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JOINT ECONOMIC REPORT

REPORT

OF THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

ON THE

JANUARY 1972 ECONOMIC REPORT
OF THE PRESIDENT

TOGETHER WITH

MINORITY AND OTHER VIEWS



MARCH 23, 1972

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

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REPORT ON THE JANUARY 1972 ECONOMIC REPORT OF THE PRESIDENT

MARCH —, 1972.—Ordered to be printed

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

REPORT

together with

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. This report is to serve as a guide to the several committees of Congress dealing with legislation relating to economic issues.

NOTE.—Senator Sparkman states: "I am in agreement with the general emphasis of this Report. However, because of my duties as Chairman of the Committee on Banking, Housing and Urban Affairs, it has been impossible for me to participate fully in the hearings and deliberations underlying this Report. I do not believe it would be appropriate for me to take a position on all of the recommendations contained therein."

NOTE.—Representative Richard Bolling states: "Unusually heavy pressures of other responsibilities prevented me from fully participating this year in the hearings and Committee deliberations pertaining to the President's Economic Report. While I share the deep concern over the serious economic problems raised in this report, under present circumstances, I cannot endorse the particular conclusions and recommendations in this report."

**STATEMENT OF AGREEMENT BY THE MAJORITY AND
MINORITY MEMBERS OF THE JOINT ECONOMIC COM-
MITTEE ON INTERNATIONAL ECONOMIC ISSUES**

1. We must promptly start negotiations on longer term international monetary reform. We should explore the potential of utilizing such reform as a means to promote capital flows toward less developed countries.

2. A reformed international monetary system should guarantee sufficient exchange rate flexibility.

3. We strongly oppose any broad system of quotas for solving our international trade problems. Any such move would invoke retaliation with special effects being felt by workers in high wage export industries. Jobs in general would decline, and the consumer also would suffer. The solution to our trade problems lies in maintaining price competitiveness and in improving our productivity. The forthcoming trade negotiations will be an important step in promoting an expansionary trade policy.

1972 JOINT ECONOMIC REPORT

I. INTRODUCTION AND SUMMARY

Recent years have provided dramatic evidence of the difficulties of achieving really good economic performance and of the high costs of failure. In the late 1960's, war-induced fiscal mismanagement introduced inflation and resource distortion into the economy. In 1969 and 1970, misguided efforts to restrain inflation by reducing real income growth, together with efforts to make military cutbacks the vehicle for restraint rather than for reallocation, led to a lengthy recession and to the tragically prolonged, still-continuing period of high unemployment. While these policies were all too effective in halting economic growth and increasing unemployment, they did little to slow inflation.

In August 1971, the Administration suddenly and belatedly made public their recognition of the disastrous results of the policies followed in 1969, 1970, and early 1971. New measures described as "the most comprehensive new economic policy to be undertaken in this Nation in four decades" were announced.

Some of the steps taken in August are commendable and have our support. The suspension of dollar convertibility, for example, had been recommended earlier by our Subcommittee on International Exchange and Payments.¹

The most distressing inadequacy of the New Economic Policy is that it has done, and will do, little to meet our most pressing economic problem, which is the need to reduce unemployment. The fiscal measures proposed in August contained almost no net stimulus. Desirable measures of fiscal stimulus, such as the expanded public service employment and the counter-cyclical aid to States and cities recommended by this Committee in our Midyear Report,² were, and are, available. The Administration's January budget continues to be devoid of the needed job-creating measures.

The New Economic Policy is equally inadequate with respect to inflation control. Given the stubbornness of inflation, the 3-month price-wage freeze was probably necessary, and the freeze could not have been lifted without substituting some more flexible form of price-incomes policy. However, the "Phase II" effort to control the entire economy in detail is ill-conceived, poorly managed, and apparently of little real help in controlling inflation.

¹ "Action Now To Strengthen the U.S. Dollar," report of the Subcommittee on International Exchange and Payments of the Joint Economic Committee, Congress of the United States, August 1971.

