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1966 JOINT ECONOMIC REPORT

REPORT

OF THE

JOINT ECONOMIC COMMITTEE CONGRESS OF THE UNITED STATES

ON THE

JANUARY 1966 ECONOMIC REPORT OF THE PRESIDENT

WITH

MINORITY AND SUPPLEMENTARY VIEWS

MARCH 17, 1966

Printed for the use of the Joint Economic Committee

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

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89TH CONGRESS 2d Session } HOUSE OF REPRESENTATIVES { REPORT No. 1334

REPORT ON THE JANUARY 1966 ECONOMIC REPORT OF THE PRESIDENT

MARCH 17, 1966.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. PATMAN, from the Joint Economic Committee, submitted the following

REPORT

together with

MINORITY AND SUPPLEMENTARY VIEWS

[Pursuant to sec. 5(a) of Public Law 304 (79th Cong.)]

INTRODUCTION

The 20th anniversary of the Employment Act was celebrated recently with a daylong symposium devoted to a review of performance under the act, and an analysis of changes and reforms that may be necessary. While it is beyond the scope of this report to discuss in detail the record of the symposium, it is highly significant that there was virtual unanimity concerning the tremendous impact that the act has had upon our economy.

The inescapable conclusion is that major recasting or amendment of the act is by no means urgently needed. While the Employment Act can be improved—like any basic legislation—the unanimous opin-

[NOTE.—Due to the pressure of other responsibilities, Senator Fulbright was unable to participate in the hearings and other committee deliberations pertaining to this report and reserves judgment on the specific recommendations made therein.]

ion was that it has and continues to function with a high degree of efficacy as is. The act not only provides for a review of past performance, programs, and policy, but also provides for a projected blueprint for executive and legislative action. It provides a tried and successful institutional framework for the coordination of economic policies to the end of maximizing employment and production within a framework of price stability and growth.

President Johnson summed up the act's efficacy in his message to the anniversary symposium:

> In developing an awareness of problems, in improving our knowledge and understanding, and in designing appropriate policies, the machinery created by the Employment Act has proved its value many times over. Hearings and reports of the Joint Economic Committee have educated the Congress and the Nation on all aspects of our economy. The advice of the Council of Economic Advisers has helped four Presidents and their administrations to propose and to carry out policies that have preserved and advanced our economic strength. And the requirement of an annual Economic Report of the President has spurred coherence and consistency in the farflung activities of the many agencies of Government, and, at the same time, made a major contribution to public understanding of economic policy.
>
> But most important of all was the spirit of the act: the recognition that all plans and policies of Government should be bent toward protecting and promoting the health of our economy.

Similar views were expressed by former President Eisenhower in these words:

> With the dedication of Government policy to full employment within the framework of an enterprise system with a stable currency that the Employment Act makes explicit, and with the facilities for shaping and evaluating policies and programs that the act created in the Joint Economic Committee and the Council of Economic Advisers, the Nation is without a doubt in a greatly strengthened position to achieve the best economic performance of which it is capable and to play a fully constructive role in the world's economy.

Clearly, one of the fundamental economic issues facing the Nation today involves the Federal Government's expenditure policy. To what extent must other programs be curtailed to cope with the increased outlays required in Vietnam? On that issue, there is a firm and reassuring consensus. Earlier reports of this committee consistently attest to our findings and confidence on this point.

Let no one, at home or abroad, doubt (1) the ability of the United States to support, if need be, simultaneous programs of military defense of freedom and economic and social progress for our people, or (2) our capacity and preference to live and grow economically without the stimulus of Government spending on national defense or a competitive arms race.

If we allow increased defense costs arising out of the Vietnam situation to seriously curtail provision of resources needed to deal with the domestic problems of poverty, misfortune, and discrimination, we may well drive those affected into opposition to the Nation's foreign policy. This would be a terrible price to pay for a lack of balance in our budgetary planning.

A related proposition stated in the President's report is especially worth emphasis:

> Production for Vietnam accounts for less than 1½ percent of our GNP. These expenditures are a part of the total demand that provides a full market for our manpower and our production. But the private demands of consumers and businesses, and high-priority civilian programs of Government, could and would provide a far more welcome market for that output if there were no war in Vietnam. Our prosperity does not depend on our military effort (p. 5).

OUTLOOK

As the American economy moves into the sixth year of uninterrupted expansion, the pace is clearly accelerating. The Council of Economic Advisers has predicted a rise in the dollar value of goods and services produced to $722 billion, which is 6.8 percent over last year's figure. Output in real terms is expected to advance by nearly 5 percent in 1966. Unemployment has dropped below the interim target of 4 percent, and the Council foresees a further drop by the end of 1966. The Council also assumed for 1966 the same rate of price rise as in 1965, when the price deflator showed a 1.8-percent increase averaged over the year.

The President indicated in his State of the Union Message that, should the necessities of Vietnam require it, he will not hesitate to return to the Congress, not only for additional appropriations but for additional revenues. In the committee's opinion, it is eminently fitting that the usefulness of tax increases to allay inflationary pressures be recognized and accepted, just as tax cuts are recognized and used as a means of reducing deflationary tendencies or a gap between actual and potential employment and production.

It appears to the committee that there are good possibilities that the economy will go beyond the $722 billion projected for 1966. There are signs that price pressures may prove stronger than the administration expected.

In view of these prospects, the signs of an increasing shiftover to a sellers' market in more and more commodities, and the increasingly vigorous surge of investment, it would be imprudent to do anything less than ready our anti-inflationary defenses, prepared to use them on short notice. As the price of complacency we could harm our long-term efforts to maintain full employment and by early neglect ultimately raise the unpleasant necessity of direct controls, such as were required during the Korean war.

In saying this, we do not belittle the views of Secretary of the Treasury Fowler and Council of Economics Advisers Chairman Ackley, who, in testifying before the committee, stressed the danger of putting on the brakes too soon or too sharply—a lesson that was learned to our loss in the 1950's. Moreover, we recognize that the major impact of the Federal expenditure increase, as contemplated in the January budget, will come in 1966 and then lessen.

However, prices have already begun to edge up more rapidly, particularly wholesale prices, which were remarkably stable over the previous 60 months. Investment intentions are moving upward with every survey that is made. Inventory accumulation is on the rise. Finally, there is an overshadowing possibility that a step-up in the Vietnam war may be forced upon us, accentuating the upward pressures on the economy.

For reasons explained in more detail below, the committee feels it would be inadvisable to depend upon monetary policy as the primary bulwark against these manifest (and threatening) inflationary pressures. The preferable solution, in our view, lies in fiscal measures and, to some extent, in selective credit restraints.

FISCAL POLICY

The President's fiscal program, formulated in December and January, was shaped in a context of monetary restraint combined with some uncertainty as to the course of events abroad and the probable extent of the economic expansion at home

Fiscal policy was consequently more moderate than many would have felt desirable even at that time. As the weeks pass, inflationary pressures are becoming more manifest, and the possibility of an early cutback in military expenditures for Vietnam is becoming more remote. At the same time restraint on the expenditure side is undernourishing social programs to aid the less fortunate in our society. We recommend, therefore, a greater reliance upon fiscal policy, including a greater readiness to provide funds needed for programs to promote social progress, cuts where expenditures are for the benefit of those already well provided for, and immediate planning to make use of further tax restraints so we can act the moment this becomes clearly necessary, as we expect it will.

Analysis of the budget figures reveals the extent to which fiscal programs in the President's budget were shaped by the uncertainties and dilemmas of December and January. Essentially, tax increases needed to stabilize the economy at full employment without inflation and sufficient funds for programs enacted in recent years to provide for social progress were both postponed with the pledge that the President would return to Congress should further funds and taxes be needed. Restraint was sought by acceleration of tax payments under existing liabilities and by the sale of financial assets, both of which have their restraining effects in an indirect manner transmitted through private financial markets. Taking both into account, about $8 billion of fiscal responsibility has been shifted over to the monetary authorities, consisting of a $3.2 billion acceleration in corporate tax payments and a $4.7 billion sale of Federal assets. Congress should consider providing authority for Government-administered trust funds to acquire such securities fully guaranteed by the Government. This would add handsomely to their income.

This $8 billion, in essentially bookkeeping type transactions, is in effect a substitute for the issuance of an equivalent amount of direct Treasury debt obligations. The proposed 1967 budget, therefore, if enacted, will be stimulating to the economy unless counteracted by monetary actions we could not accept, as indicated later in our discussion of monetary policies.

As the national economy grows in the months and years ahead, the principle of fiscal drag will reassert itself. Federal cash revenues will tend to run ahead of Federal cash expenditures. Eventually, therefore, the budget will develop sufficient restraint from the effects of the growth of the economy. For the period immediately ahead, however, we question whether it will be possible to hold the line against the inflationary pressures that seem to be developing in the short run, while such substantial stimulation is coming from Federal finances.

The committee is convinced that flexibility in fiscal policy must operate in both directions, countering recessionary influences, when appropriate, and moving to restrain total demand when inflationary excesses are clearly the dominant danger.

Unless our hopes for peace in Vietnam are realized soon, we will have to face up quickly to a need for a tax increase. On the other hand, when and if the Vietnam situation can be brought to the conference table we could confront a requirement for a quick tax reduction in the interest of economic stability.

We believe that the time has come for the appropriate committees of Congress to map out precise details of the kind of tax increase—or tax reduction—that would be warranted in either of these circumstances, although we are impressed with the increasing evidence daily that the most likely need this year will be for a tax increase, and that quickly. There are difficult questions as to the type of tax change that is most suitable, as well as its magnitude. This committee's Subcommittee on Fiscal Policy is already investigating current and future fiscal requirements and the character of the tax measures best designed for assuring this Nation a continuously stable economy in future circumstances that cannot now be fully foreseen.

At the same time, it is important that we relieve the undue strain now being put on monetary policy and the restraints on spending for social progress by immediate action on taxes as follows:

(1) A tax program should be designed and enacted immediately on a standby basis with the provision that it should come into effect whenever Congress passes, and the President signs, a joint resolution bringing it into operation.

(2) We should immediately suspend the 7-percent investment credit provision in view of the extraordinary exuberance indicated by investment programs. This is one of the major inflationary threats of this year. This action should be accompanied by a provision that the 7-percent credit would go back into effect at a fixed future date unless Congress acts to extend the suspension.

(3) There continues to be an urgent need for revision of the Federal revenue structure to broaden the tax base, improve the

fairness of our tax laws, and contribute to steady economic growth. Consideration also should be given to raising the personal exemption so as to exempt from the Federal income tax those whose income is too low to provide even a fair, decent standard of living. Such revisions are a continuing responsibility of the administration and of the tax committees of the Congress. We have urged such structural revisions to remove inequities in our taxes for some 10 years. We continue to believe they are of the most pressing importance if our tax laws are to enjoy continued public support and are to meet the test of conscience. The urgency of dealing in a timely manner with immediate tax and expenditure problems should not be allowed to divert us from removing inequities wherever they appear in the tax structure.

Taken together, these provisions should insure a noninflationary budget and one in which there would be ample room to find adequate funds for the new programs for our least fortunate citizens. This is essential since we agree fully with the President that we should not place the burdens of the Vietnam war on those least able to bear them. These burdens should be placed on those who are already well provided with the material benefits and comforts of our highly productive economy. We cannot, in good conscience, ask the poor, the sick, the aged, the infirm, nor the discriminated against, to carry the major burdens of preventing inflation in these circumstances. Programs to house and feed the poor, cure the sick, care for the aged, and break the shackles of discrimination on the economic life of the disadvantaged should have high priority. We believe that it is well within the range of possibility, with present knowledge and skills, to achieve the Employment Act objectives of full employment and stable prices without abandoning even for a moment the concern for the less fortunate to which our moral conscience calls us.

MONETARY POLICY

The committee is seriously concerned about the conduct of monetary policy in this country. Because of the precipitate action of the Federal Reserve in increasing interest rates and the interest ceiling on time deposits, we were compelled to hold special hearings in December 1965. Neither those hearings nor subsequent ones on the President's Economic Report have served to allay our fears over the lack of coordination between the administration and the Federal Reserve System.

In spite of the clear mandate in the Employment Act that all "plans, functions, and resources" be coordinated in the interest of the Employment Act's objectives, the Board of Governors of the Federal Reserve, by a 4-to-3 vote, saw fit to raise the discount rate right after the administration had made it very clear that such an increase was not warranted at that time.

While the rest of the executive branch was coordinating activities and plans preparatory to submitting them to Congress in January, the Federal Reserve went its own way.

As a byproduct of this uncoordinated monetary action, the fiscal program proposed in the fiscal 1967 budget has not only been unduly inhibited as to tax proposals but has, ironically, shifted a large added burden of some $8 billion from the responsibility of fiscal measures onto the shoulders of monetary policy. Quite apart from their merits as to public administration, the proposed budgetary offsetting of Government expenditures by reducing Government asset holdings some $4.7 billion below what they would otherwise have been, and by the acceleration in corporate income tax payments by an estimated $3.2 billion in fiscal 1967, cannot but add to the pressures on private financing in the immediate future whether as the result of temporary borrowing or the liquidation by corporations of short-term assets.

It would be most unfortunate, in our opinion, if such budgetary measures aimed at minimizing the deficit, in an otherwise potentially inflationary situation were allowed to break out in a further round of increased interest rates. It will clearly be the responsibility of the Federal Reserve authorities to adjust and supply the reserves needed for the financing of these shifts.

In the committee's view, lack of coordination in the use of the Government's principal stabilization tools is untenable in a modern, dynamic society. There should be legislation to bar any repetition.

We are far less satisfied than the Council of Economic Advisers seem to be in their report as to the adequacy of the coordination which goes on between the monetary and fiscal policy makers. The Council's report states that "effective coordination" has prevailed in the past and that consultations continue—except for the regrettable lapse in December 1965. Granting that human failures are not entirely avoidable, it is not easy for us to condone, or accept as adequate, a system of coordination which breaks down precisely when it is most needed—at a time when the economy is poised between continued and orderly expansion, possible overheating and inflation, or an unwelcome and unnecessary downturn in the rate of economic growth. The people and the Congress certainly have a right to expect better coordination of public policies than that recently witnessed.

There are other aspects of monetary policy that give the committee concern. For one thing, the December action of the Fed in raising discount rates represents one of a number of steps over the last 15 years to lift the entire structure of interest rates. In that period, interest rates have almost doubled. The effect of increases in interest rates is to redistribute income in favor of lenders and, particularly, banks. It is no accident that bank earnings have steadily risen. At the same time, millions of low-income families are increasingly burdened with interest charges. Coupled with the increased regressivity of Federal taxes, this development threatens imbalance by reducing consumer purchasing power among poorer families.

Moreover, it is much easier to raise interest rates than to lower them. When the economy again needs stimulus, as it undoubtedly will within a few years, interest rates will prove a stubborn barrier and necessitate stronger fiscal policies to offset them. Furthermore, most larger corporations are partially insulated from dependency on bank credit and the capital markets. Hence, they are less likely to be influenced by monetary policy. Yet in a period of high investment like the present, it is these large firms which should be dissuaded temporarily from some of their investments. Obviously, fiscal measures represent a more effective means of dealing with the problem than monetary measures.

At present, there is widespread expectation of further interest rate increases with all the rumors and other undesirable trappings that go with it. This creates a vicious circle. The expectation leads to anticipatory borrowing, which of course adds to credit demands and accentuates the threat of further tightening.

In the committee's opinion, there is a need to review carefully the "critical mass" monetary theory apparently followed by the Federal Reserve. We believe that this theory is false and that it is responsible in part for the Fed's historical tendency to tighten money too early and ease it too late.

The "critical mass" theory of money holds that at a certain point before inflation actually appears in the economy, even a small additional infusion of money will somehow set off an explosive expansion of credit and that an uncontrollable inflation will result. This theory has been thoroughly discredited by economists. As Governor Maisel said in commenting on the Fed's use of the "critical mass" theory before the committee:

> A large-scale credit expansion without added reserves would require peculiar types of discontinuities in our monetary system. There is no indication that they exist. They have not appeared in the past.

In fact, monetary policy is much more effective in stopping an inflation than it is in boosting us out of a depression. The Fed can always keep banks from making new loans by raising reserve requirements or selling bonds in the open market, but in a recession it is much more difficult to induce businessmen to invest by lowering interest rates. Therefore, if any bias is justified in monetary policy, all the evidence suggests that it should be toward greater caution in tightening money than in easing it. Adherence to the "critical mass" theory tends to make the Fed act as an automatic brake to the achievement of full employment by inducing it to tighten credit prematurely.

The use of general interest rate increases to fight inflation is not neutral in its effects on the economy. It tends to fall most heavily on small businessmen and on construction and other long-term investment and is not particularly effective in curbing speculative excesses.

When businessmen begin to accumulate excess inventory because of anticipated price rises, or to overinvest in plant and equipment, their profit expectations are so high that only very large interest rate increases will deter them. In these sectors of the economy interest rate increases may have an inflationary rather than a deflationary effect. On the other hand, residential construction, which we do not want to discourage, is hit much harder by higher rates.

This committee believes that it would be preferable to concentrate on a prudent and limited restriction of consumer credit as an alternative to general credit restraint. Consumer credit, we know, is not dependent on interest costs because consumers think primarily in terms of the periodic payment they are required to make and, within broad limits, are not deterred or encouraged by interest rate changes. In fact, under current practices, they usually do not know what rate they are charged—a situation which Congress should correct immediately by enacting truth-in-lending legislation.

An interest rate increase may actually have an inflationary rather than a deflationary effect in the consumer area. But the size of the downpayment and the extent of the repayment period, on the other hand, do affect the demand for consumer credit since they directly determine the size of monthly payments. Temporary and limited restraint of this sector will do far less harm than the attempt to restrain inflationary pressures by general interest rate increases, which are apt to hurt consumers generally, as well as laborers, farmers, and small businessmen, and to fall most heavily on the lower income groups.

The Federal Reserve's December action in raising the interest rate ceiling on time deposits by 37½ percent launched a major disruptive force into the flow of savings through financial intermediaries. It is impossible to foresee the extent of the dislocation and deterioration of credit that this action may cause. In the committee's view, this action emphasizes the unhealthy situation that exists in the field of financial regulation. The three Federal agencies that are responsible for pieces of the job—the Federal Reserve, the Federal Deposit Insurance Corporation, and the Comptroller of the Currency—are uncoordinated and follow no established practice even for informing each other of their proposed actions. Significantly, none of the three has to come to Congress for its funds, nor are they audited by the General Accounting Office. All are financed independently from interest on bonds held or revenues received from the regulated institutions. As a result, they are largely outside of executive direction, yet their actions have profound implications for the health of our economy, particularly in its monetary aspects.

NOTE.—Chairman Patman points out that in the case of the Federal Deposit Insurance Corporation, the limited General Accounting Office audit is highly unsatisfactory. He cites the recent report of the Comptroller General of the United States on the audit of the Federal Deposit Insurance Corporation for the year ended June 1964.

In that report, the Comptroller General states as follows: "We were unable to fully discharge our audit responsibility under the Federal Deposit Insurance Act because, except for closed banks, officials of the Corporation did not give us unrestricted access to examination reports, files, and other records maintained by the Corporation relative to the banks which it insures. This restriction made it impossible for us to evaluate the contingent adverse effect upon the financial condition of the Corporation of specific situations which may have been identified at insured banks. It also made it impossible for us to evaluate the effectiveness of bank examinations made and the degree of reliance that can be placed upon such examinations to disclose problems at insured banks."

As a result of the rise of rates in recent years, yields on U.S. bonds are higher than they have been since 1929. This poses difficulties for the Treasury because of the 4¼-percent interest ceiling on long-term obligations of the United States. Established by the second Liberty Loan Act of September 1917, this ceiling has been in effect for almost 50 years. But now, because prevailing yields are so high, the Secretary of the Treasury is forced to limit new borrowing to short-term obligations, which are not covered by the act. Obviously it is a handicap for the Treasury Department's debt-management operations to be so limited and there is already a move to lift the ceiling.

The committee believes that it would be a serious mistake to remove the longstanding ceiling on the coupon rates on public debt instruments. Its existence is a clear symbol of the Nation's intention that interest rates be restored to a more reasonable level in the future.

