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JANUARY 1964 ECONOMIC REPORT OF THE PRESIDENT

HEARINGS

BEFORE THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

EIGHTY-EIGHTH CONGRESS

SECOND SESSION

PART 2

INVITED COMMENTS

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JANUARY 1964 ECONOMIC REPORT OF THE PRESIDENT

The following letter was sent to 19 organizations inviting them to submit written comments on the materials and recommendations contained in the 1964 Economic Report of the President. The comments were given consideration by the Joint Economic Committee in the preparation of its annual report on the President's Economic Report:

JANUARY 9, 1964.

DEAR MR. ———: Because of the pressure of the legislative calendar, and a statutory deadline of March 1 for filing our annual report, our schedule of hearings on the 1964 Economic Report of the President has had to be shortened. Therefore, the Joint Economic Committee is calling upon a number of leaders of banking, business, labor, agriculture, and consumer organizations to secure written statements of economic facts and counsel for consideration in the preparation of its report.

We would appreciate having your comments on the materials and recommendations contained in the 1964 Economic Report of the President, including the annual report of the Council of Economic Advisers. In order that the members of the committee and staff may have ample time to consider these written statements, they should be received no later than February 5.

If you are willing to prepare such a statement, please let us know so that we can send you a copy of the President's Economic Report by the 20th of this month. We will also send you a list of the others participating.

It would be of assistance to the committee if we could have 20 copies of your statement for distribution to the members of the committee and the committee staff. Such comments as you care to give us will be made available to the public through a printed volume of the invited statements.

Faithfully yours,

PAUL H. DOUGLAS, *Chairman.*

Listed below are the organizations which were invited to submit written comments:

American Bankers Association.
American Farm Bureau Federation.
American Federation of Labor & Congress of Industrial Organizations.
Chamber of Commerce of the United States of America.
Committee for Economic Development.
Conference on Economic Progress.
Consumers Union.
Federal Statistics Users' Conference.
Life Insurance Association of America.
Machinery & Allied Products Institute.
National Association of Manufacturers.
National Association of Mutual Savings Banks.
National Farmers Union.
National Federation of Independent Unions.
National Grange.
National League of Insured Savings Associations.
Railway Labor Executives Association.
United Mine Workers of America.
United States Savings & Loan League.

JANUARY 1964 ECONOMIC REPORT OF THE PRESIDENT

THE AMERICAN BANKERS ASSOCIATION

INTRODUCTION

The American Bankers Association is in strong agreement with the objectives of national economic policy which are enunciated in the 1964 Economic Report of the President. Improvement in the Nation's balance of international payments, avoidance of inflation, a stronger and more productive private economy, expansion of job opportunities, and further progress in reducing the incidence of individual poverty are, indeed, the worthy objectives toward which the Nation should strive in 1964. Agreement on these objectives does not provide, however, a basis for agreement as to how the instruments of national economic policy should be used to attain the desired ends.

Traditionally, both in the United States and abroad, policymakers have experienced considerable difficulty in devising short-term policies which make maximum and simultaneous contributions to these objectives. These difficulties reflect neither deficiencies in man's wisdom nor the special characteristics of free-enterprise economies. Many of the same difficulties are present, in fact, in Socialist and Communist countries. The difficulties reflect, instead, the fact that policies which are the most productive of short-term gain can also be highly destructive of long-range potential. Recognition of this fact is a fundamental requirement for the determination of sound economic policy, for it highlights the importance of distinguishing between economic expansion which is attainable in the short run and expansion which is sustainable in the long run. Unless a nation's policymakers draw this distinction and use it as a standard against which policy recommendations are measured, the longer range economic well-being of the public is likely to be mortgaged for an interim period of high-level prosperity.

Few of the Nation's citizens knowingly would approve of such a bargain, and responsible governments do not knowingly strike it. Nevertheless, the initiation of boldly expansionary policies generally involves the risk that seeds of future economic instability may be sown. In examining the economic program outlined in the Economic Report of the President (and in the appended Annual Report of the Council of Economic Advisers) we have paid special attention to the need for assessing and minimizing these risks. We bring to our analysis of the administration's reports the following assumptions:

1. Economic expansion in 1964, however spectacular it may be, will impose severe hardships on the American people if it is secured through means which jeopardize improvement in the Nation's balance of payments and thereby threaten the stability of the international monetary system. Should this consequence

ensue, difficulties of preserving existing levels of income, output, and employment would be great—both in the United States and elsewhere around the free world.

2. Economic expansion in 1964, however favorable its short-term impact, will produce a highly unfavorable climate for sustainable economic growth if it is accompanied by a revival of price inflation. Such a revival would be highly injurious to the Nation's international financial strength, an essential requirement for economic stability in this country and elsewhere. It also would sow other seeds of domestic economic instability and thereby jeopardize the maintenance of continuing, high-level employment.

3. Economic gains in 1964 regardless of their magnitude, will cost the American people a heavy price in terms of future jobs, income, and living standards if the gains are secured through means which require the throttling of basic economic freedoms. If a market economy is to prosper, grow, and provide an increasing volume of job opportunities, competitive market forces which determine the allocation of resources (including manpower) and influence the rate of private investment must be allowed to operate without undue interference. Measures which weaken the basic strength of the economy do permanent damage to the Nation's long-range growth potential.

Many aspects of the administration's proposals reflect a fundamental awareress of the points listed above. Others do not. Our overall judgment is that the President's fiscal-policy recommendations provide for considerable stimulus to the economy without presenting necessarily insuperable barriers to improvement in the balance of payments, to the maintenance of price stability, or to the preservation of free-market processes which are essential to the favorable performance of the economy over time.

The possibility for implementing the President's fiscal-policy recommendations without encountering such barriers rests, however, on the willingness to employ both monetary policy and debt management with a greater degree of flexibility than is indicated in the administration's reports. We are not alarmed over the administration's fiscal program. We are deeply disturbed, however, over indications that the administration's attitude toward monetary policy and debt management may be so doctrinnaire as to make it hazardous to embark on the expansive fiscal program proposed.

FISCAL POLICY

Realization in the 1965 fiscal year of the target levels established in the President's budget would be a major accomplishment for the administration and a source of benefit to the Nation's economy.

In budgeting the 1965 expenditures at $97.9 billion—or $500 million below the 1964 level—the administration has taken an important step toward lessening the impact of tax reduction on the Government's fiscal position and toward reducing (though not eliminating) the inflationary potential inherent in a tax cut at a time of high-level business activity. It has been the position of the American Bankers Association for some time that fiscal prudence requires a leveling of Government expenditures during the transition to lower tax rates. The President's expenditure program for fiscal 1965 is therefore consistent with our view that expenditures can and should be held constant while the immediate impact of tax reduction is being reflected in lower Federal receipts.

We realize that holding expenditures to $97.9 billion in the 1965 fiscal year may be somewhat more difficult than is indicated in the President's budget. We note, for example, that budget expenditures reflect, as a deducted item, proceeds from the expected sale of $2.3 billion in Government-held mortgages and Export-Import Bank paper, that the prospects for realizing a projected decline of $1.2 billion in expenditures for agriculture are highly uncertain, and that some administration-backed programs are either not included in the budget or carry surprisingly low price tags. Despite these indications that difficulties may be encountered in holding expenditures to the budgeted level, the emphasis on frugality which is apparent in the budget for 1965—and which we would hope to see followed up as the months progress—receives our wholehearted endorsement.

Whether or not the size of the deficit in the administrative budget can be reduced from $10 billion in 1964 to $5 billion in 1965 appears highly problematical. Accomplishment of this objective would require that the projected expenditure totals not be breached, and that relatively optimistic revenue projections be realized. There is room for doubting whether the estimate of $93 billion in budget receipts in the 1965 fiscal year will, in fact, materialize in the wake of enactment of the tax proposals now pending before the Congress. In this connection, we note that the delay to date in enactment of the tax bill will, in and of itself, reduce revenues in the 1965 fiscal year by at least $800 million below the budget estimates.

The fiscal program announced by the administration is unmistakably expansive. In the words of the President, it will provide a greater net stimulus than in any peacetime year in history—three times as great as in 1961, when the economy began its ascent from the trough of the 1960–61 recession. The introduction of this stimulus at a time when the economy is operating at high levels of output and employment obviously adds to the dangers of inflationary price developments. Indeed, as the President pointed out in his Economic Report, price increases already are occurring in a number of important lines of manufactured goods.

RISKS OF INFLATION

The existence of unused resources in the economy offers some protection against price increases as more expansionist policies take hold, but we are not optimistic over the prospects for price stability as a result of this factor alone. Along with a number of distinguished professional economists, we have serious misgivings concerning the approach used by the Council of Economic Advisers in computing the gap between the actual and potential levels of national output. Stout resistance should be offered any inferences that this gap (placed currently by the Council at almost $30 billion) can be taken as the measure of economic expansion which could be accommodated without generating serious inflationary pressures.

The added volume of national output which can be achieved without risking general price advances depends on a number of variables—

including the mobility of the unemployed and the quality of skills which they possess, the relative efficiency of idle productive capacity which is brought into play, the character of demand, and a number of other variables which the Council appears to regard as presenting no serious obstacles to substantial economic expansion without inflation.

A review of tendencies for a concentration of unemployment among unskilled laborers and of the disparity between areas of job opportunities and areas of high-level unemployment suggests, however, that the Council's estimates may be quite wide of the mark. Due attention to the fact that much of the capacity now idle is quasi-obsolete and cannot be brought into use without raising the unit costs of production also supports this conclusion.

Even without the obstacles to noninflationary expansion which are posed by inadequate mobility of labor, shortages of labor skills, and high-cost idle capacity, the development of production bottlenecks in individual industries as the economy draws closer to capacity traditionally has generated upward price pressures long before full employment is reached. This has been the experience of the United States throughout the postwar period, and there is small reason to believe that normal cyclical occurrences will not repeat themselves in future economic expansions. In fact, the seemingly rising importance of structural unemployment (while still perhaps not the dominant portion of the unemployment total) would suggest that price pressures may become noticeable at unemployment rates somewhat higher than in other recent years.

The likelihood that this may happen would be strengthened even further by enactment of certain of the administration's labor and manpower policy recommendations. In particular, we cite the definite inflationary implications of the recommendation for an extension of overtime coverage to 2,500,000 additional workers, and the recommendation that legislation be enacted to authorize higher overtime penalty rates. If these steps are to be taken within the framework of adherence to the administration's wage-price guidelines, they necessarily will mean that employees working in the industries affected cannot be granted the same increases in hourly wage rates which they otherwise might expect.

In short, it is our judgment that economic expansion capable of producing a 6-percent growth in gross national product in 1964 ($623 billion is the midpoint of the range estimated by the Council of Economic Advisers) is also capable of producing substantial upward pressure on prices. Whether or not such vigorous economic expansion can be achieved is open to question. Certainly, in view of the GNP forecasts made by the Council in its 1962 and 1963 reports, the latest forecast must be regarded as being subject to a wide margin of error.[1]

The important point, however, is that prospects for expansion at a rate reasonably near the Council's forecast underscore the critical importance of maintaining policies which effectively will contain the inflationary impetus to which rapid expansion inevitably will give rise. If such policies are not maintained, the Nation's international financial position will be exposed to irreparable harm, and the task of maintaining a continuing high level of employment in the years to come will be all the more difficult.

[1] The Council's forecast of GNP for 1963 was only slightly smaller than the recorded figure, but this forecast was based on the assumption that there would be a major tax cut retroactive to July 1, 1963.

MONETARY POLICY

We therefore are profoundly disturbed by inferences in the President's Economic Report that the avoidance of inflation can be accomplished by principal reliance on voluntary adherence to the administration's wage-price guideposts. Monetary policy appears to be relegated to a role of secondary importance as a means of resisting inflation. While the need for flexibility in monetary policy is cited, the favorable implication of this reference tends to be negated by the definition which the administration apparently assigns to flexibility.

Flexibility in the administration of monetary policy does not consist, as the President's Economic Report suggests, of a willingness to shift on quick notice from one policy objective to a different objective requiring totally different monetary actions. Such a suggestion is contained in these remarks: "Monetary and debt policy must be directed toward maintaining interest rates and credit conditions that encourage private investment. But monetary policy must remain flexible, so that * * * it can quickly shift to the defense if, unexpectedly, inflation threatens or the balance of payments worsens." Further insights into the administration's concept of flexibility in monetary policy are provided by the characterization of monetary measures as "defensive shock troops" which, when not needed for this purpose, "can reinforce fiscal policy in promoting domestic expansion."

In commenting on these remarks, we would stress the inability of monetary authorities to shift directions so completely while retaining any effective degree of monetary control. The liquidity provided the economy through a policy aimed primarily at maintaining low interest rates and credit ease cannot be withdrawn quickly in the event that inflation becomes overt. For this reason, monetary policies which are not responsive to the threats of inflationary developments as they accumulate are virtually certain to lead to substantial and rapid price increases; and the inflation will not cease with the last-minute adoption of a restrictive monetary policy. Flexibility in monetary policy means, in fact, the preservation of a monetary posture which enables the central bank to deal quickly and effectively with economic developments as they occur. In a period of rising economic activity and strong demands, this generally means that the monetary authorities should not provide additional liquidity at a rate which is sufficient to prevent upward adjustments in interest rates and some reductions in credit availability. Failure to observe such prudence in monetary policy would result in the provision of excessive amounts of liquidity, which would lay the basis for substantial price inflation at a subsequent point in the expansion. Excessive liquidity may, in fact, be withdrawn from an economy operating at high levels—but only at the risk of generating serious deflationary pressures.

We do not say that the economic prospects point unequivocally to the need for less easy credit conditions in 1964. Whether or not less abundant credit will be appropriate will depend heavily on the strength of the economy in general and on the vigor of credit demands in particular. Faced with the prospect for substantial fiscal stimulus and with administration forecasts for sharp economic expansion, however, we are concerned over inferences that a tightening of money—without reference to the strength of credit demands—would be "self-defeating."

It would be easy for the purposes of the tax cut—including improvement in the balance of payments, cost reductions in domestic production, and improvement in the long-range performance of the economy—to be defeated by the inappropriate use of monetary policy. In this respect, however, the major danger lies in an inflexible commitment to credit ease and stable interest rates independent of developments in the strength of economic activity or credit demands.

It is important to stress, also, the serious implications of concern that flexible monetary policy might lead to a "canceling" of some of the economic stimulus being provided through tax cuts. One of the principal objectives of monetary policy is to restrain the development of speculative excesses and structural imbalances which may lead to serious economic dislocations. Whether or not the maintenance of this objective will require a shift to less easy credit conditions as the effects of tax reduction begin to take hold cannot be foretold. Attempts to decide this question in advance, however, and to preclude the use of monetary restraint if that should become necessary, reflect a disturbing tendency to emphasize short-term economic expansion at the expense of longer range stability.

On the basis of past performance, it cannot be concluded that the monetary authorities will be overzealous in applying the brakes to economic expansion. Such brakes are often needed, however, and it is conceivable that they might be required to "cancel" excessive stimulus as the existing business expansion goes forward. For this reason, we would feel more comfortable if the administration had stressed the availability of monetary policy to hold the expansion within bounds. Instead, virtually all of its emphasis is on the capacity of monetary policy to provide, along with fiscal policy, an expansive influence on the economy. This emphasis is disturbing in view of the fact that limited inflationary pressures already are present and can be expected to intensify as the economy is boosted to higher levels.

This emphasis is disturbing, also, in its reflection of dedication to the belief that the absolute level of interest rates is of decisive importance in determining the rate of private investment—the mainstay of economic growth. This inordinate concern over the level of interest rates—separate and apart from all other influences on the incentives to invest—enables the Council of Economic Advisers to criticize freely the credit tightening moves which have taken place in previous periods of intense business activity. It also appears to account for the Council's failure to discuss the contribution of credit ease in recent years to (*a*) a trend toward deterioration in the quality of credit, and (*b*) large capital outflows from the United States. These developments could seriously endanger the Nation's longer term economic prospects.

According to the President's Economic Report, the possibilities for avoiding reductions in credit availability and increases in interest rates are especially favorable because "* * * our balance of payments is improving so sharply in response to measures begun in 1961 and reinforced last July," and because "* * * the budget for fiscal year 1965 will cut the Federal deficit in half and ease pressures on interest rates from Treasury borrowings."

For reasons advanced subsequently, we are more cautious than the administration in our appraisal of improvement in the balance of payments. The recent behavior of the international accounts offers no assurance, it is clear, that monetary policy can be oriented toward more expansionary domestic objectives.

With respect to the suggestion that a smaller Treasury deficit may relieve pressure on interest rates, we may note that there are grounds for considerable skepticism: the projected budget deficit of $4.9 billion reflects a conservative estimate of expenditures and a fairly generous estimate of revenues; it therefore could exceed the projected level by a considerable margin. It should be noted in this connection that in the 1955–63 fiscal years, budget estimates submitted in January have understated the amount of the ensuing year's deficit by an average of $3.9 billion. Even if the tradition is broken in the 1965 fiscal year, it must be borne in mind that the projected deficit is $2.3 billion smaller than it otherwise would be by virtue of the budgeted sale of Government-held mortgages and loans. The interest rate impact of these sales will not be substantially different from the sale of a like amount of Government securities—the traditional means of financing a deficit.

Our interpretation of the administration's comments on monetary policy does not strengthen our confidence in the prospects for price stability in this country. Other interpretations may be possible, but the statements suggest to us that monetary policy, the traditional means through which inflation is resisted in this and all other free market nations, is to be effectively removed from the arsenal of economic stabilization tools. Within the context of the President's report, moreover, they suggest a major shift of emphasis in the attack on price inflation: the wage price guideposts, instead of serving as a second line of defense behind monetary policy, apparently are expected to become the major instrument for combating price inflation.

We hope that such a shift in emphasis is not contemplated, and we lay heavy stress on our conviction—indeed, our knowledge—that there is no effective substitute for the flexible administration of monetary policy in combating advances in wages, costs, and prices. Monetary policy must be the first line of defense against such advances. Attempts to devise substitute measures will lead inexorably in the United States—as they have led in every other country where the attempt has been made—to rapid advances in prices and to swift deterioration in the balance of payments.

One of the essential requirements for the successful implementation of tax reduction is, in fact, the maintenance of complete flexibility in the application of monetary control measures. We have consistently stressed this point in our discussion of proposals for tax reduction, and our past endorsements of proposed tax cuts have made explicit our opposition to a tax cut unless a flexible monetary stance is preserved. At the 88th annual convention of the American Bankers Association in September of 1962, this position was elaborated as follows:

"* * * the implementation of a program of tax reduction must be accompanied by a willingness to employ maximum flexibility in the use of debt management and monetary policy, including a willingness to rely on market forces for the determination of long-term rates of interest. In this connection, we cite the experience of rapidly growing countries around the world as evidence that the crucial prerequisites for sustained economic growth are strong incentives for capital investment—rather than the absolute level of interest rates as such."

We can see no greater obstacle to flexible monetary policy than the view that the development of somewhat tighter credit conditions, should this occur in the course of the economic expansion now underway, would represent a "canceling" of the stimulus of tax reduction and would be "self-defeating."

WAGE PRICE GUIDEPOSTS

In the statement which we submitted to the Joint Economic Committee last year, we commented at considerable length on the administration's guideposts for noninflationary wage and price decisions. These guideposts, originally set forth in 1962, may have served a useful purpose in helping to clarify public understanding of one aspect of the process of inflation, although they will have proved harmful if they serve to obscure inflation's basic monetary origins. It is not observable that they have been widely followed by business or labor in wage and pricing decisions. Nor is it clear that an individual firm could determine how its wages and prices should behave in conformity with the guideposts.

Difficulties in securing wage settlements and pricing policies consistent with the guideposts have been evident in both 1962 and 1963—even against a backdrop of relative price stability and larger idle capacity in the economy than now exists. The difficulties can be expected to be magnified many times over in an environment of improved business conditions and strong demand for labor in most labor markets.

It may be true that little or no harm can come from exhortations calling for business and labor restraint in wage and price demand, although even this is doubtful if business confidence in the freedom of market processes is threatened. Certainly a great deal of harm can flow from relying on the effectiveness of a policy of exhortations, however. Similarly, major damage would be done to the strength and viability of the economy if what begins as moral suasion should drift toward direct Government control. For these reasons, we reemphasize our conviction that the wage price guideposts can serve in no way to relieve the necessity for monetary measures constantly attuned to the need for price stability.

BALANCE OF PAYMENTS

We have believed for some time that a major tax cut of sound structure, carried out within the framework of fiscal prudence and monetary discipline, would bring benefits to our balance of international payments. These benefits should consist of (*a*) an improvement in the domestic climate for direct (plant) and portfolio (security) investment—particularly direct business investment; and (*b*) greater efficiency of production in this country, flowing from the impetus given to direct investment and leading to improvements in the competitive position of American producers in international markets. Thus, the initiation of tax cuts has been expected to produce short-term reductions in the volume of capital outflows from this country and longer range improvement in the Nation's trade surplus.

At the same time, it has always been recognized that the short-term impact of tax reduction on the Nation's trade surplus would be adverse as a result of the stimulus to imports which would be provided.

On balance, the adverse impact on the trade surplus has generally been expected to be somewhat less than the net improvement in capital accounts.

It is important to stress, however, that the ability of a tax cut to produce a decline in the outflow of funds is dependent upon the extent to which it produces (*a*) somewhat firmer interest rates in the United States as expansive forces generate enlarged credit demands and stronger business conditions; and (*b*) greater profitability of direct investment in this country.

The Economic Report of the President raises a serious question as to whether these favorable influences can be expected to operate. As previously noted, the report carries the strong implication that maximum efforts will be made to avoid upward adjustments in interest rates. Moreover, the Council's discussion of its wage price guideposts contains repeated warnings that rising profits constitute a lure for strongly intensified wage demands and that workers become "restive" in industries where above-average gains in productivity and profits are occurring.

These aspects of the administration's reports suggest that the favorable implications of a tax cut for the balance of payments must be considered as highly tentative. And, since any delay or inadequacy in the use of monetary policy could result in price inflation and an even greater impact on the trade surplus than generally has been forecast, the overall implication of the administration's reports is that the Nation's international financial position could be subjected to a severe jolt.

It should be stressed, moreover, that fundamental improvement in the balance of payments has not occurred over the past year, and the Nation's international financial position continues to remain vulnerable. The balance-of-payments deficit on regular transaction—the most meaningful measure of our balance-of-payments position—was roughly $3 billion in 1963, representing no improvement from the 1961 level. Even so, the deficit was held down to this level only by virtue of the sharp decline in capital outflows following announcement of the proposal for an interest equalization tax. There is a serious question as to whether the dramatic impact of this proposal may not be largely of a temporary nature—and that these outflows will again resume an upward trend. This possibility would be greatly strengthened, we might add, if a seeming aversion to flexible monetary policy should find reflection in tardy and insufficient responses in the use of monetary controls.

On balance, we see opportunities for some improvement in the balance of payments as a result of the administration's fiscal program (including tax reduction)—provided that this program is carried out within a framework of continuing monetary discipline. If this discipline is not maintained, we would expect serious deterioration in the Nation's international financial position.

THE ATTACK ON POVERTY

We believe that the greatest contribution that can be made by this or any other administration toward the elimination of poverty in the United States lies in the wise use of general instruments of economic stabilization. Specialized efforts to attack poverty, however extensive and well designed, cannot begin to produce the results which flow naturally from the maintenance of a strong, healthy, and prosperous economy. It is for this reason that we lay such heavy stress on the need for avoiding inflation, which reduces the real income of pensioners and other fixed-income groups and jeopardizes the achievement of continuing high-level employment.

We believe, nevertheless, that the program outlined by the administration for promoting greater strength in the private economy will not—at least in 1964—provide a complete solution to the problem of unemployment or the incidence of poverty among individuals who strive for improvement in their own standard of living. Accordingly, we are entirely sympathetic with the objectives which the administration would seek to serve through more selective approaches to the elimination of poverty. We agree, also, that the attack on poverty should be assigned a high priority, and we see no reason why the expenditures of amounts recommended by the President—even though likely to grow in future years—cannot be accommodated within the framework of fiscal responsibility. Should difficulties in the allocation of priorities become even more pressing, there are many Government programs which could be sacrificed with less damage to the national interest.

We are not able, on the basis of the general steps outlined in the administration's reports, to evaluate the individual avenues along which the attack on substandard levels of living may proceed.

SUMMARY

Our analysis of the Economic Report of the President leads us to the following conclusions:

1. The fiscal program outlined by the President appears to fit well into the Nation's requirements for an expansionary program which couples short-term stimulus with the removal of deterrents to longer term growth which now stem from an excessive tax burden.
2. Inflationary pressures which could be generated by an expansive fiscal program require that monetary policy remain entirely flexible in order to maintain maximum safeguards against a price upsurge. The President's report suggests that the administration is not fully sympathetic with the need for flexible monetary policy.
3. In the defense against inflation, principal reliance must be placed on monetary policy. Wage-price guideposts are certain to prove ineffective in preventing inflationary wage and pricing policies.
4. Contrary to the tone and emphasis of the President's report, the Nation's balance of international payments showed little fundamental improvement in 1963. Policies for the defense of the dollar—including monetary policy—remain as vital as ever. Reductions in credit ease and upward adjustments in interest rates—developments which could flow naturally and without harmful effects on the domestic economy if an expansive fiscal policy were pursued—would be beneficial to the Nation's international payments position. If economic expansion and enlarged credit demands are not allowed to be reflected in shifting credit conditions, however, serious international financial difficulties are likely to ensue.

5. The most effective attack against poverty is the maintenance of a strong, healthy, and prosperous economy. Still, we see the need for specialized efforts to reduce the incidence of individual poverty and to improve opportunities for those who feel the crush of its burden. We are not able to evaluate the overall merits of the President's attack on poverty, however, because of the general nature of the recommendations which are made.

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THE AMERICAN FARM BUREAU FEDERATION

By W. E. Hamilton, Director of Research

We appreciate the opportunity to comment on the Economic Report for 1964. Our comments will be directed to the major issue of whether the outlook for Federal revenues and expenditures is such as to justify a general reduction in taxes.

Prior to the submission of the Economic Report, the elected voting delegates to our last annual meeting adopted a policy statement which reads, in part, as follows:

"We recognize the need for a substantial downward adjustment in Federal taxes to create a better climate for economic growth; however, the current budget deficit and our mounting national debt make it mandatory that a cut in Federal expenditures accompany any general reduction in taxes.

"We reaffirm our recommendation that authorizations for new Federal spending be reduced sufficiently to permit both a tax cut and progress toward a balanced budget * * *."

The Economic Report indicates that even with the proposed tax cut "* * * we shall hold the fiscal 1965 budget below the fiscal 1964 budget, and cut the deficit in half * * *."

Such an achievement would represent real progress; however, on the basis of a preliminary examination of the budget proposals for the U.S. Department of Agriculture, we are concerned that the projected reduction in the Federal deficit may be more apparent than real.

The budget for fiscal 1965 proposes a reduction of $1.3 billion in new spending authority (new obligational authority or appropriation) for the U.S. Department of Agriculture. The proposed reduction reflects certain assumptions with respect to new legislation and a number of changes in funding procedures. As a result, it is by no means certain either that the proposed reduction in new spending authority will be achieved or that it would be followed by a comparable reduction in actual expenditures.

The proposed reduction in new spending authority is, of course, the net result of individual increases and decreases. Some of the major items showing a reduction in new spending authority are discussed below.

RURAL ELECTRIFICATION LOANS

Legislation is being requested to put the REA loan program on a revolving fund basis. This would permit current receipts from previous loans to be used for new loans with a resulting reduction in new spending authority of $347 million in 1965. The transfer of loan receipts to a revolving fund would, of course, reduce the need for new spending authority at the expense of Treasury receipts. The revolving fund would be started with 1964 loan receipts, so loan receipts estimated at $169 million for 1964 and $178 million for 1965 would be available to reduce new spending authority in 1965. The effect would be a bookkeeping reduction in Treasury receipts in both 1964 and 1965 with an offsetting reduction in new spending authority equal to the loan receipts for 2 years showing up in the 1965 budget. This apparently would improve the balance of the 1965 budget at the expense of a larger 1964 deficit although it would not affect the actual cost of the program in either year.

MEAT INSPECTION

Legislation is being requested to put the Federal meat inspection on a self-supporting fee basis. This would result in a reduction of $30.8 million in spending authority for 1965. In the past Congress has refused to pass such legislation on the ground that meat inspection is a compulsory service performed for the protection of the public health rather than the benefit of the livestock industry.

POULTRY INSPECTION

Legislation is also being requested to place the Poultry Inspection Service on a fee basis with a consequent reduction of $16.6 million in spending authority for 1965. As in the case of meat inspection, poultry inspection has been financed by public funds, because it is a compulsory service performed for the protection of the public health

COMMODITY CREDIT CORPORATION

The budget shows a decrease of $1.26 billion in new spending authority for price support and related programs. A substantial part of this reduction is accounted for by the fact that reimbursement is being requested for only "a portion of its 1963 realized loss." As a result, the CCC's accumulated deficit is expected to increase by $723 million in fiscal 1965.

The proposed reduction in spending authority also reflects a proposal to relieve the CCC of the obligation to pay interest on Treasury borrowings which represent "past years' realized losses." This would not affect the overall financial position of the Government as it would reduce both receipts and expenditures, but it helps to hold down spending authority for price-support programs.

If the proposal with respect to interest for borrowings should be approved, the CCC borrowings of noninterest-bearing capital would amount to $3.8 billion at the end of fiscal 1964. This total would rise to $4.9 billion at the end of fiscal 1965. Assuming an interest rate of 3.5 percent, the proposed change in the CCC's obligation to pay interest would save that agency well over $125 million in fiscal 1965 at the expense of Treasury receipts.

The budget indicates that proposed legislation for new programs for cotton and dairy products will reduce expenditures $230 million in fiscal 1965. Details of the proposed new legislation are not available; however, both the Cooley cotton bill, which is pending in the Senate, and the Talmadge-Humphrey bill would increase the cost of the cotton program.

The budget apparently has made no allowance for the possible cost of a pending proposal for new wheat legislation which appears to have the support of the administration. The budget says "Export payments on wheat and wheat flour are not anticipated in 1965, as it is estimated that the domestic market price will fall below the competitive world price * * *"; however, the USDA is currently offering to pay a subsidy of 16 cents per bushel on Hard Red Winter wheat exported after July 1, 1964. Since we could export 600 million to 1 billion bushels of wheat, an average export subsidy of 10 to 15 cents per bushel could cost $60 to $150 million. Any payments that might be made on export wheat under the so-called voluntary certificate plan would represent additional expenditures.

The wool program is being shifted from an April 1–March 31 basis to a calendar year basis, and payments for both the 1962 and 1963 marketing years are to be made in fiscal 1964. As a result, the budget shows a reduction of $9.7 million in spending authority in fiscal 1965 although the actual cost of the program is expected to increase in the current marketing year. (On a marketing year basis Wool Act payments are estimated at $40.9 million for 1962, $32.6 million for 1963, and $51.5 million for 1964.)

In summary the projected reduction of $1.26 billion in new spending for the CCC reflects an increase of $723 million in that agency's accumulated deficit, $125 million in the form of an exemption from interest on borrowings, a doubling up of Wool Act payments in 1964, and highly speculative assumptions with respect to legislation affecting cotton, dairy products, and wheat.

SCHOOL MILK PROGRAM AND SECTION 32 FUNDS

The budget proposes to finance the school milk program through a transfer from a permanent appropriation for surplus disposal (sec. 32 funds). This will result in a reduction of approximately $100 million in spending authority in 1965; however, it appears that, in the absence of this shift, approximately $100 million of section 32 funds could be returned to the Treasury. The budget for 1964 indicated that $108 million of these funds would be returned to the Treasury at the end of the current fiscal year; however, as a result of an increase in expenditures in 1964 and the proposed shift of 1965 funds to the school milk fund, the budget indicates that no funds will be returned in either 1964 or 1965.

CONCLUSION

If the above items from the Department of Agriculture's section of the budget are illustrative of the entire document, we doubt very much that it will be possible to have both the proposed tax cut and a 50-percent reduction in the Federal deficit in fiscal 1965.

Farm program expenditures can, and should, be reduced through a sound revision of basic legislation; however, neither the administration's budget nor the farm message indicates any intention to make the kind of revisions that are needed from the standpoint of both farmers and taxpayers. We are confident that real reductions are also possible in other areas of Government spending.

A tax cut financed by a Federal deficit at a time when—as the Economic Report shows—the economy is already undergoing a sustained expansion could easily bring on a surge of inflation and set the stage for a painful readjustment.

In this connection we would like to call attention to the following extract from page 4 of the President's report.

In the nearly 3 years of unbroken expansion since early 1961:

GNP is up 16 percent, measured in constant dollars.

Industrial production is up 23 percent.

Civilian nonfarm jobs are up 2¾ million.

Personal income is up $70 billion, or 17 percent.

Corporate profits before taxes are up $17 billion, or 44 percent.

Net income per farm for 1963 is up almost $375, or 12 percent.

Total after-tax income of the American people is up $56 billion, or 16 percent.

Real disposable income per family is up more than $600, or 8 percent.

If the Congress should decide to apply the stimulus of a major tax cut at a time when the economy is already moving ahead at such a rapid pace, it will not only invite inflation, but will also reduce its ability to use tax reduction as a weapon against deflation at a later time when stimulative action may be needed. The best thing that can be done to guard against an overstimulus from the proposed tax cut is for the Congress to give the budget a searching examination and to make certain that the proposed cut in taxes is earned by real reductions in Government spending. We strongly urge that the Joint Economic Committee recommend such a course.

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

Persistent lack of balance in the American economy continues, today. We are now in the midst of one of the most prolonged economic recoveries ever experienced during peacetime. Corporate profits and dividends have risen even beyond the expectations of business itself. Average stock prices have soared more than 18 percent in 1 year. And Government economists have predicted that the economy will grow this year at a rate considerably higher than the average for the past decade.

Yet, underlying the glowing statistics which give an impression of a strong, vital America, an America which is on the move, there is evidence of another America—an America overrun with tragic waste of human and other resources, with poverty, with a deep and growing alienation of millions of nonwhite citizens, with urban congestion and deterioration, and countless other indications of the failure to realize our enormous potential for a better life for all Americans.

These underlying realities of American life have convinced the labor movement that the fundamental problem of our time is not the problem of inflation, nor the problem of balancing the budget or reducing the national debt, but the problem of achieving the kind of growth in the demand for goods and services which will bring about full employment and sustain it once we have achieved it. We are convinced that demand must grow fast enough to balance our rapidly expanding productive capacity—faster, certainly, than the 3.8 percent growth of last year which failed to prevent an increase in the rate of unemployment—and that much of this expansion in demand must flow from a more rapid rise in consumer purchasing power and much greater expenditures on badly needed public facilities.

We do not claim that such growth will solve all our problems. We do insist, however, that a fundamental part of the solution to many of the major problems which confront the American people as a whole, and the American worker in particular, lies in putting an end to the waste and underutilization of resources which has persistently plagued America since 1953.

The reasons for this conviction are compelling. They have been discussed many times before. However, they must be discussed once again in the light of recent developments.

THE DIMENSIONS OF THE UNEMPLOYMENT PROBLEM

In the introduction to its annual report this year the Council of Economic Advisers declared: "By all odds, the country's No. 1 economic problem is persistent unemployment. Indeed, this would stand near the top of any list of ills afflicting our society."

Unfortunately, however, the full dimensions of this problem are not spelled out in the Council's report. To appreciate the seriousness of our unemployment problem, the American people must be aware of the fact that while European countries have consistently enjoyed rates of unemployment of 2 percent or less in recent years, unemployment in the United States has not fallen below 3 percent since 1953 nor below 5 percent since 1957. In fact, at no time during the last decade have we even reached 4 percent—the unacceptably high level which the Council of Economic Advisers now regards as an "interim" target.

Instead, we have moved up to higher and higher levels of unemployment during each succeeding recovery period. The 1962–63 period on the average was slightly higher than that in 1959–60 and almost one-third higher than that prevailing in the 1955–57 period; and in 1963, a relatively prosperous year, the 5.7 percent rate of unemployment exceeded the rate in the recession year of 1954.

But even these figures fail to reveal the full extent of the problem. The 5.7 percent rate of unemployment in 1963 approaches 7 percent when the loss of man-hours due to involuntary part-time unemployment is counted.

In addition, estimates of the number of people who are not included in the official statistics because they have given up hope of finding jobs and are therefore not actively looking for work range from approximately 1 to more than 2 million. They account for additional unemployment of at least 1 percent and possibly 2 percent of the present labor force or even more. Consequently, the true rate of unemployment in 1963 was at least 8 percent and possibly 9 percent or more, rather than the 5.7 percent referred to in the Council report.

The magnitude of the job of restoring full employment under current conditions is enormous. It must not be underestimated. Even the goal of 4 percent by the end of 1966, cited by some members of the administration, would require the creation of jobs at a rate far beyond that of recent years. We would need, according to estimates in the President's Economic Report (estimates which we regard as far too low because they fail to make adequate allowance for the number of people who would be actively seeking work if more jobs were available), "at least 2 million more jobs today just to get rid of stubborn excess unemployment." Approximately 5 million more jobs would be needed to provide for the anticipated growth in the labor force by the end of 1966. Thus, based on conservative estimates, a total of almost 7 million jobs over and above the number in existence at the end of 1963 would be needed to reduce unemployment to 4 percent by the end of 1966.

On an annual basis, we would need about 2.3 million jobs, or more than twice the average number created annually in all the years since 1953, excluding the 2 recession years, in which employment declined. In addition, several million more jobs would have to be generated each year to offset the labor-displacing effects of increased productivity.

Obviously, we are not going to reach full employment by the end of 1966 under present programs. We are not going to reach even the totally unacceptable rate of 4 percent under such conditions. In fact, according to a recent study by Columbia University's Bureau of Applied Research, if present imbalances persist, the rate of unemployment is likely to double by 1970.

The question which logically follows is whether even the proposed changes in policy, including the reduction in taxes, are enough to reduce unemployment to the target level. Clearly, they are not enough. Even if all of the changes now contemplated are put into effect, the number of new job opportunities created during the year will still leave the official unemployment rate above 5 percent for the year as a whole. Furthermore, this slow decline in the rate of unemployment is likely to be reversed in the future, as the stimulus of the tax cut is absorbed, as the growth in the labor force increases and as American technology continues to make revolutionary advances.

The President's budget depends primarily on tax cuts for its expansionary effect. Most of the tax cut will take effect this year. On the other hand, a tight lid has been placed on expenditures which will have its greatest effect in 1965. Obviously, unless some additional stimulus is forthcoming at that time, further economic expansion may very well come to a halt and the rate of unemployment may once again begin to move upward.

This unhappy prospect is made even more likely by the anticipated step-up in the growth of the labor force. Between 1963 and 1970 the labor force is expected to expand by almost 1.4 million per year—about 50 percent faster than in the previous 10 years. This record growth will take off with a vengeance in 1965 when the bumper crop of postwar babies from 1947 on begins to pour into the labor market.

In addition, the forces which have historically pushed productivity to new heights at an accelerated rather than a constant rate are likely to continue to do so in the future. Official data going as far back as 1909 confirm this tendency. They indicate a strong underlying propensity for the rate of productivity advance to increase as time goes on. Referring to the more recent acceleration, Leon Greenberg, BLS Commissioner for Productivity and Technological Developments, told a congressional committee last year that it was difficult to find any long, sustained period in which productivity advanced as rapidly as in the post-World War II period.

Actually, the record for that period would have been even better had the demand for goods and services grown rapidly enough to elicit the Nation's full productivity potential by providing the basis for more efficient business operations. In any case, evidence indicates that the historical acceleration of productivity is continuing. Despite the persistence of a good deal of underutilization, output per man-hour in the private economy rose at an average rate of 3.5 percent between 1960 and 1963.

Obviously, unless working hours are reduced, the demand for goods and services must grow rapidly enough to create a need for the workers who would otherwise be made superfluous by the growth in productivity and to create additional jobs for new workers as well. Unfortunately, however, demand has failed to grow that rapidly in the past decade. In industry after industry throughout the Nation, vast numbers of jobs, particularly jobs for production workers, have disappeared. This has been true in agriculture; it has been true in manufacturing; and it has been true in coal mining and railroad transportation, as well.

Job opportunities have increased in other industries. However, the net increase has fallen far short of our needs. Between 1953 and 1963 the civilian labor force grew by 8.9 million. The net increase in total employment, however, amounted to only 6.6 million. But even that figure is misleading because less than half of it represents full-time employment.

Moreover, the increase in the number of people working full time was only 2½ million, between 1953 and 1963. Government employment, which is overwhelmingly fulltime, rose by 2.8 million and employment in private, nonprofit institutions, which is at least in significant part fulltime, rose by 1½ million. Thus, the record of the past decade indicates that there was a substantial net decline of full-time employment in private businesses that operate for a profit.

Not only have the new jobs generated during the last decade been primarily part-time jobs; the situation has been made even more serious by the fact that the new jobs, for the most part, have been the kind which displaced factory workers, farmers, miners, railroad workers, and untrained youth cannot easily qualify for or the kind which pay abysmally low wages.

To reverse this dangerous trend in the coming period, demand must grow considerably more rapidly than the 2.9-percent average rate of growth since 1953. It must grow more rapidly than the 3.8-percent rate in 1963, which was accompanied by an actual increase in unemployment. In fact, it must grow by 8 or 9 percent annually, within the next few years, to bring us to full employment, and only when we have reached this point might we be satisfied with the 5-percent rate of growth projected for 1964 by the Council of Economic Advisers.

THE CURRENT REVOLUTION IN TECHNOLOGY

While the Council clearly recognizes the need for a more rapid expansion in demand, its recognition of the extent of this need is blurred by its failure to recognize the real nature of current technological change. It is unfortunate that the Council's report not only fails to spell out the true dimensions of this change but, even more important, minimizes its real significance.

Chapter 3 of the Council's report speaks of the changing impact of technology "in recent centuries," and it makes a special point of the long intervals between the discovery and application of new forms of technology. In support of the latter point, it cites that fact that "in a previous generation, electric power did not displace the steam engine overnight nor did the steam engine in its time take over from the water wheel overnight."

As observer after observer has pointed out, however, both qualitatively and quantitatively, the changes taking place today are distinctly different from the changes which took place even so recently as the pre-World War II period. Today, machines are not only performing physical tasks previously performed by human operators: they are exercising powers of perception and logic and replacing human judgment, as well.

Moreover, the whole process of discovery has been transformed. We have, in effect, established a new kind of industry in America, an industry in which huge research and development resources, in increasing amounts, are systematically applied to the business of discovery, to the "organized forcing of technological change."

What is more, the time interval between discovery and practical application has been strikingly reduced to years instead of decades and the application of new discoveries has been far broader than in the past.

In recent hearings before the Senate Subcommittee on Employment and Manpower, Prof. Charles Killingsworth of Michigan State University called attention to the "broader applicability of automation," noting that "computer technology in particular seems likely to invade almost every area of industrial activity." In addition, Killingsworth told the committee:

"About a century was required for the general adoption of the steam engine in those activities where it could be employed; the comparable timespan for electric power was about 50 years. The first automatic accounting systems were installed in banks some 7 or 8 years ago. Today, about half of the banks are in the process of converting to this system. When the first large-scale computers were introduced early in the 1950's, there were estimates that only about 10 or 15 of them would ever be needed in the entire United States. Today, nearly 4,000 fully transistorized computers are in use, and the number on order is about double that, so that in 2 or 3 years we will have about three times as many in use as we have today."

In reference to the same point, Prof. Walter Buckingham of the Georgia Institute of Technology has said:

"Time has been telescoped by technology. The gap between theory and invention was 50 to 100 years in the Renaissance. Now, it is more nearly a decade and sometimes less. A century elapsed between Newton's principles and Watt's steam engine. But it took only 10 years to go from the A-bomb to the H-bomb."

The Council's failure to appreciate these revolutionary aspects of current technological change has led to the further error of regarding historical experience as proof that there "will be no permanent inadequacy of total job opportunities." The past, however, is no indication of the future when we are confronted with something so radically different. The speed and the broader applicability of the new technology alone make it more difficult for society to adjust to such changes than in a less rapidly changing era. Moreover, concentrated corporate power has resulted in increasing price rigidity. As a result, price reductions which stimulate total demand and cushion the impact of technological change upon jobs are not likely to occur as commonly as in the past. This is especially true because many of the areas in which productivity has been advancing rapidly and where, therefore, price reductions should be made, are also areas in which corporate power is heavily concentrated.

In the face of such differences, it would be folly for Americans to draw assurances from the past regarding the employment impact of current technological change. If, as a result of such assurance, the necessary adjustment to technology is left to market forces alone, the waste of human resources is certain to be enormous. In order for the new technology to be directed into constructive channels instead of along a path paved with hardship for countless individuals, the American people must recognize that we are confronted with something new and different, with something that does have revolutionary implications, with something that is profoundly changing the nature of our society. Given such recognition, we can go on to realize the great promise of the new technology while avoiding the kind of social havoc which accompanied the first industrial revolution.

AMERICA NEEDS MORE THAN A TAX CUT

While tax reduction is a necessary step toward bringing demand into line with the enormous productive capacity made possible by modern technology, it is only a beginning. In view of the magnitude of the task, a tax cut alone will not push the demand for goods and services up fast enough to produce full employment within any reasonable period of time. It will not eliminate poverty. Nor will it solve many of the other major economic problems now facing the Nation. America needs far more than a tax cut.

We need a program which not only stimulates demand but guides it into proper channels. This means that we need a program which expands the economy by putting far more purchasing power into the hands of lower income groups, particularly the poor and the deprived. It means that we need a program which makes it possible for the poor to permanently break out of the vicious circle in which they are now trapped. It means that we need a program which focuses upon the great areas of public need which have been so shabbily neglected up to now. And it also means that we need a program which seeks to transform the difficult occupational changes required by modern technology into a smooth and orderly and humane process.

What we are saying is that the road which leads to justice leads to economic progress, as well. America can and must strive for both at the same time. As Gunnar Myrdal points out in his book, "Challenge to Affluence," "Never in the history of America has there been a greater and more complete identity between the ideals of social justice and the requirements of economic progress." In fact, says Myrdal, "The latter goal is not attainable if large-scale policy measures are not inaugurated to reach the former goal."

This administration has recognized the existence of both problems and its proposals are likely to make some contribution to their solution. However, if its accomplishments are to be commensurate with the Nation's needs, there must be a greater recognition of the intimate relationship between the measures which, on the one hand, provide equity and meet basic social needs and the measures which, on the other hand, stimulate economic growth.

Last month, the Chairman of the Council of Economic Advisers informed the Joint Economic Committee that "the net fiscal stimulus that the tax reduction program and the President's fiscal 1965 budget jointly will supply to the economy in calendar 1964, will be the greatest provided during any calendar year in our peacetime history." However, he indicated, only a small part of the stimulus will come from the rise in Federal purchases of goods and services in 1964. The greater part is expected to stem from an increase in private demand as a result of the proposed tax cut. Thus, whether or not the budget is sufficiently expansionary to achieve even the level of GNP predicted by the Council for 1964 will depend largely on the response of private demand to the tax cut.

However, a sustained growth in private demand is not likely to occur from programs which focus so heavily on investment incentives. At this time in history, such programs can only add to the distortion in income flows which already plague the economy.

With so much of our productive capacity lying idle, with, as the President's report indicates, "operating rates in manufacturing still * * * only 87 percent of capacity, against the 92-percent rate preferred by business managers," there is a good possibility that a major part of the additional funds for investors will be saved instead of invested. In that case, they would provide less economic stimulus than expected. On the other hand, if most of the funds are invested, they may simply add to capacity and thereby aggravate the existing imbalance between our capacity to produce and our ability to consume. Or, what is more likely, to the extent that they are invested they will be invested disproportionately in job-displacing modernization projects, thus making our already serious unemployment problem even more serious.

Certainly, our experiences with the business-oriented tax cut of 1954 and the more recent tax and depreciation changes bear this out. In the former case, an investment boom was quickly followed by a recession. In the latter case, the response to substantial investment incentives has been less than startling.

Clearly, the emphasis must be on expanding the income of consumers rather than of business. Business income has already been nutured with loving care and has responded with a growth that has amazed observers. As the table below indicates, in each of the last 2 years corporate profits after taxes have risen almost twice as fast as GNP and they are likely to continue to rise at almost the same rate this year.

Percent changes in GNP and corporate profits after taxes

Year	GNP	Corporate profits after tax
1961-62	7.1	12.8
1962-63	5.4	10.6
1963-64 (estimated)	6.2	11.0

In view of the 1960-61 recession, the fact that corporate profits rose substantially in 1962, is, perhaps, not surprising. But the fact that profits continued to advance at a very rapid pace in 1963, and that they will do so once more in 1964, is indeed unusual. As the President's report indicated, "The rise is not only large, but prolonged. At this stage in past expansions, profits had already declined from their peaks."

No wonder the President called the rise in profits "notable," or that a New York Times article on January 6 carried the headline, "Company Profits Astound Experts," or that Fortune magazine referred to "profits beyond expectation," in its October 1963 issue.

Actually, corporate profits don't even tell the whole story. After-tax profits in each of the last 2 years would have been more than $1 billion higher than they were if it were not for the fact that the new depreciation guidelines made it possible to transfer some $2½ billion of revenue each year "out of taxable profits," as the Economic Report of the President so aptly puts it, "into nontaxable depreciation."

While corporate funds have been soaring, personal income, and particularly the income of those with a high propensity to spend, has moved up much more slowly. Corporate cash flow after dividends and taxes (consisting of undistributed profits and capital consumption allowances) rose 81.7 percent from 1953 to 1963. On the other hand, aftertax personal income rose only 59.4 percent during the same period. Moreover, as indicated on a before-tax basis in the table below, within the personal income category, dividends have far outstripped compensation to all employees (including wages, salaries, and supplements).

Dividends and compensation of employees, 1953–63

[Billions of dollars]

	Dividends	Employee compensation
1953	9.2	208.8
1963	17.8	340.4
Percent change	93.5	63.0

The rapid rise in corporate profits, the relatively slow increase in personal income and the consequent lag in consumption expenditures are all strikingly revealed by figures flowing from a recent study made by the National Industrial Conference Board. In this study, entitled "The Postwar Cycles" (technical paper No. 12), the NICB computed trend lines for the period from July 1953 to May 1960, for a number of economic series and then projected the trend values through 1963. It also computed the deviation of actual values from trend values in recent years. The actual values brought up to date by the AFL–CIO, the trend values, and the percent deviations from trend for three of the series are shown below for the final two quarters of 1963:

	Dollars in billions				Percent deviation from trend	
	Actual [1]		Trend value [1]			
	3d quarter	4th quarter	3d quarter	4th quarter	3d quarter	4th quarter
Corporate profits before taxes	52.2	[2] 55	51.2	51.6	+2.0	[3] +6.6
Personal income	465.2	473	474.8	481.0	−2.0	−1.7
Personal consumption expenditures	374.9	380	387.6	392.6	−3.3	−3.2

[1] Seasonally adjusted at annual rates.
[2] Estimate in President's Economic Report, p. 5.
[3] Computed by AFL–CIO on basis of above estimate and NICB trend value for 4th quarter. All other figures obtained from NICB's Technical Paper No. 12 and its monthly publication, Selected Business Indicators, which brings the data in the technical paper up to date.