² "The 1971 Midyear Review of the Economy," report of the Joint Economic Committee, Congress of the United States, August 16, 1971.

We began 1972 in a thoroughly unsatisfactory economic situation: high unemployment, continued inflation, and great uncertainty regarding the future shape of the international monetary system. To restore the economy to a state of general prosperity and then to sustain that prosperity will be no easy task. It cannot be accomplished by the brief half-year period of fiscal stimulus proposed by the Administration. What is required is a coordinated policy program which can be sustained into next year and which can be expected both to restore prosperity and to lay the foundations for continued prosperity and greater economic justice in future years. In this Report, we endeavor to spell out such a program.

Our evaluation of the economic outlook and a summary of our chief recommendations follows.

ECONOMIC OUTLOOK

The Administration has forecast a \$100 billion increase in gross national product in 1972, made up of a 6 percent growth of real output, and a 3¼ percent increase in prices. While this outcome is within the range of possibilities, the nongovernment witnesses who testified at our Annual Hearings did not expect this large an output gain. Given present policies, most witnesses felt the more probable outcome was a GNP gain of about \$85-\$95 billion and a real growth rate closer to 5½ percent. This outlook implies little if any reduction in unemployment. *This outlook is not satisfactory, and policy steps must be taken which will improve it.* The following review of the economy by sectors shows few areas which can be expected to contribute to really vigorous recovery.

Consumption.—Personal consumption expenditures increased 7½ percent in 1971, and the Administration forecasts an 8 percent increase in 1972, indicating they do not foresee any upsurge in consumer buying. The full impact of the personal tax reduction of January 1, 1972, will not be felt this year due to the time necessary for a tax decrease to be translated into a consumption increase. The recent step-up in the withholding schedule will aggravate the delay. Furthermore, the income tax reductions are partially offset by the recent increase in the social security tax base. The negative influence of this social security tax increase will be especially evident in the latter half of 1972. Recent data on retail sales tends to confirm the view that consumer spending is continuing to grow only moderately.

Business investment.—The outlook for business investment has improved since the last quarter of 1971. The Commerce Department projection released in early March was for a 10½ percent increase in business spending on plant and equipment between 1971 and 1972. Business investment promises to be one of the stronger sectors of the economy in 1972. However, its strength is far from exceptional. In the recovery year 1956, for example, plant and equipment spending increased 21 percent.

Inventories.—Given the longer term trend for business to operate with a diminishing ratio of inventories to sales, current inventory levels are not particularly low. Inventories cannot be expected to provide any independent stimulative force in 1972.

Residential construction.—One of the few bright spots in the 1971 economy was the record high for new private housing starts. Continued support from the Federal Government through the 1972 Housing and Urban Development Act, together with a relatively high personal savings rate, should combine to help keep the level of construction high, provided long-term interest rates are not allowed to rise. The large number of building permits issued in late 1971 and early 1972 support this hope that home construction will remain strong. Even so, construction will not show the big increase in 1972 that it did during 1971. We will do well to sustain current levels.

Government purchases.—State and local government purchases are generally expected to increase at about the 11 percent rate of the last few years, although this rate could increase if there is a significant increase in the amount of Federal aid to States and cities.

Federal purchases are subject to sharper swings than State and local. After declining from early 1969 to mid-1971, Federal purchases increased at a 9 percent annual rate in the second half of last year. This increase will continue or even intensify in the first half of this year, but as we discuss in Chapter II, the sharply lower rate of Federal spending increase planned for the second half of this year could remove this main source of economic stimulus.

Prices and wages.—The Economic Report estimates that the rate of price increase will be reduced to between 2 and 3 percent by the end of 1972. This does not seem at all certain. Large price increases approved for the basic materials industries will be felt throughout the rest of the economy. The Secretary of Agriculture, in testifying before this Committee, estimated that food prices would rise over 4 percent in 1972. The general tendency for prices of services to rise more rapidly than prices of goods must also be considered in assessing the price outlook.

