which we can make a contribution.

Our opinion at this time is that this is an important problem. We see what happens in the individual bargains between labor and management. We see what happens in the overall movement of wage rates. And frankly, we are concerned about this.

If you ask me my own opinion, which is based on many things, I think it is a crucial problem for the working of the economy, a crucial one for the balance-of-payments problem.

Senator PROXMIRE. I can understand your theoretical argument. I think it is a very strong one and a very logical one. But I still would ask whether there are any statistics that would support this position.

Mr. YNTEMA. I do not think you can prove this by statistics. I think you must look also at the processes that take place.

Now, to some extent you can support this by the study of cases where wages do go up, where there is no corresponding increase in productivity.

I do not think there is an adequate study of this. I do not think you can prove this by overall statistics.

Senator PROXMIRE. Just one overall more specific question before you go.

Senator Javits asked you about the effect of competitive forces in keeping prices down, providing wages were reduced. Would you intend that if wage costs dropped in the steel industry, the price of steel would drop, because there is competition among steel producers in the steel industry with an order that would result in lower steel prices?

Mr. YNTEMA. Yes, I think it would. That would be my opinion of it.

Senator PROXMIRE. In spite of the price leadership that has been so well established and the pattern of instantaneous and precisely similar prices, and in spite of the basic point system and so on, you still feel that prices would drop because of competitive forces?

Mr. YNTEMA. There are very strong pressures on the other side. There are not only pressures on one side, here. We are smart buyers of steel.

During the 1930's, if you take that as a reference point, the steel industry had a very high break-even point. I would have to go back to check this, but this is my recollection. And I am not trying to defend the steel industry. But there is more competition than is often asserted.

And I do not mean to say that throughout the economy we have perfect competition. This is not so. But for the most part, I think it is reasonably workable competition. It is not perfect. It does not work exactly the way we would like to have it. But I think it is a pretty effective, workable competition for the most part.

Senator PROXMIRE. Thank you very much. You are dismissed, and I very much appreciate your statement and sure hope you make your plane.

I do not want to detain you gentlemen much longer. I just have a few questions.

Mr. Hagedorn, in your statement you have this very interesting table. We have done some work on this table, and I find this shows the drop in profits as a percentage of gross national product. I have raised this question with many witnesses almost every day that I have been here. I have raised this question with economists and with public officials and so forth to try to get their explanation of this, and whether or not this should be a matter of concern. You raised this in our subcommittee when we met last month. I think it is a very legitimate point.

I am somewhat concerned about the statistics, though. I have made a correction now for inventory valuation. Here is what has happened: In the period beginning 1957, 1958, 1959, and 1960—there were rising prices. So inventories increased in value. This gave business an inventory-price profit, which was not a real profit. And if you correct for that, you find that profits as a percent of GNP are very stable during all of this period.

Why isn't it proper to eliminate inventory valuation before you arrive at the accurate relationship between profits and GNP?

Mr. HAGEDORN. Well, these figures are more an illustration, rather than a nailing down, of the point I was trying to make, Senator. There would be justification for correcting for the inventory valuation. There is an argument on both sides.

I do not have here a table of figures so corrected, but my impression is that there is still a downtrend in those figures.

The early figures, in 1947 and during the Korean period, did have a substantial inventory profit elment in them. But thereafter that has been a rather minor point.

I am just speaking from recollection.

Senator PROXMIRE. There was a slight downtrend. For example, 1947, 10 percent; 1948, 12 percent; the next 3 years, 12 percent; then 12½.

Then in 1952, 10.9; 10.2, 9.3, 10.9, 10 percent, 9.7, 8 percent, 8.6, 9.0, 9.0.

So that while this is slightly down, it is quite stable, and it is not quite as large as the figures you had originally, although I think this is a very legitimate and proper point to call to our attention. And I think some argument can be made that that slight diminution may be explained on the grounds that were explained by the professors who were here, that you have fewer independent enterprises.

Mr. HAGEDORN. No, these relate only to corporations. I have not seen that study you were quoting, Senator.

Senator PROXMIRE. I have not seen it either.

Mr. HAGEDORN. But from what you said, my impression is that that is not dealing with corporate profits, but with the corporate profits and the income of independent entrepreneurs, which is a very different question. And I suspect from what you said, too, that it deals with a much longer period. We are tracing the postwar history and relating corporate profits to the gross national product in that period.

Now, I do not believe—I cannot be sure, but I do not believe—that the corporate part of the economy has changed very greatly in its relationship to the total economy during that period.

If I may go further, Senator——

Senator PROXMIRE. Just at that point, I also have some figures on the profits after taxes, depreciation, and interest, as a percentage of all income for all corporate sources. And there I find that in 1953 it was 18 percent, and it has gone up to 18.7 percent. In other words, the profit as a ratio not of the gross national product, but of the total income of corporations——

Mr. HAGEDORN. Before depreciation, Senator.

Senator PROXMIRE. It is after depreciation.

Mr. HAGEDORN. Then there are only two elements, or three, the wage and salaries——

Senator PROXMIRE. I beg your pardon. I think what this shows is profits, depreciation, and interest after taxes. It is not after depreciation. It includes depreciation. It includes interest.

Mr. HAGEDORN. I would make the same point I made earlier, Senator, that depreciation is no part of the incentive for undertaking new projects or expanding your enterprise. You do not undertake economic activity merely to get back the cost of the capital you are using up.

Senator PROXMIRE. But at the same time, depreciation also is enormously important, as you know as well as I do, perhaps even more important than profits, in a way, to have the funds available.

Mr. HAGEDORN. The chief point of this table was to point out that the incentive on business for going ahead and doing things and expanding has been reduced because of the squeeze on profits.

Now, you cannot say that that has been made up by an increase in the relative size of depreciation. That is a real increase in the rate at which capital is being used up. That cannot be counted in as a part of the incentive.

Senator PROXMIRE. There is also a change in the tax laws because of the 1954 Revenue Act, which had a very big impact on depreciation; is that not a fact?

Mr. HAGEDORN. That is true. There may be some jog in the figure after 1954 for that reason, but the trend continues thereafter.

Senator PROXMIRE. Over a period of time over the past 10 or 15 years, wouldn't it be better if you included depreciation? Leave it out, and you of course get lower profits, because some of what used to be considered profits is now considered depreciation.

Mr. HAGEDORN. Well, if you look at the trend after 1954, you still get that general downward trend. You can say there is a break in the continuity of the series in the year 1954. I have no way of guessing just how much that break in comparability would amount to. But the downward trend in the after-tax profits as a percent of gross national product continues after 1954.

Senator PROXMIRE. I would like to ask Mr. Schmidt: In the first place, I want to say I am delighted and pleased and flattered at your commendation of this study which our committee made and which Mr. Roy Moor primarily is responsible for. I think he did a fine job. I am delighted that you feel it made some constructive suggestions for improvement of the budget, some of which were followed and some of which you and I think should be followed. But then you go over, and we get a little roughing up on page 12, where you say:

> Nevertheless, it, along with part of the Economic Report may be "to Keynesian" in its orientation, in the sense of overpreoccupation with aggregates, and insufficient attention to maladjustments and roadblocks and distortions in the economy.

It seems to me that one of the main points of this study was to get away from aggregates and to emphasize the components.

I call your attention to page 106 of the study, in which we say:

> First, the emphasis in the budget must be on the nature of the components, not on a single pair of aggregates, and the deficit or the surplus difference between the aggregates. No pair of aggregates can adequately measure any kind of economic effort, because the amounts being accumulated in the aggregate have different economy consequences.

And so on.

I would agree wholeheartedly that the aggregate approach has all kinds of shortcomings. But I do feel we have tried to avoid that.

Mr. SCHMIDT. Well, I think what that sentence applies to is really more the heart of the report of the Council of Economic Advisers than the other document. That was a very refreshing document, and I certainly want to commend you orally for what you have done.

But, for example, in the Council's report, I think before you came in I mentioned this sentence:

> Unemployment of 4 percent is a modest goal, but it must be emphasized that it is a goal which should be achievable by stabilization policy alone.

By stabilization policy alone. The point Mr. Yntema was making and the point I am making in my testimony is that if you have malfunctioning, distortions in the economy, you probably cannot achieve this goal of 4 percent and stability in the price level, or even a slowly falling price level, and all the other goals that we want.

Now, this is in part, even, corrected in the fourth chapter of the Council's report. But in the other parts there is a target of 4 percent to be achieved by stabilization policy alone. I just do not think you can do that.

Senator PROXMIRE. Thank you very much.

My time is up.

Mrs. Griffiths?

Representative GRIFFITHS. I would like to ask you, in case you have never been asked: On the standby power of the President to reduce taxes, what is your viewpoint of this, regardless of whether or not it is constitutional? And if you favored this, would you also favor a power to increase taxes?

Anyone who wants to answer.

Mr. HAGEDORN. Speaking for my organization, we would be opposed to giving the President standby power to apply a temporary reduction in prices, or taxes, or to increase taxes, either.

Do you want me to explain?

Representative GRIFFITHS. Yes, I would be glad to hear the explanation.

Mr. HAGEDORN. Well, the burden of my testimony, Representative, was that the problem in our economy, the reason for the underutilization of resources and for the suppression of growth, is not a temporary cyclical one. It is a cumulative result of wage increases in excess of productivity eating into profits and reducing the incentives for growth, and for utilizing our resources freely. And that is not the type of problem that can or should be solved by a temporary tax cut.

Senator PROXMIRE. Any questions?

I want to thank you gentlemen very much. You have been very patient, and it has been very enlightening.

The committee will reconvene this afternoon at 2 o'clock to hear Mr. Walter Reuther.

(Whereupon, at 12 noon, the committee was recessed, to reconvene at 2 p.m., the same day.)

AFTERNOON SESSION

The CHAIRMAN. The committee will please come to order.

We have as our witness this afternoon Mr. Walter P. Reuther of the AFL–CIO.

Mr. Reuther, you have been before us many times before. We have always appreciated and enjoyed your testimony.

We would like to hear from you again. You may proceed in your own way, sir.

STATEMENT OF WALTER P. REUTHER, VICE PRESIDENT, AFL–CIO, CHAIRMAN OF THE AFL–CIO ECONOMIC POLICY COMMITTEE, AND PRESIDENT, UAW; ACCOMPANIED BY NATHANIEL WEINBERG, DIRECTOR OF SPECIAL PROJECTS, UAW; AND STANLEY RUTTENBERG, DIRECTOR OF RESEARCH DEPARTMENT, CIO

Mr. REUTHER. Thank you, Mr. Chairman and members of the committee.

First, I should like to express my very sincere appreciation for the opportunity of appearing and to present testimony with respect to the President's Economic Report.

I am appearing here as the vice president of the AFL–CIO and also as chairman of the Economic Policy Committee of the AFL–CIO and as president of the UAW.

We have put together a very comprehensive analysis of the President's Economic Report which I should like to have entered into the record, if I may.

The CHAIRMAN. It may be inserted at this point. You may summarize it or proceed in any way you choose.

Mr. REUTHER. Thank you.

(The analysis referred to follows:)

STATEMENT ON THE PRESIDENT'S ECONOMIC REPORT, PRESENTED ON BEHALF OF THE AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS BY WALTER P. REUTHER, VICE PRESIDENT, AFL–CIO; CHAIRMAN OF THE AFL–CIO ECONOMIC POLICY COMMITTEE, AND PRESIDENT, UAW

The advances in human knowledge of the past 20 years have transformed the world in which we live, and have ushered in a revolution in the way we work, the things we produce, and the problems we have to solve which is still only in its beginnings.

The question that faces us today is whether we have the vision and the intelligence to recognize the revolutionary changes that are taking place with every breath we draw. Will we have the wisdom to use them as they should be used to achieve some of humanity's oldest dreams—to eliminate poverty, ignorance, and disease—to share abundance among all people—to secure freedom from drudgery while preserving for every man and woman the opportunities for useful, well-remunerated work? Or will we let slip the opportunity to realize man's age-old dream of abundance and allow it to be perverted into a nightmare of dislocation and human hardship by our failure to measure up to the challenge of the technological revolution?

Can we apply the same imagination and vision to the solution of our social and economic problems as we have done to the solution of scientific problems?

To date we have not done so. We are penetrating the secrets of the atom and the mysteries of outer space. We are reaching out to the moon and the planets. We have raised our eyes to the skies. Yet millions of men and women and children, even in this country, still suffer poverty, insecurity, and want.

From our laboratories comes a stream of new products—new metals, new materials, new machines, and devices of every kind. Yet we have not found the means to provide enough new dwellings to house all our people in decency and comfort, enough new schools and well-qualified teachers to give every child and young person the opportunity of developing his talents to the full, enough new clinics and hospitals and trained medical personnel to make modern medical skills available to all who are ill.

We have the technology to build plants and factories filled with machines that can operate day and night with scarcely any need for human intervention—but we have not found the way to provide steady work for all our people.

Surely a people capable of performing the scientific miracles we have achieved is no less capable of coping with the problems of human beings.

In planning to meet our human needs we must also raise our eyes to the skies. We must face the fact that the economic and social programs of the past are no longer adequate in the age of automation, space, and the atom.

We must measure what we can do, what we have to do, not by the inadequate yardstick of what we have done before, but by the vast and growing potentialities of the present and the future.

Our country, which leads the world in wealth and in technological development, must show a new capacity for leadership, also for the development of new programs to utilize science, technology, and human skills to share abundance not only among ourselves but among all the peoples of the earth.

As our most immediate goal, we must find answers once and for all to the problem of mass unemployment in our whole economy, and of chronic distress in our 461 areas of "substantial and persistent unemployment." We must in human compassion find adequate answers to the needs of the unemployed.

We must find the means, within our principles of freedom, to prevent those abuses of great economic power which threaten the very basis of a free economy.

We must develop the means to anticipate the changing needs and problems and to realize the full potentialities of a dynamic society in the age of automation.

We must raise our sights still higher

The programs presented to Congress by the present administration to establish a national purpose and meet the needs of our people represent a vigorous and imaginative advance in leadership, both in terms of restoring health and strength to our economy and of finding compassionate answers to the needs of human beings in trouble. But even those programs fail to comprehend either the full magnitude of the problems we face or the full dimensions of our potentialities.

We have raised our national sights, but we have not raised them nearly enough. We are still aiming far too low. We are still accepting ideas of what the economy can and should do at levels which fall far short of our true capacity, levels which would leave far too much of our productive resources, both human and physical, unused or underused.

Not only are we setting our sights too low in terms of what the economy can do today, but what is even more serious, we are basing our future projections on estimated rates of productivity advance and growth in production which are substantially less than we can achieve with full employment—less than what we will need to achieve if we are to reach and maintain full employment in the age of automation.

The projections on which we are being asked to chart our course for the next 10 years would mean that we would not be able to create new jobs fast enough to match the growth of our labor force and the elimination of existing jobs by automation. They would mean, therefore, that the ranks of the unemployed would continue to grow, that purchasing power would continue to fall far short of productive capacity, and that our economy would continue to lurch unsteadily from one period of trouble to another.

The reason why we are aiming too low, primarily, is that we are still basing our plans for the present and the future on the record of the past. We are failing to take into account the technological revolution. That revolution has already changed the processes of production in America so drastically that what we could do even 10 years ago is no guide to what we can do today; and what we can do today is no guide to what we will be able to do 10 years in the future.

The new technologies have created a potentiality for abundance which we have failed to comprehend, and, failing to comprehend, have failed to achieve. The abundance of goods and services which we could have produced, and failed to produce, is represented by the tragic overabundance of unemployed men and women who ought to have been at work producing them.

We must act boldly in the knowledge that we cannot resolve tomorrow's problems with yesterday's tools and that new ideas and new concepts adequate to the dimensions of the problems must be developed.

The dimensions of automation are still expanding

The extent to which automation has already revolutionized production in one industry after another is scarcely realized yet—except perhaps by the men and women whose jobs have been destroyed by its impact, and whose lives have been undermined by our failure to create alternative work opportunities for them. Yet the revolution is still only at its beginning.

In a speech which he delivered at Reed College on November 17, 1961, Prof. Neil W. Chamberlain of Yale University pointed out that what he calls the dimensions of technological change have been expanding and will continue to expand.

Professor Chamberlain continued:

"First, on the intensity or qualitative character of the changes occurring there is good evidence that automation constitutes more than 'just another' of a long series of process developments over the years. Let me offer simply one item in that evidence, suggested by a leading student of the subject, Prof. James Bright of the Harvard Business School. Until quite recently we have tended to regard automation in the plant as quite distinct from automation in the office. One was concerned principally with product processing, the other with data processing. But now the two are meeting. The same machine intelligence which directs production equipment will 'generate information on performance which will be automatically transmitted to the data processing center' for analysis by the accountant, the industrial or systems engineer, and the finance officer. 'The unit of mechanization will be the total business—not the factory and the office as two separate spheres.'

"Concerning the extensity dimension we may take note of the fact that whereas once it was believed that automation was a form of technology reserved to the large, mass production industries, the linking of the tape-activated computer with flexible production equipment now makes possible, and increasingly economic, the introduction of automation processes even into the job-lot shops. As the Wall Street Journal reported 2 years ago, 'new multipurpose machine tools often combine several * * * operations, controlling the whole cycle automatically with a perforated tape which directs the machine much like a paper roll operates a player piano. * * * With one or more multipurpose machines, production can be switched swiftly from one "run," or product, to another just by changing tapes that "operate" the machines.'

"What is now only a footnote to this development may soon expand into an important chapter in the history of automation. The tapes of which the Wall Street Journal writes can be interchanged between plants, so that the small company does not need even to program its specific operations. From libraries of tapes which are assembled either by the equipment manufacturers or some other agency, perhaps a trade association, the small firm may be able to purchase along with its equipment virtually all of the expertise and skill needed to operate it. At this point the *intensity* of the technological change opens up sweeping vistas as to the *extent* of the institutional impact." [Emphasis in original.]

The pace of change will accelerate

The pace of change can also be expected to increase, Professor Chamberlain pointed out, as research continues to expand. He said:

"The amounts now being spent on research in the United States have been accelerating at a rate which, even though not enough to satisfy some enthusiasts, is nonetheless impressive. Roughly $10 billion is being spent annually in the United States on all forms of research and development in the natural sciences and engineering. This is twice as much as was spent only half a dozen years ago. In the last 25 years the number of industrial research laboratories has increased from 100 to 4,000."

As one example of the kind of change which may be expected in the future, the New York Times of January 31, 1962, reported a news conference held by the American Institute of Electrical Engineers to report progress on the development of a new type of "gigacycle computer" which will operate a thousand times faster than existing computers. Where today's fastest computers can perform each step in a computation in two or three millionths of a second, the new computers will be able to perform the same operation in billionths of a second—and where today's computers often take up a whole building, the new type may be able to fit into a desk drawer. Completion of the first gigacycle computer is expected before the end of next year.

The research and development being done to cope with the problems of space flight will quickly find industrial application. Already the dream of generating electrical power directly from the rays of the sun has been made a practical reality. For satellites now being tested we have developed communications and computing devices that will track the satellite around the moon and send it precise instructions to determine its flight and control the operation of its equipment from a quarter million miles away. Just as the relatively simple computing devices that were developed in World War II to control the flight of planes and the operation of antiaircraft guns led quickly to the miracles of automation, so these new breakthroughs will undoubtedly bring further transformations to industry that we can scarcely dream of today—from the robot plant to the automatic highway on which cars and trucks may cross the continent without a human driver.

Far from being prepared to deal with such future, we are still not prepared to deal with the consequences of technological changes which have already transformed the processes of industry and business.

We are not ready to accept the fact of the abundance that our economy could produce today if we were to make full use of our resources, much less the far greater abundance of which it will be capable tomorrow.

This is a doubly tragic failure. For not only have we lost forever the goods and services we failed to produce, but in failing to produce them we have condemned millions of men and women to the hardships and loss of human dignity that go with unemployment.

We must find the means to share abundance

Our problem is not that we are unable to produce abundantly. It is that we have failed to adopt the programs we must have in order to make use of abundance. We can have abundance only to the extent that we find the means to share it.

Finding those means is the major challenge that faces our economy today and for the years ahead.

To meet that challenge, we must learn to gear all our social mechanisms to the principle of living with abundance and making the fullest use of it.

In planning to meet our private needs we must assume—for it is true—that we have sufficient potential abundance now to abolish poverty in America. What we lack is not the means but the machinery. In considering all the programs to eliminate personal poverty, from a decent minimum wage to an adequate program of social security, we must recognize that it is no longer practical to say, "We can't afford it." The only thing in this context that we cannot afford is poverty itself.

In planning to meet our public needs we must turn from concentration on the problems of balancing a budget and concentrate instead upon the needs that have to be met. With 4 million unemployed, every program that builds new schools or hospitals or homes, or meets any of a thousand other public needs, also puts men and women back to work supplying the goods required to do the job. If the immediate expenditure results in a temporary budgetary deficit, the final result is more jobs, more production, increased national wealth, and a broader economic base from which higher revenue can be obtained. A balanced economy is the only sure basis and the only healthy basis for a balanced budget.

We must start to plan

If we are going to avoid in the sixties the kind of economic trouble we found ourselves in during most of the fifties, then we must start to plan for something better. We must look about us and see what other nations with far less resources and far less opportunities have done in order to achieve far faster rates of economic growth. We must study the means by which countries of Western Europe, for example, have achieved full employment and rapid economic growth while we have merely talked about it. We must adapt our economic thinking and practices to the realities of the society in which we live.

We must stop being afraid of the word "planning" in the context of solving our national problems and achieving our national goals. It is one of the paradoxes of our society that national planning for a national purpose is so often condemned by business executives who would feel derelict in their responsibility if they did not make sure that the growth and development of their own corporations were planned for years ahead.

Most of the objections to planning come from men who have kept their minds firmly fixed on the past, who would like to live still by the economic theories developed nearly 200 years ago by Adam Smith. But the world of today is not the world of Adam Smith. It is the world of the computer and the automated plant. It is the world in which key sectors of our economy are dominated by a handful of giant corporations whose decisions as to prices, production, or investment can determine whether tens of thousands of men and women have jobs or rot in idleness, can settle the fate of whole communities and can be felt in every corner of the country. It is the world in which economic competition between nations and groups of nations may well prove more decisive than military struggle, when our success or failure in achieving full employment and sustained economic growth may well determine the political allegiance of scores of emerging nations, may well decide whether the final victory is to be that of freedom or of tyranny.

Does anyone believe that we can win in such a contest without troubling to plan where we want to go and how we intend to get there?

This does not mean that we must accept a totalitarian type of bureaucratic planning in which every individual and every enterprise is subject to centralized control. On the contrary, democratic planning can and must be used to enlarge the areas of individual decision and voluntary cooperation.

We can learn from the experience of others

Practical examples of effective national planning within the framework of freedom can be found in the experience of other nations. One such example is that of France, a republic whose fierce devotion to the principles of personal freedom and individualism is at least equal to our own. It is also significant that the Conservative government of Great Britain is showing considerable interest in France's economic planning program.

Since 1946 the planning for the general direction of development of the French economy has been a responsibility of the General Commission for Planning and Productivity. This is no monster bureaucracy. When it was first organized its total staff, including secretaries, drivers, and so on, was only 100. By 1961 it had increased to 150.

Neither does it exercise any powers of control. Explaining its operation, the present Commissary General, M. Pierre Masse, said recently:

"Within the governmental and administrative apparatus, *its role is solely one of conception, counsel, and appraisal.* It takes part in procedure and prepares decisions, but it has no power of its own and administers no funds for economic action." [Emphasis in original.]

How does the planning body exercise its influence on the French economy? M. Masse went on to explain:

"It owes its strength to the fact that *it is a permanent forum for the comparison of data and projects supplied by Government and business, by the public sector and the private sector.*" [Emphasis in original.]

The chief organs through which the Commission brings about this voluntary cooperation in planning between the public and private sectors are some 25 modernization committees, consisting primarily of representatives of business, organized labor, and Government agencies, with such other groups as specialists from the universities and representatives of consumers brought in as required.

In preparing a plan, there is a constant interplay of ideas between representatives of management, labor, and Government as they work toward agreement on the economic goals to be reached. What emerges is a statement of national purpose for the ensuing 4 years which has already gained the support of those upon whose continuing cooperation its success will depend.

These procedures have so well succeeded that France today has rebuilt her economy out of the ashes of war. France has achieved full production and has reduced unemployment close to the vanishing point. She has achieved a rate of economic growth far higher than our own. In spite of the fact that there was no increase in the labor force, France's total national production of goods and services increased between 1949 and 1959 at an average rate of 4.5 percent per year, and her industrial production doubled. For the period of 1960–66, an average growth rate of 5.5 percent a year is planned for, and so far appears to have been achieved or even exceeded. By comparison, the rate of economic growth in this country has averaged only 2.4 percent a year since 1953.

We do not suggest that the French form of planning is one that can or should be adopted in this country. We do believe that certain general principles, such as that of bringing all elements of the community into the formulation of national goals and purposes, are essential to any technique of democratic planning in a free economy. What we urge above all is that the country, through Congress and the administration, accept the principle that national economic planning is essential to survival.

Specifically, we would urge in the strongest terms that this committee give leadership to the Nation in this regard by undertaking, either alone or in cooperation with the Council of Economic Advisers, a detailed study of democratic planning as it is being undertaken in other free nations. It is imperative that we learn from the practices and experiences of other democratic countries which have faced up to and found more adequate answers to some of the problems we face, and that we select from their experience and from our own thinking those methods and techniques which will best enable us—freely, cooperatively, democratically—to achieve a broader sense of national purpose, to set the economic goals at which we will aim and to work together in striving to achieve them.

We must explore the dimensions of automation

One step which can and should be taken with no further delay is to set up the machinery for bringing together all that is known now about what is actually happening in the way of automation in this country, what is being planned for the future, and what impact it may be expected to have on our lives. That impact may be far greater than any of us anticipate. Donald N. Michael, for example, director of planning and programs of the Peace Research Institute in Washington and a former consultant to UNESCO, the Department of Defense, and the National Aeronautics and Space Administration, has written a recent pamphlet for the Center for the Study of Democratic Institutions entitled "Cybernation: The Silent Conquest," in which he says:

"Both optimists and pessimists often claim that automation is simply the latest stage in the evolution of technological means for removing the burdens of work. The assertion is misleading. There is a very good possibility that automation is so different in degree as to be a profound difference in kind and that it will pose unique problems for society, challenging our basic values and the ways in which we express and enforce them."

Discussing the changes to be expected through cybernation (automation based on use of computers), he writes:

"* * * as cybernation advances, new and profound problems will arise for our society and its values. Cybernation presages changes in the social system so vast and so different from those with which we have traditionally wrestled that it will challenge to their roots our current perceptions about the viability of our way of life. If our democratic system has a chance to survive at all, we shall need far more understanding of the consequences of cybernation. Even the job of simply preserving a going society will take a level of planning far exceeding any of our previous experiences with centralized control."

Whether the changes to be anticipated will be as drastic as Mr. Michaels predicts or not, it is of the utmost importance that we stop flying blind into the age of automation, and find out what is actually taking place and what it is doing to our economy. On previous occasions we have urged the establishment of a technological clearinghouse for the gathering together of such information and we put forward that proposal with increased urgency today.

Not only economic realism but survival itself compels us to recognize that in our complex economy we cannot continue to rely upon the blind forces of the marketplace to give us a sense of direction.

Tasks for a technological clearinghouse

A technological clearinghouse would have the responsibility to gather information on a continuing basis concerning developments in automation, atomic and solar energy, new materials, new products, and other technological innovations. It would evaluate their actual and prospective impact on employment opportunities, the location of industry, the possible rise or decline of industries in importance and the many other ways in which technological progress affects the economy, from educational requirements to international trade.

The technological clearing house should, for example, maintain up-to-date information on the current and planned extent of automation and its effect in displacing workers, both directly and indirectly. It should keep abreast of trends tending to make some skills obsolete and to increase the importance of others. It should undertake studies of special problems, such as those of displaced workers approaching retirement age, for whom retraining and placement in new jobs may present special difficulties. It should have information on the number of new job opportunities that will be required both to absorb the impact of labor-saving technologies and to take care of the normal growth of the labor force. It should be empowered to obtain from employers the fullest information (with proper protection of confidentiality) on their plans for technological innovations, and the anticipated effect of such changes on employment, as well as any plans for the establishment of new plants or for moving or closing existing plants. It should study the possible adverse impact of such plans on the communities affected, and develop, in advance, programs to counteract such effects. It should keep abreast of research developments in the universities and in private and public research centers to be in a position to evaluate the impact of their combined efforts. It should acquire information on the effect of technological changes on production costs, so that those responsible for Government policy can determine whether consumers and employers are sharing fairly in cost savings. It should provide data to be used for periodic review of the standard workweek. The technological clearing house should bring together information on what is being done through collective bargaining to meet the impact of technological change, and should make such information readily available to management, labor, and Government. It should also gather and distribute information as to what is being done to solve these problems by governments, management, and labor in other democratic countries, some of which undoubtedly have valuable experience to share with us.

WHERE THE ECONOMY STANDS TODAY

America continues to face enormous economic problems despite the pickup from the recession of 1960–61. The basic difficulties of persistent high unemployment and idle productive capacity still remain.

There have been only meager and slow improvements in employment and unemployment, although production, sales, and profits have risen at a favorable pace compared to previous upturns from postwar recessions. While the real volume of total national production rose 7½ percent between the recession low point in the first quarter of last year and the final quarter of 1961, employment and unemployment were hardly touched. Total employment increased two-tenths of 1 percent and unemployment declined only 7 percent. This startling record of meager improvements in employment and unemployment since the recession low point last winter stands in sharp contrast even with the upturns from previous postwar recessions.

Productivity has risen at an extraordinary rate in these recent months, under the impact of automation in widespread parts of the economy. There has been a vast advance in America's potential to produce, but effective demand continues to lag, leaving idle men, plants, and machines. A great gap remains between our actual progress toward recovery and our potential to produce an ever-rising volume of goods and services.

What yesterday was a level of demand sufficient to insure full use of manpower, plant, and equipment is far from adequate to engage the entire productive resources of industry in the age of automation today. Not only have our capacities grown, but the needs of a growing population and the requirements of our national defense have increased also. Yet in spite of the vast and only partially used productive capacity of our economy, in spite of the needs crying out to be met, economic policies are still being developed within the limitations of the past.

The human and material resources are available for America to produce a growing abundance of goods and services, sufficient to begin to meet our public needs, while improving our private standards of living. We failed to utilize these resources fully in the past 8 years, wasting billions of potential man-hours of productive effort through unemployment and underemployment, and leaving idle billions of dollars' worth of plant and equipment. This waste continues today even in this upswing from the most recent recession.

President's report is a long step forward

President Kennedy's first economic report to the Nation—along with the report of his Council of Economic Advisers—represents a long step forward in fulfilling the administration's responsibility under the Employment Act of 1946. After 8 years of evasion, the Employment Act has been moved forward once again to its rightful place as the focal point of national economic policy. "As a declaration of national purpose and as a recognition of Federal responsibility," the President states, "the act has few parallels in the Nation's history."

In his restatement of the central importance of the Employment Act the President declares:

"The framers of the Employment Act were wise to choose the promotion of 'maximum employment, production, and purchasing power' as the keystone of national economic policy. They were confident that these objectives can be effectively promoted 'in a manner calculated to foster and promote free competitive enterprise and the general welfare.' "

Under the terms of this act, the President and his economic advisers set forth once again—after a lapse of 8 years—a statement of "current and foreseeable economic trends in the levels of employment, production, and purchasing power." In addition, they present an outline of their best estimates of the major economic trends for the next 2 years and the national economy's potential for economic growth from 1960 to 1970.

The President and his Council of Economic Advisers deserve commendation for these statements of short-run national objectives and the longer run growth potential, even though we cannot agree with their precise formulations. Although statements of these objectives are required by the letter and spirit of the Employment Act, they have been missing from the annual Economic Reports of the past 8 years. Their reappearance, we hope, is an indication that they will be continued in the future Economic Reports of this administration and its successors.

Organized labor has long believed in the importance of such declarations by the administration in office of national economic objectives in terms of production, employment, and unemployment. They provide essential guides for private and Government policies to sustain rapid economic growth and maximum utilization of manpower and productive capacity. We have also believed in their great value as yardsticks against which actual achievements can be measured—not only for ascertaining shortcomings in the achievement of stated objectives, but ever more importantly, for indicating improvement in programs and policies needed to attain our national economic goals.

The statement of national objectives provides a basis for constructive, democratic discussion. It is proper that they should be closely scrutinized by citizens in all walks of life and criticized, where criticism appears warranted, as to their adequacy and as to whether the program and policy proposals that accompany the statement of goals are adequate to their achievement. A declaration of national objectives does not, in itself, assure their achievement.

The actual course of economic developments is the result of policies and actions of business, consumers, and government, Federal, State, and local.

Only to the extent that the objectives are soundly based and detailed enough to serve as guidelines for private and Government policies can they help us move forward to sustained full employment and fulfillment of our national needs.

The goals are inadequate

The shortrun goal for 1963 is set at a gross national product of approximately $600 billion (in 1961 prices) and an unemployment rate of 4 percent. The President describes this objective as the best, "the maximum."

It represents a rise of approximately 15 percent in the real volume of total national production within 2 years—including a period of recovery from the effects of a recession and prolonged stagnation. With respect to unemployment, the stated goal is reduction from a 6.7-percent rate in 1961 to 4 percent in 1963.

These objectives, if achieved, would be a vast improvement over the record of economic weakness in recent years. But they do not, in our opinion, represent the best, "the maximum." In the past 9 months "man-hour productivity achieved an exceptional gain," as the Council of Economic Advisers notes, and the economy's potential maximum production in 1963 may well be considerably greater than $600 billion (in 1961 prices). The goal of a 4-percent unemployment rate in 1963 is likewise not the best. The President himself says that it is a "temporary target * * * ultimately, we must reduce unemployment to the minimum compatible with the functioning of a free economy."

The shortrun economic objectives for 1963, therefore, are limited. The maximum employment objective represents an unemployment rate that is too high, although it is much better than our actual record of recent years. The maximum production objective is probably too low in terms of our rapidly advancing productivity and growing labor force. To achieve even the limited objective of reducing unemployment to the still unsatisfactory 4-percent level, a greater increase in total national output will be required than the Council of Economic Advisers' estimated rise from $521 billion in 1961 to $600 billion in 1963 (in 1961 prices).

The AFL–CIO's major concern over these shortrun objectives, however, is not with their limitations. Our concern is that even these limited objectives may not be achieved. The President's proposals do not spell out an adequate program, in our judgment, to bring to reality the objectives he set forth for 1963. These objectives will certainly not be achieved automatically.

The shortcomings of the administration's program are clearly pointed up by the Council of Economic Advisers' own estimates of the increase in employment needed to reduce unemployment to a 4-percent level by 1963. Between 1961 and 1963, the Council states, total civilian employment would have to increase 4.8 million. Since total employment in January 1962 (adjusted for seasonal changes) was only about 300,000 above the average for 1961, almost the entire needed increase of 4.8 million is still to be achieved.

The great magnitude of the task of reaching even the administration's unsatisfactory objective of a 4-percent unemployment rate for 1963, can be seen by examining the actual degree of improvement achieved 2 years after previous postwar recessions. Although the comparisons are not precise because the recession low points occurred at different times of each year, the following figures indicate the general magnitude of the job we face.

Employment increase in 2 years after each postwar recession

Year	Total employment	Increase	Year	Total employment	Increase
1963 [1]	71,600,000	4,804,000	1956	64,708,000	3,818,000
1961	66,796,000		1954	60,890,000	
1960	66,392,000	2,426,000	1951	60,784,000	2,361,000
1958	63,966,000		1949	58,423,000	

[1] Council of Economic Advisers' projection of needed employment in 1963 to reduce unemployment to a 4-percent level.

Source: U.S. Department of Labor and Council of Economic Advisers.

What is needed, therefore, according to the Council's estimates, is an employment increase between 1961 and 1963 that is twice as great as that between 1958 and 1960 and 1 million greater than that between 1954 and 1956. Never before in the postwar period have we achieved such a large increase in employment coming out of a recession. The administration's programs, we believe, lack the scope and the call for immediate action necessary to insure that we will achieve it now.

There is an urgent need for Government actions now, to achieve a rapid recovery and a sustained rate of economic growth. The recession of 1960–61 is far from over in terms of employment and unemployment.

The Council's report presents a chart showing that as of December 1961 full-time equivalent unemployment was approximately 9 percent of the labor force (excluding self-employed and unpaid family workers). The preliminary release on the January employment situation suggests that the full-time unemployment rate is probably slightly lower as of now. However, the data charted in the Council's report do not take account of another form of unemployment, the hidden unemployment of those who have given up the hope of finding jobs and are not counted among the unemployed because they are not actively engaged in seeking work.

The failure of the labor force to increase appreciably over the level of January a year ago suggests that such persons number in excess of 1 percent of the total labor force. Taking them into account, true unemployment as of now may be estimated at more than 9 percent of the real labor force, as distinguished from the concept of the labor force used in compiling unemployment statistics. This volume of unemployment reflects a staggering degree of underutilization of our productive potential.

Tools to deal with recession

In his Economic Report, President Kennedy said:

"In our free enterprise economy, fluctuations in business and consumer spending will, of course, always occur. But this need not doom us to an alternation of lean years and fat. The business cycle does not have the inevitability of the calendar. The Government can time its fiscal transactions to offset and to dampen fluctuations in the private economy. Our fiscal system and budget policy already contribute to economic stability, to a much greater degree than before the war. But the time is ripe, and the need apparent, to equip the Government to act more promptly, more flexibly, and more forcefully to stabilize the economy—to carry out more effectively its charge under the Employment Act."

We fully agree with the President. The three measures proposed by him in this connection—standby tax reduction authority, standby capital improvements authority, and permanent strengthening of the unemployment insurance system—can provide powerful leverage to arrest recessionary spirals and to return the economy to the path of healthy growth. These measures have been proposed, however, to deal with the next recession. We believe they are needed now.

The level of unemployment—officially close to 6 percent and, when hidden unemployment is taken into account, probably over 9 percent—is intolerably high. We cannot afford to be satisfied with a gradual approach to its reduction. Moreover, as indicated elsewhere in this statement, there is every reason to believe that the forces making for the present upturn in production and employment will begin to lose momentum during the second half of this year. The deceleration of their rise could well be paralleled by rising unemployment resulting from the normal growth of the labor force and continued rapid advances in productivity flowing from the new technology.

We would therefore urge that the measures proposed by the President be enacted without delay with certain modifications—affecting both the preconditions for use of the requested authority and the content of the proposals—which will permit the President to put them into effect immediately and will add to their effectiveness.

Tax reductions may be needed this year

If standby tax reduction authority were granted to the President during the early months of this session of Congress, he would be able to make reductions in income tax rates at the first signs of a slowdown in the pace of the upturn. He would be able, for example, to act this summer or fall if unemployment at that time should remain intractably high or being a new rise.

We would urge, however, that the details of the President's tax proposal be modified to obtain greater leverage on the economy for the same temporary loss of revenue. The President proposes a temporary uniform reduction in all individual income tax rates, with a 5-percentage-point limit on the extent of such reduction. This would mean significant losses of revenue which would have little or no impact on the economy, as the greatest dollar amounts of tax savings would go to the highest income families who would tend to save rather than spend their gains from the tax reduction.

A family with taxable income (after exemptions and deductions) of $2,000 would gain $50 if a 5-percentage-point tax reduction remained in effect 6 months; a family with taxable income of $200,000 would gain $5,000 on the same basis. The additional purchasing power placed in the hands of low-income families through tax reduction would tend to be spent almost immediately and almost in its entirety—for these families have great unfilled needs. The additional purchasing power placed in the hands of high-income families through tax reduction will tend to remain sterile—neither spent nor invested—because such families are most unlikely to have unmet needs for consumer goods, and are equally unlikely to find profitable outlets for investment of their tax savings while the economy is on the downgrade or operating at levels far below its capacity.

For maximum effectiveness, temporary tax reductions must create high velocity dollars rather than additions to stagnant pools of savings. For this reason, we urge that the President's proposal be amended to provide for reductions in the first bracket income tax rate rather than a uniform across-the-board reduction.

Reducing the 20-percent first bracket rate by somewhat more than half would cost no more in terms of reduction of revenues than the President's proposal, but it would add significantly to the impact on the economy. On a 6-month basis, a reduction of the first bracket rate to 10 percent, for example, would add $100 to the purchasing power of both the family with $2,000 of taxable income and the $200,000-income family. Less would go to those who would not use it; more would go to those who can be counted upon to spend it quickly, to the benefit of the economy as a whole.

Speed implementation of capital improvement programs

Similarly, we urge modification of the criteria proposed by the President for triggering the exercise of standby authority to accelerate and initiate capital improvement expenditures. Specifically, we propose that the President be permitted to exercise this authority whenever unemployment has exceeded 5 percent for 3 consecutive months.

Since the use of this power would, in any case, be discretionary with the President, he would be under no compulsion to invoke it if analysis of the situation persuaded him that unemployment in the immediate future would fall below 5 percent. The modification we propose, however, would enable him to make use of the standby authority whenever unemployment was dangerously excessive—even if it were not on a rising trend. Based upon careful analyses of the factors underlying the current increase in production, it appears probable that unemployment will tend to remain above 5 percent throughout the first half of this year, and thereafter is likely, at best, to stabilize at that high level if it does not actually increase. In either case, it would be not only desirable but necessary to increase capital improvement spending and it would be well for the President to have the authority to do so without waiting for further congressional action.

Strengthen unemployment compensation proposals

The permanent reforms in unemployment compensation proposed by the President are long overdue. We support the administration's bill, but believe it should be strengthened in a number of respects.

The unemployment compensation system can and should function as our first line of defense against recession. The system, as such, is essentially a standby antirecession device because the volume of benefit payments adjusts automatically to the business cycle. Unemployment insurance has not, hitherto, performed its antirecession function effectively because benefit amounts and duration of benefits have been inadequate to meet both the needs of the unemployed and the requirements of the economy.

The President's proposal calls for immediate Federal supplementation of the duration of benefit payments provided under the State laws, up to a maximum of 13 weeks to workers with at least 3 years' experience in covered employment. Enactment of this recommendation would represent significant progress, even though the 39 weeks of total duration that would be the maximum available to workers in all but a few States would be less than sufficient to deal adequately with long-term unemployment as we have experienced it during recent recessions.

The administration bill, however, would start payments of extended benefits only after the individual worker had had 26 weeks of unemployment (beyond the waiting week, if any). Thus the individual entitled to fewer than 26 weeks of benefits under the law of his State would suffer a period of unemployment during which no benefits would be payable to him either by the State or the Federal Government. This vacuum can and should be filled by amending the administration bill to require all States to provide at least 26 weeks of benefits to all eligible workers who remain unemployed that long.

We urge also that consideration be given to liberalizing the criteria which would trigger the President's authority to proclaim an extension of duration for workers with less than 3 years of experience in covered employment.

Make benefits adequate now

With respect to benefits, the President's program calls for a phasing of increases in State maximum benefits with the last stage to be reached in 1968. The gradual approach toward the raising of benefits provided under the State laws is understandable in view of the need of many States to strengthen their unemployment compensation funds so that they will be able to carry the burden of increased benefit payments.

Unemployed workers and their families, however, need the protection of more adequate benefits now. Similarly, the economy has equally urgent need—now—for the added consumer purchasing power that more adequate unemployment insurance benefits would provide.

Approximately 2½ million workers are now drawing unemployment compensation under the various State and Federal programs. It is estimated that their weekly benefits would be approximately 25 percent higher if the final stage of the administration's benefit proposals were to be put into effect now. Average weekly benefits would therefore be increased by approximately $8.50 per week. This would add more than $20 million a week—an annual rate in excess of $1 billion—to consumer purchasing power.

Both the plight of the unemployed and the condition of the economy would be materially improved if that much additional purchasing power were available immediately. We therefore urge that the administration's unemployment compensation bill be amended to provide for immediate Federal supplementation of benefit amounts payable under the State laws to the levels that would be payable after effectuation of the final stage of the benefit improvements called for under that bill. Such supplementation could be financed either directly out of the Federal Treasury, or through an increase in the payroll tax levied upon employers to finance the unemployment compensation system. A relatively small increase in that tax, maintained over an extended period, could repay the Treasury for the cost of such benefit supplementation. Offsets against such a tax increase could be provided to employers in States which put into effect, in advance of the schedule set forth in the administration bill, the benefit improvements provided for in that bill. Such offsets would provide an incentive for those States that are financially able to do so to meet minimum standards of benefit amounts without unnecessary delay.