Should the dangers of "overheating" the economy abate, then stimulatory measures will be called for. Among these, a general lowering of interest rates should receive immediate attention. To "scrap" the present statutory ceiling under the stress of temporary circumstances would lend strength to those who, either through error or self-interest, wish to bring about permanently higher interest rates. It would work against the restoration of lower rates when the long-term interest of our economy requires them and market conditions warrant.

WAGE AND PRICE POLICIES

When the economy reaches full employment and our problem becomes one of maintaining stable prices and economic growth, private policymakers must carry an increasing share of the burden of policy formulation and execution. But this does not lessen the Government's responsibility to follow sound fiscal and monetary policies, and to prevent the injustices brought about by wage rates below a minimum standard of health and decency.

As the economy pulled out of the doldrums of the late 1950's and early 1960's, the possibility that wages and prices would get out of line brought a widespread discussion of wage-price guideposts, particularly in the reports of the Council of Economic Advisers since 1962.

These guideposts deal essentially with the problem of what kind of wage and price behavior by private individuals and organizations will best contribute to overall price stability at full employment. Full employment, stable prices, and economic growth cannot be realized year after year if private wage-price policies are inconsistent with these objectives. After all, decisionmakers are no more infallible when in private employment than when on a public payroll. But discussion of these "rules of the game" cannot be substituted for sound fiscal and monetary policies. The problems at which the guideposts are directed are essentially private, though colored with a public interest, whereas fiscal and monetary policies are public functions. We have stated elsewhere our convictions as to the necessary mix of Government programs for a noninflationary full employment economy.

Perhaps Congress might usefully assign to an existing committee, or to a newly established independent board or commission, the task of studying such issues and helping private parties come to conclusions consistent with both the public and private interest. Such a body might be empowered to make a continuing review of the guidelines and to require, on a selected basis, advance reports of wage and price decisions in industries or situations where it is likely that decisions would be of critical importance. With advance notice and facilities for advance investigation it might be able to help private policymakers of good will to reach better decisions. But we hardly think that such "jawbone" procedures alone will prevent inflation. So far as the Government has any responsibility, it is mainly to see that fiscal and monetary policies do not create the troubles.

At the same time, we are very well aware that there is always with us the problem of the marginal operator who will attempt to make a profit from exploiting workers by paying them wages far below that necessary to support individuals and families at a minimum standard of health and decency. We are convinced that caring for these cases by requiring a statutory minimum wage and extending this coverage to the maximum of our labor force is not inflationary so long as the increases are not too abrupt or extravagant—and this hardly seems likely.

Therefore we recommend that Congress at this session enact amendments to the Fair Labor Standards Act extending its coverage to as much of the labor force as possible, and provide for planned raising of the minimum wage toward a level of health and decency over the next several years.

MAINTAINING COMPETITION

Achieving full employment without inflation necessarily centers attention primarily on monetary and fiscal policy. It is easy to overemphasize the overall approach and neglect the promotion of competition and the prevention of monopoly. In this endeavor our antitrust laws play the key role.

It is disappointing that the report of the Council of Economic Advisers this year failed to return to a basic development discussed in its previous annual report, namely, the growing concentration in American industry induced by the merger movement which has spread through industry, trade, and banking.

According to the Federal Trade Commission, merger activity last year rose sharply and both the number and value of assets of large manufacturing and mining firms acquired by purchase or merger reached the highest levels on record. Mergers in the manufacturing-mining sector topped the 1,000 mark. This represented a very substantial increase over the level of merger activity in the mid-1950's, when mergers were made at the rate of about 600 per year. In the early 1950's the number ranged around 200 to 300 per year.

Most impressive is the continued upward movement in the acquisitions of large mining and manufacturing concerns. There are only some 2,400 large manufacturing and mining companies in the United

States, yet in the aggregate these large firms control over 80 percent of all manufacturing and mining assets. They thus play an important role in management decisions regarding output, investment, prices, technological innovations, and other critical factors. During the last 5 years there has been a sharply rising trend in the frequency in which large firms have been involved in mergers. Over the past 5 years, 1961–65, the number of "large" acquisitions has averaged 75 per year, with total acquired assets averaging over $2.7 billion annually. Since 1948, a total of 811 large manufacturing and mining concerns have been acquired. The assets of these firms totaled $27.1 billion at the time of their absorption through mergers with other firms.

The merger movement—in particular, the merging of large companies—is bringing about profound changes in the industrial structure of our economy. Most large acquisitions are undertaken by the top tier of already large firms. Of all large acquisitions undertaken during the past 18 years, two-thirds (in terms of aggregate assets) have been made by the 200 largest corporations.

In the meantime, concentration has been rising sharply in total manufacturing. Whereas in 1950 the 100 largest corporations held 38.6 percent of all manufacturing assets (corporate plus noncorporate), by 1962 they held 45 percent—an increase of 6.4 percentage points. The share of the 200 largest companies increased from 46.7 percent to 54.6 percent, an increase of 7.9 percentage points. In just 12 years, their share of all manufacturing assets grew by about 17 percent. At the present rate, the 200 largest corporations may control two-thirds of the total assets of American manufacturing corporations by 1975, very nearly the proportion held by the 500 largest corporations today.

Antitrust policy has dealt largely with horizontal and vertical mergers. But, as we pointed out in our 1965 report, an urgent need exists today for a clarification of public policy with respect to the conglomerate mergers. As our report stated:

> Conglomerate mergers raise basic political as well as economic questions for our society. Management and ownership have become increasingly separated in modern corporations. Managers have been able to retain earnings, often in excess of the needs of their existing businesses, even if the bulk of shareholders would have preferred to have such earnings paid out as dividends. The retained earnings may then be used for acquisition programs, extending the parent companies' operations into new areas not related to their original operations. Managements can greatly extend their control over the productive resources of our country, including the labor force, without directly increasing the real wealth of the Nation. In the process, they reduce the number of independent enterprises, and weaken an important foundation of our democracy.[1]

Conglomerate mergers can be just as anticompetitive as horizontal or vertical mergers. Conglomerate mergers often give rise to unfair advantages, for example, in securing special television advertising discounts, or enabling the combined firms to engage in reciprocity.

[1] 1965 Joint Economic Report, p. 19.

Moreover, they tend to stifle potential competition. Many leading economists have traditionally looked to the technological intervention of leading firms into each other's territory to keep industry competitive even where oligopoly prevails. With the merging of giant corporations, this potential constraint is being removed. In the real world, technological breakthroughs are no respecters of industries, so that many of the top-rung corporations are at present, or soon may be, competitors of one another. When they merge—increasing aggregate concentration in manufacturing—they may seriously stifle potential competition in the economy. Antitrust enforcement must show greater vigor in dealing with these problems.

Antitrust policy can also play an important role in implementing the wage-price guidepost program for preventing inflationary price increases. It is no coincidence that the most serious problem areas in achieving these goals have been the concentrated industries where prices are administered and do not respond freely to the forces of supply and demand.

It is pertinent to note that about 94 percent of the business firms in the United States are small businesses extending to every line of industry, commerce, and manufacturing which alone includes almost 300,000 small concerns.

It is estimated that small business provides about 30 million jobs, enough for nearly three-sevenths of the civilian labor force of this country. In addition, the programs administered by the Small Business Administration have created many thousands of new job opportunities. The new and growing company provides a vehicle for innovation and growth which keeps the economy flexible, dynamic, and competitive.

What is of equal importance is that the small business sector of our economy allows an outlet for individual initiative, invention, and ambition in the best traditions of free competitive enterprise.

The approximately 5 million such companies represent a decentralization in economic activities which is a bulwark against the concentration of economic and political power.

The small business community is thus basic not only to the functioning of the American economy but also to the preservation of the American society. The committee accordingly feels that intelligent concern and effective assistance to small business are consistent with the highest aims of the Employment Act.

HUMAN RESOURCES IN ECONOMIC GROWTH

The capabilities of human beings are the most productive force in our economy. Our most productive capital investment is accordingly in the development of our people, since this investment is the prime source of our impressive economic progress.

There is a substantial shortcoming in our economic progress. Many people have been bypassed or stunted by a material advance which has left in its wake pockets of poverty, vast urban slums, inadequate transportation, depressed areas, wasted natural resources, and polluted air and water. Such deficiencies act to impede our development, especially through their adverse effects on the development of human capabilities. Population growth and rapidly rising material production tend to widen the disparities so that they increasingly threaten the welfare of future generations.

It is to this complex of deficiencies that the Great Society is addressed—a reduction of ignorance and poverty; restoration of our cities and rural communities; improvement of our living environment and elimination of blight; and better health care. While focused on removing deficiencies, these Great Society programs nevertheless represent substantial investment because they will vastly increase our productivity, as well as improve the quality of life in the United States.

Most of these programs have been in existence for many years; for example, social security, public housing, and urban renewal. They have been given a new impetus and more coordinated design and, in some cases—notably, social security and housing—greatly expanded in scope and coverage. Others, like the Economic Opportunity Act and the Appalachian Regional Development Act, have been brought into being in the last 2 years to deal with needs that were not being met.

Legislation in the 89th Congress provided a comprehensive charter for pursuing these objectives. Federal aid to education was expanded through authorization of a 3-year program of Federal grants to school districts having a large proportion of low-income families; by establishment of community education centers, initiation of research and management assistance; and by providing a program of loans and scholarships for college students, fellowships for teachers, and other aids to college improvement.

The manpower development and training program was extended, improved, and coordinated with area redevelopment. A Department of Housing and Urban Development was established and an omnibus housing bill passed, providing for rent supplements to low-income families, expanded urban renewal, and community improvement. Several interrelated programs to improve the health of the American public were put into law. In addition to medicare—which provides hospital and medical care to people 65 years of age and older through social security—the health legislation expanded medical aid to needy individuals and increased modestly Federal grants for the indigent aged; it also provided for increased Federal aid for regional and community medical centers, professional and technical education in the medical field, and increased community health service.

The committee is gratified that this legislation relies, to the greatest possible extent, on investment in rehabilitative and developmental programs. Training, placement, community rehabilitation, and improved health care are receiving, quite properly, the major thrust. It is now important to appropriate sufficient funds to carry out this legislation.

This extensive legislation of the 89th Congress gives rise to a major challenge of effectively organizing, and supporting, these programs. Current emphasis must shift from program authorization to the establishment of a coordinated structure to carry on the tremendous task of administration. This calls for scrupulous efforts to coordinate the programs within agencies of the Federal Government. For example, manpower programs to ease the longrun transfer of population from the agricultural sector require the coordination of the Department of Agriculture, the Labor Department, and the Department of Health, Education, and Welfare. Programs to deal with depressed areas require extensive coordination of the Economic Development Administration, the Manpower Administration, and the Office of Education. In the low-income rural areas, the population may be so sparse as to make retraining inefficient. In such cases, the educational and training programs of the Labor Department might be tied to the "growth centers" that are designated by the Economic Development Administration to carry out its program.

Not only must the programs be coordinated within the Federal Government, but they also require the cooperation of State and local governments and especially of local organizations. The quality of administration will greatly influence our success as a human society for many years to come. The management of such a complex program should be a dominant concern of the administration and the Congress as well, and a major undertaking in creative federalism.

The committee believes it important to stress the fact that the incremental cost of these Great Society programs has been relatively small.

Aside from medicare, which is financed from payroll taxes through the social security trust fund, total additions to the budget for 1967 will amount to only $2.2 billion over 1966 for all these programs. Of this amount, $700 million is for health care of aged people, $500 million for education, $400 million for the poverty program, and the balance is distributed over economic development, housing, various health programs, and welfare. This $2.2 billion increase is just about 5 percent of the expected increase in gross national product over last year, and about one-fifth of the amount required for military expenditures in Vietnam.

Against this very minimal increase is the need for vast public investment. Our educational system has been undernourished for a long time and requires substantial improvement at all levels. We neglect it at the risk of cheating the generations to come. In spite of our material wealth, 32 million Americans live below a minimal poverty line, and millions of people are lacking sufficient skills to work effectively in our economy. The massive physical restoration of our cities, our land, and our lakes and rivers will eventually require outlays of billions if the job is done properly. Of course, the job does not have to be done all at once, nor should it be financed only by Federal funds. Nevertheless, it is obvious that the present Federal expenditures are merely a first stage of a growing investment, both public and private, in the development of human resources and the improvement of our environment. It is the obvious direction that the course of investment must take if we are to achieve our own destiny.

In the circumstances, to speak of our proposed rate of progress in 1967, minimal as it is, as an inflationary threat or as a luxury in view of our involvement in Vietnam, is misleading and unrealistic. The committee believes that we can do no less than is proposed in dealing with our domestic deficiencies and that, in fact, we cannot delay doing more.

Amounts appropriated for Great Society programs should be raised substantially in the years immediately ahead. The committee is impressed with the fact that failure to move promptly and effectively will not only lead to increasing imbalance in our economic progress, but also act increasingly as a brake on our rate of advance.

There is need for much more knowledge than is presently available on the whole subject of human resource investment. We need to know more about the size of the job that has to be done, the availability of resources to do it, the cost of various alternatives, and their effects on the productivity and growth of the economy. This subject area unfortunately is largely uncharted, and obtaining answers requires long, hard, patient, and imaginative analysis. Impressed with the urgency of our need for enlightenment, the committee, through its Subcommittee on Economic Progress, has begun its own inquiry. As a first phase, the subcommittee is endeavoring to project the development of Great Society programs over the next 5 years and assess the probable impact on the U.S. economy.

The present period, characterized by rising demand and dwindling supply of skilled labor, is the appropriate time for a major effort to revitalize and expand our retraining and vocational education activities. The achievement of maximum employment has two basic preconditions: higher economic demand and prompt, effective relief of labor shortages. In spite of the great progress that has been made by this Nation under the Employment Act, we need more effective ways to bring productive employment within the reach of millions of disadvantaged people.

One of the crucial shortage sectors is that of medical care. Effective demand has risen rapidly in recent years by reason of improved quality of services, increased availability of health facilities, and increased incomes. As a result, health services have been in short supply. The advent of medicare will unquestionably accentuate this shortage. Even though some expenditures under medicare will replace private outlays by older people, a substantial percentage will be additive and thus increase effective demand. The increased tightening will be relieved partly by Government efforts to improve facilities and services and to expand training. There still exists a most challenging problem, not only of increasing personnel and facilities, but also of greatly improving efficiency and effectiveness. It will tax the creativity and resourcefulness of both private and public officials in the medical care field.

Although great strides are being made to equalize opportunities for education, the task has just begun. Such equality of opportunity clearly does not exist when expenditures per pupil in some States are half of those in other States, and when school resources within some urban districts are a disgrace to all for which America stands. All other programs directed toward the poor in both rural and urban areas depend on educating the youth for any lasting success. Fortunately, the recognition of the great productivity of investment in education is beginning to call forth the same kind of creative imagination and ingenuity that has characterized the management of nonhuman capital. A substantial and much needed spurt of energy is now going into the development of more efficient techniques for teaching the disadvantaged groups in our population. This development must be encouraged.

INCOME MAINTENANCE

Growth of public support for income maintenance attests to a recognition by Americans that the care of those who are unable to participate fully in the economic life of the Nation is a public responsibility.

Transfers of income from higher income families to lower income families through organized public and private programs of income maintenance and social welfare expenditures totaled $46.8 billion in 1965. These transfers now represent 8 percent of the value of gross national product. Public programs account for 85 percent of such income transfers, and private programs make up the remaining 15 percent. Private transfer programs enjoy substantial tax benefits and, in addition, Federal and State tax systems extend direct tax advantages to the income of those families whose earning power is limited by age and infirmity or spread thin in supporting a large number of nonearners.

Many questions have been raised about the income maintenance system which we have developed over the years. It is argued that the structure is ill coordinated, that the distribution of burdens and benefits is capricious, that the operation of the system interferes with efficient resource allocation, and that the programs are costly to administer. Further, it is contended that the way in which people share in the benefits of retirement programs and tax advantages depends in highly arbitrary ways upon accidents of employment histories, the size of total income, the proportion of total income that is property income, military service, and marital status. An appropriate subcommittee of the Joint Economic Committee will undertake a study of these programs when time and resources permit. The study will consider, among other things, the number of recent proposals for a guaranteed floor income, the relative roles of public and private pension systems, and the various tax benefits which existing law affords private income maintenance programs and the income of the poor.

INTERNATIONAL TRADE AND FINANCE

As this committee has pointed out in the past, there are serious inadequacies in the international adjustment mechanism for correcting imbalances in international payments. Domestic policies to promote maximum employment and price stability prevent free market forces from producing the inflation or deflation that traditionally were supposed to maintain international equilibrium. Pursuit of domestic objectives has served to intensify problems of international balance.

Reluctance by other nations to adopt a mix of domestic policies that would better serve the objectives of international equilibrium has resulted in a particularly heavy burden for the United States and Britain as deficit countries. Hence the need for special constraints by the United States to reduce its deficits.

During the year, the committee, through its Subcommittee on Economic Statistics, has labored to clarify the important question of measuring a balance-of-payments deficit (or surplus). As pointed out in the subcommittee's report of July 1965, on the "Balance-of-Payments Statistics of the United States," the balance of payments can be measured in various ways, depending on the objectives of analysis. It was recommended that the Government show two measures. One is the "official settlements" measure, based only on the transactions of central banks and other Government institutions. The second measure includes both official transactions and changes in the amount of short-term private claims against the United States. As the name implies, the official settlements basis reflects changes during the period in the total of claims immediately realizable against U.S. gold. The liquidity measure reflects, on the other hand, the amount of potential claims, including those immediately realizable and those which may prospectively come into official hands.

In this regard, it is important to note that, in the absence of other means of providing growth in international currency reserves, businessmen and private institutions have to hold dollars—the strongest currency in the period since World War II—for use as reserves and working balances. These dollar balances would not normally be "cashed in" for gold, provided their growth is not excessive. For this reason, many experts feel that the official settlements basis of measuring the deficit more truly reflects the vulnerability of U.S. gold.

During 1965, the deficit increased slightly over its 1964 level to $1.4 billion, according to the official settlements measure. However, the liquidity measure shows a sharp drop in the deficit from $2.8 to $1.3 billion. What this means is that there has been a halt in the buildup of privately held dollar claims, but not in the dollar claims held by central banks.

The deficit in the U.S. balance of payments is somewhat abnormal in its causes. Traditional imbalances have been caused by unfavorable trade, that is, by buying more goods abroad than the Nation sold to others. The reverse is true in our case. We have a substantial trade surplus and we earn $5 billion a year on foreign investments. The factors which throw our payments balance into deficit are our heavy military expenditures overseas and the fact that at the present time our businessmen are investing heavily in Europe.

To restore equilibrium the administration has adopted direct, selective restraints on capital flows. In the past year, the interest-equalization tax, which raises the effective interest rate for foreign borrowing in the United States, was broadened in scope and extended, and a voluntary credit restraint program was begun.

Under this program, U.S. banks and other financial institutions were asked to observe appropriate guidelines with respect to their foreign operations. Banks were asked by the Federal Reserve System to limit the increase in their claims on foreigners in 1965 to 5 percent of the value of their outstanding foreign credits as of December 31, 1964. Top priority was to be assigned to bona fide export credits, and second priority to credits to less developed countries. A related program was applied to credits and investments abroad by nonbank financial institutions.

Under the part of the program administered by the Department of Commerce, about 500 large nonfinancial corporations were asked to make a maximum effort to expand the net balance of (*a*) their exports of goods and services plus (*b*) their repatriation of earnings from the developed countries less (*c*) their capital outflows to such countries. They were also asked to bring liquid funds back to the United States.

Both proved successful in reversing the outflow of short-term private capital, which shifted from an outflow of $2.1 billion in 1964 to an inflow of approximately $1 billion in 1965. The net outflow of funds for long-term direct investment, however, continued to rise. The President's Economic Report correctly singles out this sector for concentrated attention and the committee supports the proposed extension of the voluntary guidelines program into this area.

In pursuing the objectives of equilibrium in our balance of payments, the committee believes that the administration should continue to employ a policy of selective measures.