It seems equally uncertain that wage increases can be held to the Pay Board's 5½ percent guideline. The Economic Report makes the point that there is nothing in the outlook to make realization of this pay target "clearly unattainable." Nonetheless, the Secretary of Agriculture's estimate to this Committee that wages might rise as much as 7 percent seems at least equally probable.

Unemployment.—Unemployment will continue to be the country's most serious economic problem in 1972. The Administration has forecast the rate of unemployment to be in "the neighborhood of 5 percent" by the end of 1972. This Committee views that forecast as too optimistic. With the economy likely to grow at a rate below 6 percent, the labor force likely to increase rapidly, and the lack of new initiatives from the Administration, the private witnesses who appeared before the Committee were generally agreed that a year-end unemployment rate in the neighborhood of 5.5 percent is more probable. A more rapid increase in the size of the labor force than anticipated or slower real growth in the economy could make even this forecast too optimistic.

In sum, we repeat that the outlook is far from satisfactory. The economy remains sluggish. The recommendations which we summarize below are designed to promote a more vigorous recovery this year and a healthy and balanced economic growth in subsequent years.

SUMMARY OF RECOMMENDATIONS

The Committee's principal recommendations are summarized below. They are explained in greater detail in the remaining chapters of this Report.

Restoring Full Employment and Containing Inflation

- Recent suggestions that full employment can be equated with an unemployment rate greater than 4 percent are totally unacceptable. An unemployment rate no higher than 3 percent remains an appropriate long-run target for the United States. Because we are presently so far from this long-run goal, the Administration should establish an *interim* target of 4 percent, and they should make available their estimates of when this interim target can be reached.³

- The Administration's budget policy recommendations should be rejected on three fundamental grounds:

- (1) The move from a full-employment deficit in fiscal 1972 to balance in fiscal 1973 will not achieve sustainable high employment.

- (2) The realism of the budget estimates is questionable.

- (3) The composition of proposed tax and expenditure changes is not designed to have maximum job-creating effect.

- Fiscal policy must remain stimulative for as long as necessary to restore full employment. Two major new programs are required:

- (1) A substantially expanded public service employment program.

- (2) A system of counter-cyclical Federal payments to State and local governments designed to compensate these governments for the short-fall in their own revenues caused by high unemployment.⁴

- Monetary actions must accommodate an expansionary fiscal policy. The money supply growth target should be at the upper limit of the 2-6 percent range recommended by this Committee for more normal circumstances.

- The Federal Reserve should develop appropriate policy tools to achieve lower long-term interest rates, particularly those on home mortgages and on State and local bonds. The Federal Reserve should expand its direct purchases of housing obligations.

- The present price and wage control system is too complex to be administered efficiently. Decontrol of large segments of the economy and a concentration of effort on only those sectors of the economy characterized by obvious market power would enhance the chances for reducing inflation. As soon as possible, the present system of cumbersome mandatory controls should be replaced by a permanent mechanism for the administration of a largely voluntary price-incomes policy.

- The Administration and Congress should act vigorously to reform government programs and activities that significantly contribute to inflation. Wherever import quotas, regulatory policies, procurement policies, stockpile reserves, Federal subsidies, and other policies are found to artificially restrict market supply or otherwise unnecessarily

³ Senator Humphrey does not join in this recommendation.

⁴ Senator Bentsen does not concur in this recommendation absent a full examination by the Committee of the potential problems of such a program.

inflate prices, they should be eliminated or redesigned.⁵ More determined enforcement of the anti-trust laws is essential.

- Manpower training programs must be more closely tied to the provision of job opportunities. These job opportunities can be stimulated through growth of aggregate demand in the private sector and through expansion of the public sector.

- Programs providing training and employment for teenagers and young adults especially require further strengthening. These programs must be flexible enough to accommodate changing economic conditions.

- Equal employment opportunity for all remains an unmet goal. The stronger legislation recently passed by Congress must be vigorously enforced.

- The Employment Service must be considerably strengthened in order to better perform its job-matching function. Adequate placement assistance must be provided for all, including minority groups.

Strengthening Economic Statistics

- The Bureau of Labor Statistics press briefings on the monthly price and employment statistics should be restored and similar technical briefings should be initiated for other major economic statistics.

- Two nonpartisan, nongovernment committees should be appointed; one to evaluate our present labor force statistics and the other to evaluate price statistics. They should report in approximately one year.

Tax and Expenditure Reform

- Congress and the Administration should place greater emphasis on improving the distribution of income and wealth in this country.

- Congress should act to eliminate enough of the most serious tax loopholes to provide a revenue increase of approximately \$10 billion beginning in fiscal 1974 and of a somewhat lesser amount in fiscal 1973.

- The social security tax system should be made more progressive.

- The Federal estate and gift taxes should be re-examined to determine if they might be suitable as additional revenue sources.

- Congress and the Administration should immediately initiate a critical review of major subsidy programs in order to eliminate or redesign wasteful, unfair, or outmoded subsidies.

Defense and National Security

- The defense program should not be used for purposes of stimulating the economy and creating jobs. The only legitimate function of the defense program is to provide the military requirements essential for national security.

- Congress needs to scrutinize with special care Administration requests for new major weapons systems and other defense programs that have been justified on inadequate military grounds.

- The Department of Defense needs to do a better job of eliminating waste and mismanagement throughout the military establishment. Large cost overruns and gold-plating of weapons systems, excessive support costs, and mishandling of military assistance are undermining our defense program. Defense spending should be reduced. A tighter, leaner, and smaller defense budget will strengthen our real national security.

⁵ Senator Humphrey does not join in this recommendation.

- The national security budget classification should be expanded to include the total costs of military assistance and outlays for programs of all agencies other than DOD that are related to current military programs or are justified on the grounds of national security or are in payment for past wars or military programs. The costs of the war in Southeast Asia should be specifically identified in the budget document.

- The Council of Economic Advisers should pay greater attention to the impact of defense spending on the economy. The Council should conduct studies and report its findings at the earliest possible time on: (1) The extent to which defense spending and procurement practices contribute to inflation; (2) the impact of inflation on defense spending; and (3) the effects on our balance of payments of the costs of military bases and facilities in foreign countries, and the deployment of troops in Europe, Asia, and other areas of the world.

- The Office of Management and Budget should concentrate more of its efforts and resources on reviews of the proposed budget requests of the Defense Department so as to identify and recommend elimination of unnecessary and wasteful expenditures.

International Economic Issues ⁶

- The solution to the international trade problems of the United States is not to be found in quotas or similar restrictions limiting imports. Any suggestion to adopt such techniques as a general solution should be emphatically rejected. Instead, the Administration should articulate a forward-looking trade strategy and accompanying schedule for implementation.

- The appropriate solution to U.S. trade and balance-of-payments problems lies in the prompt adjustment of exchange rates and in effective policies to strengthen competitiveness through efficient management, increased worker productivity, and shifts in the composition of output toward those industries in which the United States has a comparative advantage.

- Especially at this time when unemployment is at an intolerable level and the strength of the recovery from the previous period of stagnation is in doubt, monetary and fiscal policies must be used primarily to increase employment and to insure an adequate rate of domestic economic growth.

- Negotiations on fundamental reform of the international monetary system should begin immediately. An appropriate initial focus for these discussions is how to guarantee sufficient exchange rate flexibility in the future. Without the assurance of a responsive and effective exchange rate mechanism, the United States can hardly restore dollar convertibility. The second order of business might be the discussion of the terms under which excessive liquid dollar balances now in the hands of foreign central banks can be immobilized. If these issues can be resolved, two major obstacles to the restoration of dollar convertibility will have been overcome.

- In the future, special drawing rights issued by the International Monetary Fund should replace the dollar as the primary source of additions to the global stock of reserves. As more SDR's are distributed to insure a sufficient supply of international money, special attention

⁶ Senator Humphrey states that he is in strong disagreement with some of the dogmatic conclusions stated in this section.

should be devoted to injecting these assets into the system through a mechanism that will enable an increase in transfers of real resources from industrialized nations to developing countries.