The added support that increased benefits, payable from the beginning of unemployment, would provide for the economy during a recessionary period would help to reduce the number of workers suffering long-term unemployment and therefore entitled to draw additional weeks of benefits under the administration's proposals for extension of duration.

With the changes suggested above, the antirecessionary measures proposed by the President would become much more effective bulwarks against a rising tide of negative economic forces. I should like to emphasize, however, that they should be considered not only as defenses against the next recession but as weapons to be used now against the present intolerably high level of unemployment that is costing us so much both in family hardship and in lost wealth.

Flexible workweek

We believe that the length of the statutory standard workweek is not a matter for arbitrary decision. It should be consistent with the economic needs of the Nation and the national objective of a full employment economy. We urge favorable consideration for one way of doing this which would add a fourth weapon to the arsenal of measures proposed by the President to combat recession—amendment of the Fair Labor Standards Act to provide for automatic adjustment of the statutory standard workweek based upon the level of unemployment.

This, as spelled out by my own union, the UAW, would mean that instead of being fixed at the same number of hours regardless of economic conditions, the length of the workweek would be related to the demands of industry for workers and the number of workers available to meet those demands. When industry's need for labor was high, and unemployment correspondingly low, the standard workweek would remain at 40 hours. When industry's need for labor was low, and unemployment correspondingly high, the length of the workweek would be reduced accordingly so as to help create more jobs.

We are well aware, as this statement makes clear elsewhere, of the vast public and private needs which still remain unmet in this country, as well as the demands placed upon the economy by the needs of national defense. We accept in addition our moral obligation to make available from our national resources assistance to less fortunate countries in the elimination of hunger, illiteracy, and disease and in the development of their own economies. These needs and obligations are the basis for the point of view expressed in 1960 by President Kennedy—then Senator Kennedy—when he spoke to a convention of the Steelworkers Union about the shorter workweek.

"My own feeling is that I would prefer a different solution. I would prefer the solution of this economy going ahead at such full blast that in a 40-hour week we would barely produce what we could consume * * *."

Mr. Kennedy elaborated that view following his election to the Presidency, when he told a press conference:

"* * * I would say that I am opposed to a shorter workweek. I am hopeful that we can have employment high 5 days a week, and 40 hours, which is traditional in this country, and which is necessary if we are going to continue economic growth, and maintain our commitments at home and abroad.

"So that I would be opposed to any arbitrary reduction of the workweek, and I am unhappy when I see the workweek reduced artificially, in the sense that the pressures of a declining economy reduce it, so that we get averages of 38.5 hours a week instead of the 40 hours a week * * *."

Within recent weeks the President has again indicated that his views are still what they were when he addressed the Steelworkers Union in 1960.

The standard workweek can be flexible

The President's position is understandable insofar as it relates to an arbitrary, nationwide reduction in the statutory standard workweek. But it is impossible to explain to millions of unemployed workers why the achievement of our national objectives requires the utilization of all available man-hours on the basis of a 40-hour week, while the hours that they are prepared to devote to those objectives remain unused and are lost forever. What is painfully obvious to them is that industry at the present time is not able to make use of all the man-hours available, and that if the workweek were reduced, there would be more jobs for those now unemployed.

The President's position is sound within the context of "an economy going ahead at such full blast that in a 40-hour week we would barely produce what we could consume." The unemployed are right within the context of an economy which still denies them the opportunity to provide for their own individual and family needs and to make their contribution toward the needs of their country. The apparent conflict between them disappears if we reject the assumption, now implicit in the Fair Labor Standards Act, that the standard workweek must be the same in both sets of conditions.

We should retain the statutory standard 40-hour week when we have full employment and are able to make full use of available man-hours. When we are wasting man-hours through unemployment, we should reduce the standard workweek to the extent necessary to create additional job opportunities.

Our specific proposal is that the Fair Labor Standards Act be amended to provide for automatic adjustment of the statutory standard workweek based upon the level of unemployment. When unemployment is less than a specified percentage of the labor force, the statutory standard workweek would remain at 40 hours. If unemployment should rise above that percentage for a specified period of time, the statutory standard workweek would automatically be reduced; if unemployment rose to still higher levels, the standard workweek would be further reduced accordingly. The reverse process would be applied as unemployment declined.

The specific figures to be written into the law would have to be developed on the basis of studies to determine how many unemployed workers are likely to be reemployed as a result of each successive hour of reduction in the standard workweek. Account would have to be taken of the fact that some employers, even in a general recession, and even with the additional overtime costs resulting from reduction of the standard workeek, would continue to schedule 40 hours or more of work per week to meet demands for their products. A separate sliding scale would have to be developed to restore the 40-hour standard workweek step by step as unemployment declined.

Adjustment fund would maintain weekly wages

The amendment to the Fair Labor Standards Act which we propose would have to provide for maintenance of purchasing power despite reductions in the standard workweek. Unemployment reflects a deficiency in demand. Merely spreading the same total payroll among a larger number of workers, each employed fewer hours, would only cause hardships to be spread a little farther and would contribute nothing to the correction of that deficiency. In order to achieve a balance between purchasing power and productive capacity, reductions in the workweek must be coupled with compensation for the hours cut out of the regular weekly schedule to maintain the same weekly pay.

However, when unemployment is high, the individual employer—particularly the small employer—is least able to afford the compensating pay required to maintain take-home pay in the face of reduced workweeks. We therefore propose that such compensation be financed not by the individual employer but through a national workweek adjustment fund to be accumulated out of revenues from a small payroll tax on all employers.

This method of financing would have a stabilizing influence on the economy, since in good times when demand is high, money would be drawn into the fund, and in bad times when demand needs to be stimulated it would be withdrawn from the fund and used to increase purchasing power.

When a reduction in the statutory standard workweek comes into effect, we propose that any employer who reduced hours worked accordingly would be reimbursed from the fund for the added cost of continuing to pay his workers for 40 hours a week at their normal wage rates.

An employer who did not reduce hours worked to the level of the temporarily reduced standard workweek would not be so reimbursed. He would pay out of his own pocket full wages for the hours in excess of that standard plus premium overtime rates for those hours. This would provide a stimulus to reduce scheduled hours and to hire additional workers.

The cost of this proposal, when spread over the entire business cycle, would require only a small tax on payrolls—quite likely less than 1 percent. The small cost involved would be offset to a significant degree by reductions in unemployment compensation contributions and supplemental unemployment benefits payments now borne by employers as a result of high unemployment. Whatever net cost remained would be far less than the cost of unemployment.

If the proposal for a flexible workweek were made effective without delay, as it should be as a means of immediately relieving our current heavy unemployment, it would have to be financed in the beginning through an advance to the national workweek adjustment fund from the Treasury, to be repaid later out of the revenues of the proposed payroll tax.

The benefits of the proposal are obvious. Not only would it help to stabilize the economy by helping to offset the decline in labor income which normally accompanies a recession, not only would it reduce the financial hardships suffered by workers and their families in consequence of unemployment, but by creating more jobs it would protect those workers from the loss of human dignity and self-respect and the destruction of family morale which frequently constitute the most disastrous even though immeasurable costs of unemployment.

To the extent that Government action succeeds in keeping unemployment at or close to the minimum frictional level—which we place at 2 to 2½ percent of the labor force—the amendments to the Fair Labor Standards Act which we propose would remain inoperative. Certainly the proposal itself it consistent with the mandate of the Employment Act of 1946 to "promote maximum employment, production, and purchasing power." It would be an important step in the implementation of that mandate. It would assure workers that if Government failed for one reason or another to meet its responsibilities under the Employment Act, they would not be victimized by that failure. And they would no longer be puzzled and disheartened by the argument that 40 hours of work a week are needed from everyone in the national interest while they search in vain for an opportunity to work.

The upturn from the recession of 1960–61

The necessity for a more vigorous attack on unemployment is underlined by the fact that the present upturn in economic activities is uniquely different from the record of pickups from previous postwar recessions. The rise in production has been similar to the past. But thus far there has been only a negligible increase in employment and a very small reduction in unemployment.

This is an alarming development, three-quarters of a year after the recession low point. The record of upturns from previous recessions indicates that the rapid phase of the pickup continues for only four or five quarters of a year after the low point. It is during these 12 to 15 months that production picks up sharply and unemployment declines rapidly.

On the basis of the past record, therefore, most of the rapid phase of the present upturn has gone by with a very poor improvement in employment and inadequate reduction in unemployment—unless additional demands for goods, services, and jobs are added in order to extend the rapid phase of this pickup through the second half of 1962 and into 1963.

Only the addition of an extra stimulus for the demands of goods and services, now, can prevent a slowdown of the present upturn in the second half of the year, with continuing high levels of unemployment, and the danger of another recession during 1963.

The following is the record, three-quarters of a year after the low point of the postwar recessions.

Changes in real GNP during 3 quarters immediately following trough of each postwar recession

	Percent		*Percent*
1949–50	+11.1	1958–59	+6.8
1954–55	+7.6	1961	+7.4

By the fourth quarter of 1961 the rise in real total production from the recession low point was roughly similar to the production upturns in similar periods of time from the 1954 and 1958 recessions. It was less than the upturn from the 1949 recession, which was affected by the Korean war; the third quarter after the recession low point was the third quarter of 1950, after the outbreak of the Korean conflict.

Despite the 7.4 percent rise in total national output three quarters after the recession low point in 1961, there has been hardly any rise in total employment, compared with the increases following previous recessions.

Change in total civilian employment, 3 quarters after trough of each postwar recession

	Number	Percent
1949–50	+1,741,000	+3.0
1954–55	+1,801,000	+3.0
1958–59	+1,219,000	+1.9
1961	+113,000	+.2

The rise in total employment in 1961 has been negligible. Farm employment dropped, while nonfarm employment rose at a very slow pace. Nine months after the recession low-point, the 1961 upturn in employment has lagged badly behind the pickup from the previous postwar recessions.

Change in nonfarm wage and salary employment, 3 quarters after trough of each postwar recession

	Number	Percent
1949–50	+2,738,000	+6.3
1954–55	+1,679,000	+3.4
1958–59	+1,707,000	+3.4
1961	+922,000	+1.7

The rise in nonfarm wage and salary employment has been only about one-half as fast as in the upturns from the 1954 and 1958 recessions and only about one-fourth as fast as in the pickup from the 1949 recession.

Change in unemployment, 3 quarters after trough of each postwar recession

	Number	Percent
1949–50	−1,317,000	−30.6
1954–55	−1,007,000	−26.1
1958–59	−1,002,000	−20.0
1961	−356,000	−7.3

The decline in unemployment in 1961 has been the smallest, by far, of any of the postwar upturns from recessions—approximately one-third of the reduction in unemployment during the upturns from the 1954 and 1958 recessions and less than one-fourth the reduction during the upturn from the 1949 recession. This very slow reduction of unemployment in 1961 occurred despite the fact that the civilian labor force declined between the recession low point and the fourth quarter of the year.

Unemployment rate, seasonaly adjusted, in 3d quarter after trough of each recession

	Percent		*Percent*
1949–50	4.7	1958–59	5.8
1954–55	4.4	1961	6.3

The decline in unemployment which can be attributed to economic recovery in the first three quarters following the trough of the 1961 recession is overstated in the above table, since in fourth quarter 1961 there were nearly 200,000 more men in the Armed Forces than in the first quarter, and this undoubtedly absorbed men who would otherwise have been unemployed.

The unemployment rate, three-quarters of a year after the 1961 recession's low point, was higher than it was at the same point in 1950, 1955 and 1959—indicating the possibility that unemployment once again may level off at a new and higher plateau.

Three-quarters of a year past the low point of the recession of 1960–61, unemployment has been hardly dented, with only a negligible increase in employment. Hours of work, of course, have picked up. But the increase in working hours in the 1961 upturn from the recession has not been uniquely different from the previous postwar pickups.

Productivity has risen sharply

The unique feature of the upturn from the 1960–61 recession, to date, has been an extraordinary increase in productivity. This sharp rise in productivity has not been confined to one or two sectors of the economy alone. It has been widespread—apparently in trade, construction, finance, and services, as well as in farming and manufacturing.

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The November issue of Fortune ("Business Roundup") has this to say about productivity advances through the third quarter of 1961, which was the second quarter after the recession low point:

"Although short-term measures are rough at best, it appears that overall private nonfarm productivity has risen at an annual rate of about 9.5 percent in the upturn of the past 6 months. This is a much faster rise than in the last two postwar recoveries. Productivity in manufacturing has risen at a rate of about 12 percent, but such a pace has been registered before; it appears that the extra gains have been for productivity in trade, services, and construction."

This rise in productivity in the fourth quarter of 1961, three-quarters of a year after the recession low point, was likewise sharp and widespread—continuing the general trend that got underway last spring.

This extraordinary rise in productivity means increases in profit margins from the lows that were registered during the general economic decline. But it also means substantial increases in output with little increase in employment.

During previous pickups from postwar recessions, manufacturing employment turned up slowly as factory productivity mounted. But employment picked up in other activities. During the 1961 upturn, however, manufacturing employment has picked up slowly, but other kinds of employment have also picked up only slowly or have declined. Only State and local government employment has risen somewhat more rapidly than in the past.

The extraordinary rise in productivity will slow down somewhat in the months ahead and employment will pick up as production continues to rise. But the "normal" pace of productivity advance in the coming months may well be much greater than in 1955–56 and 1959–60. The pickup in employment may continue to be at a slower rate than in past upturns.

The threat of continuing high unemployment

These trends mean that even if total national output should reach an annual rate of close to $570 billion by the middle of this year, as the Council of Economic Advisers predicts—a prediction that may prove somewhat overly optimistic—the number of unemployed will probably be approximately 5½ percent of the labor force—close to the 5.6 percent unemployment level in 1954, which was a recession year, rather than a period of upturn.

A continued reduction of unemployment in the second half of 1962 and in 1963 will require a continuing rapid increase in production. But the past record shows that the upturn will probably slow down after the spring quarter of 1962 if the stimulus of additional demands for goods and services is not added, now, to reinforce the pickup. Analysis of the major factors in the present upturn also indicates that the forward momentum will begin to lose its steam in the second half of the year.

A key factor in pulling the economy out of the decline and in providing a strong forward momentum during 1961 was the building of business inventories. The shift in inventories from cutbacks in the first quarter of 1961 to the buildup of the fourth quarter, added an annual rate of $8½ billion to total national production. But businessmen cannot be expected to build up their stocks of goods on hand at a very sharp pace indefinitely. By the spring quarter of 1962 there will have been 15 months of rapid inventory building. It is reasonable to expect the inventory buildup to level off in the second half of 1962 and possibly to weaken if sales fail to keep up to business expectations. Business inventories will probably add little or nothing to economic activities after the spring quarter of 1962.

The rise in Federal Government expenditures during 1961 has also been a key factor in the present upturn—providing much of the basis for the inventory buildup during most of last year. By the fourth quarter of 1961, Federal Government expenditures were $5.2 billion greater (annual rate) than in the first quarter. They are expected to rise an additional $3 billion (annual rate) in the first half of this year. But after the spring quarter of 1962, Federal expenditures for goods and services will rise only slightly, on the basis of present plans. If these plans are not changed, Federal expenditures will add very little to the demand for goods and services in the second half of this year.

Where will we get more momentum?

What other factors, if any, can be expected to carry the economic advance forward after mid-1962?

Consumer spending rose rapidly in the fourth quarter of 1961, at an annual rate of 9 percent. Consumer expenditures are expected to continue to rise at a rather rapid pace in the months ahead—with increases in family incomes based on a continuing, though decelerating, increase in working hours and some improvement in employment. But part of this rise in consumer expenditures, particularly for hard goods, is boosting the installment debt of many families, and installment debt cannot be expected to increase at a rapid pace indefinitely. Since the buying power of most families has increased at a very slow rate in the past 5 years, consumers have become increasingly cautious about building up large debts. In addition, working hours are tending to level off and further increases in income will depend largely on wage and salary increases. The rapid rise in consumer expenditures, therefore, will probably slow down in the second half of 1962—continuing to add to the demand for goods and services, but at a slower pace than the 9-percent annual rate of increase in the final quarter of last year.

The upturn in homebuilding is expected to continue at a slower pace this year. It may level off or even begin to decline during 1962, if money becomes tight and interest rates rise.

Expenditures for goods and services by State and local governments, it is anticipated, will probably increase through 1962 at about last year's pace—neither adding to nor detracting from the economy's forward momentum.

Can we rely on business investment to maintain momentum?

The Council rests its hope for achievement of its 1962 goal of $570 billion in gross national product primarily on a rise in business investment during the second half of this year to maintain the forward momentum of the economy as other factors in the present upturn lose their force.

The Council's report sets forth no specific figures for the components of gross national product, either for the year 1962 as a whole or quarterly. Its projections with respect to the components can therefore only be approximated by reading between the lines of its report. This is admittedly a somewhat hazardous operation, and our attempt to perform it may do the Council an injustice. Neverthless, it is important to evaluate as best we can the outlook for the period immediately ahead so that proposed policies may be appraised within a realistic framework.

Assuming the $570 billion goal for the year as a whole is to be attained by a rise in GNP at a steady pace sustained throughout the year, GNP would have to be at an annual rate $576 billion in the third quarter of 1962. The Council's report suggests that Federal purchases of goods and services will, during that quarter, be running at an annual rate of approximately $63 billion; that the rate of State and local expenditures will be about $56 billion; that nonfarm residential construction will be at a rate of $24 billion; and it may reasonably be expected that net exports will run at a rate in the neighborhood of $4 billion. If consumption continues to account for 64 percent of total GNP, its annual rate during the third quarter of 1962 would be $369 billion. This, however, may be somewhat overoptimistic in view of the fact that as recovery proceeds, profits will tend to take a larger share of GNP, and personal income a correspondingly smaller share. These factors, then, would total $516 billion, leaving $60 billion for inventories and business fixed investment.

As we noted above, by the third quarter of this year inventories should be in proper balance with sales, and continued inventory accumulation should merely be keeping pace with increases in final demand. Current stockpiling connected with forthcoming steel negotiations, however, may have a serious negative effect on the rate of inventory building. It therefore seems conservative for this purpose, and perhaps overoptimistic, to project the net increase in inventories during the third quarter at about $3 billion—only $1.5 billion less than in the fourth quarter of 1961. This would mean that business fixed investment would have to rise from an annual rate of $48.2 billion in the fourth quarter of 1961 to about $57 billion in the third quarter of 1962, an increase of more than 18 percent. It would mean a total increase of more than 27 percent from the $44.8 billion trough level in the first quarter of 1961.

This is far greater than the rate of increase achieved during any comparably long period of recovery during the postwar years. The percentages of increase in business fixed investment during the first seven quarters of recovery from the three preceding recessions were 19.6 percent from the fourth quarter of 1949 to the second quarter of 1951; 16 percent from the third quarter of 1954 to the first quarter of 1956; and 8.8 percent from the second quarter of 1958 to the fourth quarter of 1959.

Even if we allow for sufficient error in our estimates of the other components to reduce the business fixed investment quota of a $576 billion GNP in the third quarter of 1962 to $54 billion, the increase from the trough would still be in excess of 20 percent, more than in the first seven quarters of upturn following any of the preceding postwar recoveries.

The Council itself stresses the importance of a sharp rise in fixed business investment as the basis for its hopes for a $570 billion gross national product this year. Its report says, "* * * By late 1962, continued advance will depend heavily on the ability of fixed investment outlays to replace inventories as a key expansionary factor."

We are not alone in our fear that this reliance may well turn out to have been misplaced. For example, the January 25, 1962, issue of the Bureau of National Affairs Report for the Business Executive says:

"One of the big question marks in the administration's forecast of a boom into 1963 is how much increase there will be in *plant and equipment spending.*

"To get the expansion in business the President wants, investments in capital equipment will have to rise 25 or 30 percent this year. This would be a sizable hike in plant and equipment outlays, even with the stimulation to investment that would flow from the easier depreciation and tax credits that are expected this year.

"The President's advisers concede that businessmen have not yet planned any major expansion of productive facilities * * * but they hope the continuation of the recovery will lead to an upward revision in investment plans." [Emphasis in original.]

Business Week, in its issue of February 3, 1962, express similar reservations, saying:

"* * * it must be borne in mind that business forecasts have an ominous unanimity: good for the first of the year—probably very good indeed—but vague on the second half * * *.

"Rising business outlays for plant and equipment will be needed later in the year as an economic booster.

"This will be true particularly as the rate of inventory accumulation lessens—as it must once the issue of wages in steel is resolved.

"Surveys, both Government and private, indicate that 1962 outlays will increase substantially over last year. But this could be true if the rate of investment were simply to hold at its present level."

This at best uncertain outlook for the second half of the year adds weight to the proposals made earlier in this statement for putting into effect now, in order to give the economy maximum forward momentum, measures that President Kennedy has proposed for use in future recessions.

Monetary policy should stimulate demand

The Government's monetary policy should also actively encourage a rapid rise of demand for goods and services so that full employment can be reached and sustained. An expansionary monetary policy is needed in any case, but it is particularly needed, now, if the administration persists in its move to a relatively restrictive fiscal policy, with a projected budget surplus of $4.4 billion in fiscal 1963 (on income and product account).

The Government's monetary policy, thus far, has avoided the errors of the recent past, when the money supply was tightened and interest rates were raised, shortly after the upturns from the recessions of 1954 and 1958 began. In avoiding these past errors, the Government has been aided by such great business liquidity that very little of the pickup to date has been financed by bank loans. Nevertheless, interest rates on long-term Government bonds have been creeping up from 3.73 percent last May to 4.08 percent in mid-January. The 4.08-percent, long-term rates are already as high as they were in 1959. There is a danger that they will continue to move up and discourage a further expansion of homebuilding and other economic activities.

In order to encourage a continuing expansion of demand, the rediscount rate, which the Federal Reserve System charges commercial banks for loans, should be reduced from 3 percent to 2¾ percent. Such a reduction would clearly indicate the Government's determination to maintain a relatively easy money policy. It would make possible low-interest rates on long-term loans, such as mortgages, business loans, and the cost of funds borrowed by State and local governments.

In addition, the Federal Reserve System's Open Market Committee should actively engage in the purchase of long-term Government bonds in the money market. Although the Federal Reserve shifted its position last year, from its previous rigid refusal to buy long-term Government bonds, such purchases have been far too hesitant.

Purchases of long-term Government bonds by the Open Market Committee will increase the free, lendable reserves of the commercial banks above their recent level of about $500 million. Open market operations should be designed to maintain a fairly sizable level of free reserves (about $750 million or more) in the commercial banking system.

At the same time, the Federal Reserve should maintain its policy of stabilizing interest rates on short-term Government securities. Such a policy is necessary in order to make it less likely that a substantial differential will develop between short-term rates here and in foreign countries. It would help to curb the outflow of foreign-held investments in such securities to other countries.

PRODUCTIVITY: A BOON AND A CHALLENGE

CEA's projections fall short of reality

A major factor in all forward planning is our estimate of the possible rate of productivity advance, which will largely influence both our opportunities for economic progress and the extent of the need to create additional job opportunities. The Council of Economic Advisers is to be congratulated on having given recognition to the fact that rates of productivity advance in the distant past are no guide to what may be expected in the present and future; but, even so, its estimates of what may be anticipated for the next 2 years and for the whole decade of the sixties fall short of reality when we consider both what our economy showed it could do in the years of relatively unfettered growth immediately following World War II, and the continuing technological revolution which is more and more influencing our rate of productivity advance.

We must not plan for 4-percent unemployment

It comes as a shock to realize, on careful analysis of the Council's projections, that they are based on anticipation of a continuing 4-percent rate of unemployment. In the opening chapter of its report the Council indicated that an unemployment rate of 4 percent was a realistic interim goal because structural unemployment—such as the chronic unemployment in distressed areas—would take time to cure. The report stated:

"*In the existing economic circumstances*, an unemployment rate of about 4 percent is a reasonable and prudent full employment target for stabilization policy. *If we move firmly to reduce the impact of structural unemployment, we will be able to move the unemployment target steadily from 4 percent to successively lower rates.*" [Emphasis added.]

The structural rationalization for acceptance of a 4-percent unemployment rate is hard to accept in view of the impressive evidence to the contrary that the Council cited in Supplement B to its March 6, 1961, statement to this committee. The Council at that time said:

"The question sometimes arises whether the obstinate refusal of the unemployment rate to decline below 5 percent since the end of 1957 is a consequence of long-term structural changes in the age, sex, and other composition of the labor force, and not of weakness in aggregate demand. If this were so, it would mean that measures to stimulate the general level of economic activity might fail to get the overall unemployment rate down to tolerable levels. Indeed, as the cyclical component of unemployment vanished, leaving only the hard core, the result might be inflationary wage increases.

"*But this argument can be shown to be false.*" [Emphasis in original.]

The supplement on this subject concluded:

"At the end of this long argument it is worth saying that it is no part of our intention to cry down structural unemployment or explain it away. The problems of younger and older workers, of nonwhite members of the labor force, of the technologically displaced, and of the distressed need to be attacked at the source. But our concern for them ought not to divert our attention from the real cause of weakness in 1961's labor market—and that is inadequate demand."

It must be emphasized that we will not solve the unemployment problem unless we set ourselves targets based on full employment. If we intend to reduce unemployment substantially below 4 percent, as we can and must, then we must make our projections and establish our plans on the basis of that lower figure.

CEA projection assumes a slowdown in productivity advance

It comes as a further shock to realize that the Council's projections are based on the assumption that the potential rate of productivity advance from 1960 to 1970 will represent a smaller annual average than that of the period 1947–60 as calculated by the Council. The Council's estimates of potential gross national product per man-hour (which include an adjustment to take into account the fact that 1960 was a slack year because of the recession) show an average rate of advance of 3.2 percent per year for 1947–60, and only 3 percent per year for 1960–70.

Since the major problem arising out of a rapid rate of productivity advance is the necessity to create new jobs to replace those which disappear, it is clear that an underestimate of the productivity rate in future projections means that we may not be prepared to create as many new jobs as will actually be required, and unemployment will rise accordingly. It is for this intensely practical reason, rather than because of any academic theory, that a realistic estimate of the rate of productivity advance is essential in planning for the future.

We must recover the momentum of 1947–53

There is more than one reason for the Council's underestimate of what we may anticipate as the future pace of productivity advance. Obviously, it has given too much weight to the years after 1953, when the economy experienced three recessions in rapid succession. At the very least, it should have based its projections on the entire 1947–60 period, with some allowance for the fact, demonstrated by Bureau of Labor Statistics analyses, that there is a marked tendency for the pace of productivity to accelerate with time. One set of calculations by the Bureau, based upon the experience of 50 years, suggests that if we were using our potential, productivity would now be increasing at a rate greater than 4 percent per year. Although the 1947–53 period, when we operated close to potential, would be a realistic basis for projection, we may use as an alternative the 1947–54 period, for which the Council calculates a potential rate of productivity advance averaging 3.8 percent per year. The report suggests that the "vigorous growth of the early postwar period benefited from the possibility of renewing a capital stock which had aged during the depression and war years of low investment," and that "simple continuation of recent trends will not be sufficient to repeat that performance." We plead, however, for recognition of the fact that "simple continuation of recent trends" will also be totally insufficient to solve our economic problems and restore full employment. In order to create the jobs we need we must bring about a rapid increase in demand analagous to that of the early postwar years. If we succeed, we will certainly create also a similar surge of new investment, and the combination of these two factors must result in another leap forward of productivity.

Since the Council's report urges programs designed to stimulate investment, its projections should take into account the consequences of such investment in further accelerating the pace of productivity advance.

The Council's equations versus 1961 realities

The Council's underestimation of the potential of the economy may be seen in yet another way—by comparing actual developments during the current recovery with what would have happened if reality conformed to the equations upon which the Council bases its projections.

The members of the present Council presented their equations on the occasion of their first appearance before the Joint Economic Committee on March 6, 1961. These equations yield results that reasonably approximate the actual course of events during the first three calendar quarters of recovery from earlier postwar recessions but they are far wide of the mark when compared with the facts of the current recovery.

The first equation presented by the Council last March relates growth in output per person employed to percentage changes in real gross national product. The results derived from this equation for the first three quarters of recovery in each of the four postwar recessions compare with the actuality as follows:

	Increase in output per person		
	Actual	Estimated from Council's equation	Difference
	Percent	*Percent*	*Percent*
4th quarter 1949 to 3d quarter 1950	8.0	7.3	+0.7
3d quarter 1954 to 2d quarter 1955	4.5	5.0	-.5
2d quarter 1958 to 1st quarter 1959	4.8	4.5	+.3
1st quarter 1961 to 4th quarter 1961	7.2	4.9	+2.3

It is apparent from the above figures that the Council's equation for output per employed person yields a gross underestimate of the rise during the current recovery. The data for average weekly hours worked in manufacturing industry indicate increases of the same general magnitude as during previous recoveries. If this is also true of other industries, as there is reason to believe it is, the equation grossly underestimates productivity per man-hour. The probable explanation for the error resulting from application of this equation to the present recovery is that the impact of automation is now beginning to be felt in fuller measure than earlier in the postwar period.

The underestimation of the productivity increase is so great that use of this equation to forecast employment in the fourth quarter of 1961, based upon the increase in GNP to that quarter, would have led to an error of 1.6 million, compared to no error greater than 0.5 million for any of the three preceding recessions. Comparisons of actual and estimated civilian employment for each of the four postwar recessions are as follows:

[In millions]

	Civilian employment		
	Actual	Estimated from Council's equation	Difference
3d quarter 1950	60.2	60.7	-0.5
2d quarter 1955	62.4	62.1	+.3
1st quarter 1959	65.0	65.3	-.3
4th quarter 1961	66.9	68.5	-1.6

The second equation presented by the Council last March relates the rate of unemployment to the percentage gap between actual and potential output. This equation cannot be used in connection with the 1949–50 recovery because the Council's measures of potential output are not applicable to that period. For subsequent periods, however, the deviation of the results of the equation from actual experience is significantly greater for the current than for the preceding recoveries, as the following figures show:

	Unemployment rate		
	Actual	Estimated from Council's equation	Difference
	Percent	*Percent*	*Percent*
4th quarter 1949 to 3d quarter 1950	4.7	(1)	(1)
3d quarter 1954 to 2d quarter 1955	4.4	3.9	+0.5
2d quarter 1958 to 1st quarter 1959	5.8	5.7	+.1
1st quarter 1961 to 4th quarter 1961	6.3	5.5	+.8

[1] Not available.

The failure of this equation to yield a closer approximation to actual experience in the current recovery is also a reflection of an underestimation of productivity.

The Council's third equation relates changes in the rate of unemployment to percentage changes in real gross national product. Although this equation yields results for the three earlier recoveries that are within reasonable range of actual experience when applied to the current recovery it projects a decline in the unemployment rate nearly four times as great as that which actually occurred. Comparisons of actual and estimated decreases in the unemployment rate for the four postwar recessions are as follows:

	Percentage point reduction in unemployment rate		
	Actual	Estimated from Council's equation	Difference
4th quarter 1949 to 3d quarter 1950	2.2	3.0	−0.8
3d quarter 1954 to 2d quarter 1955	1.6	2.0	−.4
2d quarter 1958 to 1st quarter 1959	1.5	1.7	−.2
1st quarter 1961 to 4th quarter 1961	.5	1.9	−1.4

According to this last equation, the unemployment rate during the fourth quarter of 1961 should have been 4.9 percent instead of the 5.5 percent yielded by the second equation and the 6.3-percent actual rate.

The error in the results yielded by this third equation also is a consequence of its failure to reflect accurately the current potential for increases in productivity. This error is built into all three equations because they measure the productivity potential not on the basis of the capabilities of the technology embodied in installed equipment, but in important part on the experience of the years since 1953 when that equipment was grossly underutilized as a result of stagnation and repeated recessions.

The marked deviation of the actual course of events during the current recovery from what would have been forecast, based upon the Council's equations, is a clear indication of the urgent necessity for the Council to raise its sights with respect to the potentials of our economy, now and in the years ahead.

Mechanical application of mathematics without recognition of the underlying realities is always a hazardous venture. It is dangerous in the extreme when it results in underestimation of the dimensions of the challenge that confronts our efforts to achieve full employment. For, when projections are made, they inevitably become elements in the determination of policy. If the projections prove to be inadequate, the policies will tend to be equally so.

As previously indicated, the Council would have done much better to measure our potential without reference to the period of stagnation and recession since 1953 and to base its calculations upon the period 1947–53 when we were operating much closer to our actual potential. Even data based upon this earlier period must necessarily yield an underestimate of our current potential, for automation was then only beginning to find practical application.

Evidence shows spread of new technologies

Additional evidence that technological change is advancing rapidly in more and more sectors of the economy can be drawn from the Labor Department's Monthly Report on the Labor Force for December 1961. In the past such changes have been largely concentrated in manufacturing industries, which have shown a much faster rate of productivity advance than such other sectors as trade, finance, and service. The Report on the Labor Force shows, however, that while productivity continues to advance in manufacturing, as witness the relatively slow increase in manufacturing jobs between June and December 1961, in spite of increasing output, there seem also to have been substantial increases in productivity in such fields as trade, finance, services, construction, transportation, and mining.

December employment in trade, for example, had risen by only 40,000 above the trough of the recession, and was still 100,000 below the level of May 1960. In previous business cycles it had reached new highs by the same stage of recovery. Employment in finance and services also was failing to gain at the same high rate as in corresponding periods of the previous recoveries. These lags in reemployment probably reflect the growing tendency toward automation of clerical office jobs, which may well be the focus of the next "automation explosion."

Of the other industries, the Report on the Labor Force says:

"While there has been a lull in the employment recovery in manufacturing jobs, other commodity-producing and related industries hard hit by the recession (construction, transportation, and mining) have not only failed to recover but have continued to decline. These three industry divisions have dropped by a total of 80,000 since recovery has been underway, in addition to their recession losses of more than 300,000. *The failure of the 1961 recovery to generate an expansion of jobs in construction, even with the sharp upturn in construction expenditures, is unprecedented in postwar experience.*" [Emphasis added.]

With the exception of mining, these are industries in which previous productivity advance has been relatively slow, but it is obvious that the technological revolution is now reaching out into these new fields.

Must we lag behind other countries?

Still further evidence that the Council's estimate of the future pace of productivity advance is seriously understated may be found in the data on growth of gross national product per man-year in various other industrialized countries, published in the Council's report. The data are cited to indicate the sharp break between prewar and postwar rates of productivity advance, but they also make a sharp and unfavorable comparison between progress in the United States and that in other countries. Of the 11 countries listed, ours stands in eighth place in its rate of postwar progress in productivity.

A further point has a more direct bearing on the Council's projections. The data for other countries unfortunately are based on production per man-year, which means that they fail to take into account the reductions in hours worked per year which have taken place in many of the countries listed; if those data were available, they would undoubtely reveal an even faster acceleration of the productivity pace than the figures shown. However, even these incomplete data reveal that in six countries—Japan, Italy, Germany, France, the Netherlands, and Norway—the average annual rate of productivity advance in the period 1950–59 was greater than the rate of increase in potential productivity projected by the Council for the United States for the period 1960–70. We cannot accept as realistic a projection which assumes that with all the stimulation we can give our economy, its rate of productivity advance will lag behind what so many other countries have already been able to achieve with far less resources than ours.

Government sector included

The Council's estimates of the actual and potential rates of productivity advance since 1947 are based on data for the entire economy, including the Government sector. But because of the great difficulty of measuring productivity in the Government sector, it is the usual practice to assume that the rate of productivity advance in this sector is zero. The gross invalidity of this assumption is obvious. For example, Donald Michael points out in the pamphlet previously quoted that in 1960 the U.S. Census Bureau was able to do with only 50 statisticians the tabulations that required 4,100 in 1950, and that the Government "is already using 524 computers and is the major customer for more of them." It is because of the impossibility of measuring productivity in the Government sector that the rate of productivity advance is normally measured only for the private sector.

The Council's projections of future total GNP, including Government, are not affected by its use of figures which assume no productivity advances in Government because the deflated GNP in which such projections are expressed make the same invalid assumption. However, the lower productivity figures resulting from that assumption do create a misleading impression as to actual and potential rates of productivity advance and lead to confusion when compared to results based upon the more usual procedure of excluding Government from such calculations.

There is also the danger that the unwary may use productivity data including the Government sector in discussions of the relationship between wage and productivity movements. This the Council implicitly recognizes to be improper in its own discussion of wage policy. There it presents data for the private economy only. But it then falls into the error of using data on the actual rather than the potential trend of productivity, apparently forgetting that unless total demand—of which wages and salaries are the largest component—is adequate to make full use of the potential, the potential will not be realized.

In any case, calculations based upon the Council's own figures reveal that the average annual rate of increase in potential productivity per man-hour in the private sector was 3.6 percent for the period of 1947–60 and 4.3 percent for 1947–54, as compared with the figures of 3.2 percent and 3.8 percent, respectively, computed by the Council for the total economy.

The economy must grow much faster than CEA proposes

Coupled with an increase in potential man-hours for the current decade estimated by the Council at 1.2 percent a year, 4.3 percent annual rate of increase in potential output per man-hour would yield a growth potential of nearly 5.6 percent per year between 1960 and 1970. Applied to the $492.6 billion private GNP potential for 1960 implicit in the Council's figure for total GNP, this rate of growth would yield a potential private GNP of $849 billion by 1970, as against the $750 billion implicit in the Council's 1970 projection if we assume that Government GNP continues to account for the same proportion of the total GNP potential as in 1960. Even on the basis of an assumed 5-percent annual growth rate, potential private GNP would be $802 billion by 1970.

A 5.6-percent growth in potential would require an increase in actual private GNP over the decade of 6¼ percent per year to fill the gap between actual and potential as of 1960 based upon the Council's estimates; and a 5-percent growth in potential would require an actual increase of 5.7 percent a year. Neither of these calculations allows for the Council's underestimation of the potential as of 1960 or for the necessity to reduce unemployment below the 4-percent rate which the Council states as an "interim" goal but uses for purposes of its 1970 projections as well as for current purposes.

For all these reasons it is clear that goals for economic growth based on the Council's projection as to the rate of productivity advance for the 1960–70 period must be substantially raised. As we have already said, it is absolutely essential that a realistic projection be made, because if the actual rate of productivity advance exceeds that which we have planned for, our plans will not provide for sufficient jobs to replace those which have disappeared due to technological progress. It would be tragic enough if we were to accept the Council's projection that we will still have 4 percent of our labor force unemployed by 1970. It would be doubly tragic if we were to find that due to shortfalls in our planning the actual rate of unemployment was even higher.

Looking only to the next 2 years, a growth rate of 5.6 percent per year applied to the $492.6 billion private GNP potential for 1960 would yield a private GNP of $580 billion for 1963, as against the $559 billion implicit in the Council's projection. This would require an increase in actual private GNP of 7.9 percent a year for the 3-year period in order to take up the slack between 1960's actual and potential production and then build on the potential. This may appear to be a very high growth target, but we believe it represents what will actually have to be done in order to reduce unemployment to even a 4-percent level by 1963 and at the same time create sufficient new jobs to replace those which will be taken over by machines. Certainly we must make every effort to come as close to that goal as possible.

Productivity of capital also rising

A realistic look at the future must take into account the fact that the productivity of capital, as well as of labor, has been rising. The January-February 1962 issue of the Chase-Manhattan Bank Newsletter states the trend this way:

"* * * the economy has been using less capital per unit of output in the postwar period than in earlier decades. In the late 19th century, it took about $3.30 of invested capital to turn out $1 of annual production. The ratio rose to $3.70 to $1 in the twenties, but dropped to $2.70 to $1 in 1946–55."

In their recent work, "Capital in Manufacturing and Mining," published by the National Bureau of Economic Research, Daniel Creamer and Israel Borenstein state:

"Up to 1919, an increasing fraction of a dollar of manufacturing capital was used to produce a dollar of output; since 1919, a decreasing fraction of a dollar of capital has been sufficient to produce a dollar of output * * *. Since World War I, capital innovations serve more to increase the efficiency of capital, hence to increase output, than to replace other factor inputs * * *. Trend movements in the capital-output ratio were much the same in mining as in manufacturing."

John Kendrick, in his "Productivity Trends in the United States," declares:

"Despite the substitution of capital for labor over most of the period under review, substantial savings in capital per unit of output were realized in the economy and its major segments between 1899 and 1953. Output per unit of capital input increased at an average annual rate of 1.2 percent in the private domestic economy * * *."

In other words, it now takes less capital to produce a dollar of output than it did in the 1920's. The major pressure on the economy, therefore, is in the area of demand—to supply a rapidly expanding demand for the growing volume of goods and services that can be produced.

Obviously, a growing economy requires an increasing capital stock. But, to sustain an increasing capital stock whose productivity is rising, the economy's demand for goods and services must rise more rapidly than the increase in the stock of capital. The urgent need is not for an increased share of total national production for business investment in new plant and equipment—although that may come about as we approach full employment and the resulting high profits provide the incentive and the means to increase investment. The urgent need is, rather for a rapid and sustained advance in demand—a sufficiently high level of demand to maintain maximum utilization of a growing and increasingly productive capital stock. Above all, we need balance between capacity and demand, which today requires correction of deficiencies in public and private consumption rather than deficiencies in business investment.

PRICE STABILITY

The past year has been marked by almost complete stability of prices. Wholesale prices fell slightly between December 1960 and December 1961, and consumer prices rose by little more than one-half of 1 percent. The prospects for reasonable price stability in the period ahead can be maintained by a continuing rapid increase in the volume of production and by Government measures to place the focus of public attention on the pricing policies of those corporations which dominate key industries and administer price levels.

The Council of Economic Adivsers correctly attempts to place postwar price developments in perspective. Three-fifths of the entire postwar rise in the price level occurred in 1946–48 and in 1950, under the impact of the end of World War II and the outbreak of the Korean war, respectively. In 1955–58 there was another period of rising price levels—a slower increase than the war-induced rapid rises in the level of prices.

The Council's analysis of the 1955–58 period, however, is misleading with its concentration on wage increases and wage costs. This faulty presentation beclouds the report's views of present and future price-level developments.

The major factors behind the rise in prices in 1955–58 were: (1) in manufacturing industries generally, a sharp rise in salary payments and in overhead costs such as depreciation, while production increased at a slow pace—contributing to a rise in production costs per unit; (2) pricing policies in several key industries—such as steel, auto, and electrical machinery—in which prices were raised substantially and held at the higher levels in order to maintain or reduce break-even points, regardless of the demand for their products.

The Chase Manhattan Bank Newsletter for November–December 1961 states:

"* * * nonproduction worker employment (increased) from 2.5 million in 1947 to 4 million now, or from 16 percent to about 25 percent of manufacturing employment * * *.

"When the number of nonproduction workers is translated into overhead costs, it turns out that salaries have risen from one-fourth of factory payrolls in 1947 to more than one-third since 1958. Not only were there more salaried workers, but their earnings were higher: in 1960 average annual salaries were $7,300 compared to wages of $4,700. And, importantly, the absolute differential has been widening since the end of the Korean war, increasing from $1,900 in 1953 to $2,600 in 1960.

"With the proportion of payrolls going into salaries on the rise, total payrolls are more stable over the business cycle. A research scientist developing a new product is less apt to be dropped when factory output falls. Nor do manpower requirements for the sales force, pension plan, etc., decline in proportion to a fall in output. Thus, salary payrolls have risen even during recession years, dampening the impact on overall costs of a decline in wage payments."

As the Chase Manhattan Bank Newsletter points out, most of this impact on unit costs occurred in 1955–58, when there was a sharp rise in the hiring of salaried employees, while there was a slow increase in the volume of production. Salary and other overhead costs per unit rose sharply in 1955–58.

Furthermore, these increases in salary and other overhead costs per unit were compounded by the administered price policies of several key industries, whose substantial price increases gave an additional push to the price level in 1955–58.

Wage costs of factory production and maintenance workers per unit have been declining almost steadily since the first quarter of 1958. By the third quarter of 1961 they were 4½ percent below the same period of 1958 and 5.4 percent lower than the average level for 1953. The rising productivity of factory workers has more than offset their increased wages.

Changes in unit salary costs are dependent to a great extent on the volume of production, since these fixed costs are spread over the number of units produced. Unit salary costs declined as production rose during the upturn from the 1958 recession. They increased again when production declined during the recent recession. Since the early months of last year, unit salary costs have been declining again, with the increase in output. Although unit salary costs are still somewhat higher than they were in 1958, the continuing drop in unit wage costs has pulled down the level of combined wage and salary costs per unit of production.

Employment costs in manufacturing [1]

[1947–49=100]

	Unit wage cost	Unit salary cost	Unit wage and salary cost		Unit wage cost	Unit salary cost	Unit wage and salary cost
1953—1st quarter	112.2	114.1	112.7	1958—1st quarter	114.8	166.4	128.1
2d quarter	112.3	115.8	113.2	2d quarter	113.6	165.4	126.9
3d quarter	110.8	120.3	113.2	3d quarter	110.9	157.1	122 9
4th quarter	112.8	128 6	116.9	4th quarter	110.3	153.3	121.5
1954—1st quarter	112.7	132.9	117.9	1959—1st quarter	111.2	149.6	121.1
2d quarter	110.1	132.9	116.2	2d quarter	110.7	143.0	119.1
3d quarter	107.4	133.2	114.1	3d quarter	110.5	151.4	121.1
4th quarter	108.6	132.3	114.8	4th quarter	110.7	155.4	122.3
1955—1st quarter	106.9	127.7	112.2	1960—1st quarter	110.3	151.4	120.9
2d quarter	107.1	125.9	112.0	2d quarter	110.8	153.8	122.0
3d quarter	105.7	128.0	111.5	3d quarter	109.3	158.1	122.0
4th quarter	108.2	128.5	113.4	4th quarter	109.2	166.1	123.9
1956—1st quarter	108.6	132.6	114.8	1961—1st quarter	108.1	169.2	124.0
2d quarter	109.6	137.1	116.7	2d quarter	108.4	159.9	121.7
3d quarter	110.0	142.9	118.6	3d quarter	105.9	156.0	118.9
4th quarter	111.7	141.6	119.4				
1957—1st quarter	111.0	142.6	119.1				
2d quarter	111.6	145.4	120.4				
3d quarter	111.0	147.8	120.6				
4th quarter	113.8	155.8	124.6				

[1] The cost of wages and salaries in manufacturing industries per unit of output. Payroll fringe benefits such as holiday and vacation pay are included in these costs. Other fringes, such as pension and health-welfare plans for wage and salary employees, stock options and country club dues for salaried executives are not included.

Source: U.S. Department of Commerce, Federal Reserve Board, and U.S. Department of Labor.

The greatest assurance of continued low unit costs will be a continued, rapid advance in the volume of production. The high-volume operations and rapidly rising productivity that accompany a fast pace of economic growth should enable producers to lower unit production costs still further.

If there is a danger of substantial increases in unit production costs in manufacturing, it lies in the possibility that the upturn from the recession may slow down after mid-1962. A slower rise in the volume of production in the second half of 1962 and early 1963 could result in a much slower increase in productivity and a trend of increasing overhead costs per unit of output.

There is so much slack in the economy at present that a continuing advance in production would not create shortages. The Council pointed out in its report:

"Periods of slack and recession in economic activity lead to idle machines as well as idle men. Only once since 1949, at the through of the 1958 recession, was there more excess plant and equipment capacity in U.S. industry than at the start of 1961. While increases in output during the past year have led to fuller use of capital facilities, 1962 begins with considerable room for expanded output from existing plant and equipment and equipment, enough room to permit achievement of the full employment goal. This excess capacity is available to be tapped on demand. It is easier to expand employment at stable prices when tools are already available for new jobholders. Otherwise, capital might act as a bottleneck, obstructing the flow of increased demand for goods into improved employment opportunities for labor."

At the end of 1961, manufacturing industries were operating at about 85 percent of their capacity to produce. The McGraw-Hill Economics Department has indicated that the capacity utilization rate will rise to 87 percent by mid-1962—contrasted with McGraw-Hill's report that manufacturers prefer to operate at 94 percent of capacity.

With operations at about 87 percent of manufacturing capacity in mid-1962, there will be approximately the same proportion of idle productive capacity as in the spring of 1959 or January 1960 when there was considerable slack. Beyond mid-1962 there will be additions to capacity, as industry adds new and improved plants and machines. There wil be more than ample productive capacity to absorb a continuing and rapid advance in production beyond mid-1962. There is no threat of widespread shortages that could apply upward pressures on the price level.

WAGE AND PRICE POLICY

The Council of Economic Advisers' report includes a rather lengthy discussion of wage policy. That discussion, however, neglects to relate wage policy to the necessity to correct the deficiencies in aggregate demand that have caused the economy to fall far short of its output and growth potentials and that have contributed to the repeated recessions of the past 8 years.

Throughout its report the Council repeatedly recognizes the need for an increase in demand. In fact, the first page of the report says:

"Since inadequate demand has in recent years been a major cause of unemployment and excess capacity, expansion of demand has been and remains a principal task of Government policy."

And the third page notes:

"Even at record levels, national production had not yet reached its potential at full employment; and the purchasing power of the American people—the command over goods and services represented by their incomes—was still too low."

For the great majority of American families greater command over goods and services can come only through wage and salary increases. Substantially more than four-fifths of all employed persons are wage and salary workers. The wage policies recommended by the Council, however, would not permit families dependent upon wages and salaries to increase their incomes sufficiently to enjoy the living standards that our productive potential can supply and to take up the slack in the use of that potential.

Yet, unless we were to set out drastically to restructure the economy by greatly increasing the proportion of total demand contributed by Government, it is obvious we will be able to close the gap in aggregate demand only through a significant increase in real wages and salaries. Government must do its part in adding to demand by increasing its direct spending to meet high priority social needs. We believe that it should do more than the Council proposes. But we cannot afford to neglect the need for increasing demand in the private sector of the economy.

Business investment cannot fill the gap

Business investment, no matter how many artificial stimuli are applied to it, cannot be counted upon to fill the gap in aggregate demand. Fundamentally, and in the long run, business investment demand is derived demand. It depends upon the level of demand for the final products of industry. And that demand, with the exception of the small proportion arising in the world market, flows from consumers and Government. Together, these two sources account for 90 percent of total demand, if residential construction is included with consumer demand as it should be. Consumer demand alone (again including residential construction) accounts for 69 percent of the gross national product.

Since wage and salaries amount to 67 percent of all personal income, at least that proportion of consumption demand represents demand by wage and salary earners. In fact, the proportion is larger if account is taken of the fact that most wage and salary earners are in the lower income brackets where the percentages of income absorbed by income taxes and savings are less than the average. Thus, close to 50 percent of total demand is attributable to wage and salary workers.

Since 1956 real wages have trailed our productivity potential

Analysis of data in the Council's report clearly shows that in the years since 1956—years during which excess capacity has become a major problem—real average hourly compensation (including fringe benefits) of wage and salary workers in manufacturing has lagged far behind the productivity potential of our economy. Computations based on table 22 of the Council's report reveal that the increase in real hourly compensation has averaged about 2.3 percent per year while the productivity increase potential of the private economy, as shown elsewhere in this statement, is in excess of 4 percent annually. Real hourly wages, excluding fringe benefits, increased at a rate of only 1.8 percent during the same period. Real hourly compensation lagged behind the actual as well as the potential productivity advance in the private economy as a whole during this period.

Inadequate demand resulting in major part from the lag of real compensation of wage and salary workers behind the productivity potential is, of course, the reason why that potential has not been realized.

Unfortunately, this highly significant point is overlooked—in fact, obscured—in the Council's report. Nowhere in the report is any direct comparison presented of the relationship between real wages and productivity. Indeed, a completely misleading picture is conveyed by table 20 of the report which compares money wages with output per man-hour, and shows the former rising faster than the latter. Obviously, if prices rise, money wages must rise faster than productivity in order to give workers a fair share in the fruits of productivity advance. To expect wage earners to accept inequities in order to avoid inflation—which we seek to avoid primarily because it creates inequities—would be totally illogical and an abdication of Government's responsibility to assure that all groups share fairly in the output of our economy. Failure of money wages to increase faster than productivity in the face of rising prices would inevitably result in an even greater deficiency of demand than we are now suffering.

The Council concedes that "there is nothing immutable in fact or in justice about the distribution of the total product between labor and nonlabor incomes." No arbitrary determination can be made as to that distribution. We should, however, be seeking to achieve a workable relationship among the various forms of income so that demand can be brought into balance with potential supply and full employment thereby attained.

It is clear that the present wage-price-profit relationship does not accomplish that purpose. The recent lag of real wages behind productivity has worsened the imbalance in that relationship. Workable balance in the economy between capacity and demand requires a shift in the present distribution as between labor and nonlabor income—an increase in wages and salaries, at least in the immediate future, greater than our normal potential for increasing productivity. (The rise in the productivity of capital, discussed elsewhere in this statement, may, in fact, make it necessary for real wages and salaries to outpace the rise in output per man-hour indefinitely.)

Fears are expressed, however, that such wage increases would result in inflation. The fearful overlook the fact that productivity is now rising at an extraordinary rate and that there are substantial offsetting factors to the increases in apparent costs that would result from higher wages and salaries. The consequent increases in demand would raise the level of capacity utilization so as to permit more efficient operations. Unit costs would be reduced, thus increasing unit profits; and total profits would rise even faster as a result of increased volume. Those profits would provide the financial means and the higher demand would provide an incentive for increases in investment. That investment would go, obviously, into the most up-to-date and efficient equipment available, thus further stepping up productivity and reducing unit costs.

Inefficient production, price administration, are real inflation threats

The inflationary potential in our economy today arises not out of any danger of a too rapid increase in wages and salaries, but from two entirely different sources. The first is high costs resulting from inefficiently low levels of operation. The second is deliberate price rigging—abuse of administered price power by certain major corporations in positions of price leadership.

Increases in the price level resulting from these two factors operate to raise living costs. They thus compel workers, in order to preserve their families' living standards, to seek money wage increases in excess of productivity gains. And such wage increases, admittedly, may require employers with thin profit margins to raise their prices. This is the process by which inflation tends to spiral.

The spiral has slowed in recent years. The wholesale price index for industrial commodities at the end of 1961 was actually lower than the average for 1959. The consumer price index was up only 3 percent during the same period—only 1.6 percent for commodities, where unions have significant influence on wage rates—5.4 percent in services, where union influence is minimal.

The slowing of the spiral, however, was accomplished through means that are socially undesirable and economically unsound. It was achieved, as comparison of productivity and real wage movement shows, by a relative decline in the living standards of wage and salary earners. And this, as already stated, caused recession, retardation of growth, unemployment, and underutilization of capacity.

These means of arresting the spiral are both unjust and much too high a price to pay for prevention of inflation—particularly when there are other more equitable and less costly means to accomplish that purpose. The first is to expand demand—by wage and salary increases, among other means—so as to achieve the increased volume that reduces unit costs. The second is to face squarely and deal effectively with administered price abuses.

Pricing scrutiny proposed

At its recent convention, the AFL–CIO urged the Government—Federal agencies, congressional committees or both—to place the spotlight of public attention on the pricing policies of dominant corporations in key industries, in an attempt to curtail their price-raising ability.

My own union, the UAW, has proposed in this connection that the "price leaders" in the administered price industries be required to subject to public scrutiny the manner in which they use their power—to furnish advance notice of proposed price increases and to make available in public hearings all the facts claimed to justify such increases. Thus the force of an informed public opinion could be brought to bear as a restraining influence on price-making in industries where the restraints of the competitive market are inoperative. We have stated our willingness to submit to the same goldfish-bowl procedure where the corporation proposing to raise its prices claims that our economic demands create the necessity for the increase.

This mechanism would provide practical implementation of the suggestion made in the Council's report that:

"An informed public, aware of the significance of major wage bargains and price decisions, and equipped to judge for itself their compatibility with the national interest, can help to create an atmosphere in which the parties to such decisions will exercise their powers responsibly."

Had such a mechanism been in existence during the 1950's, it might have saved the Council from the gross blunder in analysis. In relation postwar price history, the Council's report says:

"More than three-fourths of the 1955–58 rise in the index of wholesale industrial prices was directly attributable to price increases in metals and metal products and machinery and motive products (including motor vehicles). Substantial employment cost increases were negotiated in the automobile settlement of 1955 and the steel settlement of 1956. Both were 3-year agreements, with the result that large wage commitments made in a boom environment became effective as the economy was slowing down. Price and wage behavior in this sector initiated impulses which spread to other parts of the economy, both via increases in materials and equipment cost and via imitative influences in wage settlements."

The facts are not quite as obvious as they would be if public hearings had been held on auto and steel price increases during that period; but enough evidence is available to provide definitive support for the conclusion that the references to wages in the quoted statement are wholly irrelevant.

What caused 1955–58 price rises?

In the case of autos one need look no further than the profits of General Motors, the price leader in the industry, before and since the 1955 wage settlement. Those profits show beyond all doubt that GM had no need to raise its prices. And, had GM not done so, none of its competitors would have raised its prices.

In the case of steel, the evidence may be found, among other places, in a study prepared for this Joint Economic Committee of Congress, which showed that, starting in 1955, United States Steel, the price leader in that industry, revised its prices to obtain a 12- to 13-percent rate of return after taxes when operating at 80 percent of capacity, instead of the 8 percent with which it had previously been satisfied.

The imitative influences of the 1955 and 1956 wage settlements in autos and steel, respectively, were much less influential on settlements in other industries than the simple fact that the unnecessary and unjustifiable auto and steel price increases had set off a round of inflation against which workers in those other industries were compelled to protect their families.

Why auto companies held prices down in 1961

Moreover, in 1961 negotiations, the union with which I am associated, the UAW, won economic gains the value of which, although difficult to calculate precisely, is comparable to the value of the gains won in 1955. Yet, the auto industry did not find it necessary to raise prices. In fact, price reductions were announced for many makes of cars.

The New York Times reported on September 21, 1961:

"The prices reflect the industry's agreement with the Government that the new pact with the United Automobile Workers is 'noninflationary.'

"Last week Secretary of Labor Arthur J. Goldberg conveyed that opinion to the automobile manufacturers and expressed hope that there would not be a price increase."

If the auto companies were able to hold the price line in 1961, as they did, they were equally capable of holding it in 1955. The fact that 1955 was a boom year while 1961 was a year of recession does not explain the difference in auto corporation price behavior as between the 2 years. The record shows that the industry has raised prices in the past during recessions as well as during periods of high economic activity. Moreover, we were months past the trough of recession when negotiations were concluded and prices on the new models announced.

The industry's price restraint in 1961 strengthens our conviction that public opinion can influence the behavior of the price administrators. We had challenged General Motors in the course of negotiations to supply factual support for its claims that our demands were inflationary. We backed up our challenge with an unfair labor practice charge filed with the National Labor Relations Board when GM refused to make the pertinent facts available. That refusal, we believe, helped to persuade a large part of the public, as it should have, that GM's accusations were unfounded. In addition, the strong position taken by the administration against auto price increases helped to mobilize public opinion and thereby to restrain the industry.

That the economic gains obtained by the UAW in 1961 were in truth not inflationary is attested to by the fact that General Motors profits during the last 3 months of 1961, when those gains were already largely in effect, were the highest of any quarter in its entire history even though it had not raised prices. I sincerely hope that this experience will cause the members of the Council, among others, to reconsider their judgments as to the role of wage increases in postwar inflation and to give serious thought to means to curb administered price abuses.

Had the auto industry raised its prices after 1961 negotiations, it quite likely would have set off a new round of inflation for which workers would have been widely blamed—both auto workers and workers in other industries who would have been compelled to seek wage increases large enough to compensate for higher living costs, as well as to give them their share in the fruits of productivity advance.

In any case, to compare the movement of money wages with productivity is to look at the symptoms rather than the causes of inflation, and, in the process, to lose sight of the fact that the deficiency in aggregate demand is in major part a result of the lag of real wages behind productivity. The remedy for the latter is to encourage rather than to discourage wage increases—to seek as a policy objective, at least for the immediate future, increases in real wages greater than increases in productivity.

Pursuit of such a policy today is inhibited by fears of inflation arising out of an erroneous diagnosis of the forces making for inflation. Correct diagnosis followed up by effective machinery for restraining administered price abuses would remove the basis for fear and set the stage for wage policies to promote full emploment and healthy economic growth. Full employment and growth, in turn, will contribute to the curbing of inflation by reducing unit costs.

TAX CREDIT WINDFALL

The administration's proposal for an 8 percent credit against corporate income taxes for gross investment in depreciable machinery and equipment would cost the Federal Government $1.5 billion in lost revenues in 1962, according to the Council of Economic Advisers. Most of this revenue would be lost even if the credit brought about absolutely no increase in investment over the depressed 1961 level.

It is hard to see how the gains in increased economic activity from such a tax credit could conceivably be commensurate with the amount of revenue lost, or with the gains that would be obtained either from other equivalent revenue losses resulting from tax relief for low-income families or from equivalent public expenditure increases on education, health facilities, resource conservation and development, or other similar projects of high social priority.

The effect of the tax credit, insofar as businessmen are concerned, is to reduce the cost of new equipment by 8 percent. This could induce added investment only under two conditions, both of severely limited significance. The first is where the difference of 8 percent in the cost of new equipment would make sufficiently profitable an investment that would otherwise yield no profits or unattractively low profits. The second is where the prospective purchaser of equipment can finance 92 percent or more of the cost but not quite 100 percent.

No evidence available to us, indicates that these two types of situation are so widespread as to suggest that the proposed tax credit could bring forth additional investment in a volume that would even begin to justify a revenue loss of the magnitude of $1.5 billion per year. In effect, the major part of the $1.5 billion cost of the credit would be a windfall to corporations which they would receive for equipment expenditures equal to those they would have made even in the absence of the tax credit.

What would GM do with more cash?

This windfall would add to the cash flow not only of small and financially weak corporations but also of the giants which are already having great difficulties in finding profitable investment outlets for funds they presently have on hand.

General Motors, for example, set aside depreciation reserves of $1,637 million during the years 1957 through 1960, while it invested only $1,589 million in plant and equipment combined. During those same years it retained profits, after payments of dividends, in the amount of $1,017 million, out of which it added $965 million to its cash and security holdings, so that the total of such holdings at the end of 1960 was $1,637 million (coincidentally the same as its depreciation reserves for the 1957–60 period).

Commenting on this situation, Forbes magazine in its issue of June 15, 1961, carried an article that began as follows:

"THE MIDAS TOUCH

"That rather describes what General Motors has these days. GM is loaded with cash, but what good is it all?

"Does anybody have some good ideas on how to put about $1 billion to work profitably? If so, Frederic G. Donner, chairman of General Motors Corp., would be glad to hear from him. Currently, General Motors' treasury is all but overflowing with cash and Government bonds to the tune of $1.6 billion. Of this a probable $1 billion is *surplus* cash by any ordinary standards.

"Donner, for all the acumen and experience gathered in a lifetime as a financial expert, frankly, does not seem to know what to do with the money. The trouble—if trouble it can be called—is that General Motors is piling up cash at a faster pace than it can be put to work."

Had the 8-percent tax credit been in effect during the years 1957 through 1960, Mr. Donner would have been further embarrassed by additional cash to the tune of about $75 million, because the corporation's spending for equipment for its U.S. plants during those years, as nearly as we can estimate it, amounted approximately to $950 million, of which 8 percent would have been offset against its tax liabilities. Yet it is doubtful, to say the least, that the tax credit would have stimulated General Motors to increase its equipmen spending by any appreciable amount, if at all.

The Ford Motor Co. presents a similar picture. During the period 1957 through 1960, the Ford Motor Co.'s depreciation allowance amounted to $700 million. During the same 4 years it invested only $621 million in new plant and equipment and, after paying generous dividends, it retained undistributed profits amounting to $731 million.

Ford's cash is also piling up

The current issue of Fortune magazine comments at considerable length on Ford's financial position. After noting that Ford poured more than $4 billion into capital facilities during the postwar period—all of which, except $250 million borrowed in 1956, has come from profits, Fortune continues:

"The profits continue to roll in, but the plant, substantially speaking, is all built. Of Ford's total plant today, 90 percent is new since World War II, and 60 percent is 6 years old or less (which is one of the big reasons, of course, why profits are so good). *Clearly, Ford has reached a point where it is not presently necessary or desirable to pour huge sums into plant.* The company's last big spending sprees for this purpose were in 1956, when the program hit a peak of $487 million, and in 1957, when $329 million was spent. In 1959, by contrast, capital expenditures for expansion, modernization, and replacement were only $75 million; in 1960 they were $128 million, and last year's estimated capital spending came to no more than $130 million.

"Meanwhile, Ford's cash flow (retained profits plus depreciation), despite some increases in the dividend rate, was building up powerfully. Back in 1956, the cash flow was only $252 million, considerably less than what the company laid out in capital expenditures. But by 1959 the inevitable results of Ford's big building program began to show up in the balance sheet. In the first place, there was a very substantial depreciation figure—almost $173 million. In the second place, profits, reflecting the efficiency of the new facilities, rose sharply. Consequently, Ford's cash flow in 1959 was a whopping $471 million (more than $75 million higher than in the peak car year of 1955). In 1960, Ford's cash flow was $427 million; in 1961, probably not less than $400 million.

"Looking at these figures one might explain all these new ventures of Ford simply by saying that the company is making more money out of the U.S. automobile business than it can profitably reemploy in the U.S. automobile business. This is only partly true. It certainly should not be taken to mean that Ford, not quite knowing what to do with all its money, is desperately shopping around for 'outlets.' As a public company for more than 5 years now, Ford respects its obligation to earn the best possible return for its stockholders. Unless a genuine investment opportunity presents itself, it would be more appropriate for Ford to pay its surplus earnings out directly to stockholders, and let them invest it as they see fit." [Emphasis added.]

The case of the Ford Motor Co. illustrates two serious dangers that would be aggravated by that part of the tax credit windfall—and it would undoubtedly be a substantial part—which would flow to corporations already faced with a cash flow that is greatly in excess of their needs. The first danger is that others will follow Ford's lead in worsening the U.S. balance of payments by finding investment outlets abroad because inadequate economic growth forecloses the possibilities of profitable investment at home.

In the space of 2 years, Ford Motor Co. invested $520 million of its excess cash in England and Canada.

Ford moves into new fields

The second danger is that excessive cash flow may impel giant corporations, whose economic, political, and social power is already dangerously great, to enlarge their power further by moving into new fields. Within the past year, the Ford Motor Co. has used $28 million of its excess funds to purchase the battery and spark plug facilities of the Electric Autolite Co. Ford's recent acquisition of the Philco Corp. was accomplished through a $100 million exchange of stock, and thus did not involve direct use of Ford's liquid resources. However, Ford's excessive cash flow was undoubtedly a factor in that acquisition, since converting Philco from a money-losing to a profitable operation will probably require substantial additional investment. Thus, in acquiring Philco, Ford acquired an outlet for some of its cash. The Autolite and Philco acquisitions are in addition to Ford's entrance into the missiles industry through its purchase of a research corporation that has now been developed into the company's Aeronutronic Division.

While expanding by the acquisition route in the Autolite, Philco, and Aeronutronic cases, Ford also used its huge cash resources to build facilities to produce parts and components formerly obtained from outside suppliers. The Murray Body Corp., for example, which once supplied a large proportion of the bodies for Ford automobiles, is now no longer in the automobile business mainly because Ford now supplies its entire body needs from its own facilities.

Thus it can be expected that additions to Ford's cash flow which would result from enactment of the 8-percent tax credit would be used as its present cash resources are used—to worsen the U.S. balance of payments, to extend its operations into new fields where its financial power will place existing competitors at a serious disadvantage, and to wipe out smaller corporations that presently supply it with parts and components.

No addition to total capacity

Had the tax credit been in effect during the years 1957 through 1960, for example, it would have added approximately $35 million to Ford's cash flow (as a result of an estimated $450 million of equipment expenditures by the company for its U.S. plants) which would undoubtedly have been used—if it were used at all—for the same purposes as its excessive cash is presently used. It is doubtful, however, whether in return for the aggravation of the evil social and economic consequences of Ford's excessive cash, there would have been any significant addition to the company's expenditures for machinery and equipment.

As in the case of the Autolite acquisitions, Ford's windfall from the tax credit, had it been available, would probably have been used, not to add to or modernize the stock of wealth-producing machinery, but, rather, to purchase already existing productive facilities.

Any temptation on the part of Ford, General Motors, or Chrysler to use the windfall for the purpose of expanding their productive capacity for motor vehicles would be out of the question on the face of it. The auto industry today has a productive capacity probably in excess of 10 million cars and trucks. Yet in 1962, which is being hailed as a "good year," projected output is only about 7.5 million units. It would be nonsensical for the corporations to widen this gap still further, even if the Government did pay 8 percent of the cost.

To the extent that the tax credit, if enacted, were to succeed in its objective of bringing about significant modernization of existing productive equipment, it would only further unbalance the relationship between capacity and demand—between investment and public and private consumption—unless simultaneous steps were taken to assure the creation of additional demand to absorb the output of the new equipment and to provide new employment opportunities for the workers displaced by it.

Modernization, by definition, means the replacement of old equipment with new machinery capable of turning out the same or a greater volume of output with fewer workers. In an economy which already has far more idle workers than it can supply with jobs, modernization of equipment in the absence of increased demand spells human tragedy rather than economic progress. Moreover, without adequate demand, the purpose of modernization—reduction of unit costs—is more likely to be frustrated than to be achieved because expensive new equipment adds to overhead costs, which, in the absence of sufficient volume of output, results in increased unit costs.

In its long-term effects the proposed tax credit, if it were effective as an incentive, could well have the effect of further bunching investment at the peak of the business cycle. Since fluctuations in the volume of investment accentuate the swings of the cycle itself, anything that intensifies the rate at which investment outpaces consumption on the upswing must inevitably deepen the troughs during which equipment expenditures wait upon a rise in final demand to take up the slack in idle capacity. The $1.5 billion or more which it is proposed to spend, in the form of lost Federal revenues, upon the proposed tax credit will therefore buy us additional troubles rather than contribute to the solution of our present troubles.

Tax reductions for low-income families wiser

The same revenues would be much more wisely disposed of in the interests of stability and growth if devoted either to tax reductions for low-income families who would use it to add to total demand and to improve their depressed living standards, or to improve the quality of American life by meeting our deficits in public services and public facilities. One and a half billion dollars a year, for example, would buy us 37,000 new classrooms, or 70,000 new hospital beds, or 125,000 dwelling units in public housing. One and a half billion dollars of additional revenue spent for one of these purposes, or any combination of them, would contribute far more to aggregate demand than would any increase in equipment expenditures that could reasonably be expected to be induced by the proposed tax credit. For only a fraction of the $1.5 billion would be related to investment that would not otherwise have been made; and the multiplier effect would have to be large indeed to stimulate an additional $1.5 billion in demand.

The fact that the revenue loss resulting from the tax credit is proposed to be offset by the closing of tax loopholes is of little relevance. Tax loopholes should be closed whether or not the investment credit is enacted. The revenues raised from the closing of loopholes should be devoted to constructive economic and social purposes rather than to creation of great new windfalls for corporations which, in all too many cases, presently cannot find suitable means to dispose of cash already on hand.

No insufficiency of capital

The proposed investment credit seems all the more pointless in view of the fact that no evidence has been cited to show that there is either an insufficiency of capital for investment or that the volume of investment cannot be more effectively increased, with simultaneous stimulation of modernization by measures that would increase aggregate demand.

The availability of capital is evidenced by the fact that industry has been financing an increasing proportion of its investment out of depreciation allowances and retained profits. The following table shows the rise in the proportion of internal financing over the last three business cycles:

[Billions of dollars]

Period	(1) Plant and equipment outlays	(2) Funds available from internal sources [1]	(3) Col. (2) as percent of col. (1)
1950–54	$107.2	$97.1	90.6
1955–58	113.2	108.4	95.8
1959–61	88.9	93.0	104.6

[1] Retained profits and depletion allowances, and depreciation and amortization allowances.

In the 1959–61 period, funds available from internal sources actually exceeded plant and equipment outlays, indicating that the General Motors and Ford examples, cited above, are typical of corporations generally. Slackness in the economy and its failure to grow as it should have resulted in accumulation of cash in corporate coffers for which it is difficult to find investment outlets.

Some small businesses, nevertheless, are pinched for capital. But there are other more effective means, including Government or Government-guaranteed low interest loans, to meet that problem than the proposed investment credit. More rapid growth of the economy which would increase the profits of small as well as large business would also increase the ability of the former to finance its investments.

Business investment flows from demand

Our postwar experience shows that business investment in new equipment fluctuates with the level of demand. As shown in the following table, and as should be expected, such investment has accounted for a larger proportion of the gross national product in periods of high and rising aggregate demand than in periods of slack.

Calendar quarter	Cyclical—	Producers' durable equipment expenditures as percent of gross national product
4th, 1948	Peak	7.8
4th, 1949	Trough	6.3
3d, 1953	Peak	6.1
3d, 1954	Trough	5.7
3d, 1957	Peak	6.1
2d, 1958	Trough	4.8
2d, 1960	Peak	5.3
1st, 1961	Trough	4.6

The fact that the rate of spending on equipment has tended in recent years to account for decreasing proportions of gross national product in peak and trough periods alike serves to emphasize the point. Equipment spending was low in relation to gross national product because aggregate demand was low in relation to our already existing productive potential. There was little point to adding to the supply of idle and underutilized equipment. The high figures shown in the above table for the immediate postwar period, 1948 and 1949, reflect not only the need for investment to make up for obsolescence accumulated during the war but also a relatively high level of demand in relation to capacity.

One of our difficulties has been that, during periods of relative prosperity, expansion of capacity has tended to outrun expansion in demand. This is why the high levels of equipment purchases at the 1953 and 1957 peaks proved to be unsustainable. Experience clearly demonstrates that we can call forth an increased flow of investment by raising demand to the point where it begins to press on the limits of existing capacity. Thereafter expansion of demand and capacity should be parellel. By taking this approach to the stimulation of investment, we would avoid the recurrent imbalances between capacity and demand which have led to repeated recessions and by so doing have depressed capital expenditures over the business cycle as a whole below the level it would have attained had demand grown in balance with capacity expansion.

High demand also spurs modernization

The nature of the statistics on the age of existing equipment has led to exaggeration of the extent of obsolescence. The statistics are in terms of units of machinery and give the same weight to a single-spindle drill press as they do to a transfer machine which integrates into a single unit devices capable of performing a whole complex of operations. Nevertheless, there is need to raise the efficiency of equipment in important sectors of the economy. This, however, can be accomplished much more effectively by increasing public and private demand than by such artificial stimuli as the proposed investment credit.

The high levels of demand that make for high rates of investment contribute to modernization as well as expansion. Each new and advanced unit of equipment added to the existing stock, by itself, raises the average efficiency of the total supply of capital. Although stagnation and repeated recessions have undoubtedly depressed the level of business investment in recent years, high unit costs resulting from inadequate demand have tended to concentrate investment on modernization. Expansion investment became largely pointless because existing capacity was more than adequate to meet market demand. The following McGraw-Hill figures show the growing emphasis on modernization in recent years:

Percent of total plant and equipment expenditures devoted to modernization

Year:	
1957	48
1958	56
1959	65
1960	69
1961 (planned)[1]	70

[1] The actual percentage devoted to modernization in 1961 is not yet available.

The high proportion of expenditures for modernization in the presence of serious economic slack has been a significant factor in raising unemployment to ever higher plateaus.

But it has paid to modernize only as much productive capacity as could be utilized steadily to meet current demand. Obsolescent and semiobsolescent facilities have been maintained primarly on a standby basis. They are called into use only to meet fluctuations in demand. They have not been modernized primarily because the size of the market was insufficient to justify their modernization. Their equipment would be replaced quickly if national economic policies provided assurance that there would be market outlets on a continuing basis for their output which is now required only to meet short-lived spurts in demand.

In addition, high employment and tight labor markets put pressure on employers to substitute equipment for labor wherever they can. It is significant that low levels of unemployment, to the point of severe labor shortage, have been the setting for the high growth rates and high rates of investment in the Western European economies.

The artificial stimulus of the proposed investment credit is a weak and inadequate substitute for customers, public and private.

The Council of Economic Advisers apparently recognizes the validity of these fundamental economic truths—although its policy proposals suggest otherwise—for at one point its report says:

"The single most important stimulant to investment is the maintenance of full utilization of capacity. The historical record shows that when output falls below its potential the rate of growth of the capital stock declines. Expected profit from investment is strongly influenced by the expected demand for the output that the new capital will help produce, even if the investment is meant lergely for cost reduction rather than capacity expansion. Estimates of future demand are colored by the experience of the present and the recent past. During periods of economic slack, estimates of future demand are relatively pessimistic, and many projects are foregone which would appear profitable under conditions of high demand."

Proposal would add to concentration of wealth

There is still another reason for doubts as to the wisdom of the proposed investment incentive—that is the fact that it would tend to intensify the concentration of wealth.

The high percentage of the total personal wealth of the United States held by an infinitesimal proportion of the population is already so great as to raise questions concerning the compatibilty of such concentration with democracy. As stated by Prof. Robert Lampman in a recent National Bureau of Economic Research study:

"Presumably, since wealth is a good thing to have, it would be good for all families to have some. Also, it would seem that the wider the distribution of wealth, the broader the political base for capitalism. There is doubtless a maximum degree of concentration of wealth which is tolerable in a democracy and compatible with an ideology of equality of economic opportunity."

Lampman's study, as updated by him for a recent article in Business Week, shows that the concentration of wealth, which was intensified during the twenties, decreased materially during the period of the New Deal but has since sharply reversed course. Lampman's figures on the percentage of the Nation's personal wealth held by the richest 1 percent of U.S. adults in selected years reveal the extent of the reversal.

Share of personal wealth held by richest 1 percent of adults

Year:	Percent	Year—Continued	Percent
1922	31.6	1949	20.8
1929	36.3	1953	24.2
1933	28.3	1956	26.0
1939	30.6	1961	28.0
1945	23.3		

The trend toward an increasing concentration of wealth appears to arise largely out of the concentration of stock holdings and the sharp rise in stock prices. Lampman's figures show that the wealthiest 1 percent of U.S. adults increased their share of total personal stock holdings from 61.7 percent in 1945 to 76.0 percent in 1953. His figures on this point do not go beyond 1953. However, even if there should have been some reversal in more recent years of the 1945–53 trend toward increasing concentration of stock ownership, the effect of such a reversal on the share of total personal wealth held by the top 1 percent must have been far more than offset by the sharp increase in stock prices which rose at a rate that enormously exceeded the rise in the general price level.

Even more startling are data presented by Lampman which show that as of 1953 the top wealth holders with assets of $500,000 or more, who comprised approximately seventy-five one-thousandths of 1 percent of the total adult population, held substantially greater wealth than the wealth in all forms held by the 50 percent of the total population with holdings of under $3,500. Those with holdings of $500,000 or more held gross assets valued at approximately $110 billion, while 51.7 million adults with estates of $3,500 or less owned an aggregate of $93 billion. Among the wealthiest there were 27,000 with holdings of $1 million or more whose aggregate wealth amounted to close to $75 billion. Of these 27,000, less than 3 percent, held more than $10 million each and a total of approximately $15 billion.

Along with the increasing concentration of accumulated wealth in recent years there has been, not unnaturally, a shift in the income distribution trend. Between 1935–36 and 1953, the proportion of total personal incomes received by the 5 percent of families which received the most declined from 26.5 percent of the total to 19.9 percent, while the share going to less affluent families increased accordingly. Between 1953 and 1958, however, the proportion of income received by the top 5 percent rose from 19.9 to 20.2 percent, and the share of the remaining 95 percent declined. While this reversal of the trend may seem small, it is nevertheless significant.

These data not only reveal one facet of economic imbalance in the United States but also raise serious questions about the reality of equality of opportunity.

Since the purpose of the investment credit is to increase the profitability of investment in machinery and equipment, and since the overwhelmingly proportion of all machinery and equipment is owned by corporations, the effect of the credit must inevitably be to increase further the wealth of the very small proportion of the population that holds the great bulk of all corporate stock. Thus, the investment credit, if enacted, would contribute toward the continued reversal of the process of deconcentration of wealth that took place under the New Deal.

Other measures could help stimulate investment

While we have grave doubts as to the possibility of increasing the volume of investment over the long run to any appreciable extent through such devices as the proposed investment credit, there are other means, directed in part toward the same purposes—and toward other desirable objectives as well—which we believe deserve consideration.

Specifically, we would suggest examination of the feasibility of imposing a tax on uninvested and undistributed corporate profits. A tax on undistributed profits was in effect during the New Deal, from 1936 to 1939. This suggestion differs from the statute then in effect in that the tax would not apply to profits that were reinvested in plant and equipment within a reasonable period of time after they were realized. In addition, it would make allowance for additions out of profits to working capital to the extent that such additions were reasonably related to the needs of a growing business for larger inventories and higher payrolls.

Such a tax would have an effect similar to the proposed investment credit in reducing the real cost of new equipment. At the same time, it would serve to return to the stream of active demand excessive liquid reserves, exemplified by the General Motors and Ford situations described above.

These reserves are, for all practical purposes, sterile insofar as their contribution to the level of demand in the economy is concerned. They are withheld from the stream of purchasing power. A tax that would impel corporations holding such reserves either to invest them in new plant and equipment or to distribute them in dividends to their stockholders, would assure that at least a high proportion of them would be translated into active demand. Small stockholders, in the "widows and orphans" category to which corporations like to refer, would tend to spend the increased dividends that they would receive as the result of such a tax. Larger stockholders would undoubtedly tend to save part of their increased dividends, but the likelihood of such savings sooner or later finding investment outlets would be greater than if the increased dividend amounts had remained in the treasuries of the corporations involved. Such savings would become accessible, for example, to small businesses with limited financial resources but favorable profit prospects. Additional Government revenues derived from the increased dividend payments induced by the tax could also be used to increase demand—by devoting them either to more Government spending for high priority purposes or to reduce taxes on low- and middle-income families.

DEMAND: THE MAJOR NEED

The major issue in terms of both recovery from the recession of 1960–61 and sustained, rapid economic growth in this decade is high and sustained demand. A high and rising level of demand for goods and services will create the jobs that are needed to reduce unemployment toward minimum levels. It will also create the high-volume operations, profits, and business optimism for sustained and increasing business investment in new plants, machines, and equipment, without booms and busts. What is needed is a balanced relationship between the economy's rapidly growing ability to produce and the demand for goods and services.

The need for a much higher level of demand now—and for rapidly rising demand in the years ahead—to match the economy's vast and growing capacity to produce a growing abundance of goods and services is both a challenge and an opportunity. It is a problem now only because we have failed to use our wisdom and know-how in developing the means to fully use this potential abundance for socially desirable goals. It will remain a problem if we continue to view our potential economic abundance as an unbearable weight rather than a great national opportunity.

Our unmet needs

On the one hand there is the vast potential to produce a growing abundance—with the waste of idle men, plants, and machines which is the price of failure to fully utilize this potential. On the other hand are the great unmet needs of the American people.

Education

There is the need, for example, to provide an adequate education system—the very foundation of a free and technologically advanced society.

By the fall term of 1961 there were 49.3 million children in the Nation's public and private schools—1.4 million more than in 1960, and 10 million more than were enrolled in the schools only 5 years previously. Each year the increase continues.

During the school year 1959–60 there were 1,800,000 more pupils enrolled in public schools than could be handled by the normal capacity of existing classrooms. An additional 142,000 classrooms were needed—66,000 to meet excess enrollment and 76,000 to replace obsolete and unsafe facilities. Less than half of this number of additional classrooms had been scheduled for completion by the opening of the fall 1961 semester. But the need for additional classrooms was compounded by the further addition of another 1,400,000 pupils. Classrooms are not being built as fast as old ones become obsolete and as fast as the school population grows.

Teachers' salaries, even with the improvements of recent years, are far from high enough to attract promising young people into the profession. The present shortage of teachers has been estimated to be as high as 250,000. A survey of the U.S. Office of Education indicates that each year more than 10 percent of the public school teachers leave the teaching profession altogether. In large part the shortage has been met by the use of teachers with substandard certificates.

Too few classrooms, too few teachers, and too many students for the facilities to handle—this is the tragedy of public education today even more than in the past several years. This situation has developed despite the best efforts of the States and local communities. The need for Federal aid for classroom construction and teachers' salaries is great. Our vast productive potential can begin to meet this need now—and to create gainful employment opportunities for the unemployed—through a program of Federal aid for school construction and the salaries of teachers.

There are likewise great shortages and needs at the college level. A record enrollment of 4,300,000 was reported by institutions of higher education for the fall of 1961. By 1971 enrollment is expected to increase to more than 6 million. These ranks of college students would be swollen even more were it not that many of the best qualified high school graduates are not financially able to go to college. Studies show that 100,000 of the top students of each year's high school graduating classes do not go on to college because of financial problems.

One way of expanding higher education facilities and bringing the cost of college education within the range of wage earners' families is to encourage the development of junior colleges and community colleges. To meet these needs, Federal grants-in-aid to the States and local communities are required, as well as an expanded program of adequate scholarships.

Housing and urban redevelopment

Another example of great unmet needs is in housing and urban redevelopment. Our postwar efforts in this direction have been meager in terms of the needs and these needs have grown as the population has increased and as our cities and suburbs have expanded.

The 1960 Census of Housing indicates that there were 15.7 million dwelling units that were dilapidated, deteriorating, or lacking in adequate plumbing. Of this large number, some 5 million units, it is estimated, can be rehabilitated. The others require replacement.

Furthermore, it is estimated that by 1975 an additional 5.7 million units will become substandard and an additional 5 million units will be demolished by disaster and other causes. There is the need, therefore, to replace over 21 million dwelling units by 1975.

In the meantime, the number of families is expected to increase by 14 million between 1960 and 1975—adding further to the Nation's housing needs. An adequate housing program would also provide almost an additional million dwelling units for those families that are living in crowded, doubled-up conditions. The total housing needs are approximately 36 million additional dwelling units between 1960 and 1975.

In 1960 and 1961, however, the total number of private and public housing starts was at a yearly average of only 1,325,000—not much more than half the necessary number. Between 1962 and 1975, we will have to build an average of about 2½ million dwelling units a year to provide adequate and decent housing for the American people. We are falling far short of this goal, while we waste our vast national productive potential through unemployment and idle plants and equipment.

Much of this housing need can be met by private enterprise, with adequate Federal guarantees and low-interest mortgages. However, a part of it—low-cost housing for low-income families—can be fulfilled only by direct Government programs. But the Nation's housing needs cannot be met by hesitant and piecemeal measures. A significant step forward toward the fulfillment of this social need requires a comprehensive Federal program to stimulate both private and public provision of housing and urban redevelopment—including community facilities, mass transit, and highways.

Hospitals

The Nation's record of attempting to meet the shortage of hospital facilities in the postwar period under the Hill-Burton Act program has been more successful than most of our public-service efforts. But even here, there are continuing shortages as a result of a growing population and the increase in life expectancy. According to the U.S. Public Health Service, there was the need, in early 1961, for 843,000 additional hospital beds and for almost 266,000 additional beds in nursing homes. Furthermore, there was the reported need for 2,300 additional public health, diagnostic, and treatment centers.

Resource conservation and development

There are vast needs and vast opportunities in resource conservation and development. TVA, of which some Americans seem to be ashamed, is a symbol to the rest of the world how a democratic government can wisely use public funds to transform a whole region, improve the lives of its people, raise their productivity and purchasing power, and enrich the whole Nation.

There are equal or greater opportunities in protection and renewal of our public lands and forests, in eliminating stream pollution, in developing economical means for desalting ocean and brackish water, and developing the peaceful uses of the atom. Vigorous leadership in the two last named areas, in particular, would go far to restore American prestige now somewhat tarnished because of dramatic Soviet feats in space that we have not yet matched.

These are only four areas of the unmet needs of a growing and urban population in the America of 1962. Shall we sit by and wait for some supposedly more proper time in the future or should we get our idle men, plants, and machines to work now by beginning planned efforts to meet these needs within the next one or two decades. I believe that the time to begin is now—and in beginning to meet these needs, we will be enriching our society and providing maximum production, employment, and purchasing power.

Aid to underdeveloped countries

The enormous unmet needs of the developing countries emphasize the tragic nature of the waste represented by our idle workers and idle capacity. America's productive potential is freedom's greatest material asset. It is the means whereby we can bring final defeat to man's ancient enemies—poverty, ignorance, and disease—in the vast areas of the earth where they now hold sway. It is the means whereby we can assure the fulfillment in freedom of the aspirations of the hundreds of millions of people in the developing countries. If we make use of our productive power to help them, we help ourselves at the same time. We provide jobs for our unemployed. We make our own freedom more secure. We promote the cause of peace. We cannot afford to do less than our best in the pursuit of those goals. We cannot afford to waste the productive potential that can help us attain them.

Objections based on restrictive thinking

The usual objection to such public-investment efforts is their cost in Federal expenditures. The restrictive thinking behind such objection, however, is fallacious for a number of reasons.

Certainly to begin such long-term planned efforts would cost money and require an increase in Federal expenditures. But the increase in employment and in business activities would generate rising, personal incomes, profits, and tax revenues. Maximum use of our productive potential would produce a sharp rise in Federal receipts.

Instead of establishing our policies on the basis of expansion, however, we have permitted the waste of persistent high unemployment and idle plants and machines. As a result, Federal cash receipts dropped $2.8 billion between 1957 and 1958, because of the recession, when they should have risen substantially. Similarly, Federal cash receipts declined $1.1 billion between 1960 and 1961. At maximum employment and production, Federal cash receipts last year would have been $15 billion or more above the actual level.

If we had been operating at maximum production and employment in 1961, we could have begun to meet our unmet social needs and the Government could have operated at a cash surplus, instead of a deficit.

To move from present high levels of unemployment and underutilized plants and machines, to maximum production and employment, will require programs that would produce a temporary deficit. Such a temporary deficit in the Government's financial operations would be a small price to pay for restoring the economy to balanced and rapid economic growth.

Full use of our growing production potential, in itself, is no panacea or cure-all. But it is the basic prerequisite for solving our economic problems. It would, in itself, create high and rising employment, personal incomes, profits, business investment and Federal revenues. It would restore foreign, as well as home-front confidence in the American economy and contribute towards a solution of the balance of payments problem. It would also provide a healthy environment of growing job and business opportunities, in which adequate adjustments can be made more easily to the dislocations of automation and a more liberal trade policy.

TRADE AND THE BALANCE OF PAYMENTS

The rapid progress of the six member nations of the European Common Market toward integration of their economies, the strong possibility that other European nations may join the Common Market, and the rapid economic growth of most Western European countries present new challenges that must be met and new opportunities that must be grasped.

The countries of Western Europe—and Japan, as well—are now back in world markets, vigorously competing for trade. The United States is no longer the uncontested supplier of goods in world markets. And the Common Market is quickly succeeding in the economic integration of its member nations. Continued large-scale trade with the Common Market nations in the future will require that America develop a new relationship with the Common Market.

The President has pointed the way in his trade message to Congress. We must move toward integration of the economy of the entire free world so that its overwhelming productive power can be fully mobilized in the common interests of all free people. We must gain access to the huge and rapidly growing market of Western Europe to the maximum extent possible on a basis of equality with producers located within that market. We must avoid the danger that the competitive disadvantage of tariffs against American goods, while European goods move freely from country to country, will cause the export of American capital and American jobs to avoid the necessity to hurdle the Common Market tariff wall.

In meeting this challenge, the U.S. economy is severely handicapped by persistent high levels of unemployment and idle productive capacity. Underutilization of our productive potential leads to high unit costs which make it difficult for us either to compete with countries enjoying the efficiencies of full production, or to integrate our trade with theirs.

Our competitive difficulties should not be exaggerated. With a trade surplus of $4.7 billion in 1960 and an excess of approximately $5.5 billion of merchandise exports over imports in 1961, it is clear that we have not and are not "pricing ourselves out of world markets," as is sometimes claimed. But if we are to maintain such a trade surplus and improve it, we must regain the efficiency in production that only high-volume production can make possible. At the same time it is important for management to seek every means of competing more effectively in foreign trade in such respects as product design, quality of goods and making available information on their products.

In conjunction with any program of lowering trade barriers, of course, we must provide adequate assistance through a trade adjustment program to companies, to communities, and to individual workers who may be adversely affected by the rise of imports. We must be prepared to help companies develop new lines of production, we must be ready to help communities attract new industries, and we must have programs to assist displaced workers to prepare themselves for new jobs, and, if it seems desirable and they so choose, to move themselves and their families to new locations.

We regret to say that we consider the adjustment assistance provided for workers under the administration's trade bill to be seriously inadequate both to the needs of displaced workers and their families and to discharge our moral obligations to repair, as best we may, the injury they suffered in the national interest.

We believe the unemployment compensation benefits provided by the bill should be higher than the proposed 65 percent of the individual worker's wages, and that the benefit ceiling of 65 percent of the average manufacturing wage would result in unfair discrimination against workers in relatively high-paid industries, leaving them far short of 65 percent of their own wages. We are especially troubled by the failure to provide more realistic protection for older workers.

Under the bill, a worker displaced at age 60 would be able to receive weekly benefits for only 65 weeks. After that he would have to manage without income until he reached age 62 and become eligible for a social security pension. Then he would receive a reduced pension amounting to only 80 percent of the pension to which he would have been entitled had the job lasted until he reached age 65. The bill should be amended to remedy these defects.

In moving toward greater integration of the free world economies we must take steps to narrow wage differentials in production for international trade that bear no relationships whatsoever to the relative productivity of workers employed to make the same product—often with the same technology—in different countries. We are encouraged that the President recognized the importance of this problem in his message to Congress on this subject when he referred to "appropriate consultation on an international basis" in connection with narrowing the "current wage gap" between the United States and other countries. We urge that it be made the policy of the United States to seek adoption and implementation of the principle of international fair labor standards along lines set forth in the Havana Charter for an International Trade Organization signed in 1948 by the United States and 52 other nations, but unfortunately never ratified. Implementation of the international fair labor standards principle would, among other things, help improve our balance of payments to the extent that it is adversely affected by runaway American oversea investment made for the specific purpose of taking advantage of low wages in other countries—rather than for legitimate economic reasons.

Balance of payments

In considering our international economic relations, it is important we avoid being panicked by an unfavorable balance of payments into domestic economic policies that would prevent attainment of full employment, stifle economic growth and thereby aggravate rather than improve the international payments deficit itself.

America's trade surplus and other inflows of foreign funds have been more than offset by other factors, primarily military expenditures abroad and U.S. private investment in foreign countries, together with short-term capital movements. The resultant unfavorable balance of payments was $3.9 billion in 1960, partly due to the recession. In 1961, the unfavorable balance declined to an estimated $2.5 billion.

America's basic balance of payments, however, has improved significantly. The unfavorable balance of our basic international accounts (excluding the movement of short-term investments) declined from $1.9 billion in 1960 to an estimate of approximately $700 million in 1961. This gain can be maintained and improved by strengthening America's position in world trade. It can also be improved further by full employment and rapid economic growth at home, which would encourage an increase in both American and foreign long-term investments in the United States.

There is a danger that attempts may be made to try to "solve" the outflow of short-term investments through a tight-money policy and high interest rates. Such an attempt to maintain and attract foreign short-term investments would be self-defeating. It would slow the growth of the American economy and thereby reduce the attractiveness of both long-term and short-term investments here. With inadequate growth and underutilization of capacity, unit costs would rise, placing American industry at a competitive disadvantage in international trade.

The Federal Reserve's policy of stabilizing interest rates on short-term Government securities is one important means for discouraging the outflow of such funds by mainainting world confidence in the American economy and the U.S. dollar.

Further strengthening the lending authority of the International Monetary Fund, toward which some steps have been taken recently, would help greatly to reduce possible international speculation against the U.S. dollar, such as occurred in late 1960. Efforts should be made to develop an international banking arrangement that would reduce U.S. responsibilities as a world banker and thereby relieve pressures on the U.S. dollar.

Restrictive monetary, fiscal, and wage policies that would slow the rate of economic growth provide no solution to the balance-of-payments problem. Such remedies are worse than the disease. We must attack the balance-of-payments problem constantly on two fronts—on the homefront by building a strong, stable, and rapidly growing economy, and on the international front by coordinating America's monetary and trade policies with those of other free nations within the context of an expanding domestic economy.

STRUCTURAL UNEMPLOYMENT

The dislocations that may result from a more liberal trade policy exemplify structural unemployment problems which require solution if our economy is to function at its maximum potential. There are similar personal, family, and community problems that result from technological advance and other changes that occur in a dynamic economy.

The adjustment assistance provisions of the administration's trade bill are sound in principle. The administration's manpower development and training bill is similarly aimed at solving the structural unemployment problem. The Area Redevelopment Act is also directed toward the solution of problems of structural unemployment.

The fact that measures of this kind have White House support and have been enacted or are receiving serious consideration in Congress is a symbol of progress in social responsibility and compassion as well as in economic commonsense.

Our basic unemployment problem, however, as the Council of Economic Advisers last year agreed, is not structural but a result of inadequate demand. In an atmosphere of general economic slack resulting from inadequate demand, measures to deal with structural unemployment cannot wholly fulfill their intended purposes. Retraining programs are frustrated when there are on job opportunities in the community for which to retrain the unemployed. Relocation has limited possibilities when idle workers outnumber vacant jobs in most other communities—when, for example, there are 461 "areas of substantial and persistent unemployment" according to the Labor Department list for January 1962. Making depressed communities more attractive to industry is of similarly limited help when there are so many such communities competing for new industry and when there are few employers to attract because most are already choked by idle capacity.

The problem of structural unemployment can be attacked successfully only in an atmosphere of generally full employment in which the structural problems tend to dwindle automatically to manageable numbers. When employment opportunities are available many workers will leave depressed communities at their own expenses and more will leave if they are assisted with relocation grants. When full employment is widely prevalent, employers establishing new plants will gravitate naturally to depressed communities with an available labor supply and more can be attracted to such communities with the aid of an area redevelopment program.

The natural forces that tend to minimize structural unemployment in good times can be greatly facilitated and made to work more smoothly and more quickly by sound legislation. Such legislation therefore makes an important contribution to the elimination of the economic waste and human hardship resulting from unemployment.

Nevertheless, the principle of such legislation is still new in the United States. It faces vigorous opposition and often outright hostility. The Area Redevelopment Act, the one major measure in this category now in operation, in on trial and will remain so for some time.

It would be tragic in the extreme if failure to solve our basic economic problem of inadequate demand should cause legislation directed at structural unemployment to be discredited in the eyes of the public because it is unable to function with full effectiveness in the face of widespread unemployment.

We must press on for the enactment of such legislation because of the valuable human and economic purposes it serves. It has the wholehearted support of the AFL–CIO. But the struggle for the legislation needed to provide us with the proper tools to deal with structural unemployment must not divert us from the task of creating the conditions under which those tools can be applied with maximum effectiveness—the task assumed by the Nation under the Employment Act of 1946, "to promote maximum employment, production, and purchasing power."

A PROGRAM TO ACHIEVE AND MAINTAIN "MAXIMUM EMPLOYMENT, PRODUCTION AND PURCHASING POWER"

During the past year—and for the first time in 8 years—the administration has presented Congress and the Nation with a series of proposals based on the recognition that a foremost objective of national policy must be the implementation of the Employment Act of 1946 through promotion of maximum employment, production, and purchasing power. The reports of the President and the Council of Economic Advisers to this committee bring that program together into one coherent whole.

We congratulate the President and all who have assisted him on the leadership which they have demonstrated in facing up to the responsibilities which properly belong to the administration, and in reminding both Congress and the people of the responsibilities which are also theirs.

We have dealt at length in this statement with those points at which we disagree with the administration's program, and especially with those points at which we feel it does not go sufficiently far to achieve those ends which we are confident the administration seeks. We believe that constructive criticism offered in a cooperative spirit can be of far more assistance, and is far more acceptable both to this committee and to the administration itself than any amount of uncritical acclaim could be. We wish to make it clear, however, that we are wholeheartedly in support of both the general principles and the major specifics of the administration's program. It represents an expression of strength, of imagination and of confidence in the ability of the American people to rise to new heights of achievement which have been too long absent from our leadership.

We urge this committee to support and Congress to pass the measures which are essential to the realization of our national potentials. They include the following:

1. *Planning for adequate growth.*—Adequate economic growth is the only road to maximum employment, production, and purchasing power and to the mobilization of our country's maximum economic strength. We shall never reach those goals unless we first make realistic plans and then find effective means of carrying them out. We urge this committee to commence without delay a study of the methods of democratic planning for maximum economic progress which have already been put into successful operation by some of our free world friends and allies, and we urge immediate establishment of a technological clearinghouse for gathering the information on which all wise planning must be based.

2. *Aid to education.*—We urge that there be no further delays in provision of Federal aid to education, including school construction, teachers' salaries, aid to colleges, and provision for a broad program of scholarships.

3. *Medical care for the aged.*—The national disgrace of our failure to provide medical care for the aged through the social security system must be brought to an end. Such a program would not only remedy a harsh neglect of a major need of older people, but by freeing more of their incomes for other necessary purposes would make an immediate contribution to the stream of purchasing power and demand.

4. *Department of Housing and Urban Renewal.*—The establishment of a new Cabinet post of housing and urban renewal is essential to give full recognition to the needs of the town and city dwellers who constitute the majority of our people, and to further the development of comprehensive programs to meet those needs. Such programs should include Federal initiation of and assistance to low-cost, low-rent public housing and middle-income private housing which will go beyond the sound start made in last year's legislation. They should include a comprehensive program of urban renewal and industrial rehabilitation to remove the blight of city slums and rebuild urban centers. They should include an adequate community facilities program to enable cities and towns to provide adequate sewage disposal plants, sewage lines, power facilities, cultural and recreational facilities, hospitals and nursing homes, roads, streets, mass transportation, and other essential facilities.

5. *Government contracts for distressed communities.*—One of the most obvious ways in which the Federal Government can give immediate aid to communities distressed with serious unemployment is by placing defense and other Government contracts in such areas. Such action will not only help to relieve the distress in these areas, but by insuring that the work is done by men and women who would otherwise be idle, it will make a contribution to the Nation's economic growth. Legislation should recognize the principle that reasonable additional costs involved in placing contracts in distressed areas will be offset by resultant avoidance of the heavy financial costs and other tragic consequences of unemployment, both to such communities and to the Nation.

6. *Unemployment compensation.*—Permanent reform of the unemployment compensation system can no longer be delayed. The administration's bill should be adopted with strengthening amendments to (*a*) require all States to provide at least 26 weeks of benefits to all eligible workers who remain unemployed that long, (*b*) liberalize the criteria which would trigger the President's authority to extend benefit duration for workers with less than 3 years' experience in covered employment, and (*c*) provide immediate Federal supplementation of benefit amounts up to the levels payable after effectuation of the final stage of the benefit improvements called for under the bill.

7. *Standby tax reduction authority.*—The President should be given the authority he has requested to reduce personal income tax rates temporarily when required to meet the objectives of the Employment Act.

The administration's bill should be amended, however, to provide greater upward leverage on the economy for the same amount of temporary revenue loss by confining tax reductions to the first bracket rate.

8. *Public works.*—The President's proposal to accelerate and initiate up to $2 billion of capital improvements as a means of creating new jobs and also helping to meet our public needs should be adopted, but with provisions which would enable it to be used to help combat current unemployment.

9. *Resource conservation and development.*—A program to conserve and develop our natural resources and repair the neglect of recent years should be undertaken.

10. *Youth Conservation Corps.*—Unemployed young people should be offered work in a Youth Conservation Corps to work on needed conservation projects. The object of the program should be to give young people the opportunity to become valued and self-respecting members of society by contributing to the conservation of essential natural resources, earning fair wages and learning skills which will help them to find permanent employment.

11. *Farm program.*—Organized labor is prepared, as it always has been, to support sound programs, acceptable to the farmers themselves, for bringing prosperity to our family farmers. Our surpluses of food can be used as capital in underdeveloped countries so as to give them the opportunity of freeing agricultural workers for the development of new wealth-producing industries. In cooperation with other food-producing nations, and with proper safeguards against dislocation of existing trade relationships, we can make use of our abundance to help others build the means of greater abundance for themselves.

12. *Increased consumer power through higher wages and salaries.*—The necessity for increased consumer demand, and the central position of wages and salaries as the major source of that demand, must form the focus of any effective program to restore maximum employment, production, and purchasing power. Government must apply policies calculated to right the existing imbalance between capacity and demand and thereafter to encourage a movement of wages that will maintain that balance.

This requires, among other things, that free collective bargaining be unleashed from the legislative shackles that now hamper unions in the effective performance of the role they should play in a free economy. Revision of our labor relations legislation should be aimed at returning to the Wagner Act policy of active encouragement of collective bargaining as contrasted to present legislative policy which, at best, grudgingly tolerates unions and imposes unnecessary and unjustifiable obstacles both to the organization of unorganized workers and to effective collective bargaining. Under the new administration the National Labor Relations Board has adopted more enlightened interpretations of the existing legislation, but this is an inadequate substitute for more reasonable laws.

Through vigorous application of the Walsh-Healey Act, the Government can use the powerful leverage of its vast procurement operations to raise the general level of wages by bringing substandard wages up to the levels generally prevailing in industries working on Government contracts. The act should be amended to the extent necessary to assure its quick and effective implementation, and ample administrative funds should be provided to permit frequent review of prevailing minimum wage determinations in order to keep them fully up to date.

13. *More adequate measurement of unemployment.*—In order to measure our productive potential so that our plans will be adequate to make full use of it we must have better measures of unemployment. The Joint Economic Committee is to be commended for having made a major contribution toward that objective in stressing the significance of data on full-time equivalent unemployment measures which take into account time lost by members of the labor force involuntarily on part time. These figures should be published regularly and not merely made available on request as at present.

But even such figures do not tell the whole story. There is one form of unemployment that is not reflected in any available statistics. This is the unemployment suffered by those who, in the words of the Council of Economic Advisers, "are not regarded as unemployed simply because, discouraged by a lack of suitable job opportunities, they have abandoned the search for jobs."

Admittedly the extent of this kind of unemployment cannot be measured precisely. But it is important to have a reasonable estimate of its magnitude. This can be obtained by subtracting the actual labor force from the projection of the labor force. Projections of the size of the labor force have established a sufficient degree of reliability to justify such a calculation. If, as is sometimes claimed, there are technical problems that raise questions as to the validity of such calculations on a monthly basis, they should be made at least quarterly.

We urge that the Joint Economic Committee call upon the Bureau of Labor Statistics to compute such figures regularly, making due allowance for the proportion of the individuals involved who would be available only for part-time employment. The resulting figures should be integrated with the data presently computed on the full-time equivalent of unemployment and under-employment combined, so as to provide a reasonable approximation to the extent of underutilization of the total potential labor force. The Joint Economic Committee should evaluate such data prepared by BLS with a view to determining whether or not it should call upon the Bureau to publish them regularly.

14. *Flexible workweek.*—The Fair Labor Standards Act should be amended to provide for a reduction of working hours, consistent with the objective of full employment and rapid economic growth. Weekly wages should be maintained through a national workweek adjustment fund financed by a small tax on payrolls.

15. *Fair employment practices and action against discrimination.*—The administration, through the Secretary of Labor, has made clear its support for fair employment practices both by the effective use of existing machinery and by support for more adequate legislation, and has initiated legislation to remove discrimination as to voting rights which is an essential step toward the elimination of other forms of discrimination. The program deserves unreserved support.

16. *Administered prices.*—A continued national investigation and analysis of the price structure is needed—such as the work that has been ably begun by the Joint Economic Committee and the Senate Subcommittee on Antitrust and Monopoly—to provide the basic facts and knowledge for developing possible remedies for abuses in the framework of a rapidly growing economy.

Public attention should be focused on the pricing policies of the dominant corporations in major industries, whose prices are administered by the executives of the big corporations, rather than determined by effective price competition. Each sector of the economy should be closely examined for the possible development of opportunities to reduce prices, whether because of improved productive efficiency or for other reasons.

17. *Economic aid.*—Economic assistance and technical aid for underdeveloped countries—both directly and through international agencies—are essential to our hopes of a peaceful, free, and prosperous world. The administration has already shown effective support both for an increased effort on the part of this country and for increased participation of other nations that can afford to bear their share. The alliance for progress has brought new hope to the democratic forces in Latin America. But a program closer in its scope to that of the Marshall plan is required to meet the vast magnitude of need of our neighbors to the south. Increased aid to the developing countries would not only help to strengthen freedom's defenses around the world, but would help to take up the slack in our own economy through constructive work for peace.

18. *National defense.*—The national defense effort must be kept under constant review to assure that it meets the requirements for the defense of the United States and the free world. Constant effort must be made to avoid waste and duplication and to eliminate them where they are found to exist; and defense expenditures should be raised if necessary to provide adequate national defense.

19. *Research.*—The Federal Government should encourage the development of both basic scientific research and technological application. Adaptation of the great advances in military technology to civilian purposes should be speeded up. Industries of low and slowly rising productivity should be assisted to improve technology, while other Government programs operate to cushion any adverse impact of rapid technological change on individuals, businesses, and communities. Development of atomic energy for peaceful purposes should be given high priority. Cooperation with other nations should be sought in peaceful programs of worldwide importance such as desalination of water, advances in meteorology, and the exploration of space.

20. *International trade.*—The United States must improve its trade relations with other countries, particularly since we need a wide variety of imports, as well as foreign markets for our own products. We must work to lower some of the barriers which have recently been raised against our exports, while resisting the temptation to retaliate with higher barriers against imports. The President should be granted the negotiating authority he has requested to broaden markets for our exports. Adequate provision must be made to minimize hardship and to facilitate readjustment for workers, businesses, and communities adversely affected by imports. At the same time steps must be taken to meet the problem of unfair competition with some American products from low-wage highly efficient foreign producers. To help solve this problem for all exporting countries which face it, the United States should propose, through GATT and the International Labor Organization and in negotiations with the European Common Market, the establishment of international fair labor standard pro-

visions on wages and other labor conditions in export industries, directed at raising wages in such industries step by step to levels justified by productivity.

21. *Monetary policy and the Federal Reserve Board.*—Monetary policy must be conducive to vigorous economic growth. While, in view of the outflow of gold, short-term interest rates must for the time being be maintained, long-term interest rates should be reduced through open market operations and reduction of the rediscount rate.

An adequately expanding money supply at reasonable interest rates is essential to healthy growth. This has been denied the Nation in recent years in part because of the unrepresentative character of those who set Federal Reserve policy. The Federal Reserve Act should be amended to provide for adequate representation of consumer, small business, and labor interests on the governing and advisory bodies of the Federal Reserve System which is now dominated by the viewpoint of bankers and big business.

22. *Tax reform.*—The Federal tax structure should be reformed and overhauled to provide a balanced and equitable basis for raising needed Federal revenues and an effective countercyclical fiscal tool. Recent erosions have weakened the progressive tax structure, originally intended by the law, and have contributed to the lack of balance between the economy's ability to produce and actual sales. We welcome the recommendation of the administration to close certain tax loopholes, and we urge it and the Congress to eliminate all escape hatches which enable favored taxpayers to avoid carrying their fair share of the total tax burden.

Reform of the tax structure should be based on fairness and economic balance. Some tax assistance should be afforded, for example, to small business, which usually suffers disproportionately in terms of economic stress. This assistance could take the form of reversing the present 30-percent normal and 22-percent surtax rates on corporate income. The lower 22-percent rate would thereby apply to smaller corporations, instead of the 30-percent rate as at present, and the current 52-percent tax rate would remain for larger corporations.

The proposal to provide an investment credit to corporations should be resisted strongly. Business investment in new plants and machines will not be induced on a sound and sustained basis by windfalls and grants of special privilege. A sound and sustained rise of business investment requires economic balance, rising demand, and the expectation of continued increases in sales volume and profits.

CONCLUSION

We have made a beginning on an enormous task—that of restimulating and restoring to health an economy which for nearly 8 years had been weak and halting. Substantial recovery has already been achieved in some economic indicators, and it can be achieved in all if we continue to apply the necessary economic measures with sufficient vigor and determination.

Our greatest danger now is that we may be satisfied with too little. If we let our efforts be weakened by a partial measure of recovery, if we give way before the fears and the opposition of those who would rather look to the past than venture courageously into the future, then we shall not only fail to achieve the goals we might have reached, but we shall be unable to avoid an early recurrence of recession.

We must learn to accept the vast potentialities for growth and progress that the technological revolution has already made available to us, and the new weapons against poverty and scarcity that it is daily placing in our hands. We must accept them not only as opportunities, but as challenges.

Our choice is not whether the new technologies will be applied or not. What man has created, man is bound to use. Our choice is whether they will be used to end forever the nightmare of human poverty, ignorance, and disease, or whether they will be used to create new nightmares of unemployment and human misery. Our choice is whether we shall find the means to use abundance by sharing it or whether we shall allow ourselves to be drowned in a flood of abundance that we have not learned to use.

If we are to accept the challenge, we must have faith in ourselves—and faith in mankind's dream of a world in which he has conquered want and fear. For the first time in human history, the realization of that dream has become a practical possibility. We must not allow ourselves to be deflected from it by fears or prejudice or lack of vision.

We have an opportunity to remake a world such as was never before given to any people. We must have the wisdom, the vision, and the courage to seize it. Let us determine now that we shall do so.

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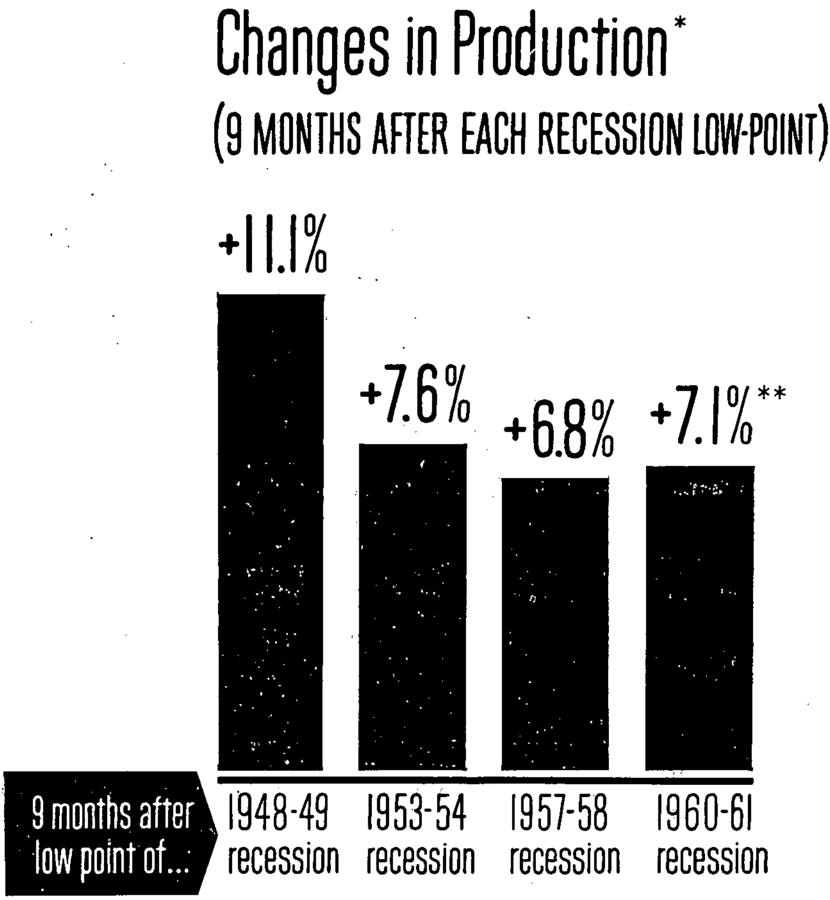
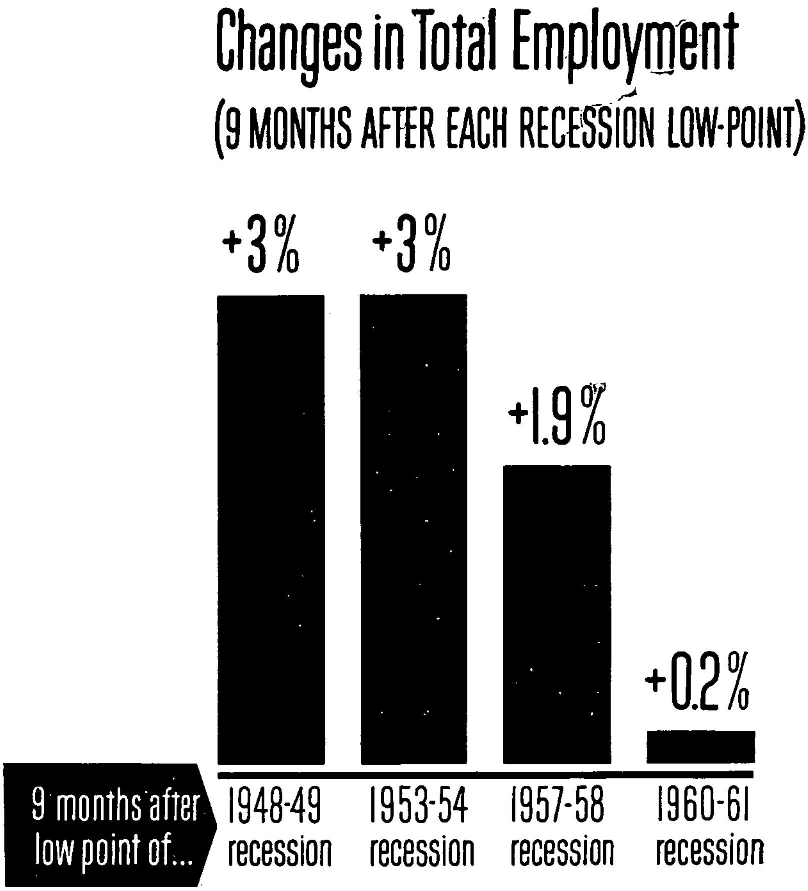


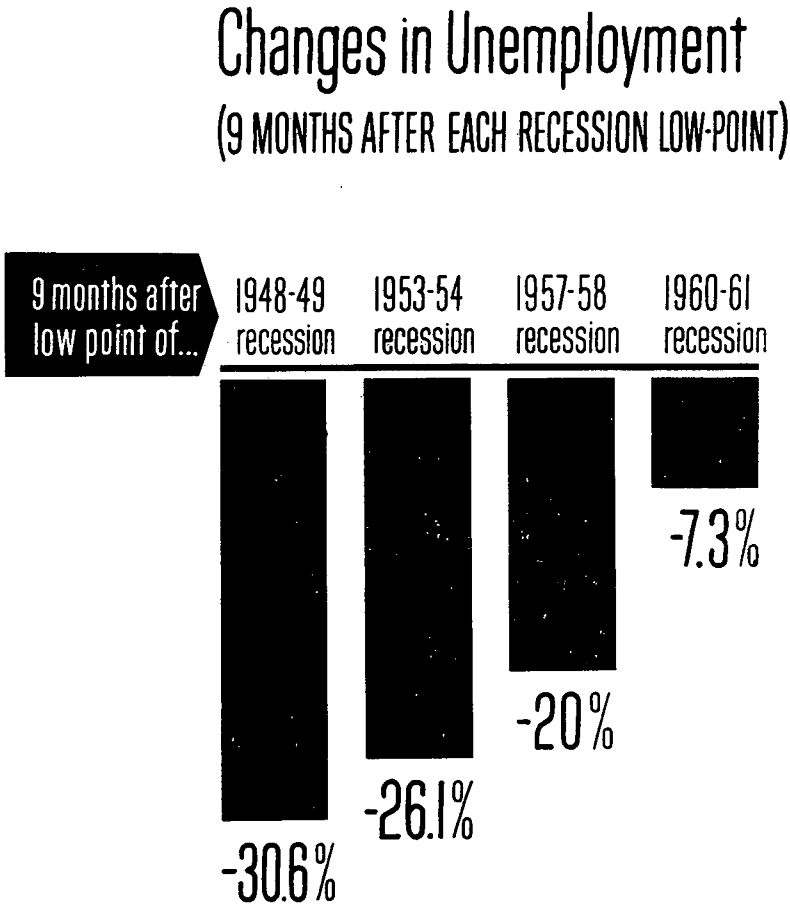
* REAL GROSS NATIONAL PRODUCT

** AFL-CIO ESTIMATE

SOURCE: U.S. DEPARTMENT OF COMMERCE

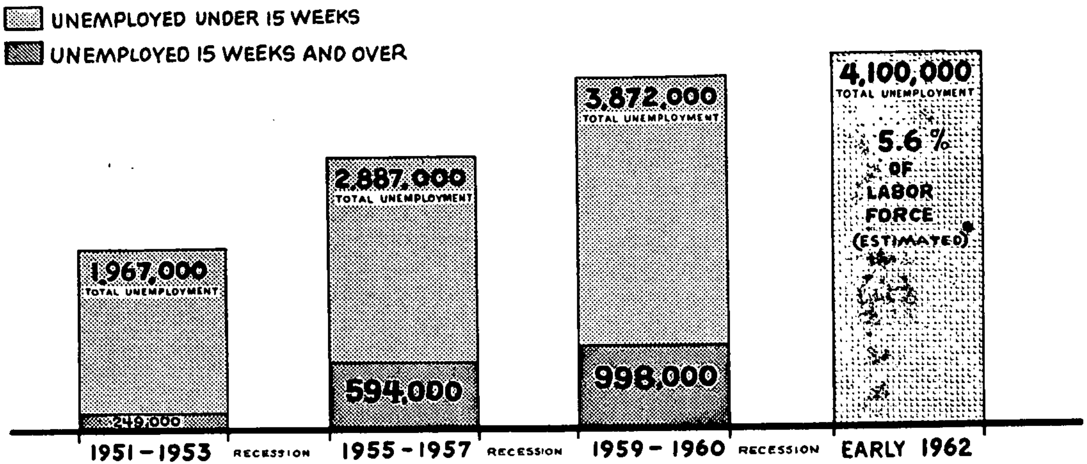


SOURCE: U.S. DEPARTMENT OF LABOR



SOURCE: U.S. DEPARTMENT OF LABOR

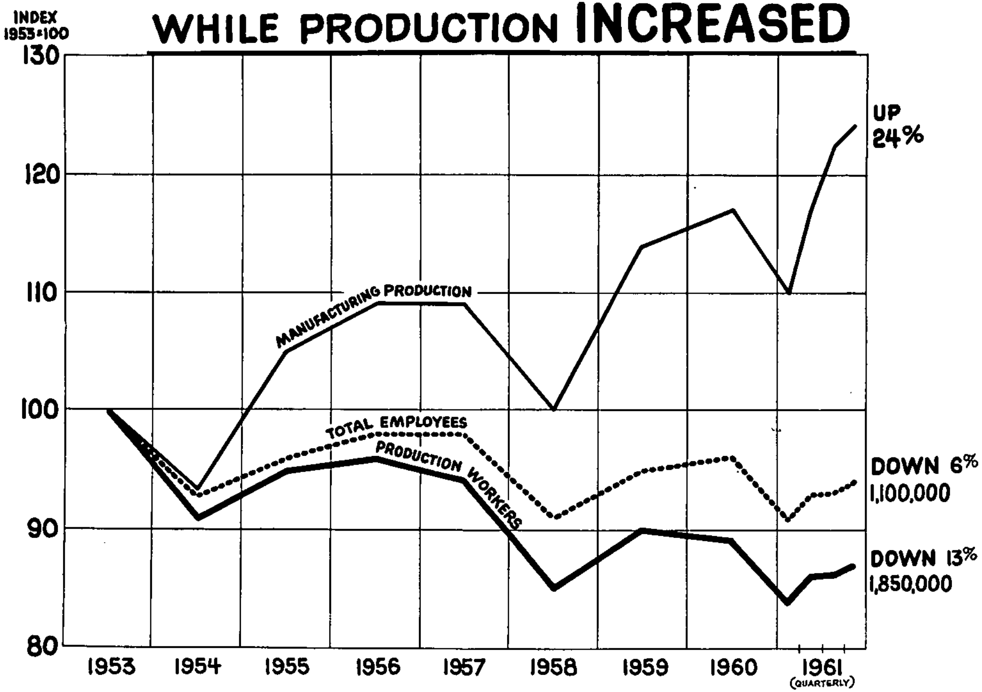
Unemployment in 1962 likely to be higher than after Previous Recessions



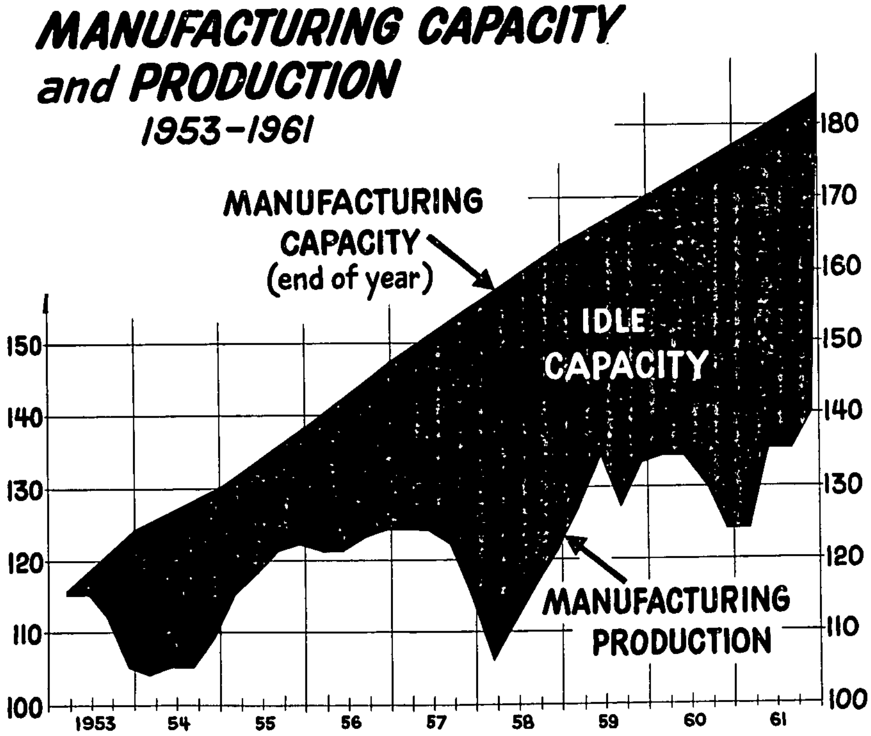
*Estimated from CEA Data, Seasonally Adjusted.
No Estimate for Long Term Unemployment Included.
Total Unemployment Unadjusted Estimated at 4.8 Million.

DATA: DEPT. OF LABOR

MANUFACTURING JOBS DECREASED WHILE PRODUCTION INCREASED



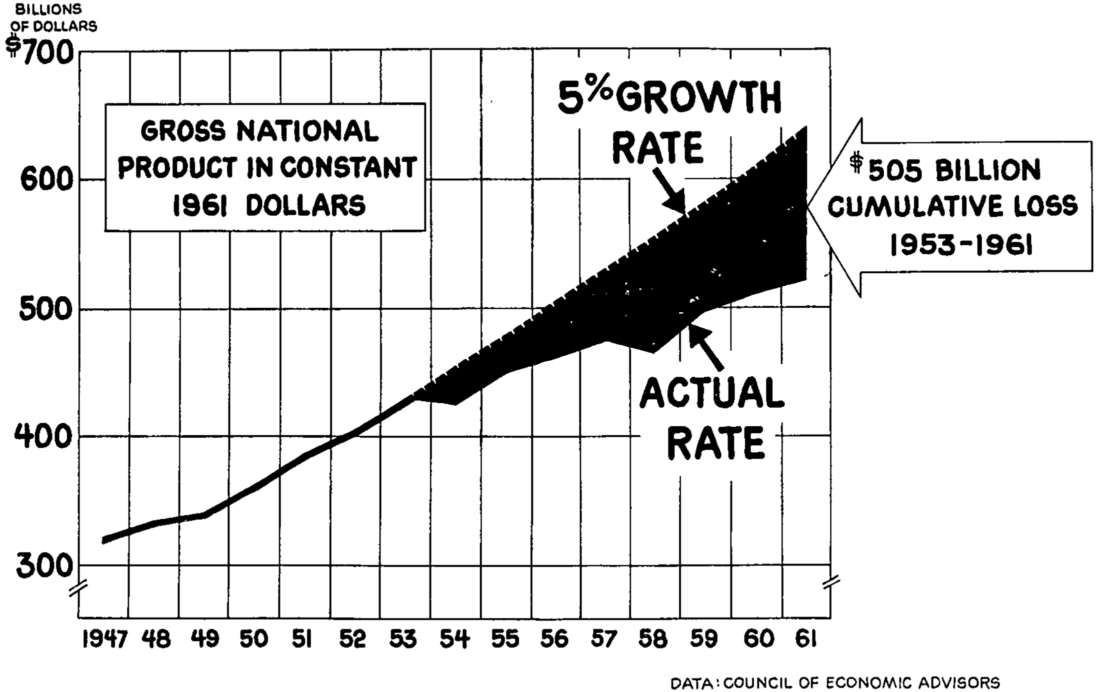
DATA: FEDERAL RESERVE BOARD; U.S. DEPT OF LABOR



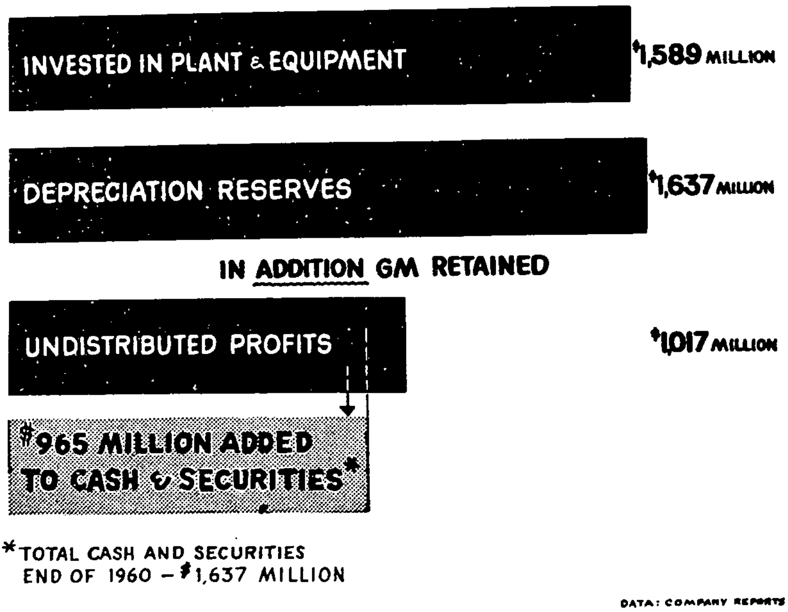
END OF 1950=100

SOURCE: FEDERAL RESERVE BOARD AND McGRAW-HILL PUBLISHING CO.

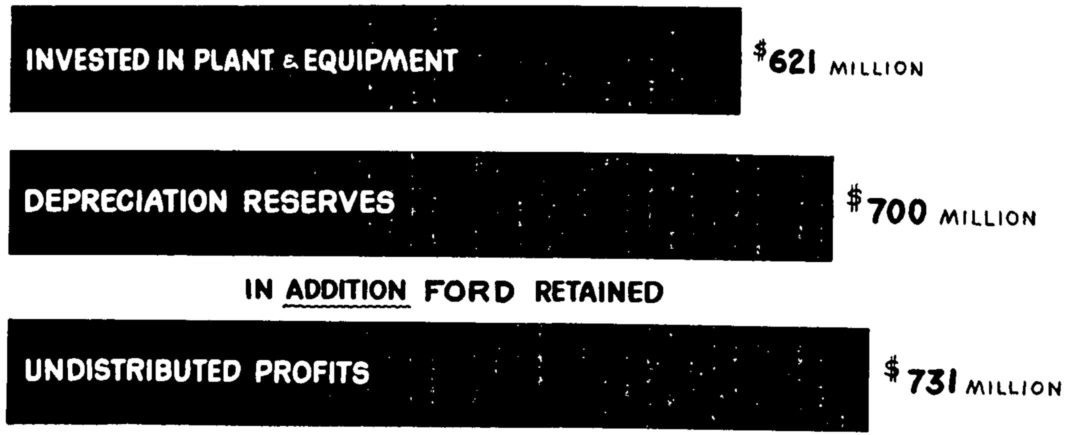
THE LOSS IN TOTAL NATIONAL OUTPUT



GM's DEPRECIATION RESERVES MORE THAN COVER INVESTMENT NEEDS 1957-1960



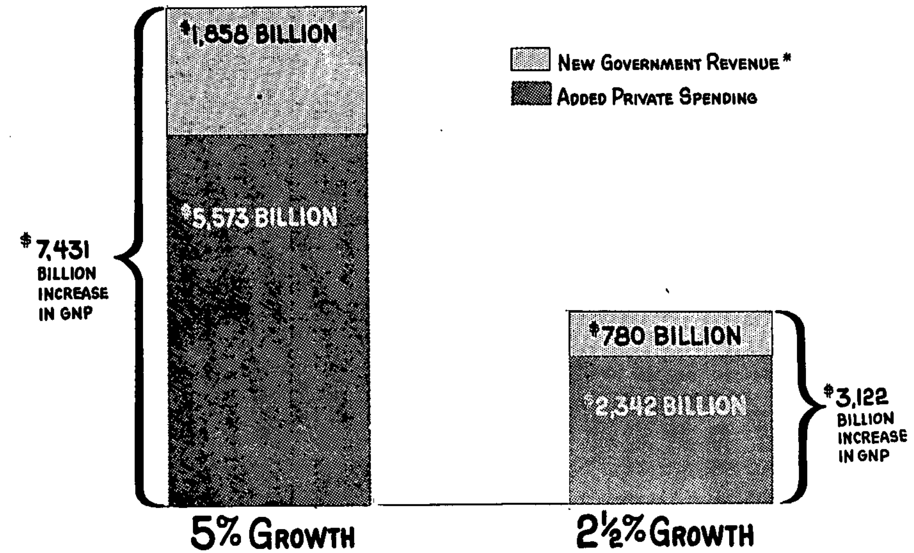
FORD's DEPRECIATION RESERVES MORE THAN COVER INVESTMENT NEEDS 1957-1960



DATA: FORD MOTOR COMPANY

5% GROWTH WOULD PRODUCE MORE THAN TWICE AS MUCH NEW GOVERNMENT REVENUE AND ADDED PRIVATE SPENDING AS 2½% GROWTH

(20 YEAR TOTAL 1961–1980)



* CALCULATED AT 25% OF ASSUMED INCREASE IN GNP 1961–1980, INCLUDING STATE AND LOCAL REVENUE

Mr. REUTHER. I come here this afternoon representing millions of American wage earners and their families, and I would like to talk to the committee about some of the very serious problems that concern us and relate these problems to the President's Economic Report.

We have said many, many times that we believe that the American economy is freedom's greatest material asset. I think it is the intelligence that we demonstrate in mobilizing its great economic potential and the sense of social responsibility that we develop in sharing the great abundance that our technology and our economy make possible that will be decisive in whether or not our kind of free society will be equal to the challenge that we face in this troubled world of ours.

We have to be strong enough on the military front to discourage aggression wherever it may raise its ugly head. But in the long pull, we are going to win over the forces of Communist tyranny by demonstrating that our kind of free society, built around the values of the worth and the dignity of the human individual, can find answers to practical problems. In the long pull, it is the quality of our society that will determine whether we shall be able to win that contest.

I believe that what we do with the American economy is going to determine that primarily.

I happen to share the belief that our system of freedom is equal to the challenge that we face in the world if we try.

I happen to believe that we are in trouble because we are not trying.

I want to address myself to that broad question this afternoon.

We have lost in the last 9 years more than 20 million man-years of labor—man-years not hours—20 million man-years. Now, this represents a total economic waste because we all understand that you cannot store an hour of human labor. You have to use it when it is available. You can store a bushel of corn or a ton of steel but you have to use an hour of human labor when it is available. When 20 million man-years have been wasted because of mass unemployment, this represents a tragic economic waste that we cannot afford. We lost more than $500 billion in gross national product in goods and services that we could have had if the American economy had been operating in high gear with full employment and full production. We believe that this 20 million man-years of wasted labor and the $500 billion in the gross national product that we could have had not only constituted a lost potential of economic progress in terms of higher living standards, better housing, and greater educational opportunities and better medical care and all the other things that we need in order to improve our way of life. In the contest between freedom and tyranny, ending this tremendous economic waste can be the margin of survival of the values that we believe in.

I wish the Communists were wasting $500 billion of their economic potential. I wish that they had 20 million man-years going down the drain. But they are crowding themselves and we have to recognize that the competition that we are up against in the world is the stiffest competition that free men have ever faced and, as I have been saying, this is a kind of one-game world series. There will be no return matches. We have to win this one.

As you know, Mr. Chairman, I spent an evening with Mr. Khrushchev when he was here and we had a most enlightening and interesting discussion. Mr. Khrushchev is a crude and cocky and confident individual, and I came away believing that Mr. Khrushchev is counting more upon America's failures than upon his own successes.

I believe that he thinks that we are incapable of the kind of total effort in peace that is required to win this contest in the world.

I think that he, like all other dogmatic Marxists, believes that our free society is composed of competing, conflicting, and irreconcilable pressure groups incapable in the absence of total war of achieving the common purpose that we need to move America ahead.

Now, I do not share that point of view. I think you can get people just as excited about the challenge and the opportunities of peace, of building the good life, of expanding the horizons on the educational front, on the medical front, and in all the other areas where there are positive rewards for human effort, to get people doing just as much together in terms of positive values as they did in war in terms of negative values. This, essentially, is the great challenge. Everything else is academic.

If America cannot find a practical way to mobilize its great potential and relate that potential to the basic needs to the whole of our society, then everything else is just so much unimportant trimming and we will lose.

I think that the President's report has to be related to that central question: Are we moving ahead? Are we doing what must be done to realize this economic potential and to relate it to the basic needs of a free people?

I think we are not. I think that the President's program is a good beginning. I think it is only a beginning. I do not think it is adequate. I do not think it will achieve the objectives that we must achieve if we are to be equal to this challenge in the world. I think that free men are capable of developing a greater sense of national urgency and a deeper sense of purpose and a clearer sense of direction. I think all of these things are essential if we are going to be equal to this problem and the challenge.

You know, when the people of the world look at America they see us quite differently than we see ourselves and they are going to judge the worth of our society not by our economic resources or by the brightness of the chrome on our new Cadillac although they respect these things. They are going to ask themselves: How does America really measure up to the realities? And the realities of the worth of a society are not what do you have in the way of material wealth but what do you do with what you have. It is the capability, it is the sense of purpose, it is the measure of resolve that a people are able to demonstrate in relating material wealth to human values.

When you compare what we have with what we are doing with what we have, it is clear that there is much unfinished work on the agenda of American democracy. The President points out the areas in which this job needs doing, and I think he should be commended for the leadership that he has demonstrated. Yet when you measure his proposals against what still must be done, his proposals fall short of the kind of progress that we think is essential.

I think the President's report and the leadership that he is providing are a sharp departure in terms of vigor, in terms of imagination, from the lack of leadership that we have had in the past.

I think it was rather significant and symbolic that, within 12 hours of assuming that high office, the President's first official act was to double the distribution of surplus foods for needy unemployed families. This I thought demonstrated a deep sensitivity and concern about the welfare and the well-being of the less fortunate in America.

The President obviously deserves the support and the commendation of the American people for his leadership in the distressed area field, unemployment compensation, minimum wage and social security, and all of his initiatives in these areas are good. But they are not good enough. They are a step in the right direction but they are a small step where we need giant steps.

I think the President is providing leadership but that leadership marks only a new beginning.

If you measure what the President is doing by the standards of yesterday, then his leadership and what proposes to do look rather impressive. But we cannot solve the problems of today by measuring what we do against the needs of yesterday. We have to talk about what the dimensions of the problems are and when we measure what the President's program proposes doing with the dimensions of the problems to be solved, with the sweep of the opportunities to be realized, then I think we have to conclude that the President's program is inadequate and that it falls far short of the goals essential to implement the purposes of the Employment Act of 1946 and to get America back to work.

The President quite properly restates in his report the objectives of the Employment Act of 1946, which is to promote maximum employment, maximum production, and maximum purchasing power.

Then the President says that this Nation, and I am quoting from the first page of his report—

> that this Nation will not countenance the suffering frustration and the injustices of employment or let the vast potential of the world's leading economy run to waste in idle manpower, silent machinery, or empty plants.

Now, that is a very clear, very forceful declaration and commitment to do something about this problem.

But the important thing is how do we take the words and put them into specific, tangible, practical economic action? How do we get America back to work?

I would like to suggest, Mr. Chairman, that the first thing we need to do is to comprehend the dimensions of the problem, and we have not done that clearly. Each time that we get a little bit of improvement we are such wonderful people that we just want to embrace that little bit of improvement and pretend that we are really on the way and that we are almost out of the woods. I say that we have only made a scratch on the surface of this hard-core problem of unemployment.

I would like to present several charts to illustrate the dimensions of this problem.

This first chart indicates the change in production, using the period 9 months after the low point of the last four recessions to compare what is happening in the present period as contrasted to those three earlier recessions.

In the 1948–49 recession, 9 months after the low point, production was 11.1 percent above the low point. In the 1953–54 recession, we were 7.6 percent, productionwise, above the low point. In the 1957–58 recession we were 6.8 percent above the low point. In 1960–61, we were 7.4 percent. So that, productionwise, the last three recessions showed similar behavior, with the 1948–49 upturn having a stronger thrust because of the impact of the Korean hostilities. So that, productionwise, the pattern is almost the same. But if you took consolation from that fact you would be running away from the very serious character of this problem.

Now, let us take what happened to employment in the same period. Nine months after the low point in the 1948–49 recession, we had picked up a 3-percent increase in employment; 1953–54, 3 percent; 1957–58, 1.9 percent; and in the 1960–61 recession, only two-tenths of 1 percent.

Now you begin to get the dimensions of this problem. Production is back where it was but instead of employment picking up 3 percent it went up two-tenths of 1 percent.

Let us take a look at the unemployment situation; here you begin to realize the dimensions of the problem.

Nine months after the low point in the 1948–49 recession we had reduced unemployment 30.6 percent, which was a sizable reduction. Nine months after the bottom of the 1953–54 recession, we had reduced unemployment 26.1 percent. Nine months after the low point of the 1957–58 recession we had reduced it 20 percent.

And here is the shocker. Nine months after the low point in the 1960–61 recession, we had only reduced unemployment 7.3 percent as contrasted to 30.6 percent.

Yet that does not tell the whole story because what has been happening in the American economy is that we have lost somewhere—and the loss would be worthy of some searching—a minimum of 750,000 workers.

Now, we reduced unemployment only 7.3 percent in this period while production went up very drastically. But the number of people in the work force should have increased 1,250,000.

The figures show it going up less than a quarter of a million.

If you make allowance for the fact that 300,000 people went into the armed services who otherwise would be in the labor force, you can figure there are at least 750,000 people who "got lost." Maybe they got lost because they figured it was just a waste of effort to look for a job in their community because there were younger people unemployed who could not get a job.

So if you take that 750,000 who got lost and add to that number roughly 2½ million more who represent the full-time unemployment equivalent of people who are partially employed and partially unemployed, the January unemployment rate of 5.8 percent of the work force is pushed up to 9 percent. And when the economy improves enough so that general employment opportunities look favorable enough, these 750,000 people who got lost will actively reenter the labor force and at that point unemployment will jump sharply, in our opinion.

The CHAIRMAN. Are these charts in your statement here, Mr. Reuther?

Mr. REUTHER. Yes; and they are also in the form of tables in the documents.

The CHAIRMAN. They will be inserted, too.

The committee agrees that you will insert anything that is material. So I hope you will insert them.

Mr. REUTHER. Fine.

You see, we would like to be optimistic, too. I think it is part of the basic American character to try to look on the bright side of things and nothing would make us happier than if we could really look at the bright side and not have to worry about what is on the other side of the coin. But we know that fighting communism and preserving freedom require the same measure of toughness and self-discipline and realism that we put into other programs.

What bothers us is what is happening in the American economy. We come out of each recession with a larger residue of unemployment and we start the next recession on a higher plateau of unemployment.

So here you have it.

In 1951–53 we had 1,967,000 unemployed. Then unemployment jumped to 2,887,000 in 1955–57; 3,872,000 in 1959–60, and now we come up to what we think is an understatement of where we are going to be in 1962, up to 4,100,000.

The lower bar indicates those with unemployment of 15 weeks and over. This is the hard core of unemployment in the major centers and some of the minor labor areas.

In the 1951–53 period we had only 249,000 in the hard-core long-term unemployment group.

In 1955–57, it went up to 594,000, a tremendous jump.

In the 1959–60 revision, it went up to 998,000. This time people are saying the recession has evaporated like a rainbow in the bright sunshine of prosperity but we are going to wind up with a larger group of Americans chronically committed to permanent unemployment.

We can ignore these kinds of basic economic facts only at great peril in terms of the ability of our free society to meet the real challenge.

We are only nibbling on the outer fringes, Mr. Chairman, we are only pretending to deal with this basic problem of hard-core unemployment. We are nibbling on the outer fringes when we need to sink our teeth deeply into the core of the hard problem.

I take the position that we have to run to stand still and if we are really going to make progress then we need to raise our sights, we need bold, adequate action that can give us forward momentum. Otherwise we will just run until we are out of breath but we are not going to make any real progress.

I would like to point out, as this chart No. 5 shows, what has been happening.

The period of 1953 through 1961 shows that manufacturing production went up 24 percent. We turned out 24 percent more of the goods that we make in our great manufacturing industries.

The number of production workers in that same period went down 13 percent; 1,850,000 fewer production workers are now turning out 24 percent more goods.

There has been a shift. There are more white-collar and technical people in these industries.

When you offset those gains against the production workers who were laid off, there is a net reduction of 6 percent, or 1,100,000 fewer workers turning out 24 percent more goods.

The point I would like to drive home is, this technological revolution has just started.

Two days ago the New York Times reported a new breakthrough in the whole technology of computer science, in the whole construction of these electronic brains, which are the core of our technological revolution because they direct machinery and schedule the flow of production.

Heretofore, the time cycle between the various impulses of an electronic computer was three-millionths of a second. That is how fast these various operations took place. Yesterday at a meeting of the President's Labor-Management Committee, I talked very briefly to Mr. Thomas Watson, president of the International Business Machines Corp. which produces these electronic brains. He told me this new one is now technologically feasible and they are working on it.

Mr. Chairman, the new electronic computer is going to be a thousand times faster than the present computers; the impulse gap is going to be three-billionths of a second. Instead of having a huge building to house a computer that operates at a cycle speed of three-millionths of a second, the new computer, small enough to be housed in a desk drawer, will operate at a cycle speed of three-billionths of a second.

Now, it is hard for you and me to comprehend the impact of that on what we are talking about. Any projection of the impact of technology upon the size and the character of the work force and upon the increase in our productivity will be understated because we cannot comprehend the full sweep and impact of this new technology. Its impact is cumulative. A breakthrough in one field opens up new doors elsewhere in an accelerating pattern.

So, this one item is symbolic of the whole complex trend of our developing technology. Science is going to have a revolutionary impact upon our whole technology and therefore we have to try to comprehend the dimensions of this problem.

Now, to put it very simply, in round figures, as a minimum we need 4 million new jobs every year for the next 10 years. When we break it down to take care of the new people arriving in the labor force, which will average roughly 1,350,000 a year for the next 10 years, and those people who will be technologically displaced by the march of automation and the new technology in the electrical computers, et cetera, we need 80,000 new jobs 52 weeks every year in the next 10 years. And, this is just to stand still. This will not put the four-point-some million people who are idle or additional millions who are partially unempolyed or the 750,000 who got lost somewhere in the shuffle, it will not put them back. The 80,000 jobs a week are just to hold our own so that it does not get worse.

How many are 80,000 jobs a week? It is hard to comprehend that, so I have broken it down. I have used these figures before because I think they are understandable.

The General Motors Corp. is the largest manufacturing corporation in the world. It employs 400,000 workers, production workers, clerical employees, technical people in the United States. We will have to create the job equivalent of a General Motors Corp. every 5 weeks.

The United States Steel Corp. has 200,000 employees in total. Every 2½ weeks we will have to create as many job opportunities as the United States Steel Corp., the biggest steel company in the world.

The Du Pont Co. is the biggest chemical company in the world. It has 80,000 employees. Every week we have to create the job equivalent of the Du Pont Corp.

Do you think we can do this by nibbling on the outer fringes of this basic problem?

I say that is a flight from economic reality, and we cannot afford that kind of wishful thinking. We have to recognize that this problem requires commensurate action. Nothing less will do the job.

Our people, people I have the privilege and responsibility of representing, whether they are automobile workers or steel workers or building trades workers or any other group of workers, ask very simple but fundamental questions. They ask: "If we can have full employment and full production making the weapons of war and destruction when we are faced with the challenge of war, why can't we have full employment and full production making good things in life for people in peacetime when our social system is faced with the challenge that the Communists pose?"

Now, the good Lord did not ordain that we are capable of our greatest achievement only in war.

What we have to do is really sit down and find answers to this problem.

Our people are just like any other Americans, they do not believe that they are automatically entitled to economic security. We do not think economic security is a right. What we do insist upon is that every American able and willing to work ought to have the right to a job, the right to an opportunity to earn his economic security. When economic and social forces beyond the control of the individual deny him an opportunity to work, then it is the moral obligation of the whole of society to use the instruments of Government to do what must be done so that every one able and willing to work will have access to the opportunity to earn his economic security.

We have pointed out in the Employment Act of 1946 our basic goals, but we have not worked out any practical methods to achieve them in a practical economic sense.

We must ask and answer certain questions. How are we going to achieve full employment, how are we going to maintain it, how are we going to realize our tremendous unrealized economic potential? How allocate our resources based upon a list of social priorities in such area as education? How are we going to build a society in which every American can share in the fruits of the abundance made possible by automation?

I tell you that I think the future of freedom hinges in a large measure on our ability within the framework of our free society to find answers to such questions.

I think our failure to find answers to the basic problem of achieving and maintaining full employment can be the Achilles heel of American democracy. How can you convince Asians that they ought to try to build a social system along the broad principles that we believe in when they say to you, "If you can't make your system work with all of your advantages, how can you expect us to make that same system work with all of our disadvantages?" That is a very potent argument. I have argued with some of these people in Asia and it is hard to answer.

What we have to do is to prove that our system can be made to work and that we can convert advantages into great assets and translate material assets into human values.

I think to do that, Mr. Chairman, we have to make a decision. We have to decide that we cannot solve tomorrow's problems with yesterday's tools. You could not sell a model T today and yet we are still peddling model T economic concepts.

The world is changing. We did not choose it. If we could go back to a peaceful world in which America had no world responsibilities, in which unemployment and many other complicated problems were not staring us in the face, maybe we would all choose to do that. Yet we cannot repeal the 20th century and its problems. We have to learn to live in it, we have to master the problems and we have to realize our potential and our promise. To do that will take new ideas and new concepts and new tools.

Now, I think that with the exception of a microscopic group, all Americans—American industry, American labor, people in public life, religious groups—almost unanimously are committed to the preservation of our free economic system. We believe in it. We think it is an essential part of the whole concept of a free society.

But I must say that I do not believe that just having pious slogans about free enterprise is an adequate substitute for a positive program. I think it is dangerously unrealistic to believe that sole reliance upon the blind forces of the marketplace will insure the achievement of the objectives of the Employment Act of 1946 or get America back to work or keep America fully employed. We have tremendous idle capacity. This chart shows what we had the capacity to do and what we did. The black represents roughly our tremendous loss in gross national product. Now, this unrealized potential can be the margin of survival. With the kind of competition we face in the world, with the kind of responsibilities that we must assume, not because we want to, because no one else is equipped to assume them, we cannot afford to waste that economic potential. No one in his right mind could pretend that in the age of the electronic computer that the theories of Adam Smith are adequate or that we can just let our future ride on the blind forces of the marketplace.

What we need to understand is that our democratic society has to accept wholeheartedly some concept of democratic planning so that we, as a free people, can begin to allocate our resources.

Democratic planning does not mean that we have to have a dogmatic bureaucratic approach. We are pragmatic people, we are very light on theory—we say if something works, good, we will do it that way. If it does not work, it can have the most perfect theory but we have no tolerance for it.

What we need to do is to recognize that in a complex society like ours, with all of these revolutionary forces playing their part, there has to be some rational mechanism for harmonizing private economic decisions with the public good.

I do not think that this will mean that we are going to get regimentation. I think that the threat of regimentation lies in neglecting the realities and the dimensions of this problem of unemployment, in wasting our great economic potential. Lack of such realism can breed a crisis and crisis can lead to regimentation.

When democracy is strong, when democracy is solving its central problems, then there is no crisis and regimentation is not going to sneak either into the front door or the back.

But if we neglect our problems, then frustration and fear will build and regimentation always rides on the back of fear and frustration and desperation.

I believe that the Economic Council ought to be asked to explore the possibilities of some rational democratic mechanism for a measure of planning, for direction in our society and economy. I think Congress would do well to explore this field.

There are many societies doing this. The Scandinavians do it one way, the British do it another way. The British Conservative Party, the Tory Party, has accepted a measure of democratic planning because Britain cannot survive without some rational allocation of resources and manpower, without some practical mechanism by which to harmonize private economic decisions with public needs and public policy. Instead of narrowing the area in which private initiative and private incentive and the free play of voluntary economic decisions would operate, I think that this would broaden the opportunities because if you have a full employment economy the opportunities for private initiative, the opportunities for greater private decisions are obviously enlarged.

So I hope that we can recognize that there is nothing un-American or subversive about the concept that a free society has to plan some of its functions on a more rational basis and relate them to decisions that are being made in the area of private economic decision, whether it be collective bargaining or management decision. There has to be some way of harmonizing these in terms of our needs as a whole.

Then we have this problem, Mr. Chairman. We are flying blind, technologically speaking. There is no person in America who can tell you what the total impact of this technological revolution is going to be upon the size and the character of the work force, its impact in terms of the location of new plants and new industries, in terms of the future.

General Motors knows about the automobile industry. United States Steel knows about the steel industry. Du Pont knows about the chemical industry. United States Rubber knows about the rubber industry. But there is no place where there is a gathering of the total information and the total knowledge where it can be evaluated and be available for public decisions or for a great corporation or smaller company that has to make a private economic decision.

We have been suggesting for a long time the need for the creation of what we call for lack of a better name a technological clearinghouse, an agency whose responsibility and function would be to bring together from private industry, from Government research centers, from university research centers, all information with respect to the broad sweep of our technological revolution. We need such a center so that competent engineers and scientists, social scientists and physical scientists, can evaluate where we are going, what will be the size of the work force in 10 years, what is going to be the ultimate impact in terms of the auto industry, the steel industry, the electrical industry, of such developments as this new computer. Nobody knows that.

The General Motors Corp. makes decisions blindfolded with respect to the future. If anybody thinks they are not infallible, ask them why it took them so long to make small compacts because they were so wrong about the American market.

If anybody thinks that all management decisions are infallible, ask the Ford Motor Co. why they poured $300 million down the drain on the new Edsel. It is because of many things they do not know and we should not expect them to know in a situation where no one has access to the evaluated information available.

Take the training program. We support the efforts to get legislation that the President has recommended for retraining programs, to help the worker through this period economically, to give him access to training opportunities, to develop new skills. But do you think there is any incentive for a worker to acquire new skills when at the end of that period he is just going to be unemployed, a more skilled unemployed worker?

You cannot know these things. You cannot train people except as you know the kind of jobs, the kind of skills needed, the number of such jobs, where they are going to be. There has to be some rational approach.

Right now no one has access to this kind of information because it does not exist; the Government has to provide leadership in facilitating the bringing together of this kind of information and its evaluation.

We detail this in our prepared statement.

I think the central core of our economic problem is that we have not learned to achieve a dynamic balance between our ability to create greater economic wealth on the one hand and our ability to create adequate purchasing power to absorb that greater productivity and facilitate growth and expansion in the economy.

We have grown, in the past 9 years, at about half the growth rate needed, at about 2½ percent. This chart indicates, as I said earlier, that we lost roughly $505 billion from the period from the middle of 1953 through 1961.

This line indicates we were growing roughly at 5 percent from 1947 to the middle of 1953 and then we slipped. Over this whole period we averaged about 2½ percent. Now, why? Is it because we are incapable of a continued thrust upward at the rae of 5 percent?

The answer is "No." We are capable of it. But why do we get into trouble? Why is it that we have this tremendous waste? Why do we have this unused capacity that this other chart indicates? It is finding the answer to that "why" that is important.

I would like to suggest that the source of the problem is that we do not know how to distribute what we know how to make; that our know-how in the creation of wealth has outrun our ability to manage abundance, which is to say to share it.

Obviously, there is trouble when you can create greater wealth than you can consume because a portion that you can create either is not created or it piles up until employers lay people off because the warehouses are bulging.

Take the question of the appliance industry. That is a good example. The appliance industry operated in 1960, at the low point of our recession, at around 45 percent of its existing capacity. Now, this is the industry that makes refrigerators, deep freezers, electric ranges. Are we saying that all the people in America who need these things have them? The answer is that there are millions and millions and millions of families with tremendous unfilled human needs. They have the need but they lack the purchasing power to translate need into active demand in the marketplace to buy what we can produce.

This imbalance between productive capacity and purchasing power is not a fixed relationship. If we were in a period where demand was crowding capacity and building up inflationary pressures, then we ought to deemphasize the creation of purchasing power and emphasize the creation of capital goods to expand our capability. But having expanded our capabilities, we have to expand our purchasing power to make the purchases that will keep our greater capacity busy.

So this is the dynamic relationship: higher productive capacity, higher purchasing power; still higher productive capacity matched again by still higher purchasing power, always getting a balance which facilitates growth and expansion and a forward thrust. Now, we have not had that. The result is that the thrust has been only half as strong as it needs to be to create the growth, expansion, and new job opportunities essential to full employment.

This is more than a matter of economic justice. I am not here pleading just for economic justice to American wage earners. Obviously, that is one of my prime functions and I do the best I can. I am here to make it, I hope, understood that this is not just a matter of economic justice, it is a matter of economic necessity. The economy won't work unless we achieve a dynamic balance between the ability to create great wealth and the ability to consume that wealth and thereby create the dynamics of growth and expansion in the process. Otherwise, the whole system will collapse. Of course, Mr. Khrushchev thinks it will. When the Communists say we are the warmongers, what they mean is that only in wartime can we create ability to balance production and consumption because we spend billions in destroying wealth in war. I think we have to prove that they are wrong.

It seems to me what we have to do is to recognize that we need to put greater emphasis upon the expansion of the purchasing power base of the American economy.

Now, where do you expand purchasing power?

Well, I think that since most purchasing power comes out of wages and salary, any policy that would tend to deemphasize the expansion of purchasing power by holding down proper adjustments in the wage and salary structure would be wrong.

We have made it very clear that we are committed to try to maintain a stable price structure because nobody gains if all you do is to cancel out the expansion of purchasing power by higher prices. All you do is accelerate the economic merry-go-round and you do not go anywhere.

So we want higher purchasing power within the framework of a stable price structure. That is possible out of our tremendous increase in productivity, out of our new technology.

If we had now a proper relationship between wages and profits to maintain a balance in the economy, then that might be one thing; but in the present situation we have got to place greater emphasis upon expanding wages and salaries in order to give us the greater purchasing power base we need.

The Council of Economic Advisers recognizes that in a number of places in its report but it deemphasizes it in other sections of the report and we think that this is a serious shortcoming of the report.

One finds on page 108 of the report of the Council of Economic Advisers:

> Faster economic growth requires above all an expansion of demand to take up existing slack and to match future increase in capacity.

Now, that is precisely what we think. But we believe that, in order to facilitate the achievement of that broadening of the purchasing power base, we have to recognize that wage earners and salaried workers and farmers must get a larger share of the fruits of our developing technology. And the economy, in our opinion, is in serious imbalance because there is a serious imbalance between productive capacity and the purchasing power to consume and absorb production.

Now, I suppose that labor people talk about the rich getting richer out of habit, but it is true.

Here is an article by Sylvia Porter the other day, quoting a report by Professor Lampman of the University of Wisconsin who did a study for the Bureau of Economic Research. This is the group headed by Mr. Arthur Burns, who was the Chairman of the Council of Economic Advisers for Mr. Eisenhower. The report came up with some very disturbing facts. It says that the rich are indeed getting richer and the poor are getting relatively poorer. The report shows that under the New Deal period, and this was one of the great contributions that the New Deal made, there was an impact upon the distribution of America's wealth and that has been reversed. We are now getting a higher concentration of economic wealth in a smaller group and the rich are getting richer and the poor relatively are getting poorer.

This report says that 1 percent of American adults hold 28 percent of the total wealth of America, and that that 1 percent also owns 65 percent of the corporate stock of America.

The CHAIRMAN. Will you please place this quoted article in connection with your remarks in the record?

Mr. REUTHER. I shall be happy to, sir.

We referred to this in our prepared statement.

(The article referred to follows:)

RICH GET RICHER AND NEW REPORT PROVES LEGEND

(By Sylvia Porter)

The concentration of wealth in our country is almost as pronounced today as it was in 1933—the year Franklin D. Roosevelt became President and began the New Deal.

The richest 1 percent of American adults now holds 27 to 28 percent of the Nation's entire personal wealth, which includes all corporation stocks, Government and corporation bonds, real estate, mortgages, cash, insurance. In 1933, the richest 1 percent held 28.3 percent.

The richest 1 percent holds 76 percent of all corporation stocks outstanding. In 1929, the year of the stock crash, 1 percent held 65.5 percent of the corporate stock.

Moreover, the wealthiest wealthy own virtually 11 percent of all State and local government bonds, 32 percent of all U.S. Government bonds, 12 percent of all real estate.

This is just a sampling of the astounding findings disclosed this week by Robert J. Lampman, economics professor at the University of Wisconsin, in a 286-page report on "The Share of Top Wealth Holders in National Wealth, 1922–56," published for the National Bureau of Economic Research by the Princeton University Press.

WEALTH NOT EQUALIZED

It is the most comprehensive report on the wealth of very rich Americans ever compiled.

Lampman's findings mock the general impression that since Roosevelt and the New Deal, there has been a vast equalization of the distribution of wealth in the United States.

Yes, there has been an equalization of the distribution of incomes and we have become the greatest middle-income nation ever known. But there has not been much of an equalization of the ownership of wealth.

Lampman's figures underline how spectacularly total personal wealth has grown—from $300 billion in 1922 to near $2 trillion in 1962. There's a much bigger wealth pie for all of us to slice.

WOMEN NOT IN MAJORITY

Who are the very rich? Those with estates of $60,000 or more, for Lampman based his study on an analysis of estate tax returns and only estates of this amount or more are subject to estate taxes.

How many rich are there? Lampman estimates there were over 1.7 million top wealthholders in 1953. Considering what has happened to stock prices since, there are probably more than twice as many today.

What about their sex? Here Lampman smashes another common notion, for he finds only one-third of the top 1 percent are women and they hold only 40 percent of the wealth of this group.

Lampman's findings on the very rich and how they've prospered under and since the New Deal are guaranteed to inflame both radicals and reactionaries alike.

Mr. REUTHER. I think, as I said earlier, that no one has a right to ask Government to give him economic security on a silver platter. One has, a right, however, to ask Government to pursue policies and to advance programs that afford every American the right to a job, with the opportunity to earn his economic security. I believe that the purpose of Government in this kind of situation can best be measured not by how it helps the few who have enough to get more but what it does to help the many who have too little to get enough. I think that is the measure of whether Government policy is economically sound or morally responsible. What does it do to help the many with too little to get enough?

When the rich are getting richer and the poor are getting poorer and millions of Americans who have tremendous unmet needs lack the purchasing power to translate need into active demand, and idle capacity and idle workers result, and the free forces of the marketplace cannot correct that, then it is the obligation of Government, as the agent of all the people, as Lincoln said, to do for the people what they are unable to do for themselves, and that is what we believe in.

We believe, basically, in a minimum of Government intervention in the economic sphere. This is why we are strong in our demand to maintain collective bargaining as a free process of freemen. Yet we recognize that there are things that the Government must do because no one else either has the capability or the responsibility of doing them.

We support in this spirit the President's request for standby authority. Why? Well, we believe that there is a problem of timelag. An economic situation can worsen before you can get the Congress to act.

We would want the President to have that authority subject to congressional review so that we could move quickly because when the snowball has only rolled a few hundred feet down the mountainside it can be stopped but if it picks up momentum and speed, then it is much more difficult. Therefore, we seek that authority.

But we point this out. We think it is a mistake to talk about that authority as though it were something related to future recessions. It ought to be related to the present one. We are not out of the woods. We are still in a recession. We have made progress but we cannot be satisfied with the present level of unemployment. While the President is not satisfied, we do not believe that his program is adequate to the dimensions of the problem.

The second observation we would like to make is that when tax relief is given it should be given to that group who are the many who have too little to help them get enough and not give a blanket tax adjustment to people who do not need it.

I think it stands to reason that a fellow who is among that 1 percent who own 28 percent of America's wealth does not really need any help. His kids are not eating badly because he cannot afford to feed them properly. As a matter of fact, those are the fellows who are drinking Metrecal. They don't need any help economically.

If you give relief to the low-income groups, this is high-velocity purchasing power. It will not be in the salt brine in the basement, it will not be invested in the future, it will be spent to buy the goods, the food, and the clothing that the people need.

So we support the President's program but we think that the timing ought to be for now and we think the emphasis ought to be in the low-income groups.

Now, we favor providing incentives for the encouragement of capital accumulations and investment because we recognize that only as there is adequate investment capital to expand an industry and facilities can we achieve growth essential to full employment. But we oppose very strongly the President's proposal for an 8-percent tax writeoff to business.

According to our projections this would deny the Government roughly $1½ billion that it needs and would provide this relief to the wrong people.

I would like to call your attention in this respect to a chart from an article that appeared in the June 15, 1961, issue of Forbes magazine, a business publication. This article is entitled "The Midas Touch" and it goes on to say in the first paragraph—

Does anyone have some good ideas on how to put about $1 billion to work profitably? If so, Frederick G. Donner, Chairman of the General Motors Corp., would be glad to hear from him. Currently General Motors' treasury is all but overflowing in cash and Government bonds to the tune of $1.6 billion.

I would like to suggest that the General Motors Corp. does not need your help. As this chart indicates, the General Motors Corp., in the period of 1957 to 1960, invested in new plant and equipment $1,589 million, and had depreciation reserves of $1,637 million, undistributed profits of $1,017 million, and added $965 million to the category called cash and securities. They had so much money they didn't know what to do with it.

Yet, the present legislation which we oppose would give the General Motors Corp. 8 percent tax relief which, in effect, would mean that they could write off all future investments on the basis of 116 percent. That is the way it works out mathematically.

We think that that $1½ billion that the Government would lose here ought to be given to people who need it and who will spend it to buy things.

If you will look at the Ford Motor Co., you find a comparable situation. In the 1957–60 period the Ford Motor Co. invested in plant and equipment $621 million. They had depreciation reserves of $700 million. They had undistributed profits of $731 million.

We hear a great deal of talk about the imbalance of payments in the world. It is a very serious problem.

I had the privilege and pleasure the other day in a meeting of the President's Advisory Committee to hear Mr. Douglas Dillon, Secretary of the Treasury. I heard a very scholarly presentation of this problem.

We are all very worried about this. This is a serious problem. We had a $5½ billion favorable trade balance last year. That is not where the problem is. The problem derives essentially from the flight of American capital. If it were going to the underdeveloped countries it would be a problem but at least it would be doing some good, but it is going mostly to the highly developed countries. The Ford Motor Co., with great unused productive capacity in the United States in the last period, sent $500 million of its unused capital to Canada and Great Britain and made a great contribution to that imbalance-of-payments problem.

Now, No. 1, they do not need relief. No. 2, you will be giving relief to the wrong people; and, No. 3, the way to deal with the imbalance-of-payments problem is not to give these people larger cash reserves, uninvested profits, but to achieve full employment so that there will be attractive investment opportunities in the American economy as present capacity is used and a need grows to create new capacity.

Senator DOUGLAS. At this point, I suppose you are addressing yourself to the proposed 8- or 4-percent tax credit on investment?

Mr. REUTHER. I am, sir. That is right. We are opposed to that.

As I said earlier, if we were now in a situation where our capacity was short and the pressure of demand was great, we would be for deemphasizing the expansion of purchasing power, wages, and salaries and for putting the most emphasis on the accumulation of capital so that we could encourage investment and expansion of capacity but when we have all of this unused capacity and great corporations have this kind of tremendous reserves, this would be money sent to the wrong place. It is not needed and cannot be defended, in our opinion. We disagree with the President on this.

Senator DOUGLAS. You have taken the two greatest concerns in the industry in which you are most interested, the automobile industry. Have you or your staff compiled figures on the overall data?

Mr. WEINBERG. We have and they are set forth in great detail in our prepared statement because we also understand that these two very favorably situated corporations may not be considered typical.

We have a table comparing plant and equipment outlays by all corporations with the funds available from internal sources, primarily depreciation allowances and retained profits.

We find in the 1959–61 period, the funds available from internal sources actually exceeded the total amount spent by new plant and equipment. So that the situation portrayed by these charts for GM and Ford pertains to the economy in general.

Mr. REUTHER. I might say, Senator Douglas, this is Mr. Weinberg, director of the special projects of the UAW, and Mr. Ruttenberg is director of the research department of the CIO.

We also want to commend the President for the leadership he has provided in the field of unemployment legislation. We feel what he is proposing for Federal standards for higher level of benefits and longer duration is a very important and necessary step in the right direction. But here again we feel the time schedule is not very realistic. We need this now. There is a large number of workers who are exhausting their benefits and you have this problem of the level of benefits. We have actually lost ground.

The level of unemployment compensation benefits today represents a smaller percentage of workers' wages than the level when the legislation was originally adopted.

The whole concept behind this legislation is that when a worker is laid off, you not only protect him and his family by insuring a substantial portion of his wage loss but you protect the economy by shoring up purchasing power and thus braking the process by which unemployment breeds more unemployment.

Therefore, from the point of view of the wage earner and the economy itself, we would like to suggest that what the President proposed doing, phased out over a longer period, be done over a shorter period and that a practical mechanism be worked out so that we can get the beneficial impact of his proposal in the present situation.

Senator DOUGLAS. May I ask a question here?

Mr. REUTHER. Surely.

Senator DOUGLAS. Turning to this table, I would like to ask whether the figures given in the second column; namely, funds available from internal sources, are in addition to those in the first column, plant and equipment outlays, or whether they are contained also within the first column.

Mr. WEINBERG. For recent years, these figures come from the table on page 283 of the Council's report. That table summarizes all the sources and uses of corporate funds.

Senator DOUGLAS. I did not catch your answer.

Mr. WEINBERG. It is page 283 of the Council's report.

This table breaks down both the funds available to corporations for various purposes and the sources from which they are available and the uses made of them.

The plant and equipment outlays are the actual figures of spending for these purposes during the years covered; the funds available from internal sources are the accumulated depreciation allowances for those years, and the accumulated undistributed profits for those years. In other words, taking the 1959–61 period corporations accumulated $93 billion in undistributed profits and in depreciation allowances.

Senator DOUGLAS. What you are saying is that if they had used the funds available from internal sources, they could have provided for all their plant and equipment outlays?

Mr. WEINBERG. That is correct.

Mr. REUTHER. With respect to the public works program, we commend the President for his leadership and his support of this program, but here again we do not think that he goes far enough. We believe that a more adequate public works program is needed not for the next recession but to help us get out of this one and we think it will create jobs and we think it will also enable us to carry out essential public works projects.

While we support the President's program, we feel he does not go far enough nor are his recommendations adequate to meet the dimensions of the problem.

We think that we need to raise our sights in all of these areas—on the educational front, the housing front, on the medical front, and we hope Congress will adopt the President's recommendation on medical care for the aged. We need to increase our research efforts, our resource developments. All of these things can be done.

But I get disturbed, Mr. Chairman, with people who say, "Well, these are all very fine. We like better education for our children. We like better housing. We like to wipe out slums in our cities. We would like to provide older citizens with a fuller measure of well-being and dignity in the autumn of their years. These are all fine, but we can't afford them." I believe that point of view would sell America short. I think this is a defeatist negative attitude that either shows no faith in America's capabilities or reflects lack of understanding of the tremendous economic potential that we are wasting. The key to this whole question lies in mobilizing this unrealized abundance.

I think that nothing would be more tragic than to replace 8 years of complacency with 8 years of caution in Government. This is not the time for complacency. This is not the time for caution. This is time for the bold, adequate action that moves us ahead and makes us equal to realizing this potential.

When you look at this chart here, you get some comprehension of what the possibilities are if we get a full employment economy. We have taken a projection of the 5-year rate of growth which we are equal to. We have proved it in the past. I personally believe that that is the minimum that we are capable of. I think we can go beyond that. The process can generate its own dynamics. But using a 5-percent figure, which is twice what we have done in the past 9 years, you can get some idea of the possibilities. We would increase the gross national product in the 20-year period $7,431 billion. Just think of that. That is an increase. The Federal Government's take out of the increase—this would not be total Government revenue but merely the increase in revenue—would be $1,858 billion.

We worry about a small temporary deficit and about balancing the budget when we ought to be worrying about balancing the economy. We ought to keep one thing in mind. You will never balance the Federal budget in Washington until you have balanced the family budget of the American people through full employment. Here is a great unrealized potential. This is what we have been throwing away. This is the margin of progress and survival. This is the margin to build schools so that we can have adequate education.

I would like to say to those people who are on the wrong end of the school argument that the real question is the quality of the people that we are going to develop in America, our ability to afford every child the opportunity of maximum growth and development.

I read that the Chinese are going to have a population by the year 2000 of a billion six hundred million people. Now, we cannot compete numerically and therefore we have to concentrate on the quality of our people and we have to facilitate their maximum growth and development.

This means a tremendously increased expenditure in terms of schools, facilities, and teachers' salaries, so that we do not lose each year 200,000 of the best high school graduates who do not go on to higher education because of economic or other reasons. Our success in reaching our goals, in education and other areas, depends on our success in realizing our economic potential. I think it is all there to be had, Mr. Chairman, if we go at it.

I hope that what we need to do is to learn. We know how to create abundance. That we have done very well. What we need to do as free people, is to be able to rise above partisan differences, economic interest, or sectional differences, to find common denominators of common purpose, a sense of common direction, to learn not only to work together to create this kind of bigger economic pie but to share it together as well.

Look how much easier it would be for labor and management to work out their differences if we all were slicing up a bigger pie. If you took home a little pie and you had five hungry kids and you had to slice that pie up, it would be hard to satisfy them, but with a pie twice as big, it would be that much easier. That is the way it is, when you are dividing up abundance it is much easier to solve the problem than when you are dividing up scarcity.

What we have to do is not only to cooperate in creating abundance but to employ abundance by being able to share it, so that we get a dynamic, expanding relationship that will give us a forward thrust, that will bring into being our tremendous unrealized economic potential. Then we can build schools, housing, and hospitals. We can help the underdeveloped countries of the world to minimize their desperation and in doing so encourage free choice, and help them find their way out of the wilderness and toward a democratic society. I think this is the guts of it.

I want to conclude by talking about a problem which is going to plague us for a long time unless we do something about it.

I have sat at the bargaining table, as a matter of fact at 6 o'clock this evening I will be sitting at the bargaining table with a committee at the Studebaker plant where we have a strike. I hope we can settle that strike. But I have been negotiating during the last year in behalf of about a million two hundred thousand workers. The most difficult problem, Mr. Chairman, at the bargaining table today is unemployment. Not matter how hard you work, no matter how ingenious you may be in drafting new proposals, when there are two workers and one job, you are in trouble, and that is our problem.

We have too many situations where there is one job and two workers.

I say that inescapably, in the face of unemployment, there will be gaining situation. The steelworkers will have it. This will be the thing that will haunt them at the bargaining table. It was the most difficult problem that we had.

I say that inescapably, in the face of unemployment, there will be a drive for a short workweek at the bargaining table. I happen to agree with the broad concept of the President of the United States: that there is enough work to do in America to keep us busy. He has taken the position that he is in opposition to a short workweek because, he says, there is so much unfinished work in America, we have such tremendous responsibilities in the world, there is enough work to keep us going on a 40-hour workweek basis. I think that is rather plausible. But it does not put bread and butter in the market basket of the unemployed worker. He cannot live on generalizations. He cannot pay his rent with them, he cannot pay a doctor's bill and he cannot buy the kid a new pair of shoes.

Until we find a rational way to solve this problem, there is going to be an intensive effort made at the bargaining table all over America in industry after industry to get a shorter workweek.

I happen to believe, and I have said this many times in the past, that the number of hours that we work in our society should not be a matter for arbitrary decision by labor or by management or by Government. That matter ought to be determined by the size of our work force, how many hands there are, how many brains there are to do the work, by the productivity of our technology and by the material standards that we want to achieve as weighed against the measure of human leisure that we want. This is a rational way for a free people to make such a decision. Unless we find a rational way to approach it, with logic and commonsense allowed to prevail, it will not be determined by logic, it will be determined by economic leverage; it will be determined not by economic facts but economic power.

I would like to suggest that that is not a very sensible way to do it.

Therefore, I would like to throw into the record here for your consideration—we have detailed it considerably in our prepared statement—what I think is a new concept for dealing with this problem. I think that we need to take a whole new look at it. I would like to suggest that what we call a flexible workweek approach be explored carefully, because if we take it on in terms of leverage and power, instead of logic and economic facts, then we will begin to build rigid concepts into our economic structure and just when we need flexibility we may find that we are prisoners, having boxed ourselves in with rigid concepts and rigid provisions. We should build on a flexible basis and say "OK," we are not going to argue with the President, if there is enough work so that everybody can have a 40-hour workweek, excepting where there are special industry situations, then fine, let us have a 40-hour week. If not, then let us reduce it to the level where we can have full employment so that we do not have a situation where some workers are asked to work overtime and their neighbor is unemployed. Then when the economy picks up and we are generating more forward thrust and we can have full employment with a longer week, we can increase the hours worked.

But if you commit yourself rigidly to a lower level of hours either through collective bargaining or legislation and you then get a situation where more hours of work are needed, you are going to be prisoners of your rigid commitment.

I think that the logical thing to do is to let the level of hours flow from the needs. Can we have full employment at 40? Fine. If we can't, if we can have it at 38, let us have 38. If we can go back to 39 2 years from now, let us have 39 or 40. But let us let the level of hours be dictated by our ability to maintain a full employment economy so that a small group of workers, percentagewise, whether it be 5 percent or 6 percent or 7 percent, are not victimized by their having to carry a disproportionate share of the cost of dislocation because of developing technology.

Now, I do not want to go into the details. We have spelled them out in our program.

I would like to say in conclusion, Mr. Chairman, not as a labor leader but just as an individual citizen of these great and wonderful United States, this is the last best hope of freemen. If we cannot make freedom work, if we cannot find answers to these problems within the framework of a free economy and a free political system, if we cannot find ways of solving economic and social problems without destroying our basic concepts of political and spiritual freedom, then nobody can find the answers. I think we can. I have unlimited faith in the capabilities of freemen and our free institutions. But I say we have to dare to try some new concepts. The old way of doing it won't do. Just stepping up public relations campaigns or self-hypnosis with fancy slogans is not going to do the job. We have got to recognize we are in the midst of a technological revolution.

What we have got to do is not to be afraid of that revolution. We have somehow to get on top of it, give it a sense of direction, and relate it to the central purposes for which our free society exists: to enable every human being to have the kind of educational opportunity that will enable him to grow to his maximum stature; to afford him the opportunity as a member of a free society to make his contribution, to perfect his measure of human genius and initiative, and to be rewarded within a framework of social policy permitting him to make progress without pushing his neighbor down. Then we can all move ahead together. I think this can be done.

I think we can beat the ears off the Communists because I believe that the creative capabilities of freemen are much greater than the creative capabilities of men who are denied freedom. But we have not given this great capacity of ours a chance to operate. We have been the prisoners of old slogans, antiquated concepts.

We have been holding on to the past when we need to shape our programs and our policies in the image of the future.

My plea simply is this: We are equal to the challenge if we have the moral courage to try.

We are in trouble, Mr. Chairman, I believe, because we are not trying. It is our plea, let us roll up our sleeves and get America back to work.

Thank you.

The CHAIRMAN. Thank you, Mr. Reuther. You and many of your members are constituents of a very famous Congresswoman serving in the House of Representatives of the U.S. Congress. She has had the great honor and distinction of being the first woman member of the Joint Economic Committee. She is the first one of her sex to be on the Ways and Means Committee of the House of Representatives, which, in itself, is a great honor regardless of whether the person is a man or woman.

So I am going to, without objection, yield my time to her to interrogate you first.

Mrs. Griffiths?

Mr. REUTHER. Not only is she a distinguished and capable lady, but she is a good Congresswoman.

Representative GRIFFITHS. I will only be a few minutes.

I would like to ask you, in the figures of those people entering the labor market annually, can you tell me whether or not those figures contain the number of women whose last child has entered school and who are now reentering the labor market? Are they considered?

Mr. REUTHER. I do not know that the figures in this particular area are complete. I think there is an increasing number of women coming into the labor market. On the specific question you raised, I am not sure that they show that. I shall be happy to have our people check into it and send you a note on it.

Representative GRIFFITHS. I would assume that they do not contain the number of women reentering the labor market until the woman has been in the labor market.

Mr. REUTHER. That is right. She has to really be in the labor market in order to be reflected in these figures.

Representative GRIFFITHS. Whereas undoubtedly a boy just graduating from school is in the figures. Is that not right?

Mr. REUTHER. He has to also actively enter the labor market. This is where the 750,000 people come in.

Representative GRIFFITHS. It is a very optimistic estimate then of the number of people who would like to enter the labor market annually. It is probably an underestimate.

Mr. REUTHER. That is right. The 1,350,000 figure, which is the figure generally accepted by both Government economists and private economists, I think is a very minimum figure. If you added these other groups the figure would be enlarged considerably.

Representative GRIFFITHS. Now I would like to ask you, in automation can you estimate or do you know on what types of employment our Nation will falter? That is, is it going to displace more women workers or more men workers?

Mr. REUTHER. I think that the first wave of the impact of automation was absorbed primarily by industrial workers, automobile workers, steel workers, and workers in the basic industries. I think the second phase of automation will hit heavier upon the white-collar worker. Since there are more women in the white-collar field they will therefore be disproportionately influenced by the second impact. I think we have to realize that.

Take this computer I was just talking about. I don't for one moment understand this technology. I read about it and I pretend I know a little bit about it, but I don't kid myself. The fact is that that new computer with a thousand times faster cycle is going to have tremendous impact upon the whole clerical field, on keeping books and that sort of thing, because you can standardize that routine more than you can productively change models. I think the women workers in the period ahead, when the effect of automation is felt in a broader area, will be more affected than men.

Representative GRIFFITHS. But it would still have an enormous effect upon puchasing power the moment they are laid off?

Mr. REUTHER. Surely.

Representative GRIFFITHS. I believe a school in my district ran a survey some years ago which pointed out that in that particular area of the district only 1 percent of the people had college education. Fifty percent had gone through the eight grade. Yet the average income per household was between $13,000 and $14,000.

Now this was possible because husband and wife were working. So if you laid off the woman worker you cut drastically into the purchasing power of the Nation.

I attended this morning a Ways and Means Committee meeting where the Secretary of Health, Education, and Welfare laid out the new welfare legislation. Among these was a nursery school. You are not subsidizing the woman, you are subsidizing her employer. Whoever heard of a nursery school for employed fathers? I would like to suggest to you that this is making women permanently second class. There is no more reason to subsidize the employment of women any more than the employment of men. She should be paid a living wage and that in a way should encompass the idea that she has to pay for her children to be in nursery school.

Mr. REUTHER. I subscribe fully to the concept that a woman doing the same job as a man ought to be paid an equal wage.

Representative GRIFFITHS. As a matter of fact, when we come to laying them off, and you have pointed out this is one of the most difficult problems, how do you make the determination which one goes, if it is a man versus a woman?

Mr. REUTHER. In our plant we have seniority lists. In most cases—I wouldn't say most, but I think about half of our cases, we have a consolidated seniority list. In other places we have separate seniority lists. This is a problem which grows out of a kind of community pattern. Some communities are more advanced, some of them are less advanced on the question of the status of women in our society. This is also true of husbands, I am told. Some are more advanced than others.

Representative GRIFFITHS. Thank you very much.

Thank you, Mr. Chairman.

The CHAIRMAN. Mr. Curtis.

Representative CURTIS. First, Mr. Chairman, I have one housekeeping matter. I regret that the representative of the National Council of Independent Unions was not invited to testify before the Joint Economic Committee as has been true in the past. I certainly think we want to get the point of view of the small union leaders as well as of course the viewpoint of Mr. Reuther who represents big labor.

The other thing is somewhat a matter of housekeeping too. I think the record, not just by my stating it, will show that Mr. Reuther's statement of some 64 pages was not available to the committee ahead of time. It will appear in the record for which I am pleased, but it should also be shown that we had no opportunity to read it and that therefore there could be no detailed interrogation on it.

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In following the oral statement which took about an hour and a half, reference was made at times to the statement, but I believe a great deal of material is outside the statement.

Is that true, Mr. Reuther?

Mr. REUTHER. No, it is not.

Representative CURTIS. There was a résumé of what was in the written statement?

Mr. REUTHER. That is right. It does not follow the same sequence in the prepared statement, but it is in the prepared document.

Representative CURTIS. That is very helpful.

Then the other item I would like to mention is that when you appeared before the Ways and Means Committee last year on health care there was a press release, I believe you have one today. You would have no objection to having the press release on your testimony go into the record, would you?

Mr. REUTHER. Not at all.

Representative CURTIS. I would like to have it in the record.

The CHAIRMAN. It may be inserted. We have an understanding that anything that is germane may be inserted by other witnesses or members of the committee.

(The information referred to follows:)

NEWS FROM THE AFL-CIO

Walter P. Reuther, appearing as chairman of the AFL-CIO Economic Policy Committee, today told the Joint Economic Committee of Congress that the United States should study economic planning as practiced in other free nations "which have faced up to and found more adequate answers to some of the problems we face."

Citing France in particular, Reuther noted that countries in Western Europe "with far less resources and far less opportunities" than the United States "have achieved full employment and rapid economic growth while we have merely talked about it."

Reuther praised President Kennedy and his Council of Economic Advisers for taking "a long step forward" toward establishing a national economic policy by utilizing the Employment Act of 1946. Government's responsibilities under this law, he charged, had been evaded for the previous 8 years.

Reuther also praised the three antirecession measures proposed by Kennedy—standby tax reduction authority, standby capital improvements authority and permanent strengthening of the unemployment compensation system. "These measures have been proposed, however," Reuther said, "to deal with the next recession. We believe they are needed now." However, he said, a fourth step should be added—a "flexible workweek."

"We believe that the length of the statutory workweek is not a matter for arbitrary decision," he said. "It should be consistent with the needs of the Nation and the national objective of a full employment economy.

"We urge favorable consideration for * * * amendment of the Fair Labor Standards Act to provide for automatic adjustment of the statutory standard workweek based upon the level of unemployment * * *.

"When industry's need for labor was high, and unemployment correspondingly low, the standard workweek would remain at 40 hours. When industry's need for labor was low, and unemployment correspondingly high, the length of the workweek would be reduced accordingly so as to help create more jobs."

Take-home pay of workers on a shorter week should be maintained through a "national workweek adjustment fund," accumulated by a small payroll tax on all employers, Reuther explained.

Reuther rejected "for the immediate future" the thesis that wage increases should be within the limits of productivity increases.

"Workable balance in the economy between capacity and demand requires a shift in the present distribution as between labor and nonlabor income, as increase in wages and salaries, at least in the immediate future, greater than our normal potential for increasing productivity," he said; otherwise demand for goods will continue to lag behind productive capacity, perpetuating the unemployment problem.

"The rise in the productivity of capital may, in fact, make it necessary for wages and salaries to outpace the rise in output per man-hour indefinitely," he asserted.

The result of a lack of balance at present can be seen in the persistence of unemployment, Reuther pointed out. Although official figures indicate a slight improvement, they "do not take into account * * * the hidden unemployment of those who have given up the hope of finding jobs and are not counted among the unemployed because they are not actively engaged in seeking work," he said. He estimated this group as 1 percent of the total labor force; "taking them into account, true unemployment as of now may be estimated at more than 9 percent of the real labor force."

Reuther opposed as unnecessary the administration's proposal of an 8-percent tax credit for investment in new plant and equipment.

"The urgent need is not—increased investment * * * but rather, a rapid and sustained advance in demand—a sufficiently high level of demand to maintain maximum utilization of a growing and increasingly productive capital stock," he said.

"The question that faces us today is whether we have the vision and the intelligence to recognize the revolutionary changes that are taking place with every breath we draw," he said. "Will we have the wisdom to use them as they should be used to achieve some of humanity's oldest dreams—to eliminate poverty, ignorance and disease—to share abundance among all people—to secure freedom from drudgery while preserving for every man and woman the opportunities for useful, well-remunerated work? Or will we let slip the opportunity to realize man's age-old dream of abundance and allow it to be perverted into a nightmare of dislocation and human hardship by our failure to measure up to the challenge of the technological revolution?

"In planning to meet our human needs we must also raise our eyes to the skies. We must face the fact that the economic and social programs of the past are no longer adequate in the age of automation, space and the atom.

"We must measure what we can do, what we have to do, not by the inadequate yardstick of what we have done before, but by the vast and growing potentialities of the present and the future.

"Our country, which leads the world in wealth and in technological development, must show a new capacity for leadership also for the development of new programs to utilize science, technology, and human skills to share abundance not only among ourselves but among all the peoples of the earth.

"Our greatest danger now is that we may be satisfied with too little. If we let our efforts be weakened by a partial measure of recovery, if we give way before the fears and the opposition of those who would rather look to the past than venture courageously into the future, then we shall not only fail to achieve the goals we might have reached, but we shall be unable to avoid an early recurrence of recession."

Representative CURTIS. The reason for that, I might say, is that in one of my questions I shall refer to the press release.

Now I was very happy and I was very interested in your reference to a technological revolution. You believe that there is and has been one going on, I understand. Is that correct?

Mr. REUTHER. That is right. I think that the rate of technological change is going to accelerate. I think what is going to happen in the next 10 years will be as great as what has happened in the last 50 years. I call this a revolution.

Representative CURTIS. Do you think this has been going on in the past few years or not? Is this something new or not?

Mr. REUTHER. I think it has been going on ever since Mr. Watt discovered the steam engine. I think it is now going on at an accelerated rate.

Representative CURTIS. I believe you have felt that for some time.

Mr. REUTHER. I have.

Representative CURTIS. I share that view, incidentally, but in interrogating some of our economists they refer to our economy as stagnant and tired and going nowhere. That does not seem to conform to these bold words of technological revolution. Would you not agree?

Mr. REUTHER. I think you can have an accelerated forward thrust in the development of new technology and have mass unemployment which represents a stagnant economy. The two things are separate and apart. In other words, the scientist working in a research lab can develop this new electric computer even though there is mass unemployment in the city in which he lives.

Representative CURTIS. You can have problems in a revolution just as well as you can have them in something that is going nowhere but it would be inappropriate in referring to an economy that is having a technological revolution and one that is accelerating as tired and listless and going nowhere.

I agree with you there are problems in this rapidly developing technological society, but I am getting around to one basic question because a lot of this relates to what we call or miscall or do not agree on the term, economic growth. Surely economic growth would encompass innovation and technological advancement, would it not?

Mr. REUTHER. They are two separate things. You can make great technological progress and yet have a situation where the overall economy is stagnant. In the last 9 years the economy grew roughly at a rate of 2½ percent when we think we should have had a 5-percent growth. That in our opinion means the economy was sluggish and stagnant. During that period we made great technological progress.

Representative CURTIS. The point is that the two terms seem to be inconsistent. I might say in regard to those figures, those are the ones you had on your chart where you started with the takeoff point in 1953. Is that an economic year? Why do you choose 1953?

Mr. REUTHER. That is where it happens to change.

Representative CURTIS. That is at the height of the Korean war, too, is it not? Is that the reason you selected that as the takeoff point? What economic occurrence existed in 1953 that you would begin at a time when the country was at war and had high economic activity because of the war? Why did you choose that as you takeoff point?

Mr. REUTHER. That is where the rate of growth had been roughly, the 5-percent growth.

Representative CURTIS. Yes, but you have a war. What economic occurrence other than the fact we had a war economy made you choose 1953? Surely there is a difference in your mind between a war economy and a peacetime economy, is there not?

Mr. REUTHER. Obviously there is a difference. But the capability is not different. Does it matter whether the General Motors Corp. is making tanks or 75-millimeter guns or whether they are making automobiles? I mean the ability to create economic wealth is the measurement and not whether they are tanks or whether they are automobiles.

Representative CURTIS. One of your tests is the fact that you have 800,000 people additional in the armed service and in the period of the 1930's when we had 10 million people still unemployed in 1938 that is just about the number that became employed, if you want to call it employed, in the armed service in the forties. So we had no unemployment.

I am just trying to point out something that I think is very basic, that there is a fundamental distinction between both production and in employment in times of war and in times of peace. I am surprised because we have had this out before, that you can persist in presenting charts that show no difference in your own mind between those two types of economies.

Mr. REUTHER. There is a great difference. We dropped further below; 1950 was a low point.

Representative CURTIS. Yes, but you are trying to talk about settling for a peacetime economy. You are not suggesting that we go to war to solve these things, are you?

Mr. REUTHER. No. We want to build schools instead of tanks. I want to build hospitals instead of military planes and battleships. I don't understand you because if you can have this tremendous growth with 4 million people in the armed services why could we have not greater growth putting them to work making good things?

Representative CURTIS. Because I am asking you about your economic statistics. Why did you not take the year 1945 as your startoff point because if you did then you would show up before the war period, which would be 1950, an actual minus growth. But that is not right because you are going from war to peace. Yet you take from war to peace to try to show us economic growth.

The point I am making, Mr. Reuther—and we have had this out on these kinds of statistics—is that I frankly think they are juggled. They do not give us a fair understanding, going from one war to another war or if we are talking about recessions, measuring from peak to peak or trough to trough. But these figures on economic growth that you present just do not hold up from an economic standpoint. They may do it from a public relations standpoint but I don't know what you are trying to prove. I think all you have proved here is that you do not distinguish between an economy at war and an economy at peace.

Mr. REUTHER. That is just your opinion. You see, it just so happens it seems to me you don't have to have a Ph. D. degree in higher economics from one of the universities to know that we have had three recessions in the last 8 years and that those recessions penalized us by mass unemployment and underutilization of capacity.

Representative CURTIS. You are avoiding the point. I am not talking about that. Let me go on to another point, one on which I agree with you. You say our country, which leads the world in wealth and technological development, I am glad you do feel we lead in something. That is an accurate statement in your opinion?

Mr. REUTHER. I think we lead in many things.

Representative CURTIS. Here is what I want to ask. You then say that probably that is where we have been leading and what we need to do is emphasize more the purchasing power and the spread, as I understand your point. The question I would ask is, Do you feel that by concentrating on this other side you in any way endanger the lead that we do have in these areas that you have so aptly pointed out, in wealth and technological development?

Mr. REUTHER. Quite the contrary because the greatest incentive for the General Motors Corp. to accelerate its technological progress is for it to be able to use 100 percent all the tools it has now. When it has idle capacity there is no incentive to create a more efficient way of doing things. Therefore, I believe a full employment economy will accelerate technological progress and we will move ahead much faster.

Representative CURTIS. How do you think we got to world leadership, because we were not following these series of planned economies?

Mr. REUTHER. I am not prepared to accept the kind of concept that says just because we have done great things we can't do better.

Representative CURTIS. I am not either. I am saying let us examine what has produced this leadership and not be foolish and jump off because we like a lot of things.

Mr. REUTHER. I am not proposing we jump off anyplace. Where did I say we should jump off?

Representative CURTIS. I have asked you to examine that and say we did reach world leadership in these two areas following a different system, one that was not a planned economy. Then you immediately say I don't want to advance any further. Of course I do. But in advancing further I do want to look at what we have got and then see how we can continue to hold that and also move into these other areas. I think you do point out an area of great concern. Unemployment is of deep concern to me. However, I think your theories are going to make things worse, not better, for the very things you seek. That is why I want to examine into some of these details and try to get what I think are more accurate economic statistics and try to interpret them with fairness rather than try to prove a particular point to find out what has caused these.

I see my time has run out. I will have some further questions when the other members have interrogated you.

Thank you, Mr. Chairman.

Mr. REUTHER. May I comment on this question about regimented economy? You see, I am also opposed to a regimented economy. I don't know whether you ever lived under a regimented society. I have. I lived under Hitler. I worked in the German underground against Hitler. I lived in the Soviet Union where I worked as a technician for a period getting a Ford automobile plant in production. So as a human being I am deeply committed to a concept of human freedom and, as a part of that, maintaining a free economy. I know that many times people who favor a free economy are not prepared to accept the social responsibility and the moral obligation that go with freedom and it is their lack of that responsibility that puts into jeopardy the whole of our free society. I don't want a planned economy.

Representative CURTIS. I do not know who these people are.

Mr. REUTHER. The people who fought against social security, who fought against minimum wage legislation, who fought against the Wagner Act, who said if this happened the whole economy would go to pot. They told us when we fought against the 12-hour day we would go to pot if we had a 10-hour day. We had higher living standards and we made greater progress.

It is this kind of negative attitude that I think represents the greatest threat to American freedom and not people who want that degree of planning that is essential to permit the free play of economic forces, to give individual incentive and initiative and individual decision the maximum opportunity.

I think one of the things we need to try to avoid is to get into these cliches. We can disagree about politics and I never question the other fellow's basic loyality to American values. I think that ought to be a two-way street.

Representative CURTIS. I agree with you. We can begin right now by stopping whipping the old dogs.

Mr. REUTHER. You asked me a question.

Representative REUSS (presiding). I think I will not allow you to go further because I think I need to go over to the floor and I would like to have my time now. You can have it on the third round.

Representative CURTIS. I will. You are entitled to it. This is just the first round.

Representative REUSS. You can have it on the second, third, fourth, as long as the lights stay on.

Mr. Reuther, I want to compliment you on the presentation you have made and particularly on your central point, that a country such as ours, which has shown the genious and the ability to split the atom and to be on its way to conquer space, ought to be able to think of economic and social measures by which we can offer job opportunities to the several millions of Americans who are today genuinely and sincerely looking for work, want to work, are able to work, but who cannot because those opportunities do not exist.

I have a number of specific questions. My first question is on a recommendation on monetary policy—and here you may want to interplead my friend, Mr. Stanley Ruttenberg, whose footnotes on monetary policy so enriched the recent economic report of the Commission on Money and Credit.

In your monetary policy recommendation the nub of what you say is one sentence. I will quote it:

> While, in view of the outflow of gold, short-term interest rates must for the time being be maintained, long-term interest rates should be reduced through open-market operations and reduction of the rediscount rate.

At another point you suggest the rediscount rate be lowered from 3 percent to 2¾ percent.

I am with you on that whole sentence except where you talk about the reduction of the rediscount rate. I wonder whether if there you are not paying obeisance to a rather superficial doctrine. I will explain what I mean.

The Federal Reserve, in recent years at least, instead of stating straightforwardly from time to time that money and credit ought to be tighter or looser, as the case may be, has resorted to a play of symbols wherbey it juggles the rediscount rate a bit and expects the sophisticated to draw certain lessons from it.

I personally think this is a very roundabout way of saying things that need to be said, whether they be, as the occasion warrants, in the direction of tightness or looseness.

As you know, the rediscount rate is related to very, very short-term credits. I am wondering whether you really want to seriously press the suggestion that in addition to producing long-term rates through open market operations, which I think is an excellent idea, we fool around with the rediscount rate? If you fool around with it to lower it, somebody the next day can make us good an argument to fool around with it to raise it.

I am still wondering if you are not merely paying an unwarranted tribute to a form of sign language which if it ever had any validity does not have any today?

I do not suggest, Mr. Reuther, that you should duck this one.

Mr. RUTTENBERG. If I might comment briefly, Congressman Reuss, I agree with you that the discount rate really has little meaning in reality in terms of the establishment in setting the rates, but it is an important psychological factor.

Normally we have tended over the years to keep the discount rate slightly above the 90-day bill rate. The 90-day bill rate has been running slightly below 2½ percent until recently when it has gone slightly above 2½ percent. Now there is no reason technically for the discount rate to be much higher, a half percent higher than the short-term rate. But we have been experiencing psychologically a creeping upward, psychologically and in reality a creeping upward, of long-term rates.

Over the last 3 or 4 months we have moved up to a long-term rate of more than 10 years, from a rate of about 3.8 to about 4.7 or 4.8, a significant upward creep. Now psychologically if the "Fed" would step in and reduce the rediscount rate to 2¾ percent this sets the stage for saying we are going to maintain an easy money policy, we are going to pursue a policy of continued excess free reserves in the economy and we are going to pursue a policy of trying to kep that long-term rate down by having the Open Market Committee move in and buy the long-term to keep the long-term rate down.

Representative REUSS. Why talk in this language of flowers? Why would it not be much better for the "Fed" forthrightly to expand its purchases of long-term Government securities in order to lower or, at least, to maintain the interest rate on long-term Government bonds. The effect of this action would be felt in some measure along the entire interest structure. It could be accompanied by a forthright statement that while we want to keep short-term capital here by somewhat higher short-term rates because of the balance of payments situation, we are lowering our long-term rates because we wish to expand home building and capital investment. We are not attempting to convey this simple and straightforward thought by such bizarre and occult means as fooling around with the rediscount rate. I fear that any encouragement given to the "Fed" in doing this, will result next week in their doing something that you do not like, namely, raising it to 3½.

Mr. RUTTENBERG. All I would add to what you have said is that you would change the psychological atmosphere toward a tight money policy, or loose or easy money policy by simultaneously having the "Fed" say all the things you suggest that they say but to demonstrate it physically not only through the announcement of a reduction in the discount rate but to demonstrate it through active participation in the open market buying long-term securities to drive down the long-term rate and increase the level of free reserves in the economy not through the purchase of short-term securities but long-term securities. It is just a question of psychological factor.

The discount rate in America has unfortunately been used at points in time by the Fed to change direction in policy, to announce publicly that we are going to up it or reduce it, change the psychology and the direction in which the money rates will move.

So if we are interested in maintaining it, as the President of the United States has said in his Economic Report, a relatively easy money policy, we can best demonstrate that through the psychological factor we have used in the past by announcement of reduction in discount rate because no harm will be done by this in the terms of outflow of short-term security because the discount rate even reduced to 2¾ would still be in excess of the bill rate.

It is just a psychological problem. I think in reality I would wish we didn't have to fool with the discount rate this way and we ought to do what Canadians do, tie it directly to the short-term, 90-day bill rate and let it fluctuate up and down as the bill rate does. Then you won't have this problem, psychologically.

Representative REUSS. I have one more question, Mr. Reuther. I have several difficulties with your discussion of the length of the workweek, even though I certainly sympathize with what you are trying to do, that is, to put idle men to work.

However, I take it that you are not advocating a mere spread-the-work, share-the-employment program. As you lower the workweek you would like to see that wages go up by an equal amount so that the wage payment to the worker remains what it was before.

Mr. REUTHER. That is correct. In my prepared statement I have this all detailed. I did not want to take the time. We proposed there what I call a wage equalization fund. With a very small percentage of payroll you can spread the cost of the program. Such a fund is necessary because industry will be having the most severe layoffs at a time when business conditions are worst.

We have detailed this. We are trying a new idea. Because we believe that in the absence of this kind of rational approach we are going to create rigidities that will plague us when we need to expand.

Representative REUSS. I realize that the question of whether wage increases tend to create employment or to cause unemployment is one on which respectable economists have differed, and I certainly don't pretend to know the answer.

I would however ask this question: If, at the time when there is unemployment, the profit situation of industry generally is not very good, if there isn't much fat on the bones, and you do lower hours and pay the same total weekly package, you are, in effect, raising wages by some amount. I wonder if you have given us a sufficient analysis of the impact this might have on our balance of payments and on domestic employment? I think these are questions that have to be answered.

I applaud your throwing the issue out. I think it is something that the committee has to think about very seriously. I do not think you attempted to exhaust the subject in your paper here. I would like to hear anything you can say on it.

Mr. WEINBERG. In the prepared statement we detail the provisions we would propose for maintenance of purchasing power when the standard workweek is temporarily reduced. We would not have the employer pay the additional wages. We would finance the additional wages by having a payroll tax in effect over the business cycle in good times as well as bad to establish a fund out of which there would be paid wages for the additional hours that the worker did not work.

In other words, if the workweek was down to 38 hours there would be withdrawals from this fund to pay wages for the 2 hours that the worker did not work so his purchasing power would be maintained as if he had worked the 40-hour week. This we think in part would be offset by the lower cost of unemployment compensation. So the net cost, we think, would be very small.

Representative REUSS. This is a fund not unlike our present unemployment compensation fund.

Mr. REUTHER. That is right. The whole concept is to build up funds during periods of high levels of employment so that when you get a drop off in employment you can maintain your work force in full at a lower number of hours but maintain the same purchasing power by drawing on the fund. If you put that additional economic cost on the employer when he was hit the hardest you would really be accelerating the negative forces and would do great damage. We don't propose to do that. We want to build up the funds in good years and have the reserves to draw upon. These reserves would perform the same function as the funds for unemployment compensation.

Representative REUSS. I take it throughout your discussion of the subject there run two points. One, that granted our present world responsibilities and our present domestic needs, your primary goal would be for a 40-hour full employment week at the present time?

Mr. REUTHER. I would say—I don't speak for the American labor movement, but I certainly speak for myself—if I were able to choose between a lower workweek with full employment at that level or a 40-hour workweek at full employment, I would take the 40 hours because I think we have great unmet needs in America and I think we have overwhelming responsibilities in the world and full employment at 40 hours, I believe, would better equip us to meet our responsibilities.

That is what I would prefer. That does not help the worker who is unemployed.

Representative REUSS. I appreciate that.

The second thought which I should think ought to underlie any disucssion of a reduction in the workweek is the fact that, whether this comes sooner or later, it is perfectly obvious we are, given our technological improvement, going to have to move ultimately in the direction of a shorter workweek.

To the extent that this is true, is it not your opinion that we must do much more than we have to evole constructive use of leisure time in this country for all people, white-collar workers, blue-collar workers, and everybody else?

Mr. REUTHER. I like to think that I am one of the pioneers in that whole concept. I believe that a shorter workweek is inevitable. I think it is a question of how we get to it and under what circumstances. That is why I believe there ought to be a more rational approach rather than one of economic leverage. It ought to be one of economic facts and commonsense judgment. I think we are going to get to a shorter workweek perhaps long before we are, as a society, prepared to use it constructively and creatively.

I think labor and management, educators and all groups, all community organizations, have to begin now to plan. I think some of this has to start in the schools and in the communities. I think we have to really begin to work now to get ourselves prepared because I frankly shudder to think that the shorter workweek and the increased amount of human leisure that that will provide may merely give people more access to more westerns on television. That is a frightening thought in my opinion. I would hope they could learn to use their greater leisure creatively and constructively.

I have said on other occasions that as our technology develops the worker becomes more and more remote from the end product of his effort. Take a fellow in an automobile plant right now. If you blindfolded him before you took him in and you led him to his work station and he stayed there for 8 hours, then blindfolded him and led him out, he could be there 20 years and not know what he was working on. He would not know whether he had been working on automobiles, missiles, or what. As technology robs the fellow of a sense of creation because he is not associated directly with the end product, we are really robbing him, I think, of a very important human sense of satisfaction.

We have somehow to satisfy that in his leisure hours. This means we have some work to do in this area.

Representative REUSS. Thank you very much.

Senator DOUGLAS. Mr. Reuther, I was very glad to see your attention directed to the decrease in the working force. Allowing for a few hundred thousand increase in the Armed Forces, there has been a decrease in the civilian working force of about 600,000.

Now there is another factor which you may have mentioned in your prepared statement; namely that normally at the present time the labor force increases each year from 1.1 to 1.2 million. So that in reality you have from 1.3 million to 1.7 million people who are unaccounted for with respect to their inclusion in the working force or as those who hold jobs.

Now isn't this reflected in nearly all the great industrial cities by the very large numbers of young men and women who are neither at school nor at work?

Mr. REUTHER. That is right. I think that is not only a very sizable portion of the problem; it is probably the most tragic aspect of the problem when the young person is out of school and out of a job. These are the formative years and lack of a sense of purpose and motivation in that period can almost put in jeopardy their whole useful life in the future.

Senator DOUGLAS. I am very glad to hear you say that. In the last few years I have become increasingly impressed with this from my experience in my own society of Chicago. I find in other cities the same thing happens there. These youngsters, not having worked, not being in school, are in a certain percentage of cases forming into wolfpacks and preying on the community.

Mr. REUTHER. That is right.

Senator DOUGLAS. I personally think this is the most explosive problem we have. It has developed really most fully in the last 2 or

3 years when, as you say, jobs have not anywhere near kept pace with the growth of the population.

Now you probably studied the Youth Opportunities Act which has this three-prong approach; namely subsidies to industry to take boys and girls on as apprentices, work for boys and girls in hospitals and schools and locally, and finally of course the Youth Conservation Corps.

I wonder if you have any comments on that?

Mr. REUTHER. I very much favor the legislative proposal. I think it is a very important beginning. I am for doing all of these things, but then again, I think we have to recognize that these are what might be called matters of expediency, that we are trying to plug the hole, that in the long pull there has to be a forward thrust in the economy that generates sufficient growth and expansion so that new job opportunities are created.

If you have a choice between creating a job opening for a young person who is just out of school or for a wage earner who has heavy family responsibilities, you can't make that choice. It is like trying to choose between your father and mother. There ought to be a job for both of them.

Therefore, while we favor all these things, and we support wholeheartedly the President's proposal, we think in the long run the real question is how we can have a dynamic economy that provides enough job opportunities in terms of growth to provide every American able and willing to work with an opportunity to do so.

Senator DOUGLAS (presiding). Thank you very much.

Mr. Curtis.

Representative CURTIS. Thank you, Mr. Chairman.

There are a couple of questions that I want to check out with Mr. Reuther.

In one of the recommendations you suggest that we need to develop mechanisms for planning. I understand it is basic, when I took these notes, that you believe that private economic decisions must be harmonized with public good. Do you believe that they are in conflict? What is your view on it?

Mr. REUTHER. I don't think they need be in conflict.

Representative CURTIS. I do not either. I think they largely go together. But the way you put it, I gathered that you felt there was actually a conflict.

Mr. REUTHER. I don't want to argue about words. I said that I think the degree of social democratic planning that I think we need as a matter of survival, would make it possible for us to harmonize private economic decisions with the general public good and to work out a more rational, intelligent way of allocating our resources and our manpower, giving proper consideration to the things that I call social priorities, education, for example.

I think it is a great tragedy, what we are failing to do on the education front.

Representative CURTIS. We are doing a tremendous job, if you look at it, in education.

Mr. REUTHER. We are doing a tremendous job measured by what we used to do, but measured by the size of the problem we are not.

There is not a city in the country that does not have a serious problem.

Representative CURTIS. Do you not agree, Mr. Reuther, what you should do is take a look at the rate at which we are meeting the problem? Of course we have a long way to go, but let us look at where we have been, too. I do not want to concentrate on the past, but I do want to see whether or not we have been stagnant and the field of education has been one of the most dynamic things in our economy. We have more than doubled, I think it is 2½ times, the amount we spend on education in the past 10 years in the public school sector.

Now maybe it should be more, but let us not act as if we have not been moving very rapidly.

In fact, one of the points that has been raised is your well-taken point on leisure time. One of the great things we find when we analyze the amount of time that the average American spends in school by years is the rapid increase today, say, compared to 20 years ago, compared to back in 1900. Today a college student is almost like a high school student used to be.

In other words, we have moved that much forward. The average number of years an ordinary American spends in school has increased rapidly and needs to; we have to continue.

Graduate study today is not uncommon at all. In fact you ask most college students where are you going to graduate school, not whether you are. That indicates the area.

All I would like to do is relate both what our problems for the future are and the rate in which we are moving forward to meet them. In that way we can tell a little more clearly, I believe, whether the programs we are presently following need to be radically changed or need actually to be moved forward.

This is all based upon your statement that any one who believes we can rely on the private marketplace to make these decisions for allocations you suggest is unrealistic.

Well, I am one who essentially believes that that is the best place. It is the laboratory where we test these things out. Just as you said in your original testimony, no one knows the answer to these questions.

We have to experiment. That is what the private enterprise system to a large degree does, to try out new economic ideas. The marketplace is the place to test them.

So that it comes down to your fundamental conception here. I think we can rely very heavily on this laboratory system to continue to produce this progress that we have been making in increased leisure time, in this technological revolution that you yourself commend, in learning how to do things with more brainpower and less muscle, and in creating an increase in the wealth.

That is the reason I point this out.

Now, one other thing I was quite concerned for you to comment on is this statement of Sylvia Porter. I am going to read that and particularly the Arthur Burns study from which you drew the conclusion indicating there was more of a concentration of wealth in fewer people.

As you said, the rich are getting richer and the poor are getting poorer, which is in contrast to the set of tables that appeared in the 1960 Economic Report. One of them, which I think is a very meaningful table, table C–8, shows real personal income of families, number and percent of families by income group, 1947–55 and 1958. We see a shift of 17 percent of the families used to be under $2,000 and today, or rather, the last figures here were 14 percent. Eighty-three were over $2,000. This is percentage.

Now it is 86 percent.

Then when we get into the next brackets, under $4,000 and $4,000 and over. Under $6,000 and $6,000 and over. Under $8,000 and $8,000 and over. We see a very splendid shift.

From 1947, for example, only 15 percent of our families were over $8,000. Today, the last day they have here, it is 22 percent.

We see another indication in the number of homeowners where it is well over 70 percent. Those are economic statistics that I think bear directly on this question of the spread of wealth. As I say, I will read the Arthur Burns views on this because I would be very surprised if we had this change, that this is any real indication that this is so.

I thought one of the good things about our economy was this better spread.

Another thing they have here, number of automobiles per capita and so forth. There are a number of these kinds of indicators that attempt, at any rate, to reveal to us what is the well-being of our people and whether it is well spread or better spread.

I agree with you there are great areas for improvement, but, again, I want to relate this to what has been so that we can see whether we are moving forward, at what rate, and whether or not we are stagnant. I am convinced that every indicator shows we are far from stagnant.

This economy of ours has just been moving in an amazing way, but it does not show up in certain economic indicators.

Mr. REUTHER. May I comment on this last point?

Representative CURTIS. Yes, please.

Mr. REUTHER. I think where we differ on this is that you are citing the rising level of incomes, and it is true. More people now are getting above a certain level and there are more homeowners. There is a difference between the rising level of income and distribution of income. With respect to the distribution of income, there was a marked shift in the years that followed the New Deal. There was a more equitable distribution of income and wealth, and now we have reversed that again.

Let me show you this study that came out of Mr. Burns' national research group. In 1922, 1 percent of American adults held 31.6 percent of the wealth of America. In 1929 it was 36.3. In 1933, it was 28.3. In 1939, it was 30.6. It started to go down. In 1945 it was 23.3; in 1949, 20.8; in 1953, 24.2; in 1956 it was 26. Now in 1961 it is 28 percent.

These are the latest figures on this. So we came down. Now we are starting to go up again.

Representative CURTIS. Those are interesting figures, but the ones I quoted to you were actual distribution. Families under 2,000, and this is percentage and actually the top figures which I do not read show the number of families. Those under 2,000, over 2,000, under 4,000, over 4,000. So we are talking about wealth distribution.

Mr. REUTHER. Excepting that is the rising level. This is a question of other people rising faster. This is distribution.

Representative CURTIS. Well, this is distribution. You take a figure of——

Mr. REUTHER. We are talking about two different things. You are talking about more people getting more income. I agree. But the rich are getting a higher percentage than they used to.

Representative CURTIS. You are picking out a very small segment, which is 1 percent. All of these statistics you give, Mr. Reuther, bear on the question we are discussing, so do the statistics I give bear on it. I do not think any one set of these is going to give us the picture. I think we have to look at these and some others, too, to understand where we are and also how we have moved.

I think my statistics that I have quoted here may bear more on the question we should be concerned with than the ones Mr. Burns uses although they are significant and certainly pertinent. That is why I said I wanted to look at them. I do believe that we need to have probably a selected series. Maybe the selected series in this report were not as good as others could be. Maybe others could suggest some. But there are some series of statistics that would be helpful in showing where we are going, whether or not there is a better spread. I think there is, and it is important to us to know whether there is.

Mr. REUTHER. You see, what bothers me about education is that it is the one thing you cannot defer. You can defer building homes for a few years and build a few more later on and catch up. You can defer building automobiles. In a few years you can put on a night shift and build some Chevrolets. When you fail to educate a young person—and we are losing each year 200,000 of our best high school graduates who cannot go to universities—they cannot go back on the assembly line later on. They are lost. It is a permanent loss in their lack of opportunity to grow and develop. It is a social loss in terms of the fact that they are less useful citizens for the rest of their lives.

Representative CURTIS. I could not agree more with your conclusion but the one thing I do disagree with is your premise that there is a lack of opportunity. It is a strange thing that some of these able high school graduates lack motivation, and I do not know why. But if you get into it and talk to people who are in this field, and I happen to deal in this constantly in some of my other work, so I have followed this, sometimes it might be lack of opportunity, but by and large it is lack of motivation that they do not go on.

I agree with your conclusion in the field of education, that is the last question, kids are kids just a short period of time, but there is a lot more to it than money. I think we are beginning to learn that.

This is one reason I am so much more interested in loans being available and not so much interested in scholarships.

Mr. REUTHER. There is more than money involved but money is essential.

Representative CURTIS. I do not think it is lack of money that is the real problem here. I think it is something more fundamental.

I have one final question. On your proposal for creating the mechanisms, as you describe them, for planning our economy, do you not feel that that would require, whatever mechanism, some sort of constitutional amendment?

Mr. REUTHER. No, I do not think so. I would not suggest that we borrow what anybody else is doing because I think there is a special kind of genius in the American character that we can summon to work out our own approach.

I would like to suggest that we might learn from what other people are doing. France has a mechanism. It is not regimenting their economy.

The Swedes do it one way. The Danes do it another way. Great Britain under a Conservative-Tory government does it another way.

I just happen to believe that a measure of planning is essential to preserve our free enterprise system. If we do not have that degree of planning, then instead of the planning putting the system into jeopardy the lack of planning will create a situation in which social and economic problems that result from neglect will be so great that there will be pressures that might threaten some of the freedom that otherwise planning might preserve.

Representative CURTIS. Do you think that that can be done within our constitutional structure?

Mr. REUTHER. No question whatsoever in my mind.

Representative CURTIS. But if it required a constitutional amendment, certainly you would be willing to move forward and suggest a constitutional amendment so that it could come about?

Mr. REUTHER. I am certain in my own mind that it does not require that because it is not a question of structural change in our society. What is required is essentially a mechanism to facilitate a more effective implementation of the established national policy, the Employment Act of 1946. The goals are all there but we have no method to implement it. That is why we get into trouble.

Representative CURTIS. Do you think what we have been doing in this fiscal and monetary policy can be done within that concept of the Federal Government's power in those two areas?

Mr. REUTHER. I think that is a very important area. I think a great deal can be done in the areas of fiscal and monetary policy. I think, however, that there are areas that need to be influenced outside of that more narrow area. Therefore, I would suggest something that goes beyond that.

Representative CURTIS. Of course, we are talking about mechanisms. If one is implemented that would mean specific legislation for specific areas of spending.

But I am concerned about your use of the word "mechanism."

Mr. REUTHER. Let us call it an "agency."

Representative CURTIS. I wonder if a mechanism to do this would not require a constitutional amendment?

Mr. REUTHER. I very deliberately did not want to come in here with a preconceived concept. I think the Congress might perhaps request some study by the Council of Economic Advisers. I have enough faith in the judgment and the good sense of America to think we can do this job and preserve our freedom and make our free enterprise system work more effectively and enable us to do a better job.

Now, certainly we now have a minimum wage law. That represents a kind of decision that we are not going to let people in certain areas of our economic life fall below a certain level. We have insurance now to protect bank depositors. We have regulations through the SEC. All of these things reflect a general sense of the need for doing something more than merely let free market forces operate.

Representative CURTIS. These are to preserve the free marketplace to a large degree.

Mr. REUTHER. That is why I am proposing this, so that we do not rely exclusively on it, so that we can protect the free marketplace.

Representative CURTIS. I have the same faith that we can do it. I would have serious question from our previous discussions of various matters what you would think was part of the free market mechanism and encouraging the private enterprise system. But I think we could always debate those out with some intelligence. I tend to disagree with your collection of ideas and actually feel they will impede the very things that you are seeking.

Mr. REUTHER. Take social security. Why did we enact social security? Why didn't we leave that to the private insurance companies?

Representative CURTIS. I tell you one thing, Mr. Reuther, and I warn you people on social security, that it has not matured yet. It will not mature for another 60 or 70 years. We all knew that it was going to work well the first 20 or 30 years because the people going on it were going to get a hundred dollars out for every one. The test of social security, and it is a validity, it is going to come in 1970 and 1980. We have to stop playing politics with it and reexamine it.

Mr. REUTHER. The group of actuaries that make a kind of periodic review of the actuarial soundness of the social security fund disagree with you.

Representative CURTIS. Wait a minute.

Mr. REUTHER. That is the way I read it.

Representative CURTIS. You had better read again the premises upon which they make their statements. It is these premises that I am pointing out or trying to point out to people, that we had better pay attention to.

I just spent a lot of time on some of these things.

The people who have cautioned you and others in the past on some of these programs were not against human progress or human beings. In fact, they are for them just as much as you are. We are deeply concerned about the techniques and how we do it and we can be wrong and you can be wrong and I could not agree with you more. Let us get away from the epithets.

Mr. REUTHER. You do not believe that social security robbed people of the sense of their independence, dignity and self-reliance, yet we had pay envelopes stuffed with that kind of propaganda, back in 1936.

Representative CURTIS. Mr. Reuther, if people were to judge you by the kind of propaganda you put out, I would not be talking to you, but I know there is more in what you have to say than propaganda. I do not judge them by their propaganda, either. I do not happen to agree with either one.

I am talking about this. These people were concerned and are concerned about human welfare just as you are. They have different concepts. If we can keep these things on our level of debate where we both agree we are interested in human things, we do better and the argument is what programs are best suited to do it.

I will chide them when they accuse you of being a Socialist and I do when they say the issue is the specific case or the area we are talking about. Let us get on with it. I do not think either you or I or a whole group of people are going to come up with the correct answer.

Mr. REUTHER. I think we ought to keep working at it, though. I have unlimited faith in the capacity of freemen and our free institutions. I think we can beat the Communists if we work at it.

Representative CURTIS. I think you are underestimating a lot of people in the society. We are all working at it. You are contributing and I am testifying to the fact that you are. So are the people you chastise, they are working at it.

Mr. REUTHER. I am not suggesting that they are not. I am suggesting we ought to work harder together at it. That is the difference.

Representative CURTIS. Thank you.

Senator JAVITS. Mr. Chairman, could I indulge Senator Pell to give me 2 minutes? I have been running in and out all afternoon and I have to go somewhere else.

Mr. Reuther, I am terribly sorry you happen to have caught me on a very bad afternoon. I wanted very much to hear your presentation which I think is tremendously important. I certainly wanted to be informed. I will read this with the greatest care. I just wanted to tell you that.

With Senator Pell's indulgence, I would like to ask only one question that troubles me. That is the challenge presented by automation. I appreciate your prescription for it but I still do not think that is a fundamental prescription because even if you had your growth rate, and so forth, this automation thing is moving so fast that you are presented with tremendous challenges in terms of the utilization of manpower, in terms of hours, in terms of compensation. I think this thing will run away from your 5-percent growth rate at a 40-hour week, let us say. This is an enormous national issue and, with all respect, and I do not have to give my qualifications as to my understanding of labor's problem, I do not think it is doing labor any particular good to go the "let's reduce the hours road, because there are people unemployed" alone. That is pretty much all that most of us have heard.

So, I wonder if even now or on some other occasion it would not be a good idea to lay before the country what is labor's prescription, unless you have already done it here.

Mr. REUTHER. You missed my section. I think if you will read my testimony, you will find that I am in essential agreement with your remarks.

Senator JAVITS. I would like to see it and I will do my best to digest it in connection with my views on the President's report, and work on labor's prescription for meeting this enormous opportunity and challenge of automation.

You feel that is covered here?

Mr. REUTHER. I think that I covered it, not completely, but I think in broad outline you will find that we have come up with what represents a realistic approach. On the short workweek, I made it very clear. I happen to believe as an individual that if I could have a choice of having full employment at 40 hours so that we could create the abundance that would make it possible to meet our needs at home and our responsibilities in the world, I would prefer that.

I think the most serious problem we face in the labor movement today is the problem posed when there are two workers and one job. Unless we start working to find a rational answer to that, there are going to be great pressures and you are going to get the sort of thing that happened in New York City on the hours.

It seems to me this is not the way to do the thing in terms of the whole country.

I hope the idea we propose will be given consideration and I recommend it to your reading.

Senator JAVITS. I will certainly do it very carefully. I hope you will excuse me for seeming to give you less time than you more than deserve but I will make it up in my homework.

Mr. REUTHER. Thank you.

Senator JAVITS. Thank you, Senator.

Senator PELL. I, too, would like to congratulate Mr. Reuther on a lively and articulate presentation.

I guess you would agree with me that perhaps Mr. Wilson was correct when he said "what was good for General Motors was good for the United States, too"; only it is possible he did not know that what was really best for so large a consuming public was money to spend. I am wondering if you would agree with that thought?

Mr. REUTHER. You know, Mr. Wilson was a friend of mine in a very unusual kind of way. I did have great respect for him as an industrialist because I think he had a lot of managerial skill. I think he was very naive as a politician and I think he got in trouble down here quite quickly.

I happen to believe that if all of the American people had adequate purchasing power and had the opportunity to share in the great abundance that is now possible and within our reach, this would be good for General Motors because they could sell more cars, their profit would be higher, they could get greater utilization of their capacity, they would have more opportunities to invest their idle capital and, in a real sense, I think Mr. Wilson was really trying to say—although he did it badly and got in trouble—that progress is a kind of indivisible thing, that while temporarily one economic group may seemingly have an advantage at the expense of another group, eventually they will pay the price because the whole country gets in trouble and nobody can escape that.

Therefore, social progress and economic progress are almost as indivisible as peace and freedom. You can have them to yourself only as you can share them with everybody in the world community.

Senator PELL. In the close of your testimony you mentioned we were still in the recession, not completely out of it. Would you enlarge upon that thought a bit?

Mr. REUTHER. I think if you look at the level of unemployment in the past when we were in recession, you will find that we now have levels of unemployment equally great and therefore I think that we are kidding ourselves if we say we are out of the recession.

We have made progress from the low point of the recession but we are still not out.

You can see what has happened. Each time the unemployment plateau, at the end of the recession, gets higher and higher. We leave behind as many unemployed as we had at the peak of the recession in the earlier period. When we take the 5.8, which is the current figure, the January figure, seasonally adjusted, 5.8 percent of the work force, and you add what I think is a conservative number, the 750,000 who got lost in the shuffle, and make allowances for the partially unemployed, who are equivalent to 2½ million totally unemployed, the rate rises to 9 percent. That is much higher than we had at the bottom of many recessions.

Senator PELL. Have you included in that the people who will be released from the military services?

Mr. REUTHER. That is right, we are going to get some of those people back. So there is no reason for complacency and there is no reason for caution.

What we need is bold action. We agree generally with the President, we support him, we are thankful for what we believe to be the affirmative leadership he is giving. I think that, as a human being, he is deeply committed and sensitive to these human problems. Yet we say very frankly, "Mr. President, what you propose is good excepting that one tax proposal. But it is not enough."

Senator PELL. Along that same line, you mentioned in your testimony a standby proposal for public works. Are you familiar by any chance with the bill that we are considering in the Senate Committee on Labor and Public Welfare which calls for more advanced programing along the same line?

Which proposal would you prefer, the one we are considering or the one mentioned in the President's message?

Mr. REUTHER. I think that is a more adequate bill. There is now in existence, I am told by people who should know, a large shelf of public projects at the local and State community level that can be gotten in motion very quickly. They have been engineered and all the preparatory work has been done. So that if we got the matching funds, we could get these things in motion very quickly and this would create increased job opportunities. We think, however, that the time schedule is wrong. We ought to apply that program now rather than save it as a kind of work shelf project for the next recession, the next downturn.

Senator PELL. The essential difference between the two is that the bill we are considering gives more leeway as to when it may be put into effect, and could be put into effect when we saw that the situation was going sour.

On the other hand, the President's bill is more, I think——

Mr. REUTHER. In the future.

Senator PELL. A bit more restrictive. You would support our bill?

Mr. REUTHER. That is right.

Senator PELL. In connection with the investment credit, would you go along with the investment credit proposal if it applied only to marginal industries where there is real need to get new equipment or do you blanket your objection to correct the investment credit to all industries?

Mr. REUTHER. Obviously, our attitude would be more sympathetic if the marginal companies were getting the relief and they needed it and this would mean the difference between capital expansion or not.

We think, however, since the tax thing is a very delicate area and since the Government is wrestling with the whole problem of trying to achieve a balance in the budget, that this billion and a half dollars that this bill proposes is money that we cannot afford to lose in terms of revenue and it would be going to the wrong people.

I would think that the number of companies in America who really would invest or not invest based on this tax allowance would be rather microscopic to its impact on the overall economic stituation—would not be considerable.

Senator PELL. Many of us would disagree with you and actually think that this might produce a real increase in purchasing power.

Mr. REUTHER. The big lag is in the basic industries where there is presently available adequate capital for investment but where there is large unused capacity.

Senator PELL. The point you have touched on is that there is no incentive to buy the equipment. Under this investment credit program, there is a very real incentive to use that capital which is piled up for the purchase of machinery.

Mr. REUTHER. What basic industry in America now needs to be expanded because the present capacity is being crowded?

Senator PELL. Put it another way, in the textile industry which is a concern in my own part of the country, if they had new equipment I think their problems would be eased.

Mr. REUTHER. Yes, and if you got more efficient mills you would have fewer workers employed. This is the nature of the animal. It is a difficult problem.

Senator PELL. Another question in connection with your views on the President's trade expansion program. In general, as I understand it, you support it fully?

Mr. REUTHER. Let me say this, while there is division in the American labor movement—and this is understandable as there are divisions in the business community, people somehow have to live with their own problems—the AFL-CIO, as an organization, will support the broad outlines of the President's economic trade program. We do that because we recognize that there must, of necessity, be developed closer economic relationships within the free world alliance. This is inescapable. It is part of our requirements for survival. Therefore, in general, we support the President's proposal.

I have been asked by Congressman Mills to testify. I intend to do that. Mr. Meany, I think, has been asked to testify and I think he intends to testify.

We would like to say, however, that we have got to recognize that the degree of economic integration that perhaps is essential and desirable and necessary between the U.S. economy and the economy of the free world cannot be achieved without very serious problems in terms of the American economy if we try to achieve that integration under circumstances of full employment and in some cases a shortage of labor in other countries while we have large pockets of mass unemployment in our basic industries. Therefore full employment is essential in facilitating the maximum integration of the free world economy.

Senator PELL. To carry your thought one step further, would you agree with the view that the President's trade expansion proposal is fine, provided there is more substantial trade adjustment legislation than presently proposed?

Mr. REUTHER. Obviously; when we appear we are going to emphasize the need for building into the legislation adequate safeguards to protect communities and workers involved where the trade program will cause dislocations in the period of transition.

Senator PELL. Do you believe that the President's trade adjustment proposals are sufficient?

Mr. REUTHER. I think our statement points out that we think they ought to be strengthened.

Senator PELL. I agree with you wholeheartedly. You feel that the present trade adjustment proposals are not in any way sufficient as yet?

Mr. REUTHER. That is our point of view.

Senator PELL. I have a final question. In connection with labor pension and welfare funds and the problem of investment of the capital, do you have any views with regard to the really conservative and really stagnant investment policies that have been followed, where a good part of the funds are invested in bonds and mortgages and less than 50 percent in the industry of our country?

Mr. REUTHER. The nature of pension funds is such that obviously there have to be regulations so that they do not wind up in highly speculative ventures, and so forth.

I think the point you make is a valid one. I think if you could get a sort of pooling of the risk you could then afford to divert a larger percentage of those funds into areas that would encourage growth and expansion without undue risk to the particular group.

If, however, the group involved absorbed the total impact of a catastrophic shift in the economy, then I think that would be unfortunate. I think the problem can be met and I think the point you make is a valid one that is worth exploring.

Senator PELL. Do you feel also that when the funds are regulated or supervised they should be supervised—or reviewed might be a better term—by people with imagination so as to see what direction the investment policies for these funds are taking?

Mr. REUTHER. I think that is true. I am for imagination in all efforts.

Senator PELL. I query whether the present management of the funds have demonstrated that imagination. Actually, I incline toward the view that if these pension funds were scrutinized by the Securities and Exchange Commission or the Federal Reserve Board greater imagination in investment policy might result.

What would be your views as to the management with the most imagination?

Mr. REUTHER. In our industry with few exceptions—I think in round figures the Big Three in the auto industry have roughly a billion dollars in their pension funds—our union has no voice in the administration of funds. They are administered by trustees chosen exclusively by the company. Chase National Bank happens to be one of the trustees for one of the big funds. They administer them.

Senator PELL. Only 2 percent of the funds of the country are managed directly by the unions. All of the rest are managed by trustees?

Mr. REUTHER. Taft-Hartley requires joint administration but there perhaps are some situations where the measure of management participation is rather small but the great bulk of the money is administered by trustees chosen by the company. We have never gotten deeply involved in that because that raises all kinds of ideological questions.

Senator PELL. Do you have any positive suggestions as to how these funds could be put more directly into the investment flow of our country?

Mr. REUTHER. We have been trying to influence the judgment of management as to investment areas. I feel very strongly, for example, that the pension funds of the Ford workers ought to be invested in part in a way that would help them get better housing. It ought to help give them security in their old age, within the framework of proper investment safeguards. We criticize some of these pension funds. Moneys are being made available to build speculative housing for people who are not in the fund and yet housing for the workers whose money is involved is being neglected. It is that sort of thing which needs exploring.

Senator PELL. As a matter of policy, do you believe these funds should be used for investment in housing and mortgages or would you be opposed to that?

Mr. REUTHER. I am in favor of using these funds in broad areas, including housing, because the pension funds already represent a very sizable portion of the available investment funds in America and in a few years they will be tremendous, of course. We, therefore, have to put them to broader and broader use in terms of the need of the whole economy, but I would also insist that it be on a basis of sound investment policy.

Senator PELL. I would like to see pension fund policies more closely resemble those of the great universities, foundations, and trusts who often place 60 to 75 percent in common stock rather than the pattern followed by most of the workers' pension funds which is the most conservative investment pattern today.

Mr. REUTHER. I think, as in the case of anything that is new, you tend to start out on a very conservative basis because there are a lot of unknown factors. I think we have learned a great deal.

A few years ago, when we negotiated our first pension programs, one of our difficulties was that there was so little knowledge of this new field. Unknown factors caused great problems.

I think we have learned a great deal. As we learn, we feel more secure, then perhaps we will be able to relax some of these ultraconservative investment patterns and do the sort of thing you are talking about.

Senator PELL. Thank you very much.

Representative CURTIS. Could I have one point to do some reverse lobbying? This pension plan discussion is what motivated me.

Mr. Reuther, I introduced a bill today to permit pension funds to be able to fund for health insurance for the pensioners. I was surprised to learn that the pension plans cannot have health insurance for the pensioners. They lose their tax exemption.

It struck me that this was very logical area that they ought to be in. Many of the people who handle the fund and economists have told me they would go into this field immediately if this were permissible. My bill simply makes it permissible.

I just wanted to take this opportunity to call it to your attention. If it does look like it is a sound thing——

Mr. REUTHER. Would you be kind enough to give me the number of your bill?

Representative CURTIS. I do not have it. I just put it in the hopper today. I will drop you a line and send you the statement I made on this.

Mr. REUTHER. I appreciate that very much.

The CHAIRMAN. This concludes the formal hearing.

Thank you very much, Mr. Reuther.

We will meet tomorrow at 10 o'clock in room 1202 of the New Senate Office Building to hear the testimony from representatives of the three major farm organizations.

(Whereupon, at 5 p.m., the committee recessed, to reconvene at 10 a.m., Thursday, February 8, 1962.)

JANUARY 1962 ECONOMIC REPORT OF THE PRESIDENT

THURSDAY, FEBRUARY 8, 1962

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

The Joint Economic Committee met, pursuant to notice, at 10 a.m., in room P–63, the Capitol, Representative Wright Patman (chairman) presiding.

Present: Representative Patman (presiding), Senators Douglas and Pell; Representative Curtis.

Chairman PATMAN. The committee will come to order.

This morning we continue hearings on the Economic Report of the President. We have with us this morning distinguished representatives of national farm organizations: Mr. W. E. Hamilton, director of research for the American Farm Bureau Federation; Mr. Angus McDonald, assistant director of the Legislative Services Division of the National Farmers Union.

I do not believe Mr. Newsom has arrived yet.

I see that Mr. Denslow is here, representing Mr. Newsom.

What is your capacity, Mr. Denslow?

Mr. DENSLOW. (L. Alton Denslow, associate legislative counsel, the National Grange.) I am associate legislative counsel.

Chairman PATMAN. Well, we will permit you to file this, if you would like to. Would you like to do that?

Mr. DENSLOW. All right. Mr. Newsom expressed his regrets, but his official duties conflicted, and he just could not get away.

Chairman PATMAN. That is all right. We will make that part of the record.

(Prepared statement presented by L. Alton Denslow, associate legislative counsel, the National Grange, follows:)

STATEMENT OF THE NATIONAL GRANGE—PRESENTED BY L. ALTON DENSLOW, ASSOCIATE LEGISLATIVE COUNSEL

The Grange appreciates very much the opportunity of being permitted once again to participate in this panel and to present to this committee its views with respect to our national economic goals and policies from the standpoint of the rural American.

At its 95th annual session held in Worcester, Mass., last November, the National Grange reemphasized the urgent need to bring home to our fellow citizens in other walks of life the fact that the American consumer is buying more and better food for a smaller part of his disposable income than ever before; that he is getting more food for less hours of his labor than are the consumers of any other country in the world; that agriculture, through its tremendous capacity and willingness to produce in abundance, is one of the principal cornerstones of our unparalleled national prosperity; and that the present level of per capita net farm income at less than half the national nonfarm average is, therefore, a situation which cannot, and in fairness must not, be tolerated longer.

Yet, notwithstanding the fact that it is the segment of our society which has demonstrated the greatest growth in productivity, agriculture continues to be a depressed segment of our economy. It is, therefore, imperative to have economic policies which will permit this great productivity to be utilized and to return to agriculture some of the benefits of its high degree of efficiency.

It is becoming increasingly clear that even though American agriculture must face some production adjustment, the simple reduction of acreage or of production quotas or goals will not, in itself, solved either the income problem of farmers or the food and agricultural problems, either of the United States or of the non-Communist world. The world needs food and fiber in ever-increasing quantities and it is essential that we leave no step unturned to insure that American agriculture will have equality of opportunity to compete for new and expanding foreign markets on the basis of its productive efficiency.

Since the enactment of the Reciprocal Trade Agreements Act in 1934, the National Grange has consistently supported the principle of expanding international trade through the mechanism of trade agreements, under which tariffs and other barriers to trade could be progressively reduced or eliminated on a reciprocal basis, thereby providing for a freer and more equitable access to the markets of the world. We believe, however, that far more vigorous action on the part of our Government is needed to bring about the elimination of discriminatory trade restrictions which are being maintained against U.S. agricultural products by many of the friendly nations of the world. These restrictions came into being and were tacitly accepted by the United States following World War II because of the so-called dollar shortage which existed at that time. This dollar shortage no longer exists in many nations of the world. On the contrary, their dollar and gold positions are sound and their currencies are strong, but these restrictions are being continued in effect.

In view of the greatly improved economic position of these countries, it is obvious that these discriminatory restrictions against U.S. agricultural commodities are totally unjuistifiable and should be removed with all deliberate speed. Not only should the discriminatory restriction by eliminated but a vigorous policy should be adopted and put into action by our Government to prevent the erection of new barriers to trade which are threatening to arise from the development of the European Common Market.

The Common Market would employ various import control measures including increased duties, variable import levies, import licenses, quotas, minimum gate prices and similar measures designed either to exclude outside agricultural imports altogether or to price such imports above domestic prices, thereby relegating the United States and other exporting countries to positions of residual suppliers. In addition to preempting its market behind and exclusionary wall, it proposes to embark upon a system of export subsidies to secure for Common Market members "a fair share of international trade." Although the General Agreement on Tariffs and Trade recognizes and permits the formation of customs unions, it is clear that it was intended that such unions should result in the broadening of trade rather than providing a mechanism for the establishment of protectionist and trade restriction policies.

The exclusionary device used would not be the same with respect to all commodities. The effect, nevertheless, would be substantially the same. The Common Market area presently represents our principal dollar market for agricultural products. About one-fourth of U.S. agricultural exports went to this area in 1960. The exclusionary device of a variable import levy would be applied against poultry, livestock products, wheat and feed grains. Imports of fruits and vegetables would be regulated through import tariffs, with additional authority to restrict or suspend imports. Tobacco imports would be restricted by sharply increased duties and preference for tobacco exporting countries associated with the Common Market countries.

The effect of these proposed measures can easily be illustrated by their impact on U.S. poultry exports. Poultry is produced in the United States under our free enterprise system without price support or subsidy. By reason of its efficient production, high quality and promotion, it is demonstrating its ability to compete and to develop markets in the Common Market countries—not at the expense of local production or imports from other countries—but largely through the development of new consumption. Under the Common Market proposals U.S. poultry would lose this market.

These restrictive measures stand out in sharp constrast to the privileges and benefits in our markets attained by the Common Markèt countries under the GATT. Equalization fees which are authorized under the Tariff Act of 1930 were suspended by virtue of entry into the General Agreement on Tariffs and trade. In addition, our tariffs have been reduced to about ont-fifth of what they were, and the limited import measures employed with respect to agricultural products are dependent upon a waiver and exception under the GATT and are limited primarily to the protection of Government programs involving a curtailment of production.

This growth of nationalism on the part of our friends designed not only to exclude from their markets our farm products in the production of which we have achieved the highest levels of efficiency, but also to expand their own less economic agricultural production behind new barriers is, in our opinion, not fully appreciated as the grave threat to the well-being of our agricultural and total national economy which it in fact is. It is certainly inconsistent with and diametrically opposed to the reciprocal and multilateral foreign trade policy which we have been following now for many years. The principle of reciprocal trade is insupportable, however, if it applies only to the industrial segment of our economy. We cannot hope to have a prosperious total economy in this country if agriculture is depressed because of the insufficiency of existing markets and is excluded from the opportunity to develop new and additional markets in which it would otherwise compete. Yet the trade barriers persist, and, notwithstanding their inconsistency with the principles of GATT, we can see no strong force within our Government, with the single exception of the Secretary of Agriculture, insisting on adherence to these principles as respects farm products. We in the Grange believe that the time is past due to see to it that the benefits of our reciprocal trade policy shall be made available to agriculture as well as to industry, and that, failing this, we must perforce take a new and hard look at that policy to determine whether a radical change in concept is not required.

Finally, we should like to call the attention of this committee to the fundamental fact that it is our exceedingly efficient American agriculture and its tremendous capacity to produce which may very well prove to be the spring from which our way of life will draw its ultimate strength to endure and to prevail over other ideologies which are seeking to undermine and supplant it. The non-Communist area of the world needs to be strong, and this depends in large part upon a strong United States. Such strength cannot but be seriously impaired if the products of American agriculture are excluded from operation of the principle of expanding trade, multilaterally among the free nations of the world on the basis of economic efficiency, comparative advantage, and a proper allocation of resources through a lowering and removal of barriers to trade.

Chairman PATMAN. We will hear the opening statements of each of the witnesses and then ask questions.

Mr. Hamilton, you may proceed in your own way.

STATEMENT OF W. E. HAMILTON, DIRECTOR OF RESEARCH, AMERICAN FARM BUREAU FEDERATION

Mr. HAMILTON. Thank you, Mr. Chairman.

I am W. E. Hamilton, director of research of the American Farm Bureau Federation, with headquarters in Chicago.

The American Farm Bureau Federation is a general farm organization with approximately 1,600,000 member families in 2,674 county units in 49 States and Puerto Rico.

Farm Bureau members are interested in a wide range of economic policies not only as farmers, but also as citizens, taxpayers, and consumers. Accordingly, we appreciate this opportunity to present brief comments on the Economic Report and related messages recently submitted to the Congress by President Kennedy.

In the Economic Report, President Kennedy cited four major "goals of economic policy" as follows:

Full and sustained prosperity without inflation.

Economic growth.

Equal opportunity.

Basic balance in international payments.

These are worthy goals and Farm Bureau fully subscribes to them. We find, however, that we are in disagreement with a number of the ideas and recommendations presented to the Congress in the Economic Report and other Presidential messages. In such cases, the underlying cause of our disagreement appears to be a basic difference in philosophy with respect to the appropriate role of the Government in economic matters.

As we see it, the basic responsibility of the Government with respect to economic matters should be to create a favorable climate for the private initiative, enterprise, innovation, savings, and investment that are essential for economic growth and development. Numerous sections of the Economic Report appear to reflect a philospohy that it is the responsibility of the Government to guide and direct private economic activities, rather than merely to improve the climate for such activities.

Farm Bureau's position is not a call for "laissez-faire" or an argument that "the government that governs least, governs best." The Government's responsibility for creating a favorable economic climate is a heavy one. Among other things, it requires—

Tax policies that raise needed revenues without acting as an undue drag on economic activity.

Fiscal and monetary policies that contribute to a relatively stable general price level to avoid the painful economic and social disruptions that inevitably result from inflation and depression.

Regulatory and antitrust policies that prohibit unfair practices, prevent the exercise of monopolistic powers, and encourage widespread, effective competition.

Trade policies that facilitate the expansion of trade with other nations on the basis of mutual advantage.

Another basic reason for our disagreement with some of the recommendations in the report involves questions of relationship between the National Government and the States, and also between the executive and legislative branches.

The principal recommendations discussed in detail in the Economic Report would, in the words of the President:

(1) Provide standby power, subject to congressional veto, for temporary income tax reductions, (2) set up a standby program of public capital improvements, and (3) strengthen the unemployment insurance system.

We have misgivings with respect to all three of these proposals.

We agree that it is appropriate, under certain circumstances, to reduce income tax rates temporarily as a stimulus to the economy. Our opposition to the President's request for discretionary authority to adjust tax rates arises from our belief in the importance of maintaining constitutional checks and balances between the executive and legislative branches of Government. The Constitution not only assigned the power to determine tax rates to the Congress, but also provided that all tax legislation must originate in the House of Representatives. We cannot agree that the proposal for discretionary executive power to change tax rates does not represent a fundamental departure from the system of divided powers envisaged by the authors of the Constitution.

While it is argued that the proposed discretionary power would be used within a framework established by Congress, the ultimate effect almost certainly would be to reduce congressional control over both the rates and structure of our tax system, as well as to reduce the responsibility of Congress with respect to such things as the relationship of Government revenues to expenditures, and the size of the national debt.

If the Congress feels that the question of changing tax rates to influence economic activity should be handled more expeditiously than it has been at certain times in the past, we are confident that it can find ways of accomplishing this objective without relinquishing its constitutional responsibility to determine tax rates.

The proposed standby authority for the President to increase spending on public works appears to reflect the depression psychology of the 1930's In our opinion, it is undesirable on a number of grounds, including the fact that it would mean another transfer of congressional responsibility to the executive branch of Government.

As a general rule, we believe that tax reduction is preferable to increased spending if either is to be used to stimulate the economy. However, the need for stimulative action, and the relative emphasis to be placed on changes in revenues and expenditures are matters that involve legislative as well as executive responsibility.

The amounts initially proposed under the standby spending proposal appear to be too small to have much effect on the economy, and it would be difficult to match projects with the greatest needs for additional employment on an area or an occupational basis. As is always the case with Government programs, there would be great pressure to spread the available money more or less uniformly across the country. Consequently, it is to be expected that larger authorizations would be sought in the future—thus, further reducing the power of Congress over the public purse—if the present proposal should be enacted into law.

While it is said that the proposed authority would be used for capital improvements, the Council of Economic Advisers indicates that:

> Appropriate projects would include resource conservation (e.g., reforestation, reseeding of rangelands, timber stand improvement) and various Federal public works, including construction, repair, or modernization of Federal buildings.

This list certainly includes some items that should be taken care of as the need for action arises. Efforts to defer needed activities until the economy needs stimulating, and the initiation of projects to make work are both likely to lead to waste. The existence of such a program could contribute to a decline in economic activity by causing State and local governments to defer projects in the hope of obtaining emergency Federal assistance.

Farm Bureau recognizes the role of unemployment compensation in an industrial economy subject to cyclical swings. In such a program, however, it is necessary to strike a balance by providing reasonable protection for workers who are unavoidably out of work without setting the benefits so high as to discourage unemployed workers from seeking or accepting new employment. Since conditions vary from State to State, we are opposed to proposals which would reduce State responsibilities under the unemployment compensation program. We also are opposed to the proposal to extend coverage of this program to groups which the Congress has intentionally excluded in the past.

The Economic Report devotes considerable space to a discussion of "Guideposts for Noninflationary Wage and Price Behavior." In our opinion, this discussion places too much emphasis on the idea that wages must increase with productivity and too little on such things as the importance of capital investment in increasing productivity, the desirability of distributing a part of the benefits of increased productivity through lower prices to consumers—including farmers—and the importance of using increases in productivity to strengthen our competitive position in world markets.

Since the Government is not now, and in our opinion should not be, directly responsible for the determination of wages and prices, its major concern in this area should be to create conditions which will result in private decisions that are consistent with the public interest. In the case of wages this means that the Government should avoid undue intervention, be neutral when it does intervene, prohibit the use of unfair practices and seek to avoid public policies which give either side an advantage in collective bargaining. In the case of prices it means that the Government should seek to foster competition by appropriate policies to curb monopoly and expand international trade.

In its analysis of "The Budget in 1958–60" (p. 81), the Council of Economic Advisers finds restrictive budget policy "a probable major cause of the incomplete and short-lived nature of the 1958–60 expansion." Regardless of whether budget policy was, or was not, too restrictive in this period, there appears to be a strong possibility that the 1959 steel strike was at least partly responsible for the "incomplete" nature of the 1958–60 expansion.

Time does not permit discussion of numerous tax reform proposals mentioned in the Economic Report, except for one which involves an important question of economic philosophy. I refer to the proposal to grant taxpayers an 8 percent tax credit for gross investment in depreciable machinery and equipment.

While we agree with the objective of encouraging capital investment, we are opposed to the proposed tax credit because it appears to us to be a wrong approach. It is a selective form of tax relief—in reality, a subsidy. As such, it would give some taxpayers a competive advantage over others. It is also a tool for Government planning of capital investment and economic activity. If it is right to grant such a tax credit for new investment, the next logical step might well be to set up a differential schedule of credits so that the Government could encourage some types of investments and discourage others. In our opinion, a better approach to the objective of stimulating capital investment would be to grant all taxpayers greater flexibility in the treatment of depreciation and to curb Government spending so that income tax rates can be reduced for all taxpayers.

Farm Bureau agrees with much of what was said in the President's special message on international trade.

Since agriculture is heavily dependent on exports, farmers have a special interest in measures to reduce the barriers to international trade on an orderly basis. We are also aware of the contribution expanded trade can make to the strength of the free world and the solution of our own balance-of-payments problem. We fully agree with the President's statement that, "Our export drive will founder if we cannot keep our prices competitive in world markets." This is a point that should be kept in mind at all times when policies affecting domestic prices are under consideration. It certainly should be a pertinent consideration in the development of Government policies on farm price supports.

Since Farm Bureau is scheduled to discuss the President's agricultural recommendations at hearings before the House and Senate Agricultural Committees in the near future, I will make only a brief comment on this subject at this time.

The need for a thorough revision of farm policy obviously is long overdue. We think it unfortunate, however, that the President has seen fit to recommend a major extension of Government efforts to fix farm prices and ration the right to produce farm products. Such programs are certainly inconsistent with the objective of meeting competition in the world market. While the President spoke of "a program for maximum freedom and flexibility in the operation of individual farm enterprises," the administration is proposing to subject producers of wheat, feed grains, and dairy products to controls far more stringent than anything we have thus far had in agriculture. In addition, producers of feed grains and wheat are to be told that they must accept the proposed controls or face the possibility that the market will be demoralized by the dumping of Government-held surpluses.

The alternatives are not, as suggested by the President's farm message, "a chaotic, inefficient, surplus-ridden farm economy," or a Government-licensed and regimented agriculture. Instead, our own recommendations point the way to an orderly solution of the surplus problem through a sound cropland retirement program and greater opportunity for market prices to guide needed adjustments in production and consumption.

Thank you, Mr. Chairman.

Chairman PATMAN. Thank you Mr. Hamilton.

Now, Mr. McDonald, we would like to hear from you, sir, and you may proceed in your own way.

STATEMENT OF ANGUS McDONALD, ASSISTANT DIRECTOR, LEGISLATIVE SERVICES DIVISION OF THE NATIONAL FARMERS UNION

Mr. McDONALD. Mr. Chairman, my name is Angus McDonald. I am assistant legislative director of the National Farmers Union.

The National Farmers Union is a farm organization of approximately 700,000 men and women residing mainly in the Mississippi and Missouri Valleys.

The Economic Report of the President, together with the annual report of the Council of Economic Advisers, in a number of respects is an excellent document. In reading it, one cannot fail to notice the awareness of this administration of the many problems and dilemmas that confront our Nation at this critical period in history. The two reports indicate that the administration is energetically and seriously attempting to solve the problems of agriculture, of unemployment, and of economic growth.

We are in accord with the principle enunciated by this administration and by the Secretary of Agriculture, that the best way to reduce excessive supplies of agricultural commodities is to reduce production until there is a balance between demand and supply plus a stockpile of commodities necessary in the event of war or other emergencies. A corollary of the managed-supply principle is that unduly depressed farm prices will adjust themselves automatically, if production is brought into balance with consumption.

We do not think it can be emphasized too often that over a long period of years, farm prices and consequently farm income have been greatly depressed because of overproduction. The farmer has, over the years, been increasing his efficiency with consequent overproduction. His reward has been low prices and low income at the same time that other sectors of the economy—which had not proportionately increased their efficiency—were enjoying an unprecedented increase in incomes and profits.

For example, during the last year farm prices stood around 87 or 88 percent of what they were in 1947–49, while industial prices were from 125 to 150 or 160 percent of what they were during the same period. Farm net income in 1961, it is true, increased by $1 billion because of the enlightened policies of the administration, but farm income still was way below the record income of $17.3 billion in 1947.

Looking backward to 1947, and using this good year as a yardstick, there was a cumulative deficiency of $55.6 billion in farm income during the years 1947 through 1960. Disposable personal income of the Nation as a whole during the period increased from $170 to $351.8 billion.

The farm depressions have no doubt been an important factor in the recession periods of the last 14 years. Low farm income is one reason why demand has not kept up with production capacity. Another is that, industrial prices have not been responsible to demand. In a number of industries, such as steel, there is reason to believe that we have been experiencing at times an administered price inflation because a number of durable goods industries were actually able to increase their prices during periods of declining demand. Increasing demand or consumption is perhaps the key that would, in large part, solve the problem of getting an increased growth of the economy which is needed because of increased population and increased efficiency.

We feel strongly that the President is on the right track in recommending the passage of two vital pieces of legislation: the Manpower Development and Training Act, and the Youth Employment Opportunities Act.

According to a report of August 2, 1961, of the House Committee on Education and Labor, the unemployment rate for youth aged 16 and 17 in June 1961, was 24 percent for males and approximately 31 percent for females. The unemployment rate for all ages in the civilian labor force that month was 7.5 percent. For the group under 25 years of age, however, it was 15.5 percent for males and 18.5 percent for females. The rate for the under-25 group—more than twice the national average—has persisted for many years. If we limit ourselves to the age group covered by this bill, 16 to 21, we find in a recent month—May 1961—that 550,000 out-of-school youths—400,000 boys and 150,000 girls—were unemployed.

The Youth Employment Opportunities Act, we hope, will do much to solve the major problem of youthful unemployment which not only causes our economy to stagnate, but contributes to crime and juvenile delinquency. Young men and women who are willing and able should be afforded every opportunity to obtain useful employment.

We also believe lower and middle income groups should be afforded some tax relief.

We suggest that those least able to pay be given relief, and not those in the upper brackets.

It seems unnecessary to belabor the point that there would be an increase in demand almost equal to the amount of tax relief accorded these categories. We also endorse the recommendation of the President in regard to an increase in unemployment benefits and the suggestion that he be given authority to inaugurate a program of natural resource development. We feel that one reason the economy has been sagging is that national resource development has been slowed down during the past 10 years.

Other parts of the President's report, we cannot endorse. We are opposed to the 20-percent withholding tax on patronage refunds and to the required written consent of the patron in regard to reinvestment of patronage refunds in cooperatives. Average net farm income per farm in 1960 amounted to only $2,990.

Since most farmers do not pay income tax, we do not see the point in sending the money to Washington and having it refunded to the farmer 6 months or 1 year later.

Instead of millions of checks, traveling the long road from cooperative headquarters to Washington, and then back to the farmer, would it not be more practical to have the cooperative merely send to Washington a list of names with dollar amounts of patronage refunds to the Bureau of Internal Revenue? Since the farmer is required under existing law to report patronage refunds as income on his individual income tax return, it would be an easy matter to check this report with the report of the cooperative.

In regard to the written consent agreement, we suggest that it is an unwarranted interference in the affairs of the farmer. We are wondering about the constitutionality of this recommendation, if enacted.

The administration has many good recommendations in regard to foreign trade, and applying certain stimulants to the end that jobs, and therefore demand, may be increased. Perhaps the greatest problem the country faces, transcending even that of agriculture, is the problem of full employment. The Full Employment Act of 1946 envisaged, we believe, an economy in which unemployment would not be a major problem. There is an inference perhaps not intended, that the President and his Council of Economic Advisers would find a 4-percent unemployment rate satisfactory. We suggest such a rate is entirely too high. Although large employers of labor would no doubt find such a situation to their liking, we do not believe the American people would concur. We must not condemn millions of our citizens to bleak and hopeless unemployment which would destroy their morale, increase crime, and weaken the economy as a whole.

We are also slightly taken aback at the President's—several times repeated—recommendations that industry, already suffering sizable excess capacity, should be persuaded by means of huge tax subsidies to further increase plant capacity. We call attention to a McGraw-Hill survey which indicated that in September 1960, 48 percent of steel capacity was idle. Idleness of plant capacity, at that time, in certain industries was as follows: Nonelectrical machinery, 28 percent; electrical machinery, 26 percent; autos, trucks, and parts, 14 percent; other transportation equipment, 27 percent; stone, 23 percent; clay and glass, 24 percent; petroleum, 17 percent; food and beverages, 19 percent; textiles, 12 percent.

Although there has been considerable recovery since that time, McGraw-Hill in a survey published in Business Week of September 16, 1961, estimated that overcapacity of all industry would be 15 percent by January 1, 1962, and 13 percent by July of this year.

It appears that industry has a long way to go before it reaches the high point in plant utilization which was reached at the end of 1955. There is another reason why industries operating at less than 100 percent capacity should not be offered tax subsidies on the condition that they increased capital investment.

Suppose, for example, the Ford Motor Co., which is reported to be troubled by an excess of liquid assets, responded to the bait, and invested $500 million in additional plant expansion. If Ford received an 8 percent tax credit, it would find itself with an additional $40 million which it otherwise would not have had. It is possible to imagine that Ford, having this extra money, would invest this money, overseas, and further aggravate the dollar shortage we have been hearing so much about lately.

The following quotation from the February 1962, issue of Fortune is pertinent to the questions we are raising in regard to proposals designed to encourage plant expansion:

> Earning more but refunding less is the position Ford finds itself in today. As its profits rose in the fifties Ford pumped much of them back into new plant. Now Ford has pretty much of a sufficiency in fixed assets, and with sales holding relatively high, the investment is paying off quite handsomely. Note that in 1960 Ford's domestic capital expenditures were only about $128 million against net income of $428 million. Strictly from the standpoint of availability of funds, it is easy to understand why Ford did not flinch, in 1961, from investing some $496 million for the purchase of Electric Autolite, Philco, and the remaining interest in Ford of the U.K. * * *. Average rate of growth of Ford's domestic dollar sales over the years 1950–60 has been 6 to 7 percent a year; growth of international sales over the same period has averaged 12 percent a year (p. 117, Fortune, February 1962).

We applaud the efforts of the administration to enforce the antitrust laws. Price fixing in the American economy until recently had become a way of life. Gouging of the public and destruction of small business by means of price discrimination and price-fixing conspiracies has not only sapped the moral fiber of the business community but has slowed down demand, caused production to decline, and ultimately contributed to unemployment and a slowdown in the growth of the economy. Stifling of competition has disastrous effects not only on consumers, small business, labor, and agriculture, but even on industry itself. An industry unresponsibe to supply and demand is not a healthy industry, and an industry such as steel, which has priced itself out of foreign markets, has contributed to the imbalance in international payments.

Chairman PATMAN. Thank you, Mr. McDonald.

I would like to ask you a few questions concerning the basic programs in agriculture.

I remember when cotton was first allocated efforts were made to make some provision for tenants, but I do not think any adequate provision was made for tenants. When the program came along for tobacco, didn't some arrangement occur that would be of help to tenants in the growing of tobacco?

Mr. McDONALD. Mr. Chairman, I am unable to answer that question. I know that the Farmers Union has always insisted, over a period of many, many years, going back to the 1930's, on a minimum amount for each grower, regardless of your cut in acreage quotas.

Chairman PATMAN. I know you advocated it. I advocated it, too. But it never did happen.

Mr. Hamilton, do you know about the tobacco program?

Mr. HAMILTON. Mr. Chairman, I cannot answer in detail. I have a general impression, first, that most agricultural legislation over the years has contained provisions for the protection of tenants; and second, that these provisions have been very difficult to enforce in a way that protected the tenants. The enforcement, of course, is up to the county committees.

Chairman PATMAN. The local committees and the State committees.

Mr. HAMILTON. Yes. But it is difficult to protect tenants, because when a landlord wants to displace a tenant, he can usually find all kinds of reasons for making the situation look like he ought to be allowed to do so, and county committees are undoubtedly responsive to that sort of thing.

Chairman PATMAN. What you say is true as to cotton, but I understand they have a different program for tobacco and rice. Are you acquainted with the rice program?

Mr. HAMILTON. I am acquainted with all of these programs in general. When you get down to the specific regulations, I am not an expert.

Chairman PATMAN. Are you acquainted, Mr. McDonald, with the rice program?

Mr. McDONALD. No, Mr. Chairman, I am not.

Chairman PATMAN. What attracted my attention is that farmers in Arkansas had a quota for the growing of rice. They were tenants, and they came over into the district I represented and actually started their quotas for the growing of rice from Arkansas. They seemed to be carrying around in their hip pocket. I do not object to the industry being in our district. It is a wonderful thing. But I am just wondering about the quotas in that case, and tobacco, which are not available to people who produce cotton and other products.

Mr. HAMILTON. I could make one comment, Mr. Chairman.

Chairman PATMAN. All right.

Mr. HAMILTON. In rice, it is permissible to allocate quotas on a personal history basis.

Chairman PATMAN. That is, on a history of growing rice?

Mr. HAMILTON. That is right. Many of the ricegrowers are tenants, and they are able to move their quotas around. I did not know they could move them across State lines. In fact, I was under the impression that they could not. And this personal history feature does not apply to the rice program in all States. It is an administrative matter which is determined by the Secretary on the basis of what has been the practice in an area.

Chairman PATMAN. Would not the same rule apply to cotton farmers?

Mr. HAMILTON. No, it does not apply to cotton farmers.

Chairman PATMAN. I mean: Shouldn't it apply? Wouldn't a tenant farmer have the same equities there? Since he has lived his whole life on a farm and done nothing else except farm, why would he not be entitled to the same consideration?

Mr. HAMILTON. I can only say that the Congress has not seen fit to give him the same privilege. And I think that the difference reflects the feeling of Congress and the people in the producing areas with regard to the practices followed in the production of these crops.

It seems that you cannot grow rice continuously on the same land, and there are growers who grow rice on one landlord's land one year and then rent from another landlord. Land that has been in rice apparently is fallowed or used for pasture for the next year or two. I believe this is partly a matter of weed control.

Chairman PATMAN. I will not pursue this further, but I would appreciate it if you gentlemen will file an additional statement in connection with your remarks about tobacco and rice and compare it with the cotton program, for instance, and tell me a reason why it should apply to tobacco and rice and not apply to cotton; or your recommendation that it extend to cotton; whatever you want to recommend about it. In other words, evaluate it, if you please. I will appreciate it if you do it in connection with your remarks, when you look at your transcript.

Mr. McDONALD. I will be glad to do that, Mr. Chairman. (See p. 839.)

I might comment: To my information, the only time such a thing as you have suggested has happened within a State—I never knew it to go across State lines—is when a county has an excess acreage. And then the committee, the State committee and county committee, could reallocate and move these quotas over to another county.

Chairman PATMAN. That is not the important part. The important part is that the farmer, although a tenant, is recognized, because he has spent his life growing a product or commodity. And he is recognized in the program and given some benefit. That is the part that I am getting to.

Mr. McDONALD. We will get that to you, Mr. Chairman. (See p. 839.)

Chairman PATMAN. In our area, we have a fine sesame industry. You know, sesame is not grown in this country very much. But one has developed down in Lamar County, of which Paris is the county seat, and also in Fannin County, Mr. Rayburn's district, and also down around Amarillo and Lubbock. The sesame industry is entirely, I think, within the State of Texas. It is a very valuable industry. It is greatly handicapped by this program.

Do you know anything about the program as it affects sesame?

Mr. McDONALD. No, sir; I do not.

Mr. HAMILTON. So far as I know, there is no program affecting sesame at all.

Chairman PATMAN. In the case of special programs, where it is a pioneering program like sesame, where it is not grown in this country, where there is a great need for it and it is a wonderful product, don't you think some consideration should be given to develop it, to permit its expansion?

Mr. McDONALD. I would think so. Otherwise, the industry might be choked off entirely.

Chairman PATMAN. What do you think about it, Mr. Hamilton?

Mr. HAMILTON. I do not know a great deal about sesame, but I know that the Feed Grain Act of last year provided special consideration for some new crops. I was just trying to check——

Chairman PATMAN. About five of them, I think, including sesame. Do you have it there with you? If you do not find it, suppose you put it in the record in connection with your remarks.

Mr. HAMILTON. All right, sir.

Chairman PATMAN. That does not apply this year, though. Just last year, wasn't it?

Mr. HAMILTON. I believe it applies this year, too.

Chairman PATMAN. In view of your encouraging statement, I am willing to wait for you to look it up.

I will ask Mr. McDonald about the dairy program.

I am getting complaints about this new bill, that the fluid milk, the class A milk, will continue to sell for about the same price, but the surplus milk will go down in price, probably $1.50 to $1, for the purpose of encouraging the farmer to use his surplus milk on the farm, feed it to pigs or chickens or something like that, and not to put it in the market.

Are you acquainted with that, Mr. McDonald? (See p. 839.)

Mr. McDONALD. Not in any great detail. I know generally about the milk situation and the great decline in consumption, which is probably caused by the stories about fallout in milk and so forth.

As I recall from reading the Secretary's recommendation, he plans to increase the price support, which would be the floor under the bill.

Now, in regard to class 2 and other types of milk, I do not recall what he recommended on that. But as you know, we have always had that situation, where out of whatever is left over, what people drink is shoved over into the other class.

Chairman PATMAN. But this particular proposal, as I understand it, is to make the price definitely low enough so that they will not market the surplus.

Mr. McDONALD. I am afraid I do not know about that.

Chairman PATMAN. Do you have that, Mr. Hamilton?

Mr. HAMILTON. I have the information on sesame, and it is included in the Agricultural Act of 1961, both in the feed grain and the wheat sections.

This means that a man who diverts acreage under either the wheat program of the feed grain program may grow a crop such as sesame rather than leave the land idle. However, if he does grow such a crop, he does not get diversion payments.

Chairman PATMAN. What is that?

Mr. HAMILTON. He does not get diversion payments, if he takes land out of feed grain or wheat and——

Chairman PATMAN. And uses it in sesame or one of those five crops?

Mr. HAMILTON. Yes. He is a cooperator under the program, but he does not get diversion payments if he grows these special crops.

Chairman PATMAN. Does that apply to this year, too?

Mr. HAMILTON. Yes, sir.

Chairman PATMAN. But at one time they got payments, did they not?

Mr. HAMILTON. I do not think so. At least not in recent years. Not under the 1961 program.

Chairman PATMAN. But to start a new crop like that is so important—you would be in favor, up to a point, of rewarding them, the same as other crops, would you not, so as to encourage the new industry to start?

Mr. HAMILTON. I am not prepared to comment on that question, Mr. Chairman.

Chairman PATMAN. Senator Douglas?

Senator DOUGLAS. I wonder if you gentlemen would turn to page 5 in the Economic Indicators, which gives statistics on farm income.

In the third from the last column, you have net farm income for 1960 and the first three quarters of 1961. The average for 1960 was $12 billion. The average in the first three quarters was about $12.9 billion. The best estimate for 1961 is a total of $13 billion. Do you accept those figures as approximately accurate; any one of you?

Mr. HAMILTON. I am sure that those are the best figures available.

Mr. MCDONALD. That would appear, Senator, to approximately agree with the figures that the Department of Agriculture has published in regard to the increase in income during the last year.

Senator DOUGLAS. Mr. Hamilton, do you agree with those figures?

Mr. HAMILTON. Yes, as far as I know, they are correct. You know, in agriculture we depend on the Department of Agriculture for our statistics. There may be disagreements on policy, but we have absolute confidence in the Department of Agriculture's statistics.

Senator DOUGLAS. Now, am I correct in understanding that the figure of net farm income includes the estimated cash value of the rental of the farm home plus food produced on the farm and consumed on the farm? In other words, this is not a figure of cash income, but of net income, including services, provided by the farm to the farmer, on estimated current prices; is that correct?

Mr. MCDONALD. It is my information that they do make some allowance for the home and for the food which the farmer raises and eats himself.

Senator DOUGLAS. Mr. Hamilton?

Mr. HAMILTON. That is correct, Senator. You can easily see that, because if you look at the section on "Realized Gross," there is a total figure which is $39.3 billion, and then you have an estimate of cash receipts from marketings, which is $34.4 billion. The difference of approximately $5 billion is Government payments, and the items you refer to, such as the rental value of farm homes and home-produced items.

Senator DOUGLAS. I have heard it estimated that the total value of services in kind, or income in kind, received by the farmers, amounts to approximately $3½ billion. Have you heard that figure?

Mr. HAMILTON. Well, the difference here, is roughly $5 billion. You would have to take out Government payments, and I do not have that figure at hand, but around $3½ billion would appear to be about right for the items you mention.

Senator DOUGLAS. So that assuming the $3½ billion is correct—and if it is not correct, I hope you will mention this in the revision of your testimony—the net cash income from farming in 1960 is $12 billion minus $3½, or $8½ billion; and 1961, approximately $12.9, minus $3½, or $9.4 billion; so that the increase of $1 billion has been in cash income, and this amounts to an increase of approximately 12 percent.

Is that correct?

Mr. HAMILTON. I am not very good at computing percentages in my head. It sounds about right.

Senator DOUGLAS. I think that is approximately correct. Between 11.5 and 12 percent. Do you regard this as a hopeful increase in farm income?

Mr. HAMILTON. Well, of course, any increase in farm income is always welcome to the farmer. I think that we ought to be somewhat concerned, though, over the fact that a considerable part of this increase in cash income resulted from Government payments; and I understand that there is some concern about the cost of agricultural programs to the Federal budget.

Senator DOUGLAS. Do you have any estimate as to how much of this increase has come from increased Government payments and how much from increased net income in the marketplace?

Mr. HAMILTON. I may have the figures in my briefcase. I do not have them in my head. I know that payments under the feed grain program were $768 million; and there were sizable payments under the wheat program, of perhaps $130 million.

Senator DOUGLAS. Were these increases? Or totals?

Mr. HAMILTON. They are totals. They are increases in Government payments. But, of course, to some extent they offset what the farmer otherwise would have received for the production of the acres that were idle.

And this becomes very complicated, of course, when you consider that some of the commodities that would have been raised probably would have been placed under price support. It depends on your definitions.

Senator DOUGLAS. If we take the feed grain program, you say that total Government payments were $768 million?

Mr. HAMILTON. Payments for land retirement were $768 million.

Senator DOUGLAS. Now was that an added payment over 1960?

Mr. HAMILTON. It is not easy to compare, because there was no payment program in 1960. There was a price-support program, under which loans were made.

Senator DOUGLAS. If you take all the feed grain programs together, what increase, if any, was provided?

Mr. HAMILTON. The $768 million, as I understand it, covers the two feed grains that were included in the 1961 program; namely, corn and grain sorghums.

Senator DOUGLAS. But you say that is for retirement of land?

Mr. HAMILTON. Yes.

Senator DOUGLAS. What about price supports?

Mr. HAMILTON. Well, the price-support program results are not all in yet. Farmers have until the end of May to place corn under support.

And, of course, as you know, Senator, it is not only the amount that is placed under support, but also the amount that is ultimately turned over to the Commodity Credit Corporation in settlement of the loans, that affects these figures.

Senator DOUGLAS. May I ask: What was the total production of corn this last year, as compared to 1960?

Mr. HAMILTON. I have the figures, I think, but I do not have them in my head.

I find that I do not have the exact figures in my briefcase.

Senator DOUGLAS. It roughly amounted to 3.3 billion bushels? Did the total production amount to that?

Mr. HAMILTON. I believe it was a little higher than that. Production of corn and grain sorghums together was down about 9 percent.

Senator DOUGLAS. In other words, there was a reduction in output of about 10 percent?

Mr. HAMILTON. About 9.

Senator DOUGLAS. This, therefore, reduced the volume of the crop which was price supported. Is that not true?

Mr. HAMILTON. That is correct.

Senator DOUGLAS. So that there would be reduced losses from price support in 1961 as compared with 1960?

Mr. HAMILTON. There should be; yes.

Senator DOUGLAS. Is that not true?

Mr. HAMILTON. Yes.

Senator DOUGLAS. And that, therefore, this should be used as an offset against the $768 million for land retirements?

Mr. HAMILTON. That is correct.

Senator DOUGLAS. Now, of course, the great question in agriculture is whether we are to abandon price and production controls for a return to the free market, or whether we will retain them or modify them in some way. Your organization, as I understand it, favors a return to the free market and the abandonment of all price and production controls. Is that correct?

Mr. HAMILTON. No; that is not correct. The alternatives are not as clean cut as high price supports or none. The Farm Bureau has been for a lower level of supports, for allowing more opportunity for market prices to guide production.

Senator DOUGLAS. What level of support do you want on the farm?

Mr. HAMILTON. Well, in terms of dollars and cents, we cannot give an absolute figure.

Senator DOUGLAS. What is the present level of support?

Mr. HAMILTON. The present level is $1.20 for corn.

Senator DOUGLAS. How much would you want to reduce it?

Mr. HAMILTON. Well, as I said, we are interested in a program which uses price supports to encourage orderly marketing and to provide a brake on price declines. But we also want to let the market help to adjust production and consumption.

And you remember a few years ago we proposed that support be based on 90 percent of the average market price for the previous 3 years. In fact, this is in the law, the Agricultural Act of 1958; but, of course, it was suspended by legislation enacted last year.

Senator DOUGLAS. Of course you are well aware of the fact that the market price tends to be the price of the corn and the feed grains not under the program, which is—I will not say done, but which is sold on the market, and which therefore is appreciably less than the support price. You are aware of that, of course.

Mr. HAMILTON. This will depend on the nature of the program, Senator.

Senator DOUGLAS. But is it not true that in the case of corn, the market price of corn has for years been very much below the support price?

Mr. HAMILTON. It is true for a number of reasons, one of which is that up until the enactment of the 1958 act there were many farmers who were not eligible for support. There has been a tendency for the market price to run somewhat below the support price; but if the Commodity Credit Corporation is prohibited from selling its stocks except at some figure above the support, and if a majority of the farmers are eligible for support, then the price will have an opportunity to rise above the support.

Senator DOUGLAS. Well, now, do you still stand on the principle that the support level should only be 90 percent of market price.

Mr. HAMILTON. This is 90 percent of the previous 3-year average. And just a minute, please, if I may.

It is coupled with a recommendation that the Commodity Credit Corporation not be allowed to sell any of its stocks at less than some percentage in excess of the support price, and we would suggest a figure of 115 percent of the support. And the purpose of this is to provide an opportunity for the market price to rise.

Senator DOUGLAS. May I ask this: What is the average market price for corn now, or for the last 3 years?

Mr. HAMILTON. I do not have——

Senator DOUGLAS. Mr. Hamilton, you are the expert on this subject, and you are the director of research of the great American Farm Bureau Federation. This is a simple fact. It comes out every month, really, in the agricultural statistics. Can't you give me the approximate avearge price for the last 3 years in the market?

Mr. HAMILTON. I suppose it is around $1.12 or $1.15.

Senator DOUGLAS. Do you really think it is as high as that?

Mr. HAMILTON. It is very difficult to keep——

Senator DOUGLAS. You know, in Illinois, which is one of the two biggest corn States, we found the price to be very frequently, very commonly, around a dollar a bushel, or $1.03 a bushel.

Assume that your figure of $1.12 is correct. Then 90 percent of that would be 98 cents a bushel.

Now, then, are you saying that we should change the basic Feed Grain Act, so that in effect we would only support corn prices if they fell below 98 cents a bushel?

Mr. HAMILTON. Well, Senator, you have to consider the alternatives. If you are going to support corn very much above the market price, eventually you are going to have to do something about the corn that is produced in response to that price. And when you consider the difficulty of putting controls on a commodity which in some cases is entirely fed on the farm where produced, it is clear that there are disadvantages to the control alternative. Corn is a raw material that is used on the farm, and it would be a job to enforce quotas, where you have to go out on the farm to collect a penalty.

Senator DOUGLAS. You are giving a defense to your position, but I want to see if I understand your position.

The application of this principle would mean in effect that the Government would only support corn if the price fell below 98 cents a bushel.

Mr. HAMILTON. On the basis of the figures that we have used. But in order to put our program in perspective, it must be considered as a whole. It includes a relatively low level of price support. It includes protection against the sale of CCC stocks until the price is above support. And then we have also recommended a very sizable land retirement program.

Senator DOUGLAS. Out of this 98 cents the farmer will have to pay storage, will he not?

Mr. HAMILTON. Well, if he put it in the support program, he would.

Senator DOUGLAS. So that a 98-cent support program would not mean that he would get 98 cents, but 98 cents minus the cost of storage, insurance, and so forth.

And what is your estimate as to the average amount that this comes to per bushel?

Mr. HAMILTON. Well, Senator, I think the important thing to remember on corn is not the type of thing you are mentioning there, but the fact that corn is used to feed livestock, and that the feeding of corn to livestock has been fairly profitable in recent years, with some exceptions, such as turkeys, this past year and hogs 2 or 3 years ago.

Senator DOUGLAS. Mr. Hamilton, I am aware of this fact. But, in all kindness, may I say that you always seem to answer my question by talking about something else.

I would like to ask what is the average cost of storing corn on the farm and insuring it per bushel in the period from the time the corn is harvested to the time it is disposed of?

Mr. HAMILTON. Well, corn can be stored very cheaply in temporary bins if it is going to be fed to livestock.

Senator DOUGLAS. Let us talk about the production of corn for sale.

Mr. HAMILTON. I do not have——

Senator DOUGLAS. Well, you are a great expert on this subject. I am not an expert on it. But I can give you the figures. Approximately 4 cents a bushel. And therefore a price of 98 cents will mean a net of around 94 cents.

Mr. HAMILTON. I would say that is very economical storage.

Senator DOUGLAS. In other words, I was very conservative. It might run more than that?

Mr. HAMILTON. Yes.

Senator DOUGLAS. And therefore the farmer would get less than 94 cents.

Mr. HAMILTON. Now, this is in terms of the support price, again. If you have a land retirement program and protection against CCC sales, the market price may well be above the support price.

Senator DOUGLAS. Then you are for a land retirement program?

Mr. HAMILTON. We are for a land retirement program with emphasis on a long-term retirement program to take some of this land out for a period of years.

Senator DOUGLAS. Are you for any limitation of production on the land which is cultivated with corn and with grain sorghums?

Mr. HAMILTON. Only that we would require that the farmer put a percentage of his cropland in the retirement program in order to qualify for price supports if we were not able to get sufficient land under long-term contracts. But we would first emphasize retirement under long-term contracts similar to the old conservation reserve program; although it might be desirable to make some changes in the old program.

Senator DOUGLAS. What effect do you think all of this would have on farm income?

Mr. HAMILTON. Well, our members are farmers, and we are interested in improving their income, and they are interested in improving their income, and we think our program would improve farm income.

Senator DOUGLAS. By paying them lower prices?

Mr. HAMILTON. Well, again, Senator, our recommendations on price support and a part of the program where the objective is not to lower farm prices, but to let the market help make some of the needed adjustments.

Senator DOUGLAS. But isn't the demand for farm products inelastic, namely, an increase of 1 percent in the output of virtually all farm products causes a decrease of far more than 1 percent in unit price? I think the average elasticity is probably no greater than 0.3; so that for farm products as a whole—and I do not think that corn is a great exception to this—an increase of 1 percent in quantity will produce a decrease of around 3 percent in price per unit, and hence a decrease of 2 percent in total income.

Now, that is the crucial factor with which we are dealing in the farm question, namely, that as agricultural technique improves, farmers produce more. As they produce more there is a greater proportionate reduction in unit price and also a reduction in net income; so that the farmers are worse off because they are producing more.

Now, this is really the essence of what we are dealing with. And that is why some of us rather blink at the idea that there should be few restraints upon output.

Mr. HAMILTON. Well, the demand for all farm products as a group and any individual product is inelastic. I think the demand for livestock products is considerably more elastic than the demand for farm products as a group. I think there is some elasticity in the demand for corn. Under the 1958 act, when the support on corn was somewhat lower than it had been in earlier years——

Senator DOUGLAS. We have received from the Department of Agriculture the price on the farm for the last 4 years: 1958–56, 112; 1959–60, 104—these are in cents—1960–61, 99.6—that is the figure that stood in my mind, it is roughly a dollar—1961–62, estimated, 107. Excluding 1961–62, the last 3 years, the average is 105. Not 112, which you say. The average would be around $1.03, somewhere between $1.03 and $1.05.

You say only support 90 percent of that. So this means a support of from 92 to 94 cents a bushel, and out of that you would deduct at least 4 cents for storage. So you are really proposing from 88 to 90 cents for corn at the farm.

Isn't that pretty stringent, as compared with the $1.20?

Mr. HAMILTON. Well, as compared with the $1.20, Senator, I believe you just said that the estimate for this year from the Department of Agriculture is $1.07. So the corn that is actually being sold on the market, as——

Senator DOUGLAS. But those who did not come under the support program; that is the point.

Mr. HAMILTON. It is not just for the noncooperators. Some people are not able to participate in the loan program due to lack of storage, high moisture corn, and various reasons like that. There are also some costs to the support program. You mentioned the storage cost, and this cost is somewhat higher for those who qualify for a loan. There is also an interest cost and a sealing cost.

Senator DOUGLAS. Mr. McDonald, do you have any comments that you want to make on this?

Mr. MCDONALD. Well, Senator, I think, as you know, as is pretty generally known, the Farmers Union's position is that when you give the farmer a higher price, he gets a better income. It seems very simple. It also seems to us that when you have too much of something which is a drag on the market and dragging it down, there should be some attempt at restricting the production, without, of course, endangering abundant supply.

We are very much aware of the inelasticity, particularly of the market for wheat and other things. Consumption, I believe, has been declining per capita. And it seems to us not intelligent to go on producing much more than we need. And some attempt should be made. In regard to the farmer doing it himself, every farmer is competing against every other farmer, and he has to have some kind of arrangement whereby he can use his Government to help him to bring production in balance with demand.

In regard to Mr. Hamilton's comment on corn allocation or restriction of corn production, we have had for a good many years now acreage allotments on corn. And I think where an intelligent attempt was made by the Secretary of Agriculture to make the program work, it has worked in large degree. I think it did not work in 1958, when Mr. Benson told the farmers that he would support corn at $1.06 a bushel—this is my recollection—and that they could grow all the corn that they wanted. And such policies as that were in part the cause of the dilemma we find ourselves in today.

Senator PELL. I would be interested in the reactions and the thoughts of both of you gentlemen on the price support system for cotton. Do you believe we should leave it as is, or reduce it, or what are your thoughts on this matter?

I hasten to add: The reason I ask this question is that I come from a part of the United States where cotton is used as a raw material, and we are asked, under the President's trade expansion program to see the duties reduced on the goods that come in. Yet some of these imported textile goods are made with American cotton bought at a price lower than our manufacturers have to pay for American cotton here in this country.

Mr. McDONALD. As I understand the situation in regard to cotton, I believe, Senator, this commodity is unique, in that if you increase the price of cotton too much, it becomes uncompetitive with rayon and other materials, synthetic fibers. There is also an international problem.

Now, the question then arises whether cotton should be subsidized in order to be competitive. And I think as a matter of national policy and international policy, in all probability the Congress will find that some element of subsidy should be in this; because to bankrupt the cotton industry would in the long run be more or less disastrous, certainly to the cotton farmer.

Senator PELL. What would happen if it was left to find its own price level?

Mr. McDONALD. Well, it is my impression that the price would fall so low—You mean without any acreage control?

Senator PELL. Yes; just let it find its own price.

Mr. McDONALD. The free market?

Senator PELL. The free market.

Mr. McDONALD. I think it would bankrupt the cotton industry completely and bankrupt the cotton farmers.

I think, incidentally, Senator Douglas, that is true of these other commodities, too.

Senator PELL. You do not think it would merely result in producing a limitation in the production of cotton?

Mr. McDONALD. Well, the tendency has been that when the price falls, the farmer puts in more acres for loss in income as a result of price declines. And of course when you pursue that to the ultimate, the farmer goes broke and goes out of business, and that is going to reduce the production, I suppose. But we are opposed to that kind of policy.

Senator PELL. What is your reaction, Mr. Hamilton?

Mr. HAMILTON. Well, Senator, we are in favor of the cotton provisions in the Agricultural Act of 1958. This act was based on the philosophy that we should go in the direction of somewhat lower supports on cotton and somewhat greater freedom for the farmers to decide how much cotton to grow.

We think Mr. Freeman made a mistake in setting the support price on cotton last spring, and we think that he would have been well advised to reduce the support somewhat this year.

In 1959 and 1960, that is, the crop years 1959 and 1960, the market price of Middling 1-inch cotton was somewhere around 30 cents a pound. The Secretary has set the support at 33.04 cents.

During the 2 years previous to 1961, cotton was more competitive with rayon than it had been for some years. There seemed to be a leveling off of cotton production in foreign countries, and our folks, I am sure, would be willing to accept a price support of somewhere around 30 or 31 cents for Middling 1-inch cotton under present circumstances.

I think the point is that where you have a program and where you have people accustomed to a certain level of price, it would be disruptive to reduce it too much in 1 year.

Senator PELL. Excuse me. You say 31 cents a—what?

Mr. HAMILTON. 30 or 31 cents a pound, starting from where we are; because any adjustment toward lower prices probably should be made gradually so that people can adjust to it.

We are for moving toward lower supports on cotton, and again, as I discussed with Senator Douglas on corn, allowing the market more opportunity to function.

Senator PELL. But the present differential is what? Around 8 or 8½ cents a pound?

Mr. HAMILTON. You are speaking of the export subsidy?

Senator PELL. Right.

Mr. HAMILTON. This does place a burden on the domestic textile manufacturers, and I think there is a very good case, as long as we have such a program, for some kind of an offset to protect domestic manufacturers perhaps through an input fee equal to this difference on imported cotton goods.

Senator PELL. Then your group would believe in a laissez faire policy to a considerable degree, and would believe the solution to this problem is to apply a duty to compensate for the subsidy; is that correct?

Mr. HAMILTON. Senator, in my prepared statement, I said our position is not one of laissez faire. I think it involves a tremendous amount of government.

Senator PELL. There is nothing wrong with laissez faire?

Mr. HAMILTON. No, sir. But we are going to have a good many programs, and we have to deal with the kind of situation in which we find ourselves.

It may look ridiculous to counter a subsidy with a tariff equalization fee; but you have to deal with the situations you find yourself in.

Manufacturers have a problem. Our longrun solution would be to move toward policies which would reduce the export subsidy.

Senator PELL. But to get a specific answer to my question, you, then, would agree that the present subsidy should remain as is?

Mr. HAMILTON. As long as the support price is 33.04 cents a pound for Middling 1-inch cotton, we have to have an export subsidy that will permit us to export cotton, because we produce almost twice as much as we can use here at home, and the acreage has already been cut very sharply.

Mr. McDonald referred to destroying the cotton industry. You can destroy the cotton industry by cutting the acreage under a control program. Many cotton allotments are already too small to be economic.

Senator PELL. But you would not suggest a reduction in the support price?

Mr. HAMILTON. Oh, but I did suggest a reduction in the support price. I would not suggest a reduction in the subsidy unless the support price is reduced.

Senator PELL. Excuse me. Let us say your suggestion is accepted. How much would you suggest the support price be reduced?

Mr. HAMILTON. Well, as I said earlier, I think our folks would have been happy with a support price of 30 or possibly 31 cents for the current crop year, which would permit the subsidy to come down 2 or 3 cents.

Chairman PATMAN. Congressman Curtis, we had just finished, and we shall be very glad to have you ask questions if you like. I know you were not here.

Representative CURTIS. No, I will take the papers and read them, and want to apologize to the committee and to the witnesses for not being here on time.

Chairman PATMAN. That is all right, sir.

In the absence of any further questioning, we want to thank you gentlemen very much. The committee appreciates your appearance and the preparation for your appearance.

The same is true of other witnesses who have appeared and submitted papers in the course of these hearings.

This concludes the committee's hearings on the January 1962 Economic Report of the President.

The committee will stand in recess subject to the call of the Chair.

Thank you gentlemen again.

(Mr. McDonald subsequently submitted the following for the record:)

NATIONAL FARMERS UNION,
Washington, D.C., February 13, 1962.

Hon. WRIGHT PATMAN,
House Office Building,
Washington, D.C.

DEAR MR. PATMAN: When I appeared before your committee on February 8, you requested that I submit for the record answers to the following questions:

Question. Has there been some arrangement in connection with tobacco whereby the acreage allotments of tenants were protected?

Answer. I am informed by the Department of Agriculture that there never has been any provision in farm legislation which protected the acreage allotments of tenants. There was, however, a provision in legislation which protected tenants under the acreage reserve program.

Question. Are rice allotments transferable? May an allotment cross a State line?

Answer. Previously, a rice allotment in the States of Texas and California were attached to the producer and not necessarily to the land. At one time in these States producers (who might be tenants) were allowed to come in from other acres and take up excess allotments. However, this situation no longer exists since existing law does not permit such transfers. The National Farmers Union agrees strongly with the chairman that some provision in the law should protect acreage allotments which are utilized by tenants. We do not, however, believe allotments should be bought and sold as such because some Wall Street or absentee operator might use such a device to force family farmers off the land.

Question. Shouldn't sesame be included in the farm program?

Answer. Yes. National Farmers Union has favored for many years the inclusion of all commodities in the farm program which are important to human nutrition and to the livelihood of family farmers.

Question. Is it true that under the new farm bill surplus milk will go down in price?

Answer. Specialists in the Department of Agriculture tell us that the bill is designed to raise the income of the dairy farmer. They say there is a floor under the farmers' manufactured milk which is a part of the blended price. But if the farmer goes over his quota there is a deduction from the blended price. Specialists say that the price floor on manufactured milk will be higher unless the farmer goes over his quota.

Sincerely,

ANGUS H. MCDONALD,
Assistant Director.

BOARD OF GOVERNORS
OF THE FEDERAL RESERVE SYSTEM,
OFFICE OF THE CHAIRMAN,
Washington, February 19, 1962.

Hon. WRIGHT PATMAN,
Chairman, Joint Economic Committee,
New Senate Office Biulding,
Washington, D.C.

DEAR MR. CHAIRMAN: When I appeared before your committee during the recent hearings on the President's Economic Report, I was asked to supply for the use of the committee memorandums on two subjects. The first, requested by Senator Douglas, related to the advantages and disadvantages of flexible exchange rates in international finance. The second, requested by Senator Proxmire, related to structural unemployment.

The Board's staff is preparing the two memorandums, and they will be furnished as soon as possible, but, as I understand the transcript of the record of the hearings is about to go to press, they will not be completed in time to be included in the printed record of the hearings.

Sincerely yours,

WM. MCC. MARTIN, Jr.

GENERAL COUNSEL
OF THE DEPARTMENT OF COMMERCE,
Washington, D.C., February 19, 1962.

Mr. JOHN R. STARK,
Clerk, Joint Economic Committee,
Congress of the United States,
New Senate Office Building, Washington, D.C.

DEAR MR. STARK: During the course of Secretary Hodges' testimony before the Joint Economic Committee on February 2, Senator Bush stated that he would send a letter to the Department requesting additional data on the trade program. Secretary Hodges has received such a letter from Senator Bush asking that we submit for the record certain statistical data on exports and imports.

Enclosed, in response to this request, is a table showing U.S. agricultural and nonagricultural exports and imports for 1960 and 1961. These are further subdivided into broad economic categories—foodstuffs, crude materials, semimanufactures, and finished manufactures. That portion of the aggregate value of our agricultural and nonagricultural exports financed by Government grants and credits is also shown. However, data are not compiled on the amount of each economic category of exports financed by Government funds. Purchases of goods abroad by U.S. Government agencies are included in the official import statistics, but are not separately identified. I have been advised that statistical information which would enable the Department of Commerce to classify exports and imports by high labor content and low labor content is not available.

Sincerely yours,

ROBERT E. GILES.

U.S. exports and imports, 1960 and 1961

[Billions of dollars]

Economic class	1960	1961 [1]
Total exports including reexports [2]	19.6	20.1
Total domestic exports [2]	19.4	19.8
Agricultural exports	4.8	5.0
Financed by Government grants and credits	1.2	1.3
Foodstuffs	2.7	3.0
Crude materials	2.0	1.9
Semimanufactures and finished manufactures	.1	.1
Nonagricultural exports	14.6	14.8
Financed by Government grants and credits	.6	.7
Foodstuffs (mainly fish)	.1	.1
Raw materials	.6	.6
Semimanufactures	3.4	3.2
Finished manufactures	10.5	10.9
Total general imports [3]	14.7	14.4
Total imports for consumption [3]	14.7	14.4
Agricultural imports	3.8	3.7
Foodstuffs	2.7	2.8
Crude materials	1.0	.8
Semimanufactures and finished manufactures	.1	.1
Nonagricultural imports	10.9	10.7
Foodstuffs (mainly fish)	.5	.5
Crude materials	2.1	2.1
Semimanufactures	3.0	3.0
Finished manufactures	5.3	5.1

[1] Data are partly estimated.
[2] Data exclude military shipments; economic class data are domestic exports.
[3] Economic class data are imports for consumption.

Prepared in the International Trade Analysis Division, Office of Regional Economics, from basic data of the Bureau of the Census, U.S. Department of Commerce, February 1962.

U.S. DEPARTMENT OF COMMERCE,
AREA REDEVELOPMENT ADMINISTRATION,
Washington, D.C., February 20, 1962.

Hon. WRIGHT PATMAN,
House of Representatives, Washington, D.C.

DEAR CONGRESSMAN PATMAN: Following my appearance with Secretary Hodges before the Joint Economic Committee, you were kind enough to offer to insert in the record of that committee the complete text of the two-part Washington Post series by Julius Duscha on the impact of the area redevelopment program on Mountain Home, Ark.

* * * * * * *

We greatly appreciate this opportunity to have the record carry the full story of the area redevelopment program, in terms of the people who are finding permanent new employment as a result of our work with private enterprise, the communities and the States.

Sincerely,

WILLIAM L. BATT, Jr.,
Administrator.

[From the Washington Post, Dec. 8, 1961]

A DEPRESSED AREA CHANGES—I

Shirt Factory Reshapes Lives Around Mountain Home, Ark.

(By Julius Duscha, staff reporter)

Mountain Home, Ark.—From out of the hills and hollows, the farmhouses and the towns, come 500 young women every morning, ready for work in the facory.

Some of them drive 100 miles a day over winding Ozark hills to earn from $1.15 to $1.60 an hour making shirts.

The women, most of them farmers' wives, work in a modern pink-and-blue brick building of the kind that hundreds of small towns and rural areas would like to have for Christmas.

Near the building is a shiny silver water tower constructed with the first Federal aid under the depressed areas program.

Without the water system, which the U.S. funds made possible, the shirt factory probably would not be in operation today.

SYMBOLIC CEREMONIES

On Saturday Senator J. W. Fulbright (Democrat, Arkansas) will dedicate the water system in ceremonies symbolizing an industrial renaissance in this northern Arkansas area. The factory will be dedicated in January.

Federal officials administering the $394 million depressed areas program hope that the Mountain Home story will soon be duplicated in struggling communities across the country.

Here is what a $535,000 air-conditioned one-story building, financed with a local bond issue and a $160,000 Federal water system, has meant to this area:

Families who were planning to leave the area, where counties have lost up to 30 percent of their population in the last decade, have decided to stay because there is now work at least for women.

Some families with little or no income for several years now have $40 or more a week in take-home pay, and this is a substantial sum in an area where waitresses get $15 a week and store clerks only $25.

Children are going to school better dressed and better fed.

Merchants are prospering, with much of the $26,000-a-week shirt factory payroll being spent immediately for food, clothing, and home furnishings.

Women who had never, for example, been in a beauty shop are now having their hair done every week or two.

Standing in a weed-filled, river-bottom field that had yielded little corn this year, strapping Gene Alexander rested a moment from the backbreaking job of picking the meager crop by hand and talked about the shirt factory.

His 32-year-old wife, Ettie Mae, was working in the factory and liking it fine, but husband Gene was not so sure an Ozark woman's place was behind a sewing machine 8 hours a day. (Nine out of ten of the plant's employees are women because they can sew better than men.)

Even though Ettie Mae's job means that her mother must look after her 5- and 10-year-old daughters, the Alexanders like that money every week. They hope to save enough to build a modern home to replace the unpainted and unsightly farmhouse they now have.

Across the ridges in another valley lives 17-year-old Maudy Jane Clark, whose shirt-factory earnings help support her mother and father and 7 younger brothers and sisters. Maudy Jane's father used to work on the railroad but has not had a job in 3 years.

At 39 her mother is 4 years over the hiring-age limit of 35 set by the factory, but if the age limit were raised Mrs. Clark would be one of the first to apply for a job.

Sharon Baker, the 18-year-old daughter of a 70-percent disabled veteran who says he cannot hold down a job, is saving some of her shirt-factory earnings so she can go to business school.

Wherever you go in Marion and Baxter Counties the Mar-Bax Shirt Corp. is generally regarded as a godsend to the people of these scenic but poor hills.

Mountain Home sits between two meandering lakes formed by Army Engineer dams on the White and Norfork Rivers. The dams were constructed during the last 15 years and form Bull Shoals and Norfork Lakes.

The lakes bring in fishermen and tourists and have attracted retired persons from the Midwest who have established year-round homes in this area.

But the resort business, the construction boomlet caused by the influx of retired persons and the traditional agricultural economy were not enough.

Tourism is a seasonal, low-paying and precarious industry at best. The construction business is often unstable too.

The farms are too small and their soil is too poor to compete with modern agricultural practices in fertile areas.

An average farmer in the area is likely to have a net cash income of only $1,500 a year from the sale of milk, cattle or poultry. His farm generally includes no more than 120 dusty, rocky and rolling acres.

In Baxter County alone the number of farms has declined from 1,300 to 700 in the last 20 years.

In adjacent Fulton County only 4 of the 40 members of the 1941 high school graduating class are still in the area. (Arkansas and West Virginia were the only two States that lost population from 1950 to 1960.)

So when in the summer of 1960 the Arkansas Industrial Development Commission (headed by Winthrop Rockefeller, who lives on top of a mountain near Little Rock) found a shirt manufacturer looking for a plant site in the Ozarks, Mountain Home was ready to do almost anything to collar him.

The manufacturer's conditions, which will be discussed in a subsequent article, demanded much of the community. But like most other depressed areas, Mountain Home, whose only industrial asset is people willing to work at almost any wage, was willing to pay dearly for industry.

A $535,000 bond issue to finance the building demanded by the manufacturer was voted by Marion and Baxter Counties with the support of nearly all the area's businessmen. Opposing the project were the retired men and women, who feared tax increases.

Then last spring, when the counties discovered that they lacked a well, water mains and a tank to supply the plant—and the resources to pay for such a water system—the Area Redevelopment Administration provided $160,000 in Federal aid—$129,000 in a grant and $31,000 in a loan.

Now, even before the water system is dedicated and before the shirt factory is in full operation, there is talk of a second plant moving into the area to manufacture shirt boxes.

The shirt factory and the water system have been good for these Ozark hills. They have kept people here who want to stay but who otherwise would have been forced to leave because of the lack of opportunities. In a small way the rush to the cities has thus at least been slowed down.

The Mountain Home experience has also demonstrated once again that industrial workers can be plucked directly from the life of farm and valley, town and village, and put into production on demanding assembly lines within a matter of weeks.

But will the national good be served by the Mountain Home project, and all the other community and federally subsidized industrial development projects that will flow from the depressed areas loan and grant programs?

The Mountain Home projects—and so many others like them—are built on shaky foundations of low wages, antiunion commitments on the part of a community, and heavy public subsidies to unstable industries seeking out low-wage and even subservient areas.

However, much such projects may help farm women of the Mountain Home area and countless other communities like it, they raise disturbing questions of public policy and economic development in the highly industrialized American society of today that the people of these hills and valleys have embraced so enthusiastically.

[From the Washington Post, Dec. 9, 1961]

A DEPRESSED AREA CHANGES—II

MOUNTAIN HOME TERRITORY DIDN'T GET ITS INDUSTRIAL REVOLUTION FOR NOTHING

(By Julius Duscha, staff reporter)

MOUNTAIN HOME, ARK.—To get a shirt factory employing 500 women at low wages this depressed area had to:

Provide a modern, air-conditioned building financed with a $535,000 bond issue.

Lease the 75,000-square-foot, one-story building to the shirt company for 35 years at a monthly rental of $1,500, a sum that is not large enough to cover the cost of the structure and interest on the bond issue.

Raise real estate levies $6 a year for the average taxpayer to make up the $90,000 difference between the cost of the plant and the rental income.

Allow the shirt manufacturer to renew his lease for another 64 years at a token cost to him of only $1 a year.

Maintain the building and its 20-acre site, which is in a field 7 miles west of here and a half mile east of the tiny town of Gassville, Ark.

Furnish temporary quarters, at a cost to area businessmen of at least $10,000, so workers could be trained and production could begin before the new building was completed.

Obtain $160,000 in aid from the Area Redevelopment Administration—the first grant and loan under the new depressed areas program—to build a water system adequate to the needs of the plant.

Agree not to encourage the location of any plant in the area that would compete with the shirt factory for women workers.

Become partner to a further agreement that in effect pledges the community to help the company keep a union out of the plant.

"We would have to pull out if this plant were unionized," Donald Cooper, the owner of the shirt company, bluntly told a citizens' meeting.

"We would continue to pay the rent on the building." he added, "but there would be no payroll."

There is no strong union sentiment in this largely rural Ozark area of northern Arkansas. Nevertheless, the AFL-CIO Amalgamated Clothing Workers regional office in Little Rock already has distributed leaflets and application cards to the workers at the new Mar-Bax Shirt Co.

In exchange for their money and promises, the people of Marion and Baxter Counties got their first real industry. They also have new hope that migration from the area will be slowed down, if not stopped, and that other industry will follow the shirt factory across the ridges and through the pleasant but economically depressed valleys.

SATISFIED COMMUNITY

The dedication of the water system today by Senator J. W. Fulbright, Democrat, of Arkansas, was looked upon by people here almost as the symbolic rebirth of the community.

Most of the businessmen, farmers, and workers in these hills think that the $26,000-a-week factory payroll is in itself ample return on the community's investment.

As one Mountain Home businessman said, "We know our only industrial resource is people. And we also know that industry won't come here unless we make it darn attractive for them."

Cooper, the man who is running the shirt factory, previously operated two plants in Tennessee, and his father was in the textile business before him.

Now considered a great benefactor to the people of the Mountain Home area, Cooper is always referred to as "Mr." and sometimes his name is pronounced almost with reverence by these religious hill people. He lives in New Jersey.

His last Tennessee plant, at Lafayette, was in a community-built structure that he leased under an arrangement similar to the one he now has for his new Mar-Bax Shirt Co.

OUTLAY OF $500,000

The agreement that Cooper negotiated with the Ozark businessmen, who set up a development corporation to construct and operate the building, is not unusual in industry-starved Southern States where bonds may be issued to pay for industrial structures.

And Cooper bought more than $500,000 worth of new sewing, cutting, pressing, and other equipment for the plant. The machinery inside the neon-lighted, bright, and pleasant building is as modern as the concrete-block and brick construction.

Businessmen and others in the Mountain Home area believe that the building is as much of an asset to the community as a new armory or high school.

They also look upon the federally financed well, 250,000-gallon water tank, and 10-inch water main, as vital assets to the town of Gassville.

The businessmen think the building will be attractive to some sort of industry for many years, whatever happens to the shirt factory.

MUCH THAT IS TYPICAL

One bond issue, one Federal grant, and one loan do not, of course, add up to a depressed areas program. But there is much in the Mountain Home situation that is typical of the problems facing the new Area Redevelopment Administration.

Most of the chronically depressed areas have no resource other than unskilled labor. Most of the areas also are ready to meet industry's terms, however unfair or generous they might seem to labor unions or businessmen in heavily industrialized cities.

Low-wage, highly competitive industries as well as companies seeking to escape from high-cost, unionized areas generally seek out the depressed areas.

Even though there are prohibitions in the depressed areas legislation against aiding runaway plants or other avowedly and irrevocably antiunion projects, these problems often do not present themselves in black-and-white terms.

The $394-million Federal program not only provides for grants and loans to help communities build water and sewer systems and othe public improvements that would help attract industry; the program also offers aid to both rural and urban areas that want to furnish buildings for industry.

SOME IMPLICATIONS

So the Federal Government finds itself in the position of assisting low-wage, precarious industries that unquestionably help the Mountain Homes of America but do not always advance national economic goals of high wages, increased productivity, sound investment and healthy profits.

But in places like Mountain Home—where the percapita income of the area is little more than $600 a year, where 1,500 persons out of a countywide population of 10,000 have been getting surplus food, and where $1.50 an hour is a high wage—it is hard to argue national economic policy versus the desperate needs of the depressed areas.

Perhaps the importance of a job—any kind of a job—to a small town and rural community like the Mountain Home area can best be summed up in a single sentence that was the first social note from Gamaliel, Ark., in last week's issue of the Baxter Bulletin.

"Miss June Lane," the item read, "is working at the Mar-Bax shirt factory."

(Whereupon, at 11:30 a.m., the committee was adjourned.)

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