Domestic economic growth and achievement of high employment must not be sacrificed to traditional, deflationary balance-of-payments remedies. The committee is particularly impressed with the importance of this precept, not only because of the paramount importance of domestic prosperity, but because our studies indicate that interest rate increases are not an important determinant of international capital movements. Furthermore, whatever influence they do have is on the flow of short-term private capital funds, and this flow has already been reversed by the selective measures adopted. Selective measures must be continued, not only in the form of the restrictions discussed above, but positive ones as well: promotion of travel in the United States, continued stimulation of exports, reduction of nonessential U.S. Government expenditures abroad, and, finally, encouragement through tax and other incentives of foreign investment in this country.

The nations of the world need an expanding supply of international currency, just as an expansion of currency is needed domestically to accommodate rising incomes and production. Unfortunately, there is no adequate mechanism for providing either growth or flexibility to international reserves.

Traditionally, gold, supplemented by the pound and the dollar, has provided the means for expanding international reserves. But the annual gold increase is much too small to serve this objective and there are grave shortcomings to continued reliance upon dollars or pounds for growth in international reserves. Under this system, the growth of international reserves requires that "banker" nations incur continuing deficits, but this condition could lead to a loss of confidence in these currencies which reduces their desirability as international reserves.

In August 1965, Secretary Fowler announced:

> * * * The United States now stands prepared to attend and participate in an international monetary conference

that would consider what steps we might jointly take to secure substantial improvements in international monetary arrangements.

Last November negotiations were begun in the Group of Ten.

It would be premature for this committee to undertake now to set forth a blueprint for a reformed international monetary system. The Subcommittee on International Exchange and Payments last August did recommend certain basic guidelines that should govern the international deliberations.

It was urged that the United States seek neither to expand nor reduce the international role of the dollar, and at the same time work for creation of a new reserve that would not require conversion of existing balances into either gold or a new reserve medium.

It was also urged that new arrangements be carried out under the International Monetary Fund, which has eminently justified itself as the international monetary institution. Moreover, it was recommended that the new method of reserve creation combine agreed minimum annual increases with supplements to be determined by annual decision.

Other recommendations were that newly created reserves be distributed to all Fund members who qualify under criteria that are applicable equally to all countries; that the new reserves not be used as a primary foreign aid device; that the Fund's conditional credit facilities be expanded at the same time that new reserves are created; and that the structure of the Fund's quotas be improved. The committee also reiterates its previous recommendation that consideration be given to broadening the limits of permissible exchange rate variations. This would permit exchange rate variations to play a more important role in the adjustment process than is now possible and would discourage speculation by increasing the risk of loss relative to possibilities for profit. An additional result would be to give monetary authorities greater freedom to pursue independent domestic monetary policies without triggering short-term capital movements.

Successful completion of the Kennedy Round trade negotiations is of the utmost importance.

We are mindful of the fact that restrictions on the international flow of capital are not healthy in the long run, either for us or for other nations. Such restrictions interfere with the most productive allocation of resources. But, with the heavy burdens of our overseas military establishment and foreign aid, it is vitally important, if we are to discard these restrictions, that our trade balance be increased. If European nations, particularly France, continue to impose artificial barriers on our exports, it will force us to continue restrictions on capital outflow. In fact, some of the necessity for capital restrictions derives directly from restrictions on our exports. American companies which are frustrated by trade barriers find it necessary to establish plants behind the foreign tariff walls in order to sell their products, thus adding to the normal capital flow.

It is most unfortunate that tariff negotiations have thus far been delayed. The United States must negotiate vigorously for resolving the dispute and permitting the European Economic Community to go forward in the form originally conceived in the Treaty of Rome. We must continue to press the Six for a significant reduction of trade barriers.

Should the deadlock imposed by France continue to prevent constructive resumption of the Kennedy Round GATT negotiations, the United States must then give consideration to ways of proceeding without her.

Many European countries also maintain nontariff restrictions on free trade. Quantitative import quotas, restrictions on their own capital outflows, and provisions making difficult foreign access to their capital markets are examples. The committee feels strongly that among the prosperous industrialized nations of the free world such restrictions are against the long-run interest of all concerned. We urge the administration to seek agreements with European nations to permit dismantling of these restrictions on both sides of the Atlantic.

SUPPLEMENTARY VIEWS OF SENATOR PROXMIRE

While concurring in the committee's report, I find it necessary to supplement it with comments on two counts: One is the proposal for suspending the investment tax credit, and the other is what I consider to be a failure to recognize fully the value of the wage-price guidelines.

Although I opposed the investment tax credit when it came before the Senate in 1962 and again in 1964 I opposed the liberalization of the terms on which the credit is granted, I think it would be a serious mistake to withdraw it now, for the following reasons:

1. *Investment credit is a sound long-range measure.*—The investment credit was adopted to provide a long-range incentive for growth and modernization of our productive capacity. It has been successful. Certainly it has proven itself as a major cause of the remarkable growth of the economy since its passage. The added capacity and efficiency that have resulted from the operation of the credit, along with the new depreciation guidelines since 1962, are of tremendous value to our economy and our defense effort now.

Such growth in capacity is the ultimate weapon against inflation. The suspension of the credit would discourage new long-range orders and commitments and this in turn would result in a cutback in investment and capacity at a later period.

That result may be entirely inappropriate at that time—for we will want a high level of investment in the years ahead after Vietnam is in back of us.

2. *Leadtime between order and delivery of productive equipment.*—A period of 18 months is sometimes cited as the average leadtime between contractual commitment and completion of capital projects in American industry. This rule of thumb includes both plant and equipment, a broader category than section 38 property. There are of course wide differences among investments. Many items such as office equipment and certain standard types of production machinery can normally be delivered within a few months. On the other hand, such investments as large aircraft, large electric generating plants, blast furnaces, heavy production equipment, and chemical processing equipment systems, may take 2 or 3 years or more to complete and place in service following the initial contract.

The design of specialized equipment requires considerable time, and the trend toward increasing use of specialized equipment makes this an increasingly important factor in the leadtime for capital projects.

Against this background, it has been estimated that some 40 percent of equipment subject to the credit has an order-to-delivery time of not more than one or two quarters, another 40 percent has a delivery time of three or four quarters, and another 20 percent has delivery times ranging between 1 year and 3½ years with an average of about 2 years. Some additional time would elapse between delivery and actual installation or placement in use in some cases.

The overall weighted average time between contract and placement in use of productive equipment eligible for the investment credit is therefore estimated at between three quarters and a year. If some allowance is made for necessary advance scheduling of equipment purchases to be installed as building construction is completed, the overall average leadtime may be somewhat longer.

3. *Suspension of investment credit not suitable as short-term restraining factor for these reasons.*—Because there is a considerable "leadtime" in carrying out investment projects; because the investment credit becomes available when assets are put in service and hence present contracts are being undertaken in reliance on the availability of the credit when the project is completed; because suspension of the credit would have to provide an exception for projects already under commitment, but which will be completed in the future; it follows that suspension of the investment credit would generally not alter investment expenditures or tax revenues for a substantial period of time.

4. *Current situation does not require changes in final income tax liabilities.*—As the President has stated, it is not necessary or desirable to change individual or corporate final tax liabilities at this time in response to the current economic situation associated with Vietnam expenditures. Since the investment credit is a component of final income tax liabilities, it follows that the current situation does not require a suspension of the investment credit.

5. *Balance of payments.*—The investment credit helps the balance of payments in two direct ways: (1) it makes investment here in the United States more attractive, and (2) it encourages modernization and cost cutting to strengthen our export position (including our defensive position vis-a-vis imports). Suspension or reduction of the investment credit in a world in which investment incentives are widely used in foreign tax systems under which our friendly international competitors operate would weaken our international competitive position.

WAGE-PRICE GUIDEPOSTS

Wage-price guidelines affirmed

This report fails to place sufficient emphasis on the value of wage-price guidelines for economic stability. It is a fact of economic life that huge sectors of our economy are not subject to marketplace discipline and therefore have considerable latitude for increasing prices, or wages, as the case may be. They are especially immune to monetary policy. Indeed, testimony before our committee in December indicated that the 1,000 largest firms would not be affected at all by the decision of the Federal Reserve Board to increase the discount rate. Most of these corporations have a self-respect which requires that they be able to look their neighbors and compatriots in the eye, as it were, and walk with their heads up. They listen carefully when the administration indicates the kind and degree of increase that is within the public interest and the kind that is excessive.

Skillful handling of guideposts by the President.

The Johnson administration has repeatedly and skillfully used the guideposts in specific bellwether situations to persuade labor and management to reach wage agreements that would not put pressure on prices.

Similarly, the administration has persuaded management in some of the leading industries in America not to raise prices.

Guideposts prime factor in stability

In steel, automobiles, aluminum, this use of guideposts has been in itself a solid and highly significant contribution to price stability, but the critical effect of guideposts is in the example they set.

Certainly the acceptance of guideposts by the Nation's great labor and business leaders in widely reported negotiations gives all of American business and labor an example of far greater significance.

Indeed until the last few months there has been no other force slowing down price increases on a great national scale; and yet the price performance of the American economy in the period since the initiation of the guideposts 4 years ago has been excellent. It has been outstanding in spite of production pressing far closer to capacity than in the preceding 5 years, and in spite of a far tighter labor market. Isn't the skillful use of guideposts at least one logical explanation of the superior price performance of the economy since 1962?

Indeed a study of the use of similar guideposts in other countries suggests that the Johnson administration has been more successful in the application of this vital stabilization technique than the government of any other country.

Guideposts do job fiscal-monetary policies cannot do

Since neither monetary nor fiscal policy can "get at" the pricing and wage-setting practices of big labor or big business, and since the pattern of economic behavior is so heavily influenced by big business and big labor, the Joint Economic Committee should affirm the desirability of wage-price guideposts emphatically, and hail the success of the administration in using them.

Serious labor inequity in guideposts

This is not to say that these guideposts have been perfect. Indeed, there is strong evidence that they will be particularly unfair to labor as applied in the coming year. This is true although labor received a two-thirds of 1 percent benefit from the increase in employer social security payments that is not included in labor's allowed 3.2 percent wage increase. The total labor compensation increase allowable in the current year within the guideposts would therefore be 3.9 percent.

Basis for labor inequity

Here is why this will shortchange labor: The guideposts assume that prices in the coming year will be stable. But the administration is virtually certain they will not be. They will increase. Virtually every administration witness before the committee agreed they would go up. The Director of the Bureau of Labor Statistics—probably the Nation's outstanding authority on price behavior—predicted a price rise in the coming year of between 2 and 3 percent, with 2½ percent likely.

If prices do rise 2½ percent and labor receives a 3.2 percent wage and fringe increase plus 0.66 percent social security payment benefit, its increase in real wages (total compensation) will be only about 1.4

percent, although it is contributing a productivity increase of more than twice that.

This means that employers will enjoy a profit increment—from the price increase of 1.6 percent on their labor costs, and of course 5½ percent (productivity 3 percent, price increase 2½ percent) on their nonlabor cost.

The committee should call this labor inequity to the attention of the administration, and the administration should either greatly increase its flexibility in handling of the wage-price guideposts to take this into account, or it should from time to time in the course of the year adjust the "wage productivity" measure upward from 3.2 percent with a cost-of-living adjustment to take actual price behavior into account.

Conclusion

In general, however, it would be a tragic mistake to abandon wage-price guideposts. Under skillful administration handling they have served the Nation well. Of course, they cannot do the whole job. But monetary and fiscal policy cannot do the whole job either without provoking a needless recession.

SUPPLEMENTARY VIEWS OF SENATOR TALMADGE

The committee's 1966 Economic Report launches a bold and ambitious attack on the forces of economic timidity which for so long have prevented the Government from taking sound and prudent cautionary measures to check the threat of inflation. Unfortunately, in the past, we have often delayed until inflation was clearly upon us before tightening the economic reins, which meant invoking severe and oppressive controls that in turn left us vulnerable to recessionary influences. Yet we should avoid taking precipitous action and imposing economic curbs as long as there is room in which to safely expand. Therefore, the solution appears to lie in an intermediate course of action. A high degree of flexibility and coordination in our economic policy movements would enable the Government to maintain a firm grasp on economic expansion without reaching the point of strangulation. The committee's report clearly recognizes the need for this form of restructuring.

However, I was somewhat disappointed by the committee's casual treatment of the meaning of the Vietnam war and its inevitable effect on domestic welfare programs. Perhaps it is true that the proverbial alternative between "guns and butter" is an outmoded concept in current economic theory, but I believe it is too fundamental to discard entirely.

The President has indicated that the war will cost in the neighborhood of $10.4 billion this year alone. In view of the progressive enlargement of our military efforts in Vietnam, it is reasonable to conclude that the costs might exceed that estimate, and surely will in following years. Nor is it likely that the war will end soon. Many high-ranking military authorities, indeed the President himself and certain Cabinet officials, have admitted that the war could drag on for a period of many years at a tremendous cost in dollars and lives.

Despite this overwhelming evidence, the committee assures us that there is no need to curtail Government spending in other areas. The committee's report goes even further and suggests that we expand some nonessential programs without delay.

I supported the education program, the medicare program, the poverty program, the Appalachian program, and other measures designed to help the less fortunate people of this country. It is undeniable that our Nation has been enriched in resources and spirit through the benefits made available by these programs. Furthermore, it is right and just for Americans to help Americans who cannot help themselves.

But these programs are by definition nonessential, irrespective of their merit. If we expand and start new nonessential spending programs while conducting a war, massive new taxes will be required. Even this probably would not prevent accelerated inflation which would hit hardest at the very groups the programs were designed to aid.

It is my considered judgment that we should postpone further spending for unnecessary programs until we are sure of our military needs. This would guarantee our revenues keeping an even tempo with the pace of the war demand, and would obviate the future necessity of hasty and sporadic revenue-raising measures.

We must put first things first.

MINORITY VIEWS

The extremely tight schedule prescribed for the committee by law provides insufficient time for the majority and minority to develop a report on areas of agreement and separate reports on areas in which our views diverge. Therefore, as in other recent years, the minority has developed independent views based upon the President's Economic Report, other messages, and this committee's hearings. The careful reader will be able to distinguish between the majority and minority opinions, both as to areas of agreement and disagreement.

INTRODUCTION AND SUMMARY

The administration's economic program exposes the American people to the twin dangers of serious inflation this year followed by a recession in 1967.

Recent increases in both consumer and wholesale prices—the largest in many years—demonstrate that inflation already is a fact of life. There is no excuse for further delaying needed action.

The administration admits that inflation is a serious threat, but stubbornly refuses to concede that effective anti-inflationary action is needed now. It promises to act sometime in the future should the situation require. But what evidence or degree of inflation is needed to trigger action by the administration? Must the country first experience price increases comparable to the early years of the Korean war?

The administration claims that its economic program, including a disguised form of price and wage controls, is adequate to hold down the cost of living. The fact is that the budget for the current fiscal year as revised in the January budget message is highly expansionary, while the 1967 budget is contrived to give the appearance of restraint but actually continues on the stimulative side.

The 1966 economic reports of the President and the Council of Economic Advisers are remarkable for their facile dismissal of mounting evidence of price pressures from both the cost and demand sides. The administration refuses to admit the full extent to which it has used illegal powers to restrain price increases and continues to express unwarranted confidence that the system of wage-price guidelines—a leaky dike at best—can hold back the tide of inflation without the exercise of restraint by Government itself.

Consistent Underestimates

In the past the administration has consistently underestimated the costs of the Vietnam war as well as the underlying strength and composition of demand in the private economy. Today it underestimates the pressures that will develop from increases in capital spending, a shrinking supply of skilled and experienced manpower, near capacity operation of plant and equipment facilities and rising unit labor costs.

The administration has in effect denied the presence of inflationary pressures by—

- —sharply increasing both spending and new obligational authority in the current fiscal year;
- —seriously underestimating budget expenditures for fiscal 1967;
- —covering up planned increases in 1967 expenditures by sales of Government financial assets that will have little effect in curbing overall demand;

—proposing revenue adjustments that largely affect the timing of tax payments and which, by their very nature, will do little or nothing to curb inflationary pressures;
—continuing its critical attitude toward the Federal Reserve Board for its timely move toward monetary restraint last December and virtually ignoring the impact of debt management in complicating the task of monetary policy;
—insisting the Nation is still enjoying a peacetime expansion when it has, in effect, moved into a wartime economy.

While the administration heats up the economy, it asks the private sector to hold the line and does little itself to effectively attack structural imbalances in labor skills and productive capacity. To enforce "responsible restraint" by management and labor, it engages in implicit or explicit price and wage fixing and other forms of harmful interference with the functioning of our economic system. This policy of economic interventionism will sap private initiative and inventiveness, impair efficiency and retard the Nation's long-term rate of growth.

Inflationary Psychology Developing

In the absence of appropriate administrative policies, speculative excesses, such as recent inventory building, will continue to mount and an inflationary psychology, already taking hold among our people, will dominate economic decisionmaking in the year ahead. Unless stopped now, this could lead to a distortion of cost-price relationships such as the Eisenhower administration was obliged to correct through its economic policies in the late fifties. This difficult but vital action of the Eisenhower administration left a sound legacy of stability which until recently permitted rapid expansion with relatively little inflation.

Barring a further acceleration of Vietnam spending, a recession next year is a likely reaction to growing inflationary imbalances and excesses already in evidence today. The tendencies toward recession will be strengthened since failure to take action to halt inflation now may force the administration to slam on the fiscal and monetary brakes later this year. Restraint—which is required now—would then begin to take hold just when economic conditions may call for a somewhat easier budget policy.

The administration's inflationary economic policy will have other serious consequences as well. The continuance of this policy will—
—severely harm those segments of our population least able to sustain economic injury, such as lower income groups, including social security beneficiaries and other pensioners, and young people trying to get a college education, buy a home, and start a family;
—intensify capital outflows from the United States, reduce further our already shrinking trade surplus, drastically worsen our balance-of-payments position, and intensify the gold outflow;
—result in a breakdown of delicate international discussions on monetary reform and threaten the successful conclusion of the Kennedy round of trade negotiations.

The relevant choice is not between "guns and butter." Our private enterprise system is flexible and inventive enough to provide both in an atmosphere of confidence fostered by wise and cooperative Government policies. The critical choice today is between inflation and a stable rate of growth which will strengthen, not weaken, our capacity to solve our domestic problems as well as meet our international commitments.

Maintain But Moderate the Expansion

Rapidly increasing civilian, military, and Government demands are beginning to exhaust available resources. As pressure mounts throughout the year on the shrinking reservoir of employables and production facilities, an opportunity is needed for the economy to adjust. An adequate but noninflationary advance can be maintained if Government policies are restrained until the adjustments take hold.

This requires a balanced and moderate program of Government fiscal and monetary restraint. However, monetary policy cannot carry too heavy a burden in tempering the boom. Interest rates already are at a high level and a further sharp and abrupt rise in rates will create serious disturbances in the financial markets. Fiscal restraint also is essential to hold down the level of demand for funds.

A reduction in the growth of the money supply and bank credit in keeping with the real growth of the economy should be accompanied by an immediate deferral of Federal spending for nonessential and low-priority projects and the elimination of those that are redundant and inefficient.[1] The administration should aim for a surplus on the national income accounts budget in calendar 1966 rather than the substantial deficit now anticipated.

If the administration is unwilling to reduce spending, an increase in taxes will be necessary, which would cause economic damage itself. Increasing taxes is a less desirable way to moderate the boom than by deferring expenditures. A cut in tax rates that are already too high is a sound way to lower barriers to economic growth. To raise taxes now would restore an obstacle to long-term growth. At the same time, another turnabout in tax policy reducing some of the high rates might be required next year if recession threatens. If more stimulus is needed next year, it would be far simpler to increase expenditures deferred this year than to cut taxes again.

The most certain way for the administration to protect the gains of the past and to insure social and economic gains in the future is by promoting a balanced and sustainable expansion without inflation.

The remainder of these minority views will elaborate on the need for immediate action to stop inflation, the inadequacy of the administration's program and the policy best suited to provide the degree of restraint required by current economic conditions.

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[1] Senator Javits would support necessary reductions or deferrals of expenditures for nonessential domestic programs, but he considers that recently enacted programs in education, welfare, and antipoverty and other human investment measures to be essential. They contribute to the Nation's economic strength and its capacity to fight inflation. He would rather increase taxes to fight current inflationary pressures than to accept material curtailment of these programs.

THE ANATOMY OF INFLATION

A. THE PRICE RECORD IN 1965

Last year witnessed a marked acceleration of the upward drift of the cost of living and a dramatic departure from the stability of the wholesale prices that prevailed for seven years.

The Consumer Price Index rose 2 percent from December 1964 through December 1965 after an annual average rise of 1.2 percent over the previous 7 years. Between January 1965 and January 1966 the wholesale price index rose 3.6 percent. From October 1965 through January of this year, wholesale prices rose at an annual rate of 6 percent.

Actually these increases understate the magnitude of inflationary forces in the economy. The reduction or removal of Federal excise taxes last year had a downward influence on the Consumer Price Index of about 0.3 percent. In the absence of these tax changes the index would have risen by 2.3 percent over the year. The index also has a downward bias to the extent that while corrections are made for quality improvements in durables they are not made for quality changes in services, which the Bureau of Labor Statistics admits "deteriorated further" last year.

The wholesale price index also masks a high degree of "hidden" inflation. The Council admits that in a period of weak demand list prices are discounted or lowered, freight absorbed and other terms of transactions changed. The wholesale price index fails to take fully into account the shaving of discounts and other changes in the terms of transactions, amounting to price increases, in a period of strong demand. The February 1966 issue of Fortune magazine reported that many executives say that prices of goods they buy have advanced faster than the price indexes, suggesting that actual prices are perhaps rising faster than list.

Guideposts Suppress Inflation

The wholesale price index also would have been higher except that the administration suppressed some price rises by the coercive use of the wage-price guideposts. Chairman Ackley admitted before the committee that industrial prices would have risen more in the second half of the year if the President had not made clear his view "that the guideposts really ought to be taken seriously." Not only have the guideposts suppressed price increases in the highly visible steel, aluminum, and copper industries but also, according to Dr. Ackley, "in a large number of industries" where the actions received no publicity.

The administration frequently denies that strong inflationary forces now exist. What forces was it acting to control in these situations if not forces of inflation? The problem is that the basic economic pressures for price increases still remain in spite of artificial restraints, and they are likely to break out sometime in the future unless fiscal and monetary restraint is pursued.

B. THE PRICE OUTLOOK FOR 1966

Although honest men may differ over the seriousness of the price inflation experienced last year, there can be little doubt that 1966 will see a substantial acceleration in the rate of price increases. Food and clothing prices will continue their strong upward trend, while other commodities and services will show larger increases than last year. There is little price weakness anywhere today. Increases in prices are being balanced off less and less by price declines.

The National Association of Purchasing Agents reported in February that its monthly survey of members showed 63 percent of those queried paid more for their purchases in January than in December, compared to 39 percent reporting higher prices from November to December. Less than 1 percent reported lower prices in January, while the number reporting higher prices was the largest in 7 years.

C. SOURCES OF INFLATIONARY PRESSURES IN 1966

The sources of inflation will strengthen this year on both the demand and cost sides.

The Council predicts that gross national product will grow 5 percent in real dollars at a time when output is already pushing against capacity and when a number of industries already are at or above the preferred operating rates. Pressures on the labor supply are already strong, and the labor market will tighten even more throughout the year. Demand for bank credit also continues at exceedingly high levels.

Some private economists are predicting an even greater increase in GNP this year than the Council, which last year badly underestimated the pace of the advance. Forecasters already are raising their sights for the year. If Vietnam spending increases more than anticipated—which is probable in light of the administration's past underestimates—then the economy will be under more severe strain than now anticipated.

Capital spending by business is continuing at a high level, and the volume of fixed investment expenditures in 1966 is expected to run well ahead of earlier projections. Dr. Walter W. Heller recently noted that in 1965 investment for the first time equaled high employment private saving. He said that in 1966 investment "threatens to exceed high employment saving and exert inflationary pressures."

Inventory accumulation is gathering speed as a hedge against price increases and as a response to rising sales. In the final quarter of 1965, inventories increased at a seasonally adjusted annual rate of over $10 billion, $2.4 billion more than in the third quarter and the highest increase since the Korean war. For all of 1965, inventories rose by $8.2 billion, almost double the increase for 1964 and the largest annual increase since 1951.

In spite of the increase in the discount rate in December, the rate of increase in money and credit continues at a high level. Bank loans to business rose 20 percent in 1965 after increasing by an average of 7 percent in the preceding 4 years. Consumer credit rose 12 percent, compared with an average of 8 percent in the preceding 4 years. Total private debt rose nearly 10 percent, or slightly faster than the average increase since 1960. Concern about the quality of private credit is voiced in many quarters.

The money supply rose nearly 5 percent in 1965, while money supply and time deposits together rose almost 10 percent. The rate of expansion of credit and money actually increased within the year itself. The increase in the money supply was nearly three times greater in the last 6 months of 1965 than in the first 6 months.

Pressures in Defense Industries

Pressures will be especially great in the defense and defense-related industries, which are receiving a flood of new Government orders. As Charles L. Schultze, now Director of the Bureau of the Budget, pointed out in a 1959 Joint Economic Committee study, inflation can originate in excess demands in particular sectors and spread to the rest of the economy through the cost mechanism. The recent sharp increases in demands in the defense industries ultimately could give added impetus to the inflation originating in excess overall levels of demand.

It is true, as the administration claims, that supply problems will be eased as the result of new capacity now being built. However, this overlooks the possibility that the growth of demand will soar even more than the growth in new capacity and particularly in those components of demand where supply is already hard pressed. This argument also fails to recognize that a considerable "shakedown" period is required for new capacity to become efficiently operative.

The greatest demand pressures will be felt on the labor force. The economy is now below the administration's 4-percent interim unemployment goal, although it should be noted that this administration over the past 5 years has added 300,000 to the Armed Forces, 200,000 to Government employment and hundreds of thousands to the munitions industry. The current aggregate unemployment rate conceals tightness within key sectors of the labor market. In February, the unemployment rate was down to 2.6 percent for adult men and 1.9 percent for married men. For the entire full-time labor force, the unemployment rate was 3.3 percent. Unemployment in manufacturing was at 3.5 percent in the final quarter of 1965.

Other signs of a tightening labor market include the fact that in late 1965 the hiring rate was at the highest point in 12 years, while layoffs were at the lowest point in 12 years. The factory workweek was at its highest since December 1945. For the first time since 1957, about one-half of the unemployed had been looking for work less than 5 weeks. One-third of the 150 major labor areas—nearly twice the number of a year ago—achieved unemployment rates of 3 percent or less. At the same time, immigration continues to fill more and more of our skill requirements.

In a presentation to the Joint Economic Committee, the Bureau of Labor Statistics admitted the existence of emerging labor shortages and signs of tightening labor markets. The Bureau called attention to unemployment rates for certain occupational groups, the low over-the-year increase in the employment of adult men and the quality of the 1.2 million adult men still unemployed. After making allowances for seasonal and fractional elements, the Bureau said that of the remaining unemployed "some have such severe educational and other handicaps that they are unlikely to enjoy steady work even in the most active job markets." The Bureau's report went on to point out that "mature, experienced, and capable workers were increasingly hard to find in 1965," although the report reassured us that the situation had not reached "the critical stage."

Growing Skill Shortages

The Bureau expressed the greatest concern about industries most closely related to the defense effort where there were growing skill shortages, sharp increases in the hours of work, and a substantial increase in the ratios of unfilled defense orders to shipments.

This year the Bureau expects 1.8 million new civilian jobs will be created. It says that "The increase in demand for workers in 1966 will be substantially above the long-term trend rate of growth." At the same time that civilian labor demands are soaring, the military services are absorbing about 300,000 young men.

What about the supply of labor? The Bureau says that male entrants under 25 "may be no more than 100,000 instead of the 420,000 implied by labor force trends." The main additional source of male workers for the civilian economy will be the increase of 230,000 in men 25 and over.

The outlook, according to the Bureau, indicates intensifying manpower demands requiring "more workers with better qualifications." Yet, the Bureau then says, "young workers and women remain the primary source of additional labor supply, with relatively few adult men."

What makes the situation even worse is that the Bureau admits the labor pinch will be felt this year in those industries, occupations, and areas already squeezed in 1965. Areas and occupations of high unemployment won't be affected. Aside from the fact that many of the unemployed are not able to fill job vacancies, they may also not be in the right place. As a result, there are grave questions as to how much a reduction in unemployment will be able to contribute to manpower needs this year.

The picture of the labor market painted by the Bureau clearly indicates that shortages of skilled manpower will be a source of inflationary bottlenecks in supply and that productivity increases are likely to be no better and possibly worse than this year.

The slow growth in productivity and strong upward pressures on wages will combine to create a substantial upward movement of unit labor costs in the private economy. This will represent one of the greatest sources of inflationary pressures throughout the year.

Productivity Growth Slows Down

Productivity in the private sector last year increased only 2.8 percent (and some private sources put the gain even lower). The increase was far below the average postwar gain and even farther below the 3.8-percent annual increase experienced from 1960 to 1964. Even the Bureau of Labor Statistics concedes that the increase "does seem low" and suggests that it should have been 3.5 percent.

The reasons for the slowing of productivity gains are found in the pressure on resources. Lower quality labor was drawn into the labor force last year and more of the same can be expected this year. Also, as the economy continues to operate at higher and higher levels, less-efficient, idle or standby facilities will be drawn into the productive process with a consequent diminution of productivity gains.

Although the Bureau cited several factors which will contribute to increasing productivity, it admitted that "some of the factors which contributed to the smaller productivity gain in 1965 can be expected to continue to operate for the next few years, particularly should output continue to increase at a high rate."

Add to this outlook the likelihood of increasing wage costs and a picture of a classic cost-push inflation emerges. In 1965 wage adjustments negotiated and scheduled to go into effect in the first contract year amounted to 3.9 percent, disregarding fringe benefits, which by themselves added another 0.75 percent to wage costs. This compares to increases of 3.2 percent in 1964 and 3.0 percent in 1963. The increase without fringes comes to 3.3 percent even when averaged out over the life of the agreements, far above the 3 percent of 1964 and the 2.3 percent of 1963. Adding fringes puts the 1965 figure far above the wage guideposts.

The situation is even more disturbing with regard to unorganized workers. Here the Bureau admitted that there were "more frequent or widespread wage increases than in previous years." The proportion of unorganized workers in manufacturing plants who got wage increases in 1965 rose to 70 to 75 percent from the 50 to 60 percent of recent years. Next year the increases among unorganized workers are likely to be even larger. For one thing, the Bureau notes that "the consumer price index is a major factor in bargaining and in wage determination among unorganized workers." Other factors noted by the Bureau that might cause larger increases in wages in nonunion firms in 1966 include growing shortages of workers and the reduction in take-home pay resulting from higher social security taxes.

A recent Labor Department study of 306 major collective bargaining agreements shows that all but 12 provide for possible wage adjustments in 1966. The number of workers scheduled to receive deferred wage increases is the greatest since 1957. About 35 percent will get increases between 10 and 11 cents an hour, compared to 1965 when the largest concentration (32 percent) received 7 to 8 cents an hour. Over 4 million workers will get deferred increases averaging 3.2 percent. In addition, 2 million of these will get another 2 to 3 percent in accordance with escalator clauses based on the consumer price index.

Payroll Tax Bite

Employers are already feeling the effects of the increase in social security taxes and the increase in the taxable wage base. The Council has estimated that this tax increase raises hourly labor costs two-thirds of a percentage point. However, the Council unrealistically does not believe that these legislated payroll costs should be considered as a wage increase or fringe benefit for purposes of the guideposts. Even if negotiated wage and fringe increases were within the guideposts this year, the increase in social security taxes would impose a clearly inflationary cost on business.

The administration's recommendations for an increase in the minimum wage and a broadening of its coverage may also be inflationary and have the additional effect of pricing unskilled labor out of the market. Whatever the merits of the minimum wage, there is a widespread feeling—apparently shared by some in the administration—that any increase that is granted should be noninflationary.

When asked whether the proposals to increase the minimum wage and its coverage would increase costs and prices, Chairman Ackley replied, "I should suppose that the effect of any increase in the minimum wage would depend on how large an increase were involved * * * an increase in the minimum wage that was consistent with the general average gain in productivity in the economy would probably have minimal effects on labor costs." Since all increases suggested so far greatly exceed the guidelines, it is obvious that current proposals would be inflationary, particularly if they were to take effect this year. The upward pressures, of course, would not only be felt at the lowest rung of the wage scale, but all through the wage structure as competing groups strive to maintain their differential wage advantages.

To the extent that the administration's proposals to change the unemployment compensation system increase employer costs, they will also be inflationary. This should be one of the primary considerations taken into account by the Congress in debating both the unemployment compensation and minimum wage proposals.[2]

If wage adjustments last year were greater than the guidepost figure, they are likely to be even larger this year. The Bureau of Labor Statistics estimates that "except for social security taxes, other components of hourly labor costs will probably rise about as fast, on the average, in 1966 as in 1965 or perhaps slightly faster." Taking into account that new payroll taxes raise labor costs two-thirds of a percentage point, the situation will clearly be one of serious cost pressures.

The combination of an inadequate growth of productivity and a strong upward pressure on costs—particularly wage costs—will mean sharply rising unit labor costs. Unit labor costs for the private economy, as Chairman Ackley told the committee, "increased almost 1 percent in 1965—which is appreciable and obviously a subject of concern."

The administration's assumption of an improvement in the growth of productivity this year is the key to its optimism about restricting inflation. As we have shown, however, this optimism is unfounded. Combined with a strong upward push on wages—which is clear from labor's complete rejection of the guideposts if not from other evidence—the combination spells a distortion of our cost-price relationships which may require strong corrective medicine sometime in the future unless prevented by timely action now.

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[2] Senator Javits thinks the minimum wage should be reasonably increased to meet new cost-of-living demands and believes we should adjust in other directions to meet inflation.

THE INADEQUACY OF THE ADMINISTRATION'S ECONOMIC PROGRAM

How does the administration's economic program fall short of effectively combating the clear and present danger of serious inflation?

The administration's claim that its present and proposed fiscal policies are mildly restrictive or neutral was questioned by the majority of private economists who submitted testimony or written statements to the committee. Prof. Richard Musgrave, of Harvard University, examined the current fiscal impact by comparing calendar year 1965 to calendar 1966 and concluded that "fiscal policy is substantially more expansionary than it was last year." The "main thrust," he said, "would come in the first half of the year."

Professor Musgrave made an important point in presenting a calendar year analysis and in calling attention to the national income and product account budget—the most useful for studying the economic impact of Federal fiscal activity. Although that budget showed a surplus of $700 million for 1965 as a whole, it was in heavy surplus in the first half of the year and progressively moved into large deficit in the second half. The deficit will continue to be substantial in the first half of the current year, but will probably taper off later in the year.

However, the deficit for calendar 1966 as a whole will be substantial and represents a major expansionary shift when compared to the surplus of 1965. This shift toward expansion comes precisely when the margin of unused resources has been reduced to the vanishing point.

Another sign of the growing Federal impact on commodity markets is the sharp increase of $6.2 billion in Federal purchases of goods and services between fiscal 1965 and 1966. This increase compares to a decline of $1.3 billion in such purchases between fiscal 1964 and 1965. Although the 1967 budget predicts a smaller rise from fiscal 1966–67, the increase will still amount to a hefty $3.7 billion. For the two fiscal years from 1965 to 1967, Federal purchases of goods and services will rise by $10 billion, compared to only $3.6 billion in the three previous fiscal years.

Procurement Effects

Prof. Murray L. Weidenbaum, of Washington University, has shown that the primary effect of military procurement on productive activity "occurs in advance of actual Government expenditures." He points out that—

> It is at the order stage that the Government action normally will have its initial and often major impact on the markets for labor, raw materials, and financial resources.

This is the situation today. New obligational authority is soaring this year and will probably fall off in fiscal 1967, barring further escalation in Vietnam. Appropriations and other new obligational authority, which are an approximate measure of the Government's intentions to spend and let new contracts, will increase 18 percent from fiscal 1965 to 1966. Most of the new spending commitments are coming in the first half of the current calendar year, a fact which Business Week noted will provide "a whopping fiscal stimulus" over the next few months.

It is this immediate situation which calls for restraint in nonessential and deferrable expenditures.[3] To date, the administration has refused to exercise the required discipline on current spending and instead directs attention to the allegedly restraining character of the 1967 budget.

The question may be raised whether the 1967 budget should not be more expansionary than it in fact is. The committee heard expert testimony that the budget will be too expansionary during the final half of this calendar year and too restrictive during the first half of next year. Although it is obviously impossible to predict conditions a year hence, this observation may have merit if revenue and spending estimates turn out as the administration predicts. This is particularly true if one concedes that an inflationary boom may be laying the groundwork for a recession next year.

However, we doubt that the 1967 budget will be overly restrictive next year, and we feel certain that it will be too expansionary in the second half of this year. The January budget estimates this year are a less reliable indication of what actual results may be than is usually the case.

Spending will almost certainly exceed the administration's estimates. Not only are some proposed outlays underestimated, but Congress may very well increase spending on programs where the administration—with tongue in cheek—has asked for reductions, such as the school milk program. Some observers have indicated that the $4.8 billion reduction in nondefense expenditures is largely concentrated in programs controlled by law. The $5.4 billion increase in nondefense expenditures, however, is said to be in those areas where the Executive has a freer hand in determining the level of spending.

Revenue Measures

On the revenue side, the tax measures requested by the administration will yield about $4.8 billion in additional income, but since these (except for the reinstatement of excises reduced in January) do not involve any increase in tax rates, their effect on demand will be minimal. To the extent that the acceleration of tax payments affects liquidity and interest rates, it may have some secondary effects in dampening demand, but the overall impact is likely to be small.

Another factor temporarily swelling revenues is the unusually large seigniorage profit from converting silver coins to copper, estimated to total close to $2.5 billion in fiscal 1966–67 combined.[4] As Prof.

[3] See Senator Javits' footnote, p. 33.

[4] It should be noted that when Congressman Widnall predicted last August the amount now conceded to be available through seignorage profits, and cautioned on its possible use for budgetary purposes, his statement was discounted by administration officials. A Presidential committee, appointed in September to report on the use of these profits for proposals such as the Republican water resources trust fund, has never submitted its report, though it was due in December.

Raymond J. Saulnier has pointed out, to the extent of these profits "budget expenditures are being financed in a thoroughly inflationary manner."

The massive sale of $4.7 billion in Government financial assets proposed in fiscal 1967 also will have the effect of producing a lower level of expenditures and deficits than would otherwise be reported in the budget. They do not, however, reduce the Government's demands on the already hard-pressed credit and capital markets, nor do they affect the actual volume of Federal outlays. In effect, these proposed sales amount to another way of financing the Federal deficit.

In connection with the sale of Government assets, we wish to call attention to a bill (H.R. 13102) introduced by Congressman Widnall to limit and gradually reduce the use of the Federal National Mortgage Association to guarantee the sale of participation certificates for Federal Housing Administration and Veterans' Administration mortgages ($1.2 billion sold, $410 million due in March) and new participation certificates for the Farmers Home Administration, Office of Education, Small Business Administration, Veterans' Administration, and the Department of Housing and Urban Development, for an anticipated total of $3.2 billion. The program to sell financial assets should not become an unlimited pipeline to the Treasury. We urge early consideration of this bill by the appropriate committees of Congress.

Not only does the administration refuse to move toward fiscal restraint, but it also continues to be critical of efforts to reduce the massive rate of growth of bank credit and the money supply. It continues to carp at the Federal Reserve Board for its "fall from grace" last December, although one suspects this public posture conceals a private sigh of relief that the Board moved when it did.

Bank Reserve Growth

Although interest rates have firmed further since the discount rate increase in December, the Federal Reserve has not yet taken sufficiently effective action to curtail the growth in bank reserves and bank credit to more accurately reflect real and anticipated economic growth. However, the move toward further monetary restraint must be neither too large nor too abrupt. The level of interest rates is already high by historical standards and a further sharp movement to higher rates would be likely to create serious disturbances in the financial markets.

It is for this reason that we believe monetary policy cannot do the whole job. The degree of monetary restraint which the economy can absorb at this time without undesirable side effects would not be sufficient to provide reasonable price stability under current conditions.

A reduction in the supply of money and loanable funds will raise interest rates and reduce demand for credit. However, credit demand for marginal projects can also be reduced by a more restrictive fiscal policy. Harnessing fiscal policy and monetary policy together in this fashion would result in reducing the overall level of demand but at a lower structure of interest rates than would be true if emphasis were placed on a restrictive monetary policy alone. Therefore, fiscal policy must reinforce monetary restraint while debt management considerations must not be permitted to impair its effectiveness.

Another phase of current administration economic policy is designed to reduce residual unemployment through structural measures to improve the training and skills of the labor force and to generally strengthen the performance of labor markets. While it is true that this approach will augment the ability of the economy to absorb increases in demand without inflation, the administration has too often pushed the wrong programs while letting those with real potential languish. Even when effective, these programs will not have any substantial effect in alleviating current pressures. Considerable lags exist between the beginning of training and the time the trainee is able to fill a pressing job vacancy.

While the administration now talks as though structural attacks on unemployment are another of its unique contributions to the economic expansion, the fact remains that the administration began to fashion structural tools only after persistent Republican pressure and then in a tardy and limited fashion. We have long pushed for and continue to urge improvement of training programs to update skills, ease adjustment to technological unemployment and improve the opportunities of minorities.

Much remains to be done in this area in order to reduce residual unemployment to a minimum while avoiding inflation. We shall comment at greater length on this critical aspect of economic policy later in these views.

THE WAGE-PRICE GUIDEPOSTS [5]

The administration hopes to restrain inflation by wage-price guideposts that were first enunciated in 1962 as a guide to private action but which have since become a disguised form of direct control over the private economy.

We Republicans believe that our economic system is designed to economize our natural and human resources and to channel and allocate them among alternative uses through the impersonal operation of the market system. We have placed chief reliance upon the forces of (1) free independent initiative and choice, (2) profit motivation, and (3) competition between independent sellers, seeking the favor and purchases of independent buyers, trying to get the "most-of-the-mostest" for their money. Through these forces our system is designed to maximize employment, production and purchasing power, and achieve the optimum use of resources at the level and in the directions we desire.

The risk is that we will drift or be led into a new pattern, downgrading collective bargaining and the free market system. The proper role of Government under our political and economic system should be to create and maintain the market machinery in good working order—not undertake to substitute for it, or confuse the issues of its imperfections by admonitions that it do better.

This is precisely the risk that we face today. We do not believe that the guideposts can restrain inflation in a period of tight labor and commodity markets, nor do we believe that they should be relied upon for this purpose even if they were effective.

From past experience, we would expect that the failure of the guideposts will lead the control-minded policymakers in the administration to seek more direct and damaging restraints on private economic decisionmaking.

The debate which would certainly follow a forthright request for authority to impose direct controls would have a healthy effect. If the administration believes controls are needed, we would prefer controls imposed and limited by statute to the ambiguous and arbitrary exercise of economic power now assumed by the administration without sanction of law or provision for redress of grievances.

A full-scale study within the Congress, such as we have urged the Joint Economic Committee to undertake, might convince well-meaning proponents of the enforcement of the guideposts of the long-run perils to which systematic interference with the market mechanism exposes our free economy. If such a debate did nothing else, however, it would make abundantly clear the technical difficulties which stand in

[5] Senator Javits agrees with much of the discussion of the guideposts advanced by his colleagues, particularly regarding their inflexibility and the coercion used by the administration to enforce them. However, he believes that the guideposts perform a useful and necessary function in a complex modern economy now burdened with the Vietnam war. He believes that they provide some economic guidance to the private sector and thus help to avoid the need for mandatory controls to curb inflation.

the way of devising a satisfactory formula governing the changes in wages and prices in our economy.

Variety of Exceptions

The complexity of the guidepost concept is demonstrated by the fact that there are a variety of exceptions which are not as clearly dealt with as behavior under the general rule. Since the average rule is more easily administered than the numerous exceptions, inefficiencies in allocation of resources may result, as Professor Musgrave pointed out to the committee.

The Council's decision to scrap the 5-year moving average as an appropriate indication of the general productivity trend and to retain instead the 3.2-percent guidepost of last year illustrates another inherent weakness of the guidepost concept: the problem of developing a measure of the trend growth of productivity. What time period truly represents the trend value of productivity in the U.S. economy? Should this value reflect only output per man-hour or output per unit of total factor input? Should the national increase in productivity include the large gains in agricultural production along with the smaller increases in the nonagricultural sectors? Should wages go up 3.2 percent in industries which experience substantially larger productivity increases? These are a few of the difficult questions which should be debated. Depending on the answers, the value of the wage-price guidepost would be vastly different.

Another difficulty with the guidepost concept is that the approach lends itself more readily to markets in which a few firms are dominant and wage settlements involve large contracts. Inescapably, their enforcement becomes selective and discriminatory.

The guideposts also miss the mark in concentrating on industries rather than individual firms, where much of the wage determination and price setting actually occurs. The concept of an industry of homogeneous enterprise has been blurred in recent years. Even if an industry could be clearly identified, the position of individual firms within that industry differ markedly from one another.

The guideposts are intended to deal with cost-push inflation caused by market power, even in the absence of excess demand. The argument that specific industries or unions exercise a high degree of arbitrary market power is often overstated. Among other factors, it frequently overlooks the competition of domestic substitute products as well as imports. For the most part, price or wage increases in these highly visible situations are a response to rising demand and limited supply, just as is the case with other industries.

The European Experience

In any event, spreading wage and price increases are only possible if a rapidly increasing supply of money supports an excessive level of aggregate demand in the economy generally. If aggregate demand is held within noninflationary bounds, guideposts will not be needed. If aggregate demand is permitted to get out of hand, the guideposts will be ineffective. The European experience with "income policies" offers persuasive evidence of the futility of trying to restrain inflation through such devices in an overheated economy.

Administration officials who castigate private decisions as "not in the public interest" or "unpatriotic" assume a depth of understanding of what constitutes the public interest that is almost mystical. Would the increase in aluminum prices which the administration rolled back have been in the public interest? If prices had been allowed to rise, resources would have been drawn into the aluminum industry, raising investment and ultimately output. Higher output would have meant lower prices sometime in the future. Higher prices now might also have shifted demand to substitute domestic products, where demand pressures may be less.

The administration's extensive arguments about the effectiveness of the wage-price guideposts in restraining price increases in the private sector have obscured the vital role that prices have to play in a predominantly free market economy. Prices are sensitive and reliable indicators of the relationship of supply to demand, and price changes serve to direct creative effort and materials to their most productive uses. A price rise indicates that more resources should be devoted to a particular productive activity, while a price decline indicates that resources can be profitably withdrawn and utilized elsewhere. In other words, prices serve as traffic signals directing resource flows to the most efficient activities in terms of satisfying demand. When the traffic signals are replaced with essentially static guideposts, there is little assurance that resources are being directed to their most productive uses. There can be no assurance when the guideposts are fixed in an arbitrary manner. A product's price rise persuades consumers to shift their demands to substitute products, thus lessening demand pressures on the more expensive items. A price rise also induces producers to increase supply by opening up opportunities for greater profit. This increased supply further lessens upward price pressures. When this adjustment mechanism is perverted, both high demand and low supply continue with no alleviation of inflationary pressures.

Antitrust Policies

Where private market power does exist to thwart the working of the price system, it can be dealt with most effectively by diligent and determined pursuit of policies to make competition more effective, including both antitrust action and lowering the barriers to imports from abroad.

If the guideposts divert attention from fundamental fiscal and monetary policies, they will have an upward bias of their own while at the same time weakening the capability of the economy to adjust to changes in demand and technology. Prof. Paul W. McCracken, of the University of Michigan, has said:

> An economy whose pricing system operates according to the guidelines as enunciated would certainly find its capability for progress severely weakened.

As Professor McCracken points out, there are serious dangers in attempting to apply aggregative rules relevant to the general price level to the ever-changing relationships among individual prices.

Budget Director Charles L. Schultze, in a paper written for the Joint Economic Committee in 1959 while professor of economics at Indiana University, maintained that it was essential to economic stability for wages and prices to be responsive to changes in demand. Commenting on guidepost policy, he said:

> Public policy statements in recent years have emphasized that wage-rate gains must stay within the bounds of productivity advances if inflation is to be avoided. This study on the other hand stresses the importance for price stability of the responsiveness of wages and prices to changes in demand. There is no single formula which can specify the appropriate relationship between changes in productivity, prices, and costs in particular industries. In a flexible economy individual wage-price-productivity relationships should reflect the strength of demands in each industry. If businessmen and labor leaders would become more demand conscious and less cost conscious, the overall wage-productivity relationship would take care of itself, so long as intelligent monetary and fiscal policies were pursued. Hence, if one must preach to business and labor about their obligations to the "public interest," the emphasis should lie on the need to orient price and wage decisions more closely to market conditions. The continual invocation of the phrase "wage-rate gains on the average should not exceed productivity gains on the average" is not sufficient to enable management and labor in an individual basis to determine the kind of price and wage behavior on their part needed to achieve a greater stability of the price level in a full employment economy.

We believe the guideposts have been useful in conducting a more intelligent public dialog. But we reject as inequitable and damaging to our economic system the selective, arbitrary, and punitive enforcement of what were intended to be no more than guides to private action.

REPUBLICAN POLICY PROPOSALS RESTATED

In the preceding discussion of administration policy, our views on the appropriate course of economic policy in the current inflationary environment have been implied but not precisely stated. In this section, we wish to set forth our policy proposals more fully.

The basic assumption upon which these proposals are based is that immediate steps are required to reverse the ever-worsening inflation in the economy. Further delay in applying anti-inflationary restraints will require a stronger and more disagreeable dose of restrictive medicine in the future.

A. MONETARY POLICY

The Federal Reserve Board should reenforce its increase of the discount rate last December by moving to slow down the growth of bank reserves. The Board should supply a level of reserves that will restrict the growth of bank credit to about 5 or 6 percent in the coming year in contrast to the growth of nearly 10 percent last year. The increase in the money supply (currency and demand deposits) should be held to the current and anticipated real growth of the economy and not permitted to continue at an excessive rate of increase.

A monetary policy such as we advocate would permit the economy to grow at or near its current real rate but would avoid an acceleration of the inflationary boom. However, even this degree of monetary restraint probably will not prevent a substantial increase in the cost of living this year in the absence of fiscal tightening designed to reduce the demand for credit.

B. FISCAL POLICY

The administration should reduce the administrative budget deficit of $6.4 billion projected for the current fiscal year and, at a minimum, produce a small surplus in fiscal 1967. The national income and product account budget for calendar 1966 should also show a surplus instead of the substantial deficit that will result from present policies.

These results should be achieved through strict control over Federal spending.[6] If expenditure control is not pursued with sufficient diligence and determination, then an increase in taxes faces the American people. These measures should be in addition to tax changes already requested by the administration.

The administration should move immediately to defer nonessential civilian expenditures, to stretch out planned spending wherever possible and to eliminate redundant and inefficient expenditures. We do not suggest a meat-ax approach to expenditure control, but rather an approach that takes cognizance of the limited skilled and professional manpower and physical plant capacity in particular areas of the economy. The Bureau of the Budget should set forth strict but carefully

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[6] See Senator Javits' footnote, p. 33.

formulated spending priorities in this spirit, recognizing that not every dollar of Federal spending is of equal importance to the national interest.

The need to set priorities for Government spending is well illustrated by the continuing housing needs for low and moderate income citizens, and the refusal of the administration during hearings this year before the House Special Subcommittee on Housing to back a Republican amendment to the urban renewal laws which would redirect the urban renewal program by setting priorities for using available funds in projects designed for this necessary housing.

Prior to the enactment of the 1964 tax reduction, administration officials maintained that reductions in spending would be virtually impossible to make. Republicans insisted that the tax cut should be accompanied by reductions in the administration's proposed spending, and time has proved the wisdom of that position. If spending had increased in the past 2 years as rapidly as in the 1961–63 period, the inflationary overheating of the economy would have occurred much sooner and would have been more severe. In fact, it is likely that tax cuts accompanied by rapid expenditure increases would have resulted in more serious inflation before the achievement of 4-percent unemployment. It was not until the administration stepped up its level of spending last fall that overheating of the economy began to appear.

Congress Should Exercise Restraint

We also urge the Congress itself to exercise restraint in considering the administration's 1967 budget requests. There may be selective cases when the Congress will increase administration requests. If so, these should at least be balanced by reductions in other areas.

Above all, we hope that discussion of expenditure deferral until economic conditions are more favorable will avoid the emotionalism that generally surrounds appeals for expenditure restraint. No one believes that the underprivileged in our society should bear the costs of the Vietnam war. But neither can anyone doubt that numerous programs of marginal value to our society can be slowed down without harm to the national interest. In some cases, a less rapid and more carefully considered buildup of Great Society programs would avoid the redundancy, inefficiencies, errors and controversy that accompany well-meaning efforts to do too much too soon. We would also remind the administration that—in the words of the minority members of the Ways and Means Committee—"we cannot win the war on poverty if we lose the war on inflation."

Whether a tax increase can be avoided depends upon monetary policy, debt management policy and a change of heart by the administration so that expenditures are held down in the coming year.

If too little is done in these areas, then taxes will have to be increased, which is preferable to increasing the debt. We would regret the necessity for a tax increase. Experience has shown that high tax rates are an impediment to economic growth. Our hope is that as Federal revenues grow in the future, expenditures will grow by a smaller amount, permitting regular tax cuts that will stimulate long-run economic growth.

We recognize that changes in tax rates starting from a level of exceedingly high rates can be a powerful weapon for economic stabilization. We would not hesitate to use the tax tool when necessary. However, our feeling is that a tax increase can be avoided today if our recommendations in the fiscal and monetary areas are followed. As we have already stated, we feel that an increase in taxes this year might be followed by a reduction again next year if recession threatens. It would be considerably more difficult and time consuming to cut taxes again next year than to reinstate the expenditures deferred this year.

However, if a tax increase becomes necessary, we believe that a flat percentage increase in corporate and personal rates would be the simplest and quickest method to pursue.

We believe that consideration should also be given to elimination or temporary suspension of the investment tax credit as part of any proposed general tax increase package.[7] Since capital expenditures are at an unsustainably high level and apparently going even higher, there is a danger that the economy may face a situation of excess capacity sometime in the future. It would be desirable under these circumstances if some currently planned capital spending were deferred until next year or beyond.

On the other hand, new capacity increases aggregate supply and enables the economy to absorb higher levels of aggregate demand without inflation, particularly in distribution and services where bottlenecks and shortages are particularly serious. More efficient capacity also strengthens our international competitive position and produces a larger growth in productivity and downward pressures on costs at home. Our long-run policy should continue to emphasize the importance of a high level of savings and productive investment in the economy.

D. DEBT MANAGEMENT

One of the most important but least debated economic issues is the impact of debt management on monetary policy. Although the Treasury-Federal Reserve Accord of 1951 was designed to free monetary policy from the iron grip of debt management, the flexibility of open market operations is still impaired to some extent by Treasury debt financing. If monetary policy is to serve its purposes effectively, considerably more understanding is needed of the relationship that exists between the operations of the Federal Reserve and the debt financing of the Treasury. We have consistently advocated that the Joint Economic Committee study this issue as a part of its continuing interest in the tools of monetary policy.

Recent developments point up our concern. Since mid-1965 changes in the composition of the debt have tended to be stimulative because newly issued debt has been relatively short term. The legal interest

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[7] Senator Javits believes the prevailing priority should continue to be the encouragement of real production, and he is, therefore, for retaining the investment tax credit. He wants to see it broadened to include manpower training expenditures by business which are approved by the Secretary of Labor and in addition to normal training already being carried on.

rate limit on long-term Government bonds is no longer competitive, forcing the Government to borrow in the form of "near money" securities with short or intermediate maturities.

The legal interest ceiling has also affected the term structure of interest rates. Yields on Treasury bills and intermediate-term securities have risen abnormally relative to yields on long-term Government bonds.

We believe that the administration must recommend immediate lifting of the 4¼-percent ceiling on Government bonds. Removal of the ceiling would facilitate noninflationary, long-term Government financing and at lower interest costs than are now possible through financing at shorter term.

EMPLOYMENT OBJECTIVES

Our employment goal is that every person, ready, able, and willing to work should be able to find a job without suffering the hardships of underemployment or unemployment. The recent reduction in unemployment is a welcome development, but it offers no excuse to rest on our oars. We believe that we must do better, and that we can do better.

We refuse to play the numbers game and specify a full employment target. We realize that in a dynamic economy marked by frequent voluntary job changing there will always be an unavoidable level of frictional unemployment. Beyond this, no level of involuntary unemployment is acceptable. And we would hope that even for the frictionally unemployed the period of joblessness could be sharply minimized.

Achieving this goal will not be easy. Not only must we equip the long-term jobless for gainful employment, but we must also insure that the ill-trained who have found jobs in the current buoyant economic environment are not dumped back on the market when the expansion slows down. A democratic society where affluence is enjoyed by many but denied to a few should do no less.

What will be required to reach our goal?

First, we believe the goal must be achieved without inflation. No foreseeable amount of Federal assistance can undo the damage to the well-being of the poor and deprived which is caused by unrelenting erosion in the purchasing power of the dollar.

Second, we must move steadily toward our goal but not try to reach it too quickly. Programs required to equip the chronically unemployed for gainful employment require considerable time to implement. Too rapid an increase in aggregate demand before these programs take hold will only result in inflation and—when the reaction sets in—disillusioned, unemployed people.

Third, we must develop a better understanding of who is unemployed and why. Our aggregate unemployment statistics are among the best in the world, but they still tell us too little. Fascination with aggregates conceals deep-seated structural changes taking place in our labor force, such as the shift from rural to urban employment, the larger role played by women and the sharp increase in young and inexperienced jobseekers. Without a full understanding of these changes our programs will miss the mark and dilute assistance to those who most need and deserve our help.

Census of the Unemployed

The logical beginning for an attack on hard-core unemployment should be an immediate effort to collect a census of the unemployed, as recommended by Prof. Raymond J. Saulnier, of Barnard College. Such a census would provide us vitally important information that we now lack with any precision. It would pinpoint the reasons for chronic unemployment, the groups most seriously afflicted, the degree of labor force attachment of the unemployed and the areas where public programs could be most beneficial. Such a census would for the first time reveal the size and shape of the problem which confronts us. Also essential is an up-to-date and realistic Dictionary of Occupational Titles in order to make job training for the unemployed meaningful.

Along with the census of the unemployed, we must make faster progress in developing a statistical series on job vacancies. Had the administration seen the vital need for such a series, it could have long ago induced the Democratic Congress to appropriate the modest sums required to launch such an effort. To the extent such statistics pinpoint unfilled job openings by occupation and geographic area they would be invaluable in shaping effective manpower training and guidance programs. Information on the relationship between the number of persons unemployed and the number of job vacancies also would help policymakers determine with greater certainty whether aggregate demand at any particular time was deficient and, if so, aid the development of policies to deal with it. When the number of job vacancies is greater than the number unemployed, policies to stimulate aggregate demand will obviously be inappropriate and probably inflationary.

We also believe that the administration or the Joint Economic Committee should study the entire system of the Nation's employment security programs, both public and private, on an integrated basis and with special emphasis on the employment consequences of these programs. In the Government sector, study is needed on the economic impact of the minimum wage and payroll taxes. These studies should try to determine, among other things, the level at which the payroll tax begins to act as a deterrent to adding new employees and its incentive effect for the introduction of laborsaving machinery and equipment.

American business itself should launch a creative effort to provide full employment for our people. Businessmen as a whole enthusiastically joined together to urge passage of the tax cut of 1964. Their support had a major impact in securing passage of that legislation. We believe that leaders of American business should now form a businessmen's committee for full employment to seek new ways in which the private sector can expand employment and training opportunities for the millions of young men and women entering the labor force in the coming years.