- The quantity of gold reserves in the international monetary system should not increase.

- Canada, Japan, and the European allies of the United States should promptly implement the guideline that no nation's balance of payments either benefit or suffer as a result of its contributions to the mutual defense.

- Widening the band within which exchange rates may fluctuate has apparently helped curtail international flows of short-term capital. The U.S. monetary authorities should cooperate with their counterparts abroad to the maximum extent feasible in swap mechanisms and in policy coordination to help maintain international short-term capital flows within appropriate bounds.

II. A COORDINATED POLICY TO REGAIN FULL EMPLOYMENT

In 1970 and 1971, the Federal Government failed to fulfill its commitment to sustain maximum employment, production, and purchasing power. The Government must recommit itself to the goal of noninflationary full employment. This goal cannot be fully achieved this year. Therefore, there is need to spell out a carefully coordinated set of policies which can be sustained until the goal is reached. In this chapter, we define what we mean by full employment, explain why we attach overriding importance to its achievement, and detail the mix of fiscal, monetary, price-incomes, and structural policies which can bring us to our goals.

THE GOAL OF FULL EMPLOYMENT

The commitment to full employment—a commitment universally endorsed in this and other industrialized countries—unfortunately does not in the United States have the force it must have if this goal is to be reached and sustained. In part this lack of force stems from a failure to recognize the full costs of unemployment. In part it stems from the absence of an agreed upon definition of full employment.

The Costs of Unemployment

Failure to make full use of available labor resources imposes a heavy human cost on those who are unemployed or underemployed. It also imposes a cost on the entire society in terms of goods and services which could be produced but are not.

The official unemployment count, important as it is, measures only a fraction of the total costs of unemployment and underemployment. During 1971, in addition to the 5 million persons officially counted as unemployed, there were 774,000 persons identified in the official statistics as not seeking work because they believed no jobs were available. These are the discouraged workers who have despaired of finding jobs. Also identified in the official statistics were 2.4 million persons working part time because full-time work was not available. When the number of hours these part-time workers were involuntarily unemployed is converted to its full-time equivalent, an additional 1.1 million persons are added to the count of unemployed.

Adding these three categories, one finds that, as measured by official statistics, there were the equivalent of 6.9 million persons unemployed in 1971. This would be 8.1 percent of the civilian labor force (after adjusting the labor force to include the discouraged workers). Table 1 contains the equivalent figures for 1969 and 1970. Even in the relatively high employment year 1969, over 5 percent of the labor force was unemployed by this expanded estimate.

TABLE 1.—TOTAL OFFICIALLY MEASURED UNEMPLOYMENT, 1969-71

[In thousands of persons]

	1969	1970	1971
Unemployed.....	2,832	4,088	4,993
Discouraged ¹	574	638	774
Part-time unemployed ²	852	1,010	1,143
Total.....	4,258	5,736	6,910
Unemployment rate ³ (percent).....	5.2	6.9	8.1

¹ Those not in labor force because they think they could not find a job.

² Full-time equivalent of part-time unemployment of those who work part-time because of slack work, material shortages, or inability to find full-time job. Full-time defined as 40 hours per week.

³ Unemployed plus discouraged plus full-time equivalent of part-time unemployed as percent of civilian labor force adjusted to include discouraged.

Source: Computed by Joint Economic Committee staff from Bureau of Labor Statistics data.

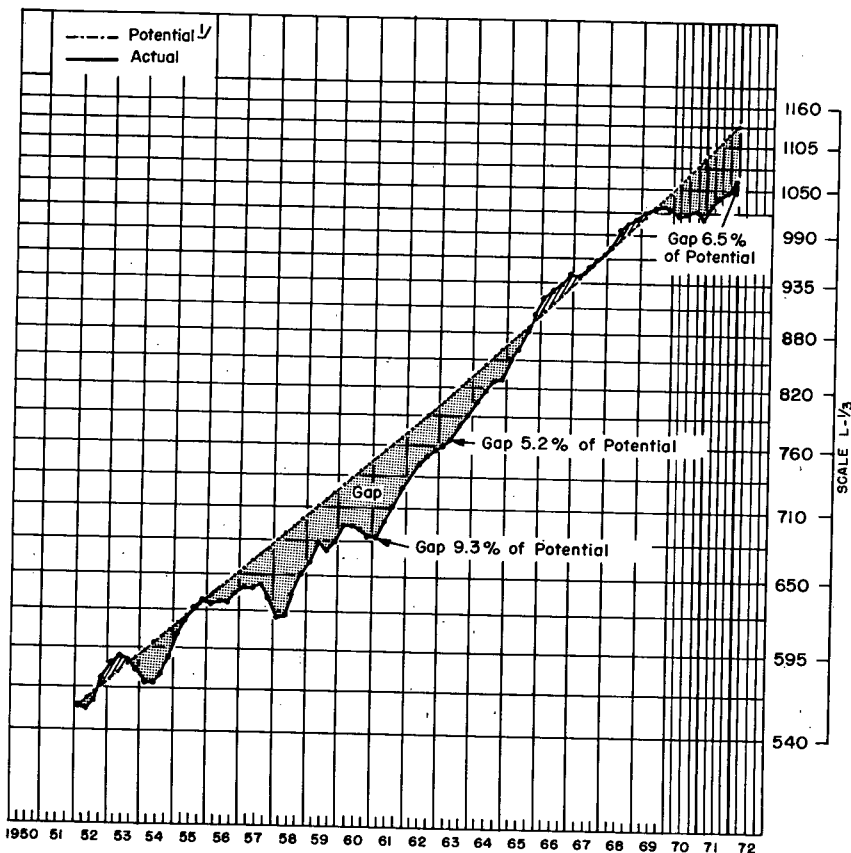
To obtain a fuller comprehension of the human costs of underemployment, it is necessary to also consider the forced early retirement of many older workers at times when unemployment is high; the increase in the welfare rolls during recessionary periods; and the enormous numbers who, because of job discrimination or shortage of good jobs, hold much less challenging and well-paying jobs than those for which they are qualified. Good statistical estimates of some of these aspects of underemployment are lacking, but there is no question of the enormity of the underutilization of human resources.

Some of the cost of unemployment in terms of output forgone can be measured by the gap between actual and potential gross national product (GNP). Potential GNP has usually been defined as the real output which would have been produced if the unemployment rate had been 4 percent. So defined, it does not represent the maximum possible level of output, but it does provide a consistent standard against which to measure actual economic performance. As can be seen from Chart 1, GNP was slightly above its potential in 1968 and early 1969, fell \$54 billion below potential in 1970, and \$73 billion below in 1971.

CHART 1

ACTUAL AND POTENTIAL GROSS NATIONAL PRODUCT

GNP in 1971 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 1971.

Whenever GNP is below its potential, this is reflected in a short-fall of Federal tax receipts below what they would be if the unemployment rate were at 4 percent. Federal tax receipts in fiscal year 1972 are estimated to be \$27 billion below what they would have been if GNP were at its potential. In addition, Federal expenditures for unemployment compensation, welfare, and the like in fiscal year 1972 are \$3½ billion above what would be required if GNP were at its potential.

A similar situation exists with respect to State and city budgets, although the magnitudes are smaller. Precise estimates are lacking, but State and local tax receipts in 1971 may have been as much as \$7 billion below what they would have been at the same tax rates if unemployment had been at 4 percent. State and local costs of poverty-

related services also rise when unemployment is high. Since State and local governments lack the deficit financing capability of the Federal Government, their response to this situation consists of raising tax rates and/or cutting back on the quality of public services. A major cost of unemployment is thus its impact on government budgets and the consequent reductions in public services, especially at the State and local level.

Types of Unemployment

In order to arrive at an adequate definition of full employment, it is necessary to understand the various causes of unemployment and to estimate the minimum amount of unemployment required for efficient functioning of the economy.

Some unemployment arises from the job search conducted by new entrants or re-entrants to the labor force; by those who voluntarily chose to change jobs; and by those dismissed from a job because of unsatisfactory performance. Unemployment of this nature is necessary both for an efficient economy and for a free society. This type of unemployment can be referred to as minimum frictional unemployment.

Another type of unemployment is structural unemployment. This term is used to describe the unemployment which persists even in a time of general prosperity because of such factors as discrimination, lack of education, changes in technology, and poor geographic distribution of job opportunities. The United States has in the past accepted far too high a level of structural unemployment. Structural unemployment can be greatly reduced if we are willing to undertake the necessary economic reforms, a number of which we discuss in later sections of this chapter.

A third type of unemployment is the aggregative unemployment which arises from a slack level of overall economic activity. The increase in unemployment since 1969 has been an increase in aggregative unemployment. It is the result of a conscious decision, to use monetary and fiscal policy to restrain the economy. It does not represent any increase in the minimum frictional level of unemployment. Nor does it represent any deterioration in the structure of the economy. As shown in Table 2, the heaviest impact of the rise in unemployment has been borne by adult males, not by women and young people, who historically have experienced somewhat higher rates of frictional unemployment. Unemployment rates in both 1969 and 1971 were much higher for blacks than for whites, evidence of the much greater structural unemployment among blacks. However, the relative *increase* in unemployment since 1969 is slightly greater for whites than for blacks.

TABLE 2.—NUMBER OF PERSONS UNEMPLOYED AND UNEMPLOYMENT RATES BY SEX, AGE, AND COLOR, 1969 AND 1971

	1969		1971		Percent increase in number unemployed 1969-71
	Number (thousands)	Percent	Number (thousands)	Percent	
Total.....	2,832	3.5	4,994	5.9	76
White.....	2,260	3.1	4,074	5.4	80
Male, 20 years and over.....	794	1.9	1,741	4.0	119
Female, 20 years and over.....	806	3.4	1,324	5.3	64
Both sexes, 16 to 19 years.....	660	10.7	1,009	15.1	53
Negro and other races.....	571	6.4	919	9.9	61
Male, 20 years and over.....	169	3.7	345	7.2	104
Female, 20 years and over.....	209	5.8	327	8.7	56
Both sexes, 16 to 19 years.....	193	24.1	247	31.7	28

Source: Bureau of Labor Statistics.

Changes in the Composition of the Labor Force

There have been significant changes in the composition of the labor force in the last 15 or 20 years. Women over 25 years of age now make up 28 percent of the civilian labor force, compared to 26 percent in 1956. Young people 16-24 years of age make up 22 percent, compared to 15 percent in 1956. Because unemployment rates historically have been somewhat higher for adult women than for adult men and substantially higher for young people than for those over 25, it has been argued that it is now more difficult to achieve in a noninflationary manner any given reduction in the overall unemployment rate. Some have even argued that the overall unemployment rate is no longer a meaningful measure of the degree of resource under-utilization.

We are not persuaded that low rates of unemployment are harder to achieve than they once were or that inflationary pressures at any given level of employment are necessarily greater now than they once were. We emphatically reject the notion that the overall unemployment rate has less meaning than it once had. No single statistic can tell us all we need to know about the labor market, but the overall unemployment rate remains the most valuable single indicator.

Several important points are being overlooked with respect to the changed composition of the labor force. First, this change in the labor force did not take place suddenly between 1969 and 1971. As shown above, the *increase* in unemployment since 1969 was not caused by the changed composition of the labor force nor by any other structural factor. It has been caused by the slow growth of aggregate demand, which in turn resulted largely from policy decisions to restrain the economy.

Second, many major labor market changes have taken place in the last 15 to 20 years. Not only has the proportion of women and young people increased, but educational levels have increased. Dr. Arthur Okun pointed out in his testimony at our annual hearings that if March 1957 unemployment rates for each educational group in the labor force are combined with the proportions of the labor force represented by each group in March 1971, the hypothetical overall unemployment rate would be 3.5 percent, compared to the actual rate of 4.1 percent in March 1957.

Furthermore, racial discrimination has diminished, although not nearly enough; the work patterns and career aspirations of women have changed; and the structure of job opportunities has changed. A smaller proportion of jobs is now in the manufacturing sector, a much larger proportion in the service sectors. There are relatively more white collar jobs, relatively fewer blue collar jobs. Some of these changes should reduce inflationary pressures at any given level of employment; others may increase it. In the absence of more comprehensive analysis of labor market changes, it is a mistake to assume either that a changed age-sex composition of the labor force is the single most important change or that all the changes taken together make noninflationary full employment more difficult to achieve.

Third, it is a mistake to argue that the employment position of women has deteriorated relative to the total labor market. Women have generally experienced higher unemployment rates than men. We support policies to eliminate the job discrimination which helps account for this difference. The situation, however, is not necessarily

worse today than it has been in the past. Unemployment rates for adult women are cyclically less sensitive than those for adult men. In 1968 and 1969 the unemployment rate for adult women was very slightly above the rate for all workers, just as it was in earlier periods of relative prosperity. In 1970 and 1971, the unemployment rate for adult women was a little below the rate for all workers, just as it was in earlier recessions.

Fourth, the relative position of young people aged 16-19 has indeed worsened relative to the overall labor market. The unemployment rate for this age group during 1971 was 16.9 percent, the highest it has been since regular statistics became available in 1948, and it has since risen steadily to 18.8 percent in February 1972. This relative worsening of position has been the result of rapid growth of the population in this age group and the lack of adequate policies to provide jobs for these rapidly growing numbers of young people. In the years ahead, the population in this age group will grow less rapidly than in the past decade so that the task of providing enough jobs for young people should become less difficult. As we discuss later in this chapter, more publicly funded jobs for young people are urgently needed. With this and other appropriate policies, it should be possible to make great progress in reducing the unemployment rate for young people. Certainly the larger number of young people in the work force must not be accepted as an excuse for tolerating higher rates of overall unemployment.

Finally, the recent discussion of the number of women and young people in the labor force tends to mask one of the most crucial problems for employment policy in the years ahead. As shown in Chart 2, in the next decade the most rapidly growing group in the labor force will be adults between the ages of 25 and 35. Those same persons who swelled the size of the teenage population in the 1960's are now swelling the number of adults seeking career opportunities. A great challenge of this decade will be to provide these opportunities. A fundamental condition for meeting this challenge is the achievement and maintenance of a full employment economy.

CHART 2

PERCENT CHANGE IN TOTAL LABOR FORCE OVER 5 YEAR PERIODS, BY AGE GROUP, 1960-1985

	percent change from:				
	1960 to 1965	1965 to 1970	1970 to 1975*	1975* to 1980*	1980* to 1985*
Total labor force	7.0	11.3	8.0	8.6	6.4
16-24 years old	23.0	27.1	9.1	6.5	-3.8
25-34 years old	-0.7	17.9	24.8	18.9	10.6
35 years old & over	5.1	3.8	1.4	4.8	8.8

* BLS projections

Source: Joint Economic Committee based on data from the Bureau of Labor Statistics Handbook of Labor Statistics 1971 and The U.S. Labor Force: Projections to 1985.

A Full-Employment Target

To this Committee, full employment means a condition in which all Americans able to work and seeking work can freely exercise their right to useful, remunerative, regular, and full-time employment. Such a definition makes allowance for a minimum frictional level of unemployment but not for structural or aggregative unemployment.

The best recent research indicates that the minimum level of frictional unemployment is less than 3 percent of the labor force. This is consistent with the long-term goal of an unemployment rate no higher than 3 percent which this Committee has repeatedly advocated. Indeed, a 3 percent unemployment target allows for some structural unemployment, since it must be recognized that structural unemployment, while it can be sharply reduced, cannot be entