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JOINT ECONOMIC REPORT

REPORT

OF THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

ON THE

FEBRUARY 1971 ECONOMIC REPORT OF THE PRESIDENT

TOGETHER WITH

STATEMENT OF COMMITTEE AGREEMENT, MINORITY AND OTHER VIEWS

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

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92D CONGRESS, 1st Session } SENATE { REPORT No. 92–49

REPORT ON THE FEBRUARY 1971 ECONOMIC REPORT OF THE PRESIDENT

MARCH 30, 1971.—Ordered to be printed

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

REPORT

together with

STATEMENT OF COMMITTEE AGREEMENT, MINORITY AND OTHER VIEWS

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

This report is submitted in accordance with the requirement of the Employment Act of 1946 that the Joint Economic Committee file a report each year with the Senate and the House of Representatives containing its findings and recommendations with respect to each of the main recommendations made by the President in the economic report. The report is to serve as a guide to the several committees of Congress dealing with legislation relating to economic issues.

This year the Report of the Joint Economic Committee is made up of four parts:

A first part comprising statements of agreement by the majority and the minority members of the committee on (1) a number of recommendations relating to the domestic economy, and (2) an analysis of current issues in the field of international economic policy with conclusions and recommendations thereon;

A second part consisting of the committee report, together with supplemental views of individual members;

A third part consisting of Minority Views together with supplemental views of minority members; and

A fourth part describing the committee and subcommittee activities in the past year and subcommittee membership.

NOTE.—Due to 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.

STATEMENT OF AGREEMENT BY MAJORITY AND MINORITY MEMBERS OF THE JOINT ECONOMIC COMMITTEE

The members of the Committee agree on certain recommendations with respect to economic policy in the period ahead. These are:

1. The Congress should adopt procedures for reviewing aggregate expenditures and receipts in order to make a determination as to the level of revenues and expenditures most consistent with the needs of the economy.
2. There is an urgent need for a more comprehensive welfare program better designed to meet standards of adequacy and equity. Any reformed welfare system must include adequate job opportunities and strong work incentives.
3. There is need for immediate expansion and improvement of manpower programs, including job opportunities for welfare recipients and low-skilled persons, and economic conversion for workers in the defense and other worker-surplus industries.
4. Additional Federal aid is required to meet pressing needs of State and local governments.
5. We must develop adequate environmental protection measures. In doing so, it should be recognized that those persons responsible for pollution should bear a fair share of the cost of our environmental clean-up. In this regard we strongly support a system of environmental user charges in the private sector of the economy. Taxes on sulphur oxides and leaded gasoline would be appropriate user charges of this type.
6. Congress and the Administration should undertake a complete reevaluation of Government regulation of transportation, with increased emphasis on a more competitive system where appropriate.
7. More assistance should be provided to rural America by the Federal Government. Additional efforts should be made to promote agricultural productivity to hold down costs of production. Moreover, there is need for study and review of widening margins between farm and consumer prices. It is vitally important to recognize the incomes of small and middle-income farmers should be raised.
8. After full consideration of the many current issues in the field of international economic policy, the members of the Committee have concurred on the analysis which follows.

JOINT VIEWS ON INTERNATIONAL ECONOMIC ISSUES

In 1970, the U.S. trade surplus rebounded with a four-fold increase from the extraordinarily depressed level of the previous year. The liquidity deficit shrank by a third to $4.7 billion, but this country's balance-of-payments deficit as measured by settlements with official foreigners ballooned to over $10 billion, the largest such deficit in U.S. history. Large short-term capital flows during 1969 and 1970 produced erratic movements in both of these commonly used measures of the U.S. balance of payments, and the exceptional official settlements deficit recorded last year gives an excessively gloomy picture of the U.S. balance of payments. Nevertheless, European monetary authorities, in contrast to 1969, are once again expressing reservations about the size of the dollar balances that they have accumulated.

A trade bill that would have substantially altered the direction of U.S. policy secured the approval of the House and of the Senate Finance Committee last year, although not without strong dissent. The bill, however, subsequently failed to come to a vote in the Senate.

The future orientation of this country's trade policies is still uncertain. Since December 1969, the Subcommittee on Foreign Economic Policy has been conducting an intensive series of hearings with the objective of formulating an appropriate set of goals for trade, international investment, and aid policies throughout the remainder of this decade. The outcome of this inquiry will be published as a report sometime in the spring of this year. In addition, a Presidential Commission on Trade and Investment Policy, chaired by Albert L. Williams, is also expected to report its findings in the next few months and will help set the tone for trade and investment policies in the seventies. In this regard, we note that the President has indicated he is withholding legislative proposals in the trade and investment area until the report has been published. White House reaction to both of these documents, a pending Executive decision on whether or not to curtail shoe imports, and the outcome of the continuing textile dispute with Japan should together give a clearer indication of the future course of American trade policy.

Regardless of the stance of American policy, progress in the further elimination of tariff and nontariff barriers to international trade will be impossible without full participation in such an effort by the European Economic Community, especially if this association is enlarged. Industrial countries need trade to insure that growth is efficient, and poor nations require expanded market opportunities in the northern hemisphere in order to purchase essential capital inputs. Thus, progress in the reduction of all types of trade barriers and the further opening of Japanese, North American and European markets is of prime importance.

Trade Policy

In addition to being a highly efficient producer of a variety of agricultural products, the United States enjoys a comparative advantage over other nations in the production of numerous capital goods, some consumer products, such as drugs and photographic supplies, and a few basic materials. Our ability to exercise the competitive potential of these industries in international trade, and so obtain imported commodities at a lower real cost than we could produce similar goods domestically, is dependent upon access to markets in other countries. But foreign markets will not remain open to the entry of American-produced goods if we ourselves do not continue to reciprocate. As the largest single trading nation, the United States plays an important role in establishing the tone of multilateral trade policies. If this country were to resort to protectionism, as distinguished from retaliatory action permissible under the General Agreement on Tariffs & Trade (e.g., sec. XIX), others would undoubtedly be prompted to retaliate or follow the U.S. lead. On the other hand, no global effort to continue on the course of trade liberalization that has been pursued since 1934 is likely to succeed without U.S. participation and support.

Attempts to estimate the number of jobs in this country dependent upon the production, shipping, and insuring of exports—as opposed to the implicit labor content of imports—invariably indicate that employment in the United States benefits from international trade. Greater numbers of export-oriented jobs are created than are lost as a consequence of imports. In addition, employment in export industries is generally more productive and pays higher wages than in import-competing industries.

Trade does oblige the United States to modify its productive capabilities and alter its output mix along with shifts in consumer tastes and the growth of productive potential in other countries. The same types of changes are necessary in response to the development of new technology at home and the appearance of unsatisfied domestic consumer desires. Shifts in the structure of the U.S. economy stemming from wholly domestic factors almost certainly each year force more adjustments by firms, managers, and wage-earners than does import competition. Only in the event of economic stagnation, inadequate government policies to aid adjustment, or a failure on the part of businessmen and workers to shift from the production of one product to another can import competition produce continued unemployment.

Imports can play a constructive role in the U.S. economy through their ability to promote the efficiency of domestic firms and to help combat inflation. The rate of inflation in the United States during 1968 and 1969 undoubtedly would have been much greater than it actually was if, in response to excessive Federal Government deficit spending following escalation of the Vietnam war, imports had not been allowed to enter this country and absorb excess demand. The drop in exports had a similar anti-inflationary impact in that domestically produced goods were consumed at home rather than being sold to foreigners. Thus, the very substantial deterioration in our trade balance those two years contributed in part to the long-run health of our economy. Impaired export capabilities may, however, not be easily regained. With the reduction in aggregate demand that occurred in 1970, the rate of growth of imports slowed substantially, exports resumed their expansion, and the U.S. trade surplus grew.

Import competition offers a practical means for promoting efficiency and combating wage-price increases in industries that are highly concentrated in the United States. Every industry in this country that is dominated by a few firms also has a strong, industry-wide union. Thus, without import competition, the industry and its corresponding union would be free to bargain collusively and to agree to combinations of wage and price increases at the expense of firms and employees in less concentrated industries. In this respect, the contrast between the automobile and steel industries—both of which are highly concentrated—is instructive.

Imports of automobiles and parts have not been restricted. The firms have instead responded to competition from abroad by introducing small cars to compete directly with imports, and the auto workers have evidenced concern for increasing productivity and holding down costs per unit of output. Over the long run, both American consumers and the employees of auto producers are likely to gain from this constructive response to competition from abroad.

In contrast, both management and labor in the steel industry have in recent years advocated the restriction of imports. Their pleas induced the Executive, in December 1968, to persuade other producing countries to voluntarily limit their steel exports to the United States. From 1960 through December 1968, wholesale prices of iron and steel products increased 5.5 percent; from December 1968 to November 1970—following the introduction of voluntary import quotas—wholesale iron and steel prices increased 13.8 percent. (The wholesale price index for all industrial commodities rose 8.8 percent and 7.7 percent in these same two periods.) Thus, iron and steel price increases in the two years following the introduction of import restrictions were more than twice the increases in the previous nine years. The industry is currently urging that existing import limitations be tightened.

The United States should continue to adhere to an expansionary trade policy in order to exploit our skills that are superior to those of other countries, to promote the efficiency of domestic firms, and to combat inflation.

Maintenance of a forward-looking, expansionary trade policy and continued progress in freeing international flows of goods from existing restrictions depend upon effective programs to aid firms, workers, and communities injured by import expansion. Adjustment assistance to these injured parties taxes a portion of the real benefits away from consumers, who gain from the ready availability of imports, and redistributes these partial gains to the parties who suffer as a consequence of import competition.

The Administration's proposed activities in this direction, as evidenced by their budget requests for fiscal 1972, indicate movement in the right direction. Authority for loans of $100 million and additional loan guarantees of the same amount are requested. If actually delivered, financial assistance in these amounts would constitute a several-fold increase in the quantity of similar aid that will be extended to firms in the current fiscal year. To supplement this assistance to firms, the number of workers paid training and relocation benefits is projected to increase some 55 percent in fiscal 1972.

Continued adherence to expansionary trade policies will almost certainly require the further growth of adjustment assistance programs in future years; hopefully spending authority for this purpose will be requested and provided. If adjustment assistance is available in adequate amounts and is extended promptly, managers and workers may lose some of their fear of foreign competition. Many of these fears are exaggerated, but without the promise of speedy financial assistance, if needed, the opportunity to demonstrate that these apprehensions are indeed unwarranted may not arise.

Financial and other assistance to firms, workers, and communities injured by import competition should be provided more promptly and in larger amounts than it is today.

Occasionally, however, temporary restriction of imports will seem desirable, primarily because the adjustments required of firms and workers that would be injured by a free flow of goods from abroad appear to be excessive. In such instances, the preferred course will probably be to expand trade at a slower rate than had initially been anticipated. But under any circumstances, appraisal of the extent of the injury imposed upon domestic producers by trade expansion and the degree to which imports are to be temporarily curtailed should be determined by the Tariff Commission.

Voluntary agreements are in effect limiting imports of cotton textiles and steel into the United States; in addition, statutory provisions place upper limits on the quantities of meat, dairy products, and sugar that can be brought into the United States. In these instances, the decision to impose quantitative limitations was based on consideration of the amount of damage that would be done to domestic producers—already in a cost-price squeeze—if burgeoning imports continued to gain admission without restriction, and of eventual dependence upon foreign countries for staple foods.

The body that has been established by the Congress to evaluate claims of producer injury is the Tariff Commission. The Commission can hear the arguments of not only producer interests, but also of import associations and consumer groups. The Commission is well equipped to evaluate the economic intricacies of trade injury and adjustment issues. It is protected, in part, by the Congress from political influences that do not necessarily work in the direction of promoting economic efficiency or an appropriate distribution of gains and losses from trade.

A decision by the Tarriff Commission, rather than a legislative committee, to restrict imports in the face of severe injury has an important advantage. Such a decision would be made only after a case has been argued pro and con before the Commission and after the commissioners have presented their own summation of the reasons for limiting imports. Such a determination is likely to be more persuasive to foreign exporters affected by the decision than the pleas of lobbyists before legislative committees.

If, in the absence of protectionist activity by our trading partners, the United States is to withdraw previous trade concessions or is to impose new restrictions, we must give compensation or expect retaliation from abroad. It is in our interest that compensation, if granted, be no more than sufficient and that retaliation, if that alternative is selected, be measured and reasonable. The responses of other countries in reaction to U.S. import limitations are likely to be more circumspect and measured if the Tariff Commission, rather than the Congress, makes the determination.

Letting the Tariff Commission decide whether particular industries should be granted temporary relief from import competition in no way impinges upon the authority of the Congress to establish the trade policy of the United States. The Congress legislates the broad principles according to which the Tariff Commission evaluates and recommends action in particular cases.

In those instances when imports must be restricted to prevent excessive injury to domestic producers, the decision to do so and the choice of individual products to be excluded should be the result of hearings and subsequent deliberations by the Tariff Commission.[1]

The U.S. Balance of Payments[2]

Attitudes towards the significance of U.S. payments deficits have changed markedly over the past two or three years. Reduction of these net external outflows is now generally regarded as far less important than the achievement of what are primarily domestic economic policy goals. Consequently, officials are probably less willing than in the past to give emphasis to balance-of-payments considerations in their formulation of monetary and fiscal policies.

This relative change in the weight given various policy goals has come about for several reasons. First, as unemployment rose to 6 percent and as inflation persisted longer than expected, the need to correct these domestic economic maladies began to overshadow the balance of payments. Second, U.S. payments deficits persisted despite the efforts of officials to curtail them. While controls over capital exports and other measures have produced some savings in the areas that were the direct focus of attention, new outflows always seemed to balloon sufficiently to leave the general problem unchanged, or even worse. But perhaps the most significant factor in producing more

[1] Senator Miller concurs as a matter of general policy, but strongly believes that Congress should not abdicate its responsibility to make these decisions in cases of great importance to the national interest.

[2] Representative Blackburn and Senator Percy believe that the report should make clear that the United States balance of payments continues to be structurally unsatisfactory, and that this does not warrant a relaxed or passive attitude on the part of the Executive Branch, the Congress, business, labor or the general public. In lieu of the first two paragraphs in this section, they believe the following statement better describes prevailing views:

> Attitudes toward the significance of the U.S. payments deficits have changed markedly over the past two or three years. There is now a clearer recognition that the U.S. payments position, however measured, is structurally unsatisfactory. There is also a clearer recognition that it would not be in the world interest for the U.S. to attempt to eliminate these deficits either by continued restraint of the domestic economy or by short-run and selective measures. The monetary system fortunately has proven capable of absorbing large fluctuations in our position, but we should not be misled into the thought that it can safely sustain continuing large U.S. deficits. Thus, as indicated in some subsequent sections of the Report, balance-of-payments considerations are important in our policy making.
>
> The multiplication of measures of our net external position both reflects the complexity of our position and re-enforces the conclusion that the structure is unsatisfactory.

relaxed attitudes about the U.S. balance of payments has been the failure of the international monetary system to disintegrate despite the persistence of U.S. deficits. The system seemed to tolerate, and perhaps even in part generate, continued U.S. deficits.

A reflection of this growing uncertainty about the significance of U.S. balance-of-payments deficits is the multiplication of measures of our net external position. The latest Report of the Council of Economic Advisers cites four different measures of the balance of payments: the liquidity balance, the official settlements balance, the current-account balance and the basic balance. In its emphasis on a variety of measures, the Council subscribes to the opinion expressed a year ago by this Committee when we asserted that "no single statistic can faithfully summarize the United States balance of payments."

The liquidity balance has been justified as a measure of the ability of the United States to pay off claims held by foreigners with our reserves. But such claims now total more than twice the size of the U.S. reserve stock, and the liquidity balance has lost its practical significance. The official settlements balance ostensibily measures the extent of the intervention by monetary authorities in exchange markets needed to maintain stable exchange rates, but this measure can be substantially distorted by the transactions of official institutions in the Euro-dollar market. The current-account balance is a rough indicator of U.S. ability to compete with other countries and to earn income from sales of goods and services and from investments overseas. The basic balance is equivalent to the current account plus net long-term capital flows. By excluding short-term monetary transactions across national boundaries, the basic balance attempts to measure structural patterns in the balance of payments that can be expected to endure from year to year. Attention to alternative measures of the external position of the United States is in line with previous suggestions of this Committee. Hopefully the Commerce Department, in its presentation of balance-of-payments data, will follow the example set by the Council in its latest report.

The external and internal economic policy goals of the United States should be regarded as being synonymous—the maintenance of full employment and price stability. If these goals can be achieved, the balance-of-payments position of the United States will be strengthened; but if we fail to realize these joint objectives, a progressive deterioration in our external position will compound domestic problems.[3]

Severe unemployment or rapid inflation would have far more damaging effects on the external economic position of the United States than could be offset by ad hoc correctives. High unemployment and associated domestic economic stagnation initially reduce the rate of growth of imports purchased by this country. But subsequently the effects of slack demand in the United States would spread to other

[3] Representative Blackburn and Senator Percy concur in the importance of the maintenance of full employment and price stability as contributing to both external and internal goals. However, their view is that there may be need for special efforts, programs and policies designed to shore up and strengthen the balance of payments, and such efforts, where practicable, should be pursued. They would accordingly replace the word "synonymous" with the word "compatible" in this recommendation.

nations, and their purchases from us would decline. In addition, if this country is not growing in line with its potential, our domestic markets will hardly constitute a healthy environment for the development of new export products or for investment from abroad. On the other hand, if inflation fails to moderate, our competitive position in foreign markets will tend to erode.

Emphasis on the domestic maintenance of full employment and price stability does not imply that we should ignore the position of the U.S. balance of payments or force other countries to accept willy nilly the external consequences of our domestic policy actions. Instead adherence to these joint objectives means that a reasonable rate of growth and stable prices are the greatest contribution that American economic policymakers can make to the rest of the world as well as to our own citizens. We must listen attentively to the criticism of other countries regarding our policies and should be willing to alter—for external reasons—the mix of fiscal and monetary policies when such adjustments can be made without appreciable domestic sacrifices.

International Adjustment Mechanisms

When confronted by repeated annual balance-of-payments surpluses that are largely the counterpart of U.S. deficits, other countries can choose from several options if they desire to curtail their surpluses. They can relax import restrictions, expand their domestic economies at more rapid rates, encourage capital outflows and increase foreign aid, or raise the dollar value of their own currencies.

The post-war evolution of the international monetary system has made the dollar the hub of that system. If the dollar were removed, the system would have to be restructured. Because of the central role of the dollar the United States cannot choose unilaterally to alter the exchange rate between the dollar and any other currency.

If the United States chose to bring about a uniform shift in exchange rates by raising the price of gold, much of this change would undoubtedly be counteracted by gold devaluations of other currencies. In addition to the undesirable effects of a rise in the price of gold—a global inflationary thrust, special gains for South Africa, the Soviet Union, and hoarders, and the abandonment of any hope of multilateral control over the supply of international liquidity—such a move would be a highly inefficient method of trying to curtail existing payments imbalances. Relatively few countries are experiencing objectionable surpluses as a counterpart of U.S. deficits, and not all of these nations would choose to curtail their surpluses by the same percentage exchange rate movement. Some might also desire a degree of expansion or import liberalization. By far the most efficient and flexible method of curtailing U.S. deficits and the corresponding surpluses of other countries is to allow foreign policymakers to choose their own desired combination of dollar accumulation, exchange rate adjustment, and other techniques for reducing net external receipts.

To the extent that other countries desire to reduce their payments surpluses but prefer not to expand domestically, liberalize imports and capital exports, or increase

foreign aid, they should raise the dollar value of their currencies. Exchange rates should be adjusted promptly to eliminate the excessive balance-of-payments surpluses and deficits that exist today and to prevent the emergence of persistent surpluses and deficits in the future.[4]

The responsibility of the United States under this type of multilateral distribution of adjustment burdens is to provide a stable base for the system so that the adjustment efforts of other countries are not frustrated. This country does not act as a stable center for the international monetary system if it is subject to periodic sharp fluctuations in the level of economic activity, in interest rates, or in the rate of inflation. On the other hand, given a future improvement in American economic performance, as measured by these indicators, other countries must play an appropriate role in avoiding persistent, excessive payments imbalances.

In most instances, the chief technique in avoiding excessive payments surpluses and deficits will probably be exchange rate adjustments. Rate changes should generally be more frequent and smaller than they have been in the past. The International Monetary Fund, through its studies of alternative methods of introducing somewhat greater flexibility in exchange rates and through continuing discussion among its executive directors of various methods for eliminating payments disequilibria, is making a continuing contribution to the solution of these problems. Further efforts on the part of the Fund in this direction may hopefully be expected to yield additional benefits in the future.

Military Expenditures.—Military expenditures overseas constitute the single largest adverse contribution that the Government makes to our continuing balance-of-payments deficits. Such expenditures totaled $4.8 billion annually in both 1969 and 1970. In an attempt to counteract in part the adverse balance-of-payments impact of military expenditures abroad, successive administrations have encouraged other governments to purchase military hardware from the United States rather than some other country. These sales remained in 1970 at the previous year's level of $1.5 billion.[5] Needless to say, care must be taken in our military sales programs that we do not encourage more purchases by foreign governments than are necessary for their security. In addition, sales and grants to developing countries have fueled

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[4] Representative Blackburn and Senator Percy believe that the second sentence in the recommendation is too sweeping and not likely to have practical effect. Changes in exchange rates in major countries are very serious decisions, economically and politically, both for the countries concerned and for other countries. Limited exchange rate flexibility may prove a useful technique if it is generally accepted, but would be aimed primarily at dealing with large-scale movements of hot money. Moreover, to avoid misunderstanding, this conclusion should frankly recognize U.S. responsibilities. Accordingly, they would subscribe to a recommendation revised as follows:

> *Given appropriate U.S. policies and performance, other countries, to the extent that they desire to reduce their payments surpluses but prefer not to expand domestically, liberalize imports and capital exports, or increase foreign aid, do have the option of adjusting the exchange rates of their currencies.*

[5] The foreign military sales figures for 1965 through 1968 are $830 million, $829 million, $1,240 million, and $1,395 million respectively. The corresponding figures for military expenditures abroad are $2,952 million (1965), $3,764 million (1966), $4,378 million (1967), and $4,535 million (1968).

regional arms races in areas of the world, particularly the Indian subcontinent, where such expenditures ought to be minimized in favor of pressing social needs, such as education, health, rural development, and the elimination of urban squalor.

As a major adverse element in our balance of payments, U.S. military expenditures abroad should be reduced.

The United States can reduce its military expenditures by withdrawing troops stationed abroad, by consolidating headquarters, and by curtailing military aid. The Subcommittee on Economy in Government has initiated an investigation of waste in military assistance to other countries. A report stemming from this investigation will present specific recommendations on how the foreign military expenditures of the United States can be reduced and on the desired magnitude of such reductions.

Short-Term Capital Flows.—In the second half of 1968, the Federal Reserve began to pursue a more restrictive monetary policy, and short-term interest rates increased until they were generally above the maximum that, according to Regulation Q, U.S. commercial banks are permitted to pay to their depositors. Pressed for liquidity the banks attempted to attract funds from the commercial paper market through their subsidiaries and holding company affiliates. In addition, commercial banks sought funds in Europe through their foreign branches; at the time, liabilities to foreign branches were free from constraints. Under the direction of head offices in the United States, the branches abroad bid aggressively for funds and in fact attracted a substantial volume of liquid assets from the United States. These funds were then redeposited with head offices in this country. The liabilities of U.S. banks to their foreign branches doubled from about $7 billion at the end of 1968 to over $14.6 billion in August of the following year.

In September of 1969, the Federal Reserve introduced a reserve requirement on liabilities of U.S. commercial banks to foreigners. The increase in the cost of borrowing in Europe that resulted from this reserve requirement, and the rapid decline in domestic short-term interest rates during 1970 induced U.S. banks to diminish their liabilities to foreigners and return to the U.S. market as a source of short-term capital. While the net inflow of short-term funds during 1969 was in excess of $5 billion, an even larger outflow most likely occurred in 1970. Lately, the Federal Reserve has for balance-of-payments reasons attempted to induce banks to stop running down their short-term liabilities to foreigners, but this attempt has as yet met with only limited success.

Since 1968, the exercise of monetary policy in the United States has produced large fluctuations in the U.S. balance of payments and has had an undesirably large impact on money market conditions in foreign countries. The independent Federal Reserve Board and the Treasury should, when it is possible to do so without significant domestic cost, alter the mix of monetary and fiscal policy to avoid disruptive international capital flows. In another period of future monetary stringency, the Federal Reserve should increase reserve requirements on liabilities to foreigners before a major build-up has occurred.

At this time, however, it would not be desirable—even for international reasons—to curtail the easing of monetary conditions that is desirable to stimulate a recovery of domestic real growth.

The Supply of International Liquidity

The reaction of some European officials to the extraordinary U.S. official settlements deficit in 1970 has been to suggest that if the U.S. deficit is still large when the present agreement to distribute SDRs expires in 1972, no additional special drawing rights should be created, or any distribution should constitute only a token amount. Given the long-run international monetary objectives of the special drawing rights amendment, this reaction on the part of Europeans seems peculiar.

In the absence of an assured supply of gold available in appropriate amounts for international monetary purposes, the special drawing rights mechanism was created to guarantee an adequate supply of international liquidity. Under the amendment, actual distribution of a specified quantity of SDRs requires the approval of members holding 85 percent of the votes in the IMF. The SDR amendment to the IMF Articles of Agreement constituted a step towards multilateral supervision of the supply of international reserves. The March 1968 two-tier gold price arrangement and the pledge of the United States to reduce its deficits in the event of activation of the SDR agreement were also moves in the same direction. The question that the unprecedented 1970 U.S. official settlements deficit now poses is whether an appropriate reaction to the failure of this country to fulfill its commitment [6]—if events during 1971 indeed demonstrate that this pledge is not being fulfilled—is to substantially reduce or halt distribution of special drawing rights.

Before adoption and implementation of the special drawing rights facility, the annual increase in the global stock of reserves available to all countries was determined by the quantity of newly produced gold that did not disappear into private hoards and by fluctuations in the U.S. balance of payments. If hoarding demand was minimal, a large proportion of newly produced gold became incorporated into the monetary stocks of various central banks. Similarly, the size of the U.S. official settlements deficit indicated the amount of U.S. reserve losses to the monetary authorities of other countries and the extent to which foreign official institutions had accumulated additional dollars. Unfortunately, during the first year of operation of the special drawing rights mechanism, the U.S. balance of payments has continued to be the dominant factor in determining reserve growth.

Some economists currently argue that the world is now effectively on a dollar standard and that, even more so than in the past, the United States can determine the growth of world reserves through the size of its official settlements deficits. These analysts maintain that other countries have no alternative but to accept accept dollars, since any demand by a large creditor for conversion of dollar balances into gold

[6] Representative Blackburn, though recognizing that the deficit in the United States balance of payments in 1970 was large and unwelcome, points out that a very substantial part of this deficit was due to short-term capital flows related to different levels of interest rates here and in Europe that in turn were appropriate to the domestic economic situations in both areas. Any "pledge" or "commitment" needs to be interpreted against that background.

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or other assets would precipitate an international monetary crisis so severe as to destroy the current system. This is an outcome no one desires.

But a U.S.-run dollar standard is not a tenable long-term arrangement for the international monetary system. Resentment on the part of other industrialized nations will grow until, if the U.S. fails to moderate its stance, gold or one or more other currencies will assume the present role of the dollar. If such a transfer of functions occurred in a disruptive way, the consequence might be the formation of a number of currency blocs and a severe drop in international trade and investment. Instead, the United States should initiate a series of well-considered gradual steps towards effectively multilateralizing the creation of international liquidity. We should perhaps cooperate in developing a guideline imposing gradually increasing discipline on the financing of U.S. payments deficits. Under such a guideline, the proportion of annual deficits financed by dollar accumulation abroad would decline and the proportion financed by U.S. losses of gold, SDR's, or exchange reserves would increase over time. Since the United States is under any circumstances unlikely to be able to retain over the long-run its position of predominance in effectively determining the global supply of reserves, little would be lost by voluntary self-discipline of this type. Moreover, important gains could be derived from an orderly transition that avoids the danger of international monetary disruption.

Three ingredients are essential to progress toward effective multilateral control over the supply of reserves. First, the United States must achieve reasonable price stability and full employment domestically and reduce government spending abroad. Second, other countries must initiate policies to curtail undesired surpluses with the United States. The need for such policies—whether currency revaluations, import liberalization, faster rates of growth, or some other choice—has been explained above. The last essential ingredient is an assured alternative supply of acceptable reserve assets created by international agreement.

To halt or virtually eliminate the supply of special drawing rights would effectively render the SDR mechanism defunct and leave no alternative but to accept a dollar standard in the immediate future. In that event, an international monetary crisis affecting the dollar would almost certainly be severe. By contrast, continuing the supply of SDRs in more-than-nominal amounts would have several important advantages. First, other countries will be less hesitant to revalue if they hold ample reserve stocks. Second, the transfer of effective authority to create reserves could be made in an environment of expanding world trade, and would therefore be easier to effect than if fears of reserve inadequacy were tending to make all countries cautious. Third, if a crisis should occur, an international mechanism for the creation of reserve assets would be in place and fragmentation of the system into currency blocs would be less likely.

In considering the appropriate size of distributions of special drawing rights (SDRs) in 1973 and thereafter, the members of the International Monetary Fund (IMF) should resolve to continue distributing these assets in

more-than-nominal amounts. Moreover, the money-creating powers of the IMF should be used to foster increased financial assistance to developing countries.[7] [8]

Continued utilization of the SDR facility and uninterrupted distribution of special drawing rights is essential to multilateral control over the supply of international liquidity. In addition, the power of the International Monetary Fund to create reserves should also be used to foster internationally desirable objectives, just as the money-creating authority of central banks in many countries is used in part to foster socially desirable programs. The total quantity of SDRs distributed should be governed by the needs of trading nations for reserves. The report of the Subcommittee on International Exchange and Payments published in August 1969 pointed out, however, that additional benefits can be realized by allocating a specific quantity of SDRs to the International Development Association, instead of to industrial countries. Alternatively, wealthy nations might be permitted to increase their proportionate share in a given distribution of special drawing rights by voluntarily pledging hard currency contributions to IDA.

Gold

In 1970, the International Monetary Fund purchased $640 million worth of gold from South Africa. This annual volume of purchases was about twice what had been expected when the executive directors of the Fund sanctioned renewed purchases from South Africa in December 1969. While the price of gold on the free market was generally weak early in 1970, it strengthened and maintained a $3 or $4 premium above the official value throughout the latter part of the year. The danger exists that this agreement may effectively work to increase the free market price of gold, particularly since it permits certain purchases from South Africa regardless of the current market price. The functioning of the agreement must be closely observed to insure that the IMF does not in fact assume a responsibility for subsidizing gold production in South Africa or anywhere else in the world. The agreement is subject to review upon request in the event of "a major change in circumstances." An amendment to the agreement could be drafted that would prohibit the fund from purchasing gold from South America when the free market price is above some specified maximum.[9]

The December 1969 gold agreement with South Africa must remain under constant review to insure that it does not effectively work to push the private market price of gold steadily upwards.

[7] Representative Blackburn and Senator Percy would not subscribe to the last sentence of the recommendation and the corresponding passage in the text. While potentially in the future such ideas might be examined on their merits, their consideration in connection with the 1972 decision on the second round of SDR creation would add difficulty to a critical phase in the development of the SDR facility.

[8] See the supplementary views of Senator Humphrey for his recommendations on increasing development assistance.

[9] Representative Blackburn, while agreeing that the function of the agreement needs to be closely observed, believes that it would be impracticable and unnecessary to attempt to modify the present arrangements with South Africa at this time. He points out that while the IMF purchased $640 million of gold from South Africa, this annual volume of purchases was far higher than may be expected on a continuing basis.

1971 JOINT ECONOMIC REPORT

I. INTRODUCTION

In its Report of last year, this Committee expressed concern that economic performance during 1970 would fall short of the Administration's modest expectations. We warned of the prospect of higher unemployment, a stagnant economy, an increasing shortage of housing and public facilities, and an inflation that would continue without substantial abatement.

Events during 1970 have justified these fears. The performance of our economy has been very disappointing. As 1970 ended and 1971 began, unemployment was at the unacceptable level of 6 percent. Prices, which rose at an average rate of 5½ percent in 1970, showed no clear evidence of any slowing in the rate of increase. The economy is suffering from a grim and unprecedented combination of unemployment and inflation.

During the year gross national product fell by 0.4 percent in real terms. The Industrial Production Index dropped from 108.2 in December 1969 to 104.0 in December 1970 and remained at only 104.2 in February 1971, despite the large expansion of automobile production following the settlement of the General Motors' strike. In the fourth quarter of 1970, our economy was operating at a rate almost $70 billion less than its potential, and there seems to be little prospect that this gap will be significantly narrowed in 1971. Chart 1 (p. 19) illustrates this widening gap between actual and potential output.

One of the most tragic aspects of this economic stagnation is the loss of vitally needed income and production. Not only are individual citizens suffering from lower incomes, lack of job opportunities, and more wide-spread poverty, but our cities are urgently in need of revenues, and some face bankruptcy. Most States face a desperate need for revenues. Part of this lost income and production could serve to meet urgent needs of our States and communities and help them not only to meet operating costs but to provide badly needed public facilities, particularly urban mass transit, schools, health facilities, and sewer systems.

One apparently encouraging factor is the pick-up in housing starts from the extremely low level that prevailed at the beginning of 1970. On the basis of current evidence, however, we have no assurance that we shall see in 1971 activity in the housing area significantly different from what we were experiencing at the start of the year. As a Nation, we are far below our housing goals, and a much better showing is needed if they are to be attained or even approximated. Hopefully, adoption of legislation during 1970 to provide additional needed funds for housing will bring about substantial improvement.

Some reduction in the excessive mortgage rates of 1970 has recently taken place. Current rates for FHA loans average 8.4 percent as compared with a high of 9.3 percent last March. Unfortunately, the prospect of heavy Federal borrowing to finance budgetary deficits plus a large backlog of State and local financing needs will increase the difficulty of achieving substantial further declines in mortgage rates.

The spending patterns of the Federal Government also leave much to be desired in terms of our human needs. Of projected expenditures of $229 billion for Fiscal Year 1972, $77.5 billion will go to national defense; $21 billion to agriculture, natural resources, and commerce and transportation; and almost $20 billion to interest on the public debt. Sixty billion dollars are proposed for expenditure on social security and welfare, most of which amount is derived from specially earmarked payroll taxes. Compared with these figures, $13 billion will be available for community development, housing, education, and manpower.

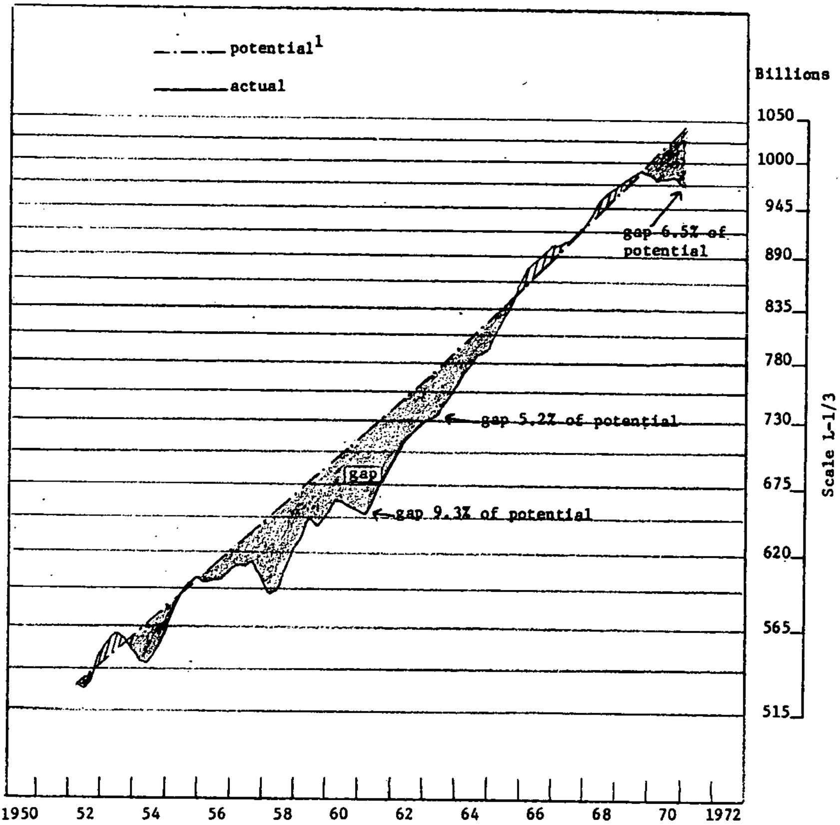
This pattern of expenditure must be considered in conjunction with the vast unmet needs for education, housing, community facilities, urban mass transportation, and the other services required to re-establish our cities as civilization centers. In the past 25 years, our society has become much more complex, and the requirements for public investment have risen greatly. We have not kept pace with these requirements so that important parts of our public sector are now underfinanced. At the same time, there is compelling evidence that we have overinvested in other programs, e.g., military hardware, highways, and other public works. Unless the deficiencies and imbalances are corrected, they will become a burden on our growth, progress, and even our stability as a Nation.

This year for the first time, the Budget and the Economic Report make explicit use of the full employment budget as a concept for economic policymaking. This is a step long urged by this Committee, and we commend the President for adopting it. Only by looking at revenues and expenditures as they would be at full employment is it possible to accurately evaluate the impact of the Federal budget on economic activity.

At a time like the present when the economy's resources are underemployed and the economy is operating substantially below capacity, an actual deficit in the budget can serve to provide an appropriate element in an economic recovery program. Consequently, we agree that recognition that a deficit is both unavoidable and appropriate is a step forward. Another helpful measure adopted by the Administration is the projection of budget expenditures through 1976. This Committee has repeatedly pointed out the futility of trying to evaluate programs without reference to their long-term effects. At the same time, we find serious inadequacies in these projections because the sector projections appear to be based on the unrealistic assumption that the Federal share of output will decline from 11 to 7 percent by 1975. In addition, the functional projections are so broad as to be misleading; for example, the "basic necessities" category includes tobacco and jewelry. These weaknesses must be improved by incorporation of more detail and realism if the Congress is to use these projections for decisionmaking.

Chart 1 ACTUAL AND POTENTIAL GROSS NATIONAL PRODUCT

GNP in 1970 dollars, annual rate



[1] Trend line of 3.5 percent per year (intersecting actual line in middle of 1955) from 1st quarter 1952 to 4th quarter 1962, 3.75 percent from 4th quarter 1962 to 4th quarter 1965, 4 percent from 4th quarter 1965 to 4th quarter 1969 and 4.3 percent from 4th quarter 1969 to 4th quarter 1970.

Source: Joint Economic Committee, based on data prepared by the Council of Economic Advisers and the U.S. Department of Commerce.

The Administration's domestic program includes proposals which would help deal with our serious economic problems. The proposed increase in aid to State and local governments is an effort to meet an urgent need. The Committee is convinced of the priority warranted by such needs. During extensive hearings early this year, we have heard from a number of mayors, governors, and other public leaders as to the extent and depth of the problems faced by our communities and their need for help. Our own inquiry leads us to propose alternatives to the Administration's program, but there is no question of the need.

The Administration is also making an historic effort to deal with welfare needs. It is generally agreed that our present welfare program is unfair, unbalanced, and inadequate. As indicated subsequently in this Report, this Committee recommends the adoption of a comprehensive Federal public assistance program, thus relieving States and communities of the crushing burden of the present welfare system.

The Administration budget allocates an additional $4 billion for general aid to State and local governments and $500 million for income maintenance. We applaud this recognition of social needs. At the same time, we are impressed with the need for substantially greater money allocation to some of these needs, as well as to manpower training, health, education, housing, and economic conversion.

The Administration is to be commended for the foregoing measures, all of which are positive and realistically directed toward serving the needs of our economy. Unfortunately, there are also serious deficiencies in the Administration's economic programs which cannot be ignored.

There is still no clear-cut program to limit price and wage increases in spite of the devastating effect that they are having on our economic stability. Much of the Administration's activity in this area during the past year has contributed to the public confusion. After eschewing any direct involvement in the operation of the market place, Administration spokesmen nevertheless resort to "jawboning" in specific cases. And, after rejecting categorically any resort to the stand-by price-wage controls enacted by the Congress one year ago, the Administration has now indicated a passive acceptance of such authority.

Moreover, the forecast of a $1065 billion gross national product for calendar 1971 is not the most likely prospect. In the absence of further measures to stimulate the economy, recovery is likely to fall short of this target; revenues would then drop below the Administration's expectations, and the budget deficit would be much larger than the $11.6 billion projected for fiscal 1972. Considering the likelihood of failure to attain the Administration's GNP target, programs to strengthen the economy should be available. As explained later, these programs could include both tax reductions and additional expenditures, especially expenditures which act directly to provide jobs.

The Committee is of the opinion that the President's action to increase business depreciation allowances will not provide an effective stimulus to the economy. A good part of it will provide windfall gains without commensurate benefits to the economy. There are many other available measures that should have been given priority over this hasty step, such as moving up to the present the currently scheduled future relief for taxpayers.[1]

Among the specific measures which we support are the following:

1. Immediate adoption of a temporary public service employment program, followed by legislation to establish a revised and expanded manpower training program and a longer term public employment program to meet the continuing needs of the public sector.

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[1] Chairman Proxmire and Senators Sparkman and Bentsen note: "We approve of the Administration's proposal to increase depreciation allowances and we think such a step is essential in view of the great importance of encouraging business investment in plant and equipment as a means of increasing efficiency and productivity, thus making it possible to pay higher wages without inflation. Moreover, we favor restoration of the investment tax credit."

Through immediate action on public service employment, our communities will be enabled to provide urgently needed services that they cannot now afford. We deplore the President's action in vetoing the manpower and public employment bill passed by the last Congress and urge the addition of at least $2 billion to projected 1972 budget outlays for this crucial purpose.

2. Because of the strong possibility that proposed policies will not produce the vigorous recovery projected by the Administration, both the Administration and the Congress should stand ready to enact an appropriate combination of expenditure programs and tax reductions to further strengthen the economy.

3. We applaud the enactment of the Social Security measures which increase benefits by 10 percent and postpone the increase in the taxable wage base until 1972. These actions will not only provide aid to those who vitally need it, but they can provide a needed stimulus to the economy and help re-attain full employment.

4. Monetary policy should support the further decline of long term interest rates and should ensure an adequate flow of credit for housing, community development, and small business.

5. A price and incomes program should be adopted by the Administration along the lines proposed by this Committee in Chapter III. We believe strongly that the Administration's virtual "hands off" policy in this matter has aggravated the problems of inflation.

These and other measures are more fully discussed in the subsequent chapters of this Report.

II. RESTORING FULL EMPLOYMENT

During 1970, unemployment rose from 3.9 percent of the civilian labor force in January to 6.2 percent in December. At the present time, approximately 5 million persons are unemployed, an increase of almost two million since the beginning of 1970. Total civilian employment today is below a year ago, so that the economy is not only failing to provide jobs for our growing population but it has also failed to keep the labor force of a year ago fully employed. As we explain below, a most significant fact is that, up to the present time, there is no basic indication that unemployment will be reduced as a result of Administration policies in 1971.

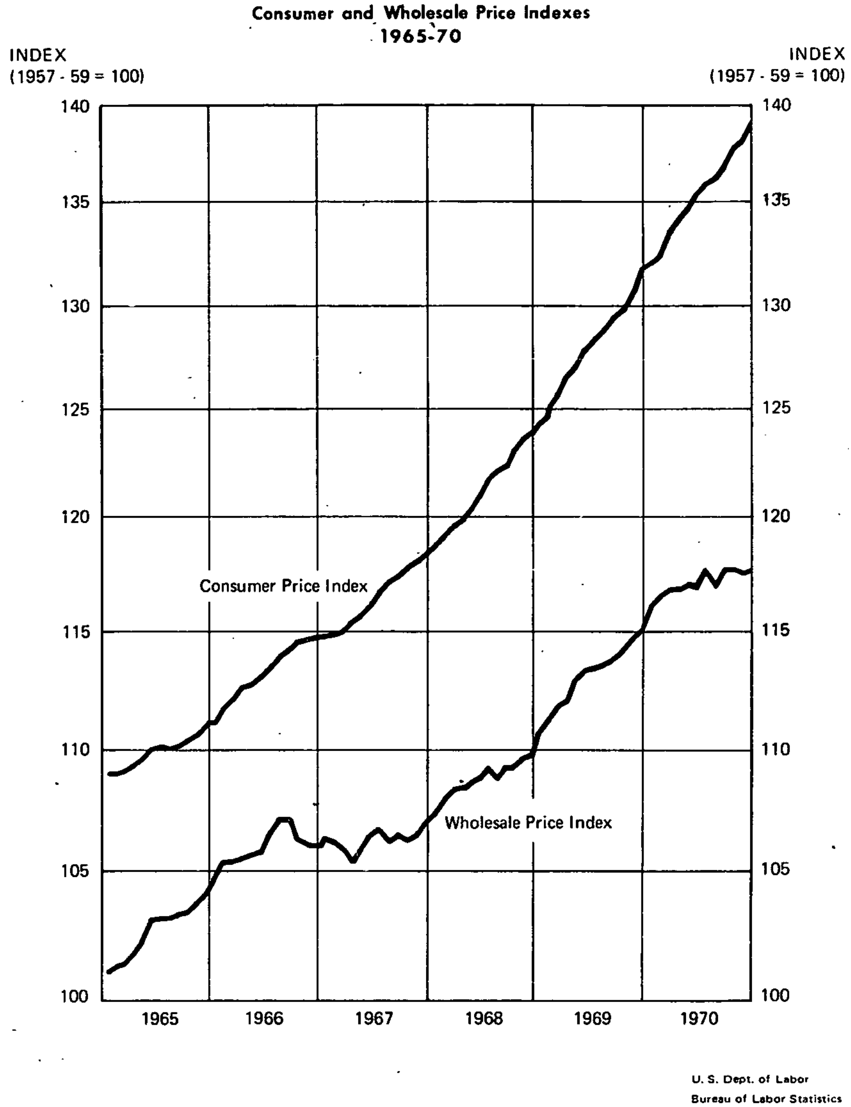
Unfortunately the deterioration in labor market conditions has not been accompanied by any clearly measurable progress against inflation. Several major price indices were rising at least as rapidly at the end of 1970 as at the beginning. (See Chart 2 on p. 23.) Further sharp increases in wholesale prices in early 1971 indicate that inflation continues to be a most serious problem.

The widespread ramifications of the General Motors' strike, which lasted from mid-September until late November, make it unusually difficult to interpret the economic developments of late 1970 and early 1971, but the evidence available as of mid-March indicates that labor markets remain weak and the economy remains sluggish. The Administration stresses that there has been a recovery in output since last spring. This is a very dubious proposition, resting largely on an estimate of the special impact of the GM strike in the fourth quarter of 1970. Output may be on a rising trend, but if so, the increase is falling well short of the level needed to achieve a gross national product of $1065 billion for 1971. Prompt and well-coordinated policy actions are required if a healthy rate of economic recovery is to be restored in 1971.

1. The Economic Outlook

The Administration projects a combination of private economic forces and public policies which would bring about a rise in gross national product, in current dollars, to $1065 billion—a rise of about 9 percent over the $976.5 billion of 1970. They expect a rise of almost 5 percent in real output and a rise in prices of over 4 percent. They believe that this rate of expansion would be consistent with reducing the unemployment rate to about 4½ percent and the inflation rate to a 3 percent range by mid-1972. Even this forecast, which we consider highly optimistic, implies average unemployment during 1971 of over 5 percent.

CHART 2



The basis for the Administration projection is decidedly confusing. In the Economic Report and in testimony before this Committee, the Council of Economic Advisers appears first to say that the $1065 billion GNP is a desirable target which must be attained if we are to reach our unemployment and price goals within the next 18 months. On the other hand, they also say this is a probable outcome—in a word, a forecast. At the hearings and in the Economic Report no detail was provided as to how they arrive at this number. Subsequently some detail behind the projections was supplied by the Council. They expect a rise in business fixed investment of about 3.3 percent; in residential construction of about 38 percent, in State and local purchases of 11.7 percent; in personal consumption expenditures of about 9½ percent; and a decline of 1.7 percent in Federal purchases. At the same time, they re-emphasize that the $1065 billion GNP for 1971 is a target for the economy which "* * * is consistent with national requirements and the requirements of the Employment Act." It was further stated that the composition of output summarized above was not the only composition that would yield the required GNP, and that they had more confidence in the total than in the components of the forecast.

The Director of the Office of Management and Budget supported the Council's projections, and like the Council, gave major weight to changes in monetary conditions in his explanation for arriving at the high figure, some $15 to $20 billion above the forecasts of most private economists. Indeed, we received the impression listening to the Administration's explanations that after having arrived first at a target they would like the nation to reach in 1971, they then built an explanation of why that was where the economy is going to end up, rather than constructing a program calculated to get us there. To make it sound like a probable forecast, they have produced what appears to be all too familiar to professional economists, namely, that magical "little black box." Our confidence that the Administration's projections have a genuine probability of realization is not increased by this resort to statistical mechanics.

Testimony of Private Witnesses

Most witnesses appearing before the Committee are expecting—given present policies—a rise of GNP to the neighborhood of $1050 billion for 1971. An increase in real output of about 3 percent is expected. The expected price rise as measured by the change in the GNP deflator is about 4 to 4½ percent. The unemployment rate is expected to remain at 5½ percent to 6 percent throughout the year.

Witnesses expected an advance in consumer spending, but not as great as that projected by the Administration. Dollar spending for residential construction is projected to show a strong advance, perhaps as much as 25 percent to 35 percent. State and local government budgets are expected to increase $12 to $13 billion over their 1970 levels. Federal outlays for goods and services are expected to change very little. The total dollar value of business purchases of new plant and equipment is expected to be slightly higher in 1971 than in 1970. In real terms such spending is expected to fall moderately below 1970.

The Unsatisfactory Prospect

It seems clear that the economy will show some sign of revival with increased output and a substantial rise in the gross national product in current dollars in early 1971. We think policy should be based on a strong probability that the expansion will come closer to a $1050 billion GNP this year than to the Administration's projected $1065 billion under their policy mix. Even if the Administration goal were reached in current dollars so that GNP turned out to be $1065 billion, the likelilhood is that more than half of this would be due to inflation and less than half to a rise in real output. Even if we were to continue to follow the policy adopted by this Administration, we believe that fiscal and monetary policy must be supplemented by other government actions and that priorities must be rearranged within the fiscal targets.

This Committee views with alarm the current combination of high unemployment and continuing rapid inflation. *We cannot be satisfied with any policy combination which does not promote an attainment of full employment with reasonable price stability at the earliest practicable date and maintenance of that condition once attained.* We cannot hope that this objective will be achieved under the Administration's proposals. The goals established by the Administration for mid-1972, unsatisfactory as they are, cannot in our view be reached under the Administration's present program.

2. Fiscal Policy

The Administration's fiscal policies are marked by the adoption of full employment budget estimates as a basis for fiscal planning. It is estimated that proposed expenditures in the fiscal 1972 Budget would be approximately equal to the revenues which would be generated by a full employment economy. As indicated earlier, we commend them for this positive step and regard it as most helpful in economic policy making.

On a unified budget basis, the Administration estimates full employment revenues of $229.3 billion in fiscal 1972 and full employment expenditures of $229.2 billion, producing a very slight full employment surplus of $100 million. The full employment surplus is little different from the $1.4 billion estimated for the current fiscal year.

Because total output is projected to average about $50 billion below potential output, the actual budget is expected to show a deficit of $11.6 billion in fiscal 1972, compared with $18.6 billion estimated for the current fiscal year, and $2.8 billion in fiscal 1970.

Many of the witnesses before the Committee in its recent hearings proposed that the full employment budget surplus be eliminated, and that an appreciable deficit be incurred. Such a shift in the budget policy would produce a considerable increase in the stimulus provided to the economy by fiscal policy. It would accelerate the rise in economic activity, particularly in output and employment; and it would help to bring the economy to full employment quicker than would be true under the present budget. The risk involved in such a step would be a continuation or aggravation of the strong inflationary pressures that now exist. Our witnesses stressed the importance of a vigorous price and incomes policy together with structural reforms to counter such inflationary pressures.

As indicated in the section on Outlook, there is an appreciable likelihood that GNP will fall short of the $1065 billion level projected by the Administration. The recent decision to defer an increase in the

Social Security tax base until 1972 removes one potential drag on the economy, but many observers feel that further steps to strengthen the economy are required.

Because of the strong possibility that proposed policies will not produce the vigorous growth projected by the Administration, both the Administration and the Congress should stand ready to enact an appropriate combination of expenditure programs and/or tax reductions to further strengthen the economy. As we discuss in Chapter III, a public service employment program is needed now. If further measures become necessary, some or all of the personal income tax reductions presently scheduled for 1972 and 1973 could be made effective immediately and/or public service employment and other vital social programs could be expanded.

The aggregate tax reduction which would be made possible in 1971 by moving forward already scheduled income tax changes would amount to $4.5 billion. The Committee is impressed that, like the recent deferral of the Social Security tax base increase, this change in timing would entail no permanent loss of Federal revenues.

Elsewhere in this report we recommend a reordering of spending priorities, including substantial reduction in military expenditures. Savings made possible in this way can become immediately available to the critical sectors of our civilian society such as urban services, housing and mass transit. In this connection, we are recommending that a public employment program be established immediately along with a greatly improved manpower training program. This measure, discussed in more detail in the section on manpower, would remove the tragic burden of unemployment from many American families; further, it would provide badly needed services in our communities throughout the country—services which they cannot now afford; thirdly, by upgrading available skills such a program would increase the efficiency of the economy.

Budget Reform

The President in his Budget Message calls attention to the fact that reform of the budget process is long overdue. It is now about fifty years since the present budget system was adopted, even longer since the present procedures for legislative review were adopted in the Congress. The President calls attention to the fact that the enactment of appropriation measures is often delayed as much as six months or more after the start of the fiscal year to which they are supposed to refer; that there is an excessive amount of detail in the appropriations bills; and that these characteristics interfere with the ability of agency heads to manage their agencies responsibly and economically. He calls attention to the need for closer cooperation between the Executive and Legislative branches to make the budget an instrument of efficient and effective Federal policy.

This Committee on previous occasions has called attention to the need for Congressional consideration of the budget in its entirety, particularly from the point of view of its effect on the economy. This is not done sufficiently at the present time with the result that the Congress cannot adequately address itself to the formulation of fiscal policy. For that reason, the Congress in the opinion of this Committee, should adopt procedures for assuring a review of aggregate expenditures and receipts annually. Furthermore, it should limit total expenditures to a level consistent with the desired full employment deficit or surplus.

While the President's general interest is welcomed, the Committee believes that budget reform must begin by specific improvements in the present budget process:

1. The budget document should contain projections for at least five years ahead and the projections for the current and upcoming year should show details by less than full fiscal years, preferably by quarters, so that judgments can be made concerning the timing and stability of government programs and their effects on the economy.

2. The budget should contain detailed economic analysis of its effects on the economy as to both expenditures and taxes. It is particularly important that the budget show anticipated effects on output, employment, prices, and the distribution of income.

3. We reiterate our past recommendations for increased capacity in both the Executive and Legislative branches of the Government to make detailed cost-benefit analyses of individual programs to assist in making selections among alternative ways of accomplishing objectives.

4. Congress should adopt procedures for annual review of aggregate expenditures and receipts and for setting an appropriate expenditure ceiling in light of the needs of of the economy.

3. Monetary Policy and Financial Developments

Developments in financial markets in 1970 and prospects for 1971 can be understood only against the background of preceding events. Monetary policy was extremely tight in the second half of 1969. From July to December of that year there was virtually no expansion of the money supply, following a 5 percent annual rate of increase in the preceding six months and an average rate of growth of 7.2 percent in the preceding two years. Indeed it should be noted that the money supply more broadly defined to include time deposits, as well as demand deposits and currency, actually declined at a rate of 1 percent over the 14 months from December 1968 to February 1970.

Costs of borrowing—both for long-term and short-term funds—had reached all-time highs in early 1970. Yields on 3-month Treasury bills reached 8 percent; long-term Treasury taxable issues 7 percent; high grade corporate bonds 8 percent; tax-exempt, top-rated municipal bonds 7 percent; and yields on FHA new home mortgages 9.3 percent.

To reduce the possibility of a financial crisis, the monetary authorities began early in 1970 to ease the excessively restrictive monetary policy of the preceding year. From February to July 1970, the money stock grew at an annual rate of 7.3 percent. In part, this rapid expansion was dictated by threatened bankruptcy of several large firms, which might have precipitated a widening panic. As the situation developed, the trend to reduce costs of borrowing was interrupted in the spring of 1970, with long-term interest rates rising to new peaks, reflecting the fears of spreading financial difficulties and also a shift of business from short to longer term borrowing.

The continuing tightness in financial markets was more remarkable in the face of the sluggishness of the economy generally. Total fixed investment, including residential construction, fell in both the first and second quarters of the year, even in current dollar terms. Throughout the year, such spending was declining in real terms. Inventory investment was likewise cut back sharply from 1969 to 1970.

Thus as 1970 progressed, two basic factors were at work to reduce tightness in capital markets. The Federal Reserve continued its policy of monetary ease, though the money stock grew at a progressively lessened pace as the year went on. Compared with the 7.3 percent rate of expansion from February to July, the stock of money rose at an annual rate of 4.6 percent in the succeeding 5 months. Because the demand for bank lending fell sharply, a substantial drop in interest rates took place, while the measured growth of the money supply declined.

The second basic factor at work in easing financial tensions in 1970 was, of course, the reduced demand for investment funds discussed above. Combined, these factors brought about a sharp decline in the short-term cost of borrowing. As of mid-March, money rates on 3-month Treasury bills and 4–6 month commercial paper had dropped more than 50 percent from their 1970 peaks. These declines, while substantial, were not exceptional in the light of prior experience. They roughly matched the relative reductions which occurred in the recessionary period of 1960–61, but were less than in the recessions of 1953–54 and 1957–58. Moreover, it should be noted that the absolute levels of these short-term rates are today far above levels prevailing in these earlier periods.

Long-term interest rates have declined somewhat in the last few months, but these rates remain at absolute levels which are extraordinarily high by historical standards. In order to achieve an increase in residential construction, provide adequate credit for farm activity and small business, and finance the rise in public facility investment needed to stimulate overall economic activity and to fill vital social needs, further declines in long-term interest rates are required. If the demands for credit continue weak for a time, interest rates may continue to fall even with a moderate growth of the money supply. However, when economic activity becomes more vigorous, demands for credit will increase and more rapid monetary expansion will be required to accommodate these credit demands. It is important that these demands be accommodated and that interest rates not be allowed to rise, thereby choking off the recovery of the economy.

We are suffering an abnormal combination of inflation, high unemployment, and lack of confidence. Witnesses who testified at our annual hearings felt that growth of the money supply in recent months has not been adequate. This Committee feels that monetary policy must be such that downward pressures on long-term interest rates be maintained to support a return of the economy to full employment. This may well take a form whereby debt management and open market operations are such as to twist the term structure of interest rates to favor reduction in long-term interest rates.[1]

Interest rates are still too high in view of the sluggish state of the economy, the still inadequate level of housing activity, the shortage of farm credit at reasonable terms, the large unmet demands of State and local governments, and the need to stimulate consumer spending. The conduct of monetary policy should be such as to affect the term structure of interest rates in order to bring about a decline in the long-term rate.

This Committee feels strongly that some institutional arrangement must be developed which ensures that low and moderate housing needs and the needs of our cities and States for public facilities will not be discriminated against in periods of heavy demand for credit. Institutional arrangements for facilitating borrowing by cities and States should take such form, preferably through interest subsidies, that benefit cities and States directly without providing tax havens for wealthy individuals.

We urge that a federally supported credit institution be established as soon as possible with a view to providing financial support to help meet these high priority needs. This would be accomplished by legislation such as H.R. 3550 and S. 580 which would establish a National Development Bank. The essential purpose of such a bank is to assure that an adequate source of loan funds at reasonable interest rates is made available to State and municipal governments, small and medium size commercial and industrial entities, and public agencies and private non-profit groups for the construction of low and moderate income family housing projects.

One salutary element in the economic picture has been the rebuilding of business liquidity. In contrast to the almost stationary position of business liquid asset holdings over the course of 1969, non-financial corporations added almost $14 billion to such holdings in 1970. Particularly noteworthy in this context is the fact that whereas there was a record increase of $8½ billion in purchases of open market paper by business in 1969—an increase which this Committee noted as a matter of grave concern in the developing liquidity crisis—corporate business reduced such holdings in 1970. See Table 1 below.

[1] See Supplementary Views of Representative Reuss, p. 76.

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TABLE 1.—SOURCES AND USES OF FUNDS, NONFARM NONFINANCIAL CORPORATE BUSINESS

[Billions of dollars]

	1967	1968	1969	1970
Sources, total	96.6	109.5	122.9	110.6
Internal sources	61.5	62.5	62.5	62.0
Undistributed profits	21.1	20.9	19.9	15.4
Corporate inventory valuation adjustment	−1.1	−3.3	−5.4	−4.9
Capital consumption allowances	41.5	44.9	48.0	51.5
External sources	35.1	47.0	60.4	48.6
Stocks	2.3	−.8	4.3	6.7
Bonds	14.7	12.9	12.1	21.3
Mortgages	4.5	5.8	4.8	4.3
Bank loans n.e.c	6.4	8.8	11.0	.6
Other loans	1.4	3.6	7.0	5.1
Trade debt	4.9	10.1	19.1	7.7
Profits tax liability	−4.7	2.8	.4	1.6
Other liabilities	5.6	3.8	1.7	1.3
Uses, total	86.5	102.4	113.3	107.7
Purchases of physical assets	72.0	76.8	86.7	85.6
Nonresidential fixed investment	62.5	67.4	76.6	79.6
Residential structures	2.3	2.4	2.9	3.2
Change in business inventories	7.3	7.0	7.2	2.8
Increase in financial assets	14.5	25.6	26.6	22.1
Liquid assets	2.1	8.6	1.3	13.8
Demand deposits and currency	.7	1.6	−.9	1.0
Time deposits	2.9	1.9	−9.8	12.8
U.S. Government securities	−2.8	1.7	−1.7	1.7
Open-market paper	1.5	4.4	8.6	−2.0
State and local obligations	−.2	−1.1	5.1	.4
Consumer credit	.9	1.7	1.3	1.4
Trade credit	7.7	13.9	17.3	6.9
Other financial assets	3.8	1.4	6.7	
Discrepancy (sources less uses)	10.1	7.1	9.6	2.9

Source: Board of Governors, Federal Reserve System.

On the other side of the coin—the side pointing to continuing upward pressure on interest rates—is the fact that all levels of government will sharply expand their demands on the credit markets. Moreover, the demands for mortgage credit will increase if we are to progress toward our housing goal. While it is difficult at present to assess the net result of total credit demands on long term rates, there is little doubt that demands on the capital market will remain heavy in 1971.

Already there are signs that business has largely moved to a longer maturity financial structure. Bond financing by corporate business, which increased at a $12–$15 billion rate in the 1967–69 period, jumped to a record high of over $21 billion last year. In addition, net stock financing rose to new highs, although the increase in net new issues was not so spectacular as that for new bond issues. It might also be noted that business demands for bank loans showed little change in 1970, compared with an $11 billion increase in 1969.

Housing

This Committee has many times noted the fact that housing has had to bear the brunt of restrictive monetary policy. As a result of the tight monetary policy of 1969, private housing starts in the first half of 1970 fell to an annual rate of 1.3 million, only half the rate required to meet the Nation's housing goal of 2.6 million units per year. With the easing of monetary policy and the greater availability of credit as the year advanced, housing starts increased during the second half of the year and reached a 1.8 million rate in the fourth quarter. In the first two months of this year, housing starts were at a rate of 1.7 million.

Some of the steps taken last year did help recovery in this vital industry. Existing Federal and federally sponsored organizations continued to make heavy net purchases of government guaranteed or insured mortgages. In July, the Congress passed the Emergency Home Finance Act which supplements these activities. The Committee also notes with approval the prospect of a developing secondary market for conventional mortgage loans.

Analysis of the President's Budget strongly suggests that the Administration is not moving fast enough or vigorously enough to provide the housing aid already authorized by Congress. For example, the Emergency Home Finance Act of 1970 gave the President the power to establish an interest subsidy which would provide an additional 250,000 to 500,000 jobs in building more homes for low and middle income families. However, the Administration has failed to request any appropriation to implement this section of the Act, either in 1971 or in 1972.

More generally, it should be noted that *net* budget outlays on housing programs for fiscal 1972 total $1.8 billion, up about $300 million from 1971, but only insignificantly higher than in 1970. Even more strikingly indicative of the lack of the Administration's sense of urgency in the housing area is the approach to financial aid to housing:

1. *Gross* outlays are estimated to rise by almost $800 million, much of which has already been scheduled under old programs, but
2. This increase is to be offset by the projected increase of $460 million in sales of financial assets which will, if realized, tend to keep mortgage interest rates from dropping to more reasonable levels.

In the Administration's economic forecast, housing starts are assumed to increase to 2 million in 1971. In his testimony before the Committee, however, the Secretary of Housing and Urban Development indicated that 2 million starts was at the upper end of the range he regarded as likely for the year, and that vigorous policy measures would be required to achieve such a level.

In view of the fact that starts were already at 1.8 million in the fourth quarter and in view of the very great need for additional housing, we feel that policies should be aimed at achieving substantially more than 2 million housing starts in 1971. Policy should also be aimed at developing a more efficient construction industry which can continue in the future to produce an adequate supply of new housing at reasonable prices.

To achieve these goals will require a truly vigorous and coordinated policy effort. First, monetary policy must ensure that credit scarcity does not again become an oppressive restraint on housing. Second, effective measures must be taken to hold down excessive cost increases in the construction industry. Third, efforts to expand the production of housing by low-cost factory methods must be accelerated.

Credit

For the moment, the supply of credit may seem adequate to support the further expansion of residential construction, although mortgage interest rates remain higher than is desirable. Monetary policy in 1971 should continue to fully support the recovery in housing. At the same time, further institutional reforms must be undertaken to more effectively insulate housing during any future periods of tight money. The Federal Reserve has under way a major study of housing finance which the Committee hopes will soon be available and which should be given prompt and thorough review by the Congress.

Construction Costs

At the present, cost pressures are obviously a major restraint on housing. It is necessary not only to build an adequate supply of housing, but to offer it at prices which are not beyond the reach of families with average or below-average income.

Much emphasis has recently been placed on excessive wage settlements in the construction industry. We recognize that there have been some serious excesses, and we hope the Administration will act effectively to discourage their repetition. However, it should also be emphasized that these large wage increases have been awarded to only a fraction of all construction workers. The Committee was surprised and dismayed to learn how little factual data is available regarding construction wages.

The Labor Department should quickly enlarge its data on construction wages. In particular, more information should be developed on the number of workers who are unionized, the spread between union and non-union wages, geographical wage differentials, the average number of hours worked annually, and average annual earnings.

It should also be noted that wages are only one small part of total construction costs, and represent less than 15 percent of the on-site cost of building an average house. An effective cost control policy is required for materials, for land, for mortgage credit and for contractor profits, as well as for wages.

Industrialized Housing

The real key to adequate supplies of housing at reasonable prices lies in developing more efficient production processes. Administration efforts have concentrated on Operation Breakthrough, a program designed to develop and test innovations in housing design, construction, and marketing. While the Committee has always supported the application of improved technology to housing, we are concerned that after almost two years of Operation Breakthrough, HUD is only now negotiating contracts to begin production. Moreover, there is concern that the scope of Breakthrough is so limited—only 3,000 units are to be built—that the production techniques used will not represent a valid test of the extent to which mass production techniques can reduce housing costs. The Committee believes that selected projects of Operation Breakthrough should be accelerated and expanded to more realistically simulate mass production, as required under section 108 of the Housing Act of 1968. Enough is already known about techniques for improving housing production to begin a more valid test of the application of these techniques to mass production.

III. ACHIEVING PRICE STABILITY AND EFFICIENT RESOURCE UTILIZATION

1. Incomes and Price Policies

Current efforts to contain inflation and to promote productivity are totally inadequate. The Administration's periodic announcements in the form of inflation alerts have been piece-meal and ineffective; recommendations are yet to be forthcoming from its productivity commission; and no concerted effort is under way to eliminate pockets of high unemployment. Moreover, the experience of recent years has indicated that exclusive reliance upon general monetary and fiscal policies has resulted in either unacceptable levels of unemployment, if chief emphasis is put upon combating inflation, or in steady and even accelerating price increases, if a concerted effort is made to provide jobs for all who desire them. Apparently the trade-off between inflation and unemployment has become more unfavorable than it was in the 1950s; we now seem to face a higher level of unemployment for any given rate of price increase, or conversely, a greater rate of inflation for any given level of unemployment. The danger exists that, to the extent such structural shifts have occurred in the U.S. economy, these changes will be accepted as inevitable and unalterable.

The Employment Act of 1946 charges the Federal Government with the responsibility for promoting "maximum employment, production, and purchasing power." This responsibility can best be fulfilled by the explicit adoption of a long-term objective related to employment and the rate of price increase and by the mobilization of public opinion to assure the eventual achievement of this objective. Much of the difficulty found in combating unemployment and inflation today lies in the feeling held by the general public that problems of excessive unemployment and inflation, although pervasive, cannot be attacked specifically, and must be accepted as virtually inevitable.

The structure of the U.S. economy can, however, be changed when both the Government and the public at large are in agreement and determined to do so. The most dramatic instance of such change is the conversion to military production that occurred in World War II and, to a smaller degree, during the Korean War. Also impressive was the reconversion to peacetime patterns of output in the late 1940s. Another similar but more gradual change has been the progressive opening of the U.S. economy to the benefits of competition from abroad that began in 1934 and is continuing—not without challenge—to date. A similar structural transformation occurred between the 1930s and 1950s in the degree of organization of industrial workers and the potency of their bargaining capabilities vis-a-vis employers. All of these structural shifts have been brought about by Government acting in conjunction with the electorate.

The United States should adopt the twin long-term goals of reducing unemployment to a rate no higher than 3 percent combined with an annual increase in the GNP deflator of no more than 2 percent.[1] While there is no reasonable expectation that this objective could be achieved in the immediate future, it is not an impossible target. The actual performance of the U.S. economy met this criteria in 1953 and nearly achieved it in the previous year. To work towards achievement of this end, a permanent incomes-price board should be established under the direct leadership of the President to function through war and peace, recession and over-expansion. The board should have no power of compulsion but would attempt to achieve acceptance of its recommendations by influencing government policies that affect wages, prices, and employment and by educating the public concerning their stake and responsibility in the attainment of full employment and price stability. Perhaps the greatest single contribution the incomes-price board could make would be to dispel the false impression that either a high level of unemployment or a high rate of inflation is somehow inevitable.

Several smaller European countries have used incomes policies and wage-price freezes to good effect. The degree of success seems to be greatest when all sectors of an economy—labor, management, professionals, and consumer groups—can agree on a joint approach to the problems posed by excessive inflation and unemployment. Guidelines issued by an incomes-price board will be generally respected only if overwhelming agreement can be reached on their fairness and desirability and if the board has the full backing of the President and the Congress. The time required to consult with spokesmen for different groups and to secure their consent is an important reason that the ultimate objective cannot be attained in the immediate future. The chief initial responsibility of the board would therefore be to establish appropriate interim goals.

In addition to consulting with representatives of various economic interests, establishing guidelines, and publicizing specific violations of these guidelines, an important function of the incomes-price board would be to deal with urgent special problems. Besides attempting to eliminate centers of disproportionate market power, the board should be particularly concerned about reducing rates of unemployment among those who are unskilled, suffer from minority group discrimination, or are isolated in an area with inadequate job opportunities. In this respect, the board could recommend adjustment assistance policies to other branches of the Government.

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[1] Representative Bolling emphatically rejects any diversion from the objectives spelled out in Section 2 of the Employment Act of 1946 which he interprets as calling for stable prices, not persistent inflation, as would be implied by the target specified here of an increase of 2 percent a year. We may, indeed, do no better than the Committee suggests, but our target should be stable prices in the long run.

The President and the Congress should adopt as a long-term objective the twin goals of an unemployment rate no higher than 3 percent and an annual increase in the GNP deflator of no more than 2 percent.[2] To this end, a permanent incomes-price board should be established. The functions of this board should be as follows:

(a) To consult with representatives of labor and management in the goods producing and service sectors on establishing guidelines for achieving the long-term objective;

(b) To issue guidelines specifying acceptable increases in wages and prices;

(c) To publicize significant wage and price decisions that are not consistent with achievement of the long-term twin goals, and to make remedial recommendations to the parties concerned;

(d) To suggest methods, on one hand, for increasing the supply goods and services and, on the other, for eliminating pockets of unemployment; and

(e) To educate the general public in the importance and feasibility of achieving the long-term objective.

Since there is no prospect of achieving the long-term goals in the immediate future, the incomes-price board should set interim goals that will insure progress towards the ultimate objective and should publish guidelines consistent with these interim goals.

If accepted enthusiastically by the Congress and the Executive, an incomes-price board can make a major contribution to the health of the American economy and to the ability of our system to satisfy the needs of those participating in it. The costs of inflation to those who are compelled to live on fixed incomes and of unemployment to idle workers desiring to find a useful role in the economy are too high for our society to tolerate.

A period of experimentation will obviously be required before any incomes-price board can develop a mode of operation and intervention that is effective and acceptable to the major participant groups in the U.S. economy. Initial difficulties must not be allowed to lead to the abandonment of the ultimate objective. Only a few times in the past twenty-five years have we come close to realizing the goals of the 1946 Employment Act. If the economic performance of this country fails to improve in the future, the cause will not be our inability to improve; the cause will be indifference and greed.

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[2] See Representative Bolling's footnote, p. 34.

2. An Anti-Inflationary Policy for 1971

The persistance of inflation in 1970 despite rapidly rising unemployment has produced much questioning of our ability to combine price stability with full employment. We are confident, however, that the long-term price and employment goals discussed in the previous section are achieveable. Important progress toward these long-term goals can be made in 1971 provided we adopt the stimulative fiscal and monetary measures discussed in Chapter II, and also begin at once to make the institutional and structural changes discussed in this chapter.

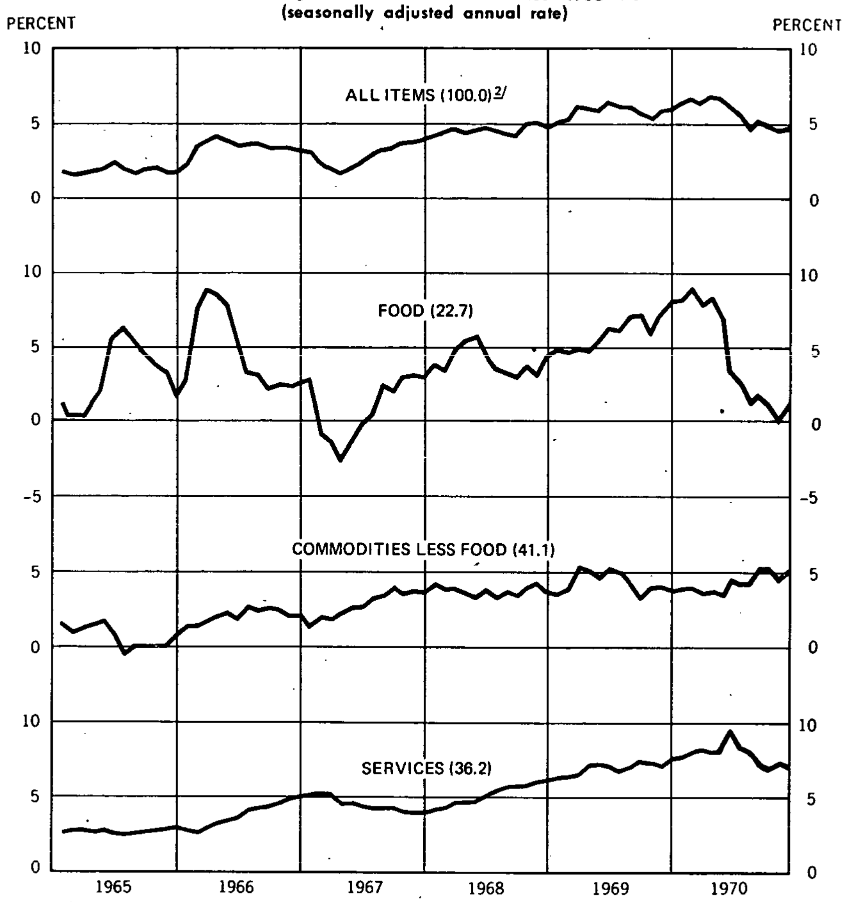
Immediate Need for a Price and Incomes Policy

Much of the public discussion of inflation in the past two years has centered around the question of whether the rate of price increase is rising or falling. Because several broad price indices are available and because they do not always move together in the short run, this question can be answered definitively only long after the fact. To us, the evidence to support claims that the rate of inflation has begun to taper off is presently not at all clear. The Annual Report of the Council of Economic Advisers discusses several alternative measures of price changes for gross national product and concludes that, whether one relies on the published GNP deflator or on any of three alternative possibilities for weighting price changes, prices increased at least as much in the fourth quarter of 1970 as in the third. The Council's Annual Report also shows that wholesale prices of consumer goods other than food and of producer finished goods rose faster in the second half of 1970 than in either 1969 or the first half of 1970.

Other price indices, including the Consumer Price Index and the total Wholesale Price Index, did show improvement in the latter half of 1970. However, only food price increases showed a really marked leveling off and, at the wholesale level, this trend was sharply reversed in the first two months of 1971. Chart 3 illustrates rates of change in the Consumer Price Index. As can be seen on the chart, the rate of increase in the price of commodities other than food was just about as rapid at the end of 1970 as it was during the earlier severe inflationary spurt of mid-1969.

CHART 3

Rate of Change[1] in Consumer Price Indexes 1965-70
(seasonally adjusted annual rate)



[1] In each month shown, the rate of change is measured over preceding 6 months, at an annual rate.

[2] Figures in parentheses are the December 1969 relative importance for the CPI.

U.S. Dept. of Labor
Bureau of Labor Statistics

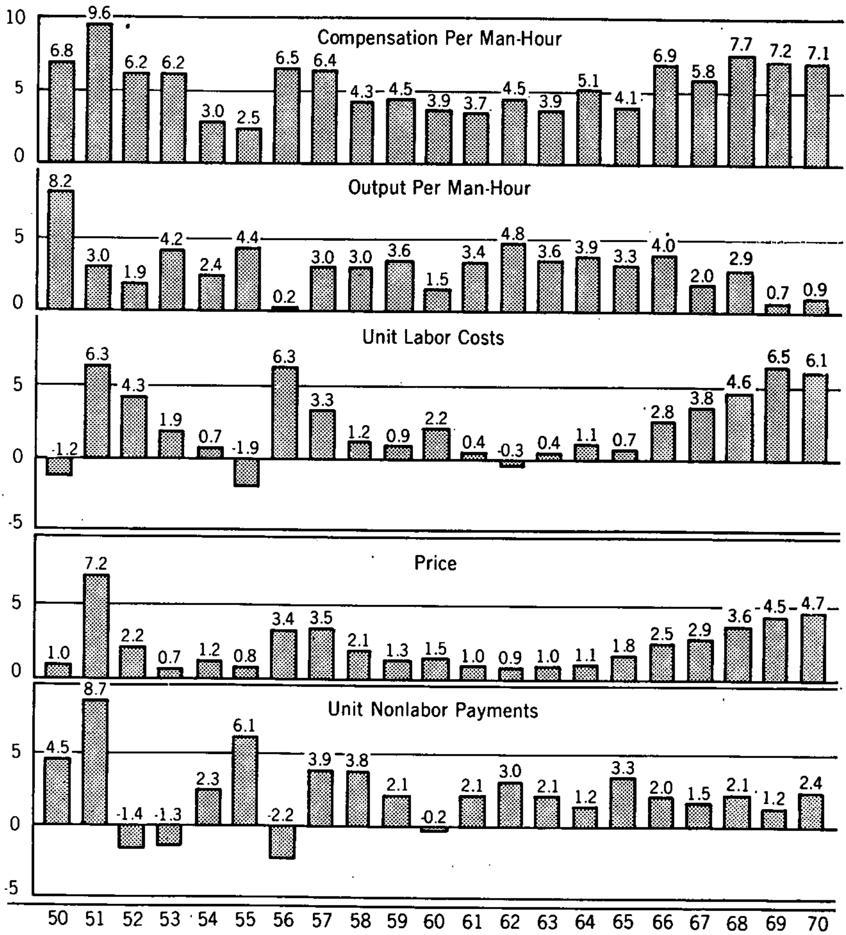
Because of the difficulty of interpreting short-run movements in the price indices, it is necessary to look also at probable supply conditions and at wage and productivity trends in order to evaluate the prospects for greater price stability this year than last.

1970 was a year marked by sudden shortages of certain basic commodities, most notably fuels, and by accompanying sharp price increases. The wholesale price of fuels and power increased 17 percent in the second half of 1970. The Administration took some action to partially alleviate the fuels shortage, but we believe stronger actions were, and are, called for. Lumber and other building materials also represent an area of potential shortage, particularly if hopes for a high level of housing starts materialize. The wholesale price of lumber and wood products has already risen sharply since the beginning of this year.

Greatly improved productivity has been widely predicted for 1971. Productivity did show gains in the second and third quarters of 1970, but there was a sharp reversal in the fourth quarter when productivity in the private nonfarm sector actually declined at an annual rate of 0.9 percent.Part of this reversal was due to the auto strike, but nevertheless these most recent productivity data are definitely not encouraging. As illustrataed in chart 4, compensation per man-hour in the private sector of the economy has increased by more than 7 percent in each of the past 3 years. In both 1969 and 1970 productivity gains (output per man-hour) have been far below the historical average of approximately 3 percent. As a consequence of these two factors, unit labor costs have advanced sharply.

CHART 4

Annual Rates of Change in Wages, Productivity, Costs and Prices--Total Private Economy



Compensation includes wages and salaries and supplemental payments for employees and an estimate of the salaries and supplements for the self-employed.

Nonlabor payments include profits, depreciation, interest, rental income and indirect taxes.

U.S. Department of Labor
Bureau of Labor Statistics

At least 4.8 million workers will be involved in major collective bargaining settlements scheduled for 1971. This is about 45 percent of all workers covered by major contracts. Virtually all of the remaining 55 percent of such workers are covered by contracts providing for deferred wage increases in 1971. These deferred increases average 7.8 percent, well above the 1970 average-deferred increase of 5.6 percent. Workers who negotiate this year will naturally feel a determination to keep up with increases in the cost of living and will also be reluctant to settle for less than the deferred increases of other workers. The prospect thus is that wage costs will continue to rise rapidly in 1971. The further prospect, in the absence of Federal guidelines for appropriate settlements, is that 1971 will be another year marked by labor disputes and major strikes.

An active and specific anti-inflationary policy is needed in 1971. The Administration should take the following steps:

1. An incomes-price board should be set up along the lines discussed in the earlier part of this chapter.

2. Pending the establishment of such a board, the President should consult with business and labor and should issue interim price and income guidelines designed to contribute toward a significant reduction in the rate of inflation.

3. Import restrictions which can be modified or removed by Executive Order should be relaxed. This applies to "voluntary" as well as mandatory restrictions. Increased imports of commodities such as steel, oil, textiles, beef, and sugar could make a major immediate contribution to price stability.

4. Government procurement policy should make a more active contribution to price stability. The 50 percent preference given domestic over foreign suppliers of defense equipment should be reduced.

5. Materials should be sold out of government stockpiles.

6. The anti-trust laws should be vigorously enforced.

7. The regulatory agencies should be encouraged to allow more price competition in regulated industries, especially in the transportation sector.

8. The General Services Administration should be instructed to serve as a purchasing agent for State and local governments on request.

We believe that the present difficult situation of continued inflation at a time of high unemployment is one in which a price and incomes policy is particularly necessary. This necessity is widely recognized. Chances of cooperation by business, labor, and the public are good.

Those who will be responsible for working out the details of a voluntary price-incomes policy may feel that the development and initiation of such a policy would be facilitated by a temporary price-wage freeze. If so, a freeze should be imposed. Such a freeze should be viewed only as a useful temporary device during a transitional period, not as a solution to the structural defects of the economy. If a freeze is imposed, it should be general. A freeze should not be imposed on only one industry, nor should it be applied to wages without also being applied to other costs or prices.

3. Manpower Policy

Of the many structural reforms which are required if reasonable price stability is to be combined with high employment, those related to the utilization of labor are the most fundamental of all. This Committee has long advocated adequate manpower training and job placement programs, both because of their direct value to individuals in providing them with the opportunity for productive and well-paid employment, and because of their value to society as a whole in promoting fuller use of the skills and abilities of the work force.

This Nation should have a comprehensive program to combat unemployment and underemployment whether the cause is technological change, changes in Federal expenditure patterns, increased import competition, or inequality of individual opportunity.

The manpower program should be funded and staffed at a level adequate to serve every citizen who has a legitimate need for job-training or job-placement assistance.

Our past failure to develop efficiently functioning labor markets is an important cause of our present economic difficulties. In order to have a full employment economy without inflation and in order to produce the particular combination of goods and services demanded by society, continuous shifts in the employment structure of the economy must take place. When a domestic industry grows less rapidly because of import competition, some individuals must leave jobs in this industry and find work elsewhere. When fewer people are needed in agriculture because of productivity gains, individuals must find jobs elsewhere. For 25 years, this Nation has made full employment a basic policy objective and commendable progress has been made in developing measures to promote that end. But we have not succeeded in developing adequate programs of assisting people to find alternative employment when old jobs disappear.

Because we do not have adequate programs to assist people in changing jobs, strong political pressures are created to maintain the existing structure of the economy, whatever the cost to the consumer and to society as a whole. Because the textile worker sees no alternative to his present job except unemployment, he is opposed to increased textile imports. Because laid-off defense workers are having great difficulty in finding alternative employment, pressures are created to re-employ them by again expanding defense procurement. If workers had assurance that new employment opportunities were available and if more of the costs of re-employment were paid by society, a major barrier to efficient functioning of the economy would be removed.

Labor shifts do not take place painlessly and automatically in response to market forces. Positive public policies to facilitate such shifts are required. Family incomes must be maintained during the transition period, moving costs must be met, workers must be retrained, and new jobs must be found. When it is in the national interest for employment shifts to take place, a considerable part of the costs of these shifts should be borne by society as a whole, rather than by the particular individual affected. Income support programs, job training programs, job placement programs, and public services employment programs represent the avenues through which the costs of structural changes can be paid by society as a whole.

An economy that combines high employment with reasonable price stability and an economy that produces the composition of goods and services which society demands is fully achievable only if workers can change jobs without loss of economic security and without fear of such loss. The costs of structural shifts in employment opportunities should be paid by society as a whole through programs of income support, job training, job placement, and public service employment.

When changes in employment patterns result from changes in Federal procurement policy, the case for Federal assistance to the affected workers is especially strong. The sharp increases in unemployment which have occurred during the past year because of reduced defense procurement and release of men from the armed forces did not have to take place. The cutback in defense spending, which has been relatively modest, was foreseen and publicly announced well in advance, as was the schedule of troop demobilization. Programs to re-employ defense workers and released servicemen could have been developed, but were not. This was a serious failure of national policy. It is a failure which should be remedied at once. An additional 910,000 servicemen are scheduled to be released in 1971 (a *net* reduction of only 264,000, since there will be 646,000 new entrants to military service). It is vital that these veterans be provided with necessary assistance in finding jobs.

If this country had in operation a comprehensive Federal program of income support and a comprehensive manpower program such as this Committee has advocated and continues to advocate, there would be less need for special programs to help particular groups of workers. Until such comprehensive programs are in operation, emergency programs of conversion assistance will be required. Conversion policy is more fully discussed in Chapter IV, but we reiterate our manpower recommendation here:

We believe it to be in the national interest that a shift in employment away from defense production take place and take place on a scale larger than appears to be presently contemplated. A shift of the desired magnitude is likely to be achieved only if defense workers can find new employment opportunities readily and can have assurance of income protection during the transition period. Since such a shift can be foreseen and planned for in advance, significant increases in unemployment during the transition period are unnecessary.

The Administration should proceed at once to activate a program which will assure returning veterans and workers who lose their jobs in defense industries that they can be confident of finding new employment and confident

of an adequate minimum level of income support during any transitional period of unemployment. This program should continue until such time as comprehensive Federal programs of income support and manpower services, discussed elsewhere in this Report, are in operation.

Shifts from one occupation to another are accomplished smoothly only in a full employment economy. When unemployment is high, workers naturally try to cling to jobs in declining industries since the probable immediate alternative is no job at all. The manpower policies we have recommended should be pursued in conjunction with fiscal and monetary policies designed to restore full employment. In addition, direct measures should be taken to provide more job opportunities in the public sector.

The Congress has presently before it The Emergency Employment Act of 1971, which would establish a significant program of public service employment. This legislation should be passed, and the President should sign it. This legislation is designed as an emergency measure to meet immediate needs. However, in view of the very great needs in the public sector—needs which will continue—there is no reason to suppose that the job opportunities which will be provided will be "make work" or "dead end." Rather, people who need jobs will be put to work quickly doing things which need to be done. When the economy returns to a high employment level, State and local governments will find themselves on a sounder fiscal basis, and it can be anticipated that many of those who are put to work now under an emergency program will advance into permanent positions. Others will find work in the private sector.

Although the President vetoed the comprehensive manpower bill passed by the last Congress, which provided for a program of public service employment, the Administration has subsequently clearly endorsed the concept of public service employment. In his manpower message of March 4, the President said:

> Transitional and short-term public employment can be a useful component of the Nation's manpower policies. . . . This Act would also provide *permanent* authority for public service job creation as part of an overall manpower program—but with the proviso that such jobs must constitute transitional opportunities. Within a two-year period participants must be enabled to move into the public employer's regular payroll, or helped to obtain other public or private employment.
>
> Public jobs created through manpower funds would thus be used to develop skills and abilities, with participants moving through such positions into permanent opportunities.

The Administration has also recently introduced legislation to provide public service jobs in conjunction with the proposed family assistance program. We support this concept. Such legislation cannot, however, be enacted as quickly as can the Emergency Employment Act. The Emergency Employment Act embodies the concept of transitional employment endorsed by the President in his manpower message. It would authorize up to $1.75 billion to finance public service employment over the next two years, if unemployment remains high. People could be put to work quickly—within a few weeks after the bill became law. Job applicants would be drawn from among all who were unemployed or underemployed, not just those covered by public assistance programs.

Because unemployment is presently so high and public service needs so vast, both the jobs provided for by the Emergency Employment Act and additional jobs which might be provided for in connection with subsequent manpower or welfare legislation are needed.

An initial program of public service employment should be enacted and put into operation as quickly as possible in order both to reduce the present high level of unemployment and to fill some of the many unmet needs in the public sector. Additional legislation providing for a longer term public service employment program, as well as for a comprehensive manpower training and job placement program, is also needed.

Unemployment Compensation

Important improvements in the unemployment compensation program were enacted last year. Insurance coverage was extended to almost 5 million additional workers, and provision was made for an additional 13 weeks of benefits at times of high unemployment. These new provisions can become effective only as conforming State legislation is adopted. As of late February, 15 States had begun paying extended benefits under the new law. Twenty-six other States had reached, or were approaching, levels of insured unemployment high enough to trigger the extended benefit provision, but had not yet taken the necessary State legislative action to permit payment.

Every effort should be made to encourage the States to act quickly to bring their laws into full conformity with the Federal Employment Security Amendments of 1970.

With the new extended benefit provision, the maximum total benefit period will be 39 weeks. Many workers, including agriculture workers, domestic household workers, and many State and local government employees are still not covered by unemployment insurance. The level of insurance benefits in most States is quite low. In only 26 States is the *maximum* benefit equal to at least 50 percent of the average weekly wage in that State. In only one State is the maximum equal to two-thirds of the average wage, a standard endorsed by both the Johnson and the Nixon Administrations.

The coverage of the unemployment compensation system should be further broadened, and the level of benefits should be increased, especially in those States where benefits are lowest relative to average wages. If unemployment continues at present levels, a further extension of the maximum duration of benefits should be considered.

IV. FEDERAL EXPENDITURE PRIORITIES

For the past two years this Committee has paid special attention to the problem of setting national priorities, through extensive work on improving budgetary systems and program analysis, by holding priority hearings, and by urging the Council of Economic Advisers, the Office of Management and Budget, and the Congress to devote greater attention to this critical area. The Committee's fundamental concern has been to ensure that the Nation's resources are used in a manner that maximizes both the private and public well-being of our society.

While not minimizing the difficulties of achieving such a goal, the Committee feels it can be done when the Nation has full information about our present priorities and their alternatives, objective analysis of the social costs and benefits of Government programs in achieving given priorities, and when a government is willing to make the hard choices that are the essence of setting national priorities. For in the end, because our basic resources and national output are limited, the setting of priorities involves choices for the Nation, of which the following are the most important:

- We must decide what economic growth and stabilization policy the Federal Government will pursue because this will determine the level of output the Nation can use in achieving its many priorities.
- We must decide between public goods and private goods.
- We must decide how we wish to allocate public resources between Federal, State, and local levels of government.
- We must decide how we will allocate resources within the Federal sector, choosing among defense, public works projects, SSTs, manpower training, pollution control, and other programs.
- We must decide which alternative is the most efficient for achieving a particular priority, using cost-benefit analysis wherever possible, because efficiency frees resources for use in satisfying other public or private demands.
- We must also decide among alternative programs on the basis of which ones provide the most equitable distribution of benefits.

The Committee is heartened by the increased interest and effort devoted throughout the country to a general reevaluation of our national priorities. It wishes to commend both the Council of Economic Advisers and the Office of Management and Budget for the additional emphasis they have placed, in each of their reports, on this critical question. On the other hand, the Joint Economic Committee finds that not nearly enough has been done, either to improve the information needed to understand how to reorder priorities, or to actually reorder priorities to meet the changing needs of our society.

It is in that spirit that the Committee wishes to stress additional considerations relevant to reordering national priorities. The first need is to focus on the major resource shifts proposed by the Administration in the FY 1972 budget, and what the Committee believes are some of the alternative choices available. The second need is to evaluate and choose the best alternative for providing financial aid to the State and local governments. The third need is to implement actions requiring that the full social cost of resources be paid in the areas of transportation and the environment. The fourth need is to establish Federal policies that will restore economic viability to the agricultural sector of our economy. Finally, there is the need for a complete reevaluation of how we account for the costs and effects of national security programs.

1. Major Budget Priority Changes in Fiscal Year 1972

In the fiscal 1971 and 1972 budget messages, the President has said that American priorities have been dramatically reordered, and he has cited as evidence that the share of the budget for human resource programs is increasing while the share of the budget for national defense is declining. Human resource programs, as defined by the Administration in the budget, include the functional categories of income security, education and manpower, health, and veterans benefits and services; the measure of national defense expenditures has been the functional category of the budget called national defense. This presentation of priority change has little overall utility and many aspects of it are misleading.

The Administration technique of explaining the shift in budget priorities is totally unsatisfactory. We urge the Administration, in future budgets, to candidly present major shifts in priorities on a program by program basis.

In order to understand the major expenditure shifts that will occur between fiscal year 1971 and 1972, one should not focus on the change in the entire budget or even on categories as broad as human resources. This is because most of the action in the budget is a continuation of programs established in past years and maintained year after year. It is more meaningful in the short run to focus on the budget margin, which represents the expenditures that are available for shifting in fiscal 1972, and which is equal to the sum of the aggregate increases in the size of the budget between fiscal 1971 and 1972 and the major decreases from the fiscal 1971 budget. This budget margin represents the total funds that are available for new or enlarged priorities in the fiscal 1972 budget.

With the concept of the budget margin in mind, it is possible to evaluate how priorities were reordered in the fiscal 1972 budget by answering three questions. First, what is the size of the total budget margin? Second, how much of the budget margin was used up by relatively uncontrollable program increases? Third, how has the administration used the remaining budget margin?

Table 2, which summarizes the major shifts in outlays between FY 1971 and 1972, shows approximately how the composition of the budget will change. The overall budget is estimated to increase by

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$16.4 billion, or 7½ percent, from $212.8 billion to $229.2 billion. In addition, major program decreases or asset sales from fiscal 1971 levels, a number of which are of dubious merit and not likely to receive congressional approval, are estimated at approximately $5.6 billion. The total of these two, $22.0 billion, represents the budget margin of funds available for new purposes in the FY 1972 budget. The uses to which this budget margin can be put are a combination of relatively uncontrollable increases and controllable increases representing the major program initiatives that are the priority choices of the Administration.

TABLE 2.—MAJOR CHANGES IN BUDGET OUTLAYS FOR FISCAL YEAR 1972

[In billions of dollars]

Sources of budget margin:		
Total budget increase from fiscal year 1971		16.4
Decreases from fiscal year 1971		5.6
Space research and technology	−0.2	
Medicare and medicaid proposals	−.8	
Assets transactions	−2.2	
Unemployment trust fund	−.8	
Postal rate increase	−1.6	
Total budget margin		22.0
Uses of budget margin:		
Relatively uncontrollable increases		12.0
Social Security	1.5	
Retirement and other trust funds	.8	
Medicare and medicaid	1.9	
Veterans benefits	.6	
Food stamps	.4	
Farm price supports (CCC)	.4	
Other public assistance	1.2	
Military and civilian pay	2.0	
Housing subsidies	.5	
Urban renewal and mass transit	.3	
Water pollution control	.6	
Interior Department assets changes	.8	
Other	1.0	
Relatively controllable increases		10.0
Welfare reform	.5	
Revenue sharing	4.0	
Social security benefits	3.0	
Department of defense	1.5	
School desegregation	.3	
Contingencies	.7	
Total budget margin		22.0

Source: Estimated from data in The Budget of the U.S. Government, Fiscal 1972.

Roughly $12 billion of the $22 billion budget margin is accounted for by pay increases, an expansion of income security programs, and other program increases that cannot be controlled through the budgetary process. Social Security, and other income maintenance programs, will rise by $6.5 billion due to increases in the number of beneficiaries, inflation, and higher benefit levels. Outlays will also increase by $2.0 billion to cover pay raises in fiscal 1972. Finally, previous commitments and contracts for housing subsidies, water pollution grants, urban renewal and mass transit, together with other similar outlays, will cause expenditures to rise by another $3.5 billion.

The remaining $10 billion of the budget margin represents the major priority decisions of the Administration. Although the immediate consequences of these decisions are shown in Table 1, some of the longer-run implications are not because the expenditure levels show only the beginnings of larger programs. In some cases, such as defense, obligational authority in the fiscal 1972 budget is a better indication of the future trend of the program. Nevertheless, taking into account both these considerations, the 1972 budget seems to reflect the following choices:

1. An increase in proposed revenue sharing from the $300 million proposal of last year to $4.0 billion. Evaluation of this proposal is undertaken in section two of this chapter.
2. An increase in aggregate Department of Defense expenditures of $1.5 billion that reverses the reduction in defense spending initiated in last year's budget. Evaluation of the Department of Defense and other national security outlays will be undertaken in section six of this chapter.
3. Continued support of $500 million to significantly revise the income maintenance area through the Family Assistance Program.
4. The first increment, $300 million, of a $1.5 billion in new authorization for project grants to local school districts to aid desegregation.
5. Expansion of social security benefits in line with Congressional desires will add $3.0 billion to costs in FY 1972. Major program changes include a 6 percent increase in benefits retroactive to January 1971, automatic benefit increases tied to the Consumer Price Index, an increase in widows' benefits, and liberalization of the work requirement.[1]

Thus, it would appear that the top priorities of the Administration are revenue sharing, defense, family assistance, and school desegregation. Although we support the concept of family assistance, along with increased outlays for social security and school desegregation, the Committee views the other choices as not really adequate to meeting the changing needs of our society. Nor is there a lack of evidence to support our concern. Our hearings on defense have developed evidence of such large-scale waste that we cannot believe the new increase in defense spending is merited at this time. On the other hand, the annual hearings of the Committee developed considerable evidence that nondefense public needs—health, housing and community development, education and manpower—were not being adequately met, in part because certain authorized and appropriated funds are not being utilized, and in part because the Administration's initiatives in this area have been inadequate.

Actual appropriations and outlays for a large number of programs, such as Model Cities, elementary and secondary education, and health care, have fallen increasingly behind their planned expansion. An analysis by the Advisory Commission on Intergovernmental Relations, issued in June 1970, reported that the authorization-appropriation gap had increased from about 20 percent in fiscal year 1966 to 35 percent in fiscal year 1970. This means that if programs were funded at just the 80 percent level of 1966, Federal expenditures for public investment could add at least $6 billion to the economy's spending stream. In addition, over $11 billion of appropriated funds are being withheld by the Administration. Together, the authorization-appropriation gap and the appropriation-expenditure gap account

[1] The Congress passed a Social Security bill on March 16th that raised general benefit levels by 10 percent but did not include the other aspects of the Administration's proposal. It is estimated that the Congressional bill will increase fiscal year 1972 social security costs to $3.5 billion, $500 million more than the Administration proposed.

for $17 billion in expenditure lag for public purposes. While we recog nize the need for some administrative discretion in order to keep total spending within a necessary ceiling, we feel that the Administration has often made poor choices of programs to cut. In some cases it has clearly flaunted the intent of Congress.

The inadequacy of the Administration's proposals in the non-defense area are quite dramatic when compared with what witnesses have advocated before this Committee. For example, the National Urban Coalition, presented *Counterbudget*—a detailed alternative budget that allocates a much larger share of the estimated $229.2 billion in Federal expenditures for fiscal 1972 to non-defense public needs. A comparison between the major budget proposals of the Administration and *Counterbudget* in table 3 reveals the following differences:

TABLE 3.—RECOMMENDED FEDERAL OUTLAYS, FISCAL YEAR 1972

[Millions of dollars]

	Administration	Urban coalition
Employment and manpower	$2,968	$4,394
Economic conversion	216	1,944
Social insurance	50,932	56,527
Income support	13,587	19,961
Health	19,140	19,745
Education	10,075	11,846
Metropolitan development	3,078	4,216
Housing	1,973	2,139
Total	101,969	120,772

Source: Estimated from data in The Budget of the U.S. Government, Fiscal 1972 and Counterbudget.

The total difference between the two proposals for these program areas is approximately $18 billion. The Urban Coalition budget would finance these and other non-defense program increases primarily through a reduction in defense expenditures of $16 billion in fiscal year 1972. While the Committee does not endorse all aspects of the Urban Coalition's *Counterbudget*, we do believe that it provides realistic alternatives to the Administration's priorities.[2]

The Committee urges Congress to establish higher priorities for manpower, health, education, housing, and economic conversion. This would require reductions in Administration priorities for defense, revenue sharing, and certain transportation expenditures, each of which are discussed separately in subsequent sections of this report. The Committee also urges Congress and the Administration to increase appropriations and outlays for previously authorized programs in the above non-defense areas.

[2] Representative Bolling states: "The use of the word 'realistic' in connection with the Urban Coalition *Counterbudget* might imply that it was realistic to attempt under present circumstances a reduction in defense spending of $16 billion between fiscal 1971 and 1972. If changing international conditions and binding agreements toward greater peace in the world should make possible substantial reductions in defense spending, I and every other American would be pleased at this prospect. We have ample uses for any budgetary savings this would make possible. I do not see anything in the present international situation suggesting that, in the face of rapidly increasing prices and wages which are increasing the defense costs (by official admission) by at least 10% a year, we could possibly make this kind of a reduction in the defense budget with safety."

2. Aiding State and Local Governments

The combination of inflation and recession which was experienced during 1970 created a financial crisis for many State and local governments. Serious fiscal imbalances existed prior to the economic deterioration of the past year, particularly in central cities and in certain rural communities, and these chronic imbalances have been sharply aggravated by depressed economic conditions. In addition, many governmental units that normally operate on a sound fiscal basis are now experiencing a severe budgetary squeeze.

In order to assess the magnitude of State and local budgetary problems and to adequately weigh alternative proposals for aiding States and localities, this Committee heard oral testimony from several mayors and governors, from the National Urban Coalition, from Congressional sponsors of legislation to aid States and localities, and from Administration spokesmen. In addition, the Committee has asked all 50 governors and a representative sample of mayors to supply us with detailed written information evaluating the effect of the Administration's proposed revenue-sharing programs on their needs and comparing these proposals with 1971 Federal assistance. While the results of this survey are not yet fully available, it is possible to set forth general conclusions regarding the need for Federal aid, the alternative possibilities for meeting this need, and the economic principles which should govern the choice among these alternatives.

The Impact of Inflation and Recession

While no precise estimate of the impact of inflation and recession on State and local governments is available, it is probable that the combined costs approached $10 billion in 1970 alone. Prices paid by State and local governments go up faster than the general price level. It has been estimated that in 1970 inflation increased State and local government costs by about $9 billion, while swelling receipts by only about $6 billion, thus creating a $3 billion gap.

During a recession, State and local revenues fall short of their potential because receipts reflect the slower growth of incomes. The effect is similar to the shortfall in Federal revenues that occurs during an economic downturn, although less sharp since State and local tax structures tend to be more regressive. It has been estimated that in 1970 State and local revenues fell almost $4 billion short of their full employment potential.

While reducing tax receipts, recession has the effect of increasing State and local expenditures due to the increased demand for public assistance and other programs of income support. It is difficult to isolate the growth in the welfare roles due to increased unemployment from the growth due to other causes, and a quantitative estimate of increased costs due to various causes in 1970 is not yet available. It is obvious, however, that the large increase in unemployment over the year has added substantially to the costs of operating welfare and other income support programs. When this substantial cost is added to the $3 billion cost of inflation and the $4 billion loss of tax revenue, it seems reasonable to suppose that the total cost to State and local governments of the depressed economic conditions of 1970 approached $10 billion.

General Revenue Sharing

The Administration has proposed a revenue sharing scheme under which a fixed percentage of the Federal individual income tax base would be distributed to the States under a formula based on population and relative tax effort. If the program were to begin when proposed, on October 1, 1971, $3.75 billion would be distributed to the States during fiscal 1972.

Many State and local governments face severe and immediate fiscal problems. Additional Federal assistance should be provided promptly. However, the general revenue sharing program proposed by the Administration does not fully meet the criteria of economic stabilization, equitable income distribution, economic efficiency, and tax equity which this Committee regards as fundamental to a sound program.

Economic Stabilization.—Because of its ability to engage in deficit financing, the Federal Government can maintain an appropriate expenditure level during periods of recession or slowdown without resorting to tax increases. State and local governments must normally balance their operating budgets and so become faced with the unsatisfactory choice of raising taxes in a recessionary period or of cutting back on necessary public services. The Federal Government thus has not only the responsibility to restore and maintain full employment with reasonable price stability, but also a responsibility to design programs of Federal aid to States and localities in such a way that increased budgetary support will be provided in times of recession or slowdown.

The Administration proposes to share with State and local governments a fixed percentage of the Federal individual income tax base. More precisely, the proposed legislation specifies a fixed percentage of "total taxable income reported on Federal individual income tax returns for the calendar year for which the latest published statistical data are available." Thus, the amount of shared revenues would be based on taxable income in a past year and would bear no direct relation to current economic conditions. The proposal contains no mechanism for providing additional budgetary support in times of recession. A revenue sharing proposal which provided for annual adjustment in response to changing economic conditions would overcome this defect.

Programs of Federal aid should contribute to the stabilization of overall economic activity. Such programs should provide additional budgetary support to State and local governments in times of economic slowdown or recession.

Income Distribution.—It is important to recognize that there are great disparities of income and of public service needs among the States and among the communities within any State. Some central cities and some rural areas have per capita incomes far below the national average, and these same areas also have larger than average demands for public services, particularly the income support, educational, and medical services required to cope effectively with concentrations of poverty. These areas do not have the tax base needed to finance an adequate level of public services. Until more progress is made in distributing tax resources more evenly within given metropolitan areas and within given States, these low income areas will remain dependent on substantial Federal aid, even in times of prosperity. In times of recession this dependence will be increased.

In communities where per capita incomes are close to or above the national average, there is much less need of Federal assistance in times of prosperity and reasonable price stability. These communities may, however, have acute needs for assistance in times of high unemployment. This will be especially true of communities which experience sharp rises in unemployment. There are major urban areas in which the unemployment rate more than tripled between mid-1969 and the end of 1970. Local budget structures are not designed to cope with the sharp divergence between increased public needs and reduced government revenues that such sudden changes in economic conditions create.

On the other hand, there are many communities where per capita incomes are well above average, tax burdens are below average, and unemployment is below average. Even in the present recessionary situation, these communities are not experiencing severe budgetary difficulties.

Programs of Federal aid should concentrate resources where the need is greatest.

The Administration's proposal would distribute revenues to States on the basis of population, with some adjustment based on the ratio of State and local taxes to average income within that State. Because of the progressive nature of Federal income taxes, this would have the effect of redistributing some tax revenues from rich States to poor States. In the words of the Assistant Secretary of the Treasury, the proposal would be "mildly income equalizing." Unless a complicated alternative procedure is elected, distribution of shared revenues to communities within a State would be based on the relative portion of total State and local revenues raised by that community. This formula makes no adjustment for differences in income levels, so that wealthy communities that find it easy to raise high revenues would receive relatively larger grants than poor communities with limited revenue-raising capacity.

Economic Efficiency.—Some public needs are national in scope and can be efficiently and equitably financed and administered by the Federal Government. Income support is an important example. The social security program illustrates the practicality of a comprehensive, and largely successful, Federal program of income support. Welfare needs are similarly national in scope and could be most effectively and equitably met by a comprehensive Federal program.

By contrast, it is widely agreed that elementary and secondary education is best administered at the local level. Yet there are important *national* benefits to assuring that every child receives an adequate basic education. A democratic society functions best if all of its citizens have been well educated. Furthermore, since individuals educated in one locality often subsequently live and work elsewhere, there is no particular equity or logic in expecting individual communities or individual States to pay all the costs of providing educations which will partly benefit other States and other communities. It is therefore appropriate for the Federal Government to contribute substantially to the costs of elementary and secondary education, while leaving administration largely to other levels of government.

Some public sector activities cannot be efficiently administered at the local level. Important examples are pollution control and metropolitan transportation systems. Air and water pollution cross local and State lines. Similarly, most of our major metropolitan areas require transportation systems which cross not only local but State lines. In both cases there is need for regional administration. In these examples, local, regional, and national benefits are involved, and financial contributions from several levels of government are appropriate. General purpose Federal grants to States and localities would be only a very indirect way of establishing and financing regional authorities to deal with regional problems. More efficient approaches are available.

Public sector activities should be administered at the level of government which can do so most efficiently. Federal financial contributions to programs administered at other levels of government should be proportionate to the national benefits of the activities being financed.

Tax Equity.—The progressivity of the Federal tax structure is often cited as an argument in support of additional Federal aid to State and local governments. But there is no reason why States, at least, cannot adopt tax structures as progressive as that of the Federal Government. One simple method of doing so is to adopt a State income tax which is a percentage of Federal income tax liability.

Some States have relatively progressive income taxes at the present time. Others have income taxes with little or no progressivity. Twelve States, including several of the wealthiest States, have no broadly based income tax. Of particular concern is the fact that many of the central city areas facing the most critical needs for public services are located in wealthy States that have failed to adopt income taxes and which, in some cases, have denied cities the authority to impose their own progressive taxes.

There is no sound economic argument for using Federal aid to close State budget gaps created by the unwillingness of the State to pay the political costs of adopting an equitable State tax structure. To the extent possible, Federal aid programs should be designed to avoid protecting States from the consequences of their unwillingness to reform tax structures.

Broadly based and equitable State tax structures, including progressive income taxes, should be encouraged.

The Administration's revenue sharing proposal rewards tax effort but not tax equity. It makes no distinction between regressive sales or property taxes, for example, and progressive income taxes. Given the wide variation among States, and the great reluctance of some States to move toward a more progressive tax structure, this is a serious defect.

An Alternative Aid Program

We have suggested four basic criteria for sound programs of Federal aid to State and local governments.

The following combination of Federal actions would conform to the fundamental criteria of economic stabilization, equitable income distribution, economic efficiency, and tax equity and would significantly improve the fiscal balance among levels of government:

1. Immediate actions to reduce inflation and increase employment. The necessary actions to achieve this goal are discussed in other chapters of this Report.

2. Enactment of a comprehensive Federal system of income support that would replace the present welfare system and to a large extent relieve States and localities of the present welfare burden.

3. Reform and consolidation of present Federal financial aid to regions, States, and cities. The basic concept of aid for definite broad purposes such as education, manpower training, community development, housing, pollution control, and transportation should be maintained.

Income Support

The enactment of a Federal system of income support, which would largely relieve the States of the costs of the present welfare system, would fully meet the suggested criteria relating to income distribution, economic stabilization, and economic efficiency. Under a well-designed system, payments would be made only to those genuinely in need, and anyone with genuine need would be provided with an adequate level of support. The program would function as an automatic economic stabilizer because the number of persons in need of public assistance rises in a recession and declines in a period of full employment. Such a program would be economically efficient because the problem is a national one which can best be met by a national program. The present system of disparate State programs is inefficient to the extent that it may provide artificial incentives for migration from one State to another. It is also, of course, inefficient in that it often fails to meet its basic objective of providing for those in need and in that it often provides disincentives to employment.

The objection has been raised that Federal assumption of welfare costs, while it may be desirable in itself, would not significantly help the cities because most of present welfare costs are carried in State rather than in city budgets. This argument is not altogether convincing. If States are relieved of welfare costs, they will have financial resources available to help the cities in other ways. The Governor of Pennsylvania testified to this Committee that if the Federal Government could relieve his State of the costs of welfare, he would recommend that the State of Pennsylvania "move quickly to relieve local communities of almost all costs of public education." We do not mean to imply, however, that cities will need no further Federal help beyond the assumption of welfare costs.

In last year's Annual Report, we discussed the general arguments in favor of a Federal program of income support. Such a program is desirable in itself and not solely because of the contribution it could make to easing State and local budget problems. We repeat the recommendation we made last year:

> **This Committee favors the adoption of a comprehensive Federal system of income support. Such a system should adhere to the following principles:**
>
> > **Equal treatment should be provided for every needy citizen regardless of location, work status, or family status.**
> >
> > **The level of support should be adequate to provide a decent standard of living.**
> >
> > **Opportunities for employment and incentives to work should be protected.**

The danger that able bodied persons might prefer "welfare to work" troubles many people. Certainly an income support program must contain a schedule of incentives which make work financially attractive. However, the far more serious problem at the present time is not willingness of the individual to work, but the ability of society to provide jobs. Work requirements or work incentives are meaningless when no job can be found. Income support programs must be coordinated with the vitally necessary job programs which we discussed earlier in this Report. In addition, if women with families are to be given meaningful opportunities for employment, greatly expanded and improved day care facilities for children must be provided.

Reform and Consolidation of Existing Federal Aid Programs

The existing programs of "categorical" Federal aid have been increasingly criticized. Much of this criticism is justified. Almost everyone would agree that there are too many separate programs, that the purposes are too narrowly defined, and that there are too many forms to be filled out. Programs need to be consolidated, some programs need to be cut back, and others need to be expanded.

In the process of consolidation, the broad national purposes which initially motivated the creation of these programs should not be forgotten. The changes in program funding levels which may accompany any consolidation proposal should be clearly spelled out and should be judged on their own merits. The transfers of administrative control to other levels of government which may accompany any consolidation proposal should also be carefully spelled out. The Federal Government should retain sufficient administrative control to ensure that funds are spent in ways which contribute to achievement of the broad national purposes for which the programs were created.

Alternatives for Further Federal Assistance

If the three basic steps we have recommended—restoration of a healthy national economy, adoption of an adequate Federal welfare system, and restructuring of Federal grant-in-aid programs—are adopted, the fiscal structure of this country will be much improved.

We believe there is wide agreement that these three steps must be taken, and taken without delay.

Even with these basic reforms, some communities may continue to need additional Federal assistance. Alternative possibilities for providing this assistance should be fully and carefully examined. The Administration's general revenue sharing plan is seriously deficient in at least four respects: it would not protect State and local governments against revenue loss in a recession; it would not do enough to concentrate aid in those communities which need it most; it would not encourage States and localities to modernize their governmental machinery; and it would do nothing to encourage more progressive State tax systems.

Alternative methods for aiding States and cities are available. Indeed, revenue sharing proposals have been introduced which overcome the basic deficiencies of the Administration proposal.

> **Full employment without inflation, an adequate Federal welfare system, and a restructured Federal grant-in-aid program are the essential elements in putting State and local governments back on a sound budgetary basis. Consideration should also be given to various alternatives for providing additional aid. While we are not endorsing revenue sharing, if limited revenue sharing or an alternative aid plan is adopted, it should contain features that encourage progressive State income taxes and the modernization of State and local governmental machinery, assure distribution of aid in accordance with need, and allow for additional budgetary support in times of recession or high unemployment.[3]**

3. The Environment

In the past, we have treated many environmental resources as free goods that could be used as lavishly as desired. On the other hand, industrial products have been underpriced because they did not include the cost of using "free" environmental resources. As a consequence, the well-being of our society has improved in the direction of inexpensive, mass-produced products while deteriorating in another direction—an increasingly polluted and unpleasant environment.

Since we desire both material goods and environmental quality, and since economic growth can provide the resources needed for environmental and social programs, we must establish new arrangements that allow us to choose among partially conflicting alternatives. Additional industrial and residential development will mean more polluted

[3] Chairman Proxmire states: "If further aid to State and local governments is required beyond the three basic steps recommended by the Committee, it can be achieved through the enactment of a partial credit against Federal individual income tax liabilities for State personal income tax payments. Such a credit should be allowed only for State income taxes which meet clearly defined standards of equity and progressivity. Provision should be made for an automatic temporary increase in the allowable amount of the credit during periods of abnormally high unemployment, with the extra amount being added to the State tax payments rather than retained by the individual taxpayer. A tax credit of this type would provide a strong incentive for the adoption of progressive State income taxes and it would act to support State revenues during periods of high unemployment."

water and less space for recreation. Improvements in the environment will often cause the prices of products to rise as a result of firms paying the full social cost for the resources they use. What we need is a set of rules for the environment that balance the benefits from improved environmental quality against the benefits foregone from the reduction of other activities, including economic activity. In addition, these rules must be supplemented by the expenditure levels needed to implement them.

Last year, this Committee called for a major attack on combating air and water pollution and solid waste disposal if future generations of Americans were to enjoy a hospitable environment. We further argued that this effort should incorporate measures based on user charges so that the financial burden of combating pollution is placed on those who do the polluting rather than the general public. These recommendations stressed our chief areas of concern and the strategy we felt best suited for dealing with pollution—that the costs of pollution be placed on polluters. This was our version of the principle that those who use resources should pay the full social cost for that use.

The Committee chose the strategy of charging polluters because it has the advantages of utilizing a price mechanism. The first advantage is that a charge is fair because it places the burden of the social cost of pollution on those who cause it. The second advantage is that a charge is an incentive for the polluter to minimize pollution, at every level of pollution, because such action will reduce his costs. The third advantage of a charge is that it is efficient, allowing the lower cost pollution control systems to undertake a larger share of the activity necessary to achieve a given level of environmental quality. The fourth advantage of a charge is that it is flexible since it can be imposed even when there is uncertainty over pollution control costs, and then adjusted as it is determined what level of charge will be necessary to achieve a particular level of environmental quality. The fifth advantage of a charge is that it would provide revenue to the Government that could be used to further pollution control in other areas.

An effluent charge is sometimes criticized on the ground that it is a "license to pollute." If properly used an effluent charge is nothing of the kind. It should be coupled with a requirement that the polluter take steps, according to a fixed timetable, to control his pollution by the best available technology. If he fails to comply, he should be subject to enforcement procedures, effluent charge or no effluent charge.

The Council of Economic Advisers has a comprehensive and intelligent discussion in this year's Economic Report of the many factors we must weigh in pursuing our attack on pollution. We especially commend the Council's statement that central to a successful strategy for improving the environment is that "the full social cost be paid for the use of resources." Moreover, we welcome certain initiatives the Administration has taken in this area, such as increased funding for recreation and municipal water treatment facilities, and the application of the principle of the payment of full social cost to air pollution in the form of charges on leaded gasoline and sulfur oxides.

We recommend that the Congress carefully consider enactment of taxes on sulfur oxide and leaded gasoline because such action would create disincentives in the use of these toxic substances by requiring that their price reflect full social cost.

The Committee is disturbed, however, by the Administration's apparent inconsistency in this area. The Administration urges noise standards while it remains silent about the social cost of noise from the SST; it calls for charges on industrial polluters who use federally assisted municipal waste treatment facilities, but excludes all other water polluters; it has requested legislation under which licenses will be required for ocean dumping without charges for the licenses; it has proposed a national land use policy with few built-in incentives to encourage its achievement; and it calls for more recycling of solid wastes while utilizing only $19 million of the $152 million Congress authorized for this purpose last year.

This Committee also regrets the implication given in the Economic Report that, while national standards for inter-state air and water pollution are desirable, all national standards for intra-state air and water pollution are to be avoided. If State A imposes strict pollution control standards on a given industry, and State B does not, the Economic Report inveighs against "governmental interference" with the reallocation of production that would occur when an industry moves from State A to State B because of State A's higher standards. The Report goes on to say that "the same considerations apply internationally as well as domestically."

The Committee disagrees with this approach. Unless vigorous steps are taken to put in place, at the national and ultimately at the international level, standards for pollution control, industries in environmentally conscious states and nations will suffer competitively with industries in states and nations that allow their environment to be degraded. We therefore urge the Administration to adopt national standards against environmental degradation, taking into account both inter- and intra-state pollution problems, and to take the lead, in the Organization for Economic Cooperation and Development and in other international organizations, to generalize these standards to as broad a group of nations as possible.

We urge the Administration to make greater efforts to comprehensively formulate rules for protecting the environment that are based on the principle that those who use resources should pay their full social costs. We also judge that the Congressional appropriations for solid waste treatment can and should be productively utilized at this time. Finally, we urge that the Administration set national air and water pollution standards that take into account both inter- and intra-state pollution problems, and take the lead in generalizing these standards internationally.

4. Transportation

Transportation is especially important to our Nation's well-being because it affects the rate of economic growth, the distribution of people and resources and the quality of our environment. As such, it is essential that government policies do not encourage the misallocation of resources through a divergence between private costs and social costs. The Council's Report places special emphasis on how such a divergence can occur when government regulation of transportation interferes with the competition that would encourage the efficient use of resources.

At the present time, the Interstate Commerce Commission regulates all rail traffic, 40 percent of truck traffic, and 10 percent of inland water traffic. The regulation is comprehensive with respect to surface transportation, covering rates, types of service, and the right of firms to enter and leave the industry or particular markets. A major effect of such regulations is to reduce rate competition among surface carriers and foster higher cost conditions in surface transportation. The regulation of the Interstate Commerce Commission has also restricted the entry of new carriers into the surface transportation field. Not only does such a policy conflict with the basic philosophy of a market economy, which is to encourage competition, but it deprives our society of the service and cost innovations that generally accompany the influx of new firms.

The restriction of competition, particularly with respect to prices, has had adverse effects on the carriers themselves. With price competition eliminated, carriers are left to compete on nonprice grounds such as speed and quality of service. Nonprice competition frequently leads to more and fancier equipment than is economically justified and excess capacity results. The costs of carrying this excess capacity have in turn tended to dissipate much of the financial gains to carriers that resulted from suppression of rate competition. The Council concludes that with respect to railroads: "The over-investment and misallocation of capital in railroad facilities, and the regulatory restriction on the ability of railroads to set rates that would capture profitable long-haul traffic where they are most efficient, have led to a steady decline in the railroads' own rate of return on investment from an average of 3.7 percent in 1950–59 to 2.8 percent in 1960–69."

The distortions that have been bred by the regulation of surface transportation also have come to characterize air transportation. Rates and entry conditions are controlled in this field by the Civil Aeronautics Board. As a result, free entry is prevented and nonprice competition and excess capacity are typical. In fact, it would appear that many of the problems the airlines experienced in 1970 are the direct result of the excess capacity they developed by overinvestment in airplanes.

Both the distortions that have occurred in the transportation area, and the regulatory policy that is to a great extent responsible, are issues that require a comprehensive reevaluation of the regulation of transportation. The Council of Economic Advisers concluded that such regulation was a "factor that interferes with an efficient use of resources in transportation, and it appears that regulatory patterns may have to be reexamined if the industry is to contribute its full potential to the Nation's welfare."

The Committee concurs with the analysis and findings of the Council. It recommends that Congress and the Administration undertake a complete reevaluation of government regulation of transportation, with increased effort made to substitute competition for regulation.

While the Council has exerted a useful initiative, the Administration has not developed the kind of unified approach to transportation that would consistently evaluate the social benefits and costs of alternative ways to meet a given transportation need. In addition, the Administration has strongly supported specific transportation expenditures that conflict with the Council's admonishment that private and social costs should not be permitted to diverge.

The Joint Economic Committee itself, through its Subcommittee on Economy in Government, has devoted considerable attention to these questions in the past year. In our report, *Federal Transportation Expenditure*, we made several recommendations that would improve the allocation of resources in the transportation area. One, that the Administration develop a unified approach to transportation based on a review of the full social costs and benefits of all proposed transportation investments. Two, that the Highway Trust Fund should be phased out because it encourages the inefficient use of transportation resources. Three, that the SST has limited public benefits but very significant social costs and, therefore, Federal financial support is not justified at this time.

The Administration should apply the principles laid down by the Council of Economic Advisers to questionable transportation programs it has advocated. It should withdraw its support for the SST, it should make plans now to phase out the Highway Trust Fund at the proper time, and it should drastically reduce the $250 million annual funding for inland waterways through a system of user charges. On the other hand, mass transportation has received too little attention and an accelerated program would be in the best interests of the Nation.[4] [5] [6]

5. Agriculture

In 1970 the agricultural sector suffered the effects of the general economic slowdown. Income received from farming declined in real terms, reversing the upward trend of the last two years. While consumer food prices rose in 1970, the prices received by farmers averaged only slightly higher than in 1969, and actually declined 10 percent between February and December. Prices paid by farmers continued to rise in 1970. Excessively high interest rates also added

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[4] Senator Sparkman states: "I find that my views on transportation differ substantially from those of my colleagues as expressed in this report and, for this reason, I must disassociate myself from the conclusions expressed in this section."

[5] See Supplementary Views of Senator Humphrey.

[6] See Supplementary Views of Senator Bentsen.

to production costs. (See Monetary Policy chapter for further discussion.) The resulting decline in income from farm sources was somewhat offset by an increase in income earned from non-farm sources.

Agriculture in the post-World War II period continued the sharp gains in efficiency that characterized it in the 1920s and 1930s. The result has been that today one farmer supplies the food needs of 40 persons, compared to only 10 persons a generation ago. The United States is required to employ only 6 percent of its labor force in agriculture, while the Soviet Union, for example, must devote 40 percent of its manpower to the agricultural sector. And the share of their income that American consumers spend on food products has declined steadily in the last 20 years—it now represents only 17 percent of their disposable personal income. This increased efficiency in farm production in the post-war years freed consumers' income for other consumption expenditures and for investment. At the same time, agricultural products continued to be a favorable contributor to the American balance of trade.

In the late 1960s, however, the large productivity increases that American agriculture had enjoyed for the last 40 years leveled off. Measured by farm output per unit of total input, which includes capital and land as well as labor, productivity on the farm has actually declined slightly since 1965. This compares with increases of 14 percent in the 1930s, 18 percent in the 1940s, and 24 percent in the 1950s. If the productivity advances that characterized the agricultural sector previously cannot be regained, there will be important consequences for our entire economy. First, the reversal of productivity trends in agriculture in the 1960s will retard further improvement in our standard of living. Second, inflationary price increases in all sectors of the economy cannot be dampened without a rise in productivity since labor and other costs will continue to rise. The large real wage gains that American workers have experienced have been made possible by productivity increases which allow wages to rise faster than prices. Productivity increases in agriculture must be regained if we are to maintain stable food prices.

Unfortunately, at a time when further research is needed to develop methods for increasing efficiency in farming, this year's budget does not increase outlays for research and development for more efficient farming techniques. Existing research and development programs should be carefully evaluated to determine if they contribute to increasing farm productivity. The Department of Agriculture should also examine the possibility of new programs in research and development which would provide new inputs into the problem of increasing efficiency in farming.

The breakdown of the increase in food prices during 1970 bears mention. Roughly 95 percent of the increase is attributable to higher prices to intermediate handlers—the food processors, distributors, and retailers. The remaining 5 percent is accounted for by higher prices at the farm. As a result, the farm-retail spread for food prices increased 7 percent in 1970. This occurred primarily in widening margins for meat products, but other products also shared in the increase.

It is not yet clear whether price increases at intermediate levels were due to a rise in profit margins or to an increase in costs. Further study of this problem is clearly warranted. If profit margins at intermediate stages of preparation have indeed increased, the President should call attention to this fact. As prices continue to rise, the consumer is worse off, but in the past year the farmer has also suffered even as retail food prices rose. Both these groups—the farmers and consumers—do not have enough market power to significantly affect prices. On the other hand, the market power of intermediaries between the farmer and the consumer should be examined to determine if they are unduly restraining market forces from operating in setting food prices.

Still another reason for the poor income position of the typical farmer is the uneven distribution of most farm subsidies. Since these subsidies are to support farm income, one would expect that they be distributed in accordance with income levels—poor farmers receiving the most and rich farmers the least. Such a distribution would improve the income of the typical American farmer. However, available evidence suggests that the largest share of farm subsidies goes to upper income farmers. This was documented in a 1968 pioneering study by James Bonnen, "The Distribution of Benefits from Selected U.S. Farm Programs." The summary data from that study is contained in Table 4. As the Table clearly shows, the top 40 percent of farmers receive approximately 75 percent of the benefits from most subsidy programs. Farm income support programs should be carefully reviewed to determine if the distribution of benefits is equitable. Every effort should be made to enforce the recently passed crop subsidy limit of $55,000 per crop.

TABLE 4.—DISTRIBUTION OF FARM INCOME AND VARIOUS PROGRAM BENEFITS: PROPORTION OF INCOME OR BENEFITS RECEIVED BY VARIOUS PERCENTILES OF FARMER BENEFICIARIES

Item	Percent of benefits received by the—						Gini concentration ratio
	Lower 20% of farmers	Lower 40% of farmers	Lower 60% of farmers	Top 40% of farmers	Top 20% of farmers	Top 5% of farmers	
Farmer and farm manager total money income, 1963 [1]	3.2	11.7	26.4	73.6	50.5	20.8	0.468
Rice, 1963 [2]	1.0	5.5	15.1	84.9	65.3	34.6	.632
Wheat, 1964:							
Price supports	3.4	8.3	20.7	79.3	62.3	30.5	.566
Diversion payments	6.9	14.2	26.4	73.6	57.3	27.9	.480
Total benefits [3]	3.3	8.1	20.4	79.6	62.4	30.5	.569
Feed grains, 1964:							
Price supports	0.5	3.2	15.3	84.7	57.3	24.4	.588
Diversion payments	4.4	16.1	31.8	68.2	46.8	20.7	.405
Total benefits [3]	1.0	4.9	17.3	82.7	56.1	23.9	.565
Cotton, 1964 [2]	1.8	6.6	15.1	84.9	69.2	41.2	.653
Peanuts, 1964 [2]	3.8	10.9	23.7	76.3	57.2	28.5	.522
Tobacco, 1965 [2]	3.9	13.2	26.5	73.5	52.8	24.9	.476
Sugarcane, 1965 [4]	1.0	2.9	6.3	93.7	83.1	63.2	.799
Sugarbeets, 1965, [4]	5.0	14.3	27.0	73.0	50.5	24.4	.456

[1] David H. Boyne, "Changes in the Income Distribution in Agriculture," Jour. Farm Economics, vol. 47, No. 5, December 1965, pp. 1221–2.
[2] For price-support benefits.
[3] Includes price-support payments and, in wheat, certificate payments as well.
[4] For price-support benefits plus government payments.

Sources: Except as noted, all figures are from the Lorens curve and Gini concentration ratio computations previously presented, although previous tables were not set up on quite the same heading intervals.

The Administration should carefully examine the adequacy of Federal research and development and credit programs for agriculture. New efforts should be made to stimulate productivity in the agricultural sector. The Administration should also determine why the margin between farm prices and consumer prices is widening and take appropriate action to rectify this situation. Finally, every effort should be made to ensure that farm subsidies are equitably distributed and to strictly enforce the recently passed crop subsidy limit of $55,000 per crop.

6. Defense and National Security

Defense Spending

Although there is no easy way of measuring the impact of national security expenditures on the economy, an attempt to evaluate the effects should be made. The sums spent in the pursuit of national security are very great, and the Administration is proposing this year that they be made greater. Unfortunately, the Economic Report of the President and the Annual Report of the Council of Economic Advisers do not address themselves to the critical issues created by defense spending.

The relationship between defense spending and inflation should be obvious by now. It is true that the causes of inflation are complex and that no single factor, such as an increase in defense spending, can be considered the sole cause of inflation. However, the correlation between defense spending increases and price increases is remarkable. In the past two decades, the fires of inflation have been stoked on two separate occasions with the fuel of war and defense spending increases: between 1950 and 1953, and since mid-1965. National security outlays must be considered a prime contributor to the inflationary trends in each of these two periods.

As was pointed out in the testimony of private witnesses before this Committee, the present high level of defense spending has been inflationary in several respects. Such spending contributes to money income and demand without a corresponding addition to output available for consumption in the private sector of the economy. It entails high opportunity costs, measured as the lost output of the men and materials absorbed by the military establishment. Moreover, the war and the high level of defense spending have contributed and are continuing to contribute to an inflationary psychology.

The procurement policies of the Department of Defense and the practices of defense contractors have also contributed to inflation. Mismanagement, waste, and inefficiency have led to unwarranted increases in the prices of military hardware. Cost over-runs on such multi-billion dollar weapons programs as the C–5A, the F–111, and the Mark 48 torpedo appear to be continuing unabated. The investigations of this Committee and others in the Congress have demonstrated that much of the over-runs and the high costs of weapons are due to poor planning, unreasonable technical specifications and requirements, sometimes known as "gold plating," and faulty managerial techniques. Both the Government and the private sector are responsible for this sorry situation.

There has been much discussion of the lack of confidence on the part of the American consumer. In the judgment of this Committee, the consumer's confidence will not fully return so long as the debilitating and demoralizing effects of the war in Southeast Asia persist. After more than two years in office, the Administration has succeeded in reducing U.S. involvement in ground action and direct outlays for the war. Defense expenditures have also been reduced, although the revised estimates for fiscal 1971 reflect a substantially smaller reduction than had been originally forecast. At the same time, U.S. involvement in air action in the war appears to have intensified, and the fighting on the ground and in the air has now spread into South Vietnam's two neighboring countries, Cambodia and Laos. Recommended budget authority for fiscal 1972 for national defense is $80.2 billion, an increase of $6 billion over the total obligational authority for 1971. This indicates that the Administration plans to resume the upward trend in defense spending in the near future.

What is most disturbing is the message implied by the figures in the budget. Despite the assertions of a successful transition to a peace-time economy, it is difficult to see anything peace-time about an $80 billion national defense budget. It is simply not possible to make a transition to a peace-time economy with a war-time level of defense spending. If it is the policy of the Administration to relieve the unemployment problem by increasing defense spending, the Committee is in strong disagreement with that policy.

In the interests of national security, defense spending should be reduced in fiscal year 1972 substantially below the estimated outlays for fiscal 1971 through reform of weapons procurement to eliminate the unnecessary cost over-runs, gold-plating, and waste that pervade the procurement system, and to achieve a more effective and efficient military program.[7] [8]

The National Security Budget

In order to understand what our Federal spending priorities are, we need to have some confidence in the annual estimate of outlays for each category of spending, and we need to be assured that the categories themselves are properly identified. The category in the Federal Budget called "National Defense" presents serious problems on both counts. First, Administration estimates for national defense expenditures are notoriously wide of the mark. The budget estimates for the current fiscal year, 1971, have already been sharply modified. Last year, the proposed budget for national defense in FY 1971 was $73.6 billion. This year, the estimate has been raised to $76.5 billion, an increase of nearly $3 billion. In general, the tendency has been for the Administration to overestimate prospective reductions and to underestimate prospective increases. In our judgment, the Administration

[7] See Representative Bolling's footnote, p. 48.
[8] See Supplementary Views of Senator Bentsen.

needs to do a better job of estimating the levels of expenditure for national defense.

Second, the budget category "National Defense" does not fully identify all of the items of expenditure that should be included in that category; the definition of national defense found in the budget is so restrictive that the outlay figures do not adequately reflect the true costs of national security. Listed under the National Defense Budget at the present time are the following items: Department of Defense—Military, Military Assistance, Atomic Energy, Stockpiling of Strategic and Critical Materials, Expansion of Defense Production, Selective Service System, and Emergency Preparedness Activities.

It is apparent from this listing that some recognition has been given to the fact that it is important to itemize the defense-related expenditures and to distinguish them from those of the Department of Defense. In addition, however, are a number of programs which also make a direct contribution, in whole or in part, to national security or which would probably not be undertaken but for the requirements of national security. In this category are the Coast Guard, the Veterans' Program, the Department of State, the United States Information Agency, the Arms Control and Disarmament Agency, the Renegotiation Board, the National Aeronautics and Space Administration, the National Security Council, and expenditures for interest on the national debt. Although experts differ on the question of whether all of these programs should be considered defense-related, economists such as Arthur Burns have concluded that expenditures for international programs and for space research and technology "are mainly pursued in the interests of our national security," that the Veterans' program is entirely a legacy of past wars, and that interest on the national debt is preponderantly a payment for past wars.

In our judgment, expenditures for defense and defense-related activites should be incorporated under the heading "National Security" and should contain the following types of information:

(1) Total outlays of the Department of Defense for military purposes;

(2) Outlays of all other agencies or programs whose activities are related to current military programs;

(3) Outlays of all other agencies or programs justified on the grounds of national security; and

(4) Outlays of all other agencies or programs in payment for past wars or military programs.

The more important reason for expanding the current breakdown of defense expenditures is to reflect as accurately as possible the full costs of national security, whether pursued through programs administered by the Department of Defense, the Department of State, or any other agency. Of course, it would not be implied by identifying total national security expenditures that all of them are subject to the same sort of control by the Administration or the Congress.

Table 5 is a breakdown of the National Security Program actual outlays for selected years from FY 1965 to FY 1970. Estimated outlays are shown for FY 1971 and FY 1972. The Administration's requested obligational authority for FY 1972 is also shown.

TABLE 5.—NATIONAL SECURITY BUDGET

[In millions of dollars]

(Fiscal years)

	Outlays						
	1965	1968	1969	1970	1971 (est.)	1972 (est.)	Authority 1972
Defense, military assistance and defense related activities:							
DOD military [1]	46,173	77,373	77,877	77,150	73,370	74,975	77,663
Military assistance [2]	2,469	1,237	1,355	1,186	1,823	1,827	2,052
Atomic Energy	2,625	2,466	2,450	2,453	2,275	2,318	2,251
Space Research and Technology	5,093	4,721	4,247	3,749	3,368	3,151	3,270
U.S. Arms Control and Disarmament Agency	7	11	10	11	10	9	9
Renegotiation Board	3	3	3	4	4	5	5
National Security Council	1	1	1	1	2	2	2
Stockpiles	16	19	18	15	27	30	30
Expansion of defense production	60	51	166	−15	−167	−24	
Selective Service	43	57	65	75	75	78	78
Emergency Preparedness	17	12	11	4	10	9	7
Deductions for offsetting receipts	−124	−116	−138	−118	−278	−898	−898
Subtotal	56,383	85,835	86,065	84,515	80,519	81,482	84,469
Payments for past wars and defense program:							
Veterans benefits	6,080	6,882	7,640	8,677	9,969	10,644	10,991
Interest [3]	8,577	10,308	11,843	13,734	14,575	14,765	14,765
Subtotal	14,657	17,190	19,483	22,411	24,544	25,409	25,756
Programs justified on grounds of national defense: [4]							
Ocean shipping [3]	253	227	236	239	326	345	374
Impacted area school aid [3]	263	380	299	492	384	365	330
Subtotal	516	607	535	731	710	710	704
Total, National Security	71,556	103,632	106,083	107,657	105,773	107,601	110,929

[1] DOD Military excludes DOD civil outlays which totaled $1.2 billion in 1965; $1.3 billion in 1968; $1.3 billion in 1969; $1.2 billion in 1970; $1.4 billion in 1971 (est.); $1.5 billion in 1972 (est.); and $1.5 billion in new obligational authority for 1972.

[2] Includes Military Assistance Program (MAP), supporting assistance, credit sales, and part of the Food for Peace Program. Excluded are outlays for military assistance purposes funded through the Department of Defense.

[3] Includes 75% of the program.

[4] Portions of programs, other than those listed, have been justified in the past as essential to national security, including the National Defense Highway System, the airport program and others. The committee intends to further analyze this matter.

Source: Estimated from data in The U.S. Budget, various years.

This is admittedly an imperfect attempt to explain to the American taxpayer the full costs of national security, whether for past or present wars or defense.

The Committee recognizes that others will question certain items contained in the national security program, that objections will be raised to parts of it, and that suggested changes will be proposed. Last year in our Annual Report, the Joint Economic Committee recommended that the full costs of past and current defense-related activities be included in the category of defense programs found in the budget document. No action was taken on this recommendation. We now hope that the national security program breakdown that we have offered will provoke widespread discussion and debate, and that the Office of Management and Budget will be moved to incorporate this concept in next year's budget.

The Office of Management and Budget should rename the National Defense Budget the National Security Budget and should include as separate line items in addition to those presently listed: outlays of all other agencies or programs whose activities are related to current military programs; outlays of all other agencies or programs justified on the grounds of national security; and outlays of all other agencies or programs in payment for past wars or military programs.

The Costs of the War in Southeast Asia

The inadequacy of the discussion of national defense in the budget document is underlined by the Administration's failure for the second year in a row to disclose the current costs of the war in Southeast Asia. Prior to 1970, the costs of the war were regularly provided to the Congress and the public through the budget document and through discussions in the Economic Report of the President. It is a basic principle of accountability that the Government explain to the people how its tax dollars are being spent, especially when part of those tax dollars are being diverted to fight a war.

While the costs of the war were steadily increasing in the past, the Government showed no reluctance in reporting the figures. It should be noted that from 1965 through 1968, total defense expenditures increased greatly, primarily as a result of the war in Southeast Asia. There was a direct correlation between the enlargement of the war and the enlargement of the defense budget. The Committee judges that the American people are as entitled to know the costs of the war during the period in which it is winding down, according to the Administration, as when it was escalating.

The omission of the costs of the war from this year's budget is puzzling for another reason. Last year, after the budget document and the President's Economic Report were released, the Defense Department discussed Southeast Asia costs in testimony before the appropriations committees of the House and Senate. Although the hearings were in executive session, the testimony was later made public. In the testimony, it was asserted that the incremental costs of the war in fiscal 1969 were $21.5 billion, and the incremental costs for fiscal 1970 were estimated at $17.4 billion. Less than one year earlier, the Defense Department provided the Joint Economic Committee with a different set of figures on the cost of the war. The costs supplied to this Committee showed that $28.8 billion would be spent for the war in fiscal 1969, and that the costs would amount to $24.9 billion in fiscal 1970. Aside from the wide variance between these two sets of figures, there is the serious question of suppressing the costs of the war from the annual budget document and Economic Report of the President and then subsequently supplying the figures to a Committee of Congress in closed-door session. Separating the costs of the war from other defense outlays defeats one of the principal purposes of the

Federal budget. Delaying the release of these costs, if they are to be released, until after the Joint Economic Committee has held its annual hearings, prevents this Committee from making a complete study of matters relating to the Economic Report.

The Administration should resume the practice of making full public disclosure in the budget of the annual costs of the war in Southeast Asia, the amount by which costs have been reduced from the previous year, and estimates for future expenditures.

Economic Conversion

In its Report, the Council of Economic Advisers points out that employment attributable to Department of Defense expenditures will have decreased by nearly 1.8 million workers from fiscal year 1968 to fiscal 1971, that most of the decline is in private employment (1.3 million workers), and that reductions in the armed forces account for most of the remainder. The Administration takes credit for managing two simultaneous transitions, in the words of President Nixon, "from a wartime to a peace-time economy and from a higher to a lower rate of inflation." It is also asserted that these transitions were inevitably accompanied by some decline in output and a rise in unemployment. According to the Council of Economic Advisers, "if the past and current inflation had not been in the picture, it would have been possible safely to maintain more expansionist pressures in the economy and the labor market; resources released from defense uses could have been more quickly redeployed to new uses; and workers affected by defense cutbacks would have found it easier to obtain new jobs." Thus, according to the Administration, the recent increase in unemployment was caused by the overall program of restraint, which itself made it impossible to take steps to counteract the unemployment.

The Committee rejects this argument. It was wrong and unnecessary to impose the costs of fiscal restraint on the shoulders of the already overburdened worker and on the backs of ex-G.I.s. Steps could have and should have been taken to provide retraining, relocation assistance, employment information, and even jobs to those persons in the defense industries and in the armed services who became unemployed as a matter of Federal policy.

The Committee notes the establishment in 1970 of an Interagency Economic Adjustment Committee under the chairmanship of the Secretary of Defense. This committee is supposed to assist communities who are seriously affected by defense cutbacks by assuring to them the services and facilities of the Federal Government. According to the Economic Report, the committee operates through a task force which "visits the community and assists the local leaders, whose initiative is indispensable, to prepare a plan for action. . . . Each plan would attempt to mobilize private, municipal, State and Federal resources to create an economic base which will utilize the local labor and capital. The Federal contribution to the combined effort, in addition to advice, may include economic and engineering surveys, public facilities grants, small business loans, surplus real property, and funds for manpower training programs, as well as Federal expenditures to carry out a variety of programs." The Committee approves of this development as a step in the right direction. But much more needs to be done.

An economic conversion program should be adopted to assist individuals and communities adversely affected by reductions in defense spending. Until comprehensive manpower and income support programs are available to all who need them, special unemployment compensation and retraining should be made available to workers displaced as a result of defense cutbacks. There are many cases where it is desirable for bases to be transferred to communities for public purposes. In such cases, communities should be assisted in acquiring possession and title to the land and facilities on the base without undue delay.

SUPPLEMENTAL VIEWS OF VICE CHAIRMAN PATMAN

I agree with the overall thrust of policy recommendations contained in our Report. However, there are some recommendations which are not entirely acceptable to me. One of the most important of these areas deals with the absolute need for the Administration to adopt forceful measures—even more forceful than is advocated by the Report—in order to halt inflation, greatly reduce unemployment, and sufficiently stimulate the construction of housing and public works and facilities to meet urgent national needs.

I wish to make it clearly understood that monetary policy is not stimulative enough. Long-term interest rates are far too high, particularly for mortgage credit and for Federal, State, and local borrowing. They must be brought down by appropriately stimulative monetary policy, and if this means that the Federal Reserve brings about an expansion of money by more than 6 percent, the upper limit to our "Rule," then this should be done.

I do not believe that fiscal policy, as outlined by the Administration, is stimulative. The deficits envisioned for this fiscal year and next are a direct result of ill-advised policies of the past year which put the economy in a straitjacket. It would indeed be possible through more stimulative budget policies, not only by postponing projected Social Security tax increases (as already initiated by Congress) and moving up the individual tax costs, but by expanding outlays for much needed social purposes—that the actual deficit realized next year will be lower than it otherwise would be under proposed policies.

These steps may involve some danger of further inflation. But this danger need not arise if the Administration uses its existing authority to impose temporary wage and price controls authorized by Congress last year. Moreover, the use of these controls should be on a basis broad enough to be effective in terms of halting the wage-price spiral by being imposed on major components of the economy. Such a course stands in sharp contrast to the narrow and discriminatory decision by the Administration to revoke provisions of the Davis-Bacon Act for construction workers employed on Federal projects. All that the Administration succeeded in doing here was to single out a relatively small group of construction workers and in essence say to them that they are to simultaneously serve as a warning and a scapegoat for continuing inflation. It would have been unfair to have placed such a burden on the construction industry alone—even if management was included with labor—but to single out only a small portion of the labor involved in the construction industry is sheer folly.

A broad set of guidelines should be developed by the Administration during any period when a temporary wage-price freeze is in effect, and these guidelines should be applied immediately following the lifting of controls. The guidelines principle should be made a permanent tool of economic policy, for as we return to full employment the danger of inflation will always be present. At the very least, the Administration should forthrightly and openly engage in actively opposing such flagrant wage and price increases as we have witnessed in the last two years. It should do so in a way that will serve to dampen pressures that are raising wages and prices rather than pursuing the present practice of announcing what damage has been done after the fact.

In connection with the need for a more stimulative fiscal and monetary policy, Congress should, as soon as possible, pass legislation similar to that which is contained in H.R. 3550 and S. 580, identical bills designed to establish a National Development Bank. The essential purpose of such a bank is to assure that an adequate source of loan funds at reasonable interest rates is made available to:

(1) State and municipal governments for public works and facilities;

(2) Small and medium size commercial and industrial entities to create employment and job training opportunities in depressed urban and rural areas through loans for the location of new industry and the expansion and improvement of existing business and industry; and

(3) Public agencies and private nonprofit or limited dividend groups for the construction of low and moderate income family housing projects.

National Development Bank loans would be available to those creditworthy businesses and industries, individuals and organizations that cannot obtain adequate loan funds at reasonable rates to achieve the purposes of such an act. To assure that the Development Bank is adequately funded, Congress should appropriate at least $1 billion to the Treasury. These funds would be earmarked for the purchase of Development Bank obligations. In addition, the Development Bank could sell its obligations in the open market. With a maximum debt ratio amounting to twenty times the paid-in capital, the Development Bank could have a total of $20 billion in loans outstanding.

Creation of a National Development Bank along these lines is a sure way of establishing a significant measure of economic stability for those State and municipal governments which are starved for vital public works funds every time fiscal and monetary policies—as they inevitably do—become too severe in their restriction. The need to have this source of loan funds available has been agonizingly demonstrated during the past year when hundreds of millions of dollars of State and municipal bonds went unsold because market conditions no longer permitted them to remain competitive. Obligations that were marketed had to provide enormous yields. The label of public works and facilities used here is presented in its broadest meaning, running all the way from pollution control to education and health expenditures, hardly the kind of investments that should be made to carry a high interest or high yield penalty.

The same economic elements that have strangled public work expenditures also fuel arguments for the creation of a National Development Bank to provide loan funds at reasonable rates for small and medium size businesses and industries in depressed areas or in areas where there are substantial pockets of occupational unemployment. This nation cannot continue to stumble toward economic stability while sacrificing millions of jobs and hundreds of businesses and industries that have been the victims of fiscal and monetary policies.

The same things can be said of the effect of fiscal and monetary policies on housing during the past year when the rate of housing starts, 1.2 million early in 1970, made a mockery of national housing goals which call for 2.6 million new and rehabilitated housing units a year.

Devoting $1 billion to the creation of a National Development Bank to serve these purposes is a relatively small investment to make compared with the returns such loans—not grants—will make possible for our people and the nation's economy. In effect, the establishment of a National Development Bank would be a real step toward reordering our often out-of-balance priorities. Moreover, the Development Bank described here would operate in a way that would not compete with conventional lending sources since Development Bank loans would be available only to borrowers who could not obtain loans at reasonable rates from conventional lending sources. It goes without saying that the existence and effective operation of a Development Bank would serve, among other things, to prompt conventional lending institutions to provide more loan funds for socially useful purposes during tight money periods if these institutions knew there was a bank of last resort for such loans.

The need for a National Development Bank is underscored by the Administration's insistence on lifting the 4¼-percent ceiling on long-term Government obligations. Lifting this ceiling means that the Treasury, for the first time in 53 years, will be free to sell 20, 30, 40 and 50-year Government obligations at market rates. Its efforts to do so will produce two extremely costly and damaging results:

(1) The taxpayers of the nation will needlessly be saddled with debt costs on these obligations which will be at least nearly twice the interest now demanded by the market on short-term government paper. The Secretary of the Treasury has estimated that long-term obligations, freed of the 4¼-percent ceiling, would carry a yield of 6 to 6½ percent in today's market. He was saying this at the same time that short-term Treasury notes were being sold in the market at interest rates of 3.6 percent. The fact that the Administration restricted the lifting of the 4¼-percent ceiling to $10 billion in long-term government obligations amounts to nothing more than a thinly disguised effort to open the door to eventual removal of the ceiling on all long-term government obligations at enormous costs for generations of our peoples to the benefit of large commercial banks and wealthy individuals—those who provide most of the market for such obligations.

(2) Sales of long-term Government obligations at market rates will automatically place such obligations in competition with State and municipal bonds and mortgage obligations which have similar maturities. This in turn means that competition for market sales will tend to push interest rates up and at the same time diminish the opportunity of State and local governments and mortgage originators to sell readily their obligations—to say nothing of being able to sell them at reasonable rates. Furthermore, the uncertainty regarding ease of marketability of State and municipal bonds produced by this additional competition from the Federal Government will inevitably be reflected by hesitation on the part of underwriters to handle the huge volume of

such paper expected to come onto the market in the coming years. As an example, State and local governments estimate they will have to raise over $150 billion in the next half dozen years to provide social, educational, health and other public facilities that the Nation's growing population demands.

The existence of a National Development Bank under such circumstances will help to provide effective protection for those States and communities which cannot and should not have to compete for funds under these conditions.

Legislative efforts to remove the 4¼ percent ceiling on long-term Government obligations were linked to raising the national debt limit to $435 billion. In its own way this too is a needless act which could have been avoided if the Treasury would cancel the $62 billion in long-term bonds held by the Federal Reserve Open Market Committee and cease the allocation to the Federal Reserve of $4 billion a year in interest on these obligations. That the Treasury should cancel these bonds and stop paying interest on them is a matter openly admitted on numerous occasions by former Federal Reserve Board Chairman William McChesney Martin. He has repeatedly made such an admission because the bonds have been paid for and there is no valid reason to continue paying the interest. By the same token, cancellation of the bonds would reduce the national debt by $62 billion, and this in turn would have made unnecessary the Administration's move to raise the national debt limit to $435 billion.

At the very least, I urge the members of the Appropriations Committees of the House and the Senate, in particular, and all the members of Congress in general, to end the practice of appropriating funds for the payment of interest on these bonds. In this way the bonds would be placed in the category of being non-interest bearing obligations and the Federal Reserve would be compelled to come to Congress to seek operating funds. This in turn would give both Congress, since it provides such funds, and the Administration, since it disburses such funds, the leverage both need to force the Federal Reserve to coordinate its actions with national fiscal and monetary policy as these are developed by Congress and the Administration. Congress has every right to take such action since there is nothing in the Constitution, any law or even any regulation which would prevent it from doing so.

By the same token reliance on Congressional appropriations would open the way for an audit by the General Accounting Office to determine how efficiently funds provided to the Federal Reserve are utilized. All other Federal agencies are subject to the same conditions and there is no reason why this one, especially since it is meant to be the tool by which national monetary policy is implemented, should not be made to respond to the elected representatives of the people.

The ridiculousness of the situation is illustrated by the present running feud between the Administration and the Federal Reserve. On the one hand, the Administration is urging the Federal Reserve to loosen its monetary policy and pump more money into the economy in an effort to approach if not achieve a full employment economy. On the other hand, the Federal Reserve is saying that it appreciates the advice but it will nevertheless do what it wants to when it wants.

To say the least, the situation is intolerable.

WRIGHT PATMAN.

SUPPLEMENTAL VIEWS OF REPRESENTATIVE BOGGS

I commend my colleagues for the excellent and extensive hearings which they held on the subject of the nation's economy during January and February and for issuing this fine Report. Unfortunately, my duties as Majority Leader did not permit me to participate fully in the hearings and, for this reason, I don't believe that I should take a position on each and every recommendation in the report. However, I have followed closely the Administration's economic programs and must record the fact that they cause me great concern.

The absence of a responsible policy to deal with wages and prices is a major defect, in my opinion, and I am pleased to identify my views with the position taken in this report strongly urging policies to achieve price stability. As indicated in the Report, a program should be adopted at once setting up a price and incomes board which would issue guidelines setting forth acceptable rates of increase for wages and prices and which would focus the spotlight of publicity on significant wage and price decisions that are inconsistent with achieving our long-term goals of stable prices and low unemployment.

Likewise, I would like to commend my colleagues for calling attention to the unrealistic character of the Administration's projection of a $1065 billion GNP for the Fiscal Year 1972. I see nothing in the Administration's policy proposals that would serve to bring about this level of production. As a matter of fact, I feel strongly that the situation is more urgent than indicated by my colleagues and I would propose stronger measures to remedy the stagnation that has brought unemployment to an untenable level of 5,400,000 and permitted a 5½ percent inflation rate to cause wholesale disruption in our economic life.

The United States cannot afford to let the economy limp along far below its potential. The needs of our own people and the other peoples of the world are so great that economic stagnation in our great economy is a world tragedy. In 1970, we lost almost $50 billion, an amount far in excess of the GNP of many nations. This is intolerable and I am proud of the record that the House has already set in efforts to get this economy back to high employment, full production and stability. The Democratic leadership regards this as the top policy priority and I believe that the Congress must devote a major part of its efforts to meeting this objective.

We are already hard at work. The House has passed legislation to extend stand-by wage and price controls, permitting the President to put them into effect whenever he deems it necessary to curb inflation. Hearings have already been held on public service employment which, as my colleagues point out in this Report, is urgently needed to help our hard pressed communities to meet shortages of vital services in law enforcement, fire protection, medical care, education and sanitation. Other hearings are being held on public works construction for communities suffering from high unemployment. Elsewhere in the Congress hearings are being held on urgent needs of our population for housing, for health care, environmental control, employment, education, and consumer protection. We must be prepared to expand our public outlays on vitally needed services. This will serve the double function of meeting crucial needs and helping to restore our economy to full growth and high employment.

I must take this opportunity to express my grave doubts about the advisability of the President's revenue sharing proposal. Revenue sharing is, of course, not a new idea. It has been around for many, many years, and, of course, we already have approximately $30 billion of revenue sharing at the present time in the form of grants for specific purposes. The President's proposal would simply provide additional funds to the States without the Federal controls that are normally associated with the grant of such funds. As I have said before, the Administration has taken an old idea, packaged it in a new wrapper, and offered it as a specious solution to the very real problems of the State and local officials who are afflicted with falling revenues and rising costs.

A recent study conducted by the staff of the Joint Committee on Internal Revenue Taxation shows that the Administration's revenue sharing proposal would not increase assistance to the States and cities but rather would result in reduced aid in such vital areas as education, the model cities program and urban and rural community development. Indeed, the 1972 budget shows actual reductions in such items as highway safety grants, school lunches, Federal impacted aid to schools, and loans for rehabilitation of water and sewer facilities.

The revenue sharing proposal would not strengthen local and State governments, in my opinion, but would weaken them. To provide funds on a "no strings attached basis" would simply lessen governmental responsibility and work against very necessary efforts now going on at all levels of government to promote responsible and effective government. Local governments increasingly dependent on Federal revenue will become decreasingly capable of directing their own destinies and this would be a tragic turn of events in this Nation.

The House Democratic leadership has been meeting monthly with a Committee of U.S. Mayors in an effort to develop a more realistic and genuinely constructive aid program. Some of the alternatives that we are discussing and which I might add the Mayors received with enthusiasm are as follows:

1. A new proposal to discontinue the various matching fund formulas that cities are finding increasingly hard to meet as their revenues decline. The idea here is to give outright grants to cities in need, and "forgive" them on the 10, 30, and 50 percent matching funds that are now required of them. This proposal would let the cities keep desperately needed funds and allow them to put the money where local officials think it will do the most good.

2. Full funding of programs for the cities. At present, Congress authorizes programs and then, in a separate action, provides money for them. There is often as much as a 30 percent "shrinkage" in the process. Congress should work to ensure that this does not happen particularly in the case of programs for the inner city.

3. Where the President has recommended little or nothing for existing programs, Congress should see to it that sufficient funds are provided. At this moment the Administration is holding up $600 million in community development funds that can be released for the current fiscal year. The breakdown is $200 million in urban renewal funds, $200 million in water and sewer funds, and $192 million in public housing contract authority. We are urging the President to release these funds.

4. Federal takeover of welfare costs. Although this would benefit States rather than cities, we are exploring the possibility of a provision that would make it mandatory for much of these funds saved by the States to be passed on to the cities.

5. Public service employment. We have now conducted hearings and will have a bill that will help pay the salaries for firemen, policemen and other municipal workers. This will provide much needed jobs for many of our unemployed and will stop the cutback in essential municipal services. President Nixon vetoed a bill like this last year and if he does it again Congress should override his veto. In the year that has passed since that veto, the problem has become worse with no relief in sight.

6. An urban development bank. This bank would provide loans to cities on a long term, low interest basis, to finance much needed public works and housing projects. Interest rates would be under 6 percent and a borrower would have to prove he could not obtain a loan from private lending sources or at reasonable terms. So this public bank would not be competition with conventional lending institutions.

7. Accelerated public works. Hearings have been held on a $2 billion accelerated public works bill which would immediately provide these extra funds for water and sewer facilities, hospitals and other public programs, local roads and streets, etc., above funds provided through the regular grant-in-aid programs in these areas. This would attack the twin problems of environment and unemployment.

8. Several Democrats have come forward with a fine new idea for intergovernmental cooperation. This proposal would have the Internal Revenue Service collect for the States and local governments their income tax. The tax would be coordinated with the Federal tax by being either a percentage of the federally computed income or the tax. This suggestion would allow the most effective and efficient tax gathering agency in the world (.004 of 1 percent collection costs) to collect the State and local tax and immediately pay it over. Not only would this greatly increase collections—variously estimated at about $1 billion—but it would eliminate the costs of collection incurred by the States of almost $200 million. At the same time, the plan would reduce the complexity of return filing for our citizens and business since the State and local returns would be eliminated and replaced by only one extra line on the Federal return.

This plan would not impinge on any States sovereignty as each would levy the tax at its own rate. I fear greatly that revenue sharing as proposed by the Administration cannot make this claim. It will only be a short time before the States are devoid of revenue potential and completely dependent on the Federal revenue sharing—at that time Federal controls may eliminate State government as real forces.

Hale Boggs.

SUPPLEMENTAL VIEWS OF REPRESENTATIVE REUSS ON MONETARY POLICY

In my supplementary views on the 1968 Joint Economic Committee report (pp. 44–46), I pointed out how widely the Federal Reserve System was disregarding the admonition of the Joint Economic Committee in its 1967 report to stay within a normal rate of growth of the money supply, narrowly defined (the formulation in recent reports of the Joint Economic Committee, including this 1971 report, sets a desirable rate of growth in the money supply narrowly defined, at 2–6 percent). I also said: "Perhaps the Joint Economic Committee's 'advice' has been too tersely stated, with insufficient regard for other factors than the money supply, narrowly defined."

I then proposed a more comprehensive set of guidelines—a general principle, and seven qualifications. During the hearings of the Joint Economic Committee on July 23, 1970, I had an opportunity to question Chairman Burns of the Federal Reserve System on these proposed guidelines. (Hearings, pp. 596–600). Dr. Burns thereafter supplemented his testimony by additional material, which is included in the printed hearings.

As a result, I am prepared to suggest guidelines which emerge from my questions and Dr. Burns' reaction to them. It seems to me that until improvements come along, these guidelines would be sensible advice for the Joint Economic Committee to give the Fed, rather than the present simplistic "Keep the money supply, narrowly defined, in the range of 2–6 percent growth per year."

The suggested guidelines follow:

> The Federal Reserve System, through open-market operations, reserve requirements, and discount policy, shall endeavor to accommodate a growing full-employment gross national product by expanding the money supply (narrowly defined to include commercial bank demand deposits and currency outside banks) by 2–6 percent yearly, with the following qualifications:
>
> 1. The target figure should be adjusted up or down from the above band from time to time to reflect the extent to which time deposits in commercial banks, and in savings and loan institutions, mutual savings banks, and credit unions, substitute for the narrowly defined money supply.
>
> 2. The target figure should be on the higher side of the band in periods of less than full use of resources, on the lower side in periods of full use of resources. This qualification is subject to the further qualification that the lag between monetary actions and their effects on output and prices, and information about the recent behavior of prices, economic activity, and the course of fiscal policy, must be carefully considered. If the recent past has been dominated by excess demand and substantial inflation, an attempt to

reach full use of resources in the short-run through accelerated monetary growth could sacrifice the prospects for noninflationary growth over the longer run. Under such circumstances, if the economy were operating somewhat below its potential, but moving upwards, a rate of money stock growth that was too high might risk overstimulating the economy. On the other hand, when the economy is relatively free from inflationary pressures, and fiscal policy is restrictive, a relatively expansionary monetary policy may be needed to maintain full resource use.

3. The target figure should be on the higher side of the band, or even higher than the band, when resources are underemployed, and simultaneously businesses are making exceptionally heavy demands on credit, not for current business expenditures, but for additional liquidity in anticipation of future needs, or to replenish unexpected liquidity losses. It must be recognized, however, that additions to money holdings to satisfy present liquidity preference would prove to be a source of funds to finance inflationary demands later on, should the preference for liquidity decline.

4. In general, cost-push inflation should be attacked by a moderate rate of growth in the money stock, a sound fiscal policy, and a wage-price-incomes policy. An effort to offset, through monetary restraint, all of the upward push that rising costs exert on prices may unduly restrict aggregate demand, and increase greatly the risk of substantial under-employed resources. On the other hand, expanding the growth rate of the money stock by the amount of inflation attributable to the pressure of costs on prices would provide the potential for an unending round of price and wage increases.

5. The target figure should generally be sought over a three-month period. But a longer period than three months may occasionally be needed to average out the targeted rate of growth in the money supply, depending on the current and immediately prospective state of the economy and of financial markets, the size of Treasury borrowings, the management of the Treasury balance, and the source of short-run variations in private money demands.

6. The proper use of monetary policy to avoid domestic inflation, as outlined above, is equally necessary from the balance of payments standpoint—the effect of price inflation on the country's international transactions in goods and services, and the vital role of the dollar as an international reserve currency.

From the point of view of international capital flows, balance of payments considerations should affect monetary policy only through varying the maturity of the Federal Reserve System's portfolio so as to achieve to the extent possible appropriate interest differentials as between long-term and short-term securities. It should be noted that differentials between short- and long-term yields in any one country are less directly relevant than are differentials between levels of both short- and long-term yields in one country and those in another. For a country experiencing persistent balance of payments difficulties, adverse differentials in long-term yields may assume considerable importance, though their effects may be offset by devices such as the Interest Equalization Tax. With respect to short-term interest rates, large changes and yield differentials may also be undesirable, because they may induce large flows of short-term investment funds. On the other hand, adverse yield relationships and adverse flows of funds may at times be unavoidable, and if they appear likely to be self-limiting, they need not be a cause of special concern,

7. The consequences of monetary policy for the home-building industry should be taken into account by including Federal National Mortgage Association and Federal Home Loan Bank Board securities in the Federal Reserve System's portfolio in meaningful amounts, and by lengthening its portfolio whenever home-building finance is unduly retarded by overall monetary stringency.

I hope that the Joint Economic Committee will carefully scrutinize monetary policy over the period ahead, with particular reference to the above-proposed guidelines. I am afraid that the Administration will not get the expansive monetary policy on which it is apparently depending in order to achieve its targets, assuming that the Federal Reserve System follows the above guidelines. It is up to the Administration, in my judgment, either to tell the Federal Reserve System and the Joint Economic Committee wherein it believes the above guidelines are too restrictive, or to propose additional fiscal and other policies which will achieve its goals with a monetary policy operating according to the above guidelines.

HENRY S. REUSS.

SUPPLEMENTAL VIEWS OF SENATOR HUMPHREY

With respect to transportation policy, Senator Humphrey states:

I see no need, at this time, to recommend phase-out of the Highway Trust Fund. Any consideration to dissolve or completely redirect the Fund should await completion of the presently planned highway system. If there is to be serious consideration, in the future, to redirect the Fund, then I would hope the Committee would make at least some tentative recommendations of economically and socially feasible alternative goals.

Language in the report recommending user charges on inland waterways needs more specific definition. Legislation regularly comes up calling for a combination of fuel tax and lockage charges. Since these bills regularly receive no consideration, I find it difficult to accept Committee language without more specific recommendations on the various user charge alternatives.

The Federal Government, to date, has supplied 90 percent of the financing for SST prototype design and construction. I suggest that alternative financing arrangements be made to continue work on the prototype, using Federal guarantees. After completion of the prototypes and their testing, then financing for production should come directly from commercial sources. This will then place the decisions for SST economic viability, as a system, where they belong—in bank and corporate board rooms.

I believe this presents a reasonable alternative that costs the Government no further SST funding, presents private financing with the opportunity to participate in the project, eliminates payment of termination costs, and still gives the proponents of the SST time in which to perfect the aircraft, eliminate, as far as possible, the environmental threats posed by the SST, and prove the economic viability of the venture through selling the system and securing production financing in the marketplace.

With respect to foreign assistance, Senator Humphrey states:

The material contribution of the U.S. to the developing nations is far below the 1 percent recommended by UNCTAD. Our foreign aid has dropped to a new post-war low. It will be increasingly difficult to understand and explain this as other developed nations continue to surpass the U.S. in the aid they are extending to the developing countries.

We must substantially increase our commitments to the development of those parts of the globe that still serve as festering points for a violence bred of despair. This economic imbalance is made all the more painful by the increasing awareness by the deprived of western and northern affluence.

Our assistance must be channeled primarily through multilateral institutions. This will place the responsibility and a peaceful-power focus on the United Nations, the World Bank, Inter-American Bank, Asian Development Bank and the International Development Association. We must bolster these organizations and not merely use them as reflectors of power initiatives we take in the regular conduct of our own foreign affairs. We must realize that substantial foreign aid is still in our own economic as well as idealistic self-interest. As Pope Paul has said, "Development is the new name for peace."

HUBERT H. HUMPHREY.

SUPPLEMENTAL VIEWS OF SENATOR BENTSEN

While I am in substantial agreement with many of the conclusions reached in the Committee Report, there are others about which I have serious differences of opinion.

In the section on Transportation, for example, the Committee contends that the Administration should withdraw its support for the SST and should phase out the Highway Trust Fund. I cannot agree with either contention.

The principal problem with the SST, as I see it, is one of timing. The SST would involve a new generation of aircraft at a time when the airlines are in difficult financial straits and cancelling many of their options on current models. They certainly will not be able to finance, for some time, new aircraft at prices that will approach $40 million a copy.

In due time an answer will be found to the sonic boom, and the airlines will have solved their financial problems. Then we will be able to produce a more economical model of the SST which can win back the market that other nations may have acquired in the supersonic field just as surely as we recaptured the market from the British Comet and the Caravelle.

In summary. I believe an SST can and should be built in due time, and that the appropriations for research and development should proceed over a longer and more studied pace in order that we might have more time to solve the technological and economic problems facing this new generation of aircraft. The taxpayers, under such an approach, would have greater assurance of recouping a very major investment.

The Highway Trust Fund offers another problem. It was established in 1956 for the sole purpose of building highways. and it should continue to be used for that purpose. The motor vehicle users of the country, who pay taxes dedicated to highway construction, have every right to expect that the federal government will use the funds for the purpose specified.

The Highway Trust Fund facilitates long-range planning, which is essential to any program of highway construction, and it would be manifestly unwise to terminate it. The original goals set for interstate highway construction have not been met, nor are they likely to be met if the Executive impounds highway money or the Congress refuses to take positive action to extend the Highway Trust Fund.

I recognize the need for a balanced transportation system, but I am also aware that our basic highway needs must be met if we are to handle the increasing burden of automobile traffic over the next several years.

In the section on Defense and National Security, the Report concludes that "In the interests of national security, defense spending should be reduced in fiscal year 1971 substantially below the estimated outlays for fiscal 1971." It goes on to suggest that this should be done "through reform of weapons procurement to eliminate the unnecessary cost overruns, gold-plating, and waste that pervade the procurement system, ..."

No one will argue with the latter statement that waste in military spending should be eliminated; that is a truism with which we can all agree. Indeed, waste in all government spending programs should be eliminated. But it is quite another matter to state categorically that defense spending should be cut to levels "substantially below" the levels for fiscal 1971.

I have been unable to locate materials in the Committee Report or in the testimony of various witnesses which would compel me to such a conclusion.

How substantial is substantial? What world conditions justify a major cut in defense spending? The Committee Report points to winding down of the war in Southeast Asia, but it fails to take into account the fact that defense spending has already been reduced substantially over the last two fiscal years, reflecting the slowing of the Indochina war.

I regret as much as any member of the Committee the conditions that create the necessity for large defense expenditures. I regret that the Soviet Union has moved into the Middle East; I regret that the Chinese are posing an increasing technological threat with new satellites and the continued development of nuclear weapons; I regret the development of new Soviet missiles, larger than the SS–9.

But while I regret these developments, I cannot ignore them. Our defense posture must remain strong enough to deter any potential enemies. That is an unhappy fact of life, which I am forced to live with, and I cannot be convinced to support glib pronouncements about the need to cut our military spending. The issues are too critical for me to adhere to that position.

Despite these reservations, I am in agreement with many sections of the Report, which pinpoint the major shortcomings of our present economic policies and suggest a number of constructive remedies to meet them.

LLOYD M. BENTSEN, JR.

MINORITY VIEWS

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1971

ECONOMIC REPORT OF THE PRESIDENT

NOTE.—These minority views are not directly responsive to the issues and recommendations included in the committee report. The extremely tight schedule prescribed by law does not provide sufficient time for the minority members to receive and analyze the report written by the majority, and then develop views based upon it. Consequently, as has been true in recent years, the two reports have been developed concurrently, and the minority's views are independently based upon the 1971 President's Economic Report, other messages and this committee's hearings. The statement of agreement contained at the beginning of this volume notes areas where the two reports reach similar conclusions, and the careful reader should be able to distinguish the points of disagreement between the committee and minority reports.

CONTENTS

THE ADMINISTRATION'S ECONOMIC POLICIES AT MID-TERM

Today's economic problem is to regain full employment while continuing to reduce inflation. It is a problem for the nation as a whole and not solely a task for the Administration. No segment of the economy or the body politic can afford to take the attitude of spectators watching the Administration struggle with the economic problem, while remaining neutral with regard to proposed solutions to the problem, or even the root of the problem. Much of what needs to be done to move the economy along the difficult path ahead will be politically unpopular, or at least not well understood, in the short run. We in the Congress have a responsibility not to exploit that fact, not to mislead the American people, and not to spread confusion and anxiety. It is our responsibility to support the Administration in necessary measures and to propose constructive alternatives when we think we can do so.

Our present situation, in which we confront both too much inflation and too much unemployment, had its origins at least as far back as the middle of 1965. Greatly increased Federal expenditures for the Vietnam War were added on top of rapidly rising expenditures for new domestic programs, but no decision was made to cut down other programs or to raise taxes in order to finance these rising Federal costs or to restrain private spending. The Federal budget deficit was allowed to rise from $1.6 billion in fiscal year 1965 to $25 billion in fiscal year 1968. Partly because of the large deficit, the rate of increase of the money supply also spurted up, from an increase of 3.0 percent in the first quarter of 1965 to a rate of 9.5 percent in the second quarter of 1968. The combined effect of the rising budget deficit and the rapid monetary expansion during a period of relatively full employment was the inflation from which we are still suffering.

Until about the Fall of 1966 the Administration tried to curb the inflation by a policy of wage-price guideposts of 3.2 percent per annum, backed up by jawboning, private arm-twisting and public threats. This did little to restrain wage and price increases once inflationary pressures began to assert themselves and was abandoned as a general policy after the guideposts had been conspicuously flouted in wage decisions.

The inflationary "Guns and Butter" boom carried with it a reduction of the unemployment rate to an unusually low level. But it did not create the conditions for keeping unemployment low. We were having a typical, temporary, unsustainable, war economy, inflationary bubble.

Employers were willing to hire additional workers because of anticipation that they could sell their product at even higher prices in the future. Workers accepted wage increases that appeared to be generous but soon discovered that such increases were consumed by the fires of inflation. The bubble would burst either when the wartime spending terminated or resistance to the inflation set in. Experience has proved that when the bubble of inflation bursts, a nation's economy does not just return to normal but falls below normal.

The Government finally initiated steps to try to check the inflation in the latter part of 1968 by imposing a tax surcharge, setting a ceiling on Federal spending and by curtailing monetary expansion. However, the major burden of bringing the inflation under control fell to the Nixon Administration and to the Federal Reserve during the Nixon Administration. The difficulty of this task was commonly underestimated at the beginning of 1969. One evidence of this was the last report of President Johnson's Council of Economic Advisers, which gave the impression that after a brief and shallow decline of the economy in early 1969 we would quickly regain full employment with a much-reduced rate of inflation. But there was no doubt that the continuing speed-up of the inflation had become intolerable, and no one has come forward to deny that the difficulties of dampening inflation, whatever they might be, had to be accepted.

The Administration's strategy called for two stages in the fight against inflation. First, demand pressures would be reduced enough to create moderate slack in the economy and thus reduce inflationary pressures. Second, the growth of demand would be speeded up, but not so fast as to reinvigorate the inflation, so that the decline of the economy would end and a revival occur.

Policy to produce the first stage was carried out in 1969. A tight lid was kept on Federal spending; the tax surcharge was extended beyond its original termination date of June 30, 1969, reduced to 5 percent on January 1, 1970, and expired on July 1, 1970. As a result of the reduction in Federal spending, together with growth factors in the tax base, there was a major fiscal shift from a $25 billion deficit in FY 1968 to a balanced budget, on average for FY's 1969–1970. Also the annual rate of growth of the money supply was drastically reduced from 7.8 percent in 1968 to 3.1 percent during 1969.

These policy measures and some spontaneous forces as well led to a slow-down in the rate of economic growth beginning in the Fall of 1969 but the slow-down was still quite small by the opening of 1970. To keep the slow-down moderate, the Administration proposed at the beginning of 1970 a turn of policy in a more expansive or less restrictive direction. The policy of severe budgetary restraint, a swing from a $25 billion deficit in FY 1968 to an approximate balance, gave way to a policy of neutrality expressed by keeping the budget in approximate balance. Moreover, the Administration suggested that the money stock should expand significantly faster in 1970 than in 1969.

The Administration set forth a target for 1970 of a gross national product of $980-990 billion which it said would be reached if appropriate policy were followed. In fact, the GNP for the year turned out to be $977 billion, or eight-tenths of one percent below the mid-point of the Administration's forecast. This is much smaller than the average error of the forecasts made in the years 1962–1969, which averaged 1.15 percent.

Nevertheless, both unemployment and inflation turned out to be greater than had been forecast. The average unemployment rate for the year was 4.9 percent as against the Administration's forecast of 4.3 percent, and in December the figure reached 6.2 percent—although it has since receded to 5.8 percent. Consumer prices rose 5.3 percent from 1970 to 1971, compared to a forecast increase of 4.4 percent.

The momentum of the inflation generated by the 1965–68 boom also turned out to be much stronger than had been expected. Continuing inflation created psychological pressures which resisted economic adjustments. Inflationary psychology had carried the economy to a point where productivity gains stopped. The result, on the one hand, was lower profit margins and, on the other hand, many workers getting no real wage increases or an actual loss in real wages in spite of increases in wages. As a consequence, during 1970 there existed strong pressure for catch-up wage increases and restoration of profit margins. The unrelenting push of wages and prices resulted in the rise of the GNP as projected, but it was totally the result of inflation. There was less real dollar output, slightly less employment and more unemployment. The most significant single cause of higher employment loss during the year was the reduction of 1.1 million jobs in defense and space programs including the reduction in the armed services, combined with the prolonged strike in the automobile industry.

As the overall economy reacted to the restrictive fiscal and monetary policies of 1969, both fiscal and monetary policies became less restrictive and then increasingly expansionary during 1970. There was a considerable relaxation of fiscal policy, although the policy change is exaggerated by contrasting the $1.3 billion surplus first estimated for FY 1971 with the present estimate of an $18.6 billion deficit. Much of that difference is the result of differences between estimates and actual results on the revenue side of the accounts as a result of the shortfall of profits below earlier projections. This automatic decline of revenues tended to cushion the economic decline, but it did not reflect policy. Expenditures increased $12 billion above the initial estimate of government spending, much of this being due to higher prices and wages paid by the Government, but more than one quarter due to Congressionally-mandated spending increases. It is of interest that the majority of the JEC a year ago recommended a full employment surplus of $8 to $10 billion in the national income accounts for FY 1971. The present estimate is that the full employment surplus on that basis will be about $7 billion. By that measure, present policy is more expansive than the Committee majority recommended.

There is no official statement from the Federal Reserve of the rate of monetary expansion it initially planned for 1970. Still we think it fair to say that few expected a rise as high as the 5.4 percent rise that occurred from December 1969 to December 1970.

This greater-than-planned expansiveness of fiscal and monetary policy during the year helped to keep the GNP rising. The continuing stubborn rise of wages and prices led the Administration to several measures not included in the plans at the beginning of the year. Two of these were very similar to measures recommended in our Minority Views last year. One is the system of Inflation Alerts issued periodically by the Council of Economic Advisers to call attention to exceptionally inflationary wage and price decisions. The second is the work of the Purchasing and Regulations Review Board, which seeks to correct or prevent specific government actions which may have an exceptionally inflationary effect. In addition, the President established a National Commission on Productivity which brings together leaders of the private sector and the government to work on some of the central economic policy issues of our time.

What can be said in retrospect about the economy in 1970?

The most important thing to say is this: in spite of the cut in defense employment by over one million, a long strike in the nation's largest industrial corporation, the anxieties generated from time to time by the international situation, and also the political effort this year to spread fear about the economy for political advantage—given all these things the Administration successfully accomplished its goal of establishing the conditions for noninflationary growth at full employment. This is a tribute to the strength of the economy and to the prudence and flexibility of policy.

Still, it is necessary to ask whether better results could have been obtained with other policies. This involves two questions. One is whether the overall behavior of the economy would have been better if the fiscal and monetary policy had been different. Should we have had a bigger budget deficit and more monetary expansion in order to get the economy rising more rapidly, or should we have had more fiscal and monetary restraint in order to check the inflation more quickly? The fact that the question is two-sided is testimony of the difficulty involved. The evidence presented before this Committee does not point clearly in either direction. In fact, in presentations to us, the fiscal and monetary policies of 1970, and the course of the year's total GNP, were not regarded as major problems. This does not mean that nothing better could have been done. But even with the benefit of hindsight, it is hard to suggest what steps would have been preferable—and even harder to assess what the results of different measures would have been.[1]

On the issue of wage and price policy in 1970 there is a wide range of differing opinions. A current topic of debate involves the question of whether more direct intervention by the government, possibly including general wage and price controls, would have been helpful in deterring inflation. Wage and price controls have a superficial appeal—until they are imposed. Many have criticized the President for failure to impose wage and price controls. However, a true measure of political-economic sentiment was demonstrated when the House of Representatives had an opportunity to vote to impose such controls by its own action but refused to do so by a vote of 270 to 11 on July 31, 1970.

One common suggestion is that the Government should have an "incomes policy."

The most frequently cited example of incomes policy today is a "Wage-Price Review Board." This a board of private citizens that

[1] Senator Percy feels that one policy action that could have been taken in 1970 to stimulate the economy would have been continuation of the 7% investment tax credit. The Minority of this Committee, which included Senator Percy, predicted in the 1970 Annual Report that repeal of the investment tax credit "can be expected to dampen economic growth significantly in the 1970s." That did occur in 1970. Senator Percy believes the investment tax credit should be reinstated on a permanent basis to help business purchase capital equipment, increase productivity, reduce unit costs, dampen inflation and to reinvigorate economic growth.

would decide when actual or proposed wage or price increases were too big and take some unspecified steps to discourage such increases. The wage-price review board is one of a large family of "voluntary control" systems.[2]

Policies for 1971

As we write this in March, the unemployment rate which had reached 6.2 percent in December has declined to 5.8 percent in February. Evidence continues to accumulate that the inflation rate is subsiding. There seems to be little doubt that economic activity is rising. Still, both the unemployment rate and the inflation rate are too high, and while a further increase in economic activity is highly probable, a rise at an adequate rate is not assured. There are, as we see it, two main policy problems confronting us:

1. What is the desirable path for economic growth in 1971 and 1972?
2. What fiscal and monetary policies are needed to move the economy along that path?

The Desirable Path

Our fundamental objective should be to raise real production and reduce unemployment as fast as can be done while continuing to make progress against inflation. Stating the goal in this way implies a choice. We do not want to stimulate the economy at the price of spiraling inflation. At the same time we do not want to delay expansion of the economy until all of the inflation has been wrung out of it. We should give high priority to reducing unemployment.

This is, we believe, the same balance of emphasis that is represented in the Economic Report. The President goes further than he is required to do by the Employment Act of 1946 and assigns numbers to these general objectives. He sets as a target getting the unemployment rate down to about 4.5 percent by mid-1972 and the inflation rate down to about 3 percent by the same time. He suggests that if the gross national product were to be $1065 billion in 1971, the economy would be moving along a path to those objectives.

The basic goal should be, as we stated earlier, the fastest reduction of unemployment consistent with progress against inflation. The $1065 billion GNP is a proper goal only as long as it is a way to getting the basic goal, and should not be regarded as additional to or competitive with the basic goal. As we listened to witnesses we have been impressed with the great uncertainty about the amount of unemployment and inflation there would be if the 1971 GNP were $1065 billion.

We do not think it is impossible or improbable that if the $1065 billion GNP were achieved the economy would move to the unemployment and inflation goals desired. We commend the President for setting ambitious goals, as the Employment Act requires him to do. We do not recommend that the $1065 billion goal be reduced at this

[2] Senator Javits supports the establishment of a wage-price review board. See Additional Views of Senator Jacob K. Javits, p. 137.

time. However, as we view the opinions expressed in the Committee's hearings, it seems that if the GNP goal has to be changed, it is more likely to require reduction than increase. For example, the Administration should be prepared to reduce the goal if the economy in the first part of the year seems to be running below the level implied by an annual goal of $1065 billion, because to achieve the goal for the year could require too sharp a rise thereafter. But in such an event, the Administration should promptly report its findings to Congress; Congress should also be promptly informed of any substantial changes in the stance of the Budget.

Fiscal Policy to Reach the Goal

The Administration proposes to achieve its GNP goal for 1971 by the combination of a budget which would be balanced if the economy were operating at full employment (but which will actually have large deficits in FY 1971 and FY 1972) and a "complementary" monetary policy.

The idea of looking at the budget as it would be at full employment is not new, but previously it has not been identified so explicitly as a guide to policy. We welcome this public emphasis on balancing the budget at full employment. We welcome it as an attempt to introduce a discipline into the budgetary process that has been lacking for many years. Obviously, we are not going to balance the actual budget under present conditions. In fact, political processes could make the FY 1972 deficit larger. Some economic standard, other than everyone's guess about the needs of the economy, which will set some limits to this political process, is needed. The standard that, except in emergencies, expenditures should not exceed the revenues that would be collected under conditions of full employment seems a reasonable one. It permits short-run adaptation to economic conditions while preserving a certain discipline over the longer-run growth of expenditures.

With the experience gained from the Administration's initiative, future budgets will be in a position to refine the full employment budget concept until it becomes a thoroughly practical tool for policy analysis. We note, for example, that the projected $0.1 billion full-employment surplus in the budget document has been computed on the basis of the unified budget rather than on a National Income Account basis; economists generally agree that the latter reflects more accurately the fiscal effects of the budget, a point which the CEA itself notes in its annual report. Moreover, other factors, such as changes in the budget surplus from year to year plus the mix of the budget among expenditures having different economic impacts, figure prominently in an analysis whether a particular budget is restrictive or expansionary. In this regard we find the CEA's discussion of the full employment budget very instructive.

Many witnesses have suggested that a more stimulative budget, with a large deficit even at full employment, is required to achieve adequate expansion. We are concerned about such suggestions because we fear that they would lead us again to a condition where the deficit would be highly inflationary. There may be situations in which a deficit at high employment is desirable for the economy. However, we should come to that conclusion reluctantly and only on the basis of stronger evidence that we now see before us.

Monetary Policy

A share of the burden of moving the economy along the desired path will, of course, rest on monetary policy. The testimony before us, including that of the Federal Reserve, suggests that this will require a relatively rapid expansion of money and credit. Just how rapid is the question on which the experts differ and one which we cannot precisely resolve. We do think it important to express our view that the over-all goal should be ambitious, and that unless there are stronger reasons than now appear we should not aim for a more expansionary fiscal policy than is now planned. Beyond that we must rely heavily on the judgment of the Federal Reserve, operating in close consultation with the Administration and reporting regularly to the Congress, to follow a sufficiently flexible course to stimulate growth toward the hoped-for goal without rekindling inflation and sacrificing real growth to the specific total figure goal.

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WELFARE REFORM AND MANPOWER PROGRAMS

WELFARE REFORM [1]

The basic plan under which the welfare system in this country distributes benefits to the poor is that which was introduced in the Depression, at a time when approximately one-third of our nation's population was considered poor and needful of assistance. This emergency plan has never been adequately revised, although amendments to it have been made piecemeal. As a result, our welfare system is grossly inequitable in many respects. The Administration's proposed Family Assistance Plan is the first comprehensive welfare reform program presented to Congress by a President since widespread public assistance was introduced a generation ago.

As a rule, the "working poor" usually qualify for very few benefits under welfare. Persons receiving welfare are discouraged from earning income because welfare benefits generally are sharply reduced as earned income rises. The system thus serves to perpetuate high costs and low efficiency. Benefits to identical families on welfare vary a great deal from state to state and locality to locality. These are but a few of the inequities. Additionally, because of the way in which our welfare system has been administered, we find that the poor are assisted in a manner which is highly destructive of initiative and self-respect, especially as to those aspects regarding eligibility certification, and is horribly expensive and wasteful. On top of all this, the welfare system, even with its extremely high cost, is not able to provide a decent existence for those supposedly benefiting from it.

In 1969, approximately 24.3 million persons in the United States were classified as poor, that is, were living in families with incomes below the federal poverty threshold. Of this number, approximately 10.4 million people were receiving some form of public assistance. A rough categorization of poor persons in this country is informative. In 1969, approximately 9.8 million poor persons were children under the age of 18. This constituted in excess of 40 percent of all poor persons and 14.1 percent of all children under the age of 18; 44.6 percent of these children lived in female-headed families, 55.4 percent in male-headed families. The elderly poor, those aged 65 and up, numbered 4.8 million in 1969, which constituted approximately 20 percent of all poor and 25 percent of all aged persons. Approximately one person in every eight in the United States is poor.

Even from this rough breakdown, certain important conclusions can be drawn. First, there are large numbers of poor persons in addition to the disabled who cannot be expected to raise their standards of living by working; namely, the elderly and children under 18 years of age. Therefore, the basic income support level is of paramount importance to these people. Work incentive provisions are of only secondary interest to most of them. Second, given the large number of poor persons

[1] Representative Blackburn does not wish to be associated with the minority views on welfare reform.

who cannot contribute to their own support and the large total number of poor persons, it is apparent that any welfare system which is to be effective at other than astronomical cost must provide strong work incentives and be accompanied by work opportunities for those poor persons who *are* in a position to contribute to their own support. **We believe that welfare reform must contain as a major element a comprehensive program for job training and job opportunities for the poor. Aside from the social basis of public assistance, the economic justification for a welfare system is the belief that such a system aids recipients of assistance in moving out of poverty and becoming productive members of our society.**

Certain goals are basic to a reformed welfare system. Our most important objective ultimately must be to see that no person is forced to live on an income below the poverty level. Indeed, we must remember that income at the poverty level provides only bare subsistence and that our nation can never be content while any of its citizens are living at such a level. A reformed system should also include comparable benefits, taking into account differences in living costs, everywhere in the country. We believe that an equitable program of assistance to the poor should not discriminate between the working and non-working poor, nor should it discriminate between families with children on the one hand and single persons and childless couples on the other hand. Poor persons who have no children or who are single suffer no less from the effects of living in poverty. And, as we have stated, any reformed system of welfare must maximize each poor person's opportunity to improve his own economic position, namely, each person must have an opportunity to receive training for jobs which offer the potential for self-fulfillment and advancement.

As we have stated, in achieving these goals adequate manpower training and job programs will be vital. We realize that the scope of the manpower problem is vast. In 1968, a federal manpower training task force estimated the number of persons for whom training is essential in order to escape poverty at 11 million. However, although the problem of welfare reform and employment provision is immense, we must solve it if we are to escape the incalculable economic loss of productive resources that the present and future generations of persons trapped in poverty represent.

Surveys have shown that most welfare recipients and other poor persons are as desirous of having meaningful employment and have the same aspirations for themselves and their families as the rest of our population. Therefore, **we believe that a vital element of any welfare reform should be adequate federal support of child care centers. These would enable mothers to participate in job training and to take jobs to supplement their family incomes.** Also, child care centers could provide cultural opportunities to deprived preschoolers which would better prepare them to start school.

The disadvantaged child often starts school with but a fraction of the verbal and other skills of the middle class child and never recovers from this initial disadvantage during his school life. Although our schools may be deficient in many respects, they are certainly made less effective in dealing with deprived children because of the many handicaps with which these children begin the educational race.

Without exaggeration, a child sent to school at the age of six with insufficient skills is really the beginning of the next generation of poor people in this country and the economic losses which poverty entails. **The economic consequences of this state of affairs, although immeasurable, are obvious.** Therefore, it is imperative that any system **of child care centers should do more than provide depositories for** children. These centers should provide meaningful educational and cultural experiences for children so that the centers may play an effective role in ending the cycle of poverty. Obviously, development of such a system of child care centers is a complex, expensive proposition. It is very important that it be developed in coordination with welfare reform and manpower training and job programs so that the child care center program will have an opportunity to develop experience in time to handle adequately the large number of participants who will hopefully appear as meaningful welfare reform and manpower training and job programs take effect. Finally, the child care centers themselves could provide an important source of satisfying employment for a number of mothers and other persons now on the welfare rolls.

We urge consideration of the various means suggested, including certification of eligibility by affidavit and supporting documentation, to reduce the costs of administering our welfare programs.[2] Additionally, we recommend that adequate counseling services concerning family planning be made available to all welfare recipients, in order that family planning information may be as available to the poor as it now is to the rest of our nation. Such family planning services have the potential to make great contributions in reducing poverty, as shown by the fact that in 1968, 44 percent of all poor children were in families with five or more children.

We firmly believe that only with comprehensive welfare reform, including adequate work incentives and opportunities, can the paradox of great want for many in the midst of great wealth be ended.

Manpower Training and Development [3]

Our present manpower training and development problem has several important aspects. We must be concerned with providing training and jobs for the "hardcore unemployed," who are out of work in both good times and bad. Many of these persons live in poverty and subsist in large part on public assistance. We must also be concerned with assisting those marginal workers who are generally the "last hired and first fired." These people are usually the first ones out of work during periods of economic slowdown; the instability of their jobs contributes to general economic instability. A third somewhat different manpower problem facing us at present concerns redirecting many highly skilled persons who have been left unemployed as a consequence of military

[2] Senator Miller points out that the Senate Finance Committee, which has jurisdiction over legislation on this point and of which he is a member, has strongly expressed its view that the matter of self-certification should be made optional with the respective states, and many governors have indicated that they will exercise their option to discontinue self-certification—except in the case of old age, blind, and disabled recipients.

[3] Senator Jacob K. Javits strongly supports the immediate creation of a Federally-funded public sector jobs program, a recommendation which this section fails to make. See the additional views of Senator Javits on page 137.

spending cutbacks. These persons represent not only the waste of a large investment but also the loss of a substantial amount of productive power.

A solution to our manpower problems is vital to more than a narrow concern such as the welfare costs of unemployment and poverty. If this nation is to have a work force in the 1970's adequate to the rapidly expanding manpower needs in such fields as health, services, housing and state and local government, sound manpower training programs must be expanded immediately. These programs must be concerned with meeting the demands of both our urban disadvantaged and the isolated rural poor. Additionally, manpower training must be aimed at more than "entry level" jobs. It must provide skills which will give trainees opportunities for advancement and job mobility.

Our manpower programs must give special attention to certain unemployed groups. For example, unemployment among our young, which generally runs at a high level, is a serious concern. Continued unemployment of a young person destroys his initiative and helps to foster a feeling that employment cannot be looked to as a source of fulfillment. This feeling helps to create a potentially lifetime-unemployed person. Additionally, **we must take care that our manpower programs include all necessary provisions to eliminate present racial, sex, and other discriminatory barriers to employment.** This country cannot afford the great economic losses which continuation of such barriers represents. **We further believe that careful consideration should be given to the opportunities for instituting meaningful training programs in many of our penal institutions.** The large number of persons in our jails and prisons represent a great untapped source of manpower. Many inmates have ended up in prison because they lack marketable skills and have therefore turned to crime as an alternative to employment. Repeat offenders are so numerous and the cost of their crimes to society so high that meaningful educational and training efforts would be well worth the trouble and expense. We must ensure that inmates have opportunities to develop other than criminal skills while they are imprisoned. At present our system of prisons is little more than a system of finishing schools for crime. In addition to providing training to inmates, emphasis must be placed on job placement upon release if we are to derive benefits from an extensive training program.

The Manpower Development and Training Act of 1962, the Economic Opportunity Act of 1964, and other manpower legislation created a number of both institutional and job-related training programs. As a general matter we prefer, where possible, on-the-job training because it provides the incentive of having a real job, exposes the trainee to actual working conditions, and takes place in the absence of the classroom atmosphere which either antagonizes or intimidates so many disadvantaged persons. However, we recognize that institutional training can serve certain needs which are not handled well by on-the-job training. These needs include preparing people deficient in such basic skills as reading and writing, upgrading certain worker skills, and providing training in skills of interest to firms unequipped to provide on-the-job training. **We support President Nixon's initiative to strengthen necessary state and local governmental participation in manpower programs (provided state and local**

governments discharge their requirements according to federal criteria), to reduce the large number of federal programs and simplify the requirements for participating in such programs, and to encourage the private sector to engage in manpower training and provision of job opportunities to the disadvantaged. We believe that simplification of programs combined with adequate financial incentives could greatly increase private participation in the manpower field.

One such financial incentive to the private sector could be a system of tax credits in connection with private job training. These credits could be made available to companies which take on new workers for training and employment.[4] Attention should be given to encouraging private firms to provide teachers, material, equipment, etc., at institutional training centers.[5]

Another aspect of manpower programs which must be carefully considered is the need to encourage research concerning increasing production in low-paying jobs in order that wages paid on such jobs may rise without contributing to inflation. Many jobs could undoubtedly be re-classified to include more challenging duties which would merit higher pay. A number of more professional jobs could be re-cast to move some duties downward to lower level jobs. One field in which this approach has been widely suggested is that of health, in which many functions now performed by highly trained doctors, nurses and other medical personnel could be performed by skilled para-professionals. The need to upgrade secondary jobs is of great importance. These jobs have a stifling effect on the poor and on work incentives because of such factors as low pay, job instability, low probability of advancement, bad working conditions, etc. These factors all contribute to high job turnover, absenteeism, tardiness, and unemployment. Many of these jobs are so ill-paid that they are not significantly more attractive than subsisting on public assistance.

One method of placing more people in jobs with potential for advancement would be the development of better job information services. In this connection, the Administration has taken important action in greatly expanding the Job Bank Program in the Department of Labor. This program, in effect in only one city in January, 1969, now serves 64 areas. We have suggested reform along these lines in past years. The importance of better job information being provided by all levels of government should not be underestimated. Significantly greater efforts must be made in this regard if many jobs are not to continue to go unfilled because of lack of information. In addition to better job information, job opportunities for the poor and near poor

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[4] Senator Percy feels that a good starting point for such incentives to employment of unskilled persons would be his bill to provide an income tax credit for wages paid to individuals certified to need training or employment—75% for the first four months, 50% for the second four months, and 25% for the next four months.

[5] Representative Blackburn notes that when job training programs are carried out in institutions, pupils often are trained for jobs with few openings or jobs that do not exist. We must make sure that the trainee will be able to find employment after he finishes his training. There is a common myth that in our more technologically-oriented society, a person needs an exceptional amount of training in order to procure a position. This is not true. Automation has made jobs simpler and thus they require less training.

must be increased by providing such persons with greater job mobility. Reforms in this regard would include provision of better transportation opportunities to and from available jobs. In recent years many low-skilled primary jobs have been moving to the suburbs, away from our urban centers, leaving behind only secondary jobs available to our central city unskilled workers. These secondary jobs have included positions in food handling, hotel service, hospital service, etc. These jobs suffer from all of the defects of secondary jobs described above.

In order that our manpower programs may be properly implemented, we believe that the Federal government should consider funding programs at various higher educational institutions to deal with manpower program development and administration. At present, far too few people working on problems of manpower development and training have sufficient academic background in the field. If larger sums of money are to be expended in our manpower programs, it is imperative that those administering the programs have the background and training to enable them to discharge their duties effectively.

Employment Conversion

An employment problem which differs in many respects from the problem of training and placing the unskilled and low-skilled is that of ensuring meaningful employment for many persons with exceptionally high levels of training and experience who have been or might soon be displaced as a result of cutbacks in our military spending programs. Many persons have been thrown out of work as defense spending has been reduced and companies with very heavy concentrations in the military field have found themselves forced to release a number of their personnel.

What is the best approach to redirecting the economic resources which these highly skilled workers represent? Many defense-oriented businesses themselves have not shown a high capability for switching from military to non-military activities. Although such companies converted from strictly military operations to a number of other high technology governmental operations, such as aerospace, fairly well in the past, their experience in non-governmental commercial ventures at the end of World War II, the Korean War and recently following defense cutbacks has generally been disappointing. A number of reasons have been given for these failures, chiefly among which are suggestions of lack of management motivation and lack of certain capabilities necessary to commercial non-governmental success, such as marketing and distribution skills, ability to control production costs, ability to produce in high volume, knowledge of market financing requirements, etc. However, these companies do possess certain valuable assets, which include strong capabilities for research and development, experience in developing and maintaining highly trained teams of engineering and scientific personnel, and experience at making high value products which are technically complex and which demand painstaking craftsmanship. Given these strengths, we would hope that the large defense businesses would be able to make substantial conversions into the commercial field, particularly into such technology-intensive activities as pollution control and ocean research and development.

The abilities of many of these defense-oriented companies to convert to commercial activities is of significant importance to many of their employees, who would find it fairly difficult to convert their skills to non-defense activities. Although a number of studies have indicated that many lower level technical persons who have been engaged in defense work can be converted to non-defense work without too much difficulty, the higher engineering and scientific personnel who represent such a high educational investment would find such transfer difficult without substantial retraining. This situation stems from the fact that the lower level defense jobs often have civilian counterparts while the higher level jobs do not. If these highly skilled persons must now devote themselves to non-defense activities, it appears desirable that they be retrained to the extent necessary while remaining with the companies which are their present employers. This would have the benefit not only of maintaining many highly skilled scientific teams, but would contribute towards redirection of both the employees' and the companies' economic activities simultaneously.

Given the high economic losses which the nation may incur from non-utilization of resources and employee skills in defense oriented businesses and the fact that the present situation in the defense industry is in part a result of governmental action in reducing government contracts, we believe that a program of Federal support for conversion studies and retraining in the defense industry should be thoroughly explored.

IMPROVED RESOURCES ALLOCATION

ENVIRONMENTAL PROTECTION

Estimates of the total annual economic costs of air and water pollution in the United States run as high as $25 billion. This amount does not take into account the lessened quality of our national life as our environment continues to deteriorate. The Federal Water Quality Administration has estimated that between $35 and $70 billion must be spent over the next five to seven years if we are adequately to control water pollution. The National Air Pollution Control Administration has estimated that $15 billion must be spent over the same period in order to control air pollution. From where is this money to come and how is it to be spent?

We believe that those persons responsible for pollution should bear most of the costs of our environmental cleanup, rather than the Federal government. We recognize, of course, that in certain situations federal assistance to the non-governmental sector will be necessary and appropriate. However, this nation is faced with a number of other pressing national priorities which will require expenditures of large amounts of funds, funds which cannot reasonably be expected to come from the private and local governmental sectors of our economy. It is both equitable and economically sound to expect the private sector, which contributes a large part of our environmental pollution, to bear a fair share of the costs of controlling such pollution. Also, state and local governments, with federal assistance, should be expected to pay their fair share of protecting our environment. The question to be answered, however, is how to achieve the maximum benefits for our environment while minimizing the cost.

As the President's Economic Report points out, under the Clean Air Act of 1967, as amended, the 1975 model year automobiles will have to reduce emissions of carbon monoxide and hydrocarbons by 90 percent from 1970 levels. Although the standards approach is appropriate in many cases—especially, as in the case of automobiles, in a single industry in which costs of emission reduction can be substantially equal given uniformity of technology—the standards approach is not universally desirable. In the case of many pollutants which are produced in a variety of industries, costs of emission control vary substantially from industry to industry. Economically, the soundest approach would be to control all of the emissions from the low control-cost sources first. However, this is not easy to accomplish. Equal standards applied to all sources would obviously be inequitable. A system of variable standards would probably result in an administrative swamp and undersirable governmental regulation.

One method by which differences in control costs could be approached is suggested in the Economic Report, namely, by setting prices for the use of air and water. Faced with such charges, each polluter would be encouraged to reduce his level of emissions to a point at which further reductions would be more expensive than paying the price per unit of pollutant at that level. Under this system, low control-cost polluters would obviously reduce their levels of pollution the most. Such a pricing system would be sounder economically than any fixed or variable standards approach because, if properly designed, it would utilize free market forces in selecting levels of control to achieve a given level of environment quality, and in so doing would consume fewer productive resources. Additionally, a pricing approach would encourage the development of pollution control technology. Obviously, any prices under this system would be set with an acceptable level of total environmental pollution by each pollutant in mind.

A pricing approach to pollution control could work in several ways, through control subsidies (including tax incentives), emission charges, or transferable environmental usage certificates. **However, subsidies tend to involve extensive administrative and fiscal costs, and we believe it undesirable to emphasize an approach under which the federal government transfers resources to private persons based upon consumption by private persons of our national environmental resources. If individuals, both producers and consumers, wish to consume our environmental resources, they must be prepared to pay the charges associated with such use.**

A system of emission charges and usage certificates could ensure that environmental users pay for that usage. Emission charges and usage certificates are appropriate for air, water, and other environmental pollution, including solid waste pollution and noise pollution. In the case of solid waste pollution, for example, sellers should have to pay an emission charge in the case of products and product containers which are nonbiodegradable. The argument that the imposition of any such charges would merely result in increased costs to consumers is not completely accurate. Sellers under such a system would have the incentive to sell products and containers which would be biodegradable in order to escape any emission charges. Sellers able to escape such charges would enjoy a pricing advantage over their rivals and would hope to capture a larger share of the competitive market. In this way an environment pricing system would foster the development of environmental technology. To the extent that usage charges could not be avoided by sellers through technological developments, it may well be that most of such charges would be passed along to buyers. However, this is not an undesirable consequence. Without a system of either emission charges or usage certificates, the real cost of many goods to the society remains hidden. High cost environmental goods should carry a correspondingly high price so that the people who desire such goods pay the true cost of them.

The direction by the President to the Environmental Quality Council and the Department of the Treasury to develop a system of emission charges in connection with sulfur oxides is a good beginning in a system of user charges. The proposal for a tax on leaded gasoline is in the same category, requiring those using leaded gas to pay the true cost thereof, while encouraging the development of non-leaded gas technology.

The choice between using emission charges and environmental usage certificates which would be sold by the Government will probably vary from industry to industry, depending upon whether the pollutant in question does about the same amount of damage per unit or whether the damage caused increases rapidly at high levels of emission. In any industry in which a system of usage certificates was applied, there would have to be very stiff charges for any usage not covered by a valid usage certificate. Without such charges, it would be extremely difficult to maintain the market price of the usage certificates at a level which reflected the true economic cost of the pollutant emitted, since polluters might be encouraged not to accumulate sufficient usage certificates. Of course, both a system of emission charges and one of usage certificates would have to be under continuous review in order to be sure that price levels reflected changing hazards from pollution and new technological developments which would make increased pollution control economically attainable, and in order to ensure that incentives for controlling pollution levels through the use of such systems were adequate.

If a system of usage certificates and emission charges were to be instituted on a wide scale in this country, it seems that they would have to be phased in over a two or three year period to avoid seriously dislocating parts of our economy. Hopefully, such a system, if adopted, could be instituted by 1975. By that time any necessary employment conversion could be developed sufficiently to minimize the hardships which might otherwise be imposed. Pending development of a dual system of emission charges and usage certificates, strict enforcement of present pollution standards should be the rule, with stiff fines and injunctions enforced in order to deter illegal pollution. Fines and fees should also be extremely high in the case of what might be called inadvertant pollution, such as, for example, oil spills, in order both to reflect the very high social cost of such incidents and to provide adequate incentives to protect against such incidents.

We support the proposals of the President in his February 1971 Environmental Message regarding powers to be granted to the Administrator of the Environmental Protection Agency regarding water pollution. These proposals include granting power to the Administrator of the Environmental Protection Agency to issue abatement orders swiftly and to impose administrative fines of up to $25,000 per day for violation of water quality standards. We also support the President's recommendation that violations of standards and abatement orders be subject to court fines of up to $25,000 a day and up to $50,000 a day for repeated violations. These and other pollution fines, and fees collected by use of a system of emission charges and usage certificates, could be placed in a federal trust fund for matching and other grants to state and local governmental units to be used for environmental research, construction of pollution control facilities, etc.

Although we have stated that we believe a system of governmental subsidies to the private sector for pollution control is inappropriate, such a practice in connection with local governments is in many respects attractive. These subsidies would generally take the form of federal grants under which the federal government would provide either unencumbered or matching funds for local pollution control.

For example, a federal program now provides up to 50 percent matching funds to local governments in connection with liquid waste treatment plants. We also feel that a system of emission charges and usage certificates from the federal government would not be appropriate in the case of local governments. Therefore, it seems that state and local governments would have to be subjected to comprehensive pollution standards. However, the imposition of additional standards in the public sector may not be as difficult as in the private because the primary wastes generated publicly for which standards would have to be developed are not nearly as numerous as those in the private sector.

In conclusion, we wish to direct ourselves to the probable impact on our international economic position which would result from the imposition of a comprehensive set of domestic environmental control regulations. It has been suggested that if the United States drastically reduces its level of pollution, other countries will be encouraged to seek a comparative economic advantage regarding many goods by not engaging in any significant environmental control of their own. We do not believe that a necessary result of a stronger environmental control in the United States will be continued or increased pollution by our trading partners. Certainly it would be a great tragedy if the less wealthy countries were to allow a great deterioration of their environment as a result of attempts to compete economically with the wealthier countries at a time when the wealthier countries were increasing some of their direct costs of production by reducing the indirect costs of pollution. It is of the utmost importance that the United States lead the way in developing international agreements for attacking problems of pollution on a multinational basis and in working to eliminate incentives on the part of any nation or nations to compete economically by polluting. As American environmental control techniques develop, it will be in our best economic interests to make available throughout the world the fruits of our technological advances on the easiest terms possible.

Transportation

As the President's 1971 Economic Report suggests, reexamination of the regulatory framework within which much of our nation's transportation system operates is long overdue. When regulation of our interstate transportation system was first imposed, it covered the railroads, a monopoly industry in which the competitors were very similar. Although detailed regulation of railroads was in many respects desirable in the late nineteenth century era of intense individuality and rapid national economic expansion when there was no well-developed body of anti-trust or labor law, the suitability of a large part of such regulation in today's world is doubtful. Today we operate in a system which contains well-developed, detailed anti-trust and labor law. Additionally, in most respects the present transportation system does not consist of firms with monopolistic powers. Generally speaking, a potential shipper has a choice among a number of alternative means of transportation, including rail, air, water and highway. That our present regulatory system is not working is abundantly clear. If it were, as the Doyle Report on National Transportation Policy presented in

1961 to the Senate Committee on Commerce stated, "[T]here would have been no need for the seemingly endless series of transportation studies—including this one."

The economic costs which result from substituting regulation for free market forces in any industry can be great, and can be justified only if the benefits resulting from such regulation exceed the cost. It is extremely doubtful whether the benefits resulting from much of the regulations in our transportation industry meet this test. A few examples of the way in which our present regulatory system works illustrate this.

Unlike the situation in a free economy, in which unwanted goods and services are inexorably weeded out, in a regulated industry such as transportation, services which become obsolete, non-functional or unwanted are often perpetuated at great economic cost by regulatory agencies, either because of political or other pressures. The demand for such services, although economically small, may be politically large, vocal, and effective. The continuation of passenger train service in many areas of our country is an important demonstration of this. The conversion in the United States to automobiles and planes as principal modes of passenger transportation has resulted in disastrously large economic losses for railroads from passenger train operation. The railroad industry, unable to discontinue many passenger train operations because of refusal of the Interstate Commerce Commission to permit them to do so, reports losses of over $10 billion on passenger trains since the end of World War II. These refusals by the Interstate Commerce Commission have in many cases been the logical consequences of various policies which the ICC has had to follow under its often economically contradictory statutory mandate. That notwithstanding, the resources used in this sector could obviously have been employed at great economic gain elsewhere in our economy.[1]

Restrictions on discontinuing services are only one means by which inappropriate regulation has resulted in economic loss in our transportation industry. The imposition of the value-of-service rate structure on our rail and trucking industry has had numerous adverse consequences. Under this structure goods of higher value are charged higher freight rates, even if it costs no more to carry them. As the President's Economic Report points out, this rate structure has contributed to rural depopulation and metropolitan congestion because under such rates, finished goods are more expensive to ship than raw materials. Therefore, manufacturers have an incentive to locate close to or in areas where major consumer markets are located. At a time when our nation is becoming increasingly concerned about the flight of much of our population from rural areas to urban centers, which adds to the many problems facing our large cities and contributes to the further economic decline of our rural areas, we believe that regulatory support for a value-of-service rate structure is economically and socially unsound.

In the trucking industry, numerous regulations contribute to economic loss and to filling our highways with empty and partially

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[1] Representative Blackburn points out that airlines have their routes and fares regulated by Federal agencies. This has forced airlines to continue flights which should be discontinued because of decreasing passengers. This is one of the reasons why airlines are losing money on domestic routes.

loaded trucks, causing great economic wastage. These regulations include regulation of backhauls, which prevents charging freight rates equal to marginal cost on return trips, restrictions on commodities hauled, restrictions against mixing regulated and non-regulated commodities, and restrictions on service to points intermediate between points to which service is certified. One result of such policies is that only slightly over 50 percent of regulated trucks have full loads in both directions. According to a study which was conducted by the Highway Research Board in 1961, regulated trucking accounts for approximately one-third of inter-city ton miles. There is no evidence to suggest that this situation has changed significantly in the last ten years. According to the same study, private, contract, and agriculturally exempt carriers, which account for the remaining inter-city ton miles, had full loads in both directions less than 10 percent of the time. The high number of such carriers and the high proportion of all ton miles which they carry is, of course, a partial result of the oppressive regulation imposed on common carriers.

The increased cost in our annual regulated freight bill, which is in addition to the substantial cost of idle economic resources, attributable to an antiquated scheme of regulation can be fairly well estimated. In the 1950's the transportation of poultry was exempted from regulation. Following exemption, the Department of Agriculture found that freight rates for poultry decreased by approximately one-third. When certain frozen foods were deregulated, the Department of Agriculture found that rates fell approximately 19 percent from 1956 to 1957. Additionally, shippers reported that following deregulation, service improved at the same time that rates declined. Assuming that these commodities are fairly typical, then given our annual volume of regulated freight, our annual regulated freight cost could be several billions of dollars too high.

We suggest that it is a matter of national urgency for the Congress to re-examine the whole regulatory framework under which much of our transportation system operates. It is clear that there are instances in which transportation needs would be better served if certain restrictions on entry and departure from transportation markets were removed and rates, commodities to be carried, and points to be served were determined by the forces of the marketplace. In addition, consideration must be given to the debilitating impact of conflicting regulation of the various modes of transportation, and differences in labor laws, tax laws, and subsidization of the modes, including the maintenance of rights of way. This Committee should explore the impact of the present structure of the transportation industry on the economy, with emphasis on the probable economic results of various forms of deregulation.

This is not a call for the end of all governmental regulation. Because transportation is vital to our survival, certain regulations in the interest of safety, national defense, international trade and development of our domestic commerce are desirable. Obviously, in cases in which actual or potential monopoly powers as to geographical areas, commodities, or shippers exist, regulation would be necessary. Additionally, the entire transportation industry should be subjected to the operation of our anti-trust laws in order to protect against collusive pricing practices, etc.

De-regulation, where appropriate, would not necessarily result in chaos, as has been suggested in some quarters, although there would certainly be movements of resources. Any de-regulation proposed could be accomplished gradually, in order to avoid serious dislocations in our economy, and it should, of course, provide for appropriate regulation machinery in times of national emergency. The proposals in the President's Economic Report regarding gradual deregulation as to prices, entry and departure from markets, points of service, etc., seem to be sound. De-regulation over perhaps a five or six year period would help to minimize economic hardship.

Corporate Liquidity

With application of the Penn Central Railroad for bankruptcy in June 1970, the difficulties of certain brokerage houses in conducting business, and the rumors of other large corporations verging on bankruptcy during 1970 and into this year, the subject of corporate liquidity has become an item of some concern to economic policymakers. Basically, corporate liquidity is a concept used to describe the ability of a corporation to meet obligations as they become due. There are a number of different statistical ways to show what the liquidity position of any corporation is. Most of these measures of liquidity compare a corporation's cash and other liquid assets with various kinds of short-term liabilities; but as this description implies, liquidity bears a close relation to cash flow, the rate of corporate investment and other dynamic concepts which cannot easily be conveyed by statistical ratios.

Within the limitations of our commonly accepted measures of liquidity it is clear that corporations have been in a progressively tighter liquidity squeeze since the late 1950's. In part, declining liquidity ratios have been the result of more efficient management; in the Appendix to the President's Economic Report, there is conjecture that confidence in the economy also caused many corporations to reduce the amount of cash and other liquid assets to a lower proportion of total assets. By the late 1960's, however, it was clear that corporate balance sheets continued to reflect a view of rising sales and prices which was not warranted by a national policy of slowing the economy and stemming inflation. New capital appropriations in the first half of 1969 rose by 17 percent over the late-1968 level, notwithstanding that the Administration's and the Federal Reserve's policies were well known. Business spending for new plant and equipment accelerated from a temporary low in mid-1968 through the third quarter of 1969; in late 1969, when interest rates were at record highs, manufacturers were still projecting a quick upturn within the next six months.

In fact, the quick upturn did not come. Although moderately expansionary policies were begun in early 1970, the Administration's announced goal in this regard was to avoid stimulating a rise in demand such as occurred in 1967. It should have been clear to most business leaders that the Administration was taking its mandate of halting inflation seriously. Nevertheless, businesses kept a pattern of financing and inventory accumulation that was more suited to boom times than to the slow conditions of 1970. The ratio of total business inventories to sales during the first half of 1970 stayed at the relatively high rate of 1.56–1.59, and the rate of inventory accumulation far exceeded the rate of increase in other current assets. The accelerating use of commercial paper to maintain cash flows reflected the apparently general expectation that any slowdown in sales was quite temporary; during the first five months of 1970, the use of commercial paper increased 25 percent.

The failure of the Penn Central Corporation to refinance its maturing commercial paper in June 1970, and the resulting petition for bankruptcy, precipitated what many observers have called a liquidity crisis. Effects of the Penn Central situation were felt in the money and securities markets, which in turn affected the ability of other corporations—some with low liquidity ratios themselves—to obtain fully adequate financing.

During the first few weeks after Penn Central's difficulties came to light, the Federal Reserve Board took action to encourage bank financing where cash flow problems of businesses were being caused by weakness in the commercial paper market. On June 23, it suspended the Regulation Q ceilings on larger denomination, short-term certificates of deposit, and announced at the same time that the discount window would be available to assist banks in financing the emergency cash needs of business. The promptness of the Fed's action, and its unequivocal objectives, helped materially to cool what could have been a crisis of major proportions. Since mid-1970 corporations have attempted to restructure their balance sheets to secure a larger proportion of liquid assets, but this has not prevented the ratio of total current assets to current liabilities from reaching new lows by the end of 1970. On the other hand, indications are that changes in the pattern of corporate financing will make some headway in improving liquidity ratios during 1971.

Several lessons can be drawn from last year's experience.

The first is the widespread effect which the insolvency of a few major corporations could have in this country. **In its Annual Report, the Council of Economic Advisors concludes that there was no liquidity crisis in 1970 "if this term is taken to connote skyrocketing interest rates, a complete absence of bids for established securities, and numerous bankruptcies of sound corporations." We do not accept the implication of the Council that these conditions need exist before a liquidity crisis is recognized.** Quite apart from the fact that the insolvency of a major source of employment in an area can result in regional economic depression and inestimable human suffering, the bankruptcy of a few large corporations, we have learned, has implications for the ability of others to raise money and thus to maintain their own liquidity positions and profit levels; the response of the Federal government to such conditions as this should be the same as in any other crisis.

A second lesson from the 1970 liquidity experience is that the Federal government has shown it has substantial powers to prevent widespread bankruptcies in the event of a potential liquidity crisis. **The power of the Federal Reserve as an emergency source of liquidity was amply demonstrated last June, and we thoroughly approve of the Fed's decisive reaction to the Penn Central situation.**

Thirdly, however, **we believe that the Government needs additional tools in order to ensure the smooth functioning of financial markets during times of unusual demands for liquidity.** As Chairman Burns said during testimony before this Committee last July, the liquidity-creation powers of the Federal Reserve should be used only under extraordinary circumstances. Therefore, **we recommend establishing a Federal emergency loan guarantee program to be used in situations where the inability of a necessitous borrower to obtain a loan would result in serious curtailment of essential services to the public.**[2] Such a program should not be used as a means to bail out poorly run corporations or to correct for misjudgments of management, and businesses receiving the benefits of the guarantee program would thus have to be subjected to far-reaching Federal supervision.[3] As our discussion of the events of 1970 indicates, misjudgments by businessmen of the Administration's rather clear intentions played a role in the liquidity squeeze, and they should not be rewarded by having available federally guaranteed loans on a no-strings basis.

Fourthly, **it is clear that better analytical tools need to be devised to assess business liquidity and potential liquidity problems.** In its Appendix to the President's Economic Report the CEA does a competent job of analyzing liquidity but concedes that its conclusions might have to be qualified to the extent its sampling of firms was not completely representative. It states furthermore that "the severe difficulties experienced by some of the large manufacturing corporations in the analysis are concealed within the general averages." **More work should be done in assessing the effect of major corporate bankruptcies and the ability of government to ease any resulting hardship. Government also owes a particular responsibility to warn the business community of any incompatibility between government objectives and business expectations, and while this was done during 1969 and 1970, it is evident that the methods employed were not effective enough.** We look forward to the report of the Presidential Commission on Financial Structure and Regulation, which will address itself to factors influencing the liquidity situation.

REVENUE SHARING [4]

During the annual hearings this Committee heard dramatic and pointed testimony from mayors and governors across the country about the deteriorating condition of state and local finances. The testimony described a situation of rising claims on state-local government services, coupled with a tax base insufficient to meet these claims. There has been general agreement among experts in public finance that this situation has reached crisis proportions.

At the same time, the Administration announced its revenue sharing plan, the first major effort by the Federal Government to reorganize the federal grant-in-aid system. The Administration's plan would give

[2] Senator Percy feels we should be cautious about such a program and be sure it is used only when no alternative source of such service would otherwise be available or competition would be seriously limited.

[3] Representative Blackburn notes an inconsistency in this paragraph since the primary example used to justify this section is the Penn Central Transportation Company's failure. Beyond any doubt, Penn Central provided essential services to the public. However, there can be no doubt that this corporation was poorly run and corporate funds were mismanaged. Before the government becomes the lender of last resort to bail out ailing corporations, it might be wise for the Presidential Commission on Financial Structure and Regulation to investigate all possible alternatives.

[4] Congressman Blackburn does not wish to be associated with the Minority Views on revenue sharing.

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considerably greater freedom to state-local governments in the spending of federal funds, would significantly reduce the number of categorical grant-in-aid programs, and would establish the precedent of automatically turning over to state-local governments a certain percentage of the personal income tax base year by year.

While our specific recommendations are described in detail below, we assert at the outset that the Congress must act this year to provide a substantial amount of long-term financial relief to state-local governments.

The origins of the present crisis in state-local government finances lie in two phenomena which will apparently be with us for some time.

The first phenomenon is the changing nature of claims on state and local governments. Ironically, our affluence has generated accelerating demands for services which non-affluent governments are unable to provide. Cleaner air, modernized education and transit systems, superior health care, and an up-to-date penal system are typical of the expensive demands which modern society places on its governments; yet each of these cases represents areas of state-local government concern. An additional complication in some cases is the fact that jurisdictional boundaries prevent the efficient solution of these problems, as the difficulty of attacking air and water pollution shows. In Mayor Gibson's written response to Minority questions, for example, we have convincing and expert testimony as to the many costs which a city government incurs by virtue of its position as the center of a larger metropolitan area over which it has little control. Finally, in administering services state and local governments are often caught up in problems which we recognize as national in scope. Trash collection, for example, though a local responsibility, is part of the broader national problem of solid waste disposal. Education is administered largely on a state and local basis, but many of the extra costs of education result from a complex of social conditions which we as a nation must solve. The effects of a good or a poor education reflect themselves directly in the quality of our society in later years.

The second phenomenon concerns the tax base which state and local governments have at their disposal. The Federal government, for example, relies chiefly on the income tax, which not only expands with growth in income, but also expands as a percentage of income as persons move into higher tax brackets. State governments on the other hand, have come to depend upon consumer taxes such as sales, alcohol and tobacco products, etc. In contrast to the Federal government, which has been able to reduce taxes three times in the last decade, state governments have had to pass more than 450 new or increased taxes and even at this rate, state revenues have increased more slowly than Federal revenues. Property taxes constitute the major portion of local revenues. While such taxes are appropriate for financing the services which we associate with property improvement and protection (e.g., fire, police, parks, trash collection), they do not respond to the increased demands being placed on localities today. Furthermore they are not a reliable source of revenue during times of economic downturn; cities like Newark, for example, collected fewer revenues in 1970 than in 1969, despite rising claims for city salaries and services. Over the past decade, the rate of Federal revenue growth has outstripped local revenue growth by 50 percent.

In short, states and local governments today are faced with accelerating demands which surpass their ability to pay. Many of these demands are the substance of what has popularly been called the "quality of life." It is therefore clear that we must make substantial commitments of our resources to improving the viability of state-local finances if we are to make headway in realizing many of the goals of modern America.

The traditional Federal response to the needs of state and local governments has been the grant-in-aid system. Federal grants in aid have been distributed either by formula to all state and/or local governments or according to specified projects submitted by public or private recipients. Distinctions are also made between block grants, which are directed to some general purpose (e.g., Model Cities grants), and categorical grants, which have a narrow purpose such as sewer construction. Although the grant-in-aid system is said to have started in 1862 with the Morrill Act, which started land grant colleges, Federal aid to help ensure the viability of state-local governments began with the Depression. The number of such grants has multiplied considerably in recent years and stands at more than 400 today.

In part these grants have served to help state and local governments perform essential services such as sewage disposal. But Federal grants-in-aid, and the conditions attached to them, have also been directed towards answering national needs as perceived by Congress. Examples of this are grants under the National Defense Education Act, which was passed in the wake of the first Russian artificial satellite launch, and the nondiscrimination provisions attached to virtually all grants-in-aid since 1964.

Over the years, therefore, the grant-in-aid system has become a major factor in intergovernmental relations, influencing the purposes for which state-local revenues are spent, and the way in which they are spent. However, most persons agree that there is a confusing amount of overlap in some programs, and that the conditions attached to grants are often not responsive to the needs of particular areas. Furthermore, the red tape of applying for federal grants reduces their effectiveness. Another problem in recent years has been the gap between authorizations and appropriations for Federal grants-in-aid, which presently stand at 36 percent of appropriations.

Under the Administration's Revenue Sharing plans (General Revenue Sharing, and Special Revenue Sharing), some of these complaints would be answered. Federal aid to states and localities would increase approximately 26 percent in 1972 over the 1971 level. Funds under the General Revenue Sharing program would be geared to a percentage of the personal income tax base, thus ensuring state-local governments a share of the Federal fiscal dividend each year; they would be distributed automatically, with no strings attached, thus eliminating the overhead costs of categorical grants. Special Revenue Sharing funds would be directed to six broad purpose categories and replace 130 categorical grant-in-aid programs.

We applaud the Administration's initiative in advancing a Revenue Sharing program and endorse the principle of sharing the Federal fiscal dividend with hard-pressed state and local governments; also with the principle of distributing funds according to

tax effort. We support the concept of grant consolidation and simplification which characterizes the Administration's Special Revenue Sharing Program. We believe that the goal of restoring the financial viability of state-local governments in this decade, with all this implies for improving the conditions of everyday life, requires a commitment similar to the commitment made ten years ago to land an American on the moon before the end of the decade. We believe Congress should expressly make such a commitment, and as a first step enact a Federal Revenue Sharing Program this year.[5] [6]

However, we recognize that many of the problems of state and local governments are jurisdictional, rather than financial, and we believe that the national effort to improve the state-local government situation must also seek reform in this area. In addition, we are concerned that appropriate performance standards be established and maintained. We in the Congress should be the first to recognize the national effect which the grant-in-aid system has had in recent years. Conditions attached to grants-in-aid, drafted in many cases only after extensive hearings and debate, have become basic instruments for achieving such national goals as social justice and highly trained manpower. While we are confident about the ability of state-local governments to administer broadly-based federal aid, we reserve the right to adapt and adjust any future federal aid system where national interests are at stake.

Productivity

In 1969 the rise in output per man hour in the private economy came almost to a halt. In two quarters of that year labor productivity actually declined. The record in 1970, based on preliminary figures, shows that labor productivity rose less than one percent. This two-year performance, the worst in the postwar economy, coincided with a time when consumers and even national leaders voiced concern over the deteriorating standards of American working men, a falloff in our competitive position overseas, and a loss of pride in American craftsmanship.

On the other hand, starting with the second quarter of 1970 productivity has been on the incline, and most economists agree that this trend will continue during the current business recovery.

Policies during this transitional period should be aimed at further stimulating the productivity growth which is already under way, and also at improving our long-term productivity performance. Although the short-term improvement in productivity will respond to roughly the same policies which we recommend for effecting economic recovery in general, we believe that additional efforts are needed to support the kind of productivity growth which this country needs over the future. As we explain below, these efforts can best be implemented through a

[5] Senator Jacob Javits and Representative Barber Conable, Jr. state: "Governor Rockefeller's testimony before the Committee pointed out that a $10 billion General Revenue Sharing Program would provide an estimated half of the increased costs of states and localities this year."

[6] Senator Jacob Javits supports a doubling of the Administration's General Revenue Sharing Program. See the additional views of Senator Javits on page 137.

permanent national productivity commission, regional offices, and local plant or community productivity councils, to expand upon the excellent work already being done in this area by the President's National Productivity Commission; also through the establishment of a multipurpose adjustment assistance fund.

By definition, productivity policy is aimed at maximizing the output which can be gained from the various factors of production, i.e., labor, entrepreneurial talent, land, raw materials and capital goods. Changes in this output come about through improvements in the way the factors of production are handled; better education of the labor force, more efficient land use, and the use of technological improvements are some examples. Because our society is so technologically oriented, scientific and engineering achievements probably account for a large share of improvements, although a comprehensive productivity policy must go beyond promoting technology alone.

Improving productivity, therefore, consists of promoting the continuous, progressive adjustment and rationalization of the private sector. Success at this venture is the key to achieving real growth with higher living standards at home, and to maintaining our competitiveness abroad. In a country like the United States, where output reflects primarily the value of services and of manufacture rather than of raw materials, the interaction of productivity and wage levels is the most important factor in setting prices. One observer has remarked that that increasing productivity is the closest thing one ever comes to getting something for nothing.

On the other hand, there are long term disadvantages which this country has as a result of our advanced state of growth and techology, and these disadvantages accentuate the need for a consistent and continued high level of productivity growth.

In the first place, most other countries can capitalize on American experience by freely "borrowing" advanced technology which has been developed, often at great cost, in this country. Over time this technology windfall can result in a substantial narrowing of the productivity gap between this country and others. One of the ironies of America's technological achievement and business prowess, in fact, relates to the rapid international transfer of technological and business know-how which our preeminent position has made possible. As a general rule, therefore, the technologically more advanced countries of the world bear almost the full cost of researching and developing new technology.

Secondly, the process of adjustment and rationalization in America sometimes creates conditions of economic dislocation which, given the higher standards of our modern society, are politically difficult. Joseph Schumpeter once observed that technological advance is a process of creative destruction; for Americans this process of destruction—meaning in some cases the closing down of obsolescent plants in "one factory towns" and the laying off of workers with obsolescent skills—must be continually countered by expensive programs to teach new skills and restore those affected to a high standard of living.

Thirdly, the advanced state of economic growth in this country has created immense social needs and environmental problems which will heavily strain our resources for decades to come. The minimization of pollution and the guarantee of a minimum income for all Americans are typical of these needs, which will require large commitments of our productive capacity. Increased productivity growth would be necessary to satisfy this new breed of priority needs without shifting resources from other priority uses.

Finally, the sheer size of America's physical plant does not permit rapid response to the changing conditions of the world economy, wherein some of our major trading partners are enjoying immense productivity gains. Although the solution to this problem does not necessarily involve increasing productivity growth in this country, the fact is that our productivity performance in recent years vis-a-vis the rest of the world has contributed markedly to the deterioration in our international competitive position and probably to the rise of protectionist sentiment in many domestic industries.

We believe that the conditions we have just described warrant a conscious national effort to promote more rapid and consistent long-term productivity growth.

A national program to improve productivity must be able to muster the technology and the capital to rationalize our productive plant, pinpoint areas where substantial improvement can be made, and finally convince businessmen and legislators of the necessity for changing existing laws to achieve greater efficiency. Such a program could be carried out only at the Federal level. Consequently, we believe the following steps would constitute a favorable departure point for such a program:

1. **A strong declaration of Congressional policy calling for improved productivity growth.**

2. **Establishment of a permanent productivity commission, with regional offices throughout the country, to keep abreast of productivity problems in the United States. We favor also the establishment of local productivity councils at the community and factory levels.** In cooperation with our universities, a system of productivity organizations should be able to disseminate technological developments of interest to factory and office managers in much the same way that agricultural developments are brought to the farmer. In special cases, and in conjunction with other government agencies, it should be able to aid communities where the decline of obsolescent industries has caused severe dislocations in the local economy.

3. **Establishment of an adjustment assistance fund, under the Commission's control, which could be drawn upon to meet the expenses of the Commission and to promote the channeling of capital into more productive pursuits.** The latter would include such activities as market surveys, incentive programs for communities to attract more efficient businesses, and working capital loans where appropriate for businesses which do not qualify for other (e.g., Small Business Administration) programs. Because our competitiveness in the world economy bears such a close relation to productivity growth in America, we believe such a Fund to be fully justified.

We believe that this kind of national commitment, and large investment of effort and money, are essential if we are to make Americans aware of the importance of faster productivity growth, and to gain the knowledge and the capability to meet higher productivity goals.

AGRICULTURE AND RURAL DEVELOPMENT

> **If the lessons of the past decades mean anything to us, they mean that as power has been concentrated more and more in Washington, D.C., as decisions have been increasingly made by remote control, the special needs of our rural communities and of the great heartland of America more and more have either been neglected or even gone unrecognized. . . .**
>
> **. . . the housewife in America, the best-fed country in the world, pays less of her budget for food than in any country of the world.**
>
> **This is an indication of what the farmer has done for America.**
>
> **And when the farmer and American agriculture have done that, when it is the most productive of all of the various phases of our economy, certainly American agriculture and the American farmer deserve a fair share of America's increasing prosperity.**
>
> **—President Nixon,**
> **Address to Iowa Legislature,**
> **March 1, 1971.**

Enactment of the bipartisan Agricultural Act of 1970 laid a foundation for better years ahead for our family commercial farmers than was the case with previous farm programs, under which nearly 6 million farmers and their families were forced to leave their farms from 1961 through 1970.

The freedom to plant the crops of their choice under the Administration's unique "set aside" program for the major crops of wheat, feed grains, and cotton represents a significant reversal in a policy of government control, while, at the same time, the Administration's policy of not lowering the overall government cost of farm programs provides assurance of a "floor" for farm income.

We do not believe that the cost of these programs should be criticized by the taxpayer-consumer, for the record shows that only 16.7¢ per consumer dollar now goes for food compared to 20¢ ten years ago.[1]

[1] Senator Percy and Representative Blackburn feel that the cost of any program, including farm programs, should be subject to constructive criticism. Indeed, looking at the record, it is the Federally supported crops that are in the most trouble and cost the taxpayer the most. Those crops that are free of Federal intervention are, generally speaking, the healthiest and the most remunerative to farmers.

This represented a reduction for consumers of $25 billion for 1970, compared with a cost to them, in taxes, of under $4 billion for farm program payments. (Of course, inflation has increased food prices, but there are more consumer dollars being spent.)

We have consistently advocated a continuation of farm programs and we have emphasized the importance of bipartisanship in developing and administering these programs. With the farm population now comprising only 4.7 percent of our total population, our agricultural economy needs all the support it can obtain from both political parties. The economic and social consequences of doing away with farm programs are too well known to bear repeating. On the other hand, excessive government controls deprive the farmer of an opportunity to benefit from a strong market economy. The difficult task of the Congress is to steer a prudent course between these extremes; and the equally difficult task of the Executive Branch is to administer the farm programs enacted by the Congress in such a way as to achieve a healthy agricultural economy in the face of uncertainties of weather, disease, foreign trade, and the overall national economy.

The Agriculture Economy in 1970

The year 1970 was a year of contrasts for many who comprise the agricultural segment of our economy. Although down somewhat from the previous year, the overall income situation proved to be one of the better years on record. Realized gross farm income came to $56.2 billion in 1970, $1.6 billion over the record high of 1969. However, this increase was more than offset by a gain of $2 billion in production expenses, resulting in realized net farm income of $15.8 billion, slightly lower than the $16.2 billion for 1969 but 35 percent higher than in 1960.

There was a smaller drop than usual (1½ percent) in the number of farms from 1969 to 1970. Realized net income per farm averaged $5,392 in 1970 compared with the record $5,437 a year earlier, but was still 82 percent above the 1960 level.

Aggregate personal income of farm people rose to $27.9 billion in 1970, $400 million over 1969. This increase is accounted for entirely by a rise in income from nonfarm sources. Disposable personal income (after taxes) per capita of the farm population was $2,633 in 1970, about $200 higher than the previous year and a new record high. The ratio of average disposable income of farm people to nonfarm people was 78 percent in 1970, up one percentage point from 1969. Clearly the farm population has not been sharing fairly in the national net income, but the gap continues to narrow. In 1960, per capita disposable income of the farm population was only 55 percent of the income of the nonfarm population; and for the period 1966–70 the ratio averaged around 75 percent. It should be noted, however, that this trend has been due largely to the fact that income from nonfarm sources has become a larger component of net incomes of farm people. Almost half (47.7 percent) of the 1970 per capita disposable income of people on farms was from nonfarm sources.

On the debt side of the picture, total farm indebtedness (including Commodity Credit Corporation loans) rose 4 percent over 1969 to $60.4 billion in 1970, 2 percent less than the rise in 1969 over the year 1968. Debt per farm rose 5½ percent, from $19,588 to $20,683—down from the 8 percent rise in the previous year. The tight money situation throughout the economy in 1970 made credit more costly and less available to the agricultural sector. Because of a greater reluctance of farmers to borrow at high rates of interest, the increase in farm debt was substantially below the average of 9 percent per year during the preceeding decade.

National net farm income for 1970 represented only a 6 percent return on net farm equity, leaving nothing whatever for the farmers' labor and managerial skills—another indication that farmers have not been sharing fairly in the national net income.

Continued Cost-Price Squeeze

In past Minority Views we have consistently stressed the seriousness of the cost-price squeeze on the nation's farmers and their families. We are disappointed that 1970 did not see any lessening of this problem. Prices received by farmers in 1970 increased by 2 percent over the 1969 level, but prices paid by farmers increased by 5 percent. The largest increases in various prices paid by farmers were for interest (up 10 percent), taxes (up 9 percent), and labor (up 9 percent). The result was a decline in the parity ratio to 72 for the year as a whole (compared to 74 for 1969), with a low of 67 in December. [However the parity ratio had moved back up to 70 for February of this year.]

The greatest contrasts in the farm economy were provided by crop and livestock prices. As 1970 moved along, crop prices rose and livestock prices declined. Livestock prices remained at high levels until mid 1970, but then began a downward path. Hog prices led the decline, which was primarily due to the large increase in pork production accompanied by large supplies of beef, poultry, eggs, and milk. [The December 1970 national inventory of hogs was nearly 11 million above December 1969.] The rise in crop prices was attributable largely to increased exports and to a smaller 1970 grain crop due particularly to an unexpected drop of 15 percent in the anticipated corn crop because of drought in the western corn belt and a fairly widespread incidence of southern corn leaf blight.

Probably hardest hit (with the exception of some farmers whose corn crops were severely damaged by drought and corn blight) were the nation's hog farmers. The average price of slaughter hogs was above $28.00 per hundredweight in February, but dropped to $15.00 in December for a yearly average of $21.95 compared to $23.89 for 1969. [Hog prices have improved somewhat of late, but large supplies may continue to hold prices below the highs of last winter.] We are pleased that the U.S. Department of Agriculture has been using its authority to increase CCC purchases of pork. During the first seven months of fiscal year 1971 USDA increased its pork purchases by more than three-fold over the same period in fiscal 1970—from 32 million pounds to almost 118 million pounds at a cost of over $61 million. The Department has also taken other actions designed to increase pork consumption.

We are concerned with the time lag between lower prices for farm products, such as pork, and lower prices for consumers in the market place. We commend the Department for its initiatives to reduce this time lag and hope that the food processing and retailing industries will cooperate.

The New Farm Program

The year 1970 marks a turning point in the history of agricultural policy with the passage of the Agricultural Act of 1970. In our previous Minority Views we have consistently recommended that the farm programs to follow the 1965 Act should move toward a strong market economy rather than a government payment and regulated economy, should achieve a more equitable distribution of benefits to our farming population, and should establish a reasonable limitation on payments. We believe the new Farm Act proceeds along the lines of these recommendations, although perhaps not as much as some of us would have preferred. Recognizing as we must the many differences of opinion among 535 Members of Congress and the need for bipartisanship in passing a major farm bill, we do feel that the new programs represent an improvement over previous programs.

The principal change in the 1970 Act is greater flexibility and a wider range of decision making for farmers in their farming operation. This is accompanied by the stated objectives of improving cash markets for farm commodities and developing a greater reliance on the marketplace as a source of farm income, protecting farm income, and achieving a reasonable balance between supply and demand. These objectives are to be realized through continuation of price support payments with guaranteed support levels, a required set aside of a certain percentage of a producer's base acreage or allotment with freedom to plant the remaining acreage to maximize net return per acre, and loan floors in the case of wheat and feed grains. There is also a payment limitation of $55,000 per crop in the case of wheat, feed grains, and cotton—the first such limitation ever attempted in these programs.

We recognize that with any new program there are a certain number of unknowns, not the least of which is the uncertainty for 1971 corn production because of the shortage of blight resistant seed and the possibility of blight again damaging the crop. Based on the farmers' planting intentions reports and other data, the Secretary of Agriculture announced a set aside requirement of 20 percent for the 1971 crop year for feed grains—a decision which apparently was calculated to err on the side of strong prices for farmers rather than an overproduction and weak price such as occurred with the 1967 crop. We are disappointed that the new Farm law does not contain authority for three, five, and ten year contracts for cropland retirement instead of restricting the Department of Agriculture to annual "set aside" contracts, but we are hopeful the Administration will request and the Congress will approve full funding of the cropland adjustment and greenspan programs.

Agricultural Trade

One of the most encouraging developments of 1970 was our favorable balance of agricultural exports over agricultural imports. Over the years this surplus has been a major factor in our overall favorable balance of trade. Indeed, in several years it has meant the difference between a favorable instead of an unfavorable balance of trade. Reversing a downward trend for the last three years, agricultural exports rose to $7.2 billion in 1970—21 percent above the 1969 level and 4 percent above the previous record of $6.9 billion in 1966. Leading this export gain were a 48 percent increase in soybean exports and a 39 percent increase in wheat exports. The principal reasons for these increases were continued improvements in the economies of Japan, the European Economic Community (EEC), and Canada which created more demand for meat and feed stuffs, smaller grain stocks in Europe, and stronger economies in some of the developing countries which increased their demand for U.S. imports.

On the other side of the coin, the value of U.S. agricultural imports rose 14 percent to a record $5.7 billion, up from the $5.0 billion in the previous year. Two of the leading items were dairy products, which rose 25 percent on the strength of volume and price increases, and meat and meat products, which rose 17 percent—about equally divided between volume and price increases. On a volume basis (carcass weight), meat imports rose from 2,202 million pounds in 1969 to 2,387 million pounds in 1970, an 8 percent increase. The main problems with meat imports were that they were up almost 50 percent during the early part of 1970, causing the President to impose limits for the balance of the year; and the trans-shipment of meat through Canada.[2]

In the case of dairy imports, the volume increase was small—1.93 billion pounds (milk equivalent) for 1970 compared to 1.62 billion pounds for 1969—considerably under the 2.9 billion pounds in 1967. Nevertheless, pressures created by a world dairy surplus and the attractiveness of U.S. prices are requiring continuing scrutiny and administrative action under existing law—the latest being Presidential Proclamation 4026 last December 31. Accordingly, the volume of dairy imports is expected to decline in 1971.[3]

The Food-For-Peace program continues to be an integral part of our foreign relations policy. This program has been maintained at a level of about $1 billion over the past few years, and the level for 1970 was only slightly less than the average. Although exports under PL 480 do not help our balance of payments problem, they have been increasingly useful in developing cash markets for the future and should continue to be funded at or near current levels. Disregarding the Food-For-Peace or non-commercial exports, our favorable agricultural trade balance was still a half billion dollars for 1970, whereas we had been in a deficit position on commercial exports versus commercial imports since 1967.

The following tables illustrate the trends in agricultural imports and exports for the last seven years.

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[2] Senator Javits believes the perpetuation of rigid import quotas on meat does not serve the broader interests of the American consumer. In memorandum to the President requesting that import quotas be liberalized, Governor Rockefeller pinpointed that fact that in recent years meat prices have been increasing at a much faster rate than the overall rate of inflation. In turn. Mayor Lindsay's Commission on Inflation and Economic Welfare has reported that in 1970 the price of meat, fish and poultry in New York City increased by 18 percent over the previous year. In dollar terms this means that for a family of four earning $6000. the additional cost each year to put meat on the table is $101; for a family of four earning $9500, the additional cost is $135. Restrictive meat import quotas should be substantially liberalized or repealed to help curtail the sharply inflationary increase in meat prices.

[3] In future Administrative actions affecting dairy quotas, the legitimate interests of the American consumer should be carefully weighed. More rigid quotas on dairy products such as cheese, would have an inflationary price effect as well as limiting consumer choice.

TABLE I.—AGRICULTURAL IMPORTS, CALENDAR YEARS 1964–70

[In millions of dollars]

Commodity	1964	1965	1966	1967	1968	1969	1970
Supplementary:							
Animals, live	56	117	118	80	113	119	157
Dairy products	62	73	118	115	101	101	126
Meat and meat products	483	525	619	664	764	861	1,011
Sugar, cane	458	441	502	587	641	638	729
Tobacco, unmanufactured	89	130	127	129	142	128	128
Wool, apparel	115	157	157	102	110	85	59
Other	675	627	986	1,019	1,167	1,157	1,310
Total	1,938	2,070	2,627	2,696	3,038	3,089	3,520
Complementary:							
Coffee (green, roasted)	1,027	1,064	1,069	964	1,144	896	1,165
Cocoa beans	131	139	122	147	136	168	201
Rubber, crude natural	201	182	177	170	188	275	231
Wool, carpet	90	71	72	38	48	43	31
Other	357	384	424	437	470	486	519
Total	1,806	1,840	1,864	1,756	1,986	1,868	2,147
Grand total	3,744	3,910	4,491	4,452	5,024	4,957	5,667

Source: Economic Research Service, U.S. Department of Agriculture.

TABLE II.—AGRICULTURAL EXPORTS, CALENDAR YEARS 1964–70

[In millions of dollars]

Commodity	1964	1965	1966	1967	1968	1969	1970
Cotton, excluding linters	682	486	432	464	459	280	372
Dairy products	224	196	126	121	143	121	127
Feed grains, excluding products	855	1,135	1,334	1,054	926	860	1,058
Fruits and preparations	279	313	315	310	277	323	334
Soybeans	567	650	767	772	[1] 810	822	1,216
Tobacco, unmanufactured	413	383	482	498	524	540	488
Vegetables and preparations	158	155	176	164	173	192	206
Wheat and flour	1,532	1,183	1,534	1,206	1,100	830	1,111
Other	1,638	1,728	1,715	1,776	1,816	1,968	2,262
Total	6,348	6,229	6,881	6,365	6,228	5,936	7,174

[1] From census unpublished data.

Source: Economic Research Service, U.S. Department of Agriculture.

TABLE III.—SHARE OF U.S. AGRICULTURAL PRODUCTION EXPORTED, FISCAL YEARS 1964–70

[In percent]

Commodity	1964	1965	1966	1967	1968	1969	1970
Wheat, including flour equivalent	75	55	65	56	49	34	41
Rice, rough basis	62	54	55	64	64	48	58
Nonfat dry milk	62	44	37	24	20	25	24
Dried edible beans	49	17	17	18	16	17	22
Tallow	44	40	37	40	38	38	36
Soybeans [1]	41	48	43	39	40	38	50
Hops	41	43	42	40	36	39	30
Rye grain	34	6	11	16	12	5	2
Cotton	32	30	20	48	55	26	29
Dried prunes	30	27	37	35	28	29	31
Lard	28	18	9	9	9	10	16
Dried whole milk	28	17	21	16	16	23	21
Tobacco, farm sales weight	26	25	29	38	32	38	36
Cottonseed	23	32	19	5	0.1	0.1	0.1
Raisins	21	25	23	24	38	27	27
Dried edible peas	20	60	65	82	74	84	79
Grain sorghums	17	24	36	39	23	14	16
Barley, grain	17	14	19	11	8	3	4
Flaxseed	11	27	15	32	25	36	16
Corn, grain	11	15	17	12	12	12	13
Cattle hides	45	56	41	41	36	42	45
Lemons and limes	9	17	21	19	18	19	21
Variety meats	9	10	10	10	9	10	10
Almonds	16	12	16	13	15	12	23

[1] Includes bean equivalent of soybean oil for export.

Source: Economic Research Service, U.S. Department of Agriculture.

Although agricultural exports in 1970 set a new record, we believe we can and indeed must do better. This basically involves two factors: maintaining and expanding our present export markets and carrying out our own trade policies in a manner to not invite retaliation from foreign countries.

During the last few years we have commented in our minority views on the Common Agricultural Policy (CAP) of the EEC. This program, which combines extremely high internal prices with a variable levy system to protect against imports, results in surpluses which are then moved into international trade with heavy subsidies. The costs are then borne by third countries—and particularly the United States, not to mention the consuming public in the EEC countries. The EEC is our largest export market for agricultural commodities (Japan is the largest single-country market), and, although our exports to the EEC in 1970 nearly reached the peak year of 1966, the intermediate years showed a steady decline with no change in the CAP. As noted previously one of the factors contributing to the rise in agricultural exports for 1970 was a smaller grain crop on the Continent—something that can change in the future.

Another development which is most disturbing is the appearance of discriminatory trading agreements negotiated by the EEC, and we particularly refer to the preferences given certain Mediterranean countries in the case of citrus exports. Such agreements are a clear violation of the GATT rules and appropriate appellate procedure has been initiated to have them discontinued. While the present consequences to U.S. trade are still relatively minor, such activities could lay a foundation for major restrictions on our access to world markets with the devastating results of a trade war.

We commend the Administration for its promptness in protesting these preferential agreements. We urge the Administration to continue its efforts to persuade the EEC to modify the CAP. If, for example, the EEC would permit some lowering of their internal feed prices, they could promote an expansion of their livestock feeding endeavors which they very much want and need. We know the Administration is closely following negotiations for British entry into the EEC and we expect Britain to be made fully aware that her adoption of the present CAP could seriously impair our exports of feed grains and other commodities to her.

The following tables show the trends of our agricultural imports and exports with our major trading partners.

TABLE IV.—U.S. IMPORTS, CALENDAR YEARS 1964–70

[In millions of dollars]

Year and area	Total imports	Agricultural imports	Agricultural imports as percent of total imports
1964	18,600	4,082	22
1965	21,283	4,087	19
1966	25,360	4,491	18
1967	26,733	4,452	17
1968	33,066	5,024	15
1969	35,863	4,957	14
1970	39,768	5,667	14
From EEC:			
1964	2,831	258	9
1965	3,316	270	8
1966	4,098	306	7
1967	4,441	331	7
1968	5,849	362	6
1969	5,787	363	6
1970	6,574	419	6
From United Kingdom:			
1964	1,132	23	2
1965	1,403	24	2
1966	1,761	30	2
1967	1,710	28	2
1968	2,016	32	2
1969	2,129	35	2
1970	2,186	37	2
From Japan:			
1964	1,763	40	2
1965	2,401	37	2
1966	2,948	37	1
1967	2,994	32	1
1968	4,044	37	1
1969	4,849	37	1
1970	5,852	37	1
From Canada:			
1964	4,227	176	4
1965	4,813	234	5
1966	6,106	240	4
1967	7,099	201	3
1968	8,918	226	3
1969	10,345	244	2
1970	11,025	305	3

Source: Economic Research Service, U.S. Department of Agriculture.

ownership, the deduction for medical expenses to relieve hardship, percentage depletion to encourage development of mineral resources and lower cost products for the public and lower rates on capital gains to encourage capital investment needed to provide jobs."

Conclusion.—What the preceding portion of this chapter attempts to point out is this: If we want to make substantial inroads into solving some of our problems and needs, we must make the necessary, and difficult decisions that sacrifice short term goals for long term benefits. With $44 billion to spare, we cannot concurrently combat pollution, put our cities and states into good liquid position, improve public transportation to facilitate travel for all Americans, provide ourselves with a fool-proof and indestructible defensive weapons system, eliminate poverty, and improve labor markets through expanded manpower programs within the next five years. Clearly we cannot achieve all we would like to on the resources which we will have to work with during this time frame within the realm of our current tax structure. But we can improve the mechanism within which we make choices and thus achieve our goals more quickly in the longer run.

Senators	*Representatives*
Jacob K. Javits	William B. Widnall
Jack Miller	Barber B. Conable, Jr.
Charles H. Percy	Clarence J. Brown, Jr.
James B. Pearson	Ben B. Blackburn

TABLE V.—U.S. EXPORTS, CALENDAR YEARS 1964-70

[In millions of dollars]

Year and area	Total exports [1]	Agricultural exports	Agricultural exports as percent of total exports
1964	26,156	6,348	24
1965	27,135	6,229	23
1966	29,884	6,881	23
1967	31,142	6,380	20
1968	34,199	6,228	18
1969 [2]	37,462	5,936	16
1970	42,593	7,174	17
To EEC:			
1964	4,481	1,416	32
1965	4,904	1,476	30
1966	5,264	1,564	30
1967	5,582	1,460	26
1968	5,994	1,367	23
1969	6,875	1,269	18
1970	8,325	1,559	19
To United Kingdom:			
1964	1,445	448	31
1965	1,537	390	25
1966	1,645	471	29
1967	1,929	424	22
1968	2,132	374	18
1969	2,278	361	16
1970	2,478	402	16
To Japan:			
1964	1,894	720	38
1965	2,042	876	43
1966	2,312	942	41
1967	2,665	864	32
1968	2,924	933	32
1969	3,462	934	27
1970	4,610	1,214	26
To Canada:			
1964	4,653	[3] 615	13
1965	5,486	[4] 620	11
1966	6,487	[5] 626	10
1967	7,053	[6] 556	8
1968	7,936	[7] 595	7
1969	8,956	[8] 710	8
1970	8,806	[9] 810	9

[1] Including Department of Defense shipments.
[2] Preliminary.
[3] Includes $160,000,000 in transit shipments.
[4] Includes $176,000,000 in transit shipments.
[5] Includes $140,000,000 in transit shipments.
[6] Includes $70,732,000 in transit shipments.
[7] Includes $111,166,000 in transit shipments.
[8] Includes $201,099,000 in transit shipments.
[9] Includes $283,550,000 in transit shipments.

Source: Economic Research Service, U.S. Department of Agriculture.

While we are concerned with the trade policies of some of our trading partners, we must also make sure that our own policies contribute to establishment of trade peace rather than trade war. We have consistently pointed out that trade is not and cannot be a one-way street—and this is true whether it is into or out of the United States. Trade among nations can make a contribution to a more orderly and peaceful world, but we must also not lose sight of the fact that policies to accomplish these objectives will not be meaningful and will not be supported by public opinion unless they deal with the facts of life. Thus, in our view, all countries of the world should work together to help solve some of our trade problems. Each country must shoulder its own responsibilities and not try to shift them to others. We strongly believe that future trade negotiations must vigorously cope with all types of trade barriers—tariff as well as non-tariff—and with all types of commodities—agricultural as well as nonagricultural, on a balanced basis.

Agriculture and Environmental Quality

The need to preserve and restore environmental quality to our life style has surfaced as a major concern of this generation. Unfortunately, accompanying this concern has been a tendency to believe that there are instant solutions to the problem when, in fact, the solutions will take time, money, professional and skilled manpower, and a great amount of patience and understanding. Indeed, those who have recognized expertise caution that it will take years to slow down and level off the downward trend in the quality of our environment as our population continues to expand.

Like all other sectors of industry, agriculture has its share of environmental problems—siltation, pesticides, fertilizers, animal wastes, agricultural processing plant wastes, smoke from the burning of forest slash, and field residues. However, fairness demands that we point out that for many years, and long before the recent surge of environmental concern, soil conservation has been a major activity of both government and individual farmers.

In meeting the problems, value judgments must be made and, therefore, we foresee considerable controversy. The use of pesticides and other agri-chemicals has contributed greatly to the efficiency of production and to the relatively low cost of food to the American consumer. Harmful effects from this use must be weighed against the benefits, and there are aesthetic, health and ecological as well as economic considerations involved. The controversy will be severe enough without aggravating it by failing to carry out the research and obtain the hard evidence needed as a basis for value judgments.

We note that the USDA estimates the cost of controlling pests at over $3 billion annually, with nearly one-fourth of agricultural production still lost as a result of pests. Even with substantial pesticide treatment of corn land, for example, soil insects are estimated to cause losses of $100 million annually to our corn crop. If we had not begun developing the use of modern pesticides back in 1945, the great increase in quality and output-per-acre of agricultural production, with its accompanying consumer benefits could not have taken place—even with advances in more productive seed and plant varieties. It has been estimated by USDA that if all pesticides were withdrawn from farm use, crop and livestock production would drop by 25 to 30 percent, resulting in a boost in prices of 50 to 75 percent. And, of course, there would be an accompanying deficiency in the diet of our people—especially among the poor and lower income groups.

Not to be overlooked are the international trade effects of any increases in cost of our agricultural production. Over and over, our foreign agricultural attaches have repeated that we must be price competitive in foreign markets if we are to maintain, let alone increase, our exports. Restrictions on the use of pesticides could, as the USDA estimates clearly show, substantially increase costs of production and reduce our competitive position unless our trading partners enforce similar restrictions in the case of their own production. We hope that international agreements on the use of pesticides will parallel developments in our own country.

Government Reorganization and the Department of Agriculture

In his March 1 address to a joint session of the Iowa Legislature, the President took note of the changes that have occurred in agriculture while we have had essentially the same Department of Agriculture since 1862. He observed:

> "You've changed and we haven't"—this could become the epitaph for rural America, for the countryside where the Nation's roots are. But to be able to say that you have changed and so have we—that could be the keynote for a new surge of vitality and progress on the farms, on the ranches, and in the towns and the open lands across this Nation.
>
> It comes to a question of whether farmers and others in rural America want an Agriculture Department for its own sake or whether what they really want are things like better farm prices, better technical assistance for agricultural problems, wider development opportunities in rural communities, better schools, better roads, and so on. I think, of course, they want the latter—the results.
>
> Under the present setup, only one Cabinet department represents the farmer in what he wants. And under my proposed reorganization, four Cabinet secretaries—half the Cabinet—will be speaking up for the farmer when his diverse interests are at stake. I submit this is not less representation, but more—and it's more effective representation, because the rural interest of America will be represented wherever decisions are being made that affect that interest.

These are laudable thoughts. If this proposed reorganization would, indeed, help bring about better farm prices and better services and opportunities for rural America—results not achieved under the present organizational structure, then few, and certainly not the farmer, should object. It would be admirable if, by a stroke of the pen or a simple act of Congress, the agricultural segment of our nation would once more be able to share in the economic progress which too frequently has been denied it. But, unfortunately, it isn't that easy, nor that simple.

Our concern is that reorganization legislation be so drafted as not to create another layer of bureaucracy in Washington which would tend to prevent prompt action in the interests of agriculture. As the President remarked, "the patronizing notion that a bureaucratic elite in Washington knows best what is best for people everywhere is completely alien to the American experience." In other words, we are not for a Department of Agriculture for its own sake, but we are opposed to any reorganization proposal that would downgrade our nation's agriculture. While we are confident that there is no intention to do so in the case of the President's reorganization proposal, this is a point that must be tested out during the course of the hearings on the proposal and the subsequent debate in the halls of the Congress.

With the decline in our farming population that has occurred over the past decade, the various segments of agribusiness must join together if farmers and all of rural America are to share fairly in our national development. The President's reorganization proposal appears to have the potential for facilitating this combination through unified and coordinated federal plans and programs affecting not only the producers of food and fiber, but agricultural labor, transportation, marketing, and manufacturing. In the present organization of the federal government and the Congress, too many things have been done without considering the impact on our basic industry of agriculture.

Farmer Bargaining Power

One of the major areas of agribusiness concern continues to be the problem of how farmers can obtain better prices for their products through improved bargaining power. We do not take a position on the various proposals which have been advanced, but we do believe this subject merits thorough consideration by the Congress.

A basic question involved is the proper role of the federal government. Whatever the answer, it would be well to understand that any increased farmer bargaining power could be completely undercut by unsound fiscal, monetary, and foreign-trade policies of the federal government.

As a general principle, the government should seek to bring about conditions under which the marketing of agricultural products can be conducted in the mutual best interests of both agricultural producers and the consuming public. Government can help by providing information, research, and regulatory services that will allow the marketing system to function honestly and responsively.

There are many different ways in which bargaining power for farmers can be improved. The marketing order system could be extended to cover products not now included, although we doubt that this approach would be feasible in the case of the major crops and livestock. Another approach would be to strengthen the legal foundation on which farmers can build their own bargaining associations. Vertically integrated farmer-owned production-processing-marketing organizations already are operating rather successfully. There is probably no simplistic solution to the problem.

Rural Development

At the time of the American Revolution almost 90 percent of the people were farmers. Today, less than 5 percent of all Americans earn their living from the soil. This reversal of the farm population ratio has been accompanied by a decline in the proportion of people living in the smaller towns and cities outside the metropolitan centers.

Seventy percent of our people now live on one percent of the land. Thirty-five percent live in only 25 metropolitan areas. Eighteen percent are concentrated in the 450 mile strip between Boston and Washington. And, if present trends continue, at least three-fifths will be concentrated in but four such giant metropolitan strips by the year 2000.

These patterns of population distribution are a reflection of economic growth trends. The rate of economic growth (as measured by newly created jobs) generally has been the highest in the metropolitan areas. The agricultural technological revolution has drastically reduced farm manpower needs. And in many smaller towns and cities the creation of new jobs has not kept pace with the new additions to the work force.

The economic and technological forces which have fueled this great gathering in of people and industry represent a form of progress. But the festering slums, the stultifying and sprawling suburbs, the abandoned farms, and stagnating rural towns are damning testimony of our failure to diversify this progress throughout the entire population.

Increasingly during the 1960's we have come to recognize that this mal-distribution of our population is attended with economic inefficiencies and social liabilities at each end of the population distribution scale.

Thus, in 1970, the Congress committed itself to achieving "a sound balance between rural and urban America" (Pub. Law 91–524, Title IX).

Achieving the goal of balanced economic and population growth in the decades ahead will not be easily or quickly realized and the policy components will be varied and complex.

Although there is much that we do not know about the development process, we do know that it occurs only over a long period of time and that the more economically depressed the area, the more difficult and costly is the redevelopment task. Thus we will save time and money by seeking to stimulate the economies of underdeveloped areas before they are allowed to sink into paralyzing poverty.

We also know that two basic components of the development process are (1) new jobs and (2) improved community infrastructure. There is a "chicken and the egg" relationship here. It is difficult for a community to attract new job-creating industries unless it has an adequate infrastructure. But improvements in the infrastructure cannot be readily financed and maintained unless accompanied or preceded by increased economic activity.

Finally, it is evident that because the development process is so complex and multi-faceted, successful rural area development cannot occur without comprehensive administrative structures for planning and coordination. The devlopment process must involve the individual citizen, private enterprise, local, state, and federal governments. Thus an organizational structure capable of energizing these various components, assuring their coordination, and maximizing the value of their representative inputs is essential. We applaud the high priority given by the Administration to rural area development.

Conclusions and Recommendations

1. More than ever before, bipartisanship is needed to help resolve the problems facing the agricultural sector of our nation. The political parties should ask, "is this good for agriculture," not "is this good for the Party."

2. The future of agriculture is tied to the improvement of net farm income. Commercial farmers ought to be able to earn sufficient income from their farming operations without having to turn to off-farm jobs to make a decent living for their families. Consumers must become more aware of the inadequate returns farmers are receiving from their labor and investment.

3. Inflation aggravates the cost-price squeeze on farmers, and those in control of the Congress should cooperate with the Administration in action to slow it down and stop it.

4. The Department of Agriculture should administer farm programs to maximize the net return to farmers. The Department should be especially careful to avoid new surpluses of farm products.

5. Improvement of our agricultural balance of trade is vital to the well-being of our farmers. The Administration should continue and increase its efforts to persuade our trading partners, such as the Common Market bloc, to modify their internal policies to permit greater access for our competitive agricultural commodities and to, thereby, lower the costs of their own consumers.

6. Our own foreign trade policies should be so constituted as to contribute to the expansion of world trade. Our Food-for-Peace program should be continued at or near current levels, with careful scrutiny given to assure that the purposes and objectives of the program are carried out in the manner the law intended.

7. In future trade negotiations, efforts should be made to cope with all types of trade barriers—tariff as well as nontariff—and any agreement so negotiated should be fairly balanced between agricultural and nonagricultural products.

8. No reorganization of the Executive Branch affecting the Department of Agriculture should be approved unless it is clearly demonstrated that it will have a beneficial effect on the agricultural sector of our economy.

9. It is in the interests of both the farmer and the consumer that great care be taken in making value judgments involved in barring or restricting the use of pesticides and other farm chemicals which have contributed so greatly to the productivity of our agriculture. These value judgments should be based on hard evidence derived from adequate research.

10. Farm programs and other policies of the federal government should be harmonious with the goal of improved farmer bargaining power.

11. We must move rapidly in our goal of rural development in order to achieve a more balanced economic and population growth. To accomplish these objectives:

a. Special economic inducements should be used to encourage the location of job-creating industries in rural areas;

b. Greater urgency and funding is needed for programs designed to strengthen the infrastructure of rural areas (water and sewer systems, health services, housing, transportation, utilities, etc.) to provide a base for economic growth;

c. Wherever practicable, the awarding of federal government contracts and the establishment of federal installations should favor rural areas and communities in order to reverse the trend towards greater congestion in our metropolitan areas;

d. Manpower training programs in rural areas should be strengthened and employment and counseling services to rural residents should be improved;

e. Steps should be taken to expand and improve rural area planning and development administrative structures. Existing structures should be strengthened and where they are lacking, special inducements to bring them into being should be devised.

NATIONAL GOALS AND PRIORITIES

Political rhetoric throughout our country's history has focused from time to time on the nature of our national goals and priorities. Usually the debate has sharpened during periods of national crisis or self-examination, such as war-time, or at some other major historical event. One such time is the present. For the past five years, the Minority of this Committee has consistently referred to the need to reorder our priorities; in so doing we have reflected the voice not only of political leaders but of our constituents as well.

Although the experience of Vietnam has intensified the debate on goals and priorities, other factors have generated interest in the subject as well. Our affluence—once a goal in itself—has undoubtedly been a major factor in the current debate. For the first time in our history, many Americans see us capable of achieving the kind of goals that require large commitments of our resources. Our success at placing a man on the moon prompts the question whether we could not have similar success at eradicating poverty in America. Our affluence also puts in sharper contrast the conditions of those who have been denied the economic benefits of American society.

Perhaps the most useful by-product of the current debate, and another factor stimulating it, is the scholarship generated by the national interest in goals and priorities analysis. For example, the attempts by the Council of Economic Advisers in the last two Annual Reports to describe our future national output and the potential claims on it are a significant addition to our knowledge about national goals and our ability to reach them.

This chapter is an attempt to carry the analysis one step further, and to relate it to the issues discussed in our Minority Views. Although it is mainly descriptive, one cannot help but conclude—as this chapter does—that Congress needs better tools with which to engage in the priorities allocation process.

What are our national goals? One concise response to the question is given in the Preamble to the United States Constitution, which states in part, "to form a more perfect union, establish justice, insure domestic tranquility and to provide for the common defense." However, conflicts arise within these goals. Governments must often balance considerations of common defense against individual justice. The broad decree of the Constitution thus gives rise to the problem of what is the best way to go about fulfilling our national goals, and points out the relationship between defining goals, on the one hand, and setting national priorities, on the other.

The priorities problem is a matter of deciding which are the most valuable uses to make of our total resources, which are limited and therefore insufficient to meet all of the possible claims that may be made upon them. A comprehensive approach to the problem does not distinguish between public and private or Federal and non-Federal sectors, even though the Federal budget provides the framework for priorities decisions and significantly affects non-Federal sectors of the economy. This is because our resources include not only the budget but all national output.

The interactions of the various sectors of the economy—and, by implication, the commanding role of the Federal budget—were explained by Council of Economic Advisers member Herbert Stein in testimony before the Joint Economic Committee last June:

> 1. Federal transfer payments to individuals affect the volume of private consumption and its distribution by income groups and other categories of persons.
> 2. Federal grants-in-aid affect the amount and composition of State and local expenditures.
> 3. Federal provision of services or facilities, such as highways, compete with and discourage some non-Federal expenditures while they complement and encourage other non-Federal expenditures.
> 4. Federal taxes profoundly affect the character of private resource use.
> 5. The relation between total taxes and expenditures—the size of the surplus or deficit—affects the volume of funds available to private, state and local borrowers, and consequently affects their investment.
> 6. Loans by the Federal Government, or by federally-sponsored agencies, and interest subsidies and guarantees affect the direction and possibly also the total amount of private investment.
> 7. Laws and regulations of the Federal Government require private expenditure of certain types. For example, air pollution regulations require private businesses to invest in certain purification equipment.

In this context government expenditures, taxes, loans, subsidies, guarantees and regulations should be considered the means through which we allocate the national output in the pursuit of our goals.

Attempts to point out our important national goals have been made in the past. In 1960 a program of action for the sixties was outlined in a report entitled *Goals for Americans* written by President Eisenhower's Commission on National Goals. A decade later, in July of 1970, President Nixon's National Goals Research staff published *Toward Balanced Growth: Quantity with Quality*. Both of these reports were predominately efforts to outline what priorities should have been in the sixties and what they should be during the 1970's, and as such, described areas of national interest which need improvement and upon which attention should be focused. However, they made no attempt to compare the costs of our goals and their long-range effect on our available resources.

One excellent feature of the CEA Report the past two years has been a section which projects the nation's output in the future and those claims which have been and will be made upon it.

According to this year's Report, with the assumptions being made that our tax structure will not be changed and no new programs will be inaugurated, the Federal government should have a surplus of $32 billion (1969 dollars) on a national income basis, five years hence in 1976. During that year federal expenditures would approximate $217 billion and revenues $249 billion.

However, these figures do not imply that we will have $32 billion of "free" funds with which to develop new programs to meet the needs of the American people, for we must take a look at the overall picture. Gross national product in 1976, making the assumption that by that time we will be following the path of full employment, is projected at $1251 billion. An estimated $1232 billion of that total will be pre-empted by government purchases already committed and by the claims of the private sector, which implies "slack" of $19 billion in what the economy is capable of putting out at full employment during that year. This compels the conclusion that, using a balanced full employment budget as a gauge for prudent policy decisions, there probably could well be an excess of potential claims on the GNP over the next 5 years, not all of which would be met. These excess claims could be reduced in a number of different ways, possibly by a lighter monetary policy or possibly by inflation, but all with the same effect of reducing the claims to potential output.[1]

We feel it imperative to discuss these long-range implications. As the President said in his 1971 Budget Message:

> A budget must be a blueprint for the future. In the 1971 budget, I seek not only to address today's needs, but also to anticipate tomorrow's challenges. Only with a plan that looks to the years ahead can we gain control over the long range use of our resources, and mark a clear course for meeting national goals. (See p. 7, 1971 Budget Message.)

The blueprint which our best estimates picture is that between now and 1976 we will have $44 billion which may be allocated for new programs to meet the needs of the nation. That is, this $44 billion is a rough measure of what we have to expand existing programs, to create new ones, to retire the national debt or to decrease taxes and put more money into the hands of the consumer. This figure of $44 billion (in 1969 prices) is arrived at by subtracting the claims against the GNP each year projected over the next five years against the dollar figures given for what gross national product is estimated to be during each of those years and combining these figures. This table below summarizes this estimate.

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[1] It should be recognized that the budgetary costs of a program do not translate dollar for dollar into claims on the GNP. In some cases, such as loan subsidies, the dollar impact on GNP claims is greater than budgetary impact. In other cases, such as repayment of the national debt, the dollar impact on GNP claims is probably smaller than the budgetary impact.

AVAILABLE GNP AND CLAIMS ON AVAILABLE GNP, 1971–76

[Billions of 1969 dollars]

	1971	1972	1973	1974	1975	1976
GNP Available	971	1040	1102	1150	1199	1251
Total Demand	971	1038	1098	1142	1188	1232
Federal Purchases	85	85	85	84	83	83
State & Local Purchases	120	128	133	136	140	144
Consumption	621	665	708	740	768	802
Gross Private Invest	142	157	170	179	192	198
Business Fixed Investment	97	106	115	121	128	134
Residential Construction	38	43	45	47	52	52
Change in Inventories	7	8	10	11	12	13
Net Exports	3	4	4	4	5	5
Unallocated Resources	0	2	4	8	11	19

Source: Council of Economic Advisers

This Table was provided by the Council of Economic Advisers with the following explanation:

The attached table lists GNP and its components by calendar years. These projections are made on the basis of two sets of information: (1) the near-term outlook is based on the policy path with a $1065 B nominal GNP; (2) the long-term outlook (1975–1976) is based on a long-run average behavior for the private sector, the achievement of certain goals such as the housing goal, and a projection of current levels of existing programs and new programs in the FY 1972 budget. The intervening years, 1972, 1973 and 1974, are based on a simple interpolation of the 1971 and 1975 years for all GNP components not controlled by Federal Government policies.

The shape of the real GNP path in these projections should not be interpreted as a policy path or as a forecast. The principal reason for this is that very little is known about the behavior of private demand in any two to four year forecast. A two to four year time span is too long for any reasonable statements about the cyclical characteristics of GNP and its components while this time span is too short to rely on long-run average behavior of GNP and its components.

Consequently, the projections for 1972–1974 should be regarded as a convenient link between the short-run and the long-run average behavior and not as a forecast or policy target of the Administration.

Previously, the budget messages of former Presidents never presented any type of 5-year projections for fiscal revenues and expenditures, nor projections on the long term use of national resources such as we have seen in the CEA reports and the Budget Messages since President Nixon came into office. What this means, apparently, is that when programs were formulated during the early 60's little or no thought was given to their implications in later years.

In 1964 when the poverty program was chartered under President Johnson's "Great Society", for example, few planners could have realized what a large percentage of the budget in 1969—five years later—this project would involve. Coupled with spending for the Vietnam War, which obviously was not an item which forecasters took into account early in the 1960's, the gigantic full employment deficit was created which led us into the serious inflationary spiral the economy encountered after 1968.

In estimating that we will have approximately $44 billion to utilize in new programs over the next five years, what is obvious to us is that those funds cannot begin to cover the costs of the many programs which Congress has *already* proposed, much less any others that may be espoused in the course of the next five years.

In the area of defense spending alone, one could find proposals which would involve expenditures of over $80 billion dollars if the projects were to be completed within the five-year time frame.

Since the largest single category of expenditure the federal government makes is defense, it is imperative that we examine the implications of the dollars spent on this category versus money poured into other areas, recognizing that over half this spending is for salaries and manpower. Our major concern must be that the money we are planning to spend on defense yields us sufficient benefits in terms of a necessary level of national security. In examining these implications CEA Chairman Paul McCracken has said that "decisions about national priorities should result from comparisons of all the alternatives, not from comparisons of an arbitrarily selected class of alternatives. Thus, it is not sufficient or even helpful to ask only whether a billion dollars of expenditures for defense is more or less valuable than a billion dollars of expenditures for, say, urban programs. The answer to this question would not tell us whether one of these programs should be increased and the other decreased unless we also know the value of still other expenditures that are also alternatives to both. Basically the priorities problem is to allocate the national output among all its uses, not to allocate some smaller amount of money between national defense on the one hand and urban-poverty programs on the other." What this statement means is that we must, in our Federal and private budgets, choose the best combination, or "mix" of programs we can to utilize the resources which are available to us.

If Congress appropriated funds for all feasible military projects it is easy to see that there would be no money left for the many human resource projects that are being advocated. Selecting only a few nonmilitary programs which some Senators and Congressmen have proposed, a conservative figure of $19 billion would be the total cost for such new items as a supersonic transport, adequate child-care centers for only one-third of our low-income families, a public sector job program that could make a significant contribution toward alleviating our unemployment problem and fully appropriating the funds that have already been authorized by Congress for grants-in-aid for states and cities.

In the Economic Report the Council has named nine basic segments of the economy which absorb our Federal outlays. They are: basic necessities (food, clothing, etc.), education and manpower, health, transportation, government expenses, defense, and new housing. The Report gives us a breakdown of the percentage of Government expenditures which each of these categories represented in 1955, 1966, and 1969.

What is evident from this table in the Report and the budgets for Fiscal years 1970, 1971 and 1972 is that the budget has, through the last decade and a half, changed the "mix" of claims on the GNP to which the Federal Government is responding. More and more we are picking up a larger percentage of the costs of education, manpower and health programs. Defense claims have declined as a total percentage of GNP over the decade. Moreover, for fiscal year 1971—the first time in twenty years—the Administration's budget requested more outlays for human resources programs than for defense, and the relative percentage for human resources is projected to increase for fiscal year 1972. We believe that the greater amount of Federal expenditures that are being channeled more and more towards fulfilling human needs is a significant accomplishment of this Administration.

The exact portion of expenditures the Government should make between the various items of federal expenditures is an unanswerable query. Honest differences inevitably exist as to which need is the most pressing.

Therefore, the single most important economic concept to understand in a discussion of national priorities goals is that of opportunity costing. Giving priority to one goal rather than another is a way of saying the benefits of that goal exceed those of another. If we commit huge funds to the health area, that leaves less to be divided among education, welfare, environment, housing, transportation and the like. In determining which programs to implement towards reaching a specific goal, we must ask whether these benefits are better than those which might be derived by pursuing another program. For example, what would be the trade off between committing a large number of dollars to a manpower training project, compared to committing the same amount to an education program? Both programs would contribute to the effective productivity of future members of the labor force. But assuming we haven't the funds to implement both, we must decide which of the two proposals will make the greater contribution to the ultimate goal—improving the work force; or whether some funds should go to each.

All goals must be evaluated in terms of the nation's total requirements, and ultimately, all proposed Federal commitments of resources must be analyzed and decided by Congress. Senator Percy recently stated that "Congress is ill-equipped now, however, to set overall priorities due to the way the legislative process is set up. Each bill and appropriation is handled separately with no real attention given as to how each piece of legislation fits into an overall framework of needs and resources available."

The problem of budget-making is compounded into the priorities problems. Congress has always been reluctant to fund fully a new project or program. In appropriating money for any one project to commence operations. Congress leaves open the amount that will be poured into the project in future years. According to the CEA projections of the 1976 level of unallocated resources, we will have $19 billion available—assuming a full employment GNP of $1251 billion, no change in present and programmed tax legislation, and no new programs aside from outstanding proposals of the Administration being inaugurated between now and 1976. Of course, this is a theoretical assumption since many new programs will probably be enacted during this five-year period. But the important thing for priorities planners to remember is that each new program that is begun is likely to reduce both the 32 billion budget surplus and 19 billion level of unallocated resources.

Congress historically has followed the pattern of enacting legislation and then partially funding at the time of its adoption. It then continues to fund the legislation during subsequent years making appropriations decisions yearly on an *ad hoc* basis. The problem is easy to see: How can we estimate the impact of prior legislation on fiscal estimates of revenues and expenditures that are projected five years in advance when the incidence of the legislative decree may fall entirely within a one-year period, or may be amortized at unknown amounts throughout the five year period. In correcting this procedure, by committing funds several years in advance, the planning procedure would be both more facile and more efficient. Such commitments would apply to both military and non-military programs. Public Law 86-801 clearly states that each substantial new piece of legislation proposed by the Administration be accompanied by a statement of its budgetary costs over a 5-year period, so that Congress could indeed approve and appropriate these long-range costs; but this act has not been followed in practice.

These arguments all point up the need for a planning organization that would be responsive to the Congress and can advise it in making these difficult decisions. An Office of National Goals and Priorities Analysis, as proposed by Senator Javits, would be responsible to the Congress, would attempt to cope with problems of diffusion that plague priorities planners, and would do away with the piecemeal approach that has heretofore been taken. It has been suggested that a five-year projection of domestic program decisions should be inaugurated comparable to the five-year defense posture statement put out by the Defense Department. Such a program would serve only to further the lack of integration which exists between defense and non-defense planning. But an Office of National Goals and Priorities Analysis could also estimate a five-year plan assimilating the total planning issue.

There are several other planning measures which could be adopted that would expedite the long-run efficiency in the use of our resources. One such consideration would be the adaption of an appropriations session of the Congress to replace the piecemeal and inefficient way in which appropriations are now considered. This problem is also complicated by the present system of offering the budget on a fiscal rather than a calendar year basis. When the Administration presents its Budget to Congress in January, it refers to a fiscal year beginning that July, and Congress has only 5½ months to appropriate the funds it deems reasonable. The Executive branch cannot effectively and economically allocate resources if it does not know what those resources will be. And until Congress has completed its appropriations calendar, this is the situation that prevails.

Finally, a program budget should be drawn up to show not only direct budget outlays, but also revenues foregone by the Treasury as a result of special provisions in the Internal Revenue Code and Government-assisted credit programs. A recent estimate by Assistant Secretary of the Treasury Wiedenbaum concluded that selected special tax provisions will cost the Federal Government more than $45 billion in Fiscal Year 1971. These outlays and subsidies should be matched against the estimated economic and social benefits that flow from them for, as Senator Miller has pointed out: "many tax savings provisions in the Internal Revenue Code were put there deliberately by the Congress for economic and social reasons—for example the deductions for real estate taxes and mortgage interest payments to encourage home

SUPPLEMENTAL VIEWS OF SENATOR JAVITS

Domestic Economic Issues

(a) *Incomes Policy*

To me the prime practical action now is pursuing an effective incomes policy to restrain inflationary price and wage increases. In its testimony, the CEA described the efforts of the Administration in this area, concluding that it was presently considering ways to make its efforts "more systematic and comprehensive, and to provide more adequately for their management."

I believe that a high level Wage and Price Board, such as has been proposed by many economists including some Government officials, would provide the "systematic and comprehensive" approach which the Administration seeks. Such a Board, consisting of three Presidential appointees chosen from private life, should be mandated with developing the ad hoc steps which the Administration has already taken into an across-the-board (and, therefore, more equitable) set of policies for keeping price and wage increases within acceptable limits. As such, its primary function would be to recommend action to the President, but the Board should also be given the power to hold hearings and conduct investigations with respect to significant price/wage actions as well as structural market inefficiencies. Obviously, a considerable amount of such a Board's power would be its ability to inform the public about inflationary price/wage actions. I also believe that the establishment of such a Board would lend weight to the Administration's determination to cool inflation. Because the emergency of price inflation is hopefully of a temporary nature, the Board itself could be made temporary.

(b) *Fiscal and Monetary Policies*

The Minority Views contain many fine recommendations for policy in 1971, and I support these Views except where noted by footnote. The other parts of the Minority Views contain excellent analyses and recommendations with regard to productivity, corporate liquidity, transportation, agriculture, rural development, etc. However, they do not give enough emphasis to the overriding issue for economic policy this year: relieving our unacceptably high levels of unemployment while dampening down serious inflation.

The President's 1971 Economic Message stated it well, that "Our first task now must be to assure more rapid expansion and so to reduce the unemployment rate." This task will require more emphasis on policies to stimulate the economy that has been given in the Minority Views.

For example, in describing a target of $1065 billion GNP for 1971, or a rise of 9 percent over 1970, the Administration has set an appropriately ambitious goal. With productivity gains, growth in the labor force and inflation accounting for at least 8½ percent of GNP rise this year, the 9 percent figure appears in fact to be the lowest goal consistent with a policy of reducing unemployment.

But the implications of this state of affairs for fiscal policy are clear: fiscal policy should be stimulative, and also expansionary enough to generate confidence about the Administration's commitment to a substantially higher economic growth rate this year.

In this setting, the President's budget proposals for fiscal year 1972 cannot be criticized as overly expansionary; indeed, I seriously question whether they are expansionary enough.

Federal expenditures on the National Income Account (NIA) basis are expected to rise less in fiscal year 1972 than in the present year. Federal sector purchases of goods and services, which add directly to GNP, are not expected to vary significantly from the past fiscal year (although it is only fair to point out that this is attributable chiefly to cutbacks in the defense budget, a trend which I approve and which can be achieved without any diminution of national security). More important, the NIA full employment budget surplus as originally proposed is not expected to change from 1971 to 1972, according to testimony from the Committee on Economic Development, which developed the full employment budget concept. This compares with the Council of Economic Advisors' own analysis in the Economic Report that "Changes in the full employment surplus from period to period are much more important indicators of how fiscal policy is moving toward contraction or expansion."

For these reasons, I regard the fiscal policy proposals in the President's budget as tentative. Fiscal policy must remain flexible and be able to respond immediately if the goal of a more rapid rate of economic expansion—with all this implies for lowering the unemployment rate—appears to be getting out of reach. Consequently the arguments for advancing the date for tax reductions under the 1969 Tax Reform Act, or postponing action on raising the base for Social Security taxes may well prove to be persuasive; for the same reasons, I believe the Congress acted wisely in recently raising Social Security benefits.

With regard to monetary policy, I am confident that the Federal Reserve Board, to paraphrase Chairman Burns' testimony, will not become the architect of a new round of inflation. This is the proper approach for the Fed. The question must be asked, however, whether this approach will result in a monetary policy which is stimulative enough to accomplish the goals of economic growth and reduced unemployment. Obviously we cannot expect much stimulus to come from the Fed if the danger of renewed inflation is too great; on the other hand, the testimony of the Council of Economic Advisors before the Committee implied that monetary policy would have to be relatively expansive if the Administration's economic policy goals are to be met.

(c) *Revenue Sharing*

With regard to revenue sharing, I believe that the degree of the present crisis in state-local government finances requires a vastly expanded revenue sharing program. I recently submitted an amendment to the President's General Revenue Sharing bill which would double the amount of money to be shared, and would advance the starting date. This would yield a $10 billion Revenue Sharing Program during its first year of operation, a figure which the Committee has heard will provide only half the additional revenues needed by states and localities to maintain the inadequate service which they are now providing.

(*d*) *Public Sector Jobs*

Manpower policies to complement this order of economic priorities should place increased emphasis on job creation measures. A Federally funded public sector jobs program for state and local governments would be a logical response to America's joblessness problem; for in addition to making a dent in unemployment, it would provide state-local government with sorely needed manpower in essential fields such as health, teaching, law enforcement and environment. Since unemployment, as well as the condition of state-local government services, have become crises of national proportions, it is essential that the Federal Government specify funds and provide guidance to ensure the effective establishment of public sector jobs programs, rather than to assume that these problems will take care of themselves.

International Economic Issues

It is perhaps symbolic of our times that the section dealing with international economic issues mentions only in passing the development assistance programs of the United States.

Nor, does it mention at all the remarkable achievement of the nations of the world during the 25th Anniversary Session of the United Nations in hammering out an international strategy for development acceptable to all nations of the world.

In turn this section also fails to mention that the United States has joined with the other developed nations of the world in support of a scheme to extend non-reciprocal, non-discriminatory generalized tariff preferences to the developing countries of the world. Legislation giving the Administration the authority to participate in this preferences scheme will be before the 92nd Congress.

Finally, this section accords scant treatment to the important role of U.S. private investment in the world. The rapid growth in private U.S. foreign investments and the importance of these investments to the continuing health of our economy increasingly demands the attention of the Adminstration and Congress.

(*a*) *The Second Development Decade*

One of the most serious problems facing mankind is the growing economic gap between the vast multitudes in the developing countries of the world and the minority of people living in the nations of the developed world.

The growing numbers of "have not" peoples in the world who now, because of the miracles of modern communications, are fully aware of their disadvantaged position is a matter to which we cannot remain indifferent. We must continue in our attempts to bridge this gap, because of humanitarian reasons, but also because the long term well being and security of our nation may depend on this. It is clear that squalor in refugee camps in Asia and the Middle East makes more difficult the search for peace in these areas of the world. It is equally clear that economic grievances and misery must be ameliorated if future generations of Americans are to live in peace and harmony with their neighbors in the developing world. It is also clear that over the long run, the United States will become increasignly dependent on the natural resources located in the developing world as the pace of our industrial society depletes the resources found on our continent. And most important of all—the world is increasingly interrelated and interdependent with the result that a world order condemning two thirds of the human race to misery is not likely to long endure.

The 25th Anniversary Session of the United Nations came to grips with this problem. At a special meeting held on October 24, 1970 to commemorate the twenty-fifth Anniversary of the United Nations, the General Assembly adopted a document on the International Development Strategy for the 1970s—the Second Development Decade. This strategy document sets forth a comprehensive and integrated program of national and international action toward the end of promoting economic and social development.

An important element of the strategy was the affirmation by the governments of the developed countries to transfer more real resources to the developing nations. I had the privilege as the United States Representative to the United Nations to announce that the U.S. Government would make its best effort to achieve an aid target of the transfer of resources, public and private, equal to one percent of our Gross National Product. When we spend approximately 7 percent of our GNP to fuel the engines of our machinery of war, is it too much to hope that we will someday spend 1 percent of our GNP to help build a better and more stable world order?

The Congress must also make a commitment in the days ahead, unless we have indeed turned neo-isolationist—which I do not believe. Additional funds will have to be authorized for the Inter-American Development Bank and the Asian Development Bank; and a Third Replenishment of the International Development Association is coming due. In all these institutions, burden sharing is the name of the game, and the U.S. is being asked to join with other developed nations in promoting economic development. It would be indeed ironic if just at the time when other nations are increasingly willing to pick up their fair share of the burden, that the United States falters. I believe that our people and particularly our young people will respond positively if they realize most of the other developed countries of the world now transfer more per capita assistance to the developing world than does the United States—even though these countries are not as rich in production as the United States.

(b) *Reorganization of U.S. A.I.D. Programs*

The 92nd Congress will soon have before it proposals of the Administration to reorganize our domestic development assistance (AID) programs. Under the distinguished leadership of Rudolph Peterson, a Presidential Task Force reviewed the AID programs and made its recommendations to the President and the Congress. These carefully thought out recommendations include the separation of development assistance security assistance, a greater channeling of assistance through multilateral institutions and greater cooperation with the multilateral institutions in the programming and channeling of our bilateral assistance, and an organizational restructuring of the AID. The President's legislative proposals for the implementation of these programs will soon be before the Congress. They are deserving of the Congress' earnest and sympathetic consideration.

(c) *Generalized Preferences Scheme*

On October 13, 1970, over 120 nations, members of the United Nations Conference on Trade and Development (UNCTAD), approved the proposals of 18 developed nations including the United States as providing the basis for a mutually acceptable system of non-reciprocal, non-discriminatory generalized tariff preferences of benefit to the developing countries. At that time, the intention of the developed countries to seek the necessary legislative actions as rapidly as possible was noted. President Nixon announced on October 31, 1970 that the United States would press for the establishment of a liberal system that would confer maximum benefits on all LDCs.

The U.S. proposal, which will soon be submitted in legislation, calls for a generalized preference of duty-free treatment on most manufactuers and semi-manufacturers produced in the developing countries (excepting textiles, shoes and petroleum products) and on a selected list of agricultural and primary products. Other proposals by developed countries also call for the elimination of duties on a broad range of products; thus while the proposals of the different developed countries differ somewhat in form, they are designed to achieve comparable results.

In an attempt to halt the proliferation of preferential arrangements and to end some of the discrimination that now exists in world trade, the U.S. proposal requires developing countries now granting reverse preferences (i.e. the trade preferences some developing countries grant to some develop countries), to give adequate assurances that those preferences will be phased out in a reasonable time before the developing countries concerned can benefit from the new U.S. preferences. In addition, the implementation of generalized preferences will go a long way toward reducing the discrimination among developing countries that now exists because of special preferences that favor some developing countries at the expense of other developing countries, i.e. Latin American countries that presently do not enjoy preferential access to any developed country market.

As the Congress considers this legislative proposal, we should be aware of the stakes. This may be the last chance for an open trading world—and an open trading world is very important for our exports—particularly our agricultural exports. If the generalized preferences scheme fails of Congressional passage or if European nations kill such a scheme by failing to phase out over a suitable period of time the reverse preferences being accorded them, the world will go regional—and protectionist. I would ask our European friends to reflect carefully on the implications of the United States moving into a closer regional association in this hemisphere and in the Pacific as they make their decisions on reverse preferences. In turn, the Congress should be aware that there is a link between the generalized preference legislation which will soon be before it and the possibility of effecting changes in the Common Agricultural Policy of the EEC and the proliferating preferential tariff arrangements which are discussed in detail in the section of this report on Agriculture and Rural development.

JACOB K. JAVITS.

COMMITTEE AND SUBCOMMITTEE ACTIVITIES IN THE PAST YEAR

The Employment Act of 1946 (Public Law 304, 79th Cong.) requires that the Joint Economic Committee file a report each year with the Senate and House of Representatives setting forth its findings and recommendations with respect to each of the main recommendations made by the President in the Economic Report. The statute requires filing by March 1, but in view of the late convening of the Congress this year and the fact that the President's Economic Report was submitted later than usual, the filing date was extended to April 1. This report is submitted in accordance with that requirement. It is intended to serve as a guide to the several committees of the Congress dealing with legislation relating to economic issues.

The terms of the Act require the President to set forth in his report to the Congress, among other things, current and foreseeable trends in the levels of employment, production, and purchasing power; a review of the economic program of the Federal Government; a review of economic conditions affecting employment in the United States; and a program for carrying out the policies of the Act, together with such recommendations for legislation as he may deem necessary or desirable.

The work of the full committee and the subcommittees for the past years is summarized below:

FULL COMMITTEE

January 1970 Economic Report of the President

On February 16, the Committee began 7 days of hearings on the 1970 Economic Report of the President. Testimony was received from the Council of Economic Advisers, the Director of the Bureau of the Budget, the Chairman of the Board of Governors of the Federal Reserve System, the Secretary of the Treasury, the Secretary of Labor, academic experts, representatives of business and economic research groups, and other experts. The printed record of the hearings, in three parts, contains in the final volume invited comments from organizations representing bankers, business, labor, agriculture, and private research groups.

The 1970 Joint Economic Report

The annual report of the Committee was filed with the Congress on March 25, the March 1 deadline having been extended by P.L. 91–188. The report also contains a statement of Committee agreement, minority, supplementary, and dissenting views.

The 1970 Midyear Review of the State of the Economy

In July, the Committee undertook a broad-scale, in-depth review of the state of the economy with 12 days of hearings. Testimony was received from the Chairman of the Securities and Exchange Commission, the Antitrust Division of the Department of Justice, the Chairman of the Federal Trade Commission, the Council of Economic Advisers, the Director of the Office of Management and Budget, the Secretary of the Treasury, the Secretary of Labor, the Chairman of the Board of Governors of the Federal Reserve System, Members of Congress, representatives of labor and industry, bankers, academic experts, and private economic research consultants. The printed record of the hearings is contained in three parts.

The Economy, Energy, and the Environment

On September 1, the Committee released a background study on "The Economy, Energy, and the Environment." This study surveys the major existing literature concerning the growth and composition of energy conversion and its environmental impact, with primary emphasis on electricity generation and the fuels for this industry. The study was prepared for the Committee by the Environmental Policy Division of the Legislative Reference Service under the direction of Richard A. Carpenter.

SUBCOMMITTEE ON ECONOMIC PROGRESS

The Subcommittee continued its review of financing requirements of communities and also conducted staff review of energy requirements of the United States in relation to growth.

Members of the Subcommittee on Economic Progress were Representative Wright Patman, Chairman; Representative Martha W. Griffiths, William S. Moorhead, W. E. Brock 3d, and Clarence J. Brown; and Senators William Proxmire, J. W. Fulbright, Herman E. Talmadge, Len B. Jordan, and Charles H. Percy.

SUBCOMMITTEE ON ECONOMY IN GOVERNMENT

Economic Analysis and the Efficiency of Government

Resuming its hearings on economic analysis and government efficiency, the Subcommittee held 6 days of hearings in May focusing on direct Federal expenditure on different types of transportation. Three days were devoted to an examination in detail of the highway program, and three days concentrated on the supersonic transport. Testimony was heard on the fundamental economic principles which should underlie a rational approach to the allocation of Federal transportation investment and the adequacy of present Federal procedures for making investment decisions. The influence of Federal expenditure policies on the allocation of State and local, as well as private investment, was also explored, together with the adequacy of our procedures for insuring that Federal decisions reflect the real wants and needs of the affected communities. Witnesses were administration officials, State government officials, Members of Congress, former government officials, businessmen, academicians, and other experts. These hearings are contained in two parts, entitled "Supersonic Transport Development" and "Federal Transportation Policy."

Federal Transportation Expenditure

In August, the Subcommittee issued its report based on the above hearings. The report makes recommendations concerning the supersonic transport development program, the Federal-aid highway program, and the general process by which transportation expenditure decisions are reached.

The Acquisition of Weapons Systems

On May 20, 21, and 23, the Subcommittee held hearings to explore the causes of and potential solutions to the problems of cost over-runs. Testimony was received from official spokesmen for the Army, Navy, and Air Force, the General Accounting Office, and former officials of the Department of Defense. These hearings are Part 2 of the series on "The Acquisition of Weapons Systems."

Changing National Priorities

The second set of hearings in the series of annual inquiries on the topic of national priorities was held for 8 days in June. The focus of these hearings was on shifting resource allocations to areas of greatest need, the proper roles of the executive and legislative branches in the decisionmaking process, and the feasibility of post-war planning. The Subcommittee received testimony from government officials, academic experts, and representatives of labor and economic research groups.

Economy in Government Property Management—Procurement of Data Processing Equipment

As a follow-up to hearings held in 1966 and 1967, on July 1 the Subcommittee held a hearing on government procurement of data processing equipment. As a result of the previous hearings, millions of dollars have been saved by bringing small manufacturers of data processing components into the data processing procurement system. Witnesses were the Comptroller General, representatives of the Bureau of the Budget, General Services Administration, Department of Defense, and private industry.

The Federal Criminal Justice System

Three days of hearings were held in September and October focusing on ways in which the Nation's criminal justice resources might be more effectively utilized to reduce the incidence of serious crime. This examination of the criminal justice system represented part of the Subcommittee's ongoing effort to apply principles of economic analysis to questions of efficiency in Government. Witnesses were a Member of Congress, a representative of the Law Enforcement Assistance Administration, the New Haven Chief of Police, and academic experts.

Members of the Subcommittee on Economy in Government were Senator William Proxmire, Chairman; Senators John Sparkman, Stuart Symington, Len B. Jordan, and Charles H. Percy; Representatives Wright Patman, Martha W. Griffiths, William S. Moorhead, Barber B. Conable, Jr., and Clarence J. Brown.

SUBCOMMITTEE ON URBAN AFFAIRS

Housing Development and Urban Planning: The Policies and Programs of Four Countries

In March the Subcommittee released its report based on the fact-finding trip taken by members of the Subcommittee to Great Britain, Finland, West Germany, and Israel to study policies and programs relating to housing development and urban planning.

Regional Planning Issues

On October 13, 14, and 15, the Subcommittee held hearings on regional planning issues in order to reach an understanding of how to adapt our political structures to facilitate planning to solve economic and social problems on whatever regional basis proves desirable in a particular case, while at the same time retaining a maximum of local and even neighborhood political power. The Subcommittee heard testimony from experts in economics and political science.

Members of the Subcommittee on Urban Affairs were Representative Richard Bolling, Chairman; Representatives Henry S. Reuss, Martha W. Griffiths, William S. Moorhead, William B. Widnall, W. E. Brock, 3d, and Clarence J. Brown; Senators Abraham Ribicoff, William Proxmire, Jacob K. Javits, and Charles H. Percy.

SUBCOMMITTEE ON INTER-AMERICAN ECONOMIC RELATIONSHIPS

Thrift Institution Development in Latin America

In June the Subcommittee released a staff study on the development of thrift institutions in Latin America. The study traces the development of savings and loan institutions and credit unions in Latin America since 1960, discusses the obstacles that have impeded the growth of these organizations, and suggests reforms that would encourage savings in the future. This study was prepared by Mrs. Ellen O. Wasfi, consultant to the Subcommittee, under the editorial supervision of Dr. John Karlik, staff international economist.

Members of the Subcommittee on Inter-American Economic Relationships were Senator John Sparkman, Chairman; Senators J. W. Fulbright, Abraham Ribicoff, Jacob K. Javits, and Len B. Jordan; Representatives Richard Bolling, Hale Boggs, Martha W. Griffiths, Barber B. Conable, Jr., and Clarence J. Brown.

SUBCOMMITTEE ON FOREIGN ECONOMIC POLICY

A Foreign Economic Policy for the 1970's

Continuing the investigation begun in December 1969 into the formulation of a foreign economic policy for the 1970's, the Subcommittee held five sets of hearings during the past year. Four days of hearings in March on the subject of "Trade Policy Toward Developed Countries" concentrated on economic regionalism, suggested strategy and agenda for future trade negotiations, the kind of trade policy the United States should pursue in the 1970's according to its own national interests, and problems of international trade in agriculture.

In May, the Subcommittee held four days of hearings on "U.S. Policies Toward Developing Countries." These hearings were devoted to a reexamination of U.S. policies to assist developing countries. Subjects covered were alternative ways to help developing countries through trade, investment, and aid policies; U.S. development policy within the framework of our global foreign policy objectives; strategies to accelerate the pace of development; and specific issues confronting the developing countries.

Four days of hearings were held in July on "The Multinational Corporation and International Investment." These hearings focused on a general consideration of the problems raised by the activities of multinational firms both in the United States and abroad; implications of investment across national boundaries for productivity, technology, employment and real incomes; international payments and other financial consequences of direct investment; legal and political conflicts arising from the activities of multinational companies.

Three days of hearings were held in September and October on "U.S. Foreign Trade: The Internal and External Adjustment Mechanism." These hearings considered the competitive ability of the United States to export and the reaction of domestic industries to the expansion of imports; the mechanisms through which trading and investing nations adjust their external balances in accordance with changing flows of goods, services, and capital; and the third day reviewed the ways in which events in the United States and abroad might influence the further evolution of the international payments system and how future reforms may affect the United States and modify the international role of the dollar.

In December three days of hearings were held on "East-West Economic Relations." The subcommittee received testimony on the political considerations that argue either for or against an expansion of economic relationships between East and West and the economic feasibility and desirability of additional forms of trade and investment between East and West.

Testimony at the above hearings was received from government officials, foreign experts, academicians, representatives of international corporations, former government officials, and representatives of economic research groups and labor.

Economic Developments in Countries of Eastern Europe

In May the Subcommittee released a compendium of invited papers covering a broad range of topics dealing with the recent performance of the Eastern European economies. Included among the topics are economic development and policy, rates of growth, capital formation, planning and management, the defense burden, transportation, agriculture, industry, population, employment, labor incentives, education and research, international trade, and foreign economic aid.

Economic Performance and the Military Burden in the Soviet Union

The latest in a series of hearings and studies of the Soviet economy, published periodically by the Subcommittee since 1955, was released in September. This comprehensive research study is designed to be responsive to the continuing interest of the Committee and the Congress in objective factual data and relevant interpretive comment on the economic performance of the Soviet Union in comparison with other industrially developed nations of the world.

Members of the Subcommittee on Foreign Economic Policy were Representative Hale Boggs, Chairman; Representatives Henry S. Reuss, William S. Moorhead, William B. Widnall, W. E. Brock 3d, and Barber B. Conable, Jr.; Senators John Sparkman, J. W. Fulbright, Herman E. Talmadge, Stuart Symington, Abraham Ribicoff, Jacob K. Javits, and Jack Miller.

SUBCOMMITTEE ON ECONOMIC STATISTICS

The Subcommittee continued its review of government statistics programs and examined the degree to which its long-standing recommendations for improvement of the system were being carried out.

Members of the Subcommittee on Economic Statistics were Senator Herman E. Talmadge, Chairman; Senators J. W. Fulbright and Jack Miller; Representatives Richard Bolling, Martha W. Griffiths, Barber B. Conable, Jr.; and Clarence J. Brown.

SUBCOMMITTEE ON INTERNATIONAL EXCHANGE AND PAYMENTS

The Subcommittee continued its review of developments in the field of international finance, particularly with reference to the evolution of the special drawing rights, as well as developments in respect to gold.

Members of the Subcommittee on International Exchange and Payments were Representative Henry S. Reuss, Chairman; Representatives Richard Bolling, Hale Boggs, William S. Moorhead, William B. Widnall, and W. E. Brock 3d; and Senators William Proxmire, Stuart Symington, Jacob K. Javits, and Charles H. Percy.

SUBCOMMITTEE ON FISCAL POLICY

Investment Policies of Pension Funds

Four days of hearings were held in April reflecting the continuing interest of the Subcommittee on the problems of older people. The Subcommittee took an over-all view of the investment activities of pension fund managers, including how well they have invested the funds which they control, and whether the funds have been used for purposes other than those which pensioners—present and future—have a right to expect. Witnesses were pension fund executives, academic experts, representatives of labor, and the Comptroller of the State of New York.

Members of the Subcommittee on Fiscal Policy were Representative Martha W. Griffiths, Chairman; Representatives Hale Boggs, William S. Moorhead, William B. Widnall, and Barber B. Conable, Jr.; Senators William Proxmire, Herman E. Talmadge, Stuart Symington, Jacob K. Javits, Jack Miller, and Charles H. Percy.

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 1970.

Brookings Institution—Panel on Economic Activity.
Business Council—Technical Consultants.
Federal Reserve System—Conference on Price Determination.
McGraw-Hill—Informal Conference.
National Bureau of Economic Research—Conference on Incomes and Productivity in Various Foreign Countries.
Washington Statistical Society.

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

The Conference Board—The Outlook for Government Spending.

Congressional Conference on National Security Affairs—Seminar.
Department of Agriculture Graduate School.
Drug, Chemical and Allied Trades—Economic Outlook.
Federal Executive Seminar, Kings Point, N.Y.—Current, Economic Policy Issues.
Financial Analysts—Economic Outlook.
Georgetown University—Symposium on Economic Policy.
George Washington University.
George Washington University Law School—Seminar.
Harvard University—Graduate Seminar.
Industrial Relations Research Association—Fiscal Policy.
Insurance Investment Officers Group—Outlook and Fiscal Policy.
Macalester College—Economic Policymaking in Congress.
Multi-State Tax Commission—Tax Reform.
Princeton University, Woodrow Wilson School—U.S. Trade Policies and Other Current Economic Issues.
Queens College—Current Economic Policy Issues.
Savings Bank Association of New York State.
Rensselaer Polytechnic Institute—Public Spending Priorities.
Stanford University—Symposium on Priorities.
U.S. Savings and Loan League—Conference on Credit Outlook and 12th Annual Conference on Savings and Residential Financing.
The Washington Journalism Center.

The executive director and other members of the professional staff submitted papers for publication to the following:

George Washington University National Law Center.
Monthly Labor Review.
San Francisco Press, article in "National Priorities, 1970."
Survey of Current Business.

The executive director conducted a seminar on public law and economic policy at the George Washington University Graduate School of Law. The director of research was a member of the Board of Governors and Chairman of the Membership Committee of the Economists Club and Chairman of the Annual Meetings Subcommittee of the American Statistical Association. The senior economist held official meetings with central bank officials of England and Ireland. The committee's international economist taught a course in international economics at the University of Maryland.

Conferences were held with Government officials or groups of foreign visitors seeking information on the activities of the Joint Economic Committee and the performance of the American economy representing the following nations:

Belgium
France
Germany
Hungary
Japan

Student Interns

The committee participated in the student intern program by having college students working in the committee offices during the past year.

CHANGES IN COMMITTEE MEMBERSHIP

Senators Hubert H. Humphrey of Minnesota, Lloyd M. Bentsen, Jr. of Texas, and James B. Pearson of Kansas were appointed to fill the vacancies created by the resignations of Senators Herman E. Talmadge, Stuart Symington, and Len B. Jordan. Representative Ben B. Blackburn of Georgia was appointed to fill the vacancy created by the election of William E. Brock 3d to the United States Senate.

CHANGES IN COMMITTEE STAFF

After more than 22 years of service with the Joint Economic Committee, Mrs. Hope G. Sham, Assistant to the Director of Research, retired this past June. Mr. Douglas C. Frechtling, Minority Economist, resigned to accept a position in the Office of the Secretary of the Treasury; Miss Leslie J. Barr joined the staff as minority economist. Miss Lucy A. Falcone and Mr. Jerry J. Jasinowski joined the staff as research economists.

DISTRIBUTION OF COMMITTEE PUBLICATIONS

During 1970, the Joint Economic Committee and its subcommittees issued 33 publications, including studies, hearings, and reports. Approximately 250,000 copies of current and previous years' publications were distributed.

In addition, the Superintendent of Documents sold in excess of 100,000 copies of current and past years' publications. The figures shown do not include the subscriptions to *Economic Indicators* that amount to about 10,000 monthly and are sold by the Superintendent of Documents.

SUBCOMMITTEE MEMBERSHIP

Priorities and Economy in Government

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Fiscal Policy

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