As the table indicates, corporate profits were significantly above their trend value in both quarters. Personal income and personal consumption expenditures, on the other hand, were well below their projected trend values. What is more, when allowances are made for the $2½ billion of revenue transferred from profits before taxes to depreciation in 1963, the disparity becomes even greater.

This gap between the growth in personal income and the growth in corporate income plus increasing doubt as to the ability of consumers to assume additional installment debt and the continued existence of large amounts of idle capacity all point to the need for expanding consumer income and consumer expenditures rather than investment. As a matter of fact, such emphasis is doubly justified at this time. It is a prerequisite for balanced economic development and, in view of the vast consumption needs of the one-fifth of our people living in poverty, it is an integral part of our war against want.

THE WAR ON POVERTY

One may legitimately question whether the richest nation in the world should define poverty in terms of an income of $3,000 annually for a family of four when the cost of a "modest but adequate" standard of living in 1959 was more than $6,000, according to BLS. However, even if we use the $3,000 figure, there can be no question that we still have substantial poverty in America. Even by such a restricted definition, one-fifth of the Nation still exists on an "un-American" standard of living.

President Johnson has performed an important service by focusing attention upon this major piece of "unfinished business." That a society as rich as ours should harbor slums is indeed a blot on the American conscience. That it should have done so little in recent years to eliminate poverty is equally, if not more, appalling.

Who are the 9.3 million families and 5 million unrelated individuals living in poverty? The answers, as set forth in the report of the Council, point to the kinds of policies which America must adopt in order to get enough money into the hands of the poor to bring them back into the mainstream of American life. America's poor are drawn from the ranks of the unemployed, the partially unemployed, the underpaid, the victims of discrimination, the aged, the sick, the poorly educated, the families without male heads.

Certainly, the answer, or at least a good part of it, for many of these is a growing, full-employment economy. An economy using its resources fully can provide more job opportunities; it can provide better job opportunities; it is less likely to draw a hard and fast color line. And it is more likely to be willing to devote part of its resources to specific antipoverty programs. Full employment is the fundamental basis for reducing poverty.

However, not even an expanding economy would put sufficient purchasing power into the hands of many of the poor unless such specific antipoverty programs are instituted. In fact, unless special efforts are made to help the poor, it may be difficult, if not impossible, to achieve a vigorous and sustained kind of economic expansion.

The poor constitute an enormous potential source of demand which, if tapped, could fill much of the gap in consumption which has persistently plagued our economy. It would take $11 billion to bring them up to the $3,000 income level which the Council regards as the minimum for a decent life. If we raised their incomes to that level, we could be sure that every bit of it would be poured right back into the economy.

We need special antipoverty programs, therefore, both to deal effectively with the problem of poverty itself and to lift the economy to the level which it is capable of achieving. Many of these special programs are already on the books and need merely to be expanded and improved. Today, for example, a variety of transfer payments help sustain the economy and the living standards of millions of people. However, those who need them most are too often the ones who benefit the least. "Only about one-half of the present poor receive any transfer payments at all," the Council reports. Twenty-three percent of all wage and salary earners are not covered by our unemployment compensation system. And 10 percent of those currently employed, and millions more who have already reached retirement age, are not covered by OASDI.

Changes in such programs are long overdue. Unemployment insurance protection should be extended to virtually all who are not presently covered and Federal standards established for minimum amounts and duration of benefits. OASDI should be improved; old-age benefit payments must not be allowed to stagnate while the Nation's wealth and general standard of living advance, and, particularly at this time, a medical care program for the aged must be made an integral part of our social security system. Also, the benefits under public assistance programs and aid to families with dependent children should be raised above the survival level and unnecessarily rigid eligibility restrictions should be changed so that people in need are not deprived of the help which they are entitled to as human beings.

Meaningful improvements in a wide variety of other existing measures must also be made if we are really serious not only about waging a war on poverty but about preventing poverty from making further inroads. We must extend full protection of the Fair Labor Standards Act to all workers employed in industries affecting interstate commerce. We must increase the minimum wage from $1.25 to $2, an amount which would lift families dependent upon such wages only slightly above the poverty level as defined by the Council and still leave them considerably below the rate required for a minimum standard of health and decency. Both the accelerated public works and area redevelopment programs should be extended and enlarged. And, a truly national public employment service with expanded testing and counseling facilities and far greater coverage of job vacancies should be established.

The resolution on "Manpower policy and retraining," adopted at the last convention of the AFL–CIO, strongly supported "any action which will bring more employers to list their job vacancies with the public employment service." It specifically urged the President to "issue an Executive order requiring all Government contractors to list all of their job vacancies with the U.S. Employment Service, provided, however, where union hiring halls and other union-management arrangements are in operation this shall be acceptable in lieu of listing with the public employment service."

In addition to the improvement of existing measures, an all-out war to eliminate existing poverty and prevent potential poverty requires a variety of new programs. We need to pass a civil rights bill which puts an end to the discrimination which deprives Negroes of an equal opportunity to develop their abilities and to obtain better paying jobs. We need a youth employment program which provides opportunities for constructive conservation and community service work. And we need a whole battery of projects to give the children of lower income families a genuinely equal education opportunity and to improve the basic literacy of adults who have never learned to read or write adequately.

Clearly, the war upon poverty must be waged on a variety of fronts and it must be financed by much more massive outlays than are currently being contemplated. An effective program costs money—lots of money. On the other hand, our failure to launch such a program can be, and probably has been, even more expensive. "Poverty," as the Council reminds us, "is costly not only to the poor but to the whole society. Its ugly byproducts include ignorance, disease, delinquency, crime, irresponsibility, immorality, indifference." They also include, the Council might have added, the growing bitterness of our Negro population, almost half of which lives in poverty. Certainly, it should be clear to everyone by this time that poverty in its most abject form is responsible, in great part, for what AFL–CIO Vice President A. Philip Randolph has described as "the militance and impatience of the current civil rights revolution" and "the apparently irrational and excessive behavior accompanying the revolution."

The fact is that the war against poverty will pay for itself not only by eliminating such ugly byproducts but also by helping to stabilize our economy and bringing it closer to our goal of full employment.

THE NEED FOR A POSITIVE WAGE POLICY

America not only needs a poverty program to expand demand in a way which will promote both equity and economic health. It needs a positive wage policy as well.

Seldom has there been such a broad justification for substantial improvements in wages and fringe benefits. Output per man-hour is continuing to increase rapidly and promises to increase even more rapidly as the economy expands. Profits have soared to a point at which corporations are having difficulty finding suitable investment outlets. Yet, at the same time real weekly earnings of factory production workers are moving ahead far more slowly than in previous years and 4½ million American families still receive less than $3,000 a year even though the heads of such families are employed. Moreover, while growth in consumer expenditures has slowed down as a result, in large part, of the lag in wages, no other source of demand—neither business nor Government—has come forth to take up the slack in the economy and to put idle men and idle machines back to work.

The labor movement will continue to insist that the Government has a responsibility under such circumstances to use its fiscal and monetary powers to restore full employment. Through substantial tax cuts for lower income groups, through increased expenditures on public works, through special programs to help the poor break out of the vicious circle in which they have been trapped, and through many other kinds of action, the Government could do much to eliminate the deficit in demand and provide the jobs which the economy needs for full employment.

However, the entire burden of achieving a more equitable distribution of income, maintaining a high level of demand and sustaining full employment cannot be placed on the shoulders of Government alone. These are functions which must be shared by private decision-makers.

Unfortunately, we are in trouble today, in great part, because the decisions made in the private sector have not contributed to a balanced economic development. The fact is, in spite of implications to the contrary in the Council of Economic Advisers' Report, that wages have lost out in the race with productivity. This is clearly apparent when we compare changes in productivity, which reflect real changes in output, with the real hourly earnings of workers over a period of years.

Between 1956 and 1963, output per man-hour in the total private economy increased 24.4 percent. Real average hourly compensation of all employees in the total private economy (including wages, salaries, and fringe benefits), on the other hand, rose only 17.1 percent.

For certain kinds of workers in particular sectors of the economy the lag was even more marked. Real average hourly earnings (excluding fringe benefits) of production and maintenance workers in manufacturing increased only 12.1 percent; of nonsupervisory employees in retail trade and wholesale trade, 14.2 percent and 12.7 percent, respectively; of nonsupervisory employees in coal mining, 3.1 percent; and of agricultural wage earners, 10.8 percent. And even if we included the fringe benefits received by such workers, there would still be a great gap between their increase in real compensation and the 24.4-percent increase in output per man-hour since 1956.

Unit employment costs in manufacturing

[1953=100]

	Total unit employment costs	Unit wage costs	Unit salary costs
1953	100.0	100.0	100.0
1954	102.0	97.8	111.1
1955	99.2	95.4	106.6
1956	103.9	98.0	115.8
1957	107.9	99.5	123.3
1958	111.2	99.9	133.6
1959	108.5	96.5	131.4
1960	109.5	95.5	135.7
1961	109.0	93.4	138.4
1962	108.8	94.0	134.8
1963	108.3	93.4	133.9

Source· U.S. Department of Commerce and Federal Reserve System.

The slowdown in wage increases has also been reflected in a decline in unit employment costs. In 1963, total employment costs (including wages, salaries, and fringe benefits) per unit of output in manufacturing were 2.6 percent lower than they were in 1958. This was attributable primarily to a drop of 6.6 percent in unit wage costs during the period. Even salary costs per unit, however, have declined recently, after rising for a good part of the postwar era.

Along with the price increases which the Council of Economic Advisers has found so "disquieting," the decline in unit employment costs has made it possible for profits to reach a new peak even though sales and production have remained substantially below capacity. But record profits based on lagging wages or rising prices or both are not the kind of profits which produce and sustain full employment.

If a portion of the fantastic profits racked up by major firms in the United States last year had gone into wages instead, the Nation's economy would not have been operating at 87 percent of capacity at the end of the year.

Consider, for example, the case of General Motors, which in addition to its regular quarterly distributions to stockholders paid two extra dividends in 1963. These extra payments were equal to 73 cents per hour for every hour worked by every General Motors hourly rated worker in the United States. Had just this portion of General Motors' staggering profits for the year been shared with workers and consumers, as it should have been, much more of it would have been poured back into the income stream instead of being saved and we would have had a more equitable, a sounder, and a more stable economy as a result.

Such an economy is possible only if responsibility is exercised in private as well as public decisionmaking. And, at this point in time, responsible decisionmaking calls for substantial wage increases to boost sales and avoid another recession. It calls for recognition of the fact that wages are not just another cost but a vital source of the greater purchasing power which the Nation badly needs and that, as such, they cannot and should not be bound at all times by a rigid productivity formula.

Although the guideposts for wage and price decisions first set forth by the Council of Economic Advisers in 1962 and reiterated in the Council's two more recent reports may have contributed, as a result of misinterpretation, to a negative emphasis on wages as costs, there is actually no conflict between the guideposts and the kind of dynamic wage policy which the AFL–CIO has been urging. In its original statement, the Council provided for specific exceptions to the general rule that increases in employee compensation should match increases in national productivity trends. For example, it acknowledged that workers receiving substandard wages were justified in seeking larger increases than national productivity trends alone would warrant.

But, the Council's recognition of the need for flexibility went beyond the point of specific exceptions. It recognized that unbending adherence to the general rule would permanently freeze the shares of a firm's income going into wages and profits. It therefore went on to make clear that it was not proposing that income shares remain fixed. There is nothing sacred about the existing distribution of income which requires that it be frozen for all time, the Council observed. "The proportions in which labor and nonlabor incomes share the product of industry have not been immutable throughout American history nor can they be expected to stand forever where they are today," it said.

Furthermore, it declared that "It is desirable that labor and management should bargain explicitly about the distribution of the income of particular firms and industries," and that such bargaining can and should take place "within the bounds of noninflationary price behavior."

The abuse of corporate pricing power

In its latest report, the Council once again emphasized the features of the guideposts which recognize the need for flexibility in wage decisions and allow ample room for collective bargaining. At the same time, however, it expressed its concern with the possibility that bargaining decisions could lead to inflationary price behavior.

Certainly, the possibility exists. It exists, however, not because labor's demands have been excessive or because a positive wage policy makes price increases inevitable. It exists primarily because of the misuse of administered pricing power by the large corporations which hold that power.

In recent months a number of corporations have once again begun to raise prices sufficiently to give the President of the United States and the Council of Economic Advisers "cause for concern." In addition, the Council has indicated its concern with the failure of corporations to reduce prices when reductions were in order. According to its latest report—

"* * * The guideposts call for reductions in those industries whose trend productivity gains exceed the national trend. It is fair to say that large industrial enterprises thus far have not widely heeded this advice. And yet, as noted earlier, there will be ample room for such price reductions in 1964. If they are not forthcoming, overall price stability will be rendered more difficult, since price increases are likely in industries that are progressing at a less-than-average rate. Moreover, in industries whose trend of productivity rises faster than the national average, if wages conform more nearly to national than to industry productivity trends (as the guideposts would have them do), failure to follow the general price guide will cause profits to pile up."

The Council warns that "such profits constitute a lure for strongly intensified wage demands." Yet, it recognizes that "there is no justification, on either economic or equity grounds, for distributing above-average gains in productivity exclusively through the profits channel." That being the case, through what methods other than substantial increases in wage and fringe benefits can such gains be properly distributed when prices are not reduced? Obviously, the only economically sound alternatives under such circumstances is to increase workers' benefits.

This does not mean that labor favors the kind of corporate pricing action which the Council and the President have both deplored. In fact, for years we have been insisting that special measures are necessary to curb administered price inflation and to assure that wage and fringe benefit gains will increase demand rather than be used as an excuse for inflationary price increases. My own union, the UAW, has urged the appointment of an administered price board which would be empowered to hold public hearings when a limited number of major corporations possessing administered pricing powers and producing key products proposed to raise prices. Unions would also be subject to the hearing procedures if their demands were alleged to be the basis of a proposed price increase. After such hearings, the board would issue a report and the corporation would then be free to raise prices and the union to press its demands. But their decision to do so would have to be made with the knowledge that the public had facts with which to judge their action.

Recently, the AFL–CIO approved the same general approach in a resolution which stated:

"To curb the potential danger from the pricing policies of the dominant corporations in major administered-price industries the spotlight of public attention is needed. Only the Federal Government—Federal agencies, congressional committees, or both—can adequately focus public attention on the facts of the cost-price-profit-investment policies of these corporations, in an attempt to curtail administered price abuses."

Thus, the labor movement in general supports the determination of the present administration, expressed both in the President's Economic Report and the Report of the Council of Economic Advisers, to focus public attention upon the real causes of inflationary price developments. We support the administration in this matter because we, too, are opposed to inflation. We support it because we know that inflation is detrimental to the economy as a whole and because we feel that the threat of inflation flowing from the misuse of corporate pricing power should not be used as an excuse for imposing a negative wage policy upon American workers.

THE WAR ON PUBLIC POVERTY

A massive increase in expenditures on public facilities is an essential weapon in our effort to stimulate economic growth by meeting our most urgent needs. Among the most urgent needs in American life today, as a matter of fact, are those which can only be met by an increase in public investment. America cannot continue to grow and its population cannot continue to pour into urban centers without a vast increase in expenditures on the essentials of civilized living.

No one can seriously question the need to provide more and better schools and hospitals, to raise public housing construction above the pitifully inadequate level of less than 31,000 nonfarm starts in 1963, to rescue our urban areas from strangulation and decay, or to restore a decent standard of living and human dignity to the areas of poverty which pockmark our Nation. These are urgent needs; they call for immediate action. Furthermore, they are longrun needs, and it is highly unrealistic for us to postpone meaningful efforts to meet them today in the expectation that we can meet them with crash programs tomorrow.

Unfortunately, some people seem to forget that we have had a population explosion in this country. Back in 1946, the experts predicted that the number of Americans would reach 165 million in 1990. The fact is that we have already passed the 190 million mark. We reached the 165 million figure some 35 years ahead of schedule in June of 1955.

This outburst is swamping the existing resources of local government. It is presenting problems with which such governments are incapable of coping.

In fact, our public needs have multiplied even more rapidly than our population growth because that growth has been concentrated in urban areas. Even if our population had not grown at all, the shift to urban areas which has occurred would have created a greater need for public goods and services. Paved streets, public sewers, and public water supplies may not be an absolute necessity for farm living, but such things are indispensable for urban living.

A substantial increase in expenditures on public works would not only satisfy these unmet needs of our population in general. It would make an enormous contribution, in addition, to the war on poverty by creating the housing, the schools, the child-care centers, and the other facilities which the poor so badly need. Furthermore, the kind of demand created by increased expenditures on public works can have a powerful impact on unemployment. Few expenditures of equal size require more labor on and off the site than the construction of public works and few provide as many opportunities for unskilled workers. In addition, public works programs can be directed into the areas of greatest economic distress. And, beyond these advantages, such expenditures will have a further impact on employment as the increased income they generate is spent on the products of other industries.

Certainly, the accelerated public works program enacted in 1962 has proven its value in terms of both the public facilities and the jobs which it has created. That is why the AFL–CIO has urged that Congress extend its life and provide it with an appropriation of $2 billion. America can afford to spend such sums for emergency programs such as this, as well as additional sums for longer range programs. We have been allowing resources capable of producing some $75 billion annually to remain idle. What better use could we find for such idle resources than to meet our vast backlog of public needs.

We must not permit the fear of unbalanced budgets and deficit financing to deter us from making an all-out attack on public as well as private poverty. Budgets are instruments of national policy and not ends in themselves. As the OECD points out in its recent survey of the American economy: "The true test of the success of fiscal policy is not whether the budget is in surplus or deficit, but whether the economy as a whole is in balance."

There is no lack of empirical data to support this thesis. This is true even in terms that mean the most to those obsessed with balanced budgets. For example, between 1947 and 1957, when unemployment averaged 4.2 percent, the Federal Government had a cumulative cash surplus of over $20 billion despite sizable tax cuts in both 1948 and 1954. On the other hand, between 1958 and 1963, when average unemployment rose to 5.9 percent, we ran a cumulative deficit of $26 billion.

The blind passion for budget balancing not only lacks empirical support; it has few supporters among economic theorists. On October 24, 1963, Prof. Lester Chandler of Princeton University presented a statement to the Senate Finance Committee signed by 313 of the leading economists in the country. That statement contained the following observations:

"We should like to assure the American people that a Federal deficit of the magnitude proposed, given the extent to which capital and labor are not now being fully utilized, carries no danger of accelerated inflation. Nor does such a deficit in any manner or degree threaten the solvency of the Federal Government. This country's outstanding record of economic growth during the last century and a half or more has been associated with increases in debt representing mobilization of the people's savings by business and Government. It should be noted, also, that the size of the deficit will automatically decline as rising incomes generate increased tax revenues at the lower rates.

"We should also like to affirm—and we do so with complete confidence—that there is nothing to fear from the present size of the Federal debt. Nor is there anything to fear from the moderate increase in the debt that will result from the deficits envisaged in the next few years. Indeed, measured as a fraction of the gross national product, the Federal debt today is much smaller relatively than it was 15 years ago. And interest payments on the debt absorb a significantly smaller fraction of the national income than they did at the end of World War II."

OTHER MEASURES FOR AN EXPANDING ECONOMY

An all-out war on poverty, substantial improvements in wages and fringe benefits and increased expenditures on public works are all urgently needed both in their own right and to help restore full employment. However, as vital as they are, America's problems are much too complex to be solved by such measures alone. Other kinds of action are also badly needed to transform the Nation's enormous potential into reality.

Reduction in hours

During the Great Depression, hours of work were reduced primarily to spread available work opportunities among those seeking employment. We are once again faced with an unemployment problem which is persistent and serious enough in terms of the needs and standards of the 1960's to warrant further reduction in working hours. Although labor has again and again expressed its preference for the achievement of full employment at 40 hours, it finds itself compelled, when faced with the alternative of a reduction in hours or high unemployment, to choose the former. At its convention in November of last year, the AFL–CIO, therefore, adopted a resolution reaffirming its goal of "amending the Fair Labor Standards Act to provide for a standard 35-hour workweek without reduction in take-home pay" and calling upon Congress to conduct an examination in depth of methods for achieving such a reduction in hours through Federal legislation. "The primary goal is stable, full employment," the resolution said. "With that goal in view," it went on, "Congress should also explore automatic and flexible adjustment of the basic statutory workweek without loss of pay to maintain full employment in the face of continuing technological change and fluctuations in demand."

Double time for overtime

As a further step toward full employment, the AFL–CIO has urged that the Fair Labor Standards Act be amended to provide double time pay for overtime work in order to discourage employers from scheduling overtime and to encourage the hiring of new workers.

There is clearly no moral justification for the wholesale resort to overtime when millions of workers are unemployed. Yet, last year, with unemployment averaging 5.7 percent of the civilian labor force, 7 percent of all the hours worked in manufacturing were overtime hours. Assuming that as much as 25 percent of this was unavoidable, we find that the remaining overtime could have provided an additional 675,000 factory jobs. On the basis of similar assumptions, 60,000 jobs would have been created in the automobile industry alone.

President Johnson recognized the problem of excessive overtime in his state of the Union message and proposed that it be dealt with on an industry-by-industry basis. His acknowledgment of the problem is a significant step forward. However, we firmly believe that the matter can be dealt with more quickly and more efficiently by an amendment to the Fair Labor Standards Act providing for double time pay for all overtime work.

Programs to cushion the impact of automation

The current revolution in technology has had an especially devastating impact upon people because it has occurred during a period of slow economic growth. However, even if the measures suggested thus far succeed in increasing our rate of growth and expanding job opportunities, additional measures would still be necessary to help people adjust to technological changes without suffering and hardship.

In addition to the improvements in unemployment compensation, in the U.S. Employment Service, in general education, and in the community development programs which we have already mentioned, the Nation must expand its training programs, extend and improve current relocation allowance provisions and establish a variety of special programs to deal with the problem of automation. Among the latter are an Automation Commission to study the overall social and economic problems created by technological change, to make recommendations for their solution and to coordinate the efforts of the various government agencies assigned to deal with parts of the problem; a technological clearinghouse to gather information about impending technological changes and their impact on jobs, on location of industry, on training needs, and so on; and a Federal Information and Guidance Service to assist unions and employers, upon request, in developing collective bargaining solutions to the problems created by technological change.

An expansionary monetary policy

The Federal Reserve Board must adopt policies which show less concern for such potential difficulties as inflation and more concern for the very real problems of the present such as unemployment. The expansionary effect of the tax cut must not be stunted by tight-money policies which push interest rates up and curtail demand at a time when the Nation still suffers an enormous deficiency of demand. A restrictive monetary policy would restrain homebuilding, durable goods purchases, and State and local government investment, all sources of major strength in the current expansion.

In our opinion, the premature monetary restrictions which have already been imposed and the threat of future action along the same lines underscore the need for broadening the membership of the Board of Governors and the other agencies which determine monetary policy. These agencies must be made much more representative and much less of an instrument of the bankers who now dominate them. Such a change is necessary in order to reduce the possibility of our being saddled with monetary and fiscal policies which work at cross-purposes.

Foreign aid

The labor movement regards aid to developing countries as an integral part of the effort to stimulate and sustain American economic health as well as a moral obligation which all of the wealthier nations of the world must rightfully assume. Without such aid, world peace and stability would be in even more danger than it currently is and the United States would have to divert an even greater proportion of its resources to the production of weapons of destruction. With such aid, we can assist in the development of viable economies which can eventually afford to purchase more of our goods and engage in mutually advantageous trade in a peaceful world. With such aid, we can put at least part of our unused resources to work, thereby creating jobs as well as goods which can help raise the poverty-stricken people of other lands to a respectable level of human dignity.

Labor is therefore opposed to cutbacks in such a vitally necessary program. We believe that the United States can well afford to spend the necessary sums, especially if we adopt the other measures which our expanding economy requires. Like the war against our own private and public poverty, our assistance to the developing countries is both a reason why we need a more rapid expansion in production and employment and an important means for achieving and sustaining such expansion.

Democratic planning

Even if all of the measures suggested thus far were adopted tomorrow, another measure would still be necessary to make certain that we achieve our goals as quickly as possible, without confusion, without waste, and without either overshooting or undershooting the mark. In most of the major countries of the free world whose economies have been performing more efficiently than our own, planning agencies have been established to guide government policy and to assist the private part of the economy in realizing its full potential. Such planning becomes increasingly necessary as society grows more complex, and there is nothing undemocratic about it. It involves no loss of individual freedom, no danger to free institutions, and no danger to private enterprise. As a matter of fact, in Western Europe, businessmen are among the most enthusiastic supporters of economic planning because they know that, without impinging upon their basic freedom, it has been responsible in great part for the amazing economic recovery of their countries; that it has been extremely helpful to them in their own business planning; and that it offers a viable alternative to totalitarian planning.

We have special problems which the Europeans and the Japanese do not have to contend with, but basically the principle of democratic planning would make as much sense for us as for other nations and because this is so the labor movement has urged that we, too, create a National Planning Agency.

At its recent convention in New York, the AFL-CIO adopted a resolution on the national economy which contained the following provision:

"Experience has shown that we cannot rely upon the blind forces of the marketplace for full employment, full production, and effective use of our resources to meet our most urgent national needs. Other advanced free and democratic industrial nations have found that they can achieve their economic and social objectives only through a rational national economic planning process involving the democratic participation of all segments of their populations together with government. We urge the creation in the United States of a National Planning Agency, which through similar democratic mechanisms will evaluate our resources and our needs and establish priorities in the application of resources to the meeting of needs."

Words like "planning" and "deficit financing" and "Government spending" unfortunately have acquired a power to evoke emotions and misconceptions which obstruct rational thought and action. I am convinced that if we can ever overcome our fears regarding such matters, America can reach undreamed of heights.

We have the physical and intellectual resources to conduct a successful crusade against poverty in both the private and the public sectors, to reach full employment and to sustain it, and to go on from there to lift life in America onto a new and higher cultural plane. However, only if we conquer the myths and the narrow self-interest which now shackle us can we hope to mobilize our resources fully enough to create the kind of economy which can provide the foundation, the framework, the launching platform for a solution to many of the most pressing problems of the 20th century.

CHAMBER OF COMMERCE OF THE UNITED STATES

By Carl H. Madden, Director of Economic Research

This opportunity to submit a written commentary on the President's Economic Report is highly valued. In any year the Economic Report is important—not only for technical analysis and data, but for political, social—even philosophical—views that color the entire conduct of an administration. But this year, as Robert Nathan pointed out before you on January 29, "a thorough and objective airing" of the report is particularly important, because it is the first policy message of the new administration.

The Economic Report cuts a wide swath. It discusses Government policies relating to production, employment, income, money and credit, taxation, public expenditures, fiscal matters, balance of payments and foreign spending. Policies in many specific fields, such as agriculture, technology, and a host of others, are indirectly affected. Thus, the committee's annual review of the Economic Report is one of the Nation's most significant political exercises in freedom of speech and discussion. This review is particularly vital to the President, the Congress and the public this year.

For this reason, it is especially regrettable that time has not permitted hearing more witnesses before the committee. The dialectic of actual discussion is a key part of the process of informing the public on these large questions of state. As the only non-Government witnesses, Messr. Nathan and Fackler have carried a heavy burden. The arithmetic of counting witnesses, indeed, leaves the non-Government sectors outnumbered by Government spokesmen.

The Economic Report—including the Annual Report of the Council of Economic Advisers—probably tends through the years to range over everwider fields of administration policy. This year's version, with chapters on poverty and technological change, is no exception. Perhaps this is to be expected. The document does not escape being political as well as economic in nature. As this committee well knows, the argument that one part is hotly political—the President's report, and the other coldly professional—the Annual Report of the Council, misconstrues the process of policymaking. As Arthur F. Burns, former Chairman of the Council of Economic Advisers, has pointed out:

"Although the Council consists of economic experts, it is also a political body. The Council cannot discharge its primary responsibility of assisting the President and at the same time express views that diverge significantly from the President's public position."

Certainly, we can all second the testimony of non-Government witness Walter D. Fackler before the committee on January 29 on this point when he referred to Dr. Burns' remarks.

The Economic Report is necessarily an intellectual exercise in interpreting and justifying administration economic policy. This seems to be a good thing. Not only does it elevate the level of public discourse on policy questions toward that of the scientist. It also sets in motion thought about social and economic issues. At least it provides conditions for such a process to be set in motion. As time moves us into the era of the scientific revolution, this thought process will become more and more valuable to the Nation. As Albert Schweitzer has pointed out in another context, it is remarkable that in such an age of discovery, there is so great a tendency to abandon thought. The Economic Report of the President and these annual hearings by the Joint Economic Committee form one of the foundation stones for assuring that the diverse interests of the public in the United States—and of the Government—should in the midst of their differences meet some of the tests of scholarly and scientific thinking in establishing the climate for those "tolerable compromises" that lie in the dynamic center of our political life and that are the strength of our free constitutional system.

This year's report reflects a broad interpretation of the Employment Act of 1946, which states:

"The Congress declares that it is the continuing policy and responsibility of the Federal Government to use all practicable means consistent with its needs and obligations and other essential considerations of national policy, with the assistance and cooperation of industry, agriculture, labor, and State and local governments, to coordinate and utilize all its plans, functions, and resources for the purpose of creating and maintaining, in a manner calculated to foster and promote free competitive enterprise and the general welfare, conditions under which there will be afforded useful employment opportunities, including self-employment, for those able, willing, and seeking to work, and to promote maximum employment, production, and purchasing power."

The Federal Government is to promote employment in ways that are consistent with primary governmental responsibilities and that foster free, competitive enterprise. Also, it is generally agreed that the Employment Act implies the goal of price stability (in the sense of a stable general price level) and of economic growth.

Strictly interpreting this mandate, the report might properly deal with the performance of the economy and the economic outlook, Government employment policy, monetary and fiscal policy, and other Government economic policies—such as balance-of-payments policy—as they relate to employment. The report might also properly deal explicitly with Government policies under the act that foster free, competitive enterprise. Since, however, the report ranges further afield to longer term problems of relative poverty and the economic impact of technological change, it is important for the committee to receive some evaluation of the economic theory and public policy implications of these discussions.

The Economic Report shows the swift and firm grasping of reins by the new administration, but it also reflects its many problems. A range of social, economic, fiscal, and international problems remain unsolved: "Welfare," agriculture, stubborn unemployment, war veterans, continued international payments imbalances and defensive maneuvers to preserve the dollar, the Alliance for Progress, foreign aid, the Cuba situation and Panama, a fractured NATO and an uncooperative De Gaulle, the splintering of the grand design and its effect on the Trade Expansion Act of 1962, the recognition by DeGaulle of Red China and the situation in South Vietnam.

The Economic Report reflects a strenuous effort to focus attention upon new initiatives. These include "war" on poverty and the sharp stimulation to be given to economic activity by Federal policy—after a surprisingly good year in 1963 even without a tax cut. However, the problems remain, and it is one of the strengths of a free society that it can survive such problems and move toward solving those within its range of action by flexibly adapting its institutions to changing conditions. It is heartening to see that the new administration says it will place its "main reliance * * * on private ingenuity, initiative, and industry."

OUTLOOK FOR 1964

Prospects for 1964 seem good. Presently, the standard forecast holds that, assuming the tax cut is passed promptly, during calendar 1964 the gross national product will increase 5 or 6 percent, to fall within a range of $10 billion centering on $615 billion. The Council's forecast lies within this range, though slightly higher than the standard. Presently, the economy is buoyant, with most of the leading statistical indicators either stable or pointing upward. Monetary policy over the past year has been expansive.

The current trend of economic growth is likely by April to set an important record. In that month the expansion will become the longest in peacetime history. The average length of peacetime business expansions from 1854 to 1961 was only 26 months. Excluding the rise following the great depression of 1933, the longest was 37 months. The current expansion has lasted 36 months. Some argue, as it appears the Council does, that the explanation for this unprecedented length lies in the absence of basic imbalances capable of producing business weakness. Such evidence as low inventory-sales ratios and low capital spending-gross national product ratios is cited to suggest "room" for further expansion of business in inventory buying and growing investment.

Others challenge this view. They point out that inventory-sales ratios have often been low just prior to recessions. They also ask why production—and investment—continue to move up in the face of excess capacity. This school of thought holds that "the basic factor motivating private spending is change in the supply of money." An increase in the money supply leads to an increase in liquid holdings, which are spent according to the regular pattern of consumption habits and induced investment. Given available supplies of capital and labor resources, increased spending leads to increased production; without them, inflation results.

Economists who argue that monetary expansion explains the length of the present cycle cite evidence that monetary expansion has lasted longer during this cycle and that the rate of expansion has been greater than in the previous two cycles.[1] Using the criterion of changes in the money supply to define the posture of monetary policy, they dispute the contention that monetary policy tightened from midyear 1963. The viewpoint of this school rests upon a weighty volume of empirical evidence. The studies by Clark Warburton, and more recently by Milton Friedman and his associates, strongly support the view that a steady growth in the money supply is the indispensable

[1] See Beryl W. Sprinkel's "Business and Money" 1964, Harris Trust & Savings Bank p. 16.

prerequisite for a sustained economic expansion.[2] The time seems to be growing nearer when the views of this school will require explicit attention in such documents as the Economic Report. As yet, the language of monetary policy in the report (e.g., p. 47) gives little indication of such an orientation of policy thinking.

The money supply—demand deposits adjusted plus currency—has been rising at an annual rate of 3.9 percent since mid-January of last year, and since July the rise has been at an annual rate of 5.2 percent. For 1963 as a whole, the stock of money rose by over 4 percent. During 1963, the Federal Reserve System added to bank reserves or offset other factors tending to reduce them by purchases in the open market of securities amounting to approximately $3.3 billion.

Thus, if monetary growth continues and the tax cut is speedily effected as planned, signs point to an excellent business year in 1964. Consumers in November showed rising buying plans and and optimism about the economic outlook. Since then, car sales have borne out such optimism. Expenditures for plant and equipment are expected to rise by more than the 4.7 percent rate of last year, and some analysts see them increasing as much as 11 percent. Construction, running at record levels during 1963, should continue to improve this year. The heavy volume of apartment building, underlined by population trends, seems likely to continue. Although mortgage funds may become slightly more costly during the year, the change is not expected to contract housing starts sharply. The low level of inventory-sales ratios, the strong business trend, and the strength of business orders indicate that inventory accumulation this year will be stronger than usual. While the rate of rise of Federal spending is tapering off, a sharp rise in State and local government spending adds a significant net amount to the expected gross national product.

MONETARY AND FISCAL POLICIES

The policy prescription of the Economic Report is for a tax cut, a budget deficit, and an expansionist or cooperative monetary policy the net stimulus of which to the economy is greater "than in any other peacetime year in history." This is coupled with the promise of Federal fiscal restraint in fiscal 1965. As for monetary policy, the President declares, "It would be self-defeating to cancel the stimulus of tax reduction by tightening money." Such steps are justified in the Economic Report by the considerable slack in the economy, with unemployment at 5.5 percent and some idle capacity in industrial plants.

Considering the policy package as a whole, the Economic Report does not make a clear case for the many benefits claimed to result from its application. The report seems to estimate an initial impact, to be fully effective by 1965, of $11 billion. Beyond this, the report relies upon multiplier analysis to foresee another $35 to $45 billion of GNP each year thereafter added over what GNP would be without the tax cut. And finally, the report claims for the tax cut a "removal of shackles" from the economy that will lead to a new era of growth. Such claims, after more than a year of assertion, reassertion, revision,

[2] Milton Friedman, "Capitalism and Freedom," University of Chicago Press, Chicago, Ill., 1962, ch. III. See also, "Can We Depression Proof Our Economy?". Chamber of Commerce of the United States, Washington, D.C.

and restatement should have further thoughtful and objective consideration. This is especially the case when the possible upward response of State and local taxes to a Federal tax reduction cannot be weighed and is seldom mentioned. Many competent economists are skeptical of multiplier analysis applied literally and arithmetically to formulate broad measures of public policy. Empirical studies by Friedman and Meiselman find a wide variation in historically constructed multiplier values.[3] The tax cut, highly desirable as it is, should not be rested to such an extent on demand-deficiency grounds.

Likewise, the tax cut is not primarily to be justified by the so-called fiscal stagnation hypothesis of the Economic Report. This holds that (p. 42) there is a tendency for the "full-employment surplus to build up to expansion-retarding levels as the economy grows." That is, the argument goes, the present tax structure "hobbles" growth by generating too much tax revenue as the economy grows. The income withdrawn by the tax system from the income stream during an upswing of the economy, it is asserted, damps down the growth before adequate levels of employment and production are reached.

However, in its own analysis of the 1958–60 cycle, the Council acknowledges the major importance of a restrictive monetary and fiscal policy in contributing to the downturn. Mr. Fackler rightly points out in his testimony of January 29 before this committee that if the Council is wholly correct in its appraisal of the impact on income of the full-employment surplus, the economy in 1963 should not have risen without a tax cut to a level ($585 billion) higher than the Council predicted it would rise ($578 billion) with one.

Too much is also claimed of the tax reduction bill, according to a sizable body of professional opinion, as a growth measure. In his written statement submitted to this committee on February 15, 1963, Emerson P. Schmidt analyzed the lack of balance in the present tax bill, its bias toward favoring consumption, and its resulting small stimulus to investment. His position is supported by the testimony this year of Walter Fackler on January 29, appraising professional views on this point. One school of thought, as mentioned earlier, holds that the sluggishness of the economy from 1957 to 1961 was more likely connected with monetary measures of restraint taken in at least partial response to a balance-of-payments problem discovered to be more serious and less tractable than anticipated.

The strong reasons for a tax cut are indeed, however, related to the fiscal drag on individual incomes of wartime tax rates and the resulting reduction of private saving. They are also, and perhaps even more importantly, related to the many harmful economic effects of the corporation income tax, including its inhibition of investment. In his written statement before the committee last year, Emerson P. Schmidt summarized the indictment of the corporate income tax now accepted by many objective scholars:

"The corporation income tax has virtually no defenders except those who view it through the eyes of the revenue collectors and those who see it as something of a recession snubber. Its incidence is capricious and uncertain. It raises the general price level. It is largely a disguised sales tax. It has put the corporate form of doing

[3] Friedman and Meiselman, "The Relative Stability of Monetary Velocity and the Investment Multiplier in the United States, 1897–1958," "Stabilization Policies," Prentice Hall, 1963; a research study prepared for the Commission on Money and Credit.

business at a disadvantage in contrast to some other forms of enterprise such as cooperatives. It retards new investment. It reduces investment per worker. It raises the average age of plant and equipment of our capital stock. It distorts investment decisions because of its severe bite. It consumes an enormous amount of time of high-priced talent in problems of compliance and efforts to avoid its burden. Virtually all major business decisions are tax oriented.

"In the face of these points, it is hard to understand the tardiness with which any cut was proposed, the smallness of the cut proposed in January 1963, and the spread of the cut over 3 years.

"The foregoing is a substantial indictment. Objective scholars, generally, have nothing good to say for the corporation income tax. Its survival can be explained chiefly in terms of its fiscal prowess as a revenue raiser, the misconceptions about its incidence and about its economic impact. Part of our indictment is based upon the assumption that the tax on corporation income is largely passed on to the consumer, and is not substantially absorbed by the shareholders. What follows is not a plea for shareholders—they do not bear its burden or at least its major burden; our analysis is designed to encourage more rapid economic growth. First, we must note the differences between those who think that the corporate tax is absorbed by the shareholders and those who think it is largely passed on to the consumer.

"For those who think the tax is absorbed (a declining number), the present tax would imply a reduction of corporate or shareholder income by 52 percent. Clearly this tax take of 52 percent would involve a striking reduction in the volume of retained earnings available for financing new investment; it would, likewise, greatly reduce the potential savings of shareholders. Since under the assumption of absorption the prospective return from new corporate investment would be greatly reduced, this impairs not only the supply of investment funds, but also the incentive to use them. It would slow economic growth.

"Now what of those who believe that this tax does not greatly reduce corporate or shareholder income? Unlike those who believe that the corporation income tax is absorbed by the shareholder, those who believe it is predominantly shifted generally tend to view (but wrongly) this tax as relatively harmless—just a hidden sales tax and a meritorious gatherer of revenue for Uncle Sam, with no adverse effect on corporation saving, investment, risk taking or innovation. Those who believe the tax is shifted tend to be largely complacent about the size of its bite, just so long as their competitors are equally taxed. But this is a dubious conclusion and a wrong inference.

"By what process is the tax shifted to the consumer? Certainly not by merely adding the tax to the price. When business costs rise, this does not mean that higher costs can automatically be passed on to the consumer * * *. In the case of a regulated public utility, insulated from competition, new costs may be added on. If all competitors could and would simultaneously raise prices by the amount of the corporate tax, this might stick. But such is not the means by which the corporate tax is shifted to the consumer in a competitive economy.

"Rather, the shift occurs slowly and gradually by the curtailment of the supply of goods and services offered. Basically, the tax reduces supply by imposing a new barrier to added investment, which barrier would not exist if there were no such tax.

"Initially when adopted or raised, the corporate tax may tend to fall on equity investment, on shareholders. For this reason the dividend credit is justified. But since the investor has alternative opportunities and weighs the risks and earnings prospects, a new investment to be justified must promise to yield a pretax return which will leave a satisfactory return after the payment of the tax. In short, new investment must promise not only a satisfactory net return, but also the tax itself. A cut to 50 percent in 1964 and 47 percent in 1965 will help, but will still prove to be an undue handicap, particularly in the face of the proposed accelerated tax collections.

"Here is the essence of the situation: Assuming 10 percent to be the needed incentive, new investment and new ventures tend to be deferred until they hold out the prospect of earning 10 percent net after tax (although some investment may be undertaken not to earn a return, but to protect the return from previous investments). The tax, nevertheless, defers new capacity and innovations. Older equipment tends to be used longer; this induces a rise in the average age and obsolescence of our plant and equipment. It reduces the investment in tools per worker.

"This protection of existing investment against new competitive investment reduces the output and permits the sale of the output at prices which are higher than could otherwise be obtained. This is the process by which the corporation income tax tends to be shifted to the market—to the consumer.

"To induce new investment, moreover, the pretax anticipated yield must be progressively higher (not just proportionately higher) as the tax rate rises.[4] Under a 50-percent corporate income tax, for example, if the investor is to keep $1, the company must earn $2—$1 for the U.S. Treasury and $1 for the investor; if the corporate income tax were 75 percent and the investor wanted to keep $1, the corporation would have to earn $4 pretax—$3 would go to the U.S. Treasury and the $1 would go to the investor. (The latter to be taxed also, of course, as individual income). The tax rate above 52 percent would not only exact heavy penalties, but substantial reductions in tax from this level would offer large advantages; a reduction of 12 percentage points from 52 percent, for example, would yield more than 40 percent of the benefit to be obtained by abolishing the corporate tax entirely. The above contrast of a 50-percent and a 75-percent tax rate shows why this is so.

"In short, the indictment against the corporation income tax is severe. Thus it should be clear why economists, generally, can find nothing good to say for it in terms of the optimum operation of our economy."

In summary, the tax bill is desirable as a rough and ready measure to stimulate investment in the short run and also to reduce the fiscal drag of wartime rates on individual income. Exaggerated claims have been made as to the precision with which the effects of the tax cut can be estimated. Its impact on investment is less than needed to promote markedly more rapid growth, its impact is likely to be

[4] See: George Terborgh, "Effect of Corporate Income Tax on Investment," Machinery & Allied Products Institute, Washington, D.C.

primarily short run, and it is not the panacea that the repetition of claims for it has tended to instill in the public mind.

One last point is the threat some observers see that in 1964 the impact of the tax policy package could overstimulate the economy—and thus increase pressure on prices, promote excessive wage increases, and borrow business from 1965. The prospects of renewed inflation, if realized, could offset the beneficial effects of the tax cut and jeopardize efforts to deal with the balance-of-payments problem. For example, the full employment budget section of the Economic Report suggests a rise of $6 billion annually in tax take at present rates, adding that the resulting full employment surplus would have to be offset either by an equivalent increase in discretionary Government spending or private sector spending. However, if $8 billion of the $11 billion tax cut is realized in 1964, at the very least no increase in Federal spending would be called for.

On the one side are prospects for some defense cuts in fiscal 1965 and beyond, as some programs and facilities are gradually phased out. if such reductions materialize and defense contracts are shifted or reduced in the next year or so, the tax cut may set the climate for ease of adjustment in all but heavily defense-dependent local areas. On the other side, if the expansion gathers force early, pushing the economy toward capacity while rising sales and reduced tax liabilities keep profits up, there may be pressures on prices. Timing is the key. Meanwhile, 1964 is an important year for wage negotiations. Already, the trucking industry and more than 400,000 teamsters have signed a nationwide contract, increasing wage and fringe benefits 40 to 45 cents per hour over a 38-month period. Soon will come negotiations of a half a million auto workers, with contracts expiring at the end of August—and hundreds of thousands more workers this year in such major industries as apparel, machinery, communications, and transportation.

The Economic Report notes with concern "a series of specific price increases in recent months—especially in manufactured goods." But the ambivalence of the report about inflationary pressures can be seen generally by comparing the deficient-demand analysis of chapter 1 with the wage-price policy analysis of chapter 4. Chapter 1 is permeated by concern about economic stagnation at less than full employment. By contrast, chapter 4 is almost strident in its concern lest 1964 lead to inflationary pressures.

In this connection, it is of course incorrect analysis to identify particular wage and price increases in a dynamic economy with inflation—made up of a rise in the general level of prices (some broad price index) and fundamentally a monetary phenomenon. This point becomes particularly crucial to preserving our whole market system when there is direct Presidential intervention in the setting of individual prices, as in April 1962 when President Kennedy revealed the awesome power available to a Chief Executive today to achieve conformity from business firms through intimidation and threatening action from a wide range of Government agencies.

UNEMPLOYMENT POLICY

One problem the administration has been unable to solve is the chronically high unemployment. The extent of the problem is suggested by the difference between a 4-percent unemployment rate and the 5.5 percent or higher rate that we have seen throughout the present 1961–64 expansion. The position of the Economic Report in its early chapters is that such unemployment is primarily the result of insufficient total demand. To be sure, this position is supported by evidence of ample industrial capacity. At the same time, the shifts in the demand for skills in the labor force and in the composition of the labor force are proceeding rapidly enough to suggest caution in interpreting the causes of unemployment. At present, it is true that unemployment is reflected through several components of the labor force and is widely spread geographically. The unequal incidence of unemployment, falling more heavily upon unskilled, young, and nonwhite, would continue, in effect, at lower aggregate rates of unemployment stemming from increased total demand for labor.

However, the Economic Report reflects in its chapters on poverty and technological change a growing albeit primarily implicit recognition that in the future unemployment is more likely to stem from structural forces. The rapid increase in 18-year-olds which has already begun will continue until 1970, while the number of more experienced workers will barely rise. In the meanwhile, the skill distribution of job openings is shifting toward more education and experience. These two forces will be at work during a period of more rapid technological change. Since in 1963, GNP rose without a tax cut by more than the Council forecast with a tax cut, and still unemployment remained about 5.5 percent, the evidence increases that the problem of joblessness is now heavily structural. The inference seems strong indeed that future unemployment rates may be less responsive to measures aimed simply at increasing aggregate demand.

The Council's recognition of longer run structural problems of unemployment and disadvantage is presumably what motivated the chapters on poverty and adjusting to technological change (chs. 2 and 3). Insofar as these chapters begin the process of analysis necessary to develop sound public and private policies to maintain employment while meeting other economic objectives, such as sustainable economic growth, price stability, balance-of-payments equilibrium, and rising living standards in a free, competitive economy, they are a valuable contribution. However, it would be regrettable if the cursory treatment of such important subjects given in the Economic Report were to be accepted as a valid analytical basis upon which to impose far-reaching Government policies.

Unemployment and poverty

The discussion in the Economic Report on the concept of poverty appears to rest primarily upon the hypothesis of the relative stagnation of the American economy. The "neostagnationist" school refers to what it sees as slow and unsteady growth—from 1952 to 1962, for example. It complains that, unlike European economies, the United States has "lagged in applying new knowledge about how to induce economic progress." Therefore, it is argued, new Government policies should push the economy into entirely new patterns.

Careful students of economic growth in the United States, however, do not accept the thesis of a "slowdown" in recent years so readily. In a very important but little noted study, Clayton Gehman of the Federal Reserve Board examined the thesis of a "slowdown" in the Federal Reserve Bulletin for August 1963. He concluded that preoccupation with aggregate measures of activity rather than actual end products of economic activity "may, because of increased efficiency in the use of resources, create an unwarranted impression of sluggish performance by the U.S. economy." Another implication of his study is—

"* * * that there is less slack in the U.S. economy than is generally supposed * * *. An accelerated rate of expansion in overall activity would increase final demands and investment requirements; and with this increased investment, incomes and consumer demands would doubtless rise faster. How much of the increase would be sustainable is another question. If expectations become too exuberant in the process of economic stimulation, this might increase upward price pressures and encourage speculative activities. The present character and location of plant and equipment facilities and the existing limited supplies of skilled and professional labor may provide fewer safeguards against such developments than is indicated by the view that a slack economy exists. Increased emphasis on expanded educational and occupational training opportunities would help reduce unemployment rates and would provide wider margins of available, effective resources" (p. 1060).

The neostagnationist tends to advocate a long line of expanded and added programs for the Federal Government. Such programs, it is felt, involve Government more directly in the economy, guiding it in "desired" ways. They also are thought incidentally to achieve Government "welfare" goals. By adding the taxpayer's money back into the spending stream—plus deficits in all except "full employment" years—their technical effect, it is argued, is to restore the otherwise stagnating economy to its potential. Full employment policies thus seem to the neostagnationist logically to include a gradual eradication of poverty—through Federal leadership and spending programs.

Some of these programs include the following.

Public policy measures to increase public works (for manual and young workers).

Reduction of tax burdens in low-income brackets.

Much more generous unemployment benefits.

Increased allocation of resources for schools, hospitals.

Expanded slum clearance and urban renewal programs.

Radical revision of education, including vocational education.

More social security-financed welfare measures.

Comprehensive minimum-wage legislation.

Organization of masses of very low paid workers into special trade unions—protected from racketeers—and unified into a force for political action.

Few would quarrel with the national goal of reducing poverty to the minimum humanly possible in a free society. However, the means by which such a reduction may take place require careful thought. The era of the scientific revolution we are now entering is likely to increase the premium that nature pays for policies based upon understanding many forces at work in our environment. Some of these forces are ecological—indirect, delayed effects upon entire populations and their environments, of actions directed at specific aspects of the life of individuals. Air pollution, water pollution, chemical damage, and other such examples readily come to mind, and we are likely soon to see more of them.

There has been, in this connection, insufficient study of what might be called "national management." For example, the Federal agriculture program, through a long history, has had effects entirely unanticipated while it has steadily failed to meet the test of reasonable performance of its stated objectives. That program has increased surpluses, complicated farm marketing, reshaped the relation of farmer to Government, and left us with a large and restive Federal bureaucracy. Or, to take a more recent example, Federal slum clearance and urban renewal, after a decade, has not produced the intended effects. In general it has subsidized more housing in higher income areas than in lower income areas. Moreover, the evidence does not indicate that improvement in housing conditions has been more rapid in subsidized communities than in unsubsidized ones. Students of architecture are more and more criticizing the drabness and monotony of urban renewal planning—as compared, even, with the original slums.

All of these results—unexpected results—of Federal programs are puzzling. Considering poverty, for example, at first thought it would seem unassailable that the United States now has the resources to move confidently toward "forever" eradicating poverty. But upon careful analysis, such an assumption reveals hidden dangers. For one thing, it cannot refer to relative poverty, unless it is assumed that (1) incomes are equally distributed (there is always a bottom 50 percent of income receivers, even on Park Avenue); (2) that incomes remain equally distributed (which most leading economists have doubted is even possible).

Another potential pitfall in such an assumption has more immediate effect on "practical policy." According to a leading student of population growth.

"In our renewed enthusiasm for childbearing and having children, we may have unwittingly created a situation which will cause those children to live at a substantially lower level of comfort and security than was enjoyed by the people who have them."

Donald J. Bogue of the University of Chicago, widely respected authority on population growth, says further.

"At present we are on a collision course that could lead us to catastrophe, timed to arrive only a very few decades after our sister nations (if they too do not alter their growth rates) have crashed on the Malthusian reefs. There is growing agreement among demographers of the world that rapid population growth does have its costs—wherever it occurs. In the United States it makes it more difficult to make progress, and may lead to a decline in well-being for a substantial share of the population." [5]

Population growth is only one example of many in which ecological effects should be considered. Another is the proposal for a widely applied higher minimum wage. The reasoning of well-meaning people might go like this: Many people with jobs are poor; to raise the minimum wage would let them escape out of the poverty level; therefore let us raise it to, say, $2 per hour. But in fact, this violates a simple economic principle. At a given demand, as the price of a service rises, the quantity demanded goes down. Few employers would be willing to pay the higher minimum wage to any workers but those thought to be producing $2 an hour or more. Young, unskilled, unexperienced labor—the very type now unduly burdened with joblessness, would find unemployment increasing. Further,

[5] Donald J. Bogue, "Population Growth in the United States," *The Population Dilemma*, ed. by Philip M. Hauser, American Assembly, New York, 1963; reprinted, Population Bulletin, vol. XX, February 1964, p. 26.

wherever possible, employers would find it paid to substitute machines for labor. Unemployment would increase further. Coal, steel, and auto industries furnish clear examples of a shift away from unskilled labor.

The administration's program for a war against poverty is of course not available at this writing. The Economic Report sets the goal, provides some preliminary analysis of the problem, and seems to set administration strategy. The following discussion is limited to some aspects of analyzing the problem. It is perhaps well, under all the circumstances, to bear in mind that the poverty campaign, if mounted, may be long and full of surprises. This is especially significant to the victims of poverty themselves, who are least able to adjust to the disappointment of false hopes.

Perhaps the most remarkable feature of the Council's analysis of poverty is its completely static framework. There is no indication, for example, of the changing relation between income levels and stage of life or the relation of income to asset holdings; no analysis of income and size of family; no projections of future expected incomes of people over 65 during the next 5 years. Some of the statistics, if not wrong, are at least not relevant. Finally, there is no indication of what is being spent or being done today to cope with poverty. There is a grave threat of large technical errors of public policy when it is based upon so incomplete a study, important and timely as that study may be.

The danger of technical mistakes in public policy is emphasized by the disparity between sums spent in accurately determining the scope and consequence of unemployment and low income, and the sums proposed to be spent based upon information (or lack of information) at hand. For example, hardly more than $2 million per year is spent to collect all our unemployment statistics. There are many questions we cannot answer. For example:

1. What is the relationship between the presently unemployed and the presently poor?
2. Should people not actively looking for work or making grossly unrealistic demands on the labor market be considered unemployed? Should they, if so, be grouped separately?
3. Is the unemployment figure an accurate measure of overall economic activity?
4. How many job vacancies do we have? What is their nature and where located? What is their relation to unemployment?
5. How productive in their past careers have the presently unemployed been?
6. How important is labor immobility in unemployment?

Answers to such questions would make possible intelligent private and public planning to cope with the problems unemployment may bring. The magnificent achievements of modern scientists through patient observation and close technical thought make plain that vague good will, while necessary, is not sufficient for modern government.

The report contains puzzling interpretations of basic statistics. A major example is the definition of poverty on pages 58 and 59. The definition is family income of less than $3,000 (1962 prices), and unrelated individuals with income less than $1,500 (1962 prices). This definition is qualified:

"No measure of poverty as simple as the one used here would be suitable for determining eligibility for particular benefits or participation in particular programs. Nevertheless, it provides a valid benchmark for assessing the dimensions of the task of eliminating poverty, * * *."

However, the definition is the basis of some 16 tables, 3 charts, and 30 pages of text in the Council's portion of the report and almost 2 pages of the President's report.

The U.S. News & World Report (January 20, 1964, pp. 36–39) points out the asset holdings of some families classified "poor" by the Council's definition. Numerous examples could be cited. The 1960 Census of Population reports Adair County, Ky., had a median family income of $1,939 with 67 percent of the families reporting incomes under $3,000. Yet 74 percent of the families occupied their own home, 77 percent of the occupied housing units had clothes washing machines, 12 percent had home food freezers, 2 percent had air conditioning, 52 percent had television sets, 57 percent had one automobile, and 16 percent had two or more automobiles.

The discussion of poverty in the Economic Report leaves many economic policy questions unanswered. Are all problems of poverty now to become a permanent Federal responsibility under the Employment Act of 1946? Is such the intent of Congress? Has Congress expressed this intent? What does Congress intend should be the relation between Federal, State, and local agencies in the field of poverty fighting?

On reflection it is hard to understand what the problems of Indians on reservations have in common with those of housing dependent urban children; or restoring the indigent, homeless male with medical care of the aged. Rather than toss all these people into the same Federal civil servant's desk file, it would seem that the multiple forms of poverty might be attacked one by one. What, otherwise, will be the unforeseen consequences of drowning in a slogan the patient and unheralded efforts of the donor of private charity, the corporate foundation, the public health doctor, the county nurse, the patient slum teacher, the faithful city welfare worker?

Adjusting to technological change

The discussion of technological change (chapter 3) can also be divided into sections on analysis and policy. The chapter is a valuable preliminary exploration of a subject about which not enough is known. The chapter, indeed, illustrates the urgency of our need seriously to study the problems it poses. The chapter, as others, is cast in the simple framework of aggregate demand analysis. It is comforting to learn that the Council believes that "historically, there is surely no evidence of any inability of demand to rise along with productive capacity, or of any permanent inadequacy of total job opportunities" (p. 94). But this is (of course) not true in the short-run (p. 95). Yet, fiscal and monetary policy "are capable of righting the balance whenever the job-destroying effects of technological progress outweigh its job-creating effects" (p. 95).

Thus, the Council misses an analytical opportunity to explore the costs of technological change, to ponder possible ways in which in the future they may be equitably shared in such a manner as to foster free, competitive enterprise and a free society.

The Council recognizes the problems of labor market adjustments, but seems to feel that the major problem is that "the flow of labor market information is unnecessarily slow and circumscribed * * * the average displaced worker spends far too long between jobs * * * even in periods of adequate demand." (Could some of this be voluntary?)

By contrast, the problem of changing skill requirements is almost ignored, or at least too easily dismissed: "It is not clear whether automation has caused any accelerating in these trends * * * further studies are needed." The general diagnosis of the Council is thus that our major problem is short-run stagnation, not long-run structural difficulties, and that mechanization problems are derivative, not fundamental. A strong body of professional opinion disagrees with this interpretation, as the present statement has indicated.

As for policy recommendations, the Council argues for more Federal participation in basic research and development as social overhead costs, and for expansion of Federal activity in the manpower field, including expansion of the Federal-State employment service. There is little question that more research and development is needed, or indeed, that labor market information can be improved. The difficult question—being pondered by more and more large universities. for example—is how to avoid Federal direction of research. Likewise, it takes no Lord Acton to appreciate the threat to small- and medium-size businesses—or to universities—of a greatly expanded Federal-State employment service occupying a dominant role in the labor market information field.

WAGE AND PRICE POLICY

The Council's discussion of wage and price policy is unsatisfactory. The core of the remarks on price and wage policy in chapter 4 of the Annual Report of the Council of Economic Advisers (January 1964) seems to lie in the following main ideas:

(1) "The general guidepost for prices specifies that when an industry's trend productivity is growing less rapidly than the national trend, prices can appropriately rise enough to accommodate the labor cost increases indicated by the general wage guidepost" (pp. 118–119).

(2) "Similarly, in an industry whose trend productivity is growing more rapidly than the national average, product prices should be lowered enough to distribute to the industry's customers the labor-cost savings it would make under the general wage guidepost."

(3) Each of the above statements represents what might be termed a Council-sponsored ideal for the outcomes of private pricing decisions and wage bargains. Rigorously applied it assumes the wage bargain will follow national trends in both kinds of cases although management incentives in the first case and union incentives in the second case may strongly resist the intended outcomes.

(4) Since actual productivity figures, if ascertained for individual firms, would be historical figures of past performance and not necessarily appropriate to current wage and price decisions they could not effectively serve as operating guidelines for current decisionmaking. In estimating future market consequences of present production, pricing and wage decisions, the relevance of numerous assumptions required could not be known with assurance in advance. Hence the applicability of the ideal "guideposts" would likewise be uncertain.

(5) Neither the theoretical concept of an "industry" nor its counterpart industry wage bargain would readily approximate actual market

structure and the institutional influence of key wage bargains closely enough so that the normative ideal could serve as the operating guideline.

(6) If the National Government were to attempt a widespread industry-by-industry evaluation of "conformity with guideposts" some sanctions would presumably be considered for nonconformists and a far-reaching intervention in the rewards, risks, and decisionmaking of the enterprise system would be implicit.

The more general or inclusive a productivity measure becomes the less likely it appears to be applicable to the circumstances of individual firms and areas covered in wage bargaining, hence the less relevant as a policy guideline. On the other hand productivity measures most relevant to small unit circumstances, would presumably vary widely with those specific circumstances, and hence be unlikely to meet the comparability criteria needed for industrywide or national "guideposts." The feasibility of constructing genuine productivity measures for individual cases sufficiently in advance of actual decisionmaking to serve as accurate and realistic guides to those decisions seems very doubtful. Thus the productivity guideposts, while expressing a desired outcome of the pricing process, can be applied only after the outcome has been established. It is hard to see how the guidepost principle, or its more interventionist counterpart—"incomes policy" now being discussed abroad—can be implemented without shaking the foundation of the market system for pricing decisions.

Perhaps the most unsatisfactory aspect of the wage-price policy discussion by the Economic Report is the continuation of the idea that the Government must intervene in individual price and wage decisions that are thought to be contrary to the public interest. Walter Fackler has accurately described this essentially know-nothing tactic as "banging on the economic machinery." For the Chief Executive of the U.S. Government, without specific legislative grant of authority, to assume the role of arbiter in particular cases of market price setting, as a matter of national policy—or to "advise" solutions after the manner of President Kennedy's display in April 1962—is in principle an inadmissible procedure in a free, constitutional society. Price control by Executive fiat would subvert not only the separation of political from economic power which has preoccupied the best minds in American political and economic thought. It also displays an unawareness that is difficult even to account for, of constitutional principle.

The idea of Government price supervision or "advice" is tantamount to price control if vigorously exercised through the coercive power of the Nation's largest purchaser, tax collector, licensor, regulative agency, law enforcement agency, and investigative agency. The threat to "call public attention" to certain price increases and wage increases—assuming it is a continuation of President Kennedy's policies instituted in his attack on the steel industry in 1962, is sufficient to be coercive. The Federal Government carries so big a stick in our era that it need not shout in order to coerce. Such a concept certainly cannot, by any stretching, fit the "framework of free enterprise" to be fostered by the Employment Act of 1946. It is not only an affront to the free enterprise economy to intervene arbitrarily in price decisions but it is also a traumatic blow to the body of U.S. constitutional law.

Consider, for example, the viewpoint implied in the doctrine that the President is the arbiter of "the public interest." This concept, upon analysis, must imply that the individual judgment of one individual is, in principle, superior in his apprehension of "the public interest" to (1) the market system of economic exchange slowly evolved by mankind over thousands of years, and (2) the competitive pressures working upon 4.7 million business firms and 3.5 million farms serving a consumer market of 190 million people. Likewise, history furnishes no evidence that Government officials and staff possess the ommiscience required to substitute for the complex judgments of freemen and free markets—quite the contrary. The wage-price discussion of the Economic Report is, in short, seriously disturbing.

The report proposes commissions to determine those industries in which imposition of double time penalty rates for overtime would lead to overtime reductions and resulting increases in employment. The very proposal itself acknowledges the uncertainty as to the extent (in fact, small) to which overtime can be substituted for additional employment. Literal arithmetic estimates of new employment reached by dividing total overtime hours by 40 hardly deserve comment. What is not well appreciated even by experts, however, is the inherent waste of time, energy and skills involved for commissions, industry, unions, and Government in making the determinations. As only one example, the definition of an industry for such purposes is interminably complex and destined to be unsatisfactory and even unworkable in many cases.

BALANCE OF PAYMENTS

The balance-of-payments problem remains unsolved. Optimism in the Economic Report that by implication balance will be achieved by 1968 is based on slender reeds. One is the heroic assumption of a "sustained expansion of the U.S. economy which, after the unemployment rate was reduced to 4 percent, would proceed at an annual rate of 4 percent and later accelerate to 4½ percent a year" (p. 131). How heroic is such an assumption? Estimates are that with an extension of postwar average productivity trends and shifts in labor force composition, to reach 4 percent unemployment by 1966 would require sustaining continuously a real growth rate of more than 5 percent per year, or a growth rate of more than 6½ percent, allowing 1½ percent for price-related effects. Other sources of the Council's optimism depend upon assumptions that increases in exports would more than offset expected import increases produced by such an economic expansion, and that the United States would be better able to maintain internal cost and price stability than Europe. When such assumptions are considered in relation to Gehman's study (Federal Reserve Bulletin, August 1963) of the weakness of GNP measures in understating growth characteristics, it seems compelling that the Economic Report is overambitious.

So far, administration policy measures admittedly have principally bought time for needed adjustments; or they have bolstered the informal international framework of central bank cooperation in an "early-warning" system to protect the dollar against runs and to reduce the gold outflow through special foreign dollar-holding arrangements. Also, monetary policy measures to maintain short-term interest rates have from time to time, according to one school of thought, resulted in measurable repression of the economic advance.

The chronic balance-of-payments deficit is a domestic problem in just the sense that it has influenced domestic monetary and other policies geared to achieve economic stability and growth, sometimes in perverse ways. The essence of the balance-of-payments problem is that, given existing foreign economic policy of the United States, the dollar is overvalued in terms of other currencies. At present fixed exchange rates the United States is unable to export enough to cover both imports and the large outflow of private and public capital including military and foreign aid.

The possible alternative solutions to the problem are limited in number. Let us examine these solutions and the report's views concerning them. One, devaluation, is not discussed, presumably because it is considered untenable. Likewise, freely fluctuating exchange rates, which automatically eliminate payments problems, but transmit relative cost and price pressures directly from country to country, are also rejected. However, less drastic measures are also politically unattractive. Various Government measures to increase price flexibility downward; such as, severe tightening of credit to force down U.S. costs and prices or measures to reduce union monopoly power over wage settlements, are looked upon as too harsh in their effect on domestic aggregate demand and employment. Vigorous negotiation with allies to reduce economic and military aid burdens has apparently proven unsuccessful.

The consequence has been a series of measures which step by step have moved or would move toward imposing arbitrary restrictions on trade and, to some degree, on capital movements. Restrictions of imports through reduced tourist allowances, the tying of loans, bilateral trade negotiations, export subsidies through defense procurement policy and Public Law 480, restriction of capital flows by negotiation and suasion, partial devaluation through the interest equalization tax, in effect gold guarantees in short-term convertibility provisions of swap agreements—all these measures regretably move away from rather than toward the ideal of a world of freely competitive, open economies.

It is difficult to foresee any end of the balance of payments problem except a new and better international monetary system. The signs are unclear that such a development is currently in prospect. The various schemes for improvement all rest upon some form of limited cooperation among leading financial countries of the Free World. Such limited cooperation through central bankers is a different system from the ideal of open, multilateral trade with freely convertible currencies among independent trading partners. There is a growing body of professional opinion that freely fluctuating exchange rates would be the next step toward securing and fostering such open societies, at the same time freeing the monetary system from dependence on a monetary commodity. As yet, however, the various studies by official bodies, such as "the Ten" and the International Monetary Fund have not proceeded far enough to permit any judgments to be made of the ultimate character or consequences of possible new international monetary arrangements.

Meanwhile, the balance of payments problem remains.

CONCLUDING REMARKS

In conclusion, it may be worthwhile for the record to note the analytical framework and posture of the Economic Report for 1964. The analytical structure sets the strategy and tactics of Government policy and so may dominate the character of the administration. The Economic Report for 1964 starts from an exercise in simple aggregative analysis with resulting lack of stress on structural deficiencies, and resulting omission of freedom criteria. At the base of the analysis is the inadequate demand hypothesis. This simply holds that the private economy does not (cannot?) generate enough purchasing power in the short run (long run?) to maintain expansion of production to its potential. Potential is naively defined a priori. It is how much could be produced if the economy grew minute by minute at a real rate of 3½ percent per year. Possible difficulties in reaching and sustaining such a growth target and historical evidence to support its choice—these are not discussed this year, so that there is an air of finality about measures of potential.

Typically, the report holds, reversals from expansion can be traced to a failure of aggregate demand to keep pace with the expansion of capital facilities. Therefore—and this is a key—Federal expenditures have and should continue to have a large role. Indeed, more Presidential discretionary power is needed, so it is argued, to vary tax rates or Federal spending without congressional "interference."

The results of this analysis are evident throughout the report. Monetary policy and its role are considered to be only complementary. Continued high Federal spending is economically necessary to prevent recession, possibly to stave off economic stagnation. Thus, while the budget appears to move toward spending reductions, at the same time provision is made for added new obligational authority or removal of appropriations limits which would soon permit very large-scale Federal spending. Such spending, popularly called "welfare-type" spending, is better understood in the report's interpretation as economically necessary increases of aggregate demand that incidentally serve "welfare" goals.

Through the Council's eyes, many seemingly bizarre or inconsistent elements in the report disappear. It is not considered inconsistent to accept naive poverty concepts unsupported by calls for empirical evidence of the relation of income to asset holdings, or of unemployment to hardship. It is not considered questionable methodology to discuss poverty entirely apart from any consideration of population growth. And it is not regarded as inconsistent to imply that there is need for added Federal expenditures for research and development without exploring the powerful analytical concept of the cost of technological change. Such analytical factors logically flow from a conviction throughout that the urgent concern is prolonged inadequacy of aggregate demand.

While the power of abstract hypotheses is to trace out non-self-evident chains of reasoning, their pitfall is, through their power of exclusion, to direct attention away from some classes of possibilities. Can economists, by analogy to Keynes' practical man, be captives of "some defunct hypothesis?" Certainly, this has been a popular view concerning the so-called classical economists. By the same token, the validity of the inadequate demand hypothesis is a seriously debatable issue among economists. Recent work in monetary economics raises vital questions about the relative roles of fiscal and monetary policy. Grave political difficulties with added centralized discretionary spending and taxing power intervene to question successful use of some prescriptions of the inadequate demand theory. The remarkable success of free enterprise policies since World War II here and abroad, particularly in Western Germany, raise further questions about the policy prescriptions of large-scale government intervention in economic affairs.

Use of the neostagnation hypothesis excludes large classes of possibilities from serious consideration. We see in the Economic Report, for example, no systematic treatment of Federal policies to foster free enterprise. Yet a case can be made that "the central question at trial in this Nation is whether man can organize together in a highly industrialized society, succeed, and still be free." The report, by ignoring the implications of more Federal Government financing of research and development, fails to consider alternative solutions—such as, for example, quasi-public foundations that would diffuse power by having public, industry and educator members. Suppose more labor market information would enhance labor mobility. There should be ways for history's most successful enterprise system (with the world's most mobile labor force) to accomplish the objective through fostering free enterprise; that is, trying to think of devices that encourage the private labor market information service industry—rather than enlarging the role of the Federal-State employment service. But such ways are not explored.

Thus the political and social bias of the Economic Report remains in the direction of big Government and large-scale spending schemes supposedly to solve unemployment. Such an economic bias provides the framework for those like a prominent magazine editor who is reported to have said about Federal aid to the arts "that he was not afraid of creeping socialism, but the creeping philistinism, creeping mediocrity in the arts." [6] To the lover of freedom, the comment of Erik Satie may have more appeal:

"To have turned down the Legion d'Honneur is not enough. One should never have deserved it."

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[6] Eliseo Vivas, "Art and the Artist's 'Citizenship,'" The New Argument in Economics, editors, Schoek and Wiggins, D. Van Nostrand, 1963.

COMMITTEE FOR ECONOMIC DEVELOPMENT

BY T. O. YNTEMA, CHAIRMAN, RESEARCH AND POLICY COMMITTEE

I submit this statement in response to the request of the Joint Economic Committee for comments on the Economic Report of the President for 1964. I respond to your invitation on behalf of the Committee for Economic Development. However, I should make clear that the CED has not had an opportunity to study and discuss the Economic Report and that my comments are my own except where I specifically refer to positions previously taken by the CED.

The 1964 Economic Report of the President and the Annual Report of the Council of Economic Advisers which accompanies it constitutes an excellent description and analysis of the economic problems before the country today. The Council is to be congratulated for the sharpness with which it has focused on the key issues and the clarity with which it has presented the relevant information and argument. The President's report and the Council's report can serve a valuable educational function; they should be widely distributed and read.

With most of the analysis and many of the recommendations contained in the reports I agree. At some points, however, in my opinion, the economic reports have stopped short of solving the policy questions to which their analysis relates; at others they seem to have reached policy conclusions not fully supported by the analysis. My comments will deal with some of the main aspects of policy about which more thought is needed.

TAX POLICY

The reduction of Federal taxes is in the foreground of the economic program contained in the report, and I shall comment on that first.

In a policy statement issued in December 1962, the Research and Policy Committee of CED recommended that a tax cut of $11 billion should be enacted early in 1963 if budgeted Federal expenditures for fiscal 1964 could be held to the fiscal 1963 level. We estimated that this combination of tax cut and expenditure restraint would leave tax rates high enough to balance the budget (income and product accounts) when the economy was operating at high employment.

It is now the administration's proposal to enact a tax cut of $11 billion early in 1964 and hold Federal expenditures in fiscal 1965 approximately to the fiscal 1964 level. The Economic Report suggests that after this has been done, tax rates will still be high enough to balance the budget (income and product accounts) when the economy is operating at high employment.

Thus, in its overall magnitudes the current proposal is to do in 1964 essentially what we recommended should be done in 1963. The proposal is a sound one for the same reasons that made it sound a year ago. The economy is still operating too far below its potential, partly because Federal taxes are taking too much out of the private income stream and depressing incentives to invest and produce.

We recognized a year ago, as we recognize today, that a tax reduction has its effects on a future that we can foresee only imperfectly. This being the case, one cannot be sure that a tax reduction today will not contribute to an inflationary tendency tomorrow. The answer to this uncertainty, in our opinion, is not to do nothing but to be prepared with corrective measures that can be taken if necessary. The main instrument that must be kept available for use if serious danger of inflation appears is restrictive monetary policy.

Enactment of the tax bill will be an achievement in which the Congress can take pride. This will obviously be the major piece of fiscal legislation of the past 10 years.

It would be natural if Congress should be reluctant to take up the problem of taxation again for many years, after the passage of so large and difficult a tax bill. But unfortunately the question of Federal taxation needs persistent attention and cannot be allowed to lapse for another 10 years. There are two reasons for this:

1. The current tax bill leaves unresolved many important issues of tax reform. This was inevitable in the circumstances. Our most urgent need was to reduce taxation. But after the tax cut we will still be left with heavy taxation, and the character of the tax structure will have major effects on the economy.

One of the critical questions, as we see it, relates to the future of corporate profits taxation. The standard rate of corporate profits tax was raised "temporarily" to 52 percent during the Korean emergency, with a legal provision that it should recede to 47 percent when the emergency was over. A succession of "temproary" extensions has kept the rate of 52 percent until the present. CED's Research and Policy Committee recommended that the rate of corporate profits tax should be reduced to 42 percent, as part of the current tax reduction. However, the present bill leaves the rate at 48 percent. We believe that so high a rate of corporate profits tax is not consistent with the national goal of more rapid growth in a free economy.

2. As the economy grows, the revenue yield of the existing tax system rises. The Economic Report estimates that with present tax rates the revenue at full employment would rise by about $6 billion a year. At the lower tax rates that will exist after the pending tax cut this figure will probably be closer to $5 billion. Also the Economic Report's estimate assumes a continuing gradual price rise, which we would hope to avoid. However, even after an allowance is made for this, the annual growth of revenues would be large.

This growth of revenues can be a blessing if we use it wisely, but it is not inevitably a blessing. One danger, as the Economic Report points out, is that the growing revenues may generate a budget surplus so large as to depress the economy. Another danger, at least equally likely, is that Federal expenditures will rise in step with the revenues, not because the expenditures are needed but simply because the revenues are there. To avoid these dangers we need a policy that will devote a significant part of the growth of revenues to reduction of tax rates. We need to get away from the idea that tax reductions come rarely and with great difficulty whereas expenditure increases are continuous and natural.

If we will exercise forethought, the prospective growth of revenues will provide an opportunity not only to reduce taxes but also to reform the tax system by concentrating reductions where they will contribute most to equity, growth, and efficiency.

THE BALANCE OF PAYMENTS

In the past 6 years the American economy has been plagued by two main problems. One has been a persistent excessive deficiency of total production below the economy's potential, with a consequent excessively high rate of unemployment. The other has been the persistent and large deficit in the U.S. balance of payments.

The administration's strategy for dealing with the first problem—the unemployment problem—is clearly outlined in the Economic Report. But its policy with respect to the balance-of-payments deficit is less clear.

The U.S. balance-of-payments deficit has been too large since 1958 and it has been the steadfast policy of the Government throughout that time to reduce the deficit. During that period the U.S. economy has operated further below capacity than most other industrial economies and our prices on the average have risen less rapidly. Also during that period we adopted, as temporary expedients to reduce the balance-of-payments deficit, a number of measures that we would not like to continue indefinitely. Among these are the requirement that our aid to underdeveloped countries be spent on exports from the United States and the effort to substitute defense expenditures at home for defense expenditures abroad even when the result is larger total expenditures. Another such measure is the proposed tax on certain forms of U.S. investment abroad.

Despite the slack in the U.S. economy, despite the relative stability of our prices, and despite the expedients to which we have resorted, our balance-of-payments deficit still remains, after all these years, excessively large.

The Economic Report points to improvements in the balance of payments which it expects to result from the pending tax cut. It is expected that the tax cut will increase the incentive to invest in the United States, rather than abroad, and improve the competitive position of American exports. On the other hand, however, the tax cut will increase the demand for goods in the United States, which will surely attract additional imports and may restrain exports somewhat. One cannot be certain that the net effect of the tax cut on the balance of payments will be favorable. Particularly one cannot be certain of the order in which the various effects will occur. It may make a critical difference whether the initial effect is negative even if the longrun effect may be favorable.

The annual report of the Council of Economic Advisers cites a study by a group of economists which concludes, on the basis of certain assumptions, that the U.S. balance-of-payments deficit will substantially decline, or turn into a surplus, by 1968. One crucial assumption is that prices will rise little in the United States and a great deal in Europe. This assumption seems hazardous. Moreover, as I am sure the authors would agree, the range of possible error in the results is large even if the initial assumptions are correct.

It may well be that we will progress steadily to a point at which we have sustainable equilibrium in our balance of payments when the U.S. economy is operating close to its potential and without the use of measures that impair the efficiency of the world economy or weaken the international political influence of the United States. However, the Economic Report supplies little basis for confidence that this will be the case. Even more serious, the report does not suggest what course of action the United States would follow if this turned out not to be the case.

No doubt, if the optimistic expectations of the report with respect to the balance of payments are disappointed, action will be taken. But it seems to me important that the United States should have contemplated this possibility and formulated a policy in advance, so that we are not forced in some future crisis to choose among the second or third best expedients that are then quickly available.

PRICE AND WAGE POLICY

The 1964 Economic Report, with its restatement of the wage and price guideposts, raises the question of the proper role of the Government with respect to the determination of particular prices and wage rates. This question deserves serious consideration, because it is at the heart of the relation between the Government and the private economy.

At issue is the role of free, competitive markets as compared with the role of Government in the guidance of our economy. One aspect of the issue is whether there is a way of exercising Government influence over prices and wages through moral suasion and leadership that will be effective without in fact constituting Government control of a kind generally considered alien to American tradition and values. Other questions, on the assumption that such influence without control is possible, include how, by what legal processes, the Government will determine the standards of price and wage behavior to which the economy should conform. How can it be assured that the standards will bear equitably and without discrimination upon all the individuals, businesses and unions to whom they are expected to apply? If the guidepost policy is a response to a belief that competition in labor and product markets is inadequate, is it better to move in the direction of more Government influence, rather than in the direction of strengthening competition?

These and other questions that could be raised about the guideposts policy are difficult questions. Merely to raise such questions is not, of course, to demonstrate that the policy is wrong. Such questions do, in my opinion, demonstrate the need for study. The Joint Economic Committee could make a valuable contribution to examination of these questions, and I hope that at some time the CED will have well-considered conclusions to offer about them.

THE IMPROVEMENT OF EDUCATION

The President's report and the Council's report both emphasize the improvement of education as a way of improving the performance of the American economy and the quality of American life. In my opinion, better education is at the heart of the programs for reducing poverty and for smoothing adjustments to technological change.

I would like to call attention to an aspect of the problem of improving education which is neglected in the reports, as it is in our thinking generally. This is the need to devote much more research to the discovery of ways to increase the quantity and quality of the educational results we get from the resources we are devoting to education. These resources are vast, especially if we consider the value of the students' time, as we should. They will certainly become larger. There is probably no other industry in the country that, in relation to its size, devotes as little research to improving methods and products as does the education industry. There are probably no other industries in which the lag between the development of an improvement and its general introduction is so long.

To exploit the potentialities of research in education is not exclusively a Federal function, but the Federal Government has a responsibility in this field which may be greater than its responsibility for some other kinds of research. It is gratifying to see that research expenditures of the Office of Education are scheduled to rise from \$11.5 million in fiscal 1963 to \$23.8 million in fiscal 1965. But one must still note that research expenditures of the Office of Education will be less than 2 percent of Federal research expenditures, excluding Defense, NASA, and AEC, and will still be less than the research expenditures of the Fish and Wildlife Service.

CONFERENCE ON ECONOMIC PROGRESS

BY LEON H. KEYSERLING, CONSULTING ECONOMIST AND ATTORNEY; PRESIDENT, CONFERENCE ON ECONOMIC PROGRESS, FORMER CHAIRMAN, COUNCIL OF ECONOMIC ADVISERS

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CHARTS

(Included at end of testimony. See pp. 85–110.)

I appreciate very much this renewed opportunity, as a year ago and earlier, to comment upon the Economic Report of the President, accompanied by the annual report of the Council of Economic Advisers, as transmitted to the Congress on January 20, 1964.

1. THE PRESIDENT'S ECONOMIC REPORT IS EXTRAORDINARILY GOOD

Less than 2 months elapsed between the tragic event of November 22, 1963, and submission by President Johnson of his first Economic Report. Even without making allowance for this shortage of time, I believe that President Johnson's Economic Report embodies what may well be the most significant and encouraging departures in our national economic and social policies during the almost 18 years which have passed since the Employment Act of 1946 became law.

President Johnson has obviously not yet had enough time to re-evaluate in detail all of his inherited economic policy commitments. But the President has had time, and has used this time magnificently, to stake out some new high policy objectives of enormous economic and social significance, and to indicate his determination in due course to implement them with adequate measures in detail.

Two great departures in Presidential policies

The first great departure in high policy is recognition, more clearly and emphatically than ever before at the Presidential level, that the problem of massive poverty in the United States is at the very core of our economic and social difficulties. The second great departure in high policy is the firm indication by the President, at least to a substantial extent, that the resources released by any safe and feasible reductions in defense spending will be turned through the instrumentality of Federal spending toward servicing the great and neglected priorities of our domestic public needs.

My admiration for what President Johnson has thus far done is unreserved. His action should be most heartening to the American people and to the Congress.

2. THE GAP BETWEEN THE PRESIDENT'S ACTION AND THE ANNUAL REPORT OF THE COUNCIL OF ECONOMIC ADVISERS

It must be a fair assumption that the President is fully aware that satisfactory movement toward his high objectives will require many changes in economic policies and programs not yet announced. Consequently, it appears to me that the most helpful procedure for me to follow at this time is to examine whether the economic analysis made available in the Annual Report of the Council of Economic Advisers offers satisfactory promise that sound foundations are being established upon which these needed policy and program reconstructions may be built.

Reluctantly, my response must be largely in the negative, despite my very high regard for the abilities of the three members of the Council and their staff. The economic analysis of the Council seems to me to carry forward some of the major errors of commission and omission reflected in its earlier reports, and my concern is deepened by the fact that the course of economic developments to date should have revealed to the Council errors which were more understandable 3 years ago or even a year ago.

The body of my comments will therefore be addressed to the 1964 Annual Report of the Council.

3. SHORTCOMINGS OF THE COUNCIL'S REPORT IN TERMS OF EQUILIBRIUM ANALYSIS

Inadequacy of purely aggregative economic analysis

The starting point for current and prospective policymaking should be careful analysis of why the American economy during the past 11 years has been characterized by so inadequate a rate of economic growth, composed of a pattern of upward and sideways and downward movements, and resulting in chronically rising levels of idle manpower and plant. The Council relies upon one central explanation of these phenomena—insufficient aggregate demand to maintain our productive resources in reasonably full use. Correspondingly, the Council offers only one basic remedy—a sufficient increase in aggregate demand to restore and maintain this reasonably full utilization.

But I believe that so simplified an analysis, in the context of the U.S. economy, is entirely unwarranted. It does not do full justice to the current state of our economic knowledge nor to our available economic tools. Starting from a period of reasonably full resource use in early 1953, economists in general would recognize that any given level of total production develops enough total purchasing power to clear the markets of the full output. How, then, has the progressive disutilization of available productive resources occurred? It has occurred because the distribution of total available purchasing power has been ill suited to maintain the economy in equilibrium at reasonably full resource use. Indeed, historic observation of the U.S. economy during most times other than total war clearly reveals a tendency toward a distribution of purchasing power and related incentives which cause our productive capabilities periodically to expand at a more rapid rate than the expansion of demand for ultimate products. And this has certainly been the central feature of the U.S. economic performance during the past 11 years. The trouble has been in the distribution of purchasing power, not in total available purchasing power.

The data cited by the Council do not support its general analysis and policy conclusions

The very data cited by the Council indicate that this disequilibrium has been the central feature of the recovery movement since early 1961. Specifically, the Council report points out (pp. 32–35) that, from first quarter 1961 through fourth quarter 1963, measured in uniform dollars, GNP rose 16 percent. Private business investment in producer durable equipment and nonresidential construction rose 20 percent, while the private consumer expenditures which constitute the major proportion of the demand for ultimate products rose only 12 percent. Meanwhile, Federal purchases of goods and services rose only 16 percent and State and local purchases of goods and services rose only 13 percent.

These indications of imbalance among the main components of GNP are then shown to be accompanied by imbalance in income trends. Data also presented by the Council indicate (p. 35) that, again from first quarter 1961 to fourth quarter 1963, disposable personal income in real terms rose only 13 percent, and net income per farm rose only 9 percent from 1961 to 1963. Meanwhile, as stated by the Council, corporate profits after taxes (apparently not adjusted for price change) rose 52 percent, and the rise was immensely greater than this (p. 32) when the capital consumption allowances resulting from increasingly favorable depreciation allowances are taken into account.

Beyond this, the fragmentary analysis by the Council (pp. 44–45) of the causes of the downturns of 1957–58 and 1960–61 indicate that these downturns were sparked by relatively excessive capital goods booms which resulted in grossly deficient ultimate demand when measured against productive capabilities then in being.

Yet nowhere does the analysis of the Council translate the foregoing into what seems to me to be the palpable conclusion that our national economic policies all along have excessively stimulated investment in the means of expanding production, relative to the stimulation of ultimate demand in the form of private consumer outlays and public outlays by governments at all levels. Entirely to the contrary, the policy arguments of the Council adhere faithfully to the early 1961 thesis that the most powerful efforts of the Federal Government should be directed primarily (or at least not secondarily) toward stimulation of saving and investment. This assertion I shall document further, when I come to discuss current tax and spending policies of the Federal Government.

Results of my own studies of the equilibrium problem

For the moment, I should like to submit the results of my own studies, pursued continually since early 1953. These studies have been based upon initial construction of a hypothetical model of the U.S. economy at full-resource-use equilibrium, and upon constant reconstruction of this model in terms of actual developments. The model includes both the product and income sides of the picture, and includes both private and public economic activity. The model is therefore no more nor less than a continuous exercise along the lines intended by those specific provisions of the Employment Act of 1946 which call for estimates of needed levels of employment, production, and purchasing power, and delineation of policies required to hold performance at maximum levels.

My chart 1 (my charts are appended at the end of my statement) indicates that the deficiency in total national production from the beginning of 1953 to date has been dominated by a deficiency in private consumer expenditures. I estimate that, in 1963, the deficiency in private consumer expenditures was about $59 billion out of a deficiency in total national production estimated at $76.5 billion.

My chart 2 indicates that the deficiency in private consumer expenditures has stemmed primarily from a deficiency in consumer incomes. It is also true, of course, that the distribution of consumer income, excessively concentrated at the top of the income structure relative to the number of recipients at the top, has tended recurrently to cause relatively excessive saving for investment purposes.

The demand for ultimate products includes not only private consumer expenditures, but also public outlays for goods and services at all levels of government. My chart 1 indicates an average annual deficiency, 1953–63, of $4.2 billion in these public outlays (measured in uniform 1962 dollars). This deficiency, occasioned mainly by trends at the Federal level, as shown by chart 3, has been much more damaging than the stated magnitudes would indicate, because of the high "multiplier" effect of Federal outlays upon private investment and private consumer outlays. I shall at a later stage go into more detail with respect to the Federal budget.

My chart 4 shows that, even while private investment in plant and equipment was deficient for the period 1953–63 as a whole, it dangerously outran the expansion of private and public demand for ultimate products during each of the upturn periods under review. No inadequacy of profit levels, nor inadequacy of other source of funds available for investment, nor any excessively heavy tax burden upon corporate and private investors, at any times inhibited the relatively inordinate investment booms. These booms were converted into investment downturns only when the excess plant capacities related to ultimate demand, and the prospect of inadequate future expansion in ultimate demand, diminished the ardor of those making the investment decisions. It is especially significant to note that, despite excess capacity during the past year in the neighborhood of 13 to 15 percent, investment in plant and equipment during 1963 expanded much more rapidly than private and public demand for ultimate products. And that neither the profit picture nor the current tax situation constitutes a threat to investment in the near future is clearly demonstrated by my chart 5, which shows the record levels of current profits in key industries despite very large unused capacities.

I find it hard to understand why, standing where we are today, with profits breaking all records, with unused plant capacity so high, with unemployment so large, with ultimate demand so sluggish, the Council still relies mainly upon economic policies which seem to me out of line with basic equilibrium analysis. Indeed, it is hard to reconcile the Council's intimation that widespread price reduction might be in order, viewing the immense profit increases in recent years, with the Council's simultaneous espousal of more billions of dollars of tax concessions to corporations and to high-income investors on the ground that these are needed to provide adequate funds or incentives for the investment process.

4. SHORTCOMINGS OF COUNCIL'S REPORT IN TERMS OF THE TRUE NATURE OF THE UNEMPLOYMENT PROBLEM AS AFFECTED BY TECHNOLOGICAL TRENDS AND AUTOMATION

The Council understates the problem of the new technology and automation

The Council's emphasis upon expansion of aggregate demand, without paying sufficient attention to distributional problems or equilibrium analysis, is accompanied by its inadequate treatment of the policy implications of the new technology and automation.

To be sure, in the appendix A statement beginning on page 166, the Council discusses once again at great length the relative merits of the argument that the main explanation of excessive unemployment is to be found in the maladjustment of a substantial part of the labor force to the changing types of available jobs (the structural explanation), as against the argument that the main explanation of excessive unemployment is to be found in the deficiency of aggregate demand. I agree entirely with the Council that the structural problem in the sense just defined is being exaggerated, that this problem is relatively no greater now than at times when total unemployment was lower. I agree also that programs of training, education, removal of discrimination, and depressed area development are of relatively secondary significance though important, and that such programs will be more fruitful in an environment where jobs are much more plentiful.

Nonetheless, the Council seems to me excessively optimistic in its treatment of the onrushing threat of technology and automation, when it implies that these trends in the long run will create more jobs than they eliminate. In the first place, the unemployed do not want jobs in the long run; they need jobs now. In the second place, the onrushing technology and automation per se do not create more jobs; they eliminate jobs. Policy inventiveness is required to provide other jobs for those so eliminated, so that the advance of technology and automation becomes an asset rather than a Frankenstein. Certainly, the Council's treatment of this problem becomes almost incredibly bland when the statement is made (p. 94) that "historically, there is surely no evidence of any inability of demand to rise along with productive capacity, or of any permanent inadequacy of total job opportunities." If an evil which has grown chronically for 11 years, and which now shows no genuine signs of diminution in the years ahead, is not "permanent," what is permanent? As a matter of fact, this condition has usually been "permanent" in the American economy as long as we can remember, except during wartime.

The structure of demand, as distinguished from the structure of the labor force

The reason why the Council's whole approach to the problems generated by the new technology and automation falls short is that the Council does not distinguish between the problem of the structure of the labor force (in terms of its job adaptability) and the problem of the structure of demand, which is quite a different thing. No matter how adaptable the labor force may be, and no matter how much may be accomplished through training and education, efforts to solve the unemployment problem through increases in aggregate demand will be very disappointing, unless the structure of demand is reshaped, responsive to disparate trends in the new technology and automation and to disparate potentials for the expansion of various types of output depending upon varying trends in consumer tastes and needs and national needs at any given levels of incomes.

In other words, the general assumption by the Council that a given increase in spending will add a given number of jobs, without due attention to where the spending is directed, is very vulnerable. There was more spending for automobiles, and more automoblies produced and sold, in 1963 than in 1955. Yet in view of technological trends in that industry, the number of workers fell by several hundred thousand. There was more food produced and distributed in the United States in 1963 than in 1953 or 1943, but nonetheless the unique advance of productivity in agriculture has resulted in very large shrinkages in the farm labor force both absolute and relative to the total labor force. This means that there must be vast changes in the structure of demand, if unemployment is to be substantially reduced.

My studies of the structure of demand

This last point is so important that I am presenting a number of charts to fortify it. Chart 6 sets forth, for various basic sectors of the economy, the number of workers required to turn out a given level of output in 1962, compared with the number required to turn out the same amount of output in the base period 1947–49. Using an index of 100 to represent the base period, the number of workers required in 1962 was about 52 in agriculture, 62.5 in all manufacturing, and 47.5 in motor vehicles and other transportation equipment. Combining these varied technological trends with varying trends in ultimate demand, chart 7 shows the very substantial variations in employment opportunity trends among production workers, for the period 1947–63. Chart 8 makes the same showing with respect to total civilian employment trends.

And chart 9, projecting ahead, sets feasible goals for civilian employment in the various important sectors of the economy, starting with 1962 as the base year and looking forward to 1966 and 1970. These projections take into account the technological factor, the likely demand factors, and some of the great priorities of our national needs.

It thus does no good to talk about needed increases in aggregate demand, without devoting comprehensive analysis to the needed structure of this demand, whether we are thinking merely in terms of providing enough employment opportunity, or whether we are thinking also (as we should) of a pattern of production and utilization which will meet the real needs of our people.

Strangely, although the Council (pp. 99–104) cites some rather dramatic examples of the changes in the job mix in recent years, it omits any substantial analysis of the implications of these trends in future, as they bear upon the problem of the structure of demand. The main solution offered by the Council is an increase in aggregate demand, which neglects a large part of the problem for reasons stated above, plus training and educational programs which do not address themselves to the point that the jobs must first be created for which to train and educate people. And the Council's persistent reiteration of the need for the proposed tax cut as the main vehicle largely misses the whole problem, for reasons to be developed later on in this statement.

5. SHORTCOMINGS IN COUNCIL'S ANALYSIS OF THE MAGNITUDES OF THE PROBLEM

Errors in the Council's use of the 3.5-percent growth-rate figure

In addition to the foregoing inadequacies in analysis, the Council's work as a guide to policy has been hampered by its persistent reluctance to recognize the size of the task confronting the economy and the Nation. This has stemmed in part from the Council's persistent underestimates of the GNP growth rate required annually to absorb the annual increments in the labor force and in productivity, and thus to hold unemployment constant. Here is found the main reason why the Council's earlier estimates of how much unemployment would be reduced by a given rate of economic growth within a given period of time have gone wrong even relative to the rate of growth actually achieved within such timespan. It is also the reason why I believe that the Council is far too optimistic in its current estimate that the unemployment rate will be reduced to 5 percent by the end of 1964 if GNP in 1964 is 5 percent higher in real terms than in 1963. And it is the reason why, even if the Council adhered to the statutory mandate (which it does not) of defining the needed rate of economic growth as distinguished from making mere forecasts, these needed growth rates as so defined by the Council would tend to be much too low.

Thus, the Council (p. 37) persists in its earlier claim that, from mid-1955 to date, an average annual growth rate of 3½ percent in real terms has been needed to hold unemployment constant. It supports this claim by arguing that variations in unemployment trends since mid-1955 have correlated with deviations from this 3.5-percent GNP growth rate. This leads the Council to assume that any growth rate substantially above 3.5 percent would reduce unemployment. The main trouble with this assumption is that it does not take account of the fact that the growth rate in the labor force and in productivity under conditions of large economic slack is not a true reflection of the potential growth rate in the labor force and in productivity under the galvanizing effect of high utilization. Thus, if it be assumed that the economy were to start to grow at a substantially faster rate than 3.5 percent, but at a substantially lower growth rate than the 5 percent which I believe now needed merely to absorb the annual increments in our labor force and productivity potentials, the inadequately accelerated growth rate would translate into more effective utilization of the labor force per man employed, a faster growth in the labor force, and a higher rate of actual productivity gains, rather than translating itself into a substantial reduction of unemployment. The Council tacitly admits this thesis, which I have been reiterating for some years now, when it admits that a 3.8-percent growth rate in real output from 1962 to 1963 did not reduce unemployment because the gains in productivity and in the labor force "somewhat exceeded past trends" (p. 52).

The fact of the matter is that the persistent use by the Council of the 3.5-percent figure is close to the 40- or 50-year average, and is not at all responsive to pragmatic observation to the effect that at no time since World War I has reasonably full employment been maintained for any significant length of time with a GNP growth rate as low as 3.5 percent. This is rather conclusively demonstrated in the first sector of my chart 10.

The Council underestimates true productivity trends

The Council uses a table on page 97 of its report to argue that the evidence of recent acceleration in the rate of productivity growth is highly inconclusive. I submit that a glance at the table itself will persuade many that the Council is far too bearish on this point. Indeed, the implicit recognition by the Council in its discussion on page 97 of my distinction between the trends in actual productivity and the trends in the productivity potential reinforce my position.

Beyond this and more important, my chart 11 would seem to make it clear that there has been a distinct and powerful long-range trend toward accelerating productivity growth in the U.S. economy, except when this growth is repressed by conditions of large economic slack. In any event, looking at this chart and at the Council's table on page 97, both certainly seem to support my conclusion that an average annual growth rate of about 5 percent is now needed to absorb the annual increments in the labor force and in productivity when these are not artificially restrained by external unfavorable forces.

The Council does not stress sufficiently the high growth rate needed until we achieve full economic restoration

In a still more important sense, the Council's persistent references to the 3.5-percent growth-rate figure begs the real issue. For the issue confronting us is not at what rate the economy needs to grow to hold unemployment constant, but rather at what rate the economy needs to grow to restore maximum employment within an acceptable period of time, after 11 years during which we have failed to enjoy this condition in varying degrees.

The bottom sector of my chart 10 shows that the growth rate averaging well above 7 percent from the first quarter 1961 through second quarter 1962 was not sufficient to get us within hailing distance of maximum employment, and the same might be said of the growth rate of 7.8 percent from 1954 to 1955 as shown in the middle sector of the same chart. The truth is that, starting from now, we need an average annual growth rate of 8 to 9 percent for about 2 years, to get us back to maximum employment and production even by early 1966. I therefore submit that the Council should be stressing this in its analysis and developing policies accordingly, instead of speaking rather glowingly of the growth rate of 3.8 percent from 1962 to 1963 and the projected growth rate of 5 percent from 1963 to 1964.

Even if the 5-percent growth rate is in fact achieved from 1963 to 1964 (and this is problematical in view of proposed policies), the growth rate for the 2-year period 1962–64 will have averaged only about half of what was needed from the start of 1962 forward to restore maximum employment and production by the end of 1964. It is no surprise, under the circumstances, that the Council now does not hazard a guess as to when maximum employment and production will be restored, although it is under statutory mandate to set targets in these terms. Further, my own belief is that a 5-percent growth rate from 1963 to 1964 will not come close to reducing unemployment to 5 percent by the end of 1964, for reasons already stated.

The real size of the tasks ahead

I offer next for consideration by the committee my chart 12, which in the framework of my equilibrium model quantifies the needed goals for employment, GNP, and various components of GNP and national income, looking ahead to 1966 and 1970. These projections take into account not only the needed aggregates, but also the needed relationships. And, of course, the establishment of appropriate relationships are a precondition to the attainment of the aggregates. As I shall indicate later on, I see nothing in policies now in being or under consideration, designed to shape the actual relationships in terms of these equilibrium needs; the most powerful policies seem to be tending in the opposite direction.

6. THE COUNCIL IS TOO OPTIMISTIC ABOUT RECENT DEVELOPMENTS, AND ABOUT THE OUTLOOK FOR 1964 AND LATER YEARS

My proposition that the Council is burdened with excessive optimism is supported substantially by what I have already said, with respect to its underestimates of needed growth rates, and its excessive commitment to policies which leave much to be desired. Moreover, I am disturbed that the recent report of the Council is packaged in a way which does not bring home what I regard to be some of the most salient facts about our economic troubles.

We are not experiencing an unusually good recovery movement

First of all, the Council says (p. 48) that "the economic expansion in 1963 substantially outdistanced most expectations," and the Council may also be responsible for the statement in the President's Economic Report (p. 4) referring to "nearly 3 years of unbroken expansion since early 1961"—an expansion which, it is said, may soon be recordbreaking in its duration.

An exceptionally long "recovery movement" is of dubious merit, when it means simply that we have failed to recover satisfactorily for an unduly long period of time. Looking again at my chart 10, the second sector seems to indicate that one of the reasons why the current recovery movement has been exceptionally long is that it did not register as large an upturn during its first year as the two previous upturns, and converted rather quickly into a period of virtual stagnation. What has really been stretched out is the stagnation period. This is shown clearly by the bottom sector of the same chart, indicating a dwindling rate of economic growth, depicted in 12-month trends, from first quarter 1961 to second quarter 1963, only a slight improvement later on in 1963, and an average annual growth rate since fourth quarter 1961 to date only about half that needed for 2 years to restore maximum employment and production. Saying that the 100 billion increase in real GNP since early 1961 has been the biggest in peacetime history for that length of time is a little beside the point, because it does not take account of the size of GNP at the base point and therefore does not take account of the fact that the growth rate has been dismally disappointing.

The true amount of unemployment and the size of the GNP gap

The Council seriously understates the size of the unemployment problem, and in my view seriously understates the size of the GNP gap. My chart 13 shows that, while full-time unemployment averaged only 5.6 percent of the civilian labor force for 1963 as a whole, the true level of unemployment was 9.4 percent, taking into account the full-time equivalent of part-time unemployment and the concealed unemployment resulting from inadequate growth in the civilian labor force due to the scarcity of jobs. It also estimates that the production gap in 1963 was $76.5 billion, contrasted with the Council estimate of less than half that amount. My estimate of this gap is based upon estimates with respect to labor force and productivity potentials, and needed growth rates, much higher than those used by the Council, for reasons already stated. My chart 14 shows in the top sector the amount by which the true level of unemployment has exceeded the level consistent with full employment, and in the bottom sector shows trends in the duration of unemployment. And my chart 15 sets forth my estimates of what we have forfeited, during the past 11 years to date, in consequence of the chronic rise of idle manpower and plant plus the margin between the actual growth in the labor force and productivity and the potentials for growth under conditions of reasonably full utilization.

The Council's views on the economic outlook

The Council's discussion of the economic outlook, on pages 51–52, leaves me a little uncertain as to the basis for its temperate optimism. The Council states that neither residential construction nor automobile production, two of the main sources of strength in 1963, are likely to provide fresh impetus in 1964. The Council anticipates no substantial independent thrust from business investment. It points out that the conventional budget will be smaller than last year, and that, while Federal expenditures for goods and services will rise by about 2½ billion, comparing 1964 with 1963, this will be a smaller rise than during the past few years. Main reliance for the forecast of a 5-percent growth rate in GNP is therefore placed upon tax reduction; I shall state my reasons for not sharing this confidence when I come to discuss the tax proposal itself. Meanwhile, I should reiterate again that, even if the Council is correct in its prognostication of a 5-percent growth rate, this in my view would be just about enough to hold unemployment constant, and would be little better than half the growth rate required for 2 years beginning now if we are to restore maximum employment and production by early 1966.

I am even more in doubt about the Council's optimism with respect to later years. Part of the stimulus which the Council now ascribes to the tax reduction within 1964 is borrowed from earlier tax reduction intentions for the second year of the tax proposal. And while the massive tax reduction in 1964 may indeed provide some temporary stimulus to the economy, I am very fearful that its irresponsiveness to the problems of distribution and equilibrium, and to the problem of needed changes in the structure of demand, will make our tasks much harder in the years following 1964 than they would be if our policy efforts now were better adjusted to the hard realities.

7. DEFECTS IN THE TAX REDUCTION PROPOSAL

As already stated, the Council places preponderant reliance upon the pending tax cut proposal to restore and maintain maximum employment and production. I do not want to overstate my case, nor to belabor excessively points which I have made many times before this committee and elsewhere. But I believe that the pending tax bill, even in the form originally presented by the administration a year ago, and more so in the form now before the Senate, embodies the most serious and costly misdirection of national economic policy during the past generation if not longer. It may seem too late to protest a step which is almost certain to be taken in the near future. Yet there is still some possibility that the tax bill may be improved in some respects before final passage. And it is still essential, in my view, to stress the urgency of other measures to supplement the tax proposal insofar as it is deficient, and to counteract those portions of it which are affirmatively undesirable. In any event, to discuss the President's Economic Report and the Annual Report of the Council of Economic Advisers without reference to the tax proposal would be like putting on a production of "Hamlet" without the Prince of Denmark. I cannot refrain from adding that some of the arguments in support of the tax proposal seem to me more muddled than the unfortunate Prince at his worst.

The tax proposal would work against economic equilibrium

First of all, as shown by my chart 16, the pending tax proposal, in conjunction with the tax action taken in 1962, would allocate about $4.2 billion worth of tax concessions to corporations. In addition, the pending tax proposal would allocate about $3.6 billion of the total personal tax cut of about $8.9 billion, or about 40 percent, to taxpayers with incomes of $10,000 and over who constitute only about 12.5 percent of all taxpayers. My estimate is that about $2.5 billion of this $3.6 billion would be saved for investment purposes. Adding this to the $4.2 billion in corporate tax concessions, the 1962 action plus the present proposal would allocate about $6.7 billion to investment purposes. In contrast, the current tax proposal would allocate only about $6.4 billion to consumption purposes, including $1.1 billion of the personal tax cuts for the top income eighth of all taxpayers, and the $5.3 billion in personal tax cuts for the other seven-eighths of all taxpayers, practically all of which I assume would be spent for immediate consumption.

I submit that this distribution of the tax cut benefits cannot possibly be squared with any of the considerations of equilibrium analysis which I have already discussed. Viewing the operational aspects of the economy, neither corporations in general nor high income taxpayers in general need or deserve so large a share of the total tax concessions, and a greatly enlarged share should be devoted to the stimulation of immediate consumption.

It may be argued that I have overestimated the portion of the personal tax cuts going to the top income eighth of all taxpayers which would be saved for investment purposes rather than spent immediately for consumption. This may possibly be so. But if it were to be assumed that a larger portion of the personal tax cuts for the top income eighth were to be used for immediate consumption, then there is absolutely no reason in economic or social policy for enlarging the Federal deficit to elevate further the consumption levels of these people, especially at the expense of those lower down, especially at the expense of other national priorities subsequently to be discussed, and especially when we purport to be launching a massive and relentless attack upon poverty in the United States.

The tax proposal in its present form is inequitable, and socially undesirable

Second, the distributional deficiencies in the pending tax proposal are further illustrated by my chart 17, which estimates that the taxpayer with an income of $200,000 a year would receive a 16-percent increase in disposable income, and the $100,000 a year taxpayer an 8.3-percent increase, while the $3,000 income taxpayer would receive only a 2-percent increase, the $5,000 income taxpayer only a 1.6-percent increase, and the $7,500 income taxpayer only a 2.1-percent increase. This regressive redistribution of aftertax income cannot be defended on economic or social or equitable grounds. Moreover, data submitted to the Senate Finance Committee by the Treasury Department make it clear that my estimates of the taxes paid by very high income people are gross overestimates, since they are based upon the tax rate structure, and do not take account of the extensive avoidance of these tax rates by those in the very high income brackets. The Treasury data shows, among other things, that taxpayers with incomes of a million dollars a year pay an effective tax rate lower on the average than taxpayers with incomes of $50,000 a year.

It is argued that any massive tax reduction must yield the largest percentage increases in disposable income to those at the top of the income structure, because they are now paying the highest tax rates. The first answer to this spurious argument is that national economic policy should first take account of the needed changes in the distributional pattern of income on economic and social grounds, and if massive tax reduction is not suited to attainment of these objectives, then alternative methods of accomplishing them should manifestly be preferred. The second answer is that it is perfectly feasible to devise an alternative proposal for massive tax reduction which would place its incidence where it is needed both on economic and social grounds. When I come to my policy recommendations, I shall make such a proposal in detail.

The tax proposal provides too little stimulus to the economy

A third defect in the pending tax proposal is that it would provide only a small proportion of the stimulus which the economy needs. The President's Economic Report (pp. 7–8) estimates that, if the withholding rate is immediately reduced to 14 percent, individual income tax collections would be cut by $8.8 billion in 1964 and corporate tax liabilities cut by $1.5 billion in 1964, and that these cuts would have a multiplier effect upon GNP of somewhere between more than 3 and somewhat more than 4, thus adding somewhere between more than $30 billion and more than $40 billion to GNP in 1964. It further estimates that, when fully effective, the tax cut would lift GNP annually by $35 to $45 billion. I think that this is an extreme overestimate of the stimulative effects, because it does not take account of the very large part of the corporate tax cuts which would not be translated into investment in view of current amplitude of funds and current excess plant capacities, and because it does not take account of the large portion of the personal tax cuts for those in the high income brackets which for the same reasons would add to inactive savings rather than to immediate investment. My own estimates are that the full tax cut when operative would have a stimulative effect upon the economy of only about $30 billion in 1965 or 1966. This contrasts with my estimate that $107 billion represents the difference between my estimate of needed total national production in 1966, and my estimate of where total national production would then be if our national economic policies were to remain about in status quo—that is, if the tax program were not put into effect.

The tax cut fails to deal with needed changes in the structure of demand

The fourth and perhaps most serious defect in the proposed tax cut is that it fails completely to take account of the needed changes in the structure of demand which I have discussed in detail above. The increased spending resulting from the tax cut will be directed mainly toward increasing productive capacity for a wide range of conventional products, and toward increasing consumer spending largely for these same conventional products. But the very meaning of the new technology and automation is that increased spending in these areas will add relatively little to net employment opportunities, and in some respects will accentuate investment imbalances which will aggravate the unemployment problem in the long run.

The needed changes in the structure of demand require much more emphasis (as shown by my earlier portrayals of employment trends in the past and projections into the future) upon such programs as housing and urban renewal, mass transportation, and facilities and personnel related to education and health and other aspects of human improvement. Such programs require a much heavier emphasis upon increased public spending. Indeed, when one compares the net cut in the Federal budget for fiscal 1965 with the average annual rate of enlargement in the Federal budget during recent years, it appears that the sacrifice of public outlays in exchange for the tax cut will have as repressive an effect upon the economy as the tax cut will have a stimulatory effect. And this is quite apart from the fact that the spending stimulated by the tax cut will be much less useful to the people and the Nation in terms of end products than comparable increases in Federal spending would be.

8. THE COUNCIL'S AVOIDANCE OF THE CRUCIAL NEED FOR MORE FEDERAL PUBLIC SPENDING

In view of certain practical exigencies or political consideration with which the Council is confronted, I can well understand its failure to point out in its analysis the need for much more Federal public spending than is now being proposed. Be that as it may, I submit that an economic analysis which avoids this issue must answer to the charge of being essentially deficient and unrealistic.

The decline in Federal spending, relative to capabilities and needs

The basic reasons why we need much more public spending now have already been detailed. I therefore need only to call attention to the actual trends. The best way to do this, in my view, is to relate the trends in Federal spending to the size of our gross national product, this being the measure of our capabilities, and in an important sense also the measure of our economic needs because of the bearing of Federal spending upon the whole economy; and to relate the trends in Federal spending on a per capita basis to the growing needs of a growing population.

As my chart 18 shows, the proposed Federal budget for fiscal 1965 will come to 15.25 percent of estimated GNP for the same period, and $486.98 on a per capita basis, measured in 1962 dollars. This contrasts with 16.32 percent and $503.88 in fiscal 1964, and 18.66 percent and $544.36 in fiscal 1954. Much has been made of the intended shift from defense outlays to domestic programs. But taking all domestic programs into account, the fiscal 1965 budget comes to 5.71 percent of estimated GNP and $182.47 on a per capita basis. This contrasts with 6.01 percent and $185.67 in fiscal 1964.

Using the same frame of reference, my chart 18 also sets forth my estimates of needed Federal outlays in calendar 1966 and calendar 1970, developed as a segment of my equilibrium model for restoration and maintenance of maximum employment and production. A glance at my estimates for such programs as education, health services and research, public assistance, labor and manpower and other welfare services, and housing and community development, indicates the vast size of the shortfalls in proposed outlays in these areas as contained in the fiscal 1965 budget. Similarly in this connection, my chart 19 contrasts the dollar magnitudes of the proposed fiscal 1965 budget, by major types of outlays, with the needed levels in calendar 1966 and calendar 1970. Thus, the proposed budget of $97.9 billion for fiscal 1965 falls about $17 billion short of my estimate of the need for calendar 1966, or in the neighborhood of $9 billion short of my estimate of the need for fiscal 1965.

9. THE HOUSING PROBLEM AS AN ILLUSTRATION OF PROGRAMMATIC INADEQUACIES

Taking into account all of the considerations which I have already discussed in detail, including the matter of our national needs, and the needed changes in the structure of demand, a vast expansion of housing activity and of related urban renewal would be in my view the most important single step that we could take toward full economic restoration, and correlatively toward the reduction of poverty. My charts 20, 21, 22, and 23, which I will not discuss in detail, indicate the reasons for my conclusion that an adequate housing program would require during the years between now and 1970 an average annual volume of new low-rent and low-cost sales housing with public subsidy ranging from 400,000 to 500,000 units a year. This would be consistent both with my equilibrium model and with fair progress toward providing decent housing for the one-fifth of the Nation who now live in slums or their equivalent.

The administration has very recently proposed a new housing program which is imaginative and constructive in the variety of programs dealt with, and in some of its innovating features. But the magnitudes of this program seem to me very small, when compared with the economic and social needs, and with our capabilities to meet these needs. I am consequently disappointed in the reluctance of the Council to put forward an analysis of the role of housing in the immense tasks confronting us.

10. SHORTCOMINGS IN THE COUNCIL'S ANALYSIS OF MONETARY POLICY

The Council's analysis of monetary policy states (p. 43) that monetary and debt management policies influence plant and investment expenditures more than they influence purchases of consumer durables. Within the ambits of monetary policy during the past decade, I do not believe that experience supports this observation. The policy of tight money and rising interest rates during the recurrent investment booms, which have outrun demand for ultimate products, has had very little effect upon business investment which has been more than amply supplied with funds in any event, and has been severely repressive of consumer purchases and public outlays.

Based upon this questionable first proposition, the Council (p. 44) implies that a more liberal monetary policy and a slightly restrictive budget are desirable when the need is to expand investment relative to consumption (i.e., a generally inflationary situation), and that a tighter money policy and a more liberal budget policy are desirable when there is need to achieve a relatively more rapid expansion of consumption in view of excess plant capacity. It would seem more correct to state that, in the face of consumption pressure against available productive resources, both monetary policy and budgetary policy should be relatively tight to deal with a general inflationary situation, and that in the face of large excess capacity and deficient consumption—an economy with a deflationary basis—both monetary policy and fiscal policy should be more liberal. This indeed is implicitly recognized by the Council, when it attributes both the 1957 downturn and the 1960 downturn to an excessive tightening of both fiscal and monetary policy.

The labored attempt by the Council to justify monetary and fiscal policies which are in conflict rather than complementary is based upon its attitude toward the balance-of-payments and gold problem. Thus, the Council argues (p. 44) that the need to stimulate the domestic economy concurrently with balance-of-payment and gold difficulties calls for a restrictive lifting of short-term interest rates to dissuade the outflow of capital, and a long-term credit and interest rate policy favorable to domestic expansion, But in my view, our balance-of-payment and gold outflow difficulties stem more from the poor U.S. economic performance in contrast with that in Western Europe than from differential interest rates. In any event, it exhibits a complete lack of balance to adopt monetary policies which cost us infinitely more in terms of domestic economic losses than they could possibly gain us in terms of our international economic problems. There are entirely different solutions available for the latter, which I cannot discuss here.

Further, the Council's discussion of monetary policies in the current expansion (pp. 47–48) seems to imply, contrary to the weight of the evidence, that it is reasonably feasible to lift short-term interest rates without exerting an upward pressure upon long-term interest rates. Nor does the Council attempt to analyze whether the average annual growth in the money supply of only 2.8 percent during the current expansion can be reconciled with the needed amount of economic growth as distinguished from the seriously deficient rate of economic growth which has actually occurred. In terms of seeking to defend an existing policy rather than to analyze or justify it, the Council's whole discussion of monetary policy seems close to the weakest portion of its entire report.

11. SHORTCOMINGS IN THE COUNCIL'S ANALYSIS OF WAGE-PRICE POLICY

Price stability is not an end in itself

The Council's discussion of wage-price policy begins (p. 112) with identifying this problem with the inflationary problem. And throughout the discussion, the Council adheres to the emphasis that only the inflationary danger is involved in wage and price trends.

This touches only one very limited aspect of the wage-price problem. Inflation is undesirable, to be sure. But a stable price level is not an economic end in itself; it is merely a major factor in determining whether resources and incomes are being allocated in ways consistent with maintenance of economic equilibrium at maximum employment and production. And as we should have learned enduringly from the period preceding the great depression, a stable price level (except for falling farm prices) was entirely compatible with the lag in wages and other consumer incomes behind advances in productivity and investment which brought on the crash. Nowhere is this theme more clearly depicted than in the great book on this subject by the chairman of this committee.

When the Council states (also on p. 112) that, in terms of the balance among wages, prices, and profits, the economy is now in a good position to avoid inflationary price and wage decisions, it is undoubtedly correct. But this avoids the really crucial question, as to whether the economy has been moving or is now moving toward wage-price-profit relationships which will reverse the tendency toward overinvestment and excess plant capacity relative to consumption.

The serious lag in wage rates behind productivity gains

Some capable economists, even within the Government, have at long last come to take note of the persistent and damaging lag in real wage rate increases as a factor in consumption behind productivity gains. My chart 24 depicts this dangerous trend during the 5-year period ending with 1962, and it continued in 1963. My chart 25, in the context of my equilibrium model, estimates how large a part the deficient rate of growth in wages and salaries has played in the growing deficiency in total consumer income, which in turn has been basically responsible for the growing deficiency in total consumer outlays. And my chart 26 depicts how, during the current economic upturn, profits, and investment in some cases, have been far outrunning wages.

The Council's use of the wage and productivity data

In the tables set forth on pages 114 and 115 of its report, and the accompanying discussion, the Council attempts to compare trends in productivity with trends in wages and profits. The use of the data in these tables leaves much to be desired.

In the first place, as I have already indicated, the Council's argument that there is no conclusive evidence of an enduring acceleration in productivity gains seems insupportable. In any event, the recent and current rates of productivity gains do not square with the Council's analysis of needed economic growth rates. In addition, the table on page 114 is highly questionable, insofar as it introduces a moving 5-year average of productivity trends which tends to minimize the trend toward productivity gains.

In the second place, the Council compares productivity gains with trends in total compensation per employee man-hour. From the viewpoint of the relationship between output and consumer demand, the comparison should be between productivity gains and wage rate increases. Fringe benefits do represent a business cost, but whether these costs are tending to run too high should be measured against profit trends and investment needs. In this frame of reference, the very tables which the Council presents on pages 114 and 115 show the inordinate gains in corporate profits after taxes relative both to productivity and total compensation per employee man-hour, especially when account is taken of capital consumption allowances. And both tables are further defective, in that they show the trends in total compensation per employee man-hour in current dollars rather than adjusting them properly for price change; the proper comparison is between productivity trends and real compensation. To be sure, the current dollar trends in employee compensation do have a bearing upon the adequacy of profits; but the tables certainly reveal the profit trends recently have left their recipients with no cause for complaint.

Impracticality of the Council's wage-price guideposts

From this highly inadequate treatment of the wage-price-profit data, the Council proceeds to its so-called guideposts. Its suggested guidepost for wages (p. 118) is that, in a particular firm or industry, the annual percentage increases in total employee compensation per man-hour (not just in straight time hourly rates) should be related to the annual increase in national trend output per man-hour (which means the average percentage increase during the most recent 5 years).

I submit that this formula is filled with errors in practical terms. First of all, as already indicated, productivity should be related to hourly wage rates rather than to total compensation, and the use of the 5-year average would always understate desirable wage gains if the productivity trend was fairly constantly upward. Of far greater importance, it is fundamentally wrong to urge wage earners in industries where productivity advances are unusually high to limit their wage rate increases to any national average of productivity gains. For if this were to be done, it is manifest that, as the wage rate increases in the very low productivity and low profit industries would not come up to the national average of productivity gains, the national average of wage rate increases would fall very far behind the national average of productivity gains. Meanwhile, the profits which would result from such a formula in the high productivity industries would rise beyond all reason (as they actually have), and would contribute to the relatively excessive periodic investment booms in these very industries.

The Council's formula for relating specific wage rate gains to nationwide productivity trends might be desirable, if the resultant excessive profits were drained off by higher taxes, and if the proceeds of these tax collections were used to finance public programs for the less fortunately situated wage earners and for the reduction of poverty. But nobody is proposing this. Entirely to the contrary, the excessively profitable industries and firms, which already have benefited unduly from the long-term lag of wage rate increases behind productivity gains, are now to be enriched further with large additional tax bonanzas, even while the Council itself now intimates that their profit gains have been so fast that they ought to reduce their prices.

On the subject of prices, the Council suggests (pp. 118–119) that firms whose productivity gains exceed their increases in employee compensation should lower their prices, and that firms whose productivity gains fall behind their increases in employee compensation should raise their prices. It is an entirely unrealistic approach to the whole behavior pattern of American industry to expect either of these two price developments to take place to a significant extent, and the Council is certainly proposing no Government measures to encourage this process. It would thus seem that the Council's guideposts would help to enrich big business, ruin small business, and leave wage earners holding the bag.

Lamentably, the Council is throwing its whole persuasive weight, which is considerable, on the side of maintaining the basic imbalances in the private economy which by now stand forth with such unmistakable clarity.

12. THE COUNCIL'S DISCUSSION OF THE POVERTY PROBLEM

The Council's discussion of the poverty problem in chapter 2 of its report, beginning on page 55, is an admirable and sympathetic portrayal of the amount of poverty in America and the nature of its distribution among its main victims.

Unfortunately in my view, the Council does not sufficiently distinguish between a description of those who are poor and the reasons why they are poor. In other places, the Council properly recognizes that, even though most of those unemployed have lower capabilities or suffer from more discrimination than those who are employed (really a truism), nonetheless most of the excessive unemployment would be taken up in a full employment environment. Similarly but without Council recognition, while it is equally a truism that most of the poor are more vulnerable in one respect or another than those who are not poor, describing these vulnerabilities does not negate the fact that an adequate rate of economic growth and a full employment environment would resume the reduction of poverty at the high rate of reduction which maintained between 1949 and 1957. In short, treating the economy should take high priority over case processing of the poor.

To avoid any possible misinterpretation of the immediately preceding statement, I hasten to add that the very programs which would do most to promote full economic restoration would be addressed on a massive scale to deal directly with the problems of the poor. The same programs which would do most to lift the capabilities and living standards of the almost 80 million people in the United States who are either poor or deprived would do most to restore the economy, by enlarging the consumption capabilities of those who constitute the greatest underdeveloped market in the world for American goods and services.

The drawing of an artificial dichotomy between the problem of economic restoration and the social and human problems of poverty results both in the misdirection of programs aimed toward economic restoration and the inadequacy of programs directed against poverty and deprivation. Thus, we have the ironic circumstance that, even while the Council urges a larger share of national income for the poor (p. 61), the actual programs now in the offing would direct on an annual basis several billions of dollars toward wasteful tax reduction for the wrong people, even while only $300 to $500 million on an annual basis are being added to the "poverty package." The net effects of this combination, plus the prevalent monetary policy, the neglect of adequate expansionary programs particularly in such fields as social security benefits, and the reduced spending in the Federal budget, are regressive rather than progressive. This, in the long run if not immediately, must enlarge rather than reduce both the economic problem and the poverty problem—which are really one problem.

13. NEED FOR CLOSER ADHERENCE TO THE EMPLOYMENT ACT OF 1946

When I consider why economists so competent and well intentioned as the Council of Economic Advisers seem to fall so far short of adequate economic analysis and policy discussion, I become increasingly convinced that the main explanation is their failure to adhere to the specific intent of the Employment Act.

The Employment Act was not intended merely to initiate the annual practice of submitting reports based upon conventional analysis of business trends and conventional forecasts of the business outlook. The act calls instead for a comprehensive, integrated, and consistent set of goals for the economy—goals for maximum employment, production, and purchasing power. And manifestly, these goals cannot be set in terms of aggregates alone. They must contain meaningful breakdowns of the composition of employment, production, and purchasing power, designed to maintain economic equilibrium at maximum resource use, and to reflect the priorities of our national needs. Indeed, the development of a qualitative model, projecting such goals, is essential to the development of adequate and consistent economic policies and programs, instead of the random development of policies and programs which are "united" by the current reports under the Employment Act only in the sense of being stated in one document.

Yet in recent years, and notably in the most recent instance, the annual report of the Council does not set forth these goals. It is instead limited to a few hopeful forecasts with respect to employment and gross national production for the year ahead. Thus, the procedure under the Employment Act, instead of bringing unity and purposefulness into the evolution of national economic policies, is resulting merely in competent repetition of published undertakings by many other organizations both private and public.

The present Council of Economic Advisers, in the past, gave tangible informal evidence of its intent to carry forward the core mandate of the Employment Act of 1946. This year marks complete abandonment of that purpose, with damaging effects upon analysis and policy treatment, apparently in response to objections from outside the Government which do not have merit and should not be yielded to by the Government.

14. SPECIFIC POLICY RECOMMENDATIONS

My specific policy recommendations flow naturally from the foregoing analysis:

(1) The pending tax measure would better serve the joint purpose of full economic restoration and attention to the human problems of massive poverty, if it were substantially revised. The $2.2 billion in proposed corporate tax reduction, and about $2 billion of the proposed $3.6 billion personal income tax reduction for the top income eighth of all taxpayers, are under current curcumstances economically wasteful and socially undesirable. This somewhat more than $4 billion should be used instead to lift personal exemptions by the amount which would absorb this sum. Such action would provide immensely more stimulus to the economy, and would be far more desirable on social and equitable grounds.

(2) In terms of the economic and social tasks confronting the Nation now and for the years ahead, any trend toward reduction in total spending under the Federal budget is highly undesirable, regardless of shifts in the composition of the budget. For balanced economic development as intended under the Employment Act, the Federal budget for fiscal 1965 should be in the neighborhood of $107 billion, or about $9 billion higher than the proposed budget. It goes without saying that, insofar as it is safe and feasible to do so—and only to that extent—national defense outlays which are of relatively low or negligible ultimate economic and social utility should be reduced, and the sums thus saved used for the vitally needed expansion of domestic public programs.

(3) Even with the foregoing, other measures involving Federal legislation are essential to achieve enough expansion of private consumption and improvement of private living standards, especially among the poor and deprived. The most important of these are very large expansion of social security benefits, especially old-age insurance payments, and the improvement of minimum wage legislation with respect both to coverage and amounts.

(4) In the absence of satisfactory evidence that measures adequate to restore maximum employment within a reasonably short time are in the offing, the reduction of the workweek to 35 hours is far more desirable than tolerance of high and chronically rising unemployment.

(5) The policy of tight money and rising interest rates is highly inimical to economic growth, socially unjust in its impact upon low income people and upon the public programs which serve them, and a frail and misguided weapon in treating the balance-of-payments and gold problem. Whatever pressures need to be exercised by the President and by the Congress toward a reversal of the tight money and high interest rate policy should be brought to bear without delay.

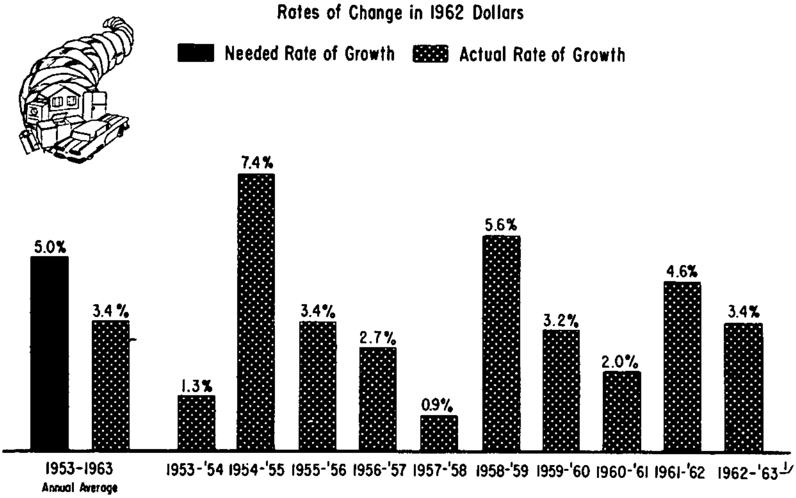
(6) The Council's wage-price guideposts are impractical of attainment, and if attained would exacerbate the serious lag in wage rate increases behind productivity gains. The Council at this stage in its

analysis ought to abandon its preoccupation with inflationary dangers, and turn rather to the private as well as the public aspects of adequately stimulative measures.

(7) While the meaning of the Employment Act of 1946 in its current form is abundantly clear, it may well be desirable to enact legislation specifically reaffirming the intent of the Congress that the Council of Economic Advisers prepare systematic, integrated, and consistent short- and long-run goals for employment, production, and purchasing power, subdivided into meaningful components. These should be used as perspectives for the development of the Council's economic policy advice to the President and through him to the Congress. Without this, the high potentials of the Employment Act cannot be achieved, even within the limitations of imperfections in economic knowledge and human judgment.

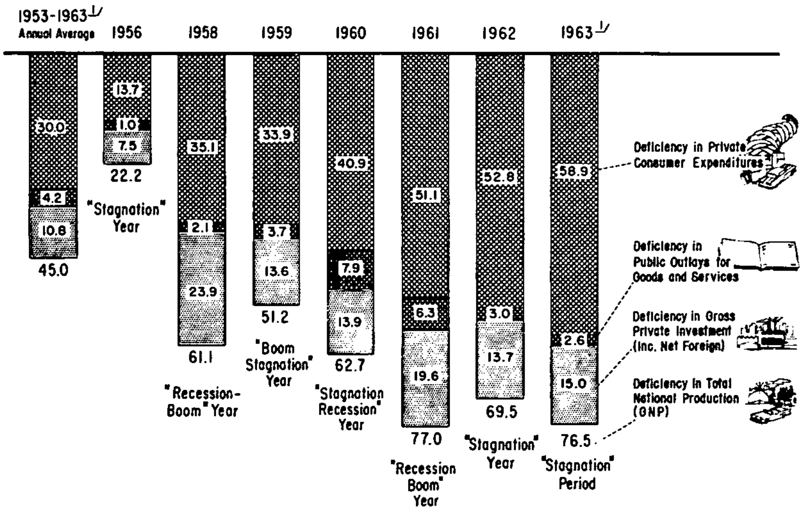
DEFICIENT RATE OF GROWTH IN PRIVATE CONSUMER SPENDING, 1953 - 1963[1]

Rates of Change in 1962 Dollars



THE PRIVATE CONSUMPTION DEFICITS DOMINATE THE DEFICITS IN THE TOTAL ECONOMY

Billions of 1962 Dollars



[1] 1963 estimated on basis of first three quarters.

CHART 1

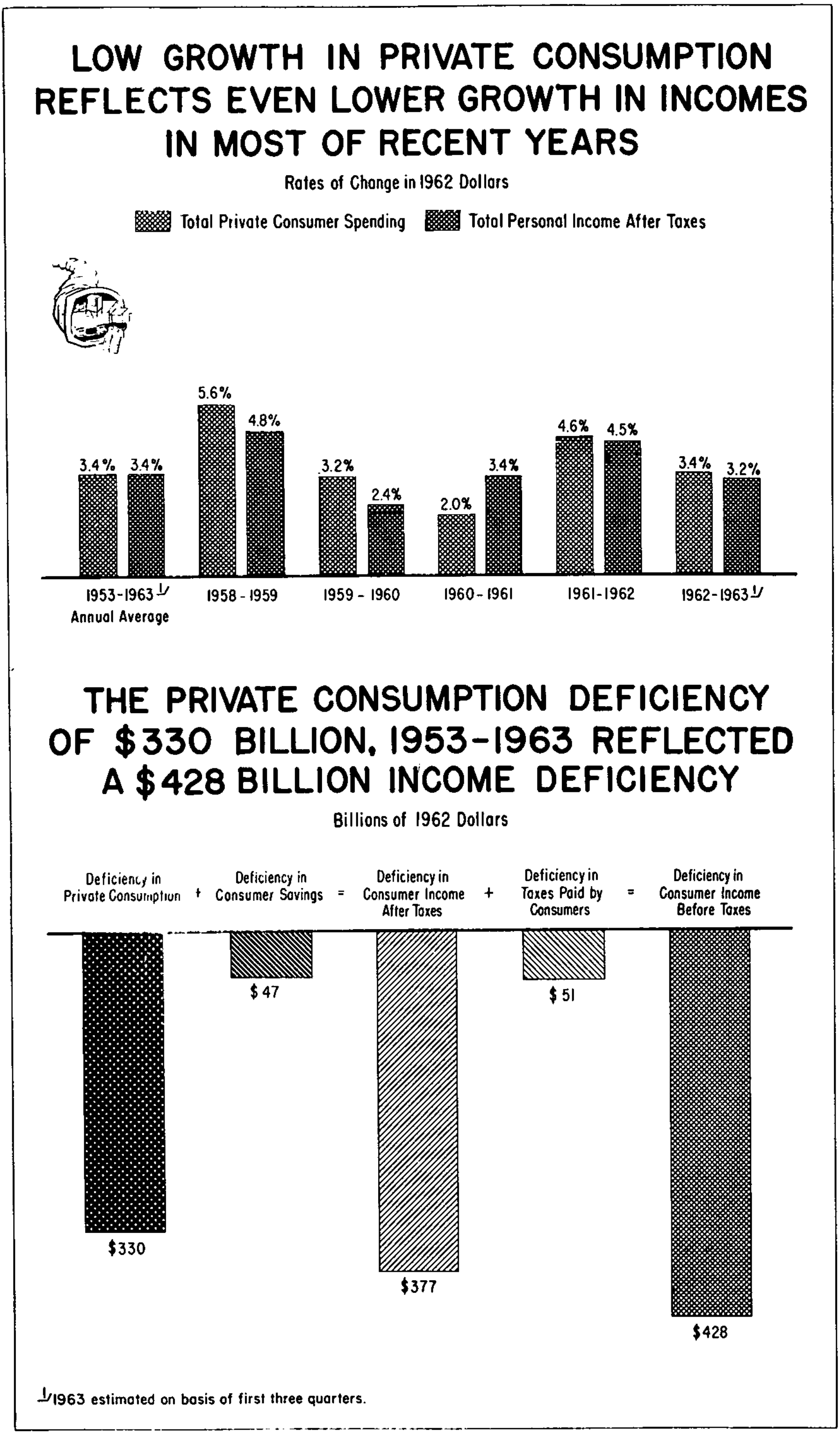
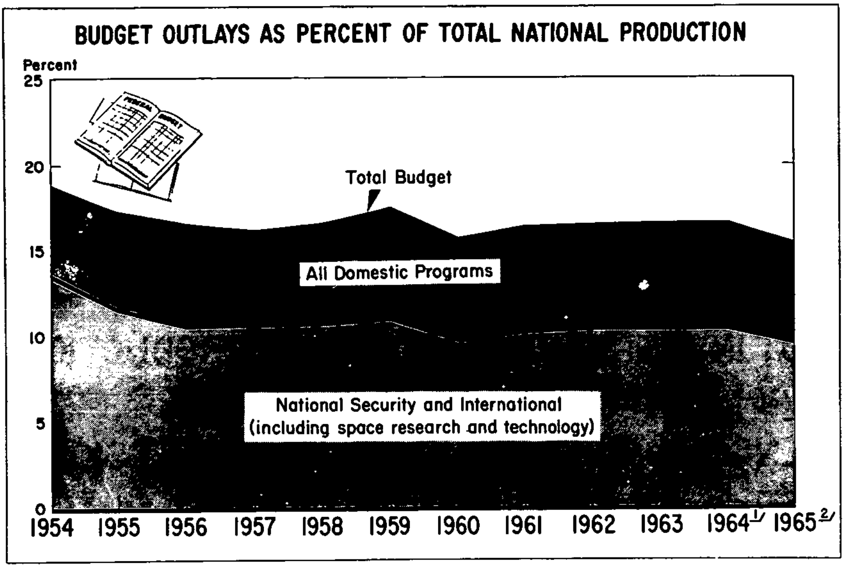
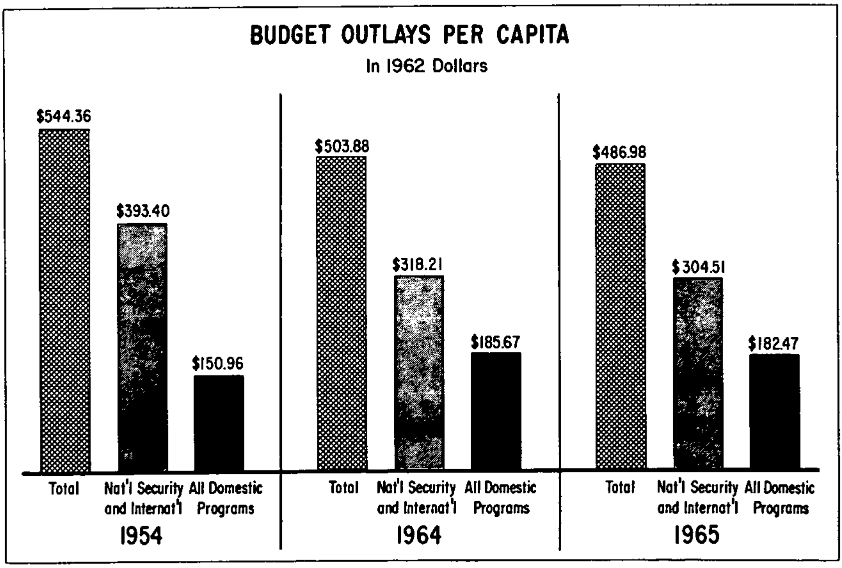

LOW GROWTH IN PRIVATE CONSUMPTION REFLECTS EVEN LOWER GROWTH IN INCOMES IN MOST OF RECENT YEARS
Rates of Change in 1962 Dollars
Total Private Consumer Spending
Total Personal Income After Taxes
3.4% 3.4%
5.6% 4.8%
3.2% 2.4%
2.0% 3.4%
4.6% 4.5%
3.4% 3.2%
1953-1963 1/ Annual Average
1958-1959
1959-1960
1960-1961
1961-1962
1962-1963 1/
THE PRIVATE CONSUMPTION DEFICIENCY OF $330 BILLION, 1953-1963 REFLECTED A $428 BILLION INCOME DEFICIENCY
Billions of 1962 Dollars
Deficiency in Private Consumption
+
Deficiency in Consumer Savings
=
Deficiency in Consumer Income After Taxes
+
Deficiency in Taxes Paid by Consumers
=
Deficiency in Consumer Income Before Taxes
$330
$47
$377
$51
$428
1/ 1963 estimated on basis of first three quarters.

CHART 2

FEDERAL BUDGET HAS SHRUNK RELATIVE TO SIZE OF ECONOMY AND NEEDS, 1954–'65

Fiscal Years





[1] Preliminary G.N.P. estimated at $603 billion, CEP.
[2] Administration's proposed Budget as of Jan. 21, 1964, G.N.P. estimated at $642 billion, CEP.

CHART 3

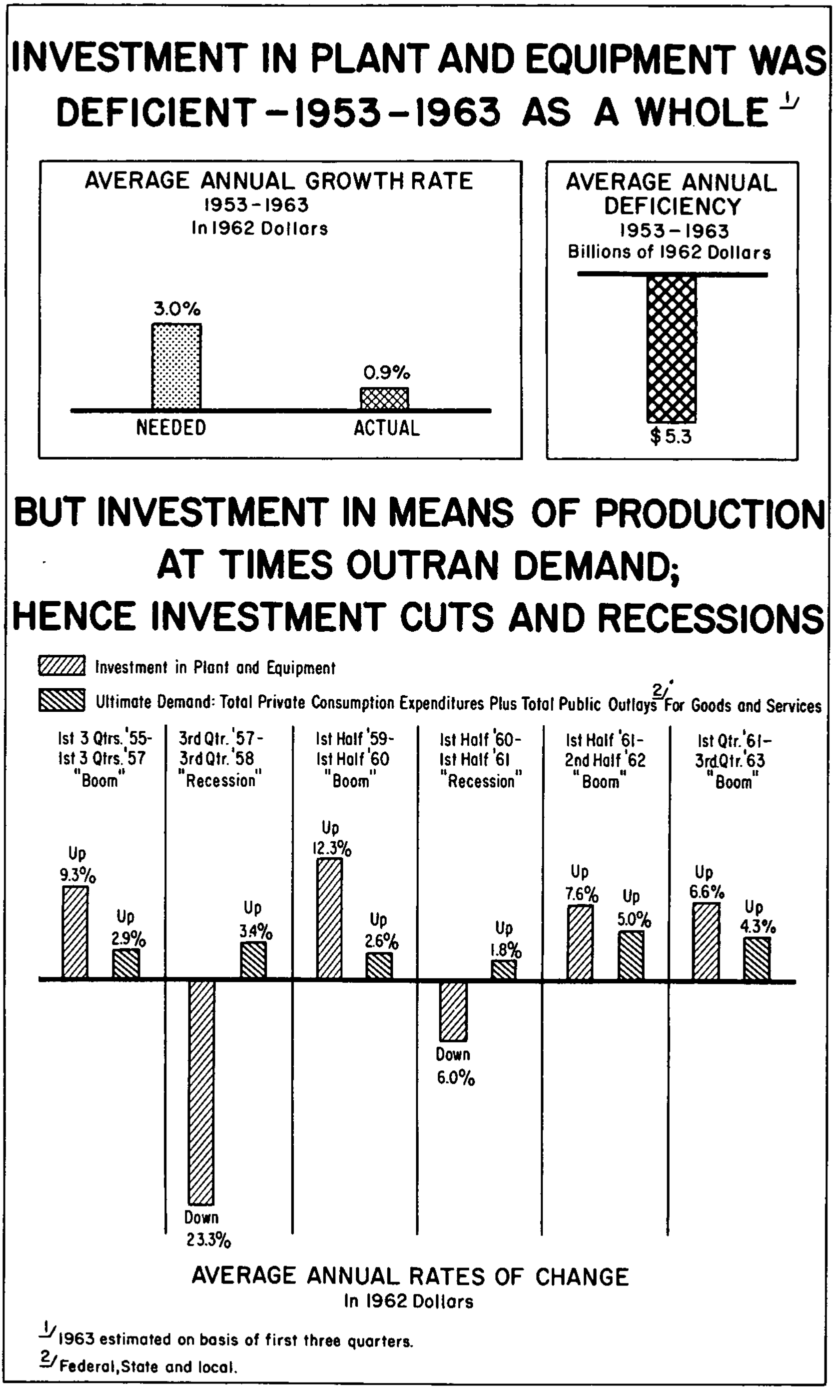
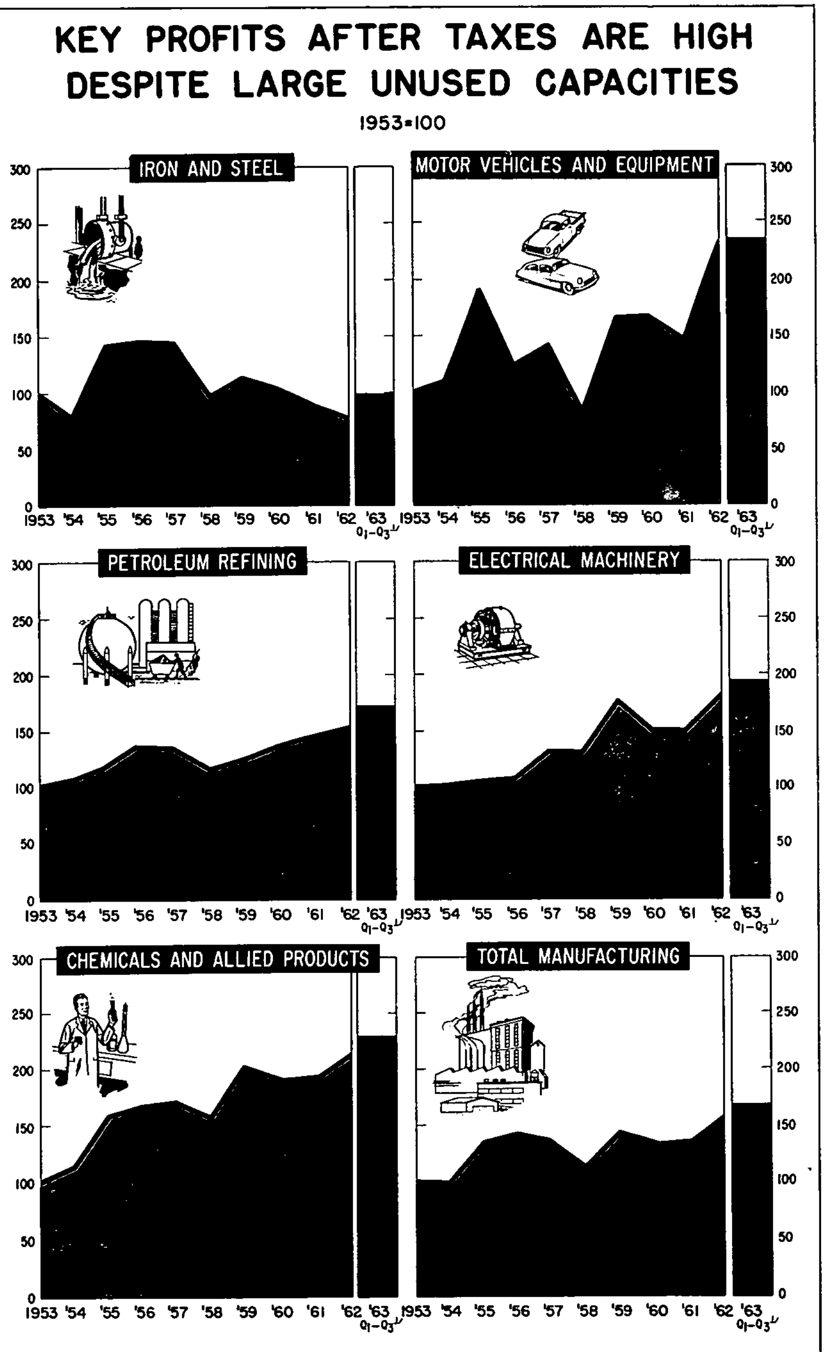

INVESTMENT IN PLANT AND EQUIPMENT WAS DEFICIENT – 1953 – 1963 AS A WHOLE [1]
AVERAGE ANNUAL GROWTH RATE
1953 - 1963
In 1962 Dollars
3.0%
0.9%
NEEDED
ACTUAL
AVERAGE ANNUAL DEFICIENCY
1953 – 1963
Billions of 1962 Dollars
$5.3
BUT INVESTMENT IN MEANS OF PRODUCTION AT TIMES OUTRAN DEMAND; HENCE INVESTMENT CUTS AND RECESSIONS
Investment in Plant and Equipment
Ultimate Demand: Total Private Consumption Expenditures Plus Total Public Outlays [2] For Goods and Services
1st 3 Qtrs. '55- 1st 3 Qtrs. '57 "Boom"
Up 9.3%
Up 2.9%
3rd Qtr. '57 - 3rd Qtr. '58 "Recession"
Down 23.3%
Up 3.4%
1st Half '59- 1st Half '60 "Boom"
Up 12.3%
Up 2.6%
1st Half '60- 1st Half '61 "Recession"
Down 6.0%
Up 1.8%
1st Half '61- 2nd Half '62 "Boom"
Up 7.6%
Up 5.0%
1st Qtr. '61- 3rd Qtr. '63 "Boom"
Up 6.6%
Up 4.3%
AVERAGE ANNUAL RATES OF CHANGE
In 1962 Dollars
1/ 1963 estimated on basis of first three quarters.
2/ Federal, State and local.

CHART 4



1/ First three quarters of 1963 at an annual rate, not seasonally adjusted.
Data: Federal Trade Commission—Securities Exchange Commission.

CHART 5

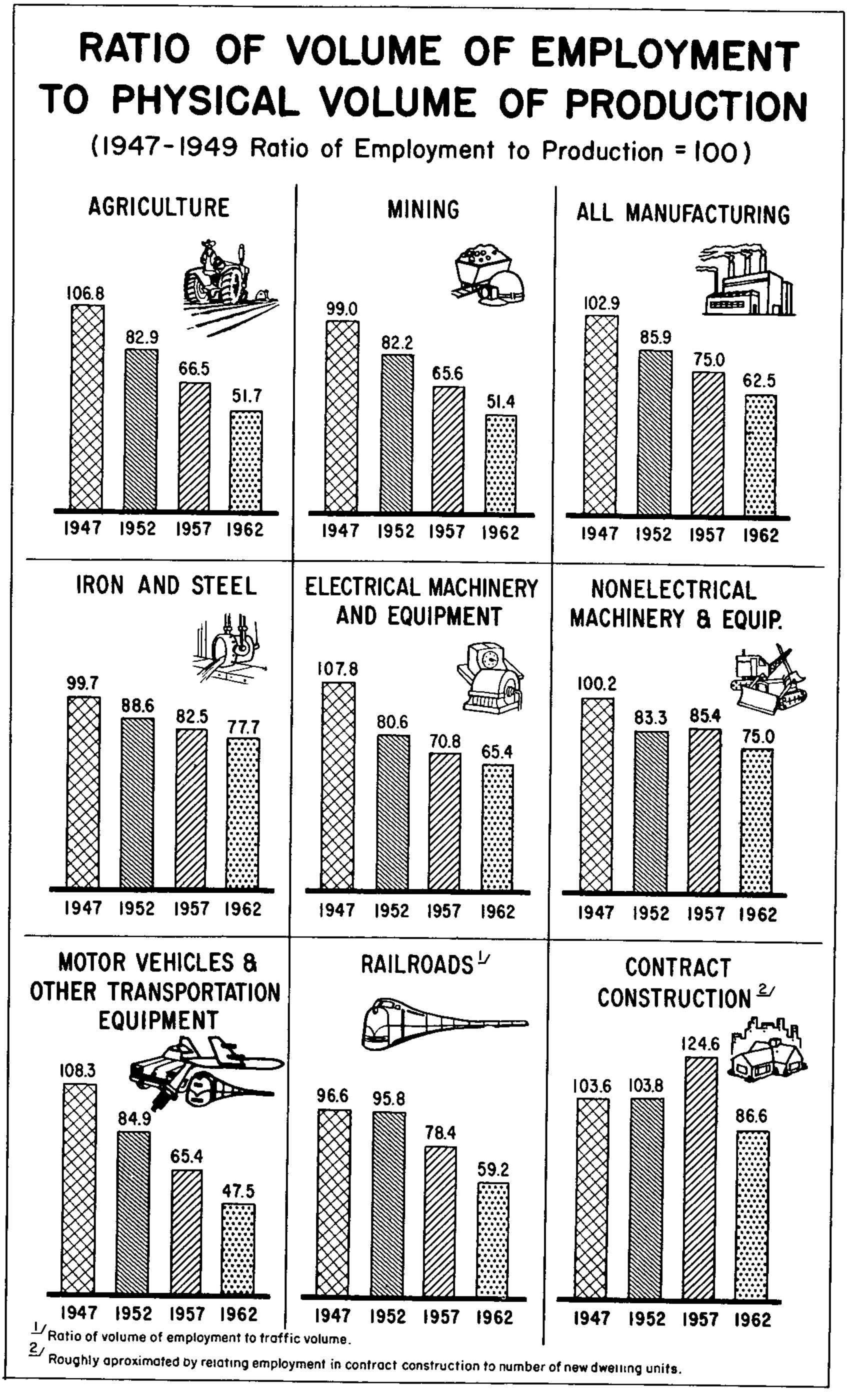

RATIO OF VOLUME OF EMPLOYMENT TO PHYSICAL VOLUME OF PRODUCTION
(1947-1949 Ratio of Employment to Production = 100)
AGRICULTURE
106.8 82.9 66.5 51.7
1947 1952 1957 1962
MINING
99.0 82.2 65.6 51.4
1947 1952 1957 1962
ALL MANUFACTURING
102.9 85.9 75.0 62.5
1947 1952 1957 1962
IRON AND STEEL
99.7 88.6 82.5 77.7
1947 1952 1957 1962
ELECTRICAL MACHINERY AND EQUIPMENT
107.8 80.6 70.8 65.4
1947 1952 1957 1962
NONELECTRICAL MACHINERY & EQUIP.
100.2 83.3 85.4 75.0
1947 1952 1957 1962
MOTOR VEHICLES & OTHER TRANSPORTATION EQUIPMENT
108.3 84.9 65.4 47.5
1947 1952 1957 1962
RAILROADS 1/
96.6 95.8 78.4 59.2
1947 1952 1957 1962
CONTRACT CONSTRUCTION 2/
103.6 103.8 124.6 86.6
1947 1952 1957 1962
1/ Ratio of volume of employment to traffic volume.
2/ Roughly aproximated by relating employment in contract construction to number of new dwelling units.

CHART 6

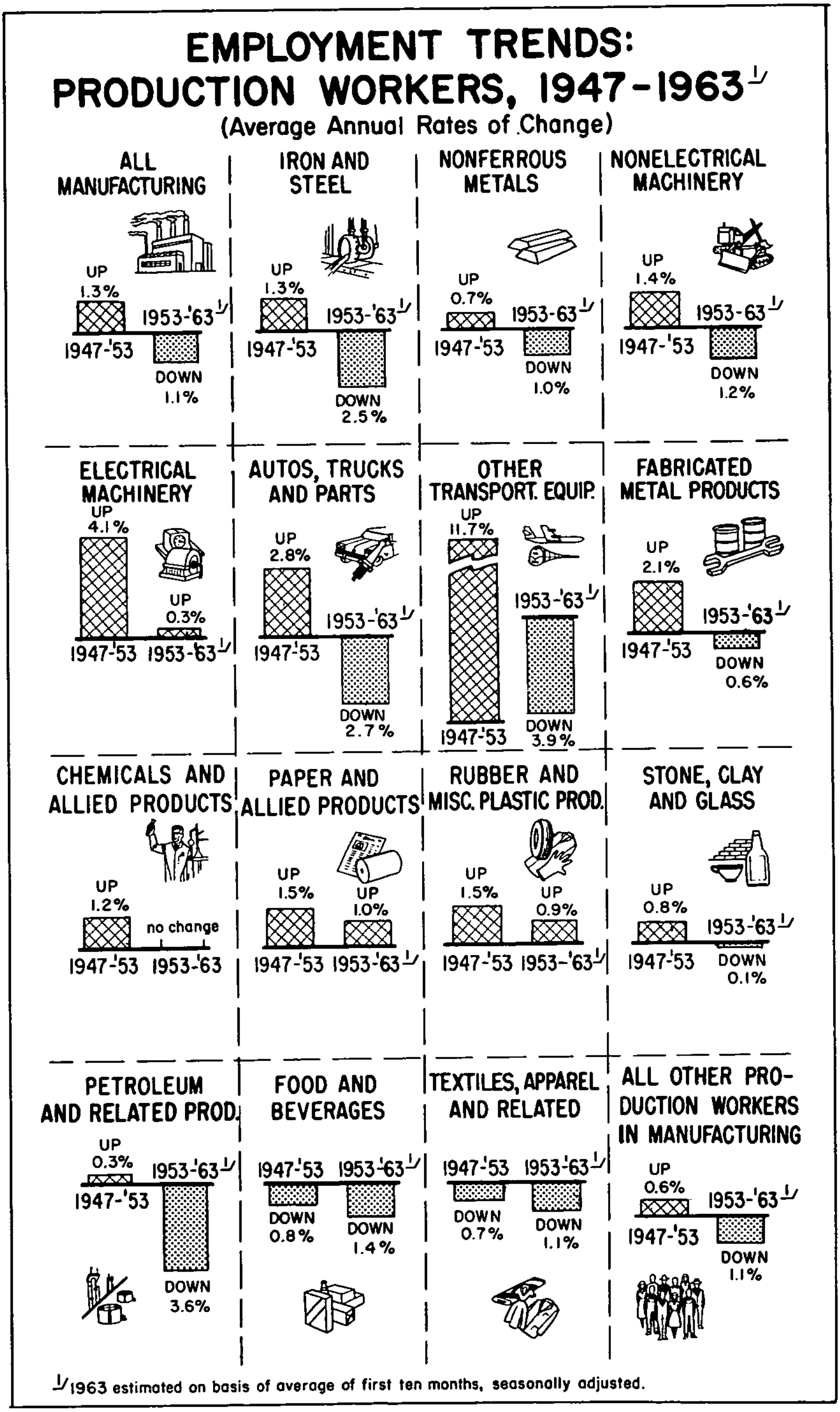

EMPLOYMENT TRENDS:
PRODUCTION WORKERS, 1947-1963 1/
(Average Annual Rates of Change)
ALL MANUFACTURING
UP 1.3%
1947-'53
1953-'63 1/
DOWN 1.1%
IRON AND STEEL
UP 1.3%
1947-'53
1953-'63 1/
DOWN 2.5%
NONFERROUS METALS
UP 0.7%
1947-'53
1953-63 1/
DOWN 1.0%
NONELECTRICAL MACHINERY
UP 1.4%
1947-'53
1953-63 1/
DOWN 1.2%
ELECTRICAL MACHINERY
UP 4.1%
UP 0.3%
1947-'53
1953-'63 1/
AUTOS, TRUCKS AND PARTS
UP 2.8%
1947-'53
1953-'63 1/
DOWN 2.7%
OTHER TRANSPORT. EQUIP.
UP 11.7%
1947-'53
1953-'63 1/
DOWN 3.9%
FABRICATED METAL PRODUCTS
UP 2.1%
1947-'53
1953-'63 1/
DOWN 0.6%
CHEMICALS AND ALLIED PRODUCTS
UP 1.2%
no change
1947-'53
1953-'63
PAPER AND ALLIED PRODUCTS
UP 1.5%
UP 1.0%
1947-'53
1953-'63 1/
RUBBER AND MISC. PLASTIC PROD.
UP 1.5%
UP 0.9%
1947-'53
1953-'63 1/
STONE, CLAY AND GLASS
UP 0.8%
1947-'53
1953-'63 1/
DOWN 0.1%
PETROLEUM AND RELATED PROD.
UP 0.3%
1947-'53
1953-'63 1/
DOWN 3.6%
FOOD AND BEVERAGES
1947-'53
1953-'63 1/
DOWN 0.8%
DOWN 1.4%
TEXTILES, APPAREL AND RELATED
1947-'53
1953-'63 1/
DOWN 0.7%
DOWN 1.1%
ALL OTHER PRODUCTION WORKERS IN MANUFACTURING
UP 0.6%
1947-'53
1953-'63 1/
DOWN 1.1%
1/ 1963 estimated on basis of average of first ten months, seasonally adjusted.

CHART 7

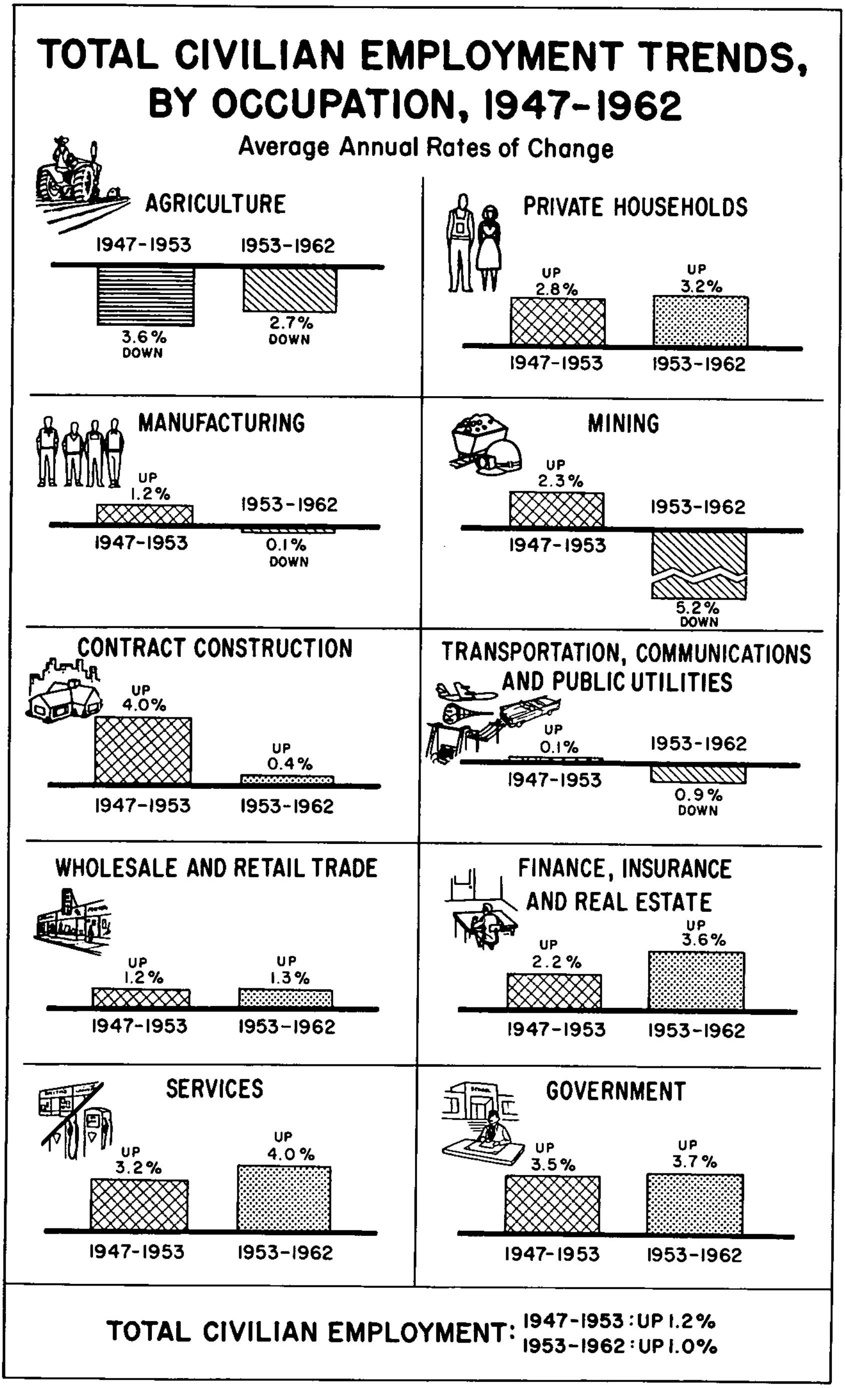
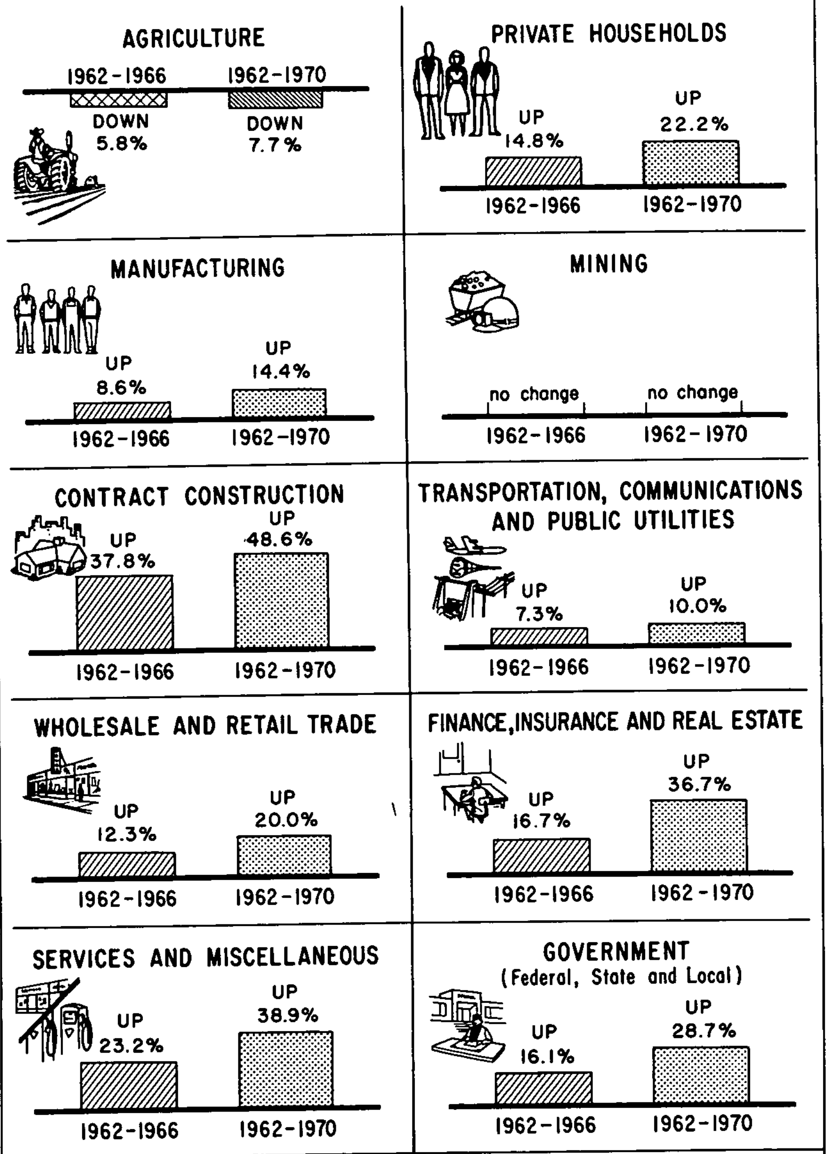

TOTAL CIVILIAN EMPLOYMENT TRENDS, BY OCCUPATION, 1947-1962
Average Annual Rates of Change
AGRICULTURE
1947-1953
3.6% DOWN
1953-1962
2.7% DOWN
PRIVATE HOUSEHOLDS
UP 2.8%
1947-1953
UP 3.2%
1953-1962
MANUFACTURING
UP 1.2%
1947-1953
1953-1962
0.1% DOWN
MINING
UP 2.3%
1947-1953
1953-1962
5.2% DOWN
CONTRACT CONSTRUCTION
UP 4.0%
1947-1953
UP 0.4%
1953-1962
TRANSPORTATION, COMMUNICATIONS AND PUBLIC UTILITIES
UP 0.1%
1947-1953
1953-1962
0.9% DOWN
WHOLESALE AND RETAIL TRADE
UP 1.2%
1947-1953
UP 1.3%
1953-1962
FINANCE, INSURANCE AND REAL ESTATE
UP 2.2%
1947-1953
UP 3.6%
1953-1962
SERVICES
UP 3.2%
1947-1953
UP 4.0%
1953-1962
GOVERNMENT
UP 3.5%
1947-1953
UP 3.7%
1953-1962
TOTAL CIVILIAN EMPLOYMENT: 1947-1953 : UP 1.2%
1953-1962 : UP 1.0%

CHART 8

GOALS FOR TOTAL CIVILIAN EMPLOYMENT, BY OCCUPATION, 1962-1966 AND 1962-1970



TOTAL CIVILIAN EMPLOYMENT: 1962-1966: UP 13.4%
1962-1970: UP 22.0%

CHART 9

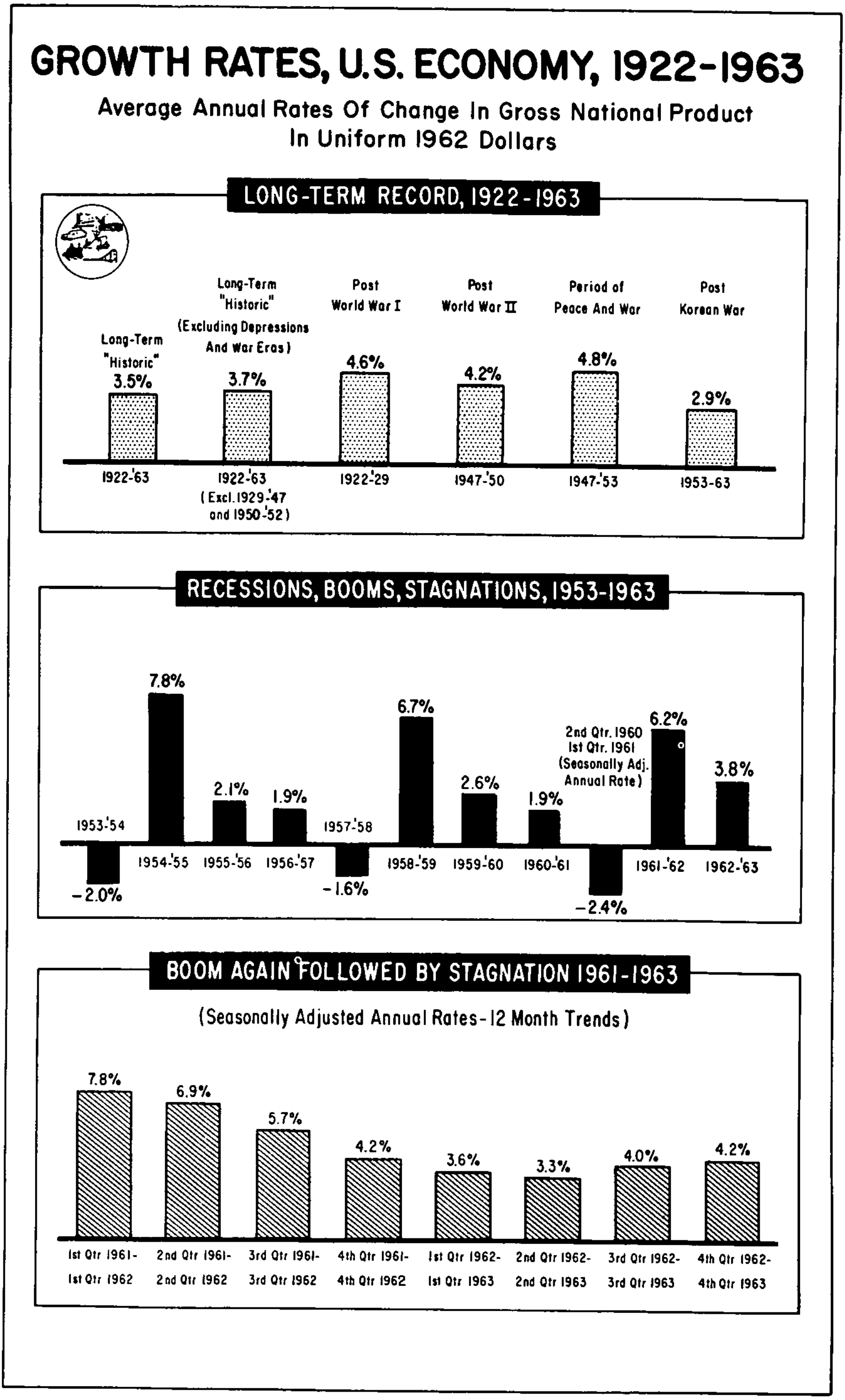
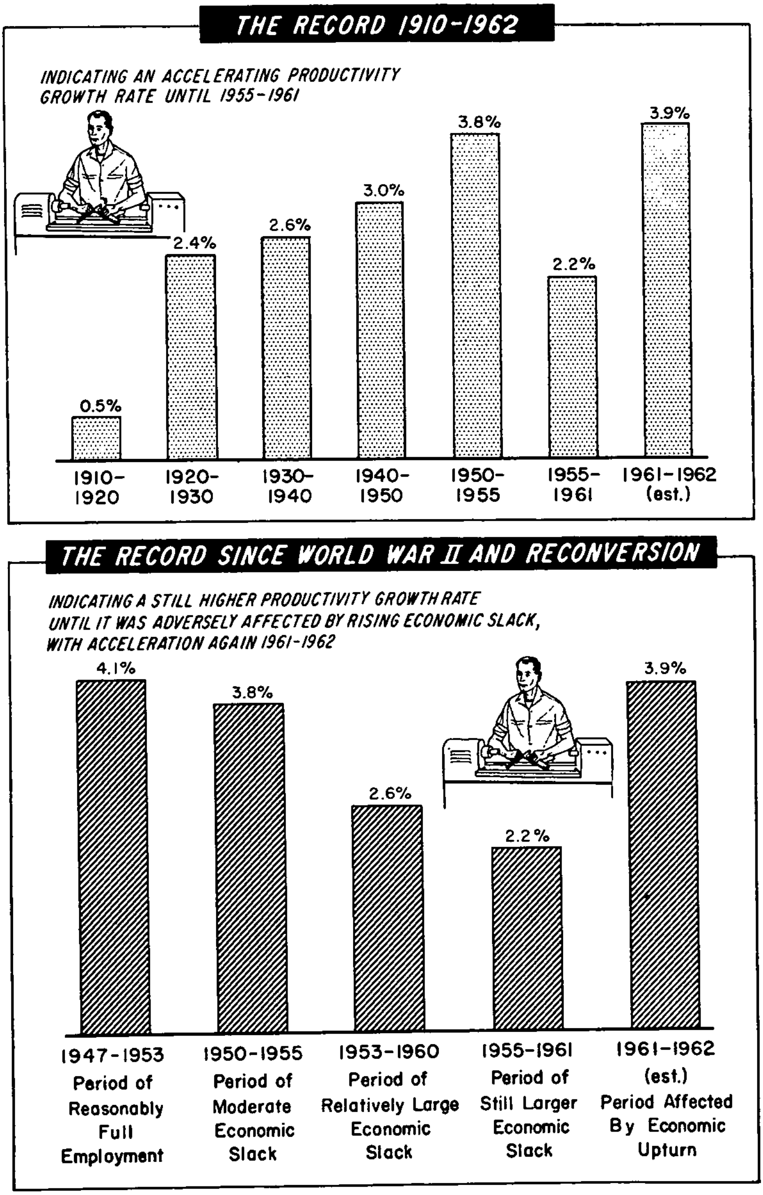

GROWTH RATES, U.S. ECONOMY, 1922-1963
Average Annual Rates Of Change In Gross National Product
In Uniform 1962 Dollars
LONG-TERM RECORD, 1922-1963
Long-Term "Historic" 3.5% 1922-'63
Long-Term "Historic" (Excluding Depressions And War Eras) 3.7% 1922-'63 (Excl. 1929-'47 and 1950-'52)
Post World War I 4.6% 1922-'29
Post World War II 4.2% 1947-'50
Period of Peace And War 4.8% 1947-'53
Post Korean War 2.9% 1953-63
RECESSIONS, BOOMS, STAGNATIONS, 1953-1963
1953-'54 -2.0%
1954-'55 7.8%
1955-'56 2.1%
1956-'57 1.9%
1957-'58 -1.6%
1958-'59 6.7%
1959-'60 2.6%
1960-'61 1.9%
2nd Qtr. 1960 1st Qtr. 1961 (Seasonally Adj. Annual Rate) -2.4%
1961-'62 6.2%
1962-'63 3.8%
BOOM AGAIN FOLLOWED BY STAGNATION 1961-1963
(Seasonally Adjusted Annual Rates-12 Month Trends)
1st Qtr 1961- 1st Qtr 1962 7.8%
2nd Qtr 1961- 2nd Qtr 1962 6.9%
3rd Qtr 1961- 3rd Qtr 1962 5.7%
4th Qtr 1961- 4th Qtr 1962 4.2%
1st Qtr 1962- 1st Qtr 1963 3.6%
2nd Qtr 1962- 2nd Qtr 1963 3.3%
3rd Qtr 1962- 3rd Qtr 1963 4.0%
4th Qtr 1962- 4th Qtr 1963 4.2%

CHART 10

TRENDS IN PRODUCTIVITY FOR THE ENTIRE PRIVATE ECONOMY—1910–1962

Average Annual Rate of Growth in Output per Man-hour for the Entire Private Economy



Note: Based on U.S. Department of Labor estimates relating to man-hours worked, based on labor force data.

Chart 11

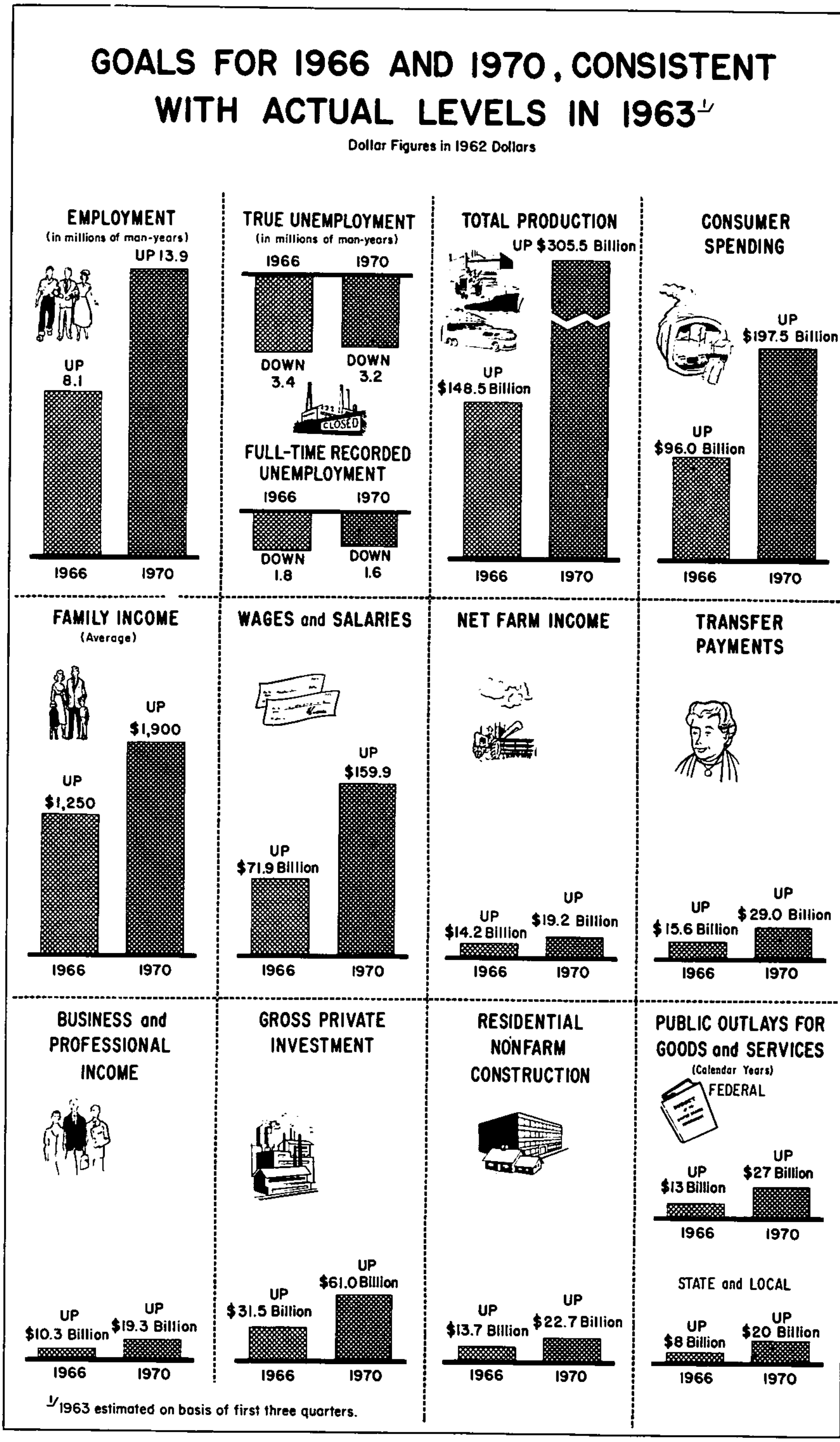
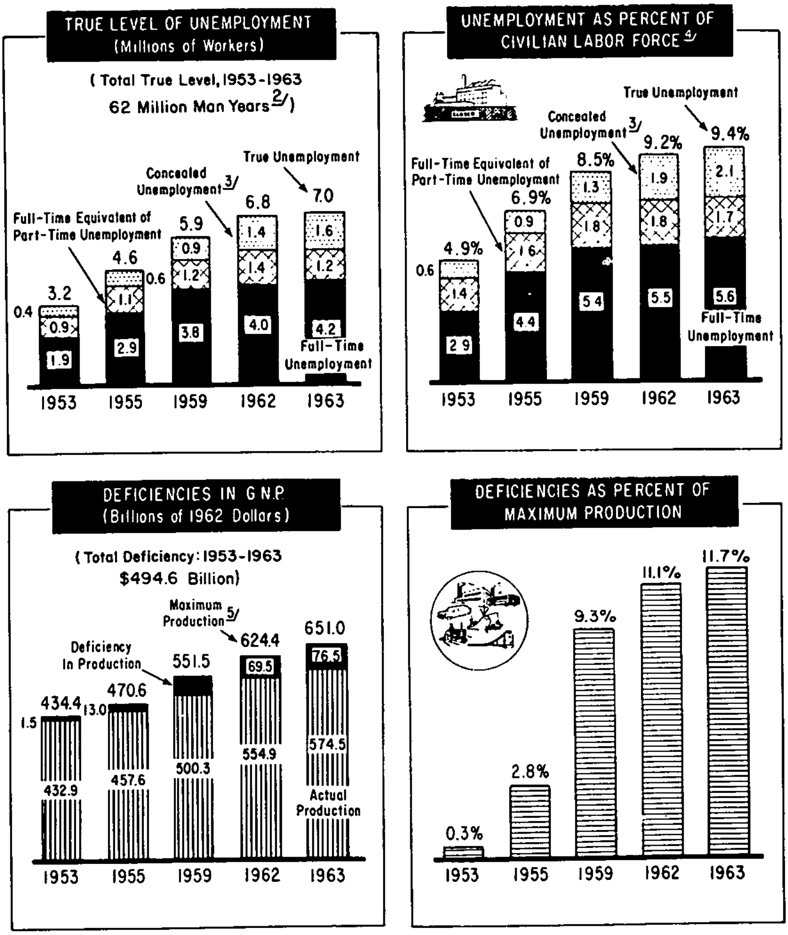

GOALS FOR 1966 AND 1970, CONSISTENT WITH ACTUAL LEVELS IN 1963[1/]
Dollar Figures in 1962 Dollars
EMPLOYMENT
(in millions of man-years)
UP 8.1
UP 13.9
1966
1970
TRUE UNEMPLOYMENT
(in millions of man-years)
1966
1970
DOWN 3.4
DOWN 3.2
CLOSED
FULL-TIME RECORDED UNEMPLOYMENT
1966
1970
DOWN 1.8
DOWN 1.6
TOTAL PRODUCTION
UP $148.5 Billion
UP $305.5 Billion
1966
1970
CONSUMER SPENDING
UP $96.0 Billion
UP $197.5 Billion
1966
1970
FAMILY INCOME
(Average)
UP $1,250
UP $1,900
1966
1970
WAGES and SALARIES
UP $71.9 Billion
UP $159.9
1966
1970
NET FARM INCOME
UP $14.2 Billion
UP $19.2 Billion
1966
1970
TRANSFER PAYMENTS
UP $15.6 Billion
UP $29.0 Billion
1966
1970
BUSINESS and PROFESSIONAL INCOME
UP $10.3 Billion
UP $19.3 Billion
1966
1970
GROSS PRIVATE INVESTMENT
UP $31.5 Billion
UP $61.0 Billion
1966
1970
RESIDENTIAL NONFARM CONSTRUCTION
UP $13.7 Billion
UP $22.7 Billion
1966
1970
PUBLIC OUTLAYS FOR GOODS and SERVICES
(Calendar Years)
FEDERAL
UP $13 Billion
UP $27 Billion
1966
1970
STATE and LOCAL
UP $8 Billion
UP $20 Billion
1966
1970
1/ 1963 estimated on basis of first three quarters.

CHART 12

CHRONIC RISE OF UNEMPLOYMENT AND OF IDLE PLANT, 1953-1963 1/



1/ Except for the base year 1953, no year during which a recession was in process is included.

2/ About 33 million man-years of unemployment (true level) would have been consistent with maximum employment.

3/ Estimated as the difference between the officially reported civilian labor force and its likely size under conditions of maximum employment.

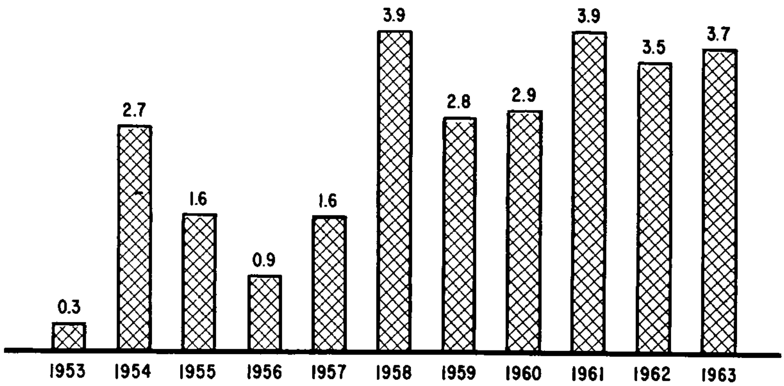
4/ In deriving these percentages, the civilian labor force is estimated as the officially reported civilian labor force plus concealed unemployment.

5/ Based upon sufficient annual rate of growth in G.N.P. to provide full use of growth in labor force, plant and productivity under conditions of maximum employment and production.

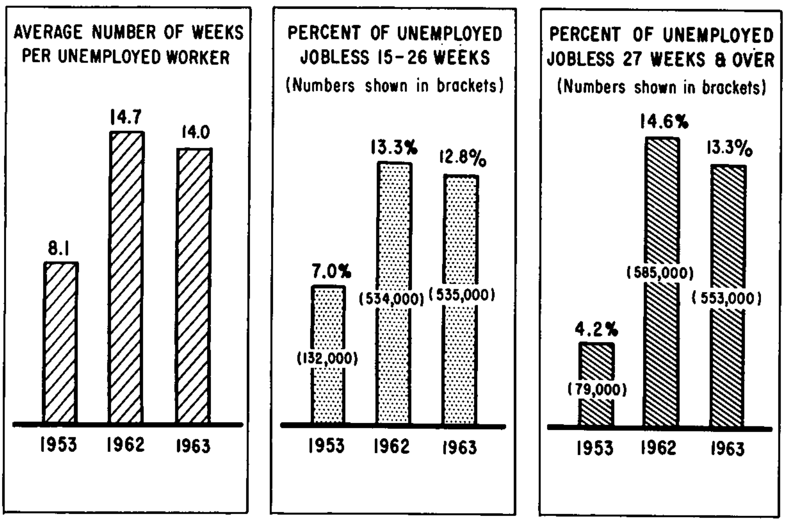
CHART 13

AMOUNT BY WHICH TRUE LEVEL OF UNEMPLOYMENT HAS EXCEEDED LEVEL CONSISTENT WITH FULL EMPLOYMENT[1]

Millions of Workers



DURATION OF UNEMPLOYMENT

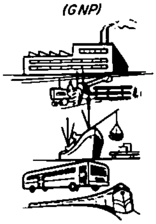
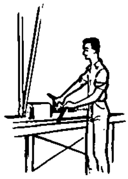
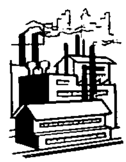


[1] Full employment is here regarded as true level of unemployment equal to 4.5 percent of the civilian labor force, which equates with full-time recorded unemployment of 2.9 percent of civilian labor force.

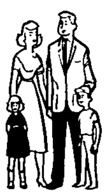
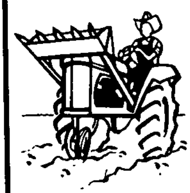
CHART 14

LARGE NATIONAL ECONOMIC DEFICITS DURING PERIOD 1953-1963

Dollar Items in 1962 Dollars

TOTAL NATIONAL PRODUCTION (GNP)	MAN YEARS OF EMPLOYMENT	PRIVATE BUSINESS INVESTMENT (Incl. Net Foreign)	PRIVATE AND PUBLIC CONSUMPTION 1/
			
$494 Billion Too Low	29 Million Too Low	$118 Billion Too Low	$376 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
			
$7,800 Too Low	$73 Billion Too Low	$326 Billion Too Low	$36 Billion Too Low

1/ Includes personal consumption expenditures plus government (Federal, state, and local) expenditures (330 and 46 billions, respectively).

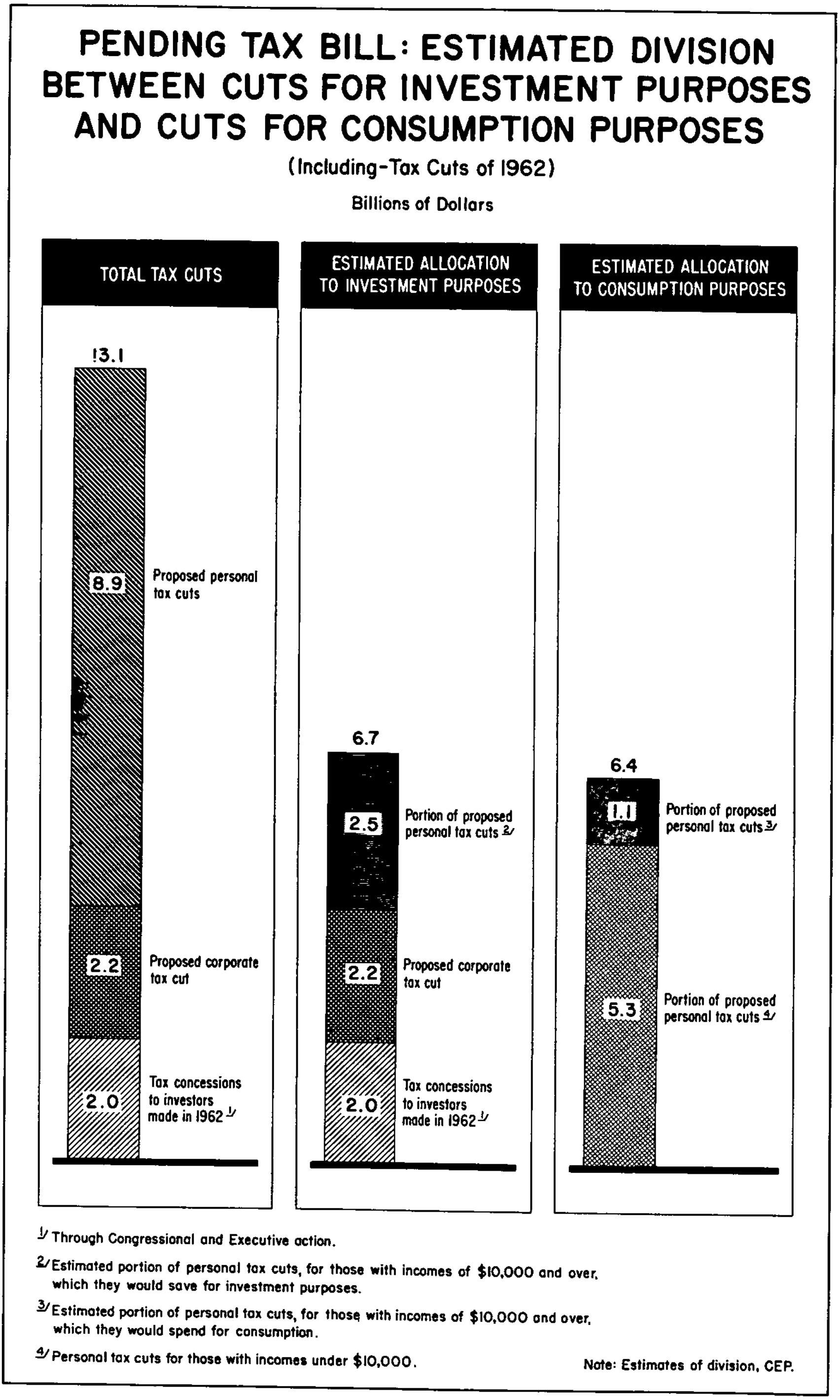

PENDING TAX BILL: ESTIMATED DIVISION BETWEEN CUTS FOR INVESTMENT PURPOSES AND CUTS FOR CONSUMPTION PURPOSES
(Including-Tax Cuts of 1962)
Billions of Dollars
TOTAL TAX CUTS
13.1
8.9
Proposed personal tax cuts
2.2
Proposed corporate tax cut
2.0
Tax concessions to investors made in 1962 1/
ESTIMATED ALLOCATION TO INVESTMENT PURPOSES
6.7
2.5
Portion of proposed personal tax cuts 2/
2.2
Proposed corporate tax cut
2.0
Tax concessions to investors made in 1962 1/
ESTIMATED ALLOCATION TO CONSUMPTION PURPOSES
6.4
1.1
Portion of proposed personal tax cuts 3/
5.3
Portion of proposed personal tax cuts 4/
1/ Through Congressional and Executive action.
2/ Estimated portion of personal tax cuts, for those with incomes of $10,000 and over, which they would save for investment purposes.
3/ Estimated portion of personal tax cuts, for those with incomes of $10,000 and over, which they would spend for consumption.
4/ Personal tax cuts for those with incomes under $10,000.
Note: Estimates of division, CEP.

CHART 16

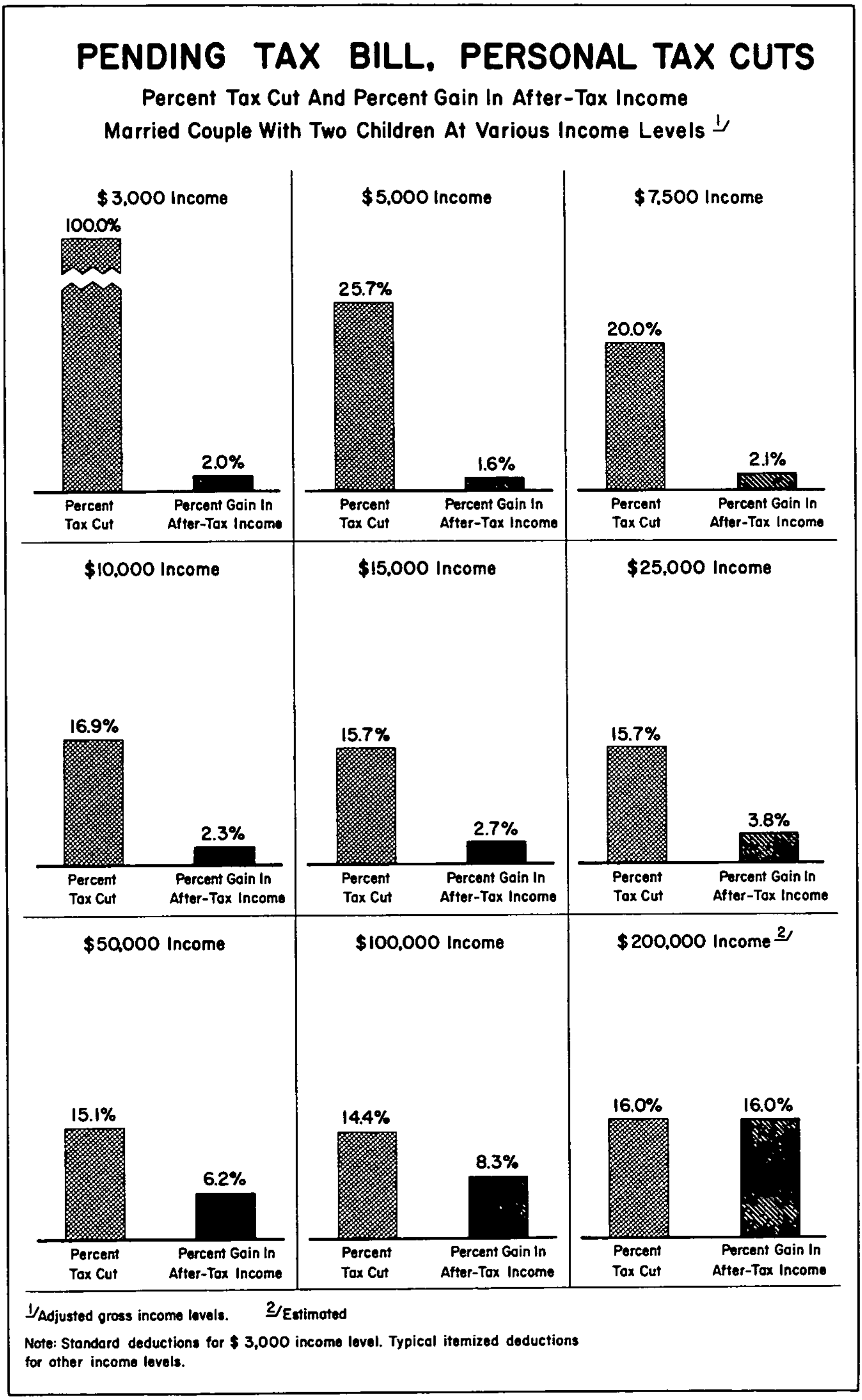

PENDING TAX BILL, PERSONAL TAX CUTS
Percent Tax Cut And Percent Gain In After-Tax Income
Married Couple With Two Children At Various Income Levels [1]
$3,000 Income
100.0%
2.0%
Percent Tax Cut
Percent Gain In After-Tax Income
$5,000 Income
25.7%
1.6%
Percent Tax Cut
Percent Gain In After-Tax Income
$7,500 Income
20.0%
2.1%
Percent Tax Cut
Percent Gain In After-Tax Income
$10,000 Income
16.9%
2.3%
Percent Tax Cut
Percent Gain In After-Tax Income
$15,000 Income
15.7%
2.7%
Percent Tax Cut
Percent Gain In After-Tax Income
$25,000 Income
15.7%
3.8%
Percent Tax Cut
Percent Gain In After-Tax Income
$50,000 Income
15.1%
6.2%
Percent Tax Cut
Percent Gain In After-Tax Income
$100,000 Income
14.4%
8.3%
Percent Tax Cut
Percent Gain In After-Tax Income
$200,000 Income [2]
16.0%
16.0%
Percent Tax Cut
Percent Gain In After-Tax Income
[1] Adjusted gross income levels. [2] Estimated
Note: Standard deductions for $ 3,000 income level. Typical itemized deductions for other income levels.

CHART 17

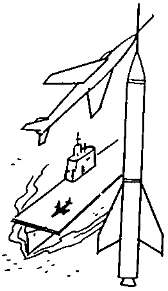
GOALS FOR A FEDERAL BUDGET GEARED TO ECONOMIC GROWTH AND PUBLIC NEEDS

1965, Fiscal Year; 1966 and 1970, Calendar Years
Per Capita Outlay in 1962 Dollars

TOTAL FEDERAL OUTLAYS

Year	% of Total Output	$ Per Capita
1965 Adm.[1]	15.25	$486.98
1966 Goal	15.91	577.89
1970 Goal	15.41	636.15

NATIONAL DEFENSE, SPACE TECHNOLOGY AND ALL INTERNATIONAL

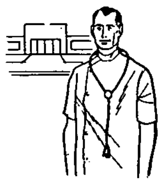


Year	% of Total Output	$ Per Capita
1965 Adm.[1]	9.54	$304.51
1966 Goal	9.82	356.78
1970 Goal	9.61	396.71

EDUCATION

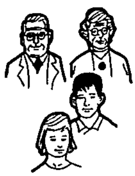
Year	% of Total Output	$ Per Capita
1965 Adm.[1]	.26	$8.41
1966 Goal	.62	22.61
1970 Goal	.80	32.86

HEALTH SERVICES AND RESEARCH



Year	% of Total Output	$ Per Capita
1965 Adm.[1]	.27	$8.62
1966 Goal	.44	16.08
1970 Goal	.55	22.54

PUBLIC ASSISTANCE

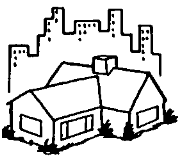


Year	% of Total Output	$ Per Capita
1965 Adm.[1]	.45	$14.27
1966 Goal	.51	18.59
1970 Goal	.51	21.13

LABOR AND MANPOWER, AND OTHER WELFARE SERVICES

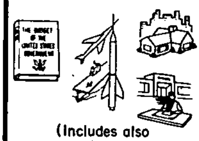
Year	% of Total Output	$ Per Capita
1965 Adm.[1]	.19	$6.12
1966 Goal	.15	5.53
1970 Goal	.14	5.63

HOUSING AND COMMUNITY DEVELOPMENT



Year	% of Total Output	$ Per Capita
1965 Adm.[1]	–	–$1.57
1966 Goal	.31	11.06
1970 Goal	.37	15.49

ALL DOMESTIC PROGRAMS AND SERVICES



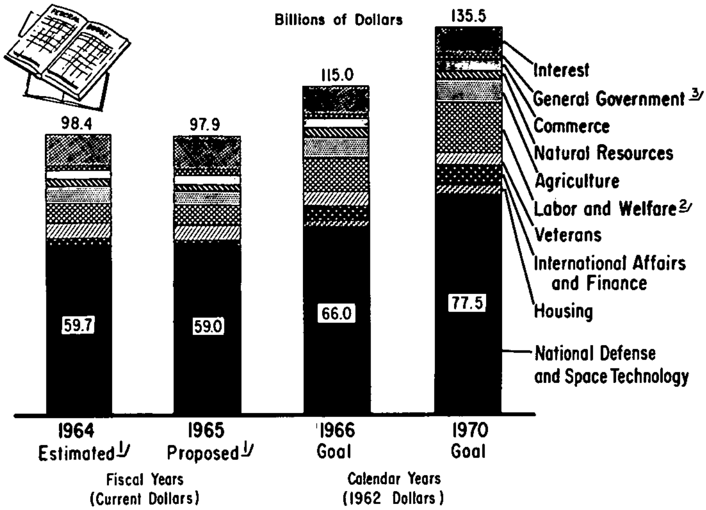
(Includes also Agriculture; Natural Resources; Veterans; Commerce; Interest; General Government, etc.)

Year	% of Total Output	$ Per Capita
1965 Adm.[1]	5.71	$182.47
1966 Goal	6.09	221.11
1970 Goal	5.80	239.44

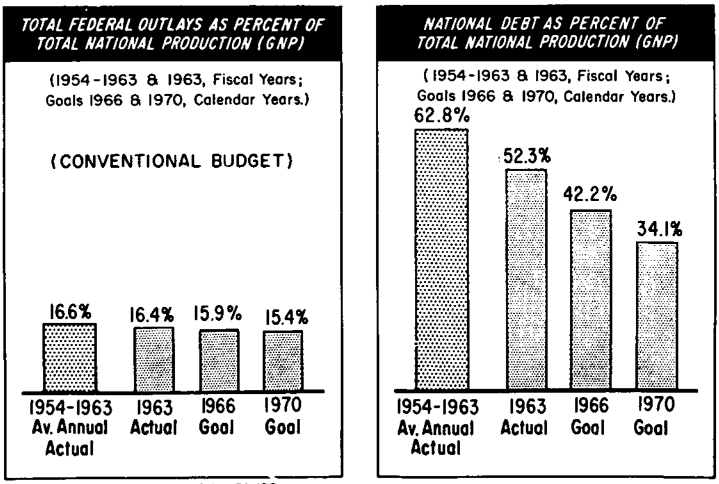
[1] Administration's proposed budget as of Jan. 21, 1964.

CHART 18

TOWARD A FEDERAL BUDGET CONSISTENT WITH MAXIMUM EMPLOYMENT AND THE PRIORITIES OF NATIONAL PUBLIC NEEDS



BURDEN OF FEDERAL OUTLAYS IN A FULLY GROWING ECONOMY WOULD BE LOWER THAN IN RECENT YEARS



1/ Based upon Budget Message of Jan. 21, 1964

2/ Including education and health services

3/ Including contingencies and less interfund transactions

CHART 19

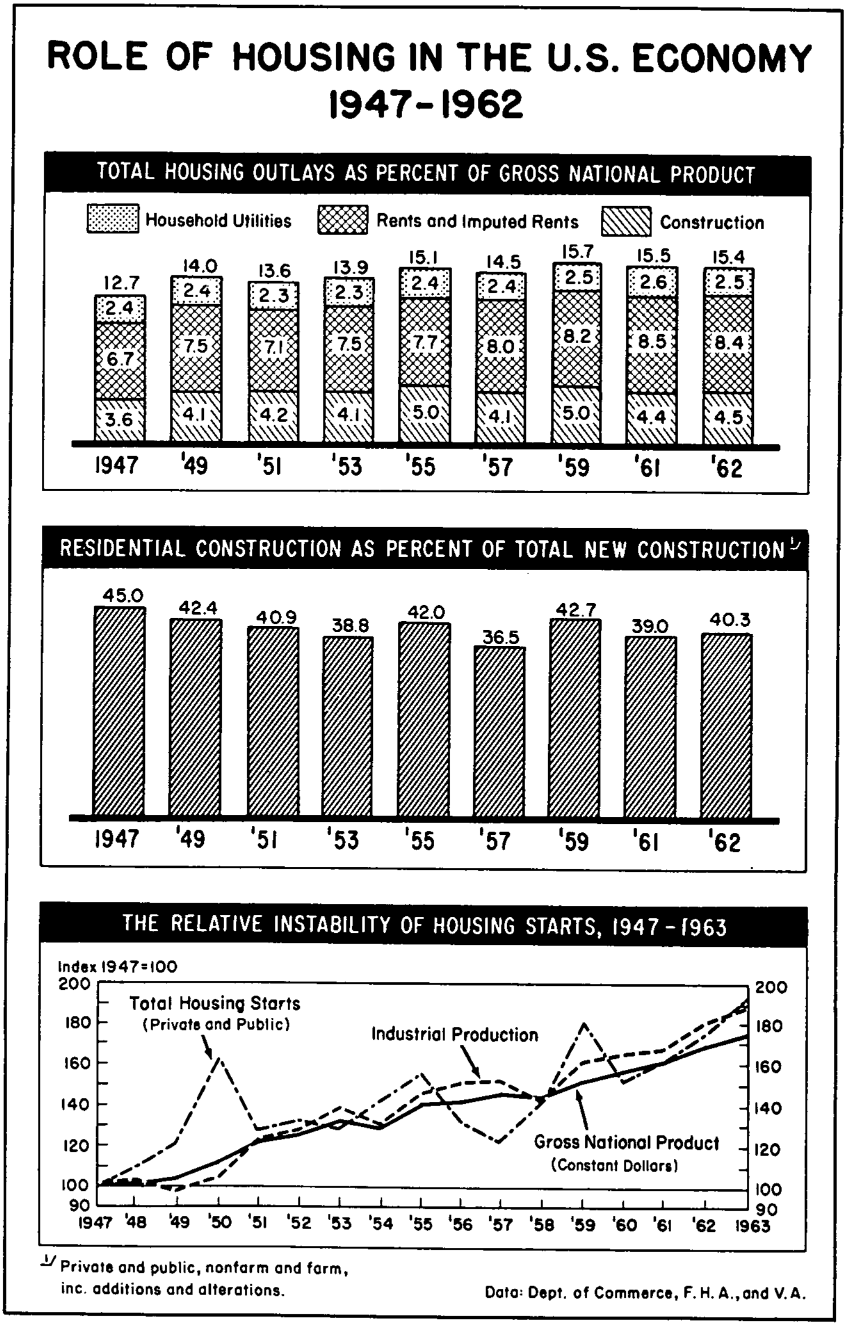
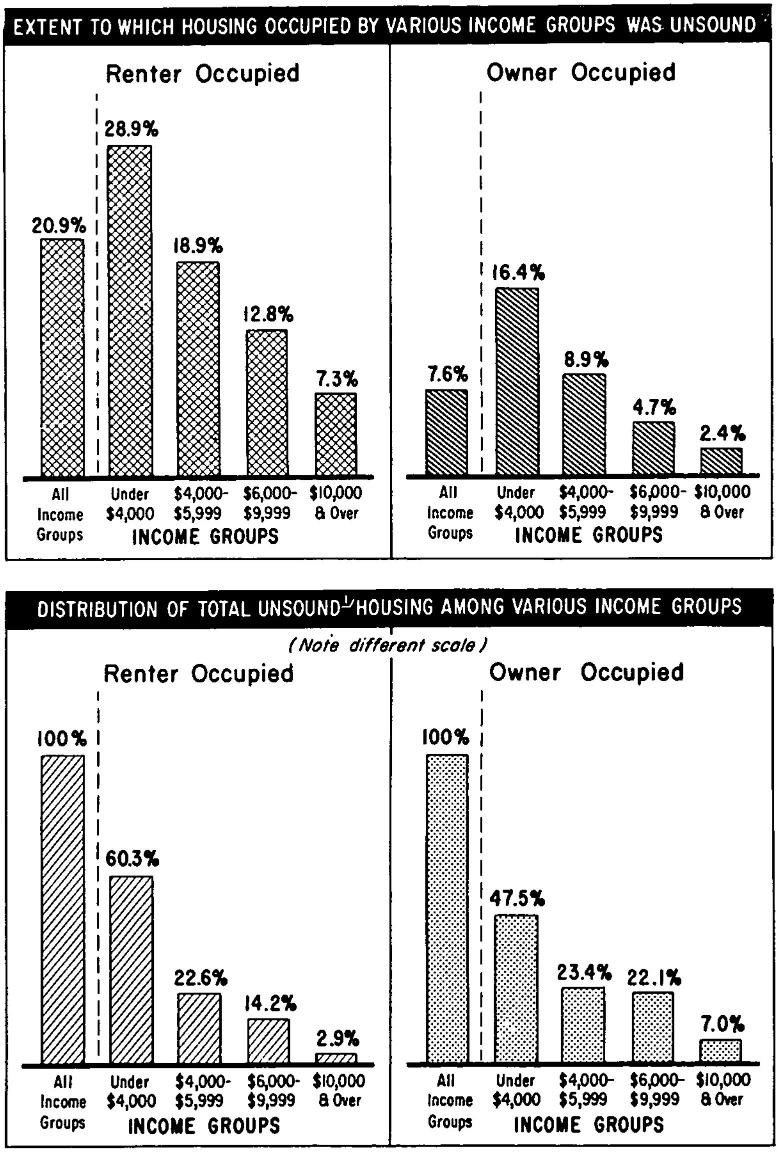

ROLE OF HOUSING IN THE U.S. ECONOMY
1947-1962
TOTAL HOUSING OUTLAYS AS PERCENT OF GROSS NATIONAL PRODUCT
Household Utilities
Rents and Imputed Rents
Construction
1947: 12.7 (2.4, 6.7, 3.6)
'49: 14.0 (2.4, 7.5, 4.1)
'51: 13.6 (2.3, 7.1, 4.2)
'53: 13.9 (2.3, 7.5, 4.1)
'55: 15.1 (2.4, 7.7, 5.0)
'57: 14.5 (2.4, 8.0, 4.1)
'59: 15.7 (2.5, 8.2, 5.0)
'61: 15.5 (2.6, 8.5, 4.4)
'62: 15.4 (2.5, 8.4, 4.5)
RESIDENTIAL CONSTRUCTION AS PERCENT OF TOTAL NEW CONSTRUCTION 1/
1947: 45.0
'49: 42.4
'51: 40.9
'53: 38.8
'55: 42.0
'57: 36.5
'59: 42.7
'61: 39.0
'62: 40.3
THE RELATIVE INSTABILITY OF HOUSING STARTS, 1947-1963
Index 1947=100
200
180
160
140
120
100
90
Total Housing Starts
(Private and Public)
Industrial Production
Gross National Product
(Constant Dollars)
1947 '48 '49 '50 '51 '52 '53 '54 '55 '56 '57 '58 '59 '60 '61 '62 1963
1/ Private and public, nonfarm and farm, inc. additions and alterations.
Data: Dept. of Commerce, F. H. A., and V. A.

CHART 20

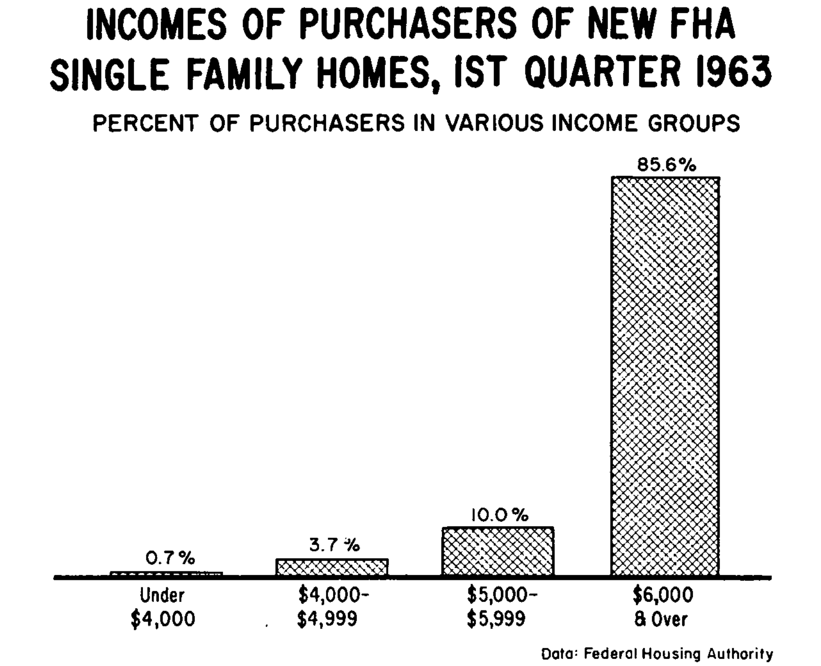
HOUSING CONDITIONS RELATED TO INCOMES IN METROPOLITAN AREAS, 1960



[1] Unsound housing is a Census classification based on some defects, but all unsound housing is not seriously deficient.

Data: U.S. Census of Housing, 1960

CHART 21


INCOMES OF PURCHASERS OF NEW FHA SINGLE FAMILY HOMES, 1ST QUARTER 1963
PERCENT OF PURCHASERS IN VARIOUS INCOME GROUPS
0.7%
3.7%
10.0%
85.6%
Under $4,000
$4,000-$4,999
$5,000-$5,999
$6,000 & Over
Data: Federal Housing Authority

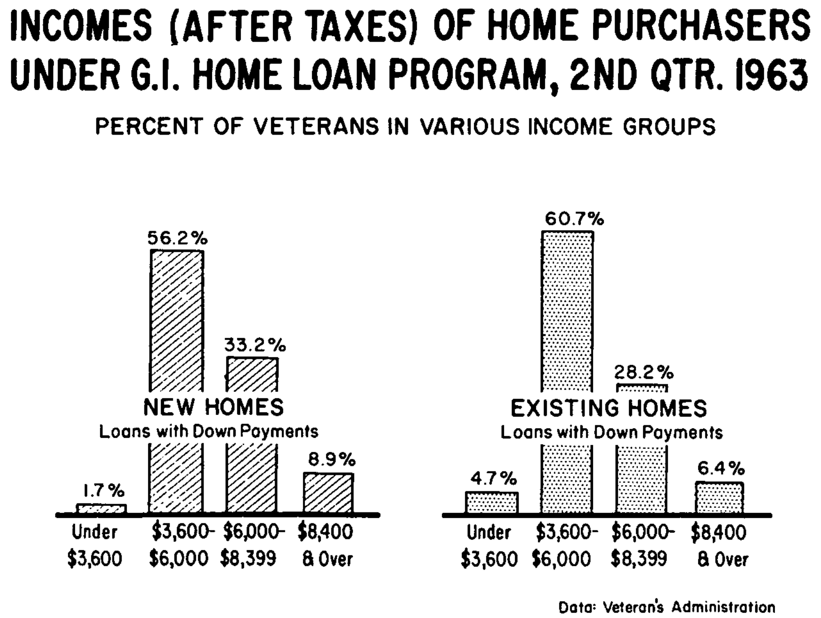
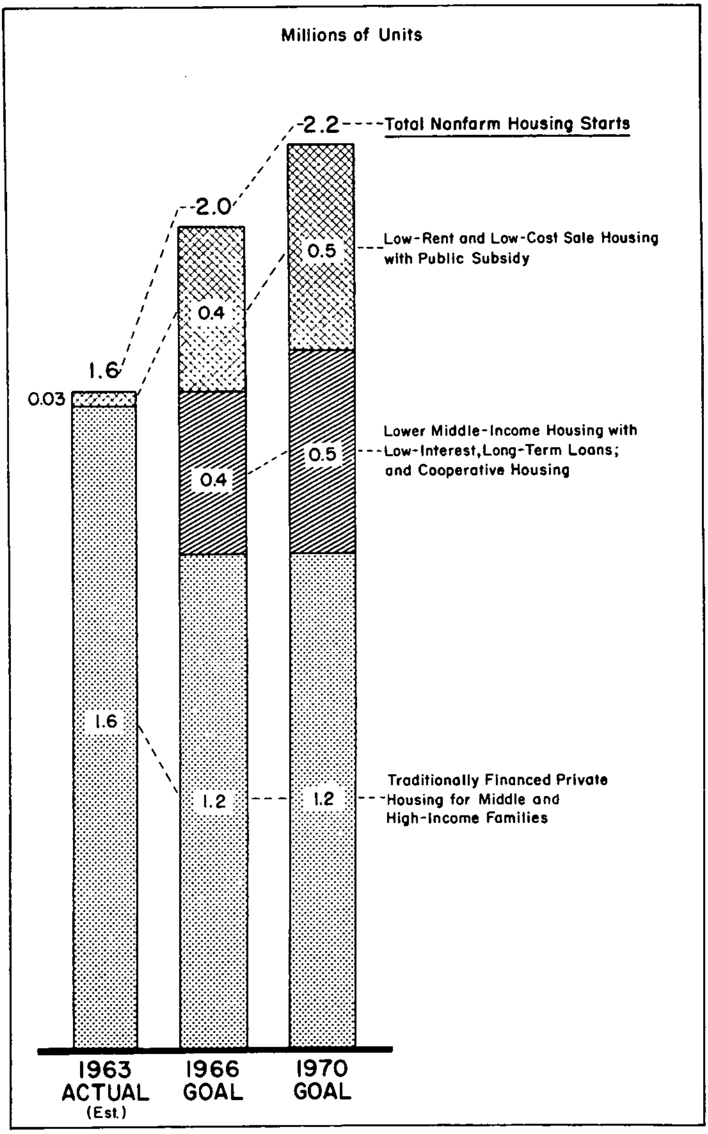

INCOMES (AFTER TAXES) OF HOME PURCHASERS UNDER G.I. HOME LOAN PROGRAM, 2ND QTR. 1963
PERCENT OF VETERANS IN VARIOUS INCOME GROUPS
NEW HOMES
Loans with Down Payments
1.7%
56.2%
33.2%
8.9%
Under $3,600
$3,600-$6,000
$6,000-$8,399
$8,400 & Over
EXISTING HOMES
Loans with Down Payments
4.7%
60.7%
28.2%
6.4%
Under $3,600
$3,600-$6,000
$6,000-$8,399
$8,400 & Over
Data: Veteran's Administration

CHART 22

TOWARD DECENT HOMES FOR ALL: GOALS FOR NEW NONFARM HOUSING



1963 Data: Dept. of Commerce, F.H.A., and V.A.

CHART 23

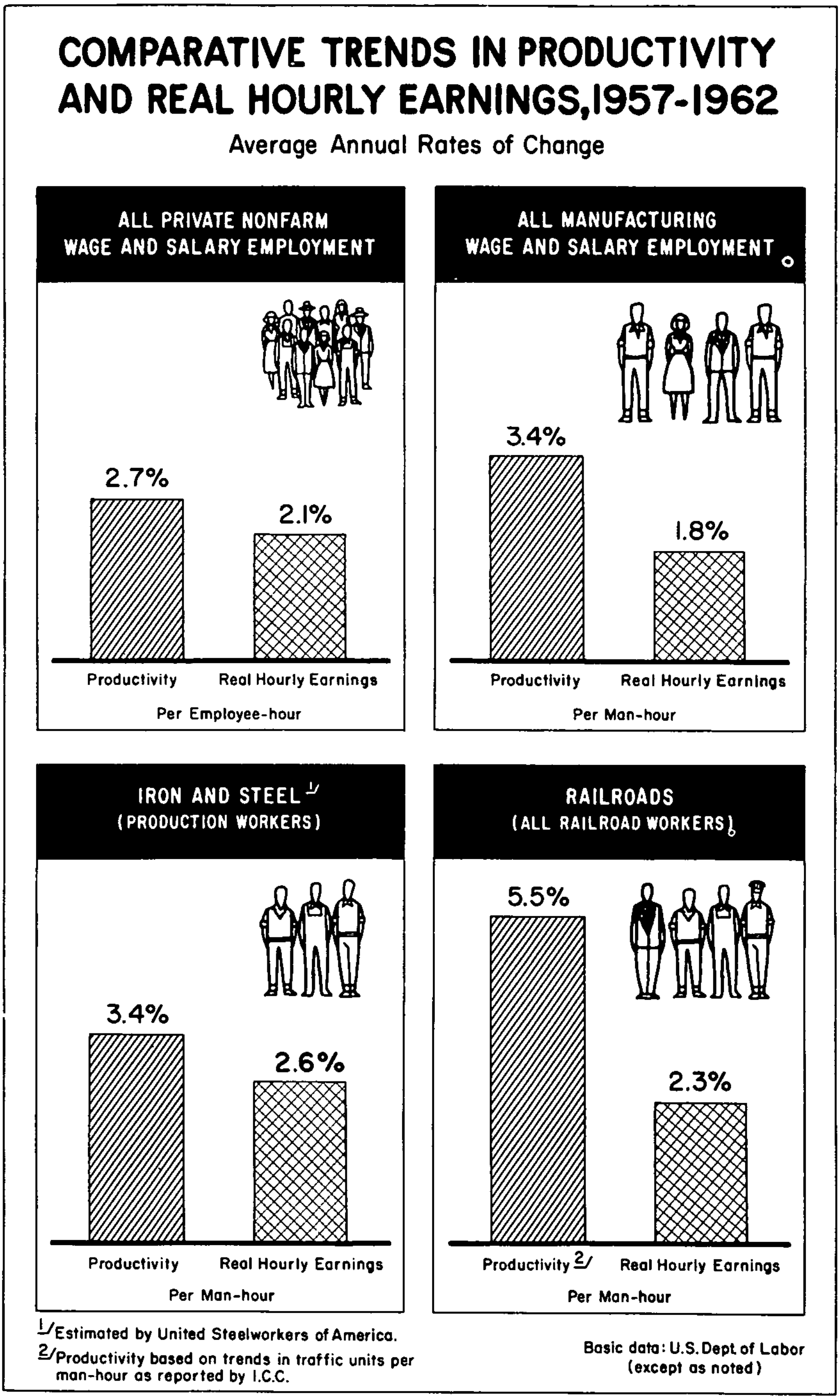
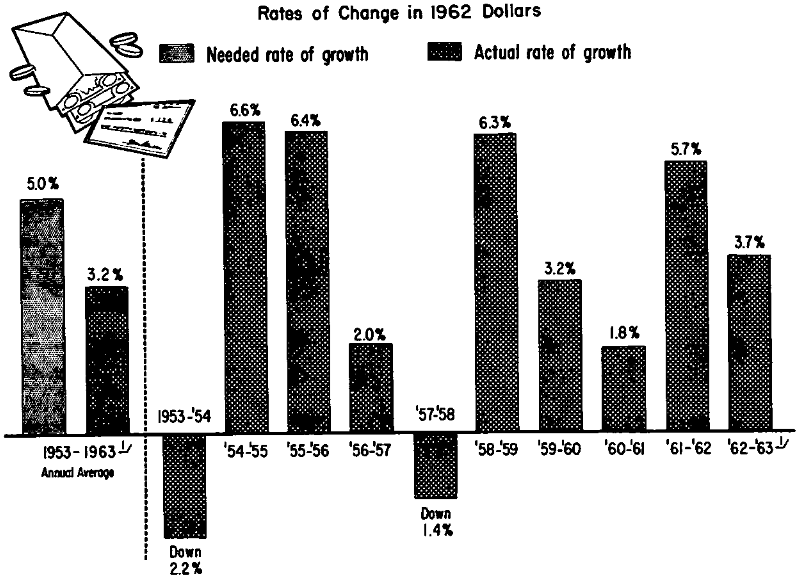

COMPARATIVE TRENDS IN PRODUCTIVITY
AND REAL HOURLY EARNINGS, 1957-1962
Average Annual Rates of Change
ALL PRIVATE NONFARM
WAGE AND SALARY EMPLOYMENT
2.7%
2.1%
Productivity
Real Hourly Earnings
Per Employee-hour
ALL MANUFACTURING
WAGE AND SALARY EMPLOYMENT
3.4%
1.8%
Productivity
Real Hourly Earnings
Per Man-hour
IRON AND STEEL 1/
(PRODUCTION WORKERS)
3.4%
2.6%
Productivity
Real Hourly Earnings
Per Man-hour
RAILROADS
(ALL RAILROAD WORKERS)
5.5%
2.3%
Productivity 2/
Real Hourly Earnings
Per Man-hour
1/ Estimated by United Steelworkers of America.
2/ Productivity based on trends in traffic units per man-hour as reported by I.C.C.
Basic data: U.S. Dept. of Labor
(except as noted)

CHART 24

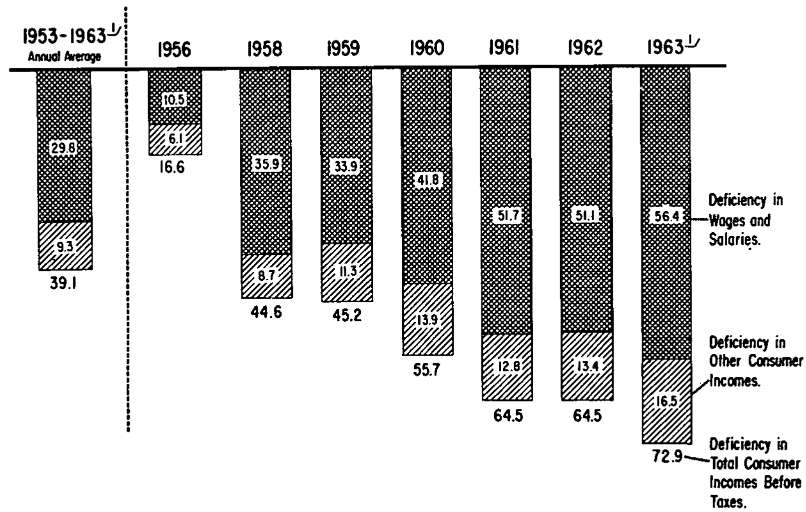
DEFICIENT RATE OF GROWTH IN WAGES AND SALARIES, 1953- 1963[1/]

Rates of Change in 1962 Dollars



DEFICIENCIES IN WAGES AND SALARIES ARE LARGE SHARE OF DEFICIENCIES IN TOTAL CONSUMER INCOMES BEFORE TAXES

Billions of 1962 Dollars



1/ 1963 estimated on basis of first three quarters.

CHART 25

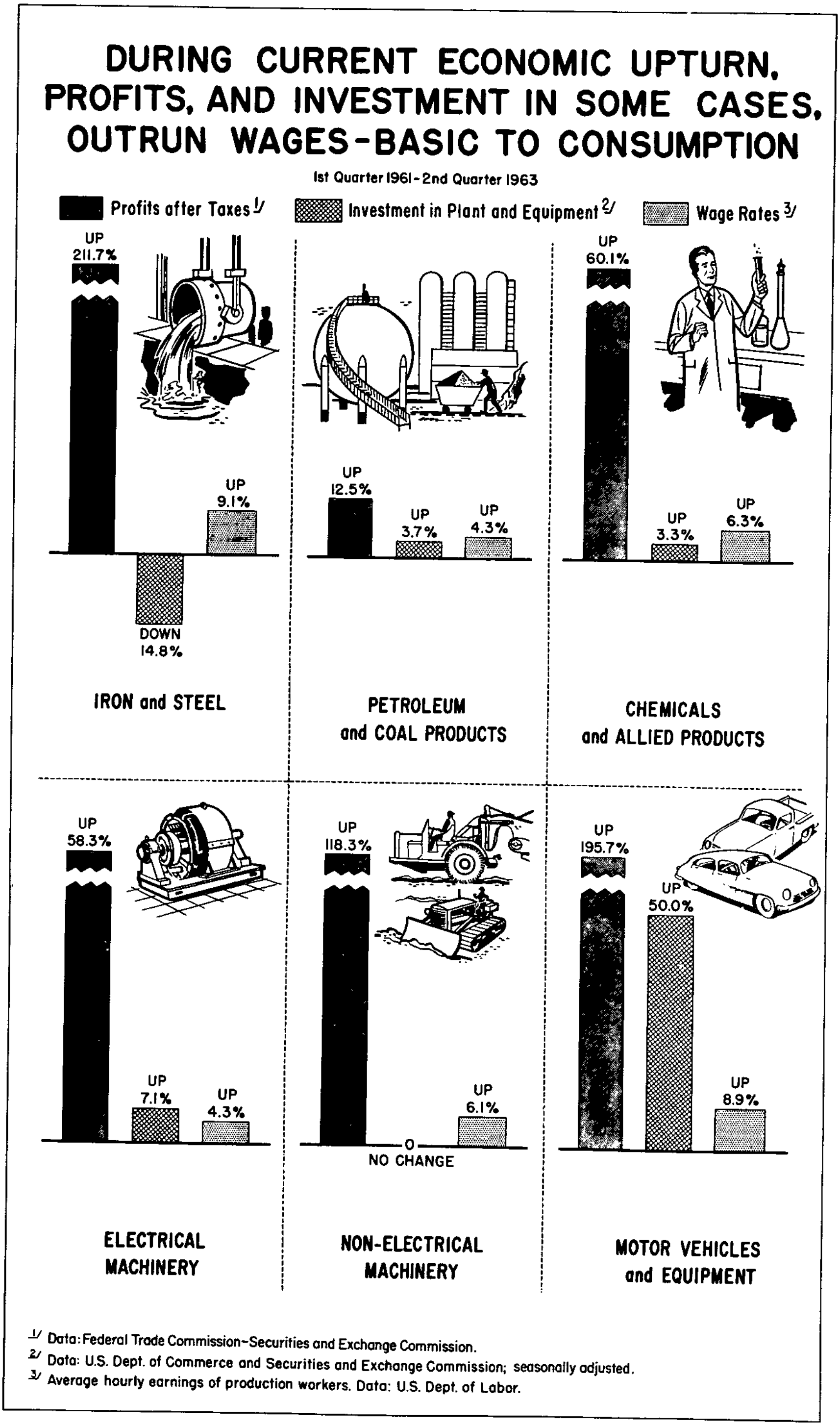

DURING CURRENT ECONOMIC UPTURN, PROFITS, AND INVESTMENT IN SOME CASES, OUTRUN WAGES-BASIC TO CONSUMPTION
1st Quarter 1961-2nd Quarter 1963
Profits after Taxes 1/
Investment in Plant and Equipment 2/
Wage Rates 3/
UP 211.7%
DOWN 14.8%
UP 9.1%
IRON and STEEL
UP 12.5%
UP 3.7%
UP 4.3%
PETROLEUM and COAL PRODUCTS
UP 60.1%
UP 3.3%
UP 6.3%
CHEMICALS and ALLIED PRODUCTS
UP 58.3%
UP 7.1%
UP 4.3%
ELECTRICAL MACHINERY
UP 118.3%
0 NO CHANGE
UP 6.1%
NON-ELECTRICAL MACHINERY
UP 195.7%
UP 50.0%
UP 8.9%
MOTOR VEHICLES and EQUIPMENT
1/ Data: Federal Trade Commission-Securities and Exchange Commission.
2/ Data: U.S. Dept. of Commerce and Securities and Exchange Commission; seasonally adjusted.
3/ Average hourly earnings of production workers. Data: U.S. Dept. of Labor.

CHART 26

FEDERAL STATISTICS USERS' CONFERENCE

The Federal Statistics Users' Conference is composed of organizations from all sectors of the economy. Business, farm, labor, and nonprofit research grups are all represented in the conference. As might be expected, members of the Federal Statistics Users' Conference have diverse views about the substance of the Economic Report. For this reason, FSUC is not in a position to be of help to the committee in evaluating this aspect of either the 1964 Economic Report of the President or the report of his Council of Economic Advisers.

While members of FSUC have a diversity of interests and diverse views on economic policies, we are joined together because we have a common interest in adequate statistical information from Federal sources. Business, farm, labor, and nonprofit research organizations all draw from the common storehouse of Federal statistics. The President and his Council of Economic Advisers also draw from this common source of information. And so does the Congress in dealing with legislative policy matters.

OFFICE OF BUSINESS ECONOMICS

The President's Economic Report relies in large part upon the work of the Office of Business Economics which is responsible for developing and publishing the statistical compilations known as the national economic accounts.

The national economic accounts are put together by a relatively small group of professionals who bring together in a single framework a wide variety of materials from different sources and of different qualities.

Last year we warned of possible deterioration in the quality of this Office's output and its staff unless remedial action was soon taken to utilize its talents more effectively.

We are glad to note that OBE is being given some challenging new tasks to do—tasks which are well within the professional competence of the staff and which reflect new confidence in the work of OBE and new respect for its ability as the prime source of economic analysis for the Department of Commerce. The recent transfers of certain activities involving regional economic analysis from Business and Defense Services Administration and Area Redevelopment Administration to the Office of Business Economics are a mark of this new attitude toward OBE.

OBE's staff will need to be strengthened if it is to do the job it can do. At the present, too much depends upon too few. For example, the balance-of-payments statistics for the Nation depend very largely upon the health, leave status, and job attachment of two individuals. Were these two professionals to be lured away to greener pastures, the balance-of-payments statistics would be seriously impaired. And this is not an isolated case. OBE is still operating at full stretch in too many places.

Adequate staffing for the Office of Business Economics is not something to be accomplished in a crash program. It will require consistent efforts over a period of years. This is a task which needs more attention than it has been getting.

FULL SCALE REVIEW OF STATISTICAL PROGRAM NEEDED

It is about time to have another careful review of the Government's statistical program as a whole. The Joint Economic Committee has contributed notably to the improvement of statistics over the past 15 years. In your report on data gaps in 1948, in your review of the Government's statistical programs in 1955, and in your particular examinations of statistics relating to commercial agriculture, the national economic accounts, prices, employment and unemployment, the budget as an economic document, and other areas of specific interest, you focused attention on the Government's statistical information structure and its output as a whole and in detail.

In 1962, the committee published "A Federal Statistical Program for the 1960's." This report included many of the numerous recommendations for statistical improvement which have been advanced over the years, together with many other suggestions. Further recommendations for statistical improvements will be forthcoming when the President's Review Committee on Balance-of-Payments Statistics makes its report.

To implement all of these recommendations would cost more than the President would be willing to recommend in his budget and more than the Congress would be willing to appropriate. If implemented, the recommendations would call for the addition of staffs beyond those likely to be obtainable. The implementation of all these suggestions would result in a substantial increase in paperwork for respondents. Bearing in mind the limitations in resources, the limitations in needed abilities, and the limitations in the patience of respondents to statistical questionnaires, it is particularly important that a renewed attempt be made to express priority needs for improvement in statistical information with a view to giving guidelines for the development of statistical programs over the next several years.

The question is not whether the Government's statistics need improvement. That answer is clear.

The real questions are: Which statistics are in most urgent need of improvement? How can resources be directed to most effectively meet our needs for information? What kinds of statistics will be needed most urgently in 1966–70? The objective of the Federal statistical program cannot be perfection—that goal is impossible. But the objective can be optimum usefulness—and that goal at least can be approached.

This would be a particularly appropriate year in which to review the Government's statistical program. The President has urged that this be a year of economy and frugality. His budget reflects this thinking in statistical as in other programs. This stress on economy in Federal expenditures underscores the need to make sure that statistical programs are meeting first needs first.

Some of the most important areas which are worthy of careful review include:

Manpower, employment, and unemployment statistics.—The persistence of a high level of unemployment is a matter of continuing national concern. The President's Committee To Appraise Employment and Unemployment Statistics proposed an elaborate program for the improvement of these data. Work is now getting underway to implement some of these recommendations. It is worth considering whether this work is going forward rapidly enough to meet the problems of the last half of the 1960's and whether it is being directed to those areas where the need for information is likely to be most critical over the next few years.

Statistics on consumer income and expenditures.—The President bases his expectations for a prosperous 1964 and first half of 1965 on strong consumer demand. The economy's heavy reliance on markets for consumer goods and services as the foundation for national economic prosperity suggests that a careful reexamination of the numerous statistical series bearing upon consumer income and demand may be worthwhile. Is it prudent to place such a heavy reliance upon an assumption that observed past relationships between disposable income and consumer expenditures are adequate for use in forecasting the course of the economy? Do we need to inquire more deeply into factors affecting consumer expenditures?

The President's economic advisers note that housing was "the most surprising performer" among major demand components in the past year. They note also that "the future of residential building depends heavily upon the sustainability of construction of multifamily units" and that vacancy rates are rising in many areas.

Many people associated with the construction industry and with the financing of housing construction share the concern of the President's advisers about the housing market and about the general question of possible "overbuilding." Like the Council of Economic Advisers, they have some fragmentary reports of varying quality about vacancies in some metropolitan areas. But neither they nor the President's economic advisers have a consistent, reliable body of current information showing the vacancy situation in the country's major metropolitan areas.

There is a growing concern about the lack of adequate information not only on vacancies but also on available housing inventories and on housing market activity. Efforts to close this data gap in the past few years have been largely unsuccessful. While efforts to improve information on the production of housing (housing starts, construction put in place) have received some needed additional resources, data affecting the demand for housing are generally lacking.

Economic impact of Federal activities.—The Federal Government's purchases of goods and services amount to about 11 percent of the Nation's total output. Statistical reporting of Federal procurement and other activities which affect the economy is very limited. The efforts now underway to improve these data need to be looked at and appraised as to their effectiveness in overcoming existing statistical gaps.

Agricultural statistics.—It has become commonplace to talk about the revolutionary changes which have taken place in American agriculture in the last 25 years. Although the Government's statistics relating to crop and livestock production are in the process of being substantially improved, other statistics relating to agriculture do not clearly reflect the changes which have occurred. Are the present data adequate for appraising policy alternatives?

Transportation statistics.—Several strides forward have been taken in recent years. The first Census of Transportation is being processed. A new commodity classification system which would tie together the production data and shipments information is being worked out. The whole area is in a state of flux at the moment. A review at this time before final decisions are made might be appropriate.

Regional information.—A Conference on Regional Data Needs and Availability sponsored jointly by the Federal Statistics Users' Conference and the Committee on Regional Accounts last October 9 reported:

"Demand for demographic and economic statistical information continue to grow. Considerations of cost, disclosure, and reporting burden pose many questions which are not fully resolved, but considerable progress has been made in some areas to overcome these obstacles.

"Technological advance, the development of new techniques in data collection, and rapid expansion in the use of computers by all kinds of organizations provide new opportunities for the development of these data. Much of this potential could be unrealized for many years to come if steps are not taken soon to assure a continuing flow of basic information from the many sources newly available.

"The Federal Government should make a detailed study of needs for subnational demographic and economic data. This study should:

"Emphasize fuller utilization of presently available information without undertaking new programs.

"Dintinguish between those areas where the Federal Government should concentrate its efforts and those areas where other organizations, groups, and levels of government should concentrate their efforts."

There is a real need for better guidelines for the development of Federal statistical programs over the remaining years of this decade. The Joint Economic Committee is particularly well-equipped to make a significant contribution to this end. We hope that your crowded schedule will permit you to undertake at least a beginning to this task this year.

LIFE INSURANCE ASSOCIATION OF AMERICA

BY JAMES J. O'LEARY, VICE PRESIDENT AND DIRECTOR OF ECONOMIC RESEARCH

I am glad to have this opportunity to comment on the Economic Report of the President, including the Annual Report of the Council of Economic Advisers. I would like to make it clear that the views presented here are my own personal views and may not necessarily represent thinking by others in the life insurance business. The limitations of time have not permitted any exchange of thinking about the report with others in the life insurance business.

I subscribe strongly to the prescription in the report of a major reduction in personal and corporate taxes as a means to spur the economic growth of the United States over an extended period. A spokesman for the life insurance business testified in favor of the principle of tax reduction in H.R. 8363 before both the House Ways and Means Committee and the Senate Finance Committee.[1] I also believe that the forecast of general business activity as set forth in the President's report and in chapter 1 of the Council's report is a reasonable one—that is, it seems to me that the effect of the tax cut plus other factors will be to carry GNP to approximately a $620 billion level this year.

My comments will be devoted largely to a consideration of what I think are important gaps in the Annual Report of the Council of Economic Advisers. One of these gaps, which I regretted, was a failure on the part of the Council to reveal their detailed analysis of the multiplier effect of the tax cut. It is true that there was a theoretical discussion of the multiplier in the 1962 report of the Council, but there is virtually a complete absence of discussion this year. It would have been helpful, in evaluating the forecast, to have had a discussion in detail of what assumptions the Council is making about the multiplier.

The biggest gap in the Council's report is an almost complete failure to consider the implications of the monetary expansion which has been going on in the United States since early 1960. There is a brief discussion on page 47, but it is hardly as penetrating as is demanded at this point in the economic expansion. Since early 1960, when the monetary authorities began a policy of active credit ease, there has been an increase of $9 billion in Federal Reserve credit, from a level of $27 billion in the first quarter of 1960 to $36 billion at the end of 1963. In this period the total loans and investments of the commercial banks (excluding interbank loans) have risen sharply by $60 billion, from $185.8 billion at the end of 1959 to $245.8 billion at the end of 1963. This expansion in loans and investments by the

[1] The statement representing life insurance views regarding H.R. 8363 recognized that the tax cut involved a serious risk of reviving inflation. It took the position, therefore, that if the bill were enacted Federal spending must be held down and that the Government must be prepared to bring monetary, debt management, and other policy measures into play promptly to avoid building up inflationary pressures and to protect the international value of the dollar.

commercial banks is far greater in duration and in magnitude than in any other peacetime period in our history. As a result, we have had a very great expansion in the money supply of the country. The money supply as traditionally defined—i.e., currency outside the banks plus demand deposits—has risen from $142 billion at the end of 1959 to $153.2 billion at the end of 1963, or by $11.2 billion. In addition, most economists are agreed today that the traditional definition of the money supply is too narrow and that time deposits in commercial banks should also be included. The reason is that economists recognize that a high proportion of the time deposits are actually demand deposits which have been shifted into the time deposit category to take advantage of the 4-percent interest that can be obtained on such deposits. Also, the time deposits have a liquidity not much less than demand deposits. During the past 4 years time deposits have increased enormously, from $67.4 billion at the end of 1959 to $112 billion at the end of 1963, or by $44.6 billion. Thus, in the more realistic definition of the term—currency outside the banks plus demand and time deposits—the money supply of the country has increased by $55.8 billion during the past 4 years. This was a rise in the money supply from $209.4 billion at the end of 1959 to $265.2 billion at the end of 1963, or 26.6 percent. During this same period GNP rose from a figure of $482.7 billion in 1959 to $585 billion in 1963, in current prices, or by 21.2 percent. Thus, the rate of increase of the money supply has considerably outstripped the rise of GNP.

As a result of the great and prolonged monetary expansion which has occurred, the national economy is more liquid than it has ever been in peacetime history. The aggregate of selected liquid assets held by the public (demand deposits and currency, time deposits in commercial and mutual savings banks, postal savings deposits, savings and loan shares, U.S. Government savings bonds, and U.S. Government securities maturing within 1 year) have risen from $393.9 billion at the end of 1959 to $493 billion at the end of November 1963, an increase of better than 25 percent. During the period since the first quarter of 1960, through the last quarter of 1963, the rise in total selected liquid assets has outpaced the increase in GNP. The ratio of such assets to GNP (seasonally adjusted, current prices) has risen from 78.5 percent in the first quarter of 1960 to over 82 percent in the last quarter of 1963.

I recount these facts not to predict any dire consequences. As a matter of fact, given the slack we had in our national economy in the period 1960–63, it was desirable, of course, to pursue an easy credit policy. It seems to me, however, that the prospective passage of the tax reduction program requires a new look into the implications of the extended period of easy credit. It requires a new look at credit policy. This I did not find in the Council's report. The report recognizes that despite the probability of a continued high unemployment rate, there is a danger that inflationary pressures will arise as the year progresses. However, the Council thinks of these possible upward pressures as originating from some abuse of economic power by business firms or trade unions that raise prices or wages unnecessarily. I submit that as a result of the great expansion of the money supply which has occurred, and the buildup in liquidity in the economy, we face the danger that continued easy credit, along with major tax reduction, will revive inflationary pressures of the "demand pull" type. That is, our problem of inflation danger in 1964 may not at all be the cost-push variety, but it may very well be the old-fashioned problem of too many dollars chasing too few goods and services. I regret that the Council did not go into this possibility although it is widely regarded as a distinct possibility by many economists.

I have serious reservations about the emphasis in the President's Economic Report (p. 11) that "a strong upswing in the economy after the tax cut need not bring tight money or high interest rates." Much depends upon what is meant by "tight money" and "high interest rates." This statement does not really face the issue. I believe that the issue is that if the tax cut is enacted and the economic effect is what the Council forecasts, it will be necessary for the Government to face up to the fact that both the tax cut and continued easy credit will be too strong an expansionary medicine. In other words, it must be expected that monetary and debt management policy should be directed promptly toward restraint. This does not mean that money has to become "tight" or that interest rates need to rise sharply. It means that monetary and devt management policy must be free to exert a restraining influence on the availability of credit and that we must be willing to accept rising interest rates as necessary for maintaining general price stability. It is true that the President's report pointed out that monetary policy "must remain flexible" so that "it can quickly shift to the defense if, unexpectedly, inflation threatens." Unfortunately, since the report was made public the interpretation in congressional circles seems to have been that pressures must be kept on the monetary authorities to assure easy credit forever, or at least for an extended period.

I believe that the monetary situation is such today that the public interest demands that the monetary authorities have absolute freedom to employ their judgment about the monetary policy to be followed. Experience indicates that there is quite a long lag between a Federal Reserve move toward restraint and the actual effect of the restraint. The reason is that the prolonged period of credit ease has made the economy so liquid. If monetary and debt management policy moves are postponed until there are overt signs of inflation, it may be too late. To be effective, monetary restraint must be started before inflationary pressures begin breaking out. Certainly the experience of 1953–57 taught the authorities how long it takes for a policy of credit restraint to exert a "bite" after liquidity has been built to a high level.

After 4 years of easy credit there are signs that the quality of credit has experienced some deterioration. The Council report suggests the need for continued easy credit despite the fact that there is no evidence that change in the quality of credit question has been considered. The facts about the quality of credit are admittedly difficult to ascertain. It is a matter of record, however, that the rates of delinquency and foreclosure on Government insured and guaranteed mortgages have risen sharply in the past few years. It is also a fact that the spread in yields between low-grade investments and high-grade investments has narrowed markedly as many investors have apparently placed increasing emphasis upon lower grade, higher yielding assets. The Federal Reserve Board has been studying the quality of mortgage credit for over a year and there have been frequent warnings by Board officials about the downgrading of quality. Similarly, the Home Loan Bank Board authorities have also been expressing concern about lowered standards in mortgage lending.

One searches in vain for any word in the Council's report about deterioration in the quality of credit. If this deterioration has progressed as far as some believe, does it make sense to continue to flood the economy with easy credit, especially if the tax cut is enacted? Would continued very easy credit not mean simply further decline in the quality of credit? If the quality of credit has indeed deteriorated, this would have important consequences for stable growth of the economy.

I believe that a move by the monetary and debt management authorities toward increasing credit restraint promptly after the tax cut has been enacted would have three advantages: (1) it would aid to prevent a renewal of inflationary forces in our domestic economy as the result of the tax cut; (2) it would aid to tone up the quality of credit; and (3) it would increase confidence of foreigners in the value of the dollar and would encourage foreigners to continue to hold their large liquid assets in the United States.

THE NATIONAL ASSOCIATION OF MANUFACTURERS

The process, specified in the Employment Act of 1946, by which Congress receives an annual Economic Report from the President, and then your committee hears comments on it, and prepares a report or reports stating its own reactions, is of the utmost importance. This procedure establishes, or should establish, a fundamental understanding of the Nation's economic situation. It thereby sets the stage for governmental actions in the economic area.

This year's Economic Reports by the President and his Council call attention to the record of sustained economic growth over the past 3 years. They quite properly add that satisfaction with this performance must be tempered by the fact that we have been unable to reduce unemployment below the 5.5-percent level. They express the belief that growth will continue in 1964 at an accelerated pace, with little or no inflation, and that we will gain some ground in reducing unemployment.

The chief basis for this optimistic expectation, as stated in these reports, is the anticipation of a major tax reduction early this year. The chief caveat taken in the reports is the possibility that the expected noninflationary growth might be upset by adverse wage and price trends.

In broad outline, our association agrees with much of this appraisal. The Nation's prospects for economic growth are on the whole favorable and tax reduction will help to support them. The emphasis on Government fiscal policy, and on wage price developments, as critical factors is well taken.

However, it is our view that the administration's interpretation of these subjects is deficient in important respects. Thus, their economic reports are inadequate as a basis for understanding the current economic situation, and unreliable as a guide to public policy.

Our association agrees most heartily that relief from the present burden of taxes is essential for the Nation's economic health and growth. But we question the description, presented in these economic reports, of the process by which tax reduction produces its beneficial effects. Tax reduction is conceived as a device for supplementing the aggregate volume of demand, rather than as a means of easing the tax restraints on the incentives and capital flow necessary to business growth. It seems to us that this emphasis on demand leads the administration into some logical inconsistencies with its other stated policies, notably its commitment to Government economy. It also leads them, we reluctantly conclude, into a mood of overoptimism which tends to downgrade the seriousness of other national problems—especially the threat of a major rise in labor costs. Tax reduction will have salutary effects on growth and employment, but they could easily be upset if a large-scale breakthrough occurs on the cost front. Extralegal intervention by the administration in the private wage and pricemaking process, as proposed in their economic reports, is not likely to be effective and could be extremely disruptive.

The fundamental economic problem of the Nation is the reconciliation of several objectives: the maintenance of the international convertibility of the dollar at its present level, the encouragement of high levels of production employment and growth at home, the avoidance of inflation and the preservation of our economic freedom. There is no magic combination of fiscal measures with money and credit policies which will allow us to use these instruments simultaneously to "stimulate demand" and to suppress inflation.

There is a way out however. Tax reform oriented toward improvement of business incentives and release of funds for private investment—and accompanied by the utmost attainable in the way of Government economy—can be highly beneficial in improving both our domestic and our international economic position. Above all, restraint on the increase of labor costs, in ways which are consistent with a free economy, is of crucial importance in preserving the value of our dollar while encouraging prosperity and growth at home.

It is only insofar as progress can be anticipated along the lines just stated that one can be truly optimistic regarding the Nation's economic future. There are grounds for optimism, albeit with reservations. The tax reduction now in preparation will make its contribution, not so much through expansion of demand as through its effects in releasing incentives and capital. The annual increase in labor costs has been relatively restrained in recent years. However, a major increase in costs during the coming year could be completely destructive of our hopes for reconciling currency stability with domestic growth.

Our reasons for these conclusions will be set forth in the remainder of this statement.

ECONOMIC EXPANSION AND "DEMAND"

The Council's Economic Report points out that there has been a 3-year expansion in the rate of economic activity and that there nevertheless still exists a substantial gap between the output possible if unemployment were reduced to 4 percent and the actual level of output. It explains these developments in terms of a growth in demand—but a growth which has not been great enough to remove the deficiency in total demand.

This one-sided emphasis on demand as the complete explanation of major economic trends strikes us as curious. As manufacturers we are well aware that goods are produced to be sold, and that if there is no demand for them they will not be produced. But this is only part of the story. Goods are produced to be sold at a profit. Unless there is a reasonable differential between the price which may be obtained for the goods and the cost of producing them, they will not be produced and the employment which they would have required will be eliminated. Thus a discrepancy between actual and potential output is to be explained primarily by an imbalance in cost-price relationships. Demand is one, but only one, of the forces which determine such relationships.

It is true that the demand approach could be the answer if we were willing to throw all other considerations—our international balance of payments, avoidance of domestic inflation, etc.—to the winds.

We could always inflate the currency sufficiently to raise prices and thereby widen profit margins. However, we do not believe that any such profligate and eventually self-defeating program would be seriously considered by your committee or any other responsible group. We are therefore left with the conclusion that the Council's discussion of the economic situation exclusively in terms of demand is incomplete and misleading as a guide to national policy.

The clue to understanding recent developments is found, not in demand, but in an analysis of corporate profit margins. The Council's report (pp. 114 and 115) contains tabulations of the margin for all U.S. corporations, and for manufacturing corporations, which are reproduced here:

Corporate profits after tax as percent of sales

	All corporations	Manufacturing corporations		All corporations	Manufacturing corporations
1948	5.1	5.7	1956	3.4	4.1
1949	4.1	4.6	1957	3.0	3.7
1950	5.0	5.9	1958	2.6	2.9
1951	3.8	4.2	1959	3.1	3.7
1952	3.2	3.4	1960	2.6	3.1
1953	3.2	3.5	1961	2.5	3.0
1954	3.0	3.4	1962	2.6	3.1
1955	3.6	4.3	1963	2.7	3.2

During the period of economic expansion since 1961 there has been some improvement in corporate profit margins, thus helping to sustain the expansion. We have not yet entered a period of declining margins such as presaged the economic downturn in 1957. This is an encouraging sign for the near future and suggests that the current expansion may still have some momentum left.

On the other hand, profit margins in the 1960's have remained well below those which prevailed in the mid-1950's and earlier. Herein lies the key to understanding why we have not been able to bring the unemployment rate back down to the level of approximately 4 percent which prevailed during the 1954–57 expansion. This is only the beginning of an explanation since the trends in profit margins in turn have to be explained. But it begins from a point which makes more economic sense than merely regarding unemployment as evidence of a demand gap.

FISCAL POLICY

The Council's approach to fiscal policy is in keeping with its overemphasis on demand. It starts from the premise that (p. 41) "the economic impact of a given program is best measured by its surplus or deficit at full employment income levels." A program is labeled "expansionary" to the extent that the resulting full employment deficit would be large or the surplus small. A program is regarded as "restraining" when the opposite conditions hold.

Based on this approach the Council comes to the following expression of its fiscal philosophy (p. 42): "The appropriate size of the surplus or deficit in the full employment budget depends on the strength of private demand and its responsiveness to fiscal policy. The budget must counterbalance private demand. The weaker the underlying determinants of private demand, the more expansionary the budget should be."

On its surface this has a certain appeal, but it has ominous overtones. It means that the expansionary effects of a fiscal program depend not on the level of spending or of tax collections but on the relation between the two. It clearly follows, if this is accepted, that there would be no point in attempting to cut expenditures along with the cut in taxes since the two moves would merely cancel each other's effects. This leaves us in some confusion as to the Council's attitude on the question of Government economy and the eventual elimination of the deficit.

But even if one accepts the argument thus far, a further question arises as to the relation of fiscal policy to money and credit policy. Can a Government deficit stimulate demand if it is not monetized by action of the Federal Reserve System and the banks? If the Government merely spends money it has borrowed from its own citizens, the net effect at the end of the process is to leave unchanged the quantity of money in private hands. It is hard to see how this could generate the self-multiplying increase in private demand described in the administration's reports.

If the alleged expansionary effect of a Government deficit depends on its being monetized through action of the monetary authorities, the question is on an entirely different footing. To the extent that the Federal Reserve System is prevented, by the balance-of-payments problem, inflationary threats, or other considerations, from taking action to expand the total money supply, it cannot make its essential contribution to the expansionary effects of the recommended fiscal policy. To the extent that it does have leeway for increasing the volume of money and credit, it can do so whether or not there is a deficit.

This analysis of the essential futility of a fiscal policy designed to "counterbalance private demand" does not apply to a tax reduction oriented toward a release of the restraints on incentives and the flow of capital to private enterprises. A simultaneous reduction in Government expenditures in no way offsets the beneficial effects of such a program. Also, these effects do not depend on whether the fiscal measures are accompanied by a substantial inflationary increase in the money supply. In fact, such tax reduction measures relieve some of the balance-of-payments pressure on the Federal Reserve System by making domestic investment opportunities more attractive relative to those abroad.

The tax reduction measures adopted in 1962—the depreciation guidelines and the investment credit—were of the incentive-and-capital-releasing character and undoubtedly helped to support continued economic expansion. We expect some further support of the same kind from the tax reduction bill to be enacted in 1964. But the Council's conception that the function of tax reduction is to fill in a demand gap is a false guide in the formulation of national fiscal policy. It is fallacious in theory, destructive of fiscal integrity in practice, and could be severely disappointing in application.

By contrast with the Council's "demand counterbalancing" view of the purpose of fiscal policy, we believe that the older commonsense approach is more soundly based economically. The proper function of fiscal policy is to provide the necessary Government services as economically as possible and to raise the needed funds in ways which interfere least with the operations of the private economy.

WAGE, PRICE, AND PROFIT TRENDS

In its chapter on "Price and Wage Policy for High Employment" the Council performs a useful service by calling attention to the importance of price, wage, and profit trends to our national economic prospects. It is a basic economic principle that, the higher employment costs per unit of output are in relation to prices, the less incentive there will be for employers to hire people. Since our balance-of-payments position prevents us from using monetary expansion on a massive scale to raise prices relative to costs (even if we wished to do so), the future course of labor costs must be a matter of critical concern.

In theory a corresponding danger exists that market power on the part of management might be used to raise prices arbitrarily and thereby restrict markets with a depressing effect on the economy. However, such arbitrary market power is effectively restrained by competition, enforced by the antitrust laws. Over large parts of the labor market there is no corresponding restraint on the power of labor to raise the price of its services. In any case the empirical evidence, to be presented shortly, makes it clear that the impediment to attainment of higher levels of employment has been on the labor cost side rather than a result of arbitrary increases in price. It is thus puzzling to find the Council delivering its admonitions on cost price behavior rather even handedly to both management and labor.

The record of prices, employment costs, and profits per unit of output is presented in the following table, based on U.S. Department of Commerce figures:

	Compensation of corporate employees per unit of real output [1]	Corporate profits after tax per unit of real output [1]	Implicit price index—business gross product		Compensation of corporate employees per unit of real output [1]	Corporate profits after tax per unit of real output [1]	Implicit price index—business gross product
1947	$0.56	$0.12	84.2	1957	$0.70	$0.10	107.6
1948	.58	.13	89.9	1958	.72	.08	109.4
1949	.57	.10	89.2	1959	.71	.10	111.0
1950	.56	.13	90.2	1960	.73	.09	112.1
1951	.61	.11	97.2	1961	.74	.09	113.2
1952	.64	.09	98.8	1962	.74	.09	114.0
1953	.65	.09	99.3	1963 (preliminary estimate)	.74	.10	114.5
1954	.66	.08	100.0				
1955	.64	.10	100.8				
1956	.68	.10	104.0				

[1] Real output is measured in terms of 1954 dollars.

Prices received by business rose substantially and quite persistently, from 1947 to 1957. But this was neither caused by, nor accompanied by, any increase in the profit realized per unit of output. In fact, unit profits declined from the levels reached in 1947, 1948, and 1950, although this may be discounted since these were "superheated" years. By contrast, unit labor costs increased by 25 percent between 1947 and 1957.

In more recent years, especially since 1960, there has been a high degree of stability in labor costs, profits, and prices per unit of output.

There has, however, been no reversal of the gain that labor costs made relative to profits in the earlier years. Thus profits have deteriorated in relation to prices and labor costs and this has been a primary factor in preventing the achievement of better economic performance.

To illustrate the point: In the period of low unemployment, 1955 through 1957, 6.7 cents was paid in labor cost for each cent earned in profit. For the years 1961 through 1963 the ratio increased to 8 cents of labor cost for each cent of profit realized. Herein lies a primary explanation of our inability to return, during the latter period, to the low levels of unemployment in the earlier period—the 4 percent unemployment which the administration regards as its goal.

The near stability in unit labor costs since 1960 is cause for some satisfaction. Although the relationship between labor costs and profits has not improved, neither has it grown any worse as it did progressively in the earlier postwar years.

The record of stability in labor costs has been accompanied, since early 1962, by a similar stability in the unemployment rate, which has remained in the 5.5 to 6 percent range. We have neither gained nor lost ground in respect to unemployment. This situation has a twofold lesson for us. First, it is a warning that any significant labor-cost breakthrough in 1964 could upset our hopes for a continuation of the economic rise. Second, it suggests that an actual reduction in unit labor costs would be a most helpful step toward reducing unemployment below its current levels. The best hope for attaining this is to improve the rate of growth in productivity while restraining the increase in hourly labor costs.

THE GUIDEPOSTS

The Council's proposed means for preventing any disastrous further rise in costs and prices is embodied in its "price-wage guideposts," first announced in the Council's report of 2 years ago. These guideposts are a useful if somewhat idealized tool for creating an understanding of the dangers involved in excessive wage increases. They are extremely limited in their usefulness as a tool for direct application to particular situations. The details of the market are always more complex than can be embodied in any simple formula. The guideposts are thus a description of what one might like to see happen on the average, rather than rules which provide useful guidance in concrete cases.

In fact any attempt to enforce these guideposts rigidly would lead to economic chaos. It would bring to a halt the process by which the wage-price mechanism adjusts the allocation of resources to changing economic circumstances.

The original statement of the guidepost approach listed four possible modifications, which were essentially recognitions of the adjustments to be made to the realities of the market. In this year's report the Council comments (p. 119): "These modifications of the general guideposts will apply, but it must be emphasized that they are intended to apply to only a relatively few cases."

With this our association must emphatically disagree. A man whose height is exactly equal to the average height of all men is exceptional. In the same way, an economic rule applicable to the average case is inapplicable to the vast majority of actual cases. It is for precisely that reason that we rely on market forces, rather than the calculations of central planners, to regulate our economy.

Our association views with some apprehension the statement in the Economic Report (p. 120) that: "(The administration) will not hesitate to call public attention to major private decisions—by either business or labor—that seriously overstep noninflationary price and wage standards." This threat of extra-legal economic intervention could be seriously destructive of individual freedom and of business confidence. The guideposts are too blunt an instrument to be applied in that way.

We also do not understand the Council's dictum (p. 120) that: "* * * it is appropriate to focus special attention this year on price reductions."

Our present situation has arisen as a result of wage-cost increases, rather than of the pricing practices of business, as the data previously presented demonstrate. Just why, then, should price behavior rather than wage behavior now become the focus of special attention?

Neither exhortation nor pressure by the administration provide a really workable defense against the danger to our economy resulting from possible further increases in labor cost. The problem remains, however. Its origin is in the excessive power of labor unions to impose their will regardless of market conditions. This is a problem which can only be dealt with on its own terms—by removing the special privileges, exemptions, and immunities of labor unions.

THE INCREASED OVERTIME PENALTY

In his own Economic Report (p. 13), President Johnson takes a forthright stand against reduction of the standard workweek to 35 hours. He points out that: "This would only redistribute work, not expand it."

One might add that such a step would increase the costs of production at a time when any such increase is economically dangerous. In fact, the President made exactly that point in his earlier State of the Union Message. There he stated that a 35-hour week "would sharply increase costs, would invite inflation, would impair our ability to compete and merely share instead of creating employment."

Our association is grateful to the President for setting forth so clearly his own disagreement with the fallacious arguments for solving unemployment by reduction in the statutory workweek. We are, however, concerned and puzzled that he couples this opposition with advocacy of an alternative which would have much the same effects. In his Economic Report (p. 13) the President indicates: "I shall ask for legislation authorizing higher overtime penalty rates on an industry-by-industry basis where tripartite industry committees determine that such rates could create more jobs without unduly raising costs."

It is difficult to see why this should not be regarded in the same light as the 35-hour week in that it merely shares instead of creating employment. There is nothing in such a step which would increase the total demand for man-hours of labor. Moreover in some industries it might bring about lower productivity.

The proviso that increased overtime rates would not be imposed where they would unduly raise labor costs is a recognition that they would inevitably have some effect in that direction. Just what criteria a tripartite committee would use in deciding how much of an increase would be undue is not clear. The issue in particular industries would be a source of conflict between labor and management with a third party on the committee becoming in effect the arbitrator.

The fact is that at this particular juncture any increase of labor costs, whether large or small, would have to be regarded as a negative factor in an assessment of our economic prospects. The reconciliation between the objectives of increased employment opportunities and a stable dollar both at home and abroad will be difficult at best. Every rise in internal labor costs will make it that much more difficult.

One might object that an employer could avoid the increase in costs involved in a rise in the penalty rate by cutting down on overtime and hiring additional people. But clearly this would involve higher costs (all things considered) than the employer's present arrangements—or else he would be doing it now.

Our association sincerely hopes that Congress will not enact the proposed legislation. It would open up a Pandora's box of new sources of labor-management contention and new avenues for undesirable increases in production costs.

THE WAR ON POVERTY

The most impressive fact revealed by the Council's chapter on "The Problem of Poverty in America" is the degree of progress that has already been made. As the Council itself readily agrees, its statistical criteria for classifying a family as "poor" are arbitrary and incomplete. Taking them as they are, they indicate that the percentage of all families with incomes of less than $3,000 in 1962 prices declined from 32 percent in 1947 to 20 percent in 1960. The poor are still with us but in considerably reduced numbers.

This should not be grounds for complacency. It should, however, be carefully considered for its implications in regard to the best way of achieving further progress.

It is clear that the recorded reduction in the proportion of poor families is the result of the general growth of the economy. It follows that our failure to gain even more ground against poverty is the result of the somewhat sluggish economic conditions which have prevailed in more recent years. The Council recognizes this in its statement (pp. 59 and 60): "In the decade 1947–56, when incomes were growing relatively rapidly, and unemployment was generally low, the number of poor families (with incomes below $3,000 in terms of 1962 prices) declined from 11.9 to 9.9 million, or from 32 to 23 percent of all families. But in the period from 1957 through 1962, when total growth was slower and unemployment substantially higher, the number of families living in poverty fell less rapidly * * *."

The President recognizes the lesson of this record in his own message, where he states (p. 15): "Today, as in the past, higher employment and speedier economic growth are the cornerstones of a concerted attack on poverty."

Our association can agree heartily with this assessment of the prime requirement for further progress against poverty. Our own views as to ways in which "higher employment and speedier economic growth" may be attained have been set forth in earlier sections of this statement.

The Council goes on however to say (p. 60) that: "We cannot leave the further wearing away of poverty solely to the general progress of the economy."

The hope for an acceleration of the decline in poverty is certainly a legitimate one. But we must make sure that efforts in that direction do not impede the general economic progress which is still more basic. Let's not undermine the "cornerstone" of better economic growth and higher employment, while we try to elaborate the facade.

The details of the administration's program in its war on poverty are not yet known and specific comments are therefore not in order. The Council does call for (p. 77): "* * * coordinated efforts of Federal agencies working in such fields as education, health, housing, welfare, and agriculture."

It may be pointed out that there has been no lack of such Federal programs during the years since 1957—years in which progress against poverty was slower than in the preceding period. The burden thereby placed on the economy may be, at least in part, the explanation for the slowing down of our economic growth.

Another danger to be kept in mind is that of creating new pockets of poverty through further inflation. There is no statistical information as to how many families are in the poverty category because of the erosion of their savings and the value of their fixed incomes through past inflation. The number must however be substantial, especially in families headed by older people.

It is undeniable that, no matter how much general economic progress is attained, there will still remain a residue of people who need assistance. There will always be a certain number who cannot participate in general prosperity because of their own special problems—physical or mental handicaps, family problems, and sometimes lack of motivation arising out of early environment.

Experience has shown that the "massive attacks" on such problems are not always successful—and many even backfire. Urban renewal programs, to get people out of the slums (with the expected benefits of increasing mental and physical health) have in many places intensified crowding and increased juvenile delinquency.

The approach to helping these people should be local and personalized. The individual and the family must participate in a change in motivation. What society can do is help financially—as it always has—either through private or public philanthropy.

The Council winds up by pointing out that the total cost of bringing all poor families up to the $3,000 income level they have taken as their standard would be $11 billion annually. They quite properly go on to say that merely giving the families concerned this amount of money is not an ideal solution to the problem. It would be ironic, however, if welfare programs undertaken as a cure for poverty wound up costing more than such a direct subsidy.

SUMMARY AND CONCLUSIONS

The economic outlook as of this date gives ground for moderate optimism—with the reservation that a renewed major increase in labor costs could halt or reverse the upward tend in economic activity.

Profit margins have been sustained and have even risen slightly during the past 3 years of expansion. We have as yet not seen the contraction in profit margins which occurred in the latter phases of previous expansionary periods and foreshadowed the downturn.

But profit margins remain well below the percentages which prevailed in the mid-1950's—the last period in which unemployment stood at the 4-percent level now regarded as our national goal. Since profits are the motive force which activates private economic activity, this compression of profit margins has kept our business growth below its potential and prevented a reduction in the unemployment rate below 5.5 percent.

The expected tax reduction should give some further support to a continuation of the business rise, not through its effects on total demand but through its impact on business and individual incentives and through its release of private capital for expansion of investment.

The doubtful factor in the present picture is the course of wages during 1964. Under present circumstances, any increase in unit labor costs would most probably lead to a constriction of profit margins. If severe enough this would end the business rise in 1964 and probably produce a downturn.

If hourly employment costs rise faster than productivity our hopes for a further business rise will be reduced. If hourly employment costs remain roughly in line with productivity increases, as they have during the past 3 years, we will probably see a continuation of the business expansion. Finally, if the increase in hourly employment costs is kept somewhat below the gain in productivity, our chances for making inroads on the unemployment problem are very good indeed.

We strongly urge that Congress reject the fiscal philosophy promulgated in the Report of the Council of Economic Advisers. The notion that the primary purpose of fiscal action should be to supplement aggregate demand is both futile and dangerous. It is futile because our balance-of-payments situation rules out any such oversimplified demand-expansion approach. It is dangerous because its basic logic encourages the increase in Government spending and deficits and, ultimately, inflation.

Instead we urge that the Government pursue a policy of strictest economy so as to permit tax reductions which can improve incentives and raise the profit attractiveness of business operations and business investment for growth.

There is no easy answer to the labor-cost problem. Intervention by Government in the form of extralegal pressures is not the solution. It is a form of second-guessing the operations of the market system which could have severely disruptive effects. The problem will eventually have to be dealt with at its source; which is the excessive power of labor unions to raise wage levels without regard to market conditions.

NATIONAL ASSOCIATION OF MUTUAL SAVINGS BANKS

BY DR. GROVER W. ENSLEY, EXECUTIVE VICE PRESIDENT

The Employment Act of 1946 requires that the Economic Report of the President and the Annual Report of the Council of Economic Advisors assess the Nation's economic progress, project trends in the economy and propose policies and programs "to promote maximum employment, production, and purchasing power." The reports transmitted to the Congress in January 1964 admirably fulfill this requirement.

Particularly useful to private business and financial institutions, as they lay plans for 1964 and beyond, are the economic projections. It cannot be overly stressed that these projections outline an economic picture based on the realization of explicitly stated, underlying assumptions. And they can be useful guidelines to the private business community only if the assumptions are reappraised and adjusted in the light of changing and unforeseen circumstances. In a dynamic, private enterprise economy, where thousands of business and consumer decisions are made daily, and Government programs and policies are emerging and changing, there can be no substitute for incisive, continuing analysis of our economic environment.

In this setting, I am gratified that my own economic projections and assumptions for 1964, spelled out in the attached November speech, are close to those of the President and Council. All economic observers agree that "the dependence of this year's forecasts on assumptions made about the nature and timing of the tax cuts is particularly heavy." The assumptions in the Council's report relating to the effect of tax cuts on economic growth are stated more precisely than I have seen anywhere else. While this presentation is quite valuable in assessing the President's 1964 economic projections, one wonders whether the potential effects of taxation can be so precisely gaged in our kind of economy. Every effort, of course, should be made to do so.

Our own analysis suggests that the impact of tax reduction, enacted early in 1964, will be felt most strongly in the second half of the year, principally because of lags in the responsiveness of capital spending. The effects of tax reduction probably will be felt first in increased consumer spending, particularly since, under proposed legislation, the individual income tax withholding rate will be cut from the present 18 percent to 14 percent 1 week after enactment. At the same time, unused industrial capacity will begin to be utilized more fully in important sectors and management will start planning to increase plant facilities. But it will take time to draw blueprints, obtain appropriations, and set sail. Because of these unavoidable delays, increases in capital spending resulting from tax reduction will not provide a major economic stimulus much before the end of 1964.

The timing of the tax reduction stimulus should also be considered in the light of the timing of the proposed cut in the administrative budget in the fiscal year beginning in July. Translated into GNP terms, the proposed budget reduction implies that Federal expenditures for goods and services will rise by a smaller amount in calendar 1964 than a year earlier, and that this retardation will begin to take effect after midyear.

Thus, slackening in the pace of Federal spending should begin to appear at a time when the economy is rising strongly. Rather than depressing economic activity, as some observers have feared, budget cuts will have the salutary effect of curbing inflationary pressures that may develop as business expansion accelerates. The interrelated timing of tax reduction and budget reduction might appropriately have received more attention in the reports of the President and the Council.

PROGRAMS FOR STABILITY

I am particularly pleased that the Economic Report of the Presicent and the Council report stressed the need to be watchful about the reappearance of inflationary pressures in our economy. The remarkable record of stability during the past 3 years of economic growth might well have lulled us into a sense of false security about the dangers of inflation. While I am one who does not anticipate that these dangers will be hard upon us in 1964, nevertheless, proposals for a program of economic stability are essential particularly since the extent of the stimulative effects of the proposed tax cuts must be considered uncertain.

For the longer run, moreover, as we continue to bend every effort to increase the Nation's rate of economic growth and thereby reduce continued high levels of unemployment, it is reassuring that the importance of economic stability has been emphasized as a major national economic goal. Indeed, the simultaneous achievement of maximum employment, sustainable economic growth and reasonable price stability must remain the primary objective of Federal economic policies and programs.

Price-wage policies

The implementation of a program for economic stability is not easy to achieve, however, in the framework of our private market economy. As I see it, the role of the Federal Government must be to achieve its objective with a minimum of interference in private market processes. In the area of price-wage policy, the President's emphasis on "a sense of responsibility" by the Nation's business and labor leaders is well advised. The responsibility of "market power" achieved in several sectors of industry and labor, carries with it responsibility for sound price-wage policies.

Leadership in private economic affairs demands a statesmanlike approach, no less than leadership in Government does. But the statesmanlike approach called for in the private sector is not a selfless one. Price-wage policies inimical to sustainable economic growth are inevitably harmful to the individual businessman, worker, and consumer. The tone of the President's report in calling for responsible price-wage policies is, therefore, quite appropriate, as is the detailed discussion in chapter 4 of the Council's report on "Price-Wage Policy for High Employment." I would suggest only that greater stress be placed on the significance of economic stability to each individual whether he be capitalist or laborer, lender or borrower, consumer or seller, for even though some may benefit temporarily from a period of inflation, all will lose subsequently in a prolonged economic contraction.

The critical test for Government policy is to be able to achieve an environment of relatively stable prices and wages without interfering directly in price-wage decisionmaking. The operation of a free market society—except in times of national emergency—demands that these decisions remain with private market participants. Government should shed as much light as possible on the prevailing situation by making available timely, comprehensive information on economic developments. If "an early warning system" can be developed to detect threats to price stability, this would be highly desirable. I must confess, however, to some skepticism that such a system can be developed, given our current economic intelligence. While our arsenal of statistics has vastly increased in recent years, we are still misled on occasion by the so-called leading economic indicators. In any event, I am convinced that in the area of price-wage policy, Government must walk a very narrow line between an environment of guidance and one of coercion, between moral suasion and interference.

Monetary and fiscal policy

Notwithstanding the importance of appropriate price-wage policies, the Government must place major reliance for sustaining stable economic growth on flexible monetary and fiscal policies. The key word here is *flexible* and it is reassuring to note the emphasis on this word in the President's Economic Report. Given the recognized fallibility of economic projections, our money managers must be alert to unexpected changes in domestic and international developments, shifting quickly either to active ease to stimulate lagging growth, or to less ease or tightening, to harness speculative excesses.

In the clarity of hindsight, one can point to instances of inappropriate monetary policy. But on balance the record during the past 10 years has been a good one. In the recent, especially difficult, period of balancing domestic needs with international balance-of-payments problems, moreover, the Federal Reserve has performed amazingly well.

In looking ahead, it is well to remember that many of the basic, determining forces that give impetus to financial change cannot be influenced by the monetary and debt management authorities. Actions by foreign central banks leading to increased interest rates in money market centers abroad might, for example, lead to increased U.S. dollar and gold outflows. This would, of course, weaken our balance-of-payments position and require in this country credit-tightening measures, that might not be warranted by domestic considerations alone. Clearly, the Federal Reserve and Treasury face difficult tasks in reconciling domestic growth objectives with our international responsibilities.

Voluntary saving

A soundly conceived program of economic stability, so aptly stressed in the President's Economic Report, requires recognition of the importance of voluntary saving. The realization of proposed capital expansion programs, in both the private and Government sectors, will require an increased volume of voluntary saving if inflationary pressures are to be avoided. Moreover, steadily rising saving is needed to finance Federal deficits in a noninflationary manner and to relieve upward pressure on long-term interest rates. In view of these considerations the Economic Report might appropriately have placed greater emphasis on the significance of a high rate of personal saving to the achievement of sound economic growth.

At the same time, it is gratifying that in its report to the President on 1963 activities, the Council noted the work of the President's Committee on Financial Institutions which "formulated goals and objectives of Federal policy designed to enable private financial institutions to function more effectively." The Committee, which was headed by the Chairman of the Council, concluded that:

"* * * To the extent that the availability of Federal charters led to increased competition for savings, the public would benefit from more favorable returns on amounts saved. Moreover, although an excessive multiplication of savings institutions could threaten the solvency of existing and new institutions, this danger seems remote in view of the chartering standards that now exist for other types of institutions and the standards that would presumably be applied in chartering new Federal mutual savings banks * * *. The Committee concludes that voluntary Federal charters should be available for mutual savings banks, subject to adequate supervisory standards and safeguards."

Provision for Federal charters, which would permit the nationwide expansion of mutual savings banks, would stimulate personal saving in this country. The basic economic analysis and other supporting evidence underlying this statement have been presented in the hearings on Federal Charter Legislation for Mutual Savings Banks held last October before a subcommittee of the House Banking and Currency Committee.

Experience of foreign nations indicates that government actions can effectively encourage private saving. In this country, Federal charter legislation is a prime example of constructive action which the Federal Government can take to foster higher levels of saving within the framework of our private and public institutions.

ATTACK ON POVERTY

Of the specific programs accorded special attention in the reports of the President and the Council, the attack on poverty is perhaps the most significant in terms of relieving human misery, eliminating economic waste, and fulfilling for all our people the promise of an amazingly productive economy. As indicated in these reports, the existence of widespread poverty in the midst of plenty is associated with complex economic and social factors including unemployment, inadequate education and skills, poor health conditions, and decaying urban and rural communities. Furthermore, chronic poverty reflects in some cases the introduction of new, more efficient equipment and techniques—the very basis of the unequaled productive power of the economy as a whole. The President has rightfully given strong emphasis to the need for a coordinated program to cure the cancer of poverty in American society.

With regard to inadequate education—one of the basic elements in the condition of the chronically poor—it should be borne in mind that the Federal Government has long played an important role in helping to provide improved educational opportunities for our citizens. Land grants to colleges, NYA grants during the 1930's, VA assistance to veterans of World War II and the Korean conflict, as well as recent education bills, are important examples of this longstanding Federal involvement. Some of these Federal education programs, which have had a major impact on the past, have been discontinued or are diminishing in importance. A broadened Federal education program, therefore, needs to be developed and included as a basic part of our attack on poverty, lest we slide backward in this area.

A meaningful and realistic concept of poverty should be reflected in the specific standards applied in the formulation of remedial programs. The $3,000 money income "boundary" utilized by the Council, while helpful in providing guideposts of the extent of poverty, should not be regarded as a practical criterion for specific legislative and administrative action.

Clearly, a given money income implies widely different levels of living for a retired couple than for a family with young children, for a family on a farm than for one living in a big city slum. Appropriate standards must be applied to assure the most effective use of available funds, both to prevent the exclusion from proposed programs of needy families and the inclusion of those in real financial need.

CONCLUDING COMMENT

In formulating Federal economic policies to meet the Nation's needs, the Joint Economic Committee has played a crucial role. The committee showed foresight a decade ago in undertaking basic studies which shed light on such economic issues as: the implications of automation; the importance of flexible monetary and fiscal policy; the impact of reduced armament expenditures; unit labor costs and prices; urban and rural underemployment and poverty; and Soviet and United States rates of economic growth.

It is a tribute to the committee that many of these issues are among the major problem areas on which the 1964 reports of the President and the Council are focused. It is a further tribute that the committee conducted its inquiries into these problems in the truly nonpartisan manner necessary for their solution.

The Joint Economic Committee should continue to perform a constructive role in broadening understanding of key national economic issues and formulating sound public economic policies.

(Following is the speech referred to above:)

NATIONAL BUSINESS OUTLOOK FOR 1964 UNDER VARYING TAX ASSUMPTIONS

(By Dr. Grover W. Ensley,[1] executive vice president, National Association of Mutual Savings Banks)

The national business outlook for 1964 is good. We will start 1964 with a $600 billion economy, and should see it grow steadily throughout the year. There are, as always, elements of uncertainty in the private sector and in public policy. But in spite of these imponderables, we can be reasonably sure that in the next 12 months the Nation will achieve new records of employment, production, income, investment, and consumption. These new records, moreover, will be attained in a climate of relatively stable prices and interest rates.

I would like to spell out my views on the likely course of business next year, and discuss some of the uncertainties that surround the outlook. In my judg-

[1] An address by Dr. Ensley before the business outlook conference, College of Business Administration, University of Washington, Seattle, Wash., Nov. 15, 1963.

ment, resolution of major pending issues will affect the business scene only slightly in the shortrun, but could have significant longrun results. These results may well dominate discussion of the outlook at your conference next year.

Turning now to the short-run business outlook, it should be pointed out that this is a bit early in the season for forecasters. Results of a number of important surveys of intentions and plans for next year are not yet available. Therefore, I am compelled to speak in more general terms than I would like.

With these limitations in mind, how does 1964 look by major segments: Government, including Federal, State and local; private investment, encompassing capital expenditures, inventory changes, and residential construction; and finally, consumer expenditures? Will the resulting aggregate gross national product fully utilize our labor force and industrial capacity? Will the balance-of-payments problem be eased or worsened? What will happen to prices and interest rates? What effect will a tax cut, or on the other hand, failure to reduce taxes, have on the main economic sectors and on the economy as a whole?

As I have intimated, action or inaction on the pending tax bill in the Congress probably will not materially affect the pace of business activity in the short run. Furthermore, recent improvement in the balance of payments situation, I believe, provides assurance that the Federal Reserve authorities will not be forced to take steps that might divert the domestic economy from its current upward path. As I proceed with an analysis of the various sectors of the economy, however, I will try to indicate some of the longer run effects of pursuing alternative tax and monetary policies.

Government demand is the first major category to review. Currently, Federal, State and local government expenditures account for about 21 percent of gross national product. Although the Congress has not acted on all the appropriations for the current fiscal year and the President's budget for the next year is only now being prepared, it would appear that Federal expenditures for goods and services alone in calendar 1964 will exceed 1963 by upwards of $3 billion—somewhat less than the increase in 1963 over 1962. Efforts are being made by the administration to hold outlays down. There is some flexibility in the picture, however, which would permit a speed-up in public works outlays. The Federal budget will certainly continue unbalanced, but probably not with as great a deficit as some predicted a few months ago.

State and local expenditures will increase—probably by close to $4 billion next year—as population growth makes demands on community facilities and related local services.

Private investment, which now accounts for 14 percent of national production, will also increase in the aggregate next year over the present relatively high level. These outlays are intended not so much to expand capacity, but to modernize plant and equipment in the face of keen competition. Machine tool orders through September were up 27 percent over the first 9 months of last year. Plant and equipment outlays next year, according to the McGraw-Hill survey released last week, will be up 4 percent over this year, but other informed observers predict the rise will be double that. I lean toward the higher figure because of the recent rise in profits and profit margins, improved sales, the stimulus of tax incentives provided last year, increased operating rates relative to capacity, and efforts to meet competition by improving quality and devising new products.

If the pending tax bill passes, I would foresee no appreciable immediate boost in plant and equipment outlays over the levels I have just cited. Rather, consumer demand would first increase, unused industrial capacity—now estimated at 15 percent of total capacity—would be utilized more fully in important sectors and management would start planning to increase plant facilities. But it would take time to draw blueprints, obtain appropriation, and set sail. A year hence we would start seeing results in the private investment area of a tax cut undertaken now. It would be hoped that a combination of forces would not trigger an unsustainable capital spending boom.

A word about inventories. Will private investment in this area provde a stimulus to the economy in the next year? I think not unless taxes are cut. Actually the inventory picture overall is pretty good. There will be some accumulation next year—about $4.5 billion on the basis of no tax cut—the same as this year. In recent years, business has followed a conservative inventory policy because of efforts to minimize carrying costs, ample availability of supplies, absence of inflation and improved control procedures. If taxes are cut, however, the upward thrust of consumer demand would undoubetedly accelerate inventory accumulation, particularly as the year wears on. Hopefully, tax cuts will not trigger speculative excesses in this area.

A very important segment of private investment is construction. And because of its implications for demands for lumber, the construction outlook is particularly important to the Northwest. Total construction this year will be up 5 percent over 1962. The big increase in 1963 has been in residential building, particularly apartments. The likely prospect is that there will be little change in housing starts next year compared with the 1.5 million plus expected this year. The big question is whether the momentum in apartment construction will run another year in the face of growing vacancy rates in some areas. This is a volatile area of construction activity and we are likely to have a pause soon before another upsurge occurs later in the decade to meet demands arising from the increasing importance of age groups that favor rental housing. Of increasing importance in the residential market, is the mobile home business which has grown significantly in recent years and promises to continue strong next year.

Industrial construction should increase slightly next year. Commercial office building will continue at about this year's pace, but a temporary saturation in this area may be approaching. Noncommercial building—religious, hospital, and other institutional building—is expected to be a bit better than this year.

TOTAL CONSTRUCTION

All in all, total construction in 1964 should be about 3 percent greater than in 1963. One of the major underpinning of another strong housing year in 1964 will be the continued availability of ample mortgage credit at rates and terms favorable to borrowers. With employment high, personal incomes rising, prices relatively stable, and competition among savings institutions unabated, "over-the-counter" savings should continue to grow at a fast pace next year. Thus, mortgages will continue to be in strong demand, both from traditional mortgage lenders and from such relatively new entrants into the market on a large-scale as commerical banks and pension funds. Mortgage yields are likely to show little change from their present relatively low levels. With a move toward significantly tighter money for balance of payments reasons unlikely next year, other long-term yields will probably show little change, also, although there may be some slight upward movement as the business expansion progresses throughout the year.

One of the major reasons for the abundance of long-term investment funds at relatively low interest rates in recent years has been the intense competition for savings among financial institutions. Following the change in Regulation Q in 1961, commercial banks sharply raise their rates on savings deposits. In response, other deposit-type institutions raised their rates in order to remain competitive. The result has been an unprecendented growth in savings held in these institutions and in the volume of funds they have channeled into mortgage markets.

REPROVES INTENSIFIED COMPETITION FOR SAVINGS

This intensified competition among institutions see'-ing savings has benefited savers through higher returns and borrowers through lower costs, and has tended to stimulate economic expansion. However, coming at a time of some slackening in the growth of housing demands, this aggressive competition has contributed to a disturbing deterioration in lending standards and in the quality of credit that is potentially harmful to both borrowers and lenders. To be sure, a widespread financial collapse similar to the 1930's is hardly li'-ely in view of tighter supervisory practices, the strengthening of our entire financial system during the three decades since 1933, and the powerful role of the Federal Government in preventing general economic decline. Furthermore, as long as the economy continues to grow, it will not take long for demands to catch up with the available housing supply in areas where overbuilding has occurred.

Nevertheless, continuation of the financial growthmanship recently indulged in by financial institutions could have serious consequences in individual situations. In their determination to grow fast at whatever cost, these institutions have been caught in a vicious circle. In order to attract more funds, they pay higher rates to savers. They then invest these funds in higher yielding, riskier assets in order to earn sufficient returns to attract more savers in order to grow even faster. In the face of less than buoyant credit demands and generally stable long-term interest rates, these pressures have been reflected in the steady liberalization of credit terms, the promotion of new and more liberal types of loans and, in the mortgage area, in a rising trend of delinquencies and forcclosures. These developments have caused concern in Washington, among State regulatory authorities, and among many of the institutions involved.

ADVISES SAVINGS AND LOAN ASSOCIATIONS

In passing, I might point out that mutual savings banks—and there are five excellent ones here in the Northwest—are in a far better position to withstand competitive pressure on their earnings and protective reserve positions than are other deposit-type institutions. In part, this reflects the broad, flexible investment powers of savings banks, as compared with savings and loan associations, whose investments are largely restricted to home mortgages. Operating under diversified powers savings banks are able to shift funds readily among competing investment outlets in accordance with changes in credit demands. The continuing replacement of assets acquired in earlier low-interest rate periods with higher yield assets currently available, and the greater operating efficiency of savings banks compared with savings and loans and commercial banks are additional long-run sources of competitive strength.

CONSUMER CONSUMPTION

Let us now look at the largest and most significant demand category—consumption—accounting for 64 percent of national output currently. The University of Michigan's recent survey of consumer attitudes tends to reinforce statistical evidence that consumer confidence and willingness to spend is high and likely to remain so in the months ahead. The survey particularly noted that plans to buy new cars have remained at recent high levels. It should be noted that only 25 percent of those interviewed thought taxes would be cut. Thus, if taxes were cut effective early next year, it would be reasonable to expect consumer optimism and confidence to be strengthened and outlays to increase still further.

Even without the possible additional stimulus of a tax reduction, however, the outlook for automobile and appliance sales next year is excellent. It is no secret that Detroit has put together two 7-million-car years, in terms of both sales and production, for the first time in history and that 1963 is shaping up to be the best auto year on record. Total sales, including imports, are sure to surpass the record of 7.4 million set in 1955, although sales of domestically built cars are likely to trail slightly the peak 1955 level.

The 1964 models are off to a resounding reception. Sales of autos in October were at a record seasonally adjusted annual rate of 8.4 million, and new car sales breed more sales. Some observers say a tax cut would have its major and most immediate impact on the auto industry. An early cut, they believe, would increase sales in 1964 by 600,000.

The impact of teenage pressures on the automobile market is well known by all those of my generation. The number of 17-year-olds will increase by about one million between mid-1963 and mid-1964. Kids put pressure on parents to buy a second or third car so that they can inherit the old one. If you have noticed the parking lots at any high school in the country, you will see what I mean. Another interesting phenomenon is the growing demand, by both youngsters and oldsters alike, for optional equipment on these new cars—bucket seats, electric windows, air conditioning, rear seat speakers, and the like. Although basic prices are fairly stable, customers are spending more on each unit.

The home appliance industry is also currently enjoying one of its best years in history. Consumers have been heavily in the market for such big ticket items as refrigerators, washing machines, and television sets, and for smaller appliances as well. Strong demands here reflect the growing replacement market as well as first-time purchases by newly formed families and purchases of second and third units by our more affluent families. Although there is some concern over narrowing profit margins, appliance manufacturers have voiced confidence that sales should continue to advance and that 1964 will be a banner year.

To finance these rising expenditures, consumers will continue to increase their indebtedness. Although the September rise in consumer credit was the smallest for any month this year, the high level of auto and appliance sales, together with ample availability of funds to lenders, should make for a substantial increase in consumer borrowing later this year and in 1964.

At the same time, individuals will continue to save between 7 and 7.5 percent of their disposable income, and to regard deposit-type institutions as a favored place to put these savings. Prices in wholesale and retail markets will remain relatively stable, and if inflation fears are avoided, the stock market will not significantly divert the flow of savings from deposit-type institutions. The recent increase in margin requirements by the Federal Reserve Board will help prevent speculative activity that could result in rapidly rising stock market prices.

Furthermore, as I indicated earlier, interest rates, both short- and long-term, are not likely to change materially from present levels. Rates of return on savings accounts at 4 percent or higher are likely to be maintained at many financial institutions. In this environment, the volume of funds channeled by individuals into savings accounts will continue large, although possibly somewhat smaller than the record savings flow occurring since early 1962.

To summarize prospects for these various categories of demand, I would say they add up to a $610 billion gross national product next year, assuming no tax cut. With passage of the pending tax bill effective January 1, 1964 the GNP could amount to $620 billion next year, with the difference appearing largely in the late months of the year. Gross national product in 1963 is now estimated at about $585 billion.

Thus, 1964 shapes up as a good year for the economy, whether or not taxes are cut. It may be anticipated, however, that unemployment will be at an unsatisfactory 5-percent level and that there will be unutilized industrial capacity. At best, it would appear that it will take at least another 2 years to attain the objectives of optimum use of the Nation's resources, generally meaning employment of 96 percent of the labor force and utilization of 92 percent of our physical capacity.

AREAS OF UNCERTAINTY AND PROBLEMS

The economic climate in 1964, and particularly the situation late in the year, cannot be appraised fully without further consideration of the key uncertainties and problem areas—the fate of the Administration's tax program and developments in our balance of payments. The tax reduction program represents a head-on attempt to solve the problem of inadequate domestic economic growth relative to growth of the labor force. The balance-of-payments situation, on the other hand, represents a continuing problem that, depending upon developments next year, may or may not require more drastic corrective measures than have heretofore been applied.

TAX REDUCTION: PROSPECTS AND IMPACT

With regard to the administration's tax program, there appears to be widespread agreement that a bill along the general lines of the measure approved in September by the House of Representatives will be enacted sometime in 1964. As you know, that bill provides for a total net tax reduction of $11.1 billion in two steps during 1964 and 1965. Individuals' tax bills would be reduced by an estimated $8.8 billion over the 2-year period, with about two-thirds of the rate cut effective in 1964. Corporate taxes would be reduced by an estimated $2.3 billion by 1965. A good part of the tax saving of corporations in the next several years, however, would be offset by a speedup in quarterly tax payments designed to put them on a more current basis.

The major questions regarding the tax bill now are ones of timing: when in 1964 will the bill become law and when next year will the reductions become effective—January 1, July 1, or some other date?

It is beyond human power to give you definite answers to these questions this morning, because in the political area anything can happen. I am willing to offer the guess, however, that the tax bill will probably be enacted before the next baseball season begins and that it will be effective as of January 1, 1964. I admit to being influenced in this forecast by the fact that 1964 is a year divisible by 4, and legislators may well be mindful of their need to face the electorate in November. Although President Kennedy's legislative generals still hope to get a bill through before the end of this year, the slow pace of the Senate hearings and the large number of witnesses scheduled to appear indicate that action early next year is the more likely bet. Should tax reduction be enacted in the opening months of 1964, as I believe it will, it is possible that the cuts would be made retroactive to the beginning of the year. The longer passage of the bill is deferred, however, the greater the possibility of a later date, perhaps July 1, being made the effective date.

Should taxes be reduced in the magnitude and with the timing set forth in the House bill, there is no question but that the effects will be expansionary in 1964—particularly later in the year. As I have already noted, there are strong reasons for optimism over continuance of the current moderate expansion throughout 1964 even in the absence of tax reduction, were it not for the possible adverse impact on expectations that failure to reduce taxes would bring about.

With regard to the whole longer term question of taxes and economic growth, some interesting comparisons can be made between the current reliance upon tax reduction and the policies being advocated when I began my apprenticeship in economics here three decades ago. As you will remember, many people back in the thirties felt that the American economy had attained a state of maturity in which investment opportunities were insufficient to attract all of current private savings back into the spending stream. The resulting danger of continuing high levels of unemployment and "secular stagnation" prompted massive Government spending to counteract the sharp decline in private investment. Tax cuts were not seriously considered by the Government at that time; indeed, taxes were increased to finance the additional Federal outlays. I believe that it has not been sufficiently appreciated that the present program of tax reduction to stimulate growth reflects a basic reaffirmation of the dynamic potential of the private sector of our American economy.

With developments on the tax scene likely to work in an expansionary direction, it remains to consider the likely effect of our balance-of-payments situation upon monetary policy and the pace of business expansion next year.

OUTLOOK FOR THE BALANCE OF PAYMENTS

The "balance-of-payments problem" that has come into prominence in recent years reflects, and is the result of, the role played by the U.S. dollar as a key currency in the postwar international payments system. Not only does the dollar serve as domestic money, it is widely used as international money as well—both by foreign private holders and by foreign governments, who hold large amounts of liquid dollar claims as part of their monetary reserves.

Although the United States had run moderate deficits in its balance of payments since 1950 in every year except 1957, this had caused little concern because the major problem in the early 1950's was a shortage of dollars, which our deficits helped to supply. As the decade drew to a close, however, two basic events occurred which were to exert a profound effect upon subsequent economic developments and policy in the United States. First, with the recovery of war-shattered economies abroad, world markets of the major industrial nations have grown increasingly competitive. Second, external convertibility of the currencies of most of these nations has been reestablished.

These two events meant that henceforth the United States would have to recognize the importance of international economic developments in the formulation of domestic economic policy. Of great importance of course, has been the leading role of the United States in providing economic and military assistance to foreign nations, involving heavy commitments abroad. The changed environment was reflected in our balance-of-payments deficits, which expanded sharply and averaged $3.7 billion in the 3 years 1958–60. Although some progress has been made in reducing the size of our deficits in recent years, they have still remained uncomfortably large. The new environment was also reflected in an accelerated attrition of our official gold stock, which has declined by $7.2 billion since 1958.

Although the "art of dollar defense" is still an evolving process, it is a fair statement, I believe, that the measures taken in the past 3 years have virtually precluded the possibility of successful speculative attacks on the position of the dollar.

One of the measures adopted by the United States to stem the outflow of short-term capital and slow down the rate of gold loss has been the effort to keep short-term interest rates at levels high enough to be competitive with comparable short-term rates abroad. At the same time, the monetary authorities have tried to prevent such action from raising the level of long-term rates, at a time when there is concern over the rate of our economic growth here at home and the existence of unused human and physical resources.

SUCCESSFUL POLICIES

To date, this policy has been remarkably successful. Long-term rates have moved within a relatively narrow range since early 1961 while short-term rates have increased substantially, particularly in recent months. With 3-month Treasury bills now close to 3½ percent, however, there is some question as to how much further short-term rates can be pushed up before long-term rates will be affected. Indeed, there has already been some evidence of a gradual firming of longer term rates under the slightly less easy monetary policy of recent months.

The pace of business expansion next year, and particularly the all-important sector of private investment, could be adversely affected if developments in our balance of payments led the monetary authorities to adopt a significantly tighter policy in the months ahead. These fears were given added strength when results for the second quarter of this year were published, showing that the payments deficit had risen to a record $5.1 billion annual rate.

Recent and prospective developments, however, indicate that our balance of payments will show considerable improvement in the second half of this year and throughout 1964, thus obviating the need for a more restrictive monetary policy insofar as international considerations are concerned. On the basis of current estimates, our balance-of-payments deficit apparently declined to less than $2 billion at annual rates in the third quarter. The dramatic improvement from the second quarter can be largely attributed to the effects on our international capital accounts of the "action program" announced by President Kennedy last July 18.

The higher level of short-term rates achieved in the wake of last summer's increase in the discount rate and in the rates commercial banks may pay on short-term time deposits helped to reduce the short-term capital outflow from this country from an annual rate of $2.2 billion in the second quarter to $1 billion or less in the third quarter. Moreover, the proposed interest equalization tax on foreign securities has virtually dried up the capital outflow resulting from sales of these securities, which had been at an annual rate of $2.1 billion in the second quarter. And the Government has stated that it looks for the deficit in the fourth quarter to hold near the improved level of the third quarter. Thus, it is likely that the deficit for 1963 as a whole will be about $3 billion.

With regard to balance-of-payments developments next year, there are a number of reasons for expecting continuing improvement. Measures taken in the past few years to reduce the size of the deficit, including export expansion programs and increased export and credit insurance facilities, further tying of U.S. economic aid to spending in the United States, and the negotiation of military procurement agreements with our allies designed to offset the oversea costs of our defense commitments, will continue to make inroads into the deficit.

It is ironic that perhaps the most dramatic short-run source of improvement in our international accounts could be our much maligned agricultural surpluses. The proposed $250–$300 million sale of wheat and other agricultural products to the Soviet Union and other Eastern European nations could reduce the balance-of-payments deficit significantly in the current quarter and in the opening months of 1964. Indeed, agricultural exports in general will provide a strong plus next year in our efforts to reduce the balance-of-payments deficit. Since most of these increased sales will be to countries holding large amounts of dollars, or gold, an additional effect could be to reduce the potential attrition of our gold stocks in 1964.

CONCLUSION

In conclusion, on the basis of my assumptions regarding tax reduction and the balance of payments, it appears likely that the pace of business expansion and conditions in the capital markets during most of next year will not be too much different from what they were this year.

Toward the end of 1964, however, it is quite possible that the economy may be entering a period of accelerated expansion as the effects of tax reduction on business and consumer spending decisions begin to be fully felt. With expansive factors already widely diffused throughout the economy and no serious imbalances present, the stage may be set for a rapid surge in economic activity. In the long run, tax reduction could be the spark that ignites a capital spending boom reminiscent of the mid-1950's, bringing with it an accelerated rise in production, income and employment.

Thus, a year from now, we may be concerned with a basically different set of problems than those that concern us now. It might then appear that we have passed through a transition from a period of relatively modest growth to a period of considerably more rapid expansion. Should this prove to be the case, then in late 1964 we could conceivably see a re-emergence of many of the inflationary pressures and related economic problems that characterized the mid-1950's.

But this time there will be one all-important difference for business. Competition in world markets and international capital flows relatively unimportant then, will have an increasingly important influence on Government policy and business performance. If we are to remain competitive in world markets, correct our payments deficits, and fulfill our leading role in the international payments by then, it will be imperative that reasonable wage and price policies be followed and that accelerated growth be achieved without inflationary excesses.

In this climate, the Federal Reserve will play a crucial role. Whether the economy will be able to maintain a stable and high-level growth rate in the face of the possible reappearance of inflationary forces in the late 1964 will depend in part upon the sensitivity and responsiveness of monetary policy to changes in business conditions. In retrospect, the experience of the mid-1950's, when, according to some observers, the Federal Reserve authorities waited too long and then acted too strongly to curb an expansion that had already lost its steam, shows the importance and the difficulty of precise adjustments in monetary policy. Correct decisions regarding the timing and degree of changes in monetary policy could become even more important in 1964.

In addition to the threat of an unsustainable boom, other long-run problems will remain, even in a high-growth economy. Much remains to be done, for example, in the area of specialized training and development programs designed to counteract the dislocations that technological and economic change will inevitably bring to individuals, industries, and regions. And much remains to be done in the area of mutual tariff reduction and trade negotiations to insure that the United States will be able to have access to the growing markets of Europe and Asia. Also, in the international area, a continuing effort will have to be made to strengthen the international payments system and provide for long-run international liquidity.

Thus, while there is reason for confidence in the short run, there is no reason for complacency in the longer run. The problems facing the United States in the years ahead will be serious but not insurmountable; they present a challenge that will put the good will and common sense of all Americans to the test, a challenge I am confident we will meet.

NATIONAL FARMERS UNION

By James G. Patton, National President

We appreciate the invitation to present our views on the annual Economic Report of the President and the Council of Economic Advisers. We consider the President's Council together with this committee as one of the most important instrumentalities of modern government.

Unfortunately, the committee, the Council of the President, and the Congress have not implemented the Full Employment Act of 1946. Due to the lack of action of the executive agency and the Congress, we find ourselves in a paradoxical situation with unprecedented prosperity on the one hand and millions of unemployed and poverty stricken citizens on the other. The shortcomings of the executive branch were particularly marked during the years 1953 to 1960 when leadership in the Government was transported to the dream world of laissez-faire economics. The President's Council, the Secretary of the Treasury, and the Federal Reserve Board were, during those years, completely in the dark as to the causes of economic recessions and therefore adopted remedies which has no effect whatsoever on the disease of unemployment.

However, during the last 3 years there are increasing signs that economists in Government have become aware of the administered-price system which is usually referred to as market power. The report of the President's Council in 1962 indicated that the price inflation of the 1950's was an administered-price inflation and that tinkering with the monetary machinery of the economy could not, therefore, solve the problem of recurring recessions. This committee also during the last few years has shown an awareness of our economic problems and has suggested remedies which, if enacted, will go far toward the cure of the economic disease of unemployment.

We wish particularly to commend the President and the Council of Economic Advisers for the report to which we now address ourselves. The report transmitted to the Congress in January is a milestone in economic thinking and represents a sincere attempt to come to grips with the evils of poverty and structural unemployment.

I do not need to reiterate to this committee facts that have been presented to it by means of documents and public hearings, particularly the fact that the United States during a period when the gross national product amounted to more than $600 billion. was haunted by millions of our citizens living in abject poverty at or near the starvation level. According to a report in the New York Times of January 26, there are actually 9,352,602 families with an income of less than $3,000 a year. I do not need to dwell on these statistics. The poverty situation from a humanitarian viewpoint is tragic and from an economic point of view it means that potential demand is not realized and that the economy is eventually dragged into a recession.

President Johnson is to be commended for his awareness of the poverty problem and his determination to do something about it.

We believe that steps called for in the President's Economic Report are a good beginning and that this committee and the Congress will act to alleviate the horrible conditions existing among the unemployed.

The facts of automation are well known. It is estimated that 36,500,000 new jobs must be created during the next 10 years. About 2 million workers a year, it is reported, will be replaced by automatic and electronic machines. Since 12½ million additions will be made to the labor force during the next 10 years, it is obvious that we must run very fast in order to stand still. Output increased during the years 1956–62 amounted to 20 percent; however, 1 million less workers were actually employed by the end of 1962 in manufacturing than in 1947.

The tide of automation rolls on together with increasing efficiency on American farms which adds to the unemployed pools which gravitate to the cities. A partial solution to unemployment lies on the farms and in the small towns, although recent statistics indicate that the number of displaced farmworkers has slowed down and that we may soon reach a point when farm population will cease to decline. Agriculture still contributes to the number of those unemployed.

To solve the problem of automation there must be created as an instrumentality of Government a commission on automation, technology, and employment such as the one suggested by Senator Humphrey. Our retraining program must be broadened and facilities created to implement it. Agencies of Government must take responsibility in areas where plants will be closed and workers may be laid off because of installation of automatic devices. We must somehow get one step ahead of automation so that the problem may be solved as soon as it appears. Workers should be trained in anticipation of their losing their jobs. Transportation, housing, and funds to support families must be supplied during the interim period when a worker is transferred from one job to another.

A planning agency should be set up by the President's Council to determine where plants should be built, whether raw materials and water supplies are adequate, and whether the proposed new industry or expansion of an old one fits in with the rest of the economy. We have arrived at a point where we can no longer afford to expand our economy in a haphazard and piecemeal fashion. Planning is obviously called for in the Full Employment Act of 1946 as well as measures which will keep the economy on an even keel and check and eliminate unemployment.

We commend the Council for the recommendation of measures designed to prevent administered price inflation such as existed during the 1950's. Sellers with monopoly market power must be contained. Monetary tinkering will not prevent United States Steel and other gigantic corporations from increasing prices regardless of demand. It is well known that this industry and other price-administered industries have repeatedly raised prices during periods of falling demand, thus aggravating the situation and bringing on an economic recession. There must be, if we are to act as responsible citizens, under our democratic government, some control of the economic monster which threatens the well-being of millions of our citizens. The durable goods industries have long been subjected to private price control. However, price manipulation is not limited to durable goods industries. It is practiced in the food industry by the chainstores which have extended their market power by means of vertical integration which extends all the way back to the farm.

For example, the National Tea Co. in Denver, Colo., by means of its market power and operation of processing facilities and feed lots, actually depressed the price of a thousand-pound fat steer by $70 with no reduction in the price in its retail outlets. This gigantic corporation together with its affiliates is the third largest grocery chain in the United States and has operations extending into four continents. During 1961, it is estimated that the affiliates of this gigantic food corporation realized sales of over $4 billion in the United States, Canada, Great Britain, Germany, France, Australia, and other countries. The shadow which National Tea, controlled by the Weston interests, casts on our economy and the economy of other lands is frightening.

It has been predicted by an official of the Department of Agriculture that within a relatively short time 10 or 12 food corporations will control the entire food industry of the United States. We suggest that if present trends are not reversed that a few food corporations will eventually control the food industry of every country in the world. Chainstores will be in the same relative economic position as the durable goods, price-administered industry. These trends mean that the farmer ultimately will be at the complete mercy of off-farm interests and that he will lose control of his farm. Consumer demand will be curtailed and poverty will be aggravated. It is estimated that recent price manipulation in the cattle industry has cost livestock producers more than $1 billion. Because the price reduction has not been passed on, consumers have been deprived of another billion dollars.

Tax legislation now before the Senate is relied on to pump more consumer dollars into the economy and thus increase demand. We are in accord with the purpose of this legislation. However, we feel that the administration has an inflated idea of what it will accomplish. A mere $9 billion net reduction in taxes will not solve the problem of unemployment. We have recommended to appropriate committees of the Congress that a public works program of $50 billion for a period of 5 years be immediately inaugurated. Millions of our citizens need low-cost housing, millions of our children have inadequate schools and other facilities. Teachers' salaries should be increased regardless of any religious controversy. We are confronted with massive unemployment; therefore massive remedies must be applied.

As we move into the year 1964, economists are predicting another prosperous year. However, there are signs that the long-time enemies of the working people of this country are planning measures which will automatically cancel benefits from the tax program and from other programs in the war on poverty.

Recently an article appeared in the New York Times predicting that interest rates which have been increasing for the past 6 months will be further increased. It is not generally known that interest rates and credit are rigidly controlled by a small group of men known as the Open Market Committee. The Open Market Committee, consisting of seven members of the Federal Reserve Board, appointed by the President, and five members from the Federal Reserve banks, operate in secret and often to the detriment of our economy. The Federal Reserve Board and the Open Market Committee constitute a fourth branch of Government, independent of the executive branch and of Congress.

Recently when Mr. William McChesney Martin, Chairman of the Federal Reserve Board, appeared before the House Banking and Currency Committee, he refused to say what the plans of the Board were in regard to the increase in the rate of interest. A member of the committee attempted to get Mr. Heller, Chairman of the Presidents' Economic Council, to find out what the plans of the Federal Reserve Board were. Mr. Heller promptly responded that he would not be able to find out since, under the Employment Act, it is assumed that the Federal Reserve Board is responsible to Congress; the Congressman replied that the only way that Congress would find out if monetary policies increased interest rates would be to read about it in the papers. The little colloquy before the Banking and Currency Committee gives us a clue as to how monetary policies are made by the power behind the throne. New York bankers have caused inspired stories to be published in the Wall Street Journal and the New York Times to the effect that interest rates are going up drastically during 1964.

I do not believe we can dismiss these newspaper stories. If the Federal Reserve Board plans to raise interest rates, it would be completely consistent with its past activities. Ever since its inception the Federal Reserve Board by control of the amount of money in circulation, by control of the interest rates, and by control of the discount rate has on a number of occasions plunged the country into a depression or a recession. A few examples will suffice to prove this contention.

In 1920 the Federal Reserve Board raised the discount rate 7 percent and brought about the agricultural recession. Attention is called to the attached document (app. A) in which a responsible individual stated that in January 1920 he was reliably informed that the Board planned a deflation policy which ruined 2 million farmers and hundreds of thousands of small businessmen. I have also attached another documentation, a speech made by Congressman Swing of California on the floor of the House on May 23, 1922 (app. B). This committee has documented the fact that the Federal Reserve Board brought about the recessions of 1953–54, 1957–58, and 1960 by tightening up on credit. We feel strongly that the Federal Reserve Board is planning the same thing over again. Reference to these activities of the Federal Reserve Board of many years ago may not seem applicable to the present situation but we suggest that the attitude of the members of the Federal Reserve Board has not changed. The FRB Chairman's statement before the House Banking and Currency Committee indicates that he will use the tight-credit hard-money policy in the future as he has in the past.

Several years ago the National Farmers Union supported a bill by Representative Thompson of New Jersey which would abolish the Open Market Committee and provide for representation of farmers, small businessmen, and labor on the Federal Reserve Board. We suggest that such legislation is still necessary. The monetary policy of this country must not continue to be dictated by a small group of eastern bankers, who have, as the record proves, deliberately inaugurated policies to line their pockets and to increase profits of the institutions they control. One example will suffice.

In 1950 the Morgan Guaranty & Trust Co. (the J. P. Morgan Bank) kept a daily average inventory of $1.2 billion in Government bonds. The average interest rate earned on these bonds was 1.4 percent. By 1959, the average interest rate earned had jumped 142 percent to 3.46 percent. The average interest rate charged on money lent by the Morgan bank to other agencies was jacked up from 2.15 percent in 1950 to 4.34 percent in 1959, more than 100 percent. These interest rate hikes were engineered by the Secretary of the Treasury and the Open Market Committee. Over a period of several years the Secretary of the Treasury deliberately increased interest rates by offering Government bonds at higher than the going rates. By repeatedly using this device the price of intermediate- and long-term bonds was more than doubled. The Federal Reserve as one of the partners of the tight-money high-interest-rate conspiracy used its vast power to tighten bank credit and lessen the supply of money in circulation.

There are signs that the President's Council is looking with a tolerant eye on interest rate increases. It has approved the recent activity of the Federal Reserve Board in this direction and it has excused interest rate increases by saying such action was necessary to make more funds available for mortgages and to prevent money from seeking more profitable rates in other countries. Two studies have disapproved these fallacious ideas. We call attention to a statement by Philip W. Bell, professor of economics, Haverford College, presented to this committee in August, 1962 and to a Ford Foundation survey titled "Wealth of the Nation," by John J. McCloy published in June 1959 (Library of Congress, card No. 59–12–2). These two studies indicated that high interest overseas had little relation to the outflow of gold and that individuals did not save because of high-interest rates.

In summary we approve the body of the economic report and urge the committee to approve the recommendations contained therein. We congratulate the administration in its announced war on poverty and its recognition of the administrated price problem We urge this committee to cooperate with the President in regard to various suggested programs and to see its great influence to bring about activation of them by the Congress.

APPENDIX A

EXCERPT FROM RADIO ADDRESS, FARM AND HOME HOUR, NBC, JUNE 24, 1933 (JOHN A. SIMPSON, NATIONAL PRESIDENT OF THE FARMERS EDUCATIONAL COOPERATIVE UNION OF AMERICA FROM 1930 TO MARCH 1934)

* * * In January 1920, while in Washington on business for the Oklahoma Farmers Union of which I was State president at that time, I visited John Skelton Williams, Comptroller of the Currency. We had the following conversation:

"Mr. SIMPSON. When is deflation going to begin?

"Mr. WILLIAMS. The other members of the Federal Reserve Board voted a few days ago to have it begin in May.

"Mr. SIMPSON. Don't you know that will be a calamity to this country?

"Mr. WILLIAMS. I have told the other members of the Board that it would break a lot of little banks and they cold bloodedly replied to me, 'they ought to break, there are too many of them.' I told the other members of the Board such policy would ruin lots of farmers and they just as cold bloodedly answered, 'they ought to be ruined; they are getting so prosperous they will not work.' "

Friends of the radio audience, since May 1920 when this terrible deflation policy was inaugurated, nearly 20,000 banks have closed their doors. Two million farmers have lost their homes through foreclosures and tax sales. Hundreds of chousands of small businessmen have been put out of business by bankruptcy courts. All the wars in which this Nation ever engaged; all the calamities from the elements—fires, floods, tornadoes; all the pestilence of disease in the 150 years of the life of our country; all of it combined, wars, calamities, pestilences does not equal the misery and suffering brought on the people by those selfish, covetous, greedy, grasping, international bankers through the control of the money crop of the country.

APPENDIX B

EXCERPT FROM STABILIZATION HEARINGS BEFORE HOUSE BANKING AND CURRENCY COMMITTEE ON H.R. 7895, TO AMEND FEDERAL RESERVE ACT, PART 2, APRIL 20, 1926—FEBRUARY 4, 1927, PAGE 1111

On the 23d of May 1922, the Honorable Mr. Swing of California made a speech on the floor of the House in which he made these remarks:

"I was present at a meeting of the bankers of southern California held in my district in the middle of November 1920, when W. A. Day, then deputy governor of the Federal Reserve Bank of San Francisco, spoke for the Federal Reserve bank and delivered the message which he said he was sent there to deliver. He told the bankers there assembled that they were not to loan any farmers any money for the purpose of enabling the farmer to hold any of his crop beyond harvesttime. If they did, he said, the Federal Reserve bank would refuse to rediscount a single piece of paper taken on such a transaction. He declared that all the farmers should sell all their crops at the harvesttime unless they had money of their own to finance them, as the Federal Reserve bank would do nothing toward helping the farmers hold back any part of their crop, no matter what the condition of the market.

"Mr. COOPER of Wisconsin. Did the gentleman from California hear that?

"Mr. SWING. I did. I think I was the only person present who was not a banker. This was in a way confidential advice being given by the Federal Reserve bank for the guidance of small bankers.

"I say that was the admitted declared policy of the Federal Reserve Board made by an officer of the Board delegated for the purpose of making an announcement for the information and guidance of the bankers of my district. No one could be in doubt for one minute as to what the natural, logical, and necessary consequences of such a policy would be. If the entire crop of the country is thrown on the market at the time of harvest, of course the market would be depressed."

NATIONAL FEDERATION OF INDEPENDENT UNIONS

By Don Mahon, Executive Secretary

I am presenting this statement as national executive secretary-treasurer of the National Federation of Independent Unions. I am also president of the National Brotherhood of Packinghouse & Dairy Workers. We maintain our national federation headquarters in Washington, D.C.

In commenting on the materials and recommendations contained in the 1964 Economic Report of the President, our statement is based on the attitudes expressed, and the experience of representatives of more than 2,500 unions in this country, with whom we are in direct contact.

Since these unions have been denied representation on advisory committees in the Department of Labor, and other administrative branches, we welcome this opportunity to express views we believe common to more than 50 million American workers. These workers constitute the overwhelming majority who are not presently a part of the 13 million, or less, who are cited as being represented by the other labor federation.

We find ourselves in sympathy with certain other minority groups in this country who have been given considerable lip service but little else from the standpoint of equal representation. Therefore, we appreciate this opportunity to present our views to the committee.

We are quite concerned with the reference in the President's report to: "Contributions of Business, Labor, and Government." We call your particular attention to the statement that "Average wage rate increases over the period 1961–63 have been the most modest since World War II, thereby helping to stabilize unit labor costs and improve our ability to compete with Europe and Japan." This appears to give greater weight to stabilizing unit labor costs for the purpose of competing with the cheap-labor foreign-made products from Europe and Japan rather than the providing of additional wages and benefits for American workers. Such theories contradict most of the principles underlying our system. Increased productivity as a result of more automation and the natural resources of our country, both human and scientific, should obtain a brighter future than this low level of foreign competition would imply.

FOREIGN WATCH INDUSTRY ILLUSTRATES EVILS NOW THREATENING OTHERS

Our mistrust of foreign trade panacea is based on sad experience and not on theory. We cite specifically the national and economic conditions in the American jeweled watch industry which was once quite healthy but is now a dying industry. Economic conditions in this industry continue to worsen due to imports. Over the past 10 years, the industry has suffered steady economic deterioration by the flood of imports of jeweled watch movements. During this period the Waltham Watch Co. was forced out of the jeweled watch business. Its successor, Waltham Precision Instrument Co., Inc., has been unsuccessfully attempting to compete with low-wage oversea sources for the aircraft clock requirements of our own Government. This was permitted despite the fact that it is the only American plant now tooled and manned to supply such products. This country is now left dependent on foreigners for these defense essentials. Employment at Waltham has declined from 3,000 to less than 100 people.

Forced with the same unfair import pressures, the Hamilton Watch Co. of Lancaster, Pa., in an effort to maintain its business, has itself imported jeweled watch movements which now represents 50 percent of its sales of watches. Hamilton has added to Pennsylvania's already serious economic problems with a reduction in employment from 1,400 to approximately 700 people.

A similar condition persists with Elgin National Watch Co. of Elgin, Ill., which also has 50 percent of its sales now represented by imported jeweled watch movements. This resulted in a decline of employment at Elgin from approximately 5,000 to 1,400.

At the end of 1963, employment in our American jeweled watch industry was the lowest in history with no relief in sight. These facts alone should cause grave concern to those who knew the critical shortage of such skilled workmen, needed to produce precision instruments such as bombsights, during World War II.

Similar situations in the electrical industry are resulting in elimination of worker skills and manufacturing facilities that cannot be replaced in time to avert disaster in case of national emergency. Nor when foreign imports, parts, and replacements, needed in installations previously obtained from foreign countries, are suddenly cut off by the enemy.

Another deplorable situation now threatens the great American livestock industry as well as its dependent workers in meatpacking and food-related subsidiaries. This results from the heavy imports of red meat into the United States. Some of this meat is even coming from behind the Iron Curtain where it could have been eliminated long ago under existing law. For some unexplained reason this authority has not been exercised and the amount imported is continually permitted to increase.

Most of the countries, whose products in these categories are threatening our own industry and the related workers, do not permit us to compete in their markets on a comparable basis, if at all.

Closing loopholes in our foreign trade system, such as indicated by the above, would certainly go far in removing the "long shadow" of unemployment, plus the creation of greater incentive for small, as well as big, business in this country. In this case, as all others, that which helps labor helps all Americans.

When referring to international economic activities the report of the President states that "economic policy decisions in the United States must be made increasingly in an international context." This would indicate that the plan is to sacrifice even more industry in the United States, as well as the related workers, on the same altar where the watchworkers have already been the victims and where agricultural and food-related workers' jobs are now facing destruction.

EQUITABLE ADVISORY REPRESENTATION A NECESSITY

It is evident that the suicidal practices as cited resulted from failure to give fair representation or consideration to all sectors of the economy when formulating such policy. Under terms of the Employment Act of 1946, there is a provision for consultation with "representatives of industry, agriculture, labor, consumers, State and local governments, and other groups."

As indicated in our introductory statement this representation from the standpoint of labor is entirely monopolized by the representatives from one union federation, the AFL-CIO. It claims to represent about 13 million of the more than 70 million gainfully employed workers in the United States. It would appear that the other 57 million should be represented too or at least permitted to express their views in an advisory capacity.

We agree with the President's recommendation that "to reduce the persistent high rate [of unemployment] for the unskilled and the uneducated groups demands measures to help them acquire skills and knowledge." To reduce this excessive unemployment, plus that associated with declining industries and technological advances, will require constant retraining and even relocation.

We also wish to stress that in order to encourage proper training of our youth, and to make the most of this priceless resource, positive consideration should be given to make it possible for average-income families. The exempting of college expenses and technical training costs under terms of the Internal Revenue Act would be most realistic. We believe this provision alone would create the greatest incentive. It would make possible a better education and the brighter future so desired by thousands of our young citizens. It would create more benefits for common good than all of the exemptions ever handed to millionaire philanthropists, including those of the past, present, and future.

Our brief statement is based on the experience of our working members and those in business who are constantly in contact with these everyday problems. We trust that the committee, after weighing them accordingly, will give due consideration with regard to corrective measures.

In the event that we can provide additional information on specific items we have cited, please feel free to contact our organization.

NATIONAL LEAGUE OF INSURED SAVINGS ASSOCIATIONS

WASHINGTON, D.C., *February 4, 1964*.

Hon. PAUL H. DOUGLAS,
Chairman, Joint Economic Committee,
Congress of the United States, Washington, D.C.

DEAR MR. CHAIRMAN: We are pleased with the emphasis of the Economic Report of the President on the importance of achieving "the full potential of our resources."

We are, of course, interested most of all in the sections on housing and home financing. The tax cut will help younger families with relatively small assets and incomes to meet the reduced monthly payment which the longer mortgages make possible and the tax cut will enable other families to save more. This will help provide the savings with which to finance an increased volume of housing. The tax cut therefore will create both a bigger market for housing and provide savings to finance it.

The report points out that the increase in housing activity in 1963 was due to the boom in multifamily housing units. This boom was due almost entirely to the fact that the net increase in households is now in the youngest-age groups, the groups that normally start their married life in part in multifamily units. The number of these families is continuing to increase. The number of marriages was 11 percent greater in November of 1963 than in November of 1962. Many of these young families tend to stay in multifamily units until the children start coming. So the demand for apartment houses will continue to be strong for several years at least.

The Economic Report recognizes this. It says that "the future of residential building depends heavily on the sustainability of construction of multifamily units." But it does not point out that savings and loan associations are by Federal regulation sharply restricted in their ability to help meet this need. We hope the Joint Economic Committee in reviewing the prospects for the immediate and long-range future can inquire into the possibility that savings and loans may be permitted to serve the small apartment house business as effectively as they have been serving single-family business.

We have made a detailed economic analysis of the market for the smaller multifamily apartments, which we will be glad to make available to the committee should it pursue this subject.

We were somewhat surprised to find the report stating that "outlays for residential construction are not likely to rise from the level at the end of 1963." With the increase in incomes, a reduction in taxes and the increase in marriages, it seems to the National League of Insured Savings Associations that the market for housing is bigger in 1964 than it was in 1963, and that if we are allowed to finance the units which we are capable of financing wisely, the outlays for residential constructions this year will average above the "level at the end of 1963."

Our consulting economist, Dr. Robinson Newcomb, whom you and James Knowles know, is at your service in case you wish to ask more detailed questions about the housing and community development aspects of the Economic Report and our judgments on them.

Sincerely yours,

KENNETH G. HEISLER,
Executive Director.

UNITED MINE WORKERS OF AMERICA

By W. A. Boyle, President

On behalf of the United Mine Workers of America I appreciate the opportunity to present to this committee our views on the Economic Report of the President and to comment on the economic challenges which this Nation faces.

Poverty is or should be the major concern of all Americans. It seems impossible to conceive that 35 million Americans, that is, one-fifth of our entire population, live below the minimum standard of living. Certainly the United States, with its vast resources and the relative prosperity of the majority of its citizens, will find this situation intolerable.

We applaud the determination of the President to wipe out the blight of poverty in our land. We hope that his determination will be speedily translated into effective programs, which will raise the standards of those who cannot now enjoy the affluence of our fellow citizens.

For many years the United Mine Workers of America has called attention to the danger of poverty on such a vast scale. We see in the deprivation of great numbers of our citizens a danger, not only to them but to the future of the Nation as well. We recognize and hope that there is a growing realization generally that poverty and wealth cannot exist for long in the same Nation, especially a nation that is dedicated to the promulgation of human dignity and economic justice.

Yet, the poor have remained the forgotten people in America. They have been forced from the national conscience and out of view of prosperous America. But we contend that this must end. The American dream, the treasures of our productive wealth, and the genius of our technology, must be used and enjoyed throughout the Nation, as it is in the more fortunate areas. The fathers of the underprivileged children want the same opportunities for their young as the prosperous fathers do for theirs. We cannot brag of our national opulence in the face of the gaunt and desperate faces of the poor who need our help and want the better life, but who have thus far been deprived of it. We cannot point to our adherence to the concept of human dignity while many of the aged must fear the catastrophe of a serious illness and the drain that such illness will place upon the savings of a lifetime.

Our poor are with us today just as they always have been. But they are not as evident. We have shut them up in ghettoes, or run away from them in depressed areas, or ignored them on small and substandard farms. But they remain and they challenge us to help them or face a gradual loss of all that is America.

The elimination of poverty is not merely economic. Many would have it so. But to us and to labor unions in general, poverty is a moral question as well. Poverty in our affluent society is a perversion, a crime that calls for immediate and effective remedial action. Poverty should prey upon the conscience of any who respect the moral principles of Christianity and the dedication of our Nation to these principles.

Therefore, we call for concrete programs to end poverty in our Nation. We ask for a mobilization of our national resources to any extent necessary to achieve this end. Surely a nation that has spent untold billions of dollars in the struggle against poverty around the world will not shrink from doing what must be done to wipe it out here at home where logic and justice indicate that it should not exist at all.

The outline of the President's program on poverty is not yet clear. However, we would like to offer some comments on possible approaches to the whole question which we feel will be beneficial in the overall campaign to wipe out this stigma on our society.

First, the question of poverty is structural. Therefore, the solution to it must also in a sense be structural. It is not enough to raise the gross national product or increase national income. Rather, we must approach the various poverty groups from the standpoint of their particular problem.

For example, the coal areas of this Nation suffer from a great deal of poverty. This is not new to the members of this committee or to the Nation. Yet, we do not believe that sufficient attention has been given to certain facts which in our opinion must be given serious study in any proposed program to eliminate poverty in the coal areas.

Coal lies at the foundation of these areas. Thus, the area must begin with coal and build upon it. Yet, very often just the opposite occurs. Army bases using coal convert to other fuels, often on the basis of dubious cost figures and without giving proper weight to coal's modern technology. Of course, no weight at all is given to the social cost of displacement, to the additional men who will lose employment in coal mines, and to the women and children who will suffer from want and privation.

The recent announcement by Consolidated Edison Co. of New York that they intend to import a large amount of hydroelectric power from Canada is another case in point. This hydropower will come via long-distance transmission of a new and advanced type. It will cost, from what we have been able to determine, approximately the same as a mine-mouth plant in the Appalachian area. We believe that the development of high-voltage transmission technology can be of great benefit to the Appalachian area. It can, for many reasons, form the basis for the resurgence of Appalachia. But if it is to be used merely to import the energy of a foreign nation, it will be of little value in the struggle against poverty in the coal areas.

A study recently made by the coal industry shows that the mining of coal pours more than $2 billion into the economy of America. Most of this money goes into the seven major coal-producing States, four of which are located in hard-pressed Appalachia.

We are making one fundamental point. The best way to help poverty in Appalachia, for example, is to create jobs for coal miners there. The best way to utilize the resources of the region is to start with the basic resource of that region, in this case coal, and the human resources available and build from there. It makes little sense to take steps on the one hand to help the poor in Appalachia, while on the other hand following, or allowing others to follow, policies which destroy the entire economic structure of the region and render impossible the achievement of any rational rehabilitation.

Second, we have supported and will continue to support youth training programs. To our minds the greatest waste in our wasteful society is the thousands of our young men and women who enter the work force each year without the least chance of being able to cope with its increasing complexities. These young people, for instance, the school dropouts, the sons and daughters of the poor, those who inherit from their parents the terrible legacy of poverty, constitute a longrun problem of the most serious proportions. It is one thing to see a man displaced at a relatively advanced age. But it is quite something else to consign a youth of 18 to this low level for the rest of his life, especially when all indications are that the rest of the society will continue to increase in affluence. We contend that this has the ingredients of a social problem of the worst sort, a problem that demands some type of solution.

Third, public works programs are an excellent way to help in the stimulation of depressed economies and provide them with a basis for redevelopment. We urge that the committee and those in Congress charged with the formulation of antipoverty programs consider this in their deliberations.

Fourth, medical care for the aged is a vital part of the program in the antipoverty struggle. Our "senior citizens" require some type of protection against the ruinous financial impact of disease. We believe that the medical care program of the President is sound and should be given serious consideration by Congress.

Fifth, the research and development program of the Federal Government can be and should be a vital part of the antipoverty war. Research can create new industries and provide job opportunities. Research can show the way to cheaper production methods and thus lower the cost of goods and services, making them more readily available to our citizens. Research can provide new avenues of harnessing the resources of the Nation and thus provide for a greater and more abundant life for all.

We spend billions of dollars each year on Federal research programs. Many of these programs deal with defense and with defense related activities. Others deal with programs such as nuclear power, which are to our minds in great need of review. We contend and agree strongly with the recommendation of President Johnson that some of the governmental research money might be well utilized in the pursuit of civilian technology, that will aid every American and, most importantly, those Americans who now live in the shadow of want and hopelessness.

Sixth, the UMWA strongly endorses the President's call for a revision and extension of the Fair Labor Standards Act. This law will give to many millions of Americans currently employed—but at wages so low that they cannot afford a decent standard of life—a chance to share in the overall prosperity of the Nation. It will raise the living standards of millions of Americans, men and women who cannot on their own achieve even the minimum standards enjoyed in this Nation.

Seventh, we urge the continuation and strengthening of the area redevelopment program. This program gives to the communities of the depressed areas a chance to help in their own rehabilitation. Further, it assures them of the opportunity to secure Federal help in their efforts.

Eighth, we believe that the trade policies of the United States should be so conditioned as to preserve, insofar as possible, markets for American products. We do not mean to infer that the UMWA opposes foreign trade. However, we do oppose the unwarranted dumping of low-wage waste products into coal markets, thus depriving American coal miners of wages and income. This feeling of indignation is intensified by the patent refusal of practically every foreign nation to allow American coal to enter their nations because they are able to undersell their own coal. We believe that Congress will have to establish a modicum of sanity in the foreign trade program to allow our workers to maintain their standards, while not infringing upon legitimate foreign transactions.

In this same regard, we feel that the heavy investment of American capital abroad is a danger to the future viability of our economy. We have seen in the last several years a heavy outflow of American capital abroad. This export of our capital has been accompanied by a similar export of American know-how and technology and more importantly, by the exportation of American jobs. Abroad, in the most efficient factories in the world and paying wage levels which are a fraction of domestic levels, our own American manufacturers are able to avoid high tariff walls and thus penetrate foreign markets. But they are also able to ship their excess capacity back into the United States to further add to the unemployment burden of this Nation and add to the incidence of poverty here. We do not believe that this should be allowed to continue. We feel that the time is long overdue for America to adopt the same policies toward the protection of its domestic interests as is the case in other nations. We are saying that the prime responsibility of the U.S. Government is to the citizens of the United States and we urge that the Government in the area of foreign investments exercise that responsibility with a great deal more vigor.

Ninth, we support the expansion of the food stamp plan to all of the depressed areas. This plan has proven to be extremely beneficial in the alleviation of human suffering and making food available to those people who need it most. We feel that its success fully justifies the extension of the program.

President Johnson has promised a special report on Appalachia. Therefore, we shall not make any specific comments on this section of the Nation at this time, other than the slight reference previously mentioned, pending the issuance of that report. We might point out to the members of this committee, however, that the UMWA has a deep and abiding interest in any program, no matter how constituted, which will aid in bringing that area back into the mainstream of American life. We could, if time would permit, spend a great number of hours talking about the Appalachian area, its problems and its potential. But we shall defer this discussion pending the report of the President.

The question of automation received a great deal of attention in the Economic Report of the President. As we see it, the President did two things: First, he stated that automation, or advancement in technology, is a vital part of our economic progress. Second, he recognized the need for more planning in the introduction of automation and in meeting some of the needs of the new age.

The United Mine Workers of America is well versed in the effects of rapid production improvement. I submit to this committee that because of technology, both in consumption and in production, the employment in the coal industry has dropped from more than 400,000 men in 1950 to slightly over 140,000 in 1962.

This is a factor that many people would like to foreget, not only when we discuss coal but in all phases of automation and technical change. They like to point to the good side of the coin, to the improvement in production per man-day and to the stability of the price level of the past decade in coal, an improvement which has allowed the coal industry to survive one of the most crucial periods of its existence.

We also recognize the necessity for technical improvement. We realize that improvement in production is necessary and essential, not only for increasing wage levels and living standards, but also for the survival of an industry. However, there are casualties, those who suffer because of progress. Again, this is not peculiar to coal. The impact of automation in practically every major manufacturing industry in the Nation is great. Men are being displaced, men who will not find employment again, under the present economic conditions. It is true that society benefits from the advancement of technology. But it should also be true that society is willing to accept the responsibility of aiding those men who bear the final cost of automation, the unemployed and the underemployed, the real victims of technical change.

We are suggesting that steps be taken to bridge any "cultural gap" which may develop between our usable technology and the impact of that technology upon human beings. We are saying that the human values in the question of automation are superior to the other considerations. These human values must be given primary consideration and the human equation injected into the cost factor of automation.

Remember that the United Mine Workers of America does not oppose technical change. We are, however, convinced that a part of the decision for rapid technical change should account for the human factors involved.

With this in mind, we support the Presidential concept of a broad investigation of the problem and potential of automation. We are convinced that this area requires and will come to require more and more the close relationship between labor and management and the support of Government. For example, the introduction of new machinery should take place only after a lengthy discussion of its impact between labor and management. This would presuppose that the channels of communications are open and functioning properly and that both sides are willing to look at the position of the other with open minds.

We are saying that the challenge of automation is a national one, a challenge which will tax all of resources of labor, management, and Government. We feel that the best place to start is by gathering information on the problem, realistic information, pertinent information, information which can lead to effective programs. Then, with this information in hand, all of the forces of our national life can map a program or programs which will best meet the needs of all concerned.

In line with this we firmly believe in the ability of private enterprise to solve many of the problems caused by automation. But we also recognize that automation and technical displacement is also a national problem, one that will require the resources of Government if truly effective results are to be achieved.

We have gone over the President's program on wage and price stability. We must confess to a great deal of chagrin at the program outlined there and in the section of the report of the Council of Economic Advisers dealing with this subject.

It has long been the policy of the United Mine Workers of America that truly free collective bargaining is the best way to determine wage levels in a free society. President Emeritus John L. Lewis has long urged a return to the collective bargaining table. The UMWA has used this method to secure for its membership a high wage level. We have also been able to secure for our membership an almost unparalleled hospital and pension plan, entirely apart from any Federal assistance.

This is the record and despite it, the price level of coal has actually declined over the past 10 years. The coal industry, because of mechanization, has lowered its price in an inflationary era.

The coal miner has made possible this increase in productivity. We feel that he should share in this increase to the fullest extent. We do not feel that his wage level should be tied to average national productivity increases when his superior output per man-day allows the industry to lower its price and still pay the miner a high wage level.

We might point to the market as the true determinant of price levels. For example, in the energy industry, price competition is fierce, with all three fuels vying for dominance, usually on a price basis. In fact, we know of no other basic industry, with the possible exception of agriculture, where the concept of pure competition is approached to such an extent as in the markets where bituminous coal must compete.

Thus, we do not believe that the so-called wage-price policy guidelines are sound economically. Nor do we believe that they will provide incentive for labor to increase its productivity, nor for management to invest in more advanced production techniques. And we certainly oppose the intervention of Government into the collective bargaining arrangement.

We have reviewed the entire question of the tax cut. We do not feel that a detailed analysis is necessary in the light of the great volume of material that has been written and spoken on the subject. There are, however, several comments which we feel are pertinent.

The tax cut should create demand for the products of American industry. It should place in the hands of consumers, and especially low-income consumers, money to purchase more goods and services.

Therefore, we feel that the major thrust of the tax cut should be directed toward the lower income groups, toward those who tend to spend more rapidly than others. We feel that a great deal of tax relief has already been given to industry through the accelerated depreciation schedules and through the recently enacted investment credit legislation. Thus, we believe that we must bring the consumption ability of the American people into line with the productive capacity of American industry. Unless we do this there is little need to build factories or push ahead to greater amounts of new investments.

We do not mean to infer that we oppose capital spending, business incentives, or tax reductions to business. However, we feel that this is the time to stimulate the greatest single force in our economy, the consumer, to buy the products of American industry and to utilize the 13-percent excess capacity that the President mentions in his report.

We wish next to discuss the problem of unemployment. This ties into the problem of poverty and a great many other sections of the report. However, we wish to deal with it separately because it is to our minds a pressing national problem in itself.

We have a 5½-percent unemployment rate in this Nation. This rate has remained steady for months, even though the economy has soared to the heights over the past year or so. The presence of nagging unemployment is a chronic problem, a problem that requires more than the stimulus of fiscal, monetary, or expansionistic policies.

We concur with the recommendation of the President that the unemployment compensation system be strengthened and expanded. This system has been a boon to those men and women who are thrown out of work. It has served to place a floor under consumption in times of stress and thus to act as a countercyclical force in our economy.

For many years the United Mine Workers of America has urged that unemployment compensation be paid for the duration of unemployment. We still favor that policy. We believe that a man who is out of work and who cannot find work should not be allowed to shift for himself and endure the tragedy of unemployment. With a reasonable amount of unemployment insurance he may maintain his standard of life until he is able to secure some type of work, either in his own industry or at a comparable level in another industry.

But this is not the ultimate objective. In the final analysis society must endeavor to find jobs for those who do not have them. Society must take appropriate actions to see that unemployment will be a transient thing, a passing phase in the life of the worker, a hardship with a visible ending.

The presence of a 5½-percent unemployment rate in our society is intolerable. It must not remain, although there is every reason to believe that it will, unless strong action is taken immediately.

The Congress in 1946 put itself on record as demanding full employment as a major goal of our society. We suggest that Congress and the President and all of the American people rededicate themselves to that goal and do what is necessary to achieve it. We suggest that all responsible segments of our national life recognize unwanted unemployment as a curse, a stigma which must be eliminated at all costs insofar as is possible.

Coal regions of the United States are well aware of the problem of unemployment and intimately familiar with its ravages. Many thousands of coal miners are out of work, most of them for extended periods of time. They stand as living examples of the effect of governmental neglect and the failure of the free enterprise society to provide jobs for all those seeking them.

But something must be done. We hope and we urge that it be done immediately to put these men and others so afflicted throughout the Nation back to work in a constructive manner.

The past is filled with the glory of a nation which has risen from a wilderness to the most powerful industrial nation on earth. Our people have ever been eager to meet the challenges of the unknown, of the difficult. We have prided ourselves on our ability to scale any obstacle, to meet any challenge, and to conquer any foe to our national progress. Because of this—because we met adversity and conquered it, because we recognized difficulty merely as a spur to success—we became great.

Today as we face 1964 and beyond we are confronted with many and vexing problems. We must respond to them as we have done so often in the past, by moving ahead, by bringing forth an even more glorious nation than we now possess.

UNITED STATES SAVINGS & LOAN LEAGUE

CHICAGO, ILL., *February 4, 1964.*

Senator PAUL H. DOUGLAS,
Chairman, Joint Economic Committee,
Congress of the United States, Washington, D.C.

DEAR SENATOR DOUGLAS: We appreciate greatly the opportunity of commenting on the President's Economic Report and the report of his Council of Economic Advisers. Both reports make impressive as well as pleasant reading. They provide a valuable record of the progress made by the Nation during the present business expansion. They reinforce the confidence in the economic outlook presently being exhibited by the Nation's consumers and businessmen, including savings and loan executives.

With prospects generally bright and this fact well advertised, it may be useful to consider what kinds of problems 1964 may create for the Nation's economy as it moves toward 1965. The past record of American business history indicates that we plant the seeds of a recession in the boom that precedes it. Although talk that we have overcome the business cycle and that this time it is going to be different may once again be heard, any prudent member of the older generation can well recall how many times before he has heard this siren call. We see the following areas as those places where the seeds of future recession might well be planted before the year is out:

1. *Productivity and wages.*—During 1964, 119 major collective bargaining agreements expire. With corporate profits high and rising and union membership failing to grow as rapidly as output or total employees, some labor groups may be able to drive hard bargains. The ability to keep wage increases within the bounds of productivity gains, as was the case in 1962 and 1963, may prove much more difficult in 1964. In an election year, Government may be inclined to go along with labor.

2. *Consumer prices.*—Although an upward creep of prices continues, we should note that a major portion of the gains since 1950 have occurred in a few years, 1950–51 and 1956–57. These were years when the prices of goods rose. The impending tax cut, when coupled with certain types of wage contracts and crises abroad, could restart the motors of inflation.

3. *Monetary conditions.*—Prospects of tighter money cannot be ruled out. A tax cut is an experimental rather than a tested and proven adjustment in our economic affairs. It may already be discounted, but it may not be. If it produces surprises on the plus side, then we must expect that monetary authorities will react in their traditional manner.

4. *The outside event.*—Finally, no analysis of the domestic economy would be complete without recognition of the fact that more often than not it is an event outside our shores, the crises in Suez, Vietnam, or some yet unnamed locale, that does more to shape the destiny of

the Nation than the neat and efficient projections of known forces within our shores.

SAVINGS AND HOME FINANCING, 1964

From the point of view of savings and real estate financing, the problems caused by peak levels of business activity are twofold:

1. *A slowdown in savings flows.*—Past peak years, such as 1950–51, 1955, and 1957, have seen a slowdown in gross savings inflows, an increase in withdrawals, and a significant reduction in net savings gains at financial institutions. There are signs that this situation will be duplicated in 1964. Savings associations, for example, ended 1963 with the largest deficit of loanable funds of any year in recent history. Savings inflows ran 36 percent ahead of year earlier levels during the first half of 1963, but during the second half, they just matched those of the previous year. Loan demand, however, continued to be very strong through yearend. Loan volume during the second half of the year ran 21 percent ahead of the comparable 1962 period. In addition, at yearend, future commitments were 26 percent over the same date in 1962. Life insurance companies also report heavy advance commitments for mortgages. The funds deficiency at savings and loan associations caused them to borrow from the Federal Home Loan Bank. Advances reached a peak of $4.9 billion by yearend 1963, up $1.4 billion over the level of the previous year. If 1964 turns out to be anything like 1963 in terms of homebuilding and demands for mortgage funds, the combination of new and more restrictive Federal regulations and the slowdown of savings flows may produce a surprising shortage of mortgage money and possibly higher mortgage interest rates.

2. *Home financing funds.*—A second effect of peak levels of business activity in the past has been a drying up of the pools of credit available to home financing. Typically, lenders with discretionary investment powers, such as banks and insurance companies, move away from mortgages to other investment media as aggregate demand increases. The year 1964 may well provide a real test as to whether those lenders with alternate investment opportunities, who have moved into mortgages during the past few years of credit ease, will stay in these markets or whether they will once again move funds elsewhere, essentially leaving the area to savings and loan associations.

DEMISE OF HOUSING AS A SOCIOECONOMIC PROBLEM

Persons interested in housing will find the report of the Council of Economic Advisers a particularly significant document. What is not said is even more impressive than what is said. Residential construction received only slightly more than one page of commentary in the 1964 report. Furthermore, what does appear is more a description of the current situation than a statement of concern with what the Government might and should do for housing. This lack of attention to housing programs caused us to go back and review year by year the commentary made by the Council regarding housing in its annual reports. At no time, except during the Korean crisis, was so little space given to housing in these annual reviews of the state of the economy.

Going back to the first of the Council reports, that of January 1947, we find this statement: "No subject—other than housing—received more protracted study by the Congress leading to more uniform conclusions" (Economic Report of the President, Jan. 8, 1947, p. 21). In the midyear report for the same year, the Council noted, "Housing remains, in some respects, our domestic problem No. 1" (Midyear Economic Report of the President, July 21, 1947). In most of the succeeding years, three, four, and five pages of textual analysis were accorded to housing. The high point was reached in 1954 when the Council devoted an entire chapter, seven pages of text, to housing problems and programs.

In reviewing the reports, one notes that in the late 1940's attention centered on items such as public housing, rent control, and construction costs. Concern was exhibited over the capacity of the building industry to provide suitable units in volume. During the mid-1950's, attention centered on the capacity of the financial community to provide the funds to support housing demand at low cost. By 1964, all such concerns had disappeared and for the first time terms like "adequate supply of mortgage funds at favorable interest rates," rising "rental vacancy rates," and homeowner's "vulnerability to personal misfortune" appeared. Thus, we have come a long way since World War II. In the marketplace, housing supply has caught up with and perhaps surpassed demand. Government's role and concern have naturally and properly diminished greatly.

In one sense, the homebuilding and home financing industry can take the diminution of Government interest in housing as a significant compliment to their ability, energy, and industry. One of the great domestic challenges of the postwar period has been successfully met. We have provided adequate shelter for the mass of American households deprived of this good by depression and war.

Apparently, the policy planners in Government have become convinced that this goal has been accomplished. Thus, it is reasonable to assume that housing matters can be left more fully and completely to the marketplace. The issue of mass housing will now be more economic and less socioeconomic.

There is one overriding lesson in the demise of housing as a topic for Federal attention. Congress, by relying on those techniques which maximize private participation through the marketplace and minimize governmental intervention, such as was the case with the FHA and VA programs, has employed a highly efficient way for reaching a solution to a major socioeconomic problem of the type represented by housing. Equally important is the fact that through the use of such a technique the Government can ultimately work its way out of the need to support certain market sectors as soon as supply and demand conditions permit. One reason is that through its efforts it has encouraged the development of private concerns that could and would accept the responsibilities here.

THE LEGISLATIVE RECORD

The chart submitted with this statement shows the number of bills concerned with housing introduced into Congress and the number of such proposals adopted by the Congress between 1947 and 1963.

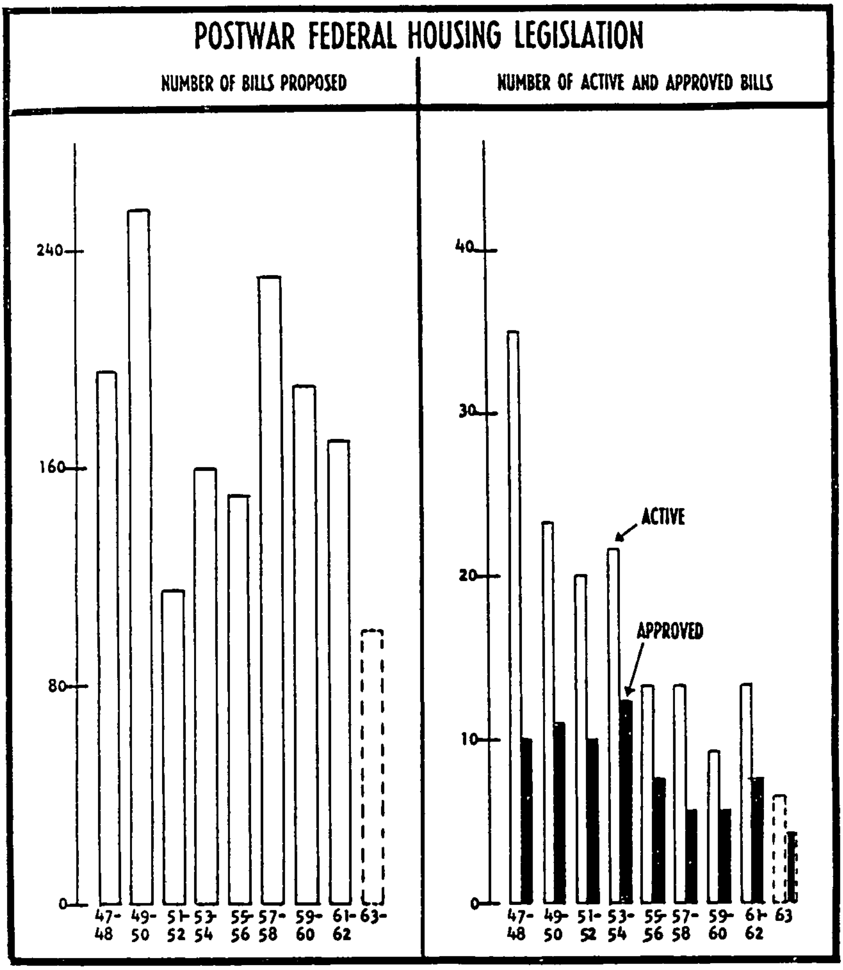
It provides an overview of congressional interest in housing during the postwar years.

The panel on the left shows the number of bills affecting housing introduced into the House and the Senate during each of the Congresses from the 80th to the 88th. The 1,500-plus bills covered a host of proposals, ranging from aid for disaster victims and control of excessive rents to appropriations for FHA. The panel on the left shows the number of bills that went beyond the committee of original reference (those listed as "active") and the number actually approved. Note that the downward trend in congressional interest in housing seems destined to hit its low in the current Congress.

As the priority given to housing matters becomes lower, hundreds of millions of dollars of expenditures might be eliminated from Federal budget totals. More and more housing matters might well be left to lower levels of government and to private individuals and groups. Funds and Government personnel required to wage an effective "war on poverty" might well be found in part in the housing agencies and in the housing budget.

Sincerely yours,

NORMAN STRUNK,
Executive Vice President.


POSTWAR FEDERAL HOUSING LEGISLATION
NUMBER OF BILLS PROPOSED
NUMBER OF ACTIVE AND APPROVED BILLS
240
160
80
0
47-48
49-50
51-52
53-54
55-56
57-58
59-60
61-62
63-
40
30
20
10
0
ACTIVE
APPROVED
63

(The following letters were received from organizations that were unable to submit statements:)

CONSUMERS UNION

MOUNT VERNON, N.Y., *February 4, 1964.*

Hon. PAUL H. DOUGLAS,
Chairman, Joint Economic Committee,
Congress of the United States,
Washington, D.C.

DEAR SENATOR DOUGLAS: Thank you for sending us a copy of the Economic Report.

I regret that Consumers Union is not in a position to comment on it at this time.

Sincerely yours,

ROBERT L. SMITH, *Assistant Director.*

MACHINERY & ALLIED PRODUCTS INSTITUTE

WASHINGTON, D.C., *January 10, 1964.*

Senator PAUL H. DOUGLAS,
Chairman, Joint Economic Committee,
Congress of the United States,
Washington, D.C.

DEAR SENATOR DOUGLAS: We greatly appreciate your letter of January 9. We would certainly be willing to prepare comments on the 1964 Economic Report of the President including the annual report of the Council of Economic Advisers, provided we can make a contribution in the light of the contents of these documents. With this in mind, we look forward to studying the materials.

Respectfully,

CHARLES W. STEWART, *President.*

WASHINGTON, *February 5, 1964.*

Mr. JAMES W. KNOWLES,
Executive Director, Joint Economic Committee,
Congress of the United States, Washington, D.C.

DEAR MR. KNOWLES: Thank you for your letter of January 17. You will recall that in my letter of January 10 to Senator Douglas we indicated that we would be willing to prepare comments on the 1964 Economic Report of the President, including the annual report of the Council of Economic Advisers, provided we could make a contribution in the light of the contents of the reports.

We have since concluded that it is not possible within the time limits for MAPI to offer useful comments and suggestions. Moreover, we observe that certain of the points covered in these documents will be the subject of special Presidential messages and perhaps specific legislative proposals, so that at a later date the ideas will be more definitively stated for study and reaction.

We greatly appreciate the opportunity which Senator Douglas and the Joint Economic Committee have provided for the Institute to review these materials and consider the possibility of presenting comments. You will recall that last year we filed a detailed statement, and I hope you will continue to keep us in mind in connection with your very important work.

Cordially,

CHARLES W. STEWART, *President.*

RAILWAY LABOR EXECUTIVES' ASSOCIATION

WASHINGTON, D.C., *February 17, 1964.*

Hon. PAUL DOUGLAS,
Chairman, Joint Economic Committee,
Congress of the United States, Washington, D.C.

DEAR SENATOR DOUGLAS: In behalf of the 24 standard railroad labor organizations, I wish to express our appreciation for your thoughtfulness in extending us an invitation to submit our views on the 1964 Economic Report of the President and the annual report of the Council of Economic Advisers.

I regret to say that the press of other matters will prevent us from taking advantage of your kind offer.

Sincerely yours,

DONALD S. BEATTIE, *Executive Secretary.*

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