Aside from these basic steps to attack the problem of residual unemployment, there is a need for a complete evaluation and inventory of present Government programs designed to reduce unemployment, help the poor, raise economically depressed areas to their full productive potential, and provide welfare to the unemployable.

Programs Fall Short

In recent years, there has been a proliferation of new Federal, State, and local programs to achieve these goals. We have supported many of these programs, particularly in the area of training and retraining, and feel that they undoubtedly have accomplished much. The trouble is that too often these programs have fallen short of their potential.

The unhappy experience of the former Area Redevelopment Administration and the confusion and controversy surrounding the poverty program are only two examples of programs which have failed to live up to expectations. These programs and others have been weakened by inefficient administration, bureaucratic conflicts, poor coordination, political meddling and overenthusiastic efforts to produce quick and sensational results.

Contrary to what we are sometimes told, Americans of both political parties do care about the hopeless and deprived of our society. But there is a difference between concern and accomplishment.

There is still a place for new, well-conceived programs to aid the unemployed and poor. However, we feel that there is an even greater need to improve our present programs. We should seek to—

—modernize and better coordinate training and retraining efforts carried on under the vocational education program, the military services, the Manpower Development and Training Act, apprenticeship programs, the poverty program and the Economic Development Administration;

—strengthen the Federal-State Employment Service by improving its capacity to provide occupational guidance and testing, by developing interarea recruitment procedures by the use of modern computer techniques, by closely coordinating the Service's work with private employers to encourage voluntary listing of job vacancies and advance notice of mass layoffs, by carrying on more research on manpower problems and by strengthening the critically important private employment services rather than competing with them where they are doing a good job;

—improve our economic security programs, principally unemployment insurance, by raising benefit payments and lengthening the benefit period, increasing slightly the waiting period for benefits and by more adequately tying in manpower training for the long-term unemployed with the provision of unemployment compensation;

—facilitate the mobility of the labor force by encouraging the transferability of pensions and other rights, eliminating tax impediments to changing jobs, considering subsidizing the migration of workers out of severely depressed areas and paying transportation and living allowances to unemployment insurance claimants who seek a job beyond a predetermined distance from their homes;

—encourage individuals to upgrade their skills by eliminating tax obstacles in the path of new skill development, by increasing training in basic skills of reading, writing, and arithmetic, by convincing the States to permit unemployment insurance claimants to receive normal benefits while undergoing training or retraining and by providing tax incentives to business (as through the Human Investment Act proposed by House Republicans) to step up their programs of on-the-job training.[8]

[8] Senator Javits supports the objective of the Human Investment Act, but favors an approach such as is developed in his bill (S. 2343), which provides for including the expenses incurred by employers in providing training and retraining programs for their employees and prospective employees as expenses which qualify for the investment credit under sec. 38 of the Internal Revenue Code of 1954.

—encourage employment of teenagers and other low skill individuals by considering enactment of a two-step minimum wage, with the Government subsidizing the employee for the difference between the actual wage paid and the minimum wage.

By no means does this list exhaust possibilities where existing programs could be strengthened. It does emphasize, however, the extent to which such programs could be improved and often at small cost. While progress along these lines may sometimes seem slow and unspectacular, it offers more chance of success than efforts to do too much too soon. These objectives could be better realized over the long run by creation of a National Commission on Economic Goals along the lines of the Eisenhower model and as proposed in a bill introduced by Senator Javits.

We believe it is time to stop playing emotional and political football with the hopes of the poor and deprived. The goals of the Great Society can be achieved, but not by the grandstand play. The humdrum business of collecting job vacancy statistics or conducting a census of the unemployed may not win many votes, but it will enable our policymakers to chart their course with an intelligent and well-informed understanding of the problem. With the present gaps in information, this is more than they can do now. The knowledge gained can be applied to better conceived and better coordinated programs that can offer the deprived a passport to the Great Society that is already a reality for the vast majority of Americans.

THE BALANCE OF PAYMENTS AND THE GOLD DRAIN

Administration officials have painted a misleading picture of the progress that was made in reducing our chronic balance-of-payments deficit in 1965. The payments deficit and the gold outflow continued at a high level last year, and we see little prospect for improvement during the current year despite the heavy price paid for the time being bought.

A committee of distinguished experts appointed by the administration to review our balance-of-payments statistics unanimously recommended last April that the official settlements basis should be the main measure of surplus or deficit. The committee said that—

> The United States has a deficit which cannot be indefinitely continued * * * if its reserve assets are declining and/or if the claims of foreign monetary authorities on the United States are rising.

By this test the United States continued in serious deficit in 1965.

Although the administration incorporated the official settlements figure in its balance-of-payments statistics as a result of the committee's recommendation, its statements on the results for 1965 have played down the official settlements computation and have stressed instead the improvement registered by the liquidity measure.

On the official settlements basis the deficit for 1965 was $1.38 billion, compared to $1.25 billion in 1964. The official settlements deficit actually was slightly larger than the deficit on a liquidity basis. This is particularly meaningful since from 1958 to 1964 the official settlements figure was lower by about $900 million a year than the liquidity measure.

Large Gold Loss

The deepening of the deficit on an official settlements basis reflects the growth in official foreign dollar balances last year as well as the large gold losses which the United States sustained. The gold drain totaled nearly $1.7 billion between December 1964 and December 1965, following a loss of only $125 million in 1964. Increases in official dollar holdings represent an additional threat to the diminishing U.S. gold stock.

Short-term dollar liabilities to foreigners, both private and official but excluding international and regional organizations, reached $24 billion in 1965. Our gold stock today covers only 57 percent of these liabilities. This compares with ratios of gold to the same liabilities of 65 percent in 1964 and 73 percent in 1963. Clearly the improvement in the balance of payments on a liquidity basis is being accompanied by a heightened vulnerability of our existing gold stock to large and sudden withdrawals. This represents one of the greatest sources of instability in the present international monetary system.

Even the improvement on the liquidity measure is, in a sense, artificial and bought at a very high cost in terms of the movement away from a more open international economy. It depended on the existence of what the administration terms "temporary" and "voluntary" restraints on U.S. private direct investment and bank lending. While these programs have achieved temporary short-term results, their long-term effectiveness in reducing capital outflows is open to serious question.

The short-term effectiveness of these programs also masks a serious deterioration in other items of our balances of payments. Principal among these was a shrinkage of our trade surplus by $1.9 billion in 1965. Partly as a result of a booming domestic economy combined with a slowdown of growth in Europe, U.S. exports rose only 4 percent while imports increased by 15 percent. This development was particularly disturbing in the light of the administration's optimism about the trade surplus expressed in its 1965 Economic Report.

Another reason for the decline in the trade surplus was the worsening of our competitive position overseas. From 1964 through the third quarter of 1965 prices of U.S. exports rose slightly faster than export prices of the rest of the developed world. A recent report by the United Nations showed that during the first 9 months of 1965 Western Europe strengthened its trade position in the developing world relative to the United States. While our exports to the less developed countries rose only 3 percent during this period, those of Western Europe rose 12 percent. Also, for the first time in years, wholesale prices have been rising faster in the United States than in most countries of Western Europe.

Investment Linkage to Exports

The close linkage of U.S. private investment and our export trade raises another fundamental question about the degree to which the "voluntary" program of capital restraints contributed to the sharp reduction in the rate of increase of our exports. The linkage between overseas investment and exports was recently studied by the Department of Commerce. The results showed that exports from the United States to foreign affiliates of U.S. firms comprised 25 percent of total U.S. exports in 1964 and one-third of nonagricultural exports. Moreover, exports to affiliates grew by 18 percent from 1963–64, faster than exports as a whole. In addition, some U.S. businessmen have complained that the reduction of bank lending abroad has curtailed export financing and contributed to the difficulties of increasing their exports.

Restraining capital outflows not only diminishes our trade surplus, but the program will have the inevitable effect of reducing income from foreign investments, which again in 1965 was one of the strongest elements in our overall payments position. The longer the voluntary program continues (and its promised termination next February is now in grave doubt), the more prolonged and serious will be the ultimate reduction in foreign income flows.

We commented at length in our minority views last year on the self-defeating character of capital controls. Not only are the immediate benefits of the program offset in part by reduced exports, but they will result in reduced income flows. Most seriously, perhaps, they undermine the financial leadership of the United States. The United States is a capital-rich country. The rest of the free world depends on U.S. funds very heavily in order to develop and strengthen their own economies. This in turn strengthens the U.S. economy and the entire free world.

If 1965 was not as good a year for the balance of payments as the administration claims, the current year is likely to be little better. The administration already is hedging its earlier predictions that the United States would be in approximate balance this year. The blame is laid at the door of Vietnam spending.

Trade Surplus Increase Unlikely

The administration expects a substantial increase in the trade surplus to offset the foreign exchange costs of the Vietnam war. It would be more realistic to assume that the booming domestic economy and sharp increases in the wholesale price index would make an improvement in the trade surplus exceedingly unlikely. In addition, the tourist deficit will continue to widen. The balance of payments will also fail to benefit this year as it did in 1965 from large and essentially one-shot repatriations of liquid funds by financial and nonfinancial corporations in response to the "voluntary" program.

There will be some offsetting gains. Private investment income will continue to grow and direct investment outflows may continue to moderate. But on balance we look for little or no improvement in the balance of payments this year. If the costs of the Vietnam war—which have been consistently underestimated—grow sharply, or if domestic inflation accelerates, there will surely be a worsening of our payments position.

We strongly urge that the program of "voluntary" restraints on capital movements be abandoned at the earliest possible time.[9] They should be replaced by a balance-of-payments program which deals with fundamental economic forces as well as certain Government policies which lie at the root of our chronic deficit. Such a program should include:

1. *Elimination of inflationary pressures in the domestic economy.*—Unless domestic costs and prices are controlled, other policies to correct the balance-of-payments deficit will be superfluous. For the first time in a number of years the requirements for a stable domestic economy and a more favorable balance-of-payments position coincide. The sharp worsening of our trade surplus last year lends particular urgency to the need to control costs and prices at home. A stepup in cost and price inflation will produce massive deterioration in our trade position. Under these circumstances, preventing a collapse of international confidence in the dollar probably would require the imposition of compulsory controls over capital outflows and tourist spending. Certainly present programs would be inadequate to do the

[9] Senator Javits has long opposed the interest equalization tax and has pointed out that the voluntary program of restraints on private capital outflows is counterproductive, especially if maintained over a long period. He would prefer to see a more selective approach that would not impair U.S. financial leadership abroad. He would emphasize expanding exports and reform of the world monetary and credit system.

job of keeping our overall deficit within tolerable bounds under these conditions. Since every effort must be made to avoid compulsory controls, we urge implementation of our recommendations for stabilizing the domestic economy as also being essential for an improved balance of payments.

2. *Redoubled efforts to stimulate U.S. exports.*—The administration's efforts to expand U.S. exports have been feeble and unimaginative. Some of its policies have actually resulted in a decline of exports. We urge that the administration make new proposals to create interest among businesmen in selling abroad, stimulate foreign interest in U.S. products and devise new and improved methods of financing exports. Vigorous efforts are needed to bargain down tariff and nontariff barriers to our exports and to remove discriminatory ocean freight rate differentials. We also believe that ways of rebating the corporate tax payments to U.S. exporters should be a subject for negotiation in the Kennedy round in order to bring our practices into line with that of many other foreign countries.

3. *Reexamination of military and foreign aid expenditures overseas.*[10]—The added requirements of the war in Vietnam lend special urgency to finding means of reducing the foreign exchange costs of other expenditures by the U.S. Government overseas.

The administration has called for a new look in foreign aid, an objective which the Clay committee recommended as long ago as 1963. We urge support for these efforts to streamline the foreign aid program and increase its efficiency and effectiveness. At the same time, we believe the administration should press for implementation of the recommendations of the Advisory Committee on Private Enterprise in Foreign Aid in order to speed the flow of private capital to the developing countries.

Deployment of American troops, particularly in the NATO countries, should be reexamined in the light of Western Europe's increasing strength and the Nation's growing airlift capacity. The administration should also make an effort to increase offset agreements, involving allied purchases of U.S. military equipment, with those countries possessing large and growing international reserves.

4. *Promoting foreign investment in the United States.*—We urge the passage of legislation to provide tax reciprocity for foreign investment in the United States.

5. *Promoting foreign travel to the United States.*—Greater efforts should be made to increase foreign travel to the United States. A proposal designed to achieve this by strengthening the U.S. Travel Service has been introduced by Senator Javits and cosponsored by a bipartisan coalition in both the House and Senate.

6. *Achieving international monetary reform.*—We have been gratified that discussions have finally started on reform of the international monetary system. For the past 2½ years we have strongly urged that the administration take the initiative in this area in order to prepare for the day when the United States eliminates its balance-of-payment deficit. It is clear, however, that any serious deterioration

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[10] Senator Javits continues to believe that foreign economic and military aid is on a parity with military expenditures in terms of the national interest. He believes we must look to our worldwide responsibilities notwithstanding the Vietnam struggle.

in the U.S. balance of payments during the current year will undermine the work that has been done and delay needed improvements in the system.

Agreement on a rational method of creating reserve assets is particularly urgent in the light of the sharp slowdown in the growth of reserves over the past year. The reserve assets created by international agreement should be large enough to provide for the growing needs of world trade and payments and should be distributed in equitable fashion not only to the rich industrial countries but to the developing nations as well. We urge the administration to move forward with this work while undertaking fundamental correctives to alleviate our continuing balance-of-payments problem. It must be constantly emphasized that improvements in the international monetary mechanism are no substitute for correcting our balance-of-payments deficit.[11]

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[11] While Senator Javits believes that the recent levels of U.S. balance-of-payments deficits have been too high, he does not feel that immediate elimination of the deficit is a necessary or desirable goal in view of the key currency role of the United States, our position as banker for the world, and the important part dollars have played in increasing international liquidity.

INTERNATIONAL TRADE

A. THE "KENNEDY ROUND" OF TRADE NEGOTIATIONS

The sixth round of tariff negotiations under the General Agreement on Tariffs and Trade (GATT) began in May 1963, with great expectations to increase international trade through reciprocal reduction of tariffs on industrial as well as agricultural products. There was also a new emphasis on removing nontariff trade barriers and a special concern for the less-developed countries.

The sixth round was conceived as more than a simple tariff bargaining session. It was to help create a stronger and more cohesive Atlantic Community, a central goal of American foreign policy in Europe for over a decade. The political importance of the Kennedy round has not diminished with time. Thus, for political as well as economic reasons the United States should continue to use every means at its disposal to press the trade negotiations to a successful conclusion.

The 6-month hiatus in EEC activity arising partially from the French boycott beginning June 29, 1965, was broken at a ministerial meeting of the Six on January 28, 1966. Now the EEC must complete its internal economic negotiation and decisionmaking on issues regarding the Kennedy Round. The EEC has little time to do so, and it has been so informed. Deputy Special Representative for Trade Negotiations Ambassador William M. Roth in a speech on February 14 said that:

> We must get back to the hard bargaining by midspring so that we have the outline of a package by midsummer. It will take another 6 months or so to negotiate the many fine points that give balance to the package. The deal must be set by early 1967 so that all necessary procedures can be completed in time.
>
> The Six have a very short period in which to resolve their internal problems if they are to return to the negotiations by spring. Soon after returning, they will have to table concrete and specific agricultural offers and these must be of real trade meaning if they are to be accepted as a basis for bargaining.

But the prognosis is not optimistic. Very delicate, very difficult matters must be settled. Among them are the size of the EEC exceptions list vis-a-vis that of the United States, the issue of "tariff disparities," the problems involved in achieving the goal of "acceptable conditions of access to world markets for agricultural products," and various nontariff barrier items, which can, however, carry over beyond the June 30, 1967, deadline.

If, however, by the end of 1966 the EEC has not demonstrated clearly and unequivocally its intention to move forward in concrete bargaining on both the industrial and agricultural fronts, new avenues of approach should be sought. Under no circumstances should the United States rush to complete an arrangement that could make a mockery of the original hopes and goals of the 1962 Trade Expansion Act. On the other hand, if by the end of the year, there is concrete evidence that the EEC will come willingly to the bargaining table with constructive intent, then the 90th Congress should consider extending the 1962 Trade Act's negotiating authority for one year.

The goal of a greater Atlantic community, closely knit economically, politically, and militarily, and open to all free countries, is one which we must pursue as the central theme of U.S. policy. Constructive proposals to avoid the deadlock in which we find ourselves are welcome, always recognizing that the continuing effort at Geneva is one of the best means at the disposal of the United States to encourage the EEC countries to reach internal agreement on key economic issues, and in so doing to resolve political differences.

B. EMPHASIS ON NONTARIFF BARRIERS TO INTERNATIONAL TRADE

The GATT trade negotiations, since their beginning in 1947, have concentrated on the reduction of tariffs. This GATT effort, of course, was part of the postwar movement to free international flows of capital and trade. As such it recognized the importance of good economic relations in maintaining peace. It was an attempt to strike at the many root economic causes of World War II.

In large measure the GATT tariff negotiations under the five previous tariff negotiating rounds have done their work. The tariffs of most nations are at a reasonably low level, with those of the United States among the lowest. In the U.S. case the extraordinarily high tariff rates imposed by the Smoot-Hawley Act (Tariff Act of 1930) have been greatly lowered, with some notable exceptions. The U.S. tariff schedules have been newly systematized and rationalized somewhat along the lines of the Brussels tariff nomenclature.

Thus, were the "Kennedy Round" to be successfully completed, tariffs on the whole would cease to become a major trade barrier. Unfortunately, as tariff barriers have diminished other barriers to international trade, more pernicious and often hidden, have arisen. These "nontariff barriers" can take many forms. Such barriers can be built into tax systems, health and sanitary regulations. They can have a highly protective effect. The United States maintains some notable nontariff barriers to trade, but in contrast to those of many of our trading partners, ours are relatively few and those that exist are largely published and "above the table."

As Mark S. Massell, senior staff member of the Brookings Institution, wrote recently:

> Agreements to reduce import duties constitute only the first step of an effective program to free world trade. If tariffs are reduced to a minor role in international trade, the nontariff barriers will take on major importance. As a con-

> sequence, even an effective program to lower tariffs, standing alone, may not achieve a major improvement in the flow of international trade. Indeed, the complete elimination of tariffs would encourage the proliferation of a wide variety of the more subtle import barriers which bear the tag "nontariff."

We believe the future trade negotiations must concentrate not on tariff but on nontariff trade barriers. These far more knotty international problems should be the subject of consistent effort by the Special Representative for Trade Negotiations, during and between formal GATT negotiating rounds. Fetters on international trade cannot be removed so long as there is a preoccupation with tariffs and a neglect of nontariff barriers.

Among the efforts in the nontariff area which should receive special attention by the President's Special Representative for Trade Negotiations, we urge the development of an international code to harmonize antidumping laws and procedures of trading nations: House Resolution 405 and Senate Resolution 133 (89th Cong., 1st sess.), introduced respectively by Representative Curtis and Senators Javits, Jordan, and Miller, called on the U.S. Government to negotiate an international agreement that would harmonize the operation of the antidumping laws and regulations of major trading nations. The Special Representative for Trade Negotiations has recently made significant progress toward this goal, with the cooperation of the Treasury Department. We urge them to continue to seek agreement on such a code. The goal of an international antidumping agreement is a realistic one, and through it a nontariff trade problem common to all major nations will be solved.

FEDERAL-STATE-LOCAL FISCAL RELATIONS [12]

By any measure, expenditures of State and local governments have risen substantially over the past decade. In the 10-year period beginning in 1954, when gross national product rose at an average annual rate of 5.5 percent, State and local direct general expenditures rose an average of 8.5 percent a year. During the same period, Federal spending rose at an average annual rate of 6 percent. State and local outlays totaled over $70 billion in 1965 and are expected to pass $100 billion by 1970.

Pressures producing higher and higher levels of spending at the State and local levels are not likely to abate in the foreseeable future, but are almost certain to increase. The total population will continue to grow at a rate at least as fast as in recent years. Within the total, there will be relatively large increases in the rate of growth of those segments of the population making the largest demands on the services of State and local governments. For example, the number of elderly dependent persons will increase substantially, as will those people living in costlier, urban areas.

The growth of demand for government services at the State and local levels will experience a qualitative increase as well as the quantitative increase noted above. With generally increasing economic affluence comes a growing demand for improved government services. The aspirations of the lower income classes are being raised and consequently their demand for more and improved government services at the State-local level also rises.

The increase in State and local revenue from their own sources has also risen substantially over the past 10 years. General revenues from internal sources rose 124 percent to $58 billion during that time, while GNP rose only 71 percent. In spite of this growth, however, State and local governments have relied increasingly on borrowing and Federal grants-in-aid to finance their rapidly growing expenditures. Revenue from the Federal Government has increased 237 percent over the past decade to over $10 billion in 1964. State and local debt outstanding rose to $92 billion in 1964, a 137-percent increase over its level 10 years before.

Revenue Sources Grow Slowly

The primary reason State and local governments have been unable to meet their increasing expenditure commitments from their own sources is that their revenue sources tend to grow at a slower rate than GNP. The traditional instruments of State and local revenue, sales, excises and property taxes, are by and large income inelastic, that is, their yields grow at a slower rate than overall GNP. This is especially

[12] Representative Curtis disagrees with the conclusions and recommendations of this section. (See his supplementary views, p. 76.)

undesirable at a time when expenditure increases are far outpacing the growth of the economy. The States and localities have mitigated somewhat the results of the low sensitivity of their revenue sources by increasing tax rates, but this action still has not yielded sufficient revenue to cover rising expenditures. And it is doubtful that States and localities can continue to raise consumption, payroll, and service taxes at anywhere near the rate they have been increasing them over the last decade.

The financial plight of our larger cities is particularly acute and deserves special attention. The influx of population into the cities consists largely of those groups with the greatest demands for Government services. Newcomers to the cities often lack the skills necessary to earn a decent living and tend to settle in deteriorating neighborhoods, increasing the load on health, education, and welfare programs. At the same time, there is an increasing outflow of citizens in the upper and middle income classes to the suburbs, stripping the cities of leadership talent, the self provision of many services which the cities would otherwise have to provide and essential tax dollars.

This outflow seldom diminishes the need for maintaining costly inner-city operations because the emigrants often continue to earn their living in the cities as commuters. Add to this outflow the exodus of industry to the suburban areas, where land and taxes are cheaper and the labor plentiful, and an even further erosion of the cities' tax base takes place, as well as a decrease in sources of employment. The growing needs of our cities for increased revenues must be considered especially critical at this time with little prospect that they can satisfy their needs from their own resources.

The tightening fiscal squeeze on State and local governments has received a great deal of attention recently, and justly so. But unfortunately, although the financial positions of States and localities have been rapidly deteriorating since the end of World War II, it has been only in recent years that significant steps have been taken by the Federal Government to provide aid. This assistance has largely taken the form of grants-in-aid tied to specific activities, which has proven to be a mixed blessing. Although the grants have enabled the lower levels of government to expand functions that the Federal Government has designated vital, these governments have little influence on which projects are considered critical and often are required to direct a portion of their own revenues toward federally chosen projects, aggravating the shortage of funds available for activities in which the States and localities are vitally interested. For example, about 45 percent of the increase in Federal aid to the States over the last 10 years has been earmarked for highways and another 25 percent restricted to public welfare.

Federal Grant Programs

There are presently over a hundred different specific Federal grant programs, each with many conditions attached. Aside from increasing the complexity of State and local budgetary problems, this situation unavoidably leads to overlapping and waste, confusion of objectives, and inefficient administration at the Federal level. While we do not suggest a reduction in the present size of the Federal grant-in-aid program, we do oppose increased complexity, regulation, and awkwardness.[13]

The strengthening of State and local control over their own spending is essential in a federal system of government such as ours. A level of government without effective control over directing its expenditures has essentially lost its identity and justification as a separate political entity. Those levels of government closest to the people are most responsive to their wishes and best equipped to most efficiently administer programs for the health, education, and welfare of their citizens. In order to strengthen these governments to meet their increasingly heavy responsibilities, the trend toward fiscal centralization must be restrained.

Among many proposals to help solve the State-local financial dilemma, three stand out as being particularly worthy of consideration. These are the revenue-sharing plan introduced by Senator Javits in the Senate (S. 2619) and by Representative Ellsworth in the House (H.R. 11600), the revenue-sharing proposal for education made by Senator Miller, and the income-tax-credit approach.

Under the Javits and Ellsworth plan, a trust fund would be established into which the Federal Government would deposit 1 percent of aggregate taxable income each year. Payments from the trust fund to the States would be made in the following manner. The most substantial portion of the trust fund would be distributed to each State on a population basis with each State's allotment being adjusted according to its revenue effort relative to the average effort of all the States. The remaining portion of the fund would be distributed to the lowest quarter of the States in per capita income, each State's allotment determined on the basis of population. The only restriction placed on the State allotment is that it must be spent on programs in the fields of health, education, and welfare and not on programs already liberally provided for by the Federal Government, such as highway construction and disaster relief, or on general administrative expenses or debt service. Provision is made for local government aid by requiring the States to contribute to its local governments no less a percentage of its own revenues than the average over the previous 5 years.

Under the proposal made by Senator Miller, the Federal Government would allocate a percentage of the total Federal revenue collections to the various States "for education purposes." This would provide assistance to the States in coping with the increasing costs of education, while avoiding Federal bureaucracy and controls in this area.

Tax Credit Proposal

A uniform tax credit approach to providing unrestricted Federal fiscal aid to States and localities has not been spelled out in detail or introduced as a bill in Congress, yet the concept deserves careful attention. The object of this approach is to have the Federal Government

[13] Senator Javits notes that Federal grant-in-aid programs tend to discriminate against highly urbanized States. Traditional allocation formulas ignore the fact that the extraordinary growth of the cities has multiplied their need for funds more sharply than the allocation formulas provide increased Federal funds. He urges early enactment of S. 561, which calls for periodic congressional review of further grant-in-aid programs, so that allocation features are not endlessly perpetuated without any conscious reevaluation from time to time, as conditions change, of formulas, ratios, and maximum limitations.

help the States and localities raise more revenue through their own revenue instruments without increasing appreciably the combined Federal-State-local tax burden on individual taxpayers.

All plans in this category involve a credit against Federal income tax liabilities for taxes paid to State and local governments either in place of or in addition to the present provision allowing taxpayers to deduct State and local taxes in figuring Federal taxable income. Some experts propose to allow only certain State and local tax payments, such as on income, to qualify for the credit while others would permit all types of State and local taxes paid to qualify.

Some suggest that a certain percentage of State and local taxes paid be allowed to comprise the credit, while others recommend allowing some percentage of the individual's Federal income tax liability as a ceiling on the amount credited. While the many different tax credit approaches differ in details, all provide for unrestricted aid to State and localities to strengthen their fiscal positions.

Both the tax credit approach and the revenue sharing proposals deserve careful study. Although budgetary conditions now preclude immediate enactment of such legislation, we believe that the groundwork should be laid now for early action when inflationary pressures ease. To that end, we strongly recommend that the relevant congressional committees begin hearings soon on these approaches to saving our State and local governments from fiscal impotence and ultimate Federal assumption of control.

STRENGTHENING THE FARM SECTOR

Despite the self-serving claims of the President's Economic Report that living standards have risen at an unprecedented rate and that realized net income per farm rose in 1965, the fact is that the continued cost-price squeeze has prevented the Nation's farmers from sharing fairly in the national net income. There are two reasons: (1) Continued inflationary increases in the prices farmers pay for goods and services; and (2) farm parity prices consistently below 81 for the fifth consecutive year.

On the cost side, the November 1965 issue of the Farm Cost Situation, published annually by the Economic Research Service of the Department of Agriculture, shows an increase in the index of the cost of goods and services used in agricultural production from 103 to 112 from 1960 through 1965. Farm machinery, seed, and wages represent the largest increases, mainly because of general inflationary pressures.

When the purchasing power of the dollar goes down, it is to be expected that wage earners will ask for wage increases. An increase in the social security tax withheld from the worker's paycheck will be followed by a demand for an offsetting wage boost. Increased costs to the manufacturer—wage hikes and more taxes to match the increase in employee social security taxes—means an increase in farm costs of production. Over the past 5 years, these costs have climbed $4 billion—almost $1 billion in 1965 alone. A substantial portion of this increase is the result of inflation.

It is truly alarming to farmers that notwithstanding increased costs of farm production and costs of Federal farm programs, farm prices have remained depressed. Farm parity prices were at 81 in December of 1960 and have been consistently lower ever since. Notwithstanding an improvement in livestock prices, the average parity ratio for 1965 was 77; and it has averaged less than this since October of 1962. The Food and Agriculture Act of 1965 continued the power of the Secretary of Agriculture, through sales of surplus commodities by the Commodity Credit Corporation, to hold down market prices of grains; and the Secretary has made it clear that he intends to continue to use this power.

Indebtedness Increases

Indebtedness of our farmers has increased by $14.8 billion during the last 5 years—from $26.2 to $41 billion. Although proprietors' equities have grown to record levels, as noted in the President's Economic Report, as farms have been consolidated into larger units and more farmers have been forced out of agriculture by the continued cost-price squeeze, the ratio of farm debt to total farm assets has worsened.

The total increase in net farm income over the last 5 years compared to 1960 net farm income has been $5.2 billion. During the same period, Federal Government payments increased by over $6 billion. Thus the agriculture sector has grown more dependent on the Federal Government—necessarily so as markets have been adversely affected by the power of the Secretary of Agriculture to dispose of surpluses at low prices; at the same time, farmers have not been sharing fairly in the national net income due to the cost-price squeeze.

The number of farmworkers continued to decline in 1965. There has been a loss of 401,000 hired farmworkers and 1,047,000 farm family workers since 1960. The loss in farm employment in 1965 alone was more than 500,000. Total farm population declined in 1965 by 554,000, bringing the 5-year loss to over 3.2 million.

The Republican Party has continued to emphasize that farm programs should be continued, but that they should enable our farmers to share fairly in the national net income by moving toward good market prices and not away from them. The foregoing record lends little credibility to the nice-sounding recitals which appear in the administration's farm bills: "to increase farm income, reduce surpluses, and reduce costs to the Government." Net farm income, in terms of "real" dollars (and not the present cheap dollars resulting from inflation), has not kept pace with the rest of our economy. The administration's farm programs have not reduced production, and production has actually increased under them. Surpluses have been reduced because of increased domestic usage and increased disposals under Public Law 480 (the food-for-peace program), which was commenced during the Eisenhower administration. And, as shown above, costs to the taxpayers have increased.

We are pleased to note that the Economic Report for 1966 contains a chapter specifically devoted to agriculture and farm sector problems. Unfortunately the Council of Economic Advisers has not fulfilled its obligation under the Employment Act of 1946 to consult with representatives of agriculture.

Rural Poverty

We are pleased to note that the President has recognized the necessity for a different type of planning to attack rural poverty. We have pointed out in previous years that many of the areas of chronic economic depression are rural and that these areas do not share proportionately in existing antipoverty programs.

It is significant that agricultural labor has the lowest per-hour return of any of the major segments of our economy. This reflects the unsatisfactory level of farm parity and the steadily increasing costs of production, which deprive farm operators of the means to increase wages.

Republican spokesmen have long supported the concept of adequate reserves of feed and food grains that are needed to provide security to our country in the event of national emergencies. Not until this is done can one intelligently talk of surpluses, because only the amounts of such commodities which are in excess of such needed reserve are properly termed "surplus."

We support improvements in and continued development of Public Law 480 enacted during the Eisenhower administration to enable our agricultural production to meet the needs of the developing nations on a self-help basis. We have consistently advocated maximum efforts to make such use of our agricultural abundance and support efforts to strengthen the structure and performance of the program.

The greatest emphasis in the research activities of the Department of Agriculture continues to be on the production side as distinguished from the marketing and consumption sides. While foreign exports, disaster relief, Public Law 480, and other tools we are now using to dispose of agricultural commodities are very useful, we have not yet made full use of our research resources in finding industrial uses for agricultural commodities. Exceptional developments have occurred in recent years. However, less than 10 percent of the fiscal 1966 research budget is devoted to industrial uses of agricultural commodities; whereas the great portion of these research funds is earmarked for continued production research. We believe that the emphasis should be the other way.

We recommend that the administration take coordinated action along the following lines:

1. Reorient the whole network of Government price-support programs toward a strong market economy for agriculture.
2. Reject the doctrine of "supply management," which, as presently administered, means strict Government controls and supervision over farmers with market controls exercised by the Secretary of Agriculture.
3. Reorient the research activities of the Department of Agriculture to develop new and increased uses for agricultural products.
4. Establish sound inventory and reserve policies for all price-supported commodities, with disposal of such stocks not to be permitted in a manner which disrupts normal markets.
5. Take action to encourage greater industrial and economic development in rural areas through coordinated Government efforts and program administration to provide rural areas a fair opportunity to share in increased economic growth.
6. Adopt enlightened fiscal policies to stop inflation and, in turn, stop the increases in costs of farm production.
7. The Council of Economic Advisers should take immediate action to fulfill its obligation to consult with a fair representative cross section of farmers.
8. In order to further the objective of increasing U.S. agricultural exports, U.S. negotiators at the Kennedy round of trade negotiations in Geneva must continue to insist that U.S. concessions on industrial products be contingent upon European concessions on our agricultural products.

NATIONAL EMERGENCY STRIKES

Recent labor disputes in key industries have demonstrated the lack of adequate Government powers to assert the public interest in disputes which affect the health and safety of the Nation or a substantial part of it.

A crisis of national proportions in the railroad industry was narrowly avoided in 1963, but may threaten again this spring. Last year's dock strike closed some of our major ports for long periods, while the steel labor crisis last fall was resolved only after it brought the Nation to the brink of economic disaster. And it will be some time before New York's crippling transit strike last January is forgotten.

If we learn nothing else from these unhappy experiences, it should be that the whole Nation or individual communities can be immobilized by key labor disputes and that Government is virtually powerless to do anything about it.

The steel dispute provided a glimpse of another danger arising from the lack of adequate machinery to deal with national emergency strikes. In that instance, the President personally intervened to protect the national interest. In the absence of adequate legal machinery, the administration virtually wrote the contract for steel management and labor. The dangers of such interference with private decisionmaking is obvious. Settlements dictated by third parties cannot solve the underlying causes of labor-mangement disputes, but only suppress them until they arise again some other day. For lack of better machinery to deal with this problem, we are edging close to a system of compulsory arbitration which is inconsistent with free collective bargaining and a free trade union movement.

Legislation is needed to give the President new and critically necessary powers to protect the public interest in labor disputes of a national character, without in any way depriving the parties of the power to write their own collective bargaining agreements. A bill (S. 2797) introduced by Senator Javits would establish machinery to accomplish this goal.

The bill would authorize the President to appoint a board of inquiry to make public recommendations for a settlement based on factfinding in cases where a labor dispute materially affects the national health or safety.

The President would also be authorized to order a 30-day freeze during which the parties would be required to bargain upon the recommendations. However, neither party would be required as a matter of law to accept the recommendations.

Finally, the President could seek appointment by a Federal court of a special receiver to operate the struck facility to the extent necessary to protect the national health and safety.

This bill would extend coverage of the emergency labor disputes provisions of the Taft-Hartley Act to controversies which, though they may not affect an entire industry nor imperil the health of the Nation as a whole, do affect interstate commerce and imperil the health or safety of a substantial part of the population or territory of the Nation.

The Javits plan is a constructive proposal for providing maximum protection of the public interest with a minimum of Government interference with the collective bargaining process. Under the procedures of the bill, labor and management could bargain rationally and produce a settlement beneficial to both. At the same time, the public would be protected against harmful disruptions in key industries affecting the national health and safety.

We believe the proposal merits most careful study and recommend that the appropriate committees of Congress begin immediate consideration of the bill.

CONCLUSION

The administration never tires of claiming that its "new economics" have brought the American people 5 years of unprecedented prosperity and economic growth. How valid are its claims?

There is a danger that the administration's attempts to rewrite economic history may convince the Nation that the road to permanent prosperity requires continuing budget deficits, ever-higher levels of Government spending and increasing Federal controls over private economic decisionmaking. For this reason, we think the record must be set straight.

The record of the past 5 years actually shows that—

—the dynamism inherent in the private economy was already powering a vigorous recovery from recession as the Kennedy administration entered office in 1961.

—after increasing Government spending sharply in 1961 and 1962 and applying other stimulative measures, the advance stalled and the economy was threatened with recession in 1962.

—the recovery resumed its advance in 1963 only after the administration restored business confidence shaken by the steel-pricing episode of the previous year by supporting incentives for job-creating private investment and risk taking, which Republicans had long urged.

—the tax cut of 1964 was successful in removing impediments to economic growth because it made reductions in exceedingly high rates and at Republican insistence was accompanied, at least temporarily, by firm restraint of Federal spending.

—in the face of administration indifference and even hostility, Republicans successfully fought for legislation to correct structural imbalances in the economy through manpower training and retraining and strengthening the vocational education system.

—the Kennedy administration inherited a sound cost-price structure from the Eisenhower years which permitted expansion without inflation until the Johnson administration unleashed a new wave of Federal spending in 1965.

—the administration continues to talk about a peacetime recovery when, in fact, our current growth results from the demands of the Vietnam war rather than the "new economics."

—the administration has proven itself indifferent to the special problems and opportunities connected with the Nation's small business community. Despite Republican prodding, it refuses to adequately fund the Small Business Administration disaster and regular loan programs in separate accounts, and moves to deprive the small businessman of an independent Small Business Administration voice within Government counsels.

The lesson to be drawn from this brief accounting of recent economic history is that balanced policies to stimulate the private sector and remove impediments to economic growth has been the source of our prosperity. When business confidence was impaired or when the Government relied too heavily on budget deficits and higher spending, trouble appeared in the forms of inflation, a slowing of business investment and economic growth early in the expansion, and a continuing gold outflow and balance-of-payments problem.

By misrepresenting recent history, the administration has been able to win wide support for enlarging the dimensions of Federal control over the economy. Both the scope and the nature of the Government's involvement in economic affairs have changed significantly in the past 5 years. Government not only plays a larger role in influencing the general level of economic activity, but it has also moved in on areas formerly reserved for private decisionmaking. A few men in Washington have substituted their judgment for that of the marketplace as expressed by millions of daily decisions by leaders of business and labor.

It is surprising and disturbing that the new and ominous dimensions of Federal economic power have been accepted—at least until recently—with such calm acquiescence. Should the trend continue, the relationship between the private sector and the Federal Government will be sharply recast. Our economic system, which has produced unparalleled opportunities and abundance for our people, would be the loser.

Government has an important role to play in economic affairs. But we believe this role should be limited to the wise and balanced use of time-tested weapons of fiscal and monetary policy designed to stimulate creativity and growth among our corporate enterprises, small businesses, farmers, and labor organizations.

Senator JACOB K. JAVITS.
Senator JACK MILLER.
Senator LEN B. JORDAN.
Representative THOMAS B. CURTIS.
Representative WILLIAM B. WIDNALL.
Representative ROBERT F. ELLSWORTH.

SUPPLEMENTARY VIEWS OF REPRESENTATIVE CURTIS

I appreciate the desire of my colleagues to strengthen the fiscal capacity of State and local governments to meet their growing problems. However, I find the arguments they and others advance for new forms of Federal assistance without merit.

These arguments ignore that State and local governments have met their revenue needs successfully in the past. With greater efforts to mobilize their financial resources, they can meet their growing needs in the future. Particularly important is the modernization and updating of the property tax.

One cry for increased Federal Government participation is that the State and local governments are so hard pressed financially that they cannot assume the increased costs of education and other services. This is a peculiar theory in that there is only one source of taxation. Governments, whether State, local, or Federal, are only tax collectors and they can collect taxes only from one source, people. The corporate income tax, as in any business tax, is a tax upon people—not upon some unidentifiable fictitious person—it is primarily a sales tax because every business, if it is to stay in business, has to pass the tax it pays on to the consumer in the price it charges for the goods and services it is selling. Maybe the investor pays a bit of the corporate income tax, but very little, and even if the investor pays some, we must remember that investors are people, too, and increasingly in the United States the investor is becoming every one of us.

So when it comes to easing any tax burden, I am not so inclined to worry about the tax collector—the State or local government—or the Federal Government, as I am about the taxpayer. I think of tax collection from the efficiency of the collection system—the efficiency from the standpoint of the taxpayer so that the minimum amount of cost goes into the collection of the tax and the maximum amount can go into the expenditure of the funds for the purposes intended by the governmental agency. I also want the tax collection for efficiency's sake to be pretty close to the agency of government that is going to spend the money so that there is a minimum of cost in transferring the money from the agency that collects it, to the agency that spends it. Also so that those who spend have a better understanding of the cost of spending, which they do if they are close to those who have to raise the revenues.

By these criteria the Federal Government is not a very efficient tax collector for educational and other expenditures. It is not even an efficient tax collector per se in minimizing the economic cost of the mere collection aspects. The Federal Government is merely efficient in hiding the economic cost of collecting the Federal income tax because it passes the main cost burden of bookkeeping, accounting, and collecting over to the private sector—to the individual person and businesses making out the complicated tax returns. But passing the cost of tax collection over to the private sector does not save the cost economically to our society, it merely avoids some of the blame for the cost being placed where it belongs on the type tax itself and on the governmental body using it. The most efficient tax economically to collect is the real estate property tax. All it requires is an assessment every 10 years or so and a yearly billing—no accounting, no time on the part of the taxpayer, and little time on the part of the tax collector. It is almost all done by mail.

Furthermore, I would observe that it is the Federal income tax that has come in for the greatest criticism from economists and tax theorists in recent years, as well it should. It is the high rates of the Federal income tax which has created the economic damage to our society which we are now trying to remedy by timely tax reduction, not the real property tax or the State sales and use taxes. Yet there are people who would put a further burden on the Federal income tax.

Further, since the Federal Government is not the sector of government which is charged with spending the education dollar, it has the difficult and costly job of transferring the tax dollars collected to the local governmental agencies which are charged with the spending of them. As has often been observed, send a tax dollar to Washington, D.C., to be returned to be spent in the community and it comes back badly clipped. We certainly can cut down on the amount the dollar gets clipped when it is sent on its long journey to Washington and thence back to the community, but we must recognize that there will always be considerable cost in undertaking the round trip journey in the first place. And we may well ask, Is this trip necessary?

The answer is made that the trip and the clip are necessary because we need the Federal governmental mechanism to equalize between the rich and the poor States. It is said that many of the children who need to be educated are in the poor States which cannot afford to bear the costs of education while the ability to pay taxes lies in the richer States. Well, I have often sought to answer this syllogism. I ask, where are these so-called poor States? The answer to that question is quite ready, in the South: Arkansas, Alabama, Mississippi, et cetera. I then ask, But on what basis do you say these are poor States? The answer to this is also quite ready. "Take a look at the per capita income of these States." Indeed, per capita income in these States is relatively low. But then, I ask the next question, and the answer to this is not quite so ready. But these States do not pay for education out of taxes on income, do they? Don't they pay for education costs and community facilities of all sorts essentially by use of the property tax? If this is so, and it is so, let's take a look at the assessed valuation in these States which allegedly are so poor. Here we have the true answer. There are not really any poor States in the United States. The States so often cited are States where there are poorly developed and enforced property taxes, where there is a considerable amount of absentee ownership, among other things, where the assessments on real estate hardly match the true value of the land and structures. These are the very States, by the way, which are digging themselves further in the hole by waiving property taxes for a period of years to entice businesses to locate in their area—on the assumption, I suppose, that having the payrolls will assist them to have a better tax base than one based upon property wealth. This is surely regressive thinking for the 20th century. This theory can be found entrenched in most of our Latin American neighbors and throughout the world and until the theory is abandoned these societies will not move ahead.

No, there is no need for the Federal Government to get into the business of Federal equalization laws, although there is still plenty of reason for all the States to continually update their State equalization laws for education. And there is much room for counties to pass education equalization laws so that tax revenues can be spread from wealthy areas, measured in terms of property wealth to areas of less property wealth. Above all, there is ample room for modernizing our property tax laws and keeping them up to date—which means, among many things, modernizing our zoning laws and keeping them up to date. No community can support schools or community facilities—except the very few unusually wealthy communities—with a property tax based heavily on home assessments.

I like to point to Crestwood, Mo., as an example of up-to-date zoning and assessment. Here is a new community—nonexistent in 1945, about 12,000 population. To a casual observer it looks like a typical middle-income, suburban bedroom community. Yet look at its tax assessment books. Look at its zoning laws and you have the real story. Seventy-five percent of its assessed valuation comes from industry, commerce, and the utilities, only 25 percent from the private homes of its citizens. It has fine schools, fine community facilities, ample revenues, and little debt.

Henry George extolled the values of the property tax further than I would go to the single tax idea and these values should be considered today. In America the real estate tax provides the money which is spent largely in increasing the valuation of the very real estate taxed. Build roads, schools, sewers, provide fire departments and police protection, and the value of the real estate and the buildings increase. The expenditures from the real estate tax go to and relate to increasing and preserving wealth. This makes a neat package and is the basis of the grassroot community growth in America. Furthermore, a well-designed real estate tax is a discouragement to the greatest of all economic sins—to hoard rather than to utilize wealth. A well-designed real estate tax system places an incentive on utilizing real estate to its greatest economic potential—and if a good tax system is established in context with up-to-date zoning laws and building codes, increased wealth flows to the community.

It is the property tax which has responded nobly since the end of World War II—not the Federal income tax. It is the property tax which has financed the increased expenditures for education from a $2.3 billion figure in 1940 to a figure now well over $18 billion in 1965—not the Federal income tax.

Nor is it true that this cornucopia of our communities is running low or needs priming. The expenditures on education have produced what we anticipated they would produce in new and greater wealth which in turn increases the potential for the future flow. Educational bond issues are continuing to be passed by the local citizenry. The HEW statistics reveal that beginning in 1957 when they first collected the percentage of public school bond issues passed per bond issues submitted to the voters, only once has the figure fallen below 70 percent: 1957, 74 percent; 1958, 78 percent; 1959, 62 percent; 1960, 83 percent; 1961, 71 percent; 1962, 70 percent; 1963, 70 percent.

And I hazard a guess that of the bond issues failing many should have failed but undoubtedly most of these bond issues were resubmitted in an improved and corrected form and then passed—a healthy situation in itself not duplicated by the process of local school districts submitting their needs to a political bureaucracy in Washington, D.C.

The second observation I wish to make is that the property tax responded in this noble fashion in spite of the serious difficulties it experienced as the result of the failure of the Federal Government to perform one of its primary functions, namely maintain the dollar as an accurate economic weight and measure by following sound Federal governmental fiscal policies.

The drastic inflation which occurred from 1946 until 1951 placed the property tax systems all over the United States in very serious jeopardy. The property tax systems are based, as I have pointed out, on assessed valuations. Most systems make the specific and multitudinous assessed valuations when the improvements are made to the land inasmuch as improvements amount to the major part of most valuations. Accordingly, most assessments reflect the dollar cost of making the improvement in the year in which it was made. So in 1946, the assessment books reflected valuations in terms of the many years of the preinflated dollar. All new improvements, new homes built after 1951 went on the books in terms of the post-World War II inflated dollar. This process by itself created an inequity in the tax system to the owners of new homes and new improvements, vis-a-vis the owners of older structures. However, the cost of services and goods—teachers' salaries and blackboards—went up with the inflated dollar. Therefore, the revenues, the tax collections, had to be increased, just to stand still, let alone to progress. However, increasing the rate of the property tax aggravated the inequity already existing in the base because of the measuring of new improvements in terms of the inflated dollar. Every community in the United States was faced with a very difficult process, difficult mechanically as well as politically, the process of reassessing all the property on the assessment books in terms of the same dollar. Over 80 percent of our communities have now done this and I would observe they are now in relatively good shape. A small percentage have not assumed their responsibility. Many of these are the communities, and some of them are sizable, which are creating a great deal of the pressure on the Federal Government, through its overburdened income tax system, to bail them out. Yet these communities have it within their power to do exactly what the others have done, painful as it was.

COMMITTEE AND SUBCOMMITTEE ACTIVITIES IN THE PAST YEAR

The Joint Economic Committee is directed by the Employment Act of 1946 (Public Law 304, 79th Cong.) to report to the Congress on the main recommendations of the President's Economic Report and to make a "continuing study" of the economy.

The work of the full committee and the subcommittees for the period March 1965 through February 1966 is summarized below:

FULL COMMITTEE

January 1965 Economic Report of the President

The committee held 7 days of hearings on the 1965 Economic Report of the President (February 19, 22–27), receiving testimony from the Council of Economic Advisers, the Director of the Bureau of the Budget, the Secretary of the Treasury, the Chairman of the Board of Governors of the Federal Reserve System, academic economists, and others. Part 4 of the printed hearings contains invited comments from organizations representing bankers, business, labor, and agriculture.

The 1965 Joint Economic Report

The annual economic report of the committee was filed with the Congress on March 17. This report also contains minority and additional views. (H. Rept. 175.)

Recent Federal Reserve action and economic policy coordination

The committee held 4 days of hearings on December 13–16, to inquire into the actions of the Federal Reserve System in raising the discount rate and the maximum rate that member banks are permitted to pay on time deposits and on certificates of deposit, and the apparent absence of economic policy coordination between the Federal Reserve Board and the executive branch of the Government. Witnesses heard were the Chairman and Members of the Board of Governors of the Federal Reserve System and economists from outside the Government.

SUBCOMMITTEE ON FEDERAL PROCUREMENT AND REGULATION

The Subcommittee on Federal Procurement and Regulation is composed of Senator Paul H. Douglas (chairman), Senators John Sparkman, William Proxmire, and Len B. Jordan, and Representatives Wright Patman, Martha W. Griffiths, Thomas B. Curtis, and William B. Widnall.

Economic impact of Federal procurement

The staff study "Background Material on Economic Impact of Federal Procurement, 1965" was published early in April. The materials contained in this volume provided a useful background for the hearings on "Economic Impact of Federal Procurement" held April 27, 28, and 29. Witnesses included representatives of the Department of Defense, the General Accounting Office, General Services Administration, and the Bureau of the Budget. In July the subcommittee issued its report "Economic Impact of Federal Procurement" as a followup to the recommendations of the subcommittee reports of October 1960, July 1963, and September 1964. The report was based on the hearings held in April, staff field investigations, and staff materials.

Discriminatory ocean freight rates and the balance of payments

Continuing its interest in the subject of discriminatory ocean freight rates, the subcommittee held a series of hearings on "Discriminatory Ocean Freight Rates and the Balance of Payments." On April 7 the subcommittee heard representatives of the Department of Agriculture, the Agency for International Development, and the Military Sea Transport Service. On April 8, representatives of the steamship industry and labor unions testified. On May 27 officials of the Federal Maritime Commission were heard, and on June 30 the Assistant Secretary of Commerce for Economic Affairs and officials of the Office of Transportation of the Department of Commerce presented testimony relating to problems associated with ocean freight rate differentials.

The impact of Government-generated cargo on the U.S.-flag foreign trade fleet for calendar year 1964

In April, during the course of the Maritime Administration's testimony before the subcommittee, a question arose as to the relative importance of Government cargoes to total freight shipments. Subsequently, the Maritime Administration investigated all of the sources of revenue received by the American merchant fleet from Government-sponsored cargo as well as Government-sponsored passenger travel.

This analysis, published by the subcommittee in November, provides very useful knowledge pertinent to the subcommittee's efforts to see established a more rational and equitable basis for setting ocean freight rates.

SUBCOMMITTEE ON FISCAL POLICY

The Subcommittee on Fiscal Policy is composed of Representative Martha W. Griffiths (chairman), Representatives Hale Boggs and William B. Widnall, and Senators Paul H. Douglas, William Proxmire, Herman E. Talmadge, Jacob K. Javits, and Jack Miller.

Fiscal policy issues of the coming decade

Following publication in February of a compendium of statements by individual economists and representatives of interested organizations on "Fiscal Policy Issues of the Coming Decade," the subcommittee on July 20, 21, and 22 held hearings on the same subject. Witnesses included the three members of the Council of Economic Advisers, a representative of the Treasury Department, and the Director of the Bureau of the Budget.

SUBCOMMITTEE ON ECONOMIC PROGRESS

The Subcommittee on Economic Progress is composed of Representative Wright Patman (chairman), Representatives Henry S. Reuss, Martha W. Griffiths, and William B. Widnall, and Senators William Proxmire, Herman E. Talmadge, Jacob K. Javits, and Len B. Jordan

The Federal Reserve portfolio

This volume contains the statements of 86 individual economists who replied to a letter of inquiry sent out by the subcommittee on September 1, soliciting their views concerning the structure and management of the portfolio of financial assets held by the Federal Reserve System.

Great Society programs

The subcommittee submitted a questionnaire on human resource activities to Federal agencies as a first phase of preparing a detailed compilation of human resource programs and a projection of their economic impact in the next 5 years.

A second detailed questionnaire was sent to Federal agencies and a number of private organizations on the financing requirements for State and local public works during the next decade.

SUBCOMMITTEE ON ECONOMIC STATISTICS

The Subcommittee on Economic Statistics is composed of Senator William Proxmire (chairman), Senators Paul H. Douglas, J. W. Fulbright, Herman E. Talmadge, and Jack Miller, and Representatives Richard Bolling, Thomas E. Curtis, and Robert F. Ellsworth.

Measuring the Nation's Wealth

On June 1, 2, and 3 the subcommittee held hearings on "Measuring the Nation's Wealth" based on a report by the Wealth Inventory Planning Study established by the George Washington University under a grant from the Ford Foundation. The text of this report entitled "Measuring the Nation's Wealth" was published by the Joint Economic Committee in December of 1964 for consideration by the subcommittee. Witnesses were chosen from those who prepared the study, and other experts who gave their appraisals of the findings contained in the study.

Measuring the Nation's material wealth

In August the subcommittee issued a report on "Measuring the Nation's Material Wealth," containing its findings and recommendations.

Improved statistics for economic growth: A compendium of views and suggestions from individuals, organizations, and statistics users

In July the subcommittee published a compendium of statements by economists and statisticians on measures to strengthen the Federal Government's contribution to statistical and diagnostic tools for dealing with economic policy.

The balance-of-payments statistics

The report of the Review Committee for Balance-of-Payments Statistics (the so-called Bernstein committee) entitled "The Balance-of-Payments Statistics of the United States, a Review and Appraisal" was the subject of hearings by the subcommittee on May 11, June 8, and June 9.

In July the subcommittee issued a unanimous report on "The Balance-of-Payments Statistics of the United States" containing its findings and recommendations.

SUBCOMMITTEE ON INTERNATIONAL EXCHANGE AND PAYMENTS

The Subcommittee on International Exchange and Payments is composed of Representative Henry S. Reuss (chairman), Representatives Richard Bolling, Hale Boggs, William B. Widnall, and Robert F. Ellsworth, and Senators Paul H. Douglas, William Proxmire, and Jack Miller.

Guidelines for international monetary reform

On July 27, 28, and 29 the subcommittee held hearings on "Guidelines for International Monetary Reform," receiving testimony from 10 witnesses. Part 1 of the printed hearings also contains statements from five experts who did not appear in person. Part 2—supplement—contains articles and speeches and excerpts from articles and speeches, quoting from specialists in international affairs.

Guidelines for improving the international monetary system

In September the subcommittee issued a report on "Guidelines for Improving the International Monetary System" climaxing 6 years of work by the committee and subcommittee on problems of international monetary reform.

Off dead center; Some proposals to strengthen free world economic cooperation

Following a trip to Western Europe, Representative Reuss and Representative Ellsworth on December 23 issued a report offering 12 recommendations to deal with the problems of free world economic cooperation.

SUBCOMMITTEE ON INTERAMERICAN ECONOMIC RELATIONSHIPS

The Subcommittee on Inter-American Economic Relationships is composed of Senator John Sparkman (chairman), Senators Jacob K. Javits and Len B. Jordan, and Representatives Richard Bolling, Hale Boggs, Henry S. Reuss, Martha W. Griffiths, and Thomas B. Curtis.

Latin American development and Western Hemisphere trade

The subcommittee on September 8, 9, and 10 heard the testimony of eight witnesses on "Latin American Development and Western Hemisphere Trade." In addition to the oral testimony the printed record contains extended answers submitted in writing by representatives of the Department of State to questions raised by subcommittee members after the close of the oral hearings.

OTHER COMMITTEE STUDIES COMPLETED SINCE MARCH 1965

In carrying out its duty to make a "continuing study" of the economy, the Joint Economic Committee from time to time releases for public information pertinent materials prepared for the committee under the direction of the staff.

Economic policies and practices

The committee published further brief studies which are designed as aids to understanding comparative economic policies and institutions in the various industrial countries under the general title "Economic Policies and Practices." The following were published since March 1965:

Paper No. 7: "European Social Security Systems."

Paper No. 8: "Programs for Relocating Workers Used by Governments of Selected Countries."

Subsidy and subsidy-effect programs of the U.S. Government

This study, prepared by the Legislative Reference Service of the Library of Congress, represents an updating and revision of an earlier publication which has long been out of print.

Current economic indicators for the U.S.S.R.

This compendium of statistical materials is a continuation of the studies on the Soviet economy published periodically by the committee.

STAFF PARTICIPATION IN MEETINGS WITH OUTSIDE GROUPS

In addition to conducting formal studies and arranging hearings for the committee and subcommittees, the staff participated in discussions of economic problems and research techniques with outside groups. The following list of meetings illustrates the nature of these activities in which the staff took part in 1965:

American Economic Association, Annual Meeting.

American Bankers Association Symposium on Federal Taxation.

American Statistical Association, Annual Meeting.

Conference on the Economic Report—Woodrow Wilson School of Public and International Affairs, Princeton University.

Escort interpreter training program, Department of State.

Business Research Advisory Committee Meeting, Bureau of Labor Statistics.

McGraw-Hill Informal Conference on Business Outlook.

National Association of Tax Administration Revenue Estimating Conference.

National Bureau of Economic Research—Conference on Research in Income and Wealth.

National Industrial Conference Board—Economic Forum.

National Planning Association—Seventh Annual Conference of Center for Economic Projections.

Princeton-Brookings Roundtable on Business-Government Relations.

University of West Virginia Conference on Poverty.

The executive director and other professional staff members made addresses or presented papers to the following groups:

Columbia University, International Affairs Department.
Goucher College.
George Washington University.
Hollins College.
Insurance Investment Officers.
U.S. Savings and Loan League.
Omicron Delta Epsilon National Society for Economists.

Wesley Theological Seminary seminar.
Williams College.
Johns Hopkins International Center, Bologna, Italy.
Federal Bar Association.

Conferences were held with groups of foreign visitors seeking information on the activities of the Joint Economic Committee, representing the following nations:

Czechoslovakia	Sweden
Iran	The Netherlands
Italy	Yugoslavia
Germany	Philippines
Japan	

The staff also met with two groups from Canada: The Royal Commission on Taxation representatives and the Economic Council of Canada representatives.

Student interns

As usual, the committee participated in the student intern program by having college students working in the committee offices who were able to take advantage of the many programs offered to interns by the various Government agencies.

CHANGES IN COMMITTEE STAFF

Gerald A. Pollack, international economist, resigned to accept the post of Deputy Assistant Secretary of Commerce for Economic Affairs. Nelson D. McClung and George R. Iden joined the staff as economists in the fields of fiscal policy and wage-price policy, respectively.

DISTRIBUTION OF COMMITTEE PUBLICATIONS

During the past year the Joint Economic Committee and its subcommittees issued 35 publications. Approximately 226,202 copies of current and previous committee publications were distributed during the year to fill individual requests. Committee publications are also on sale by the Superintendent of Documents. In the past year, individual and quantity orders of committee publications, current and past, were nearly 50,000. This figure does not include the approximately 9,000 subscriptions to the committee's monthly publication, Economic Indicators, sold by the Superintendent of Documents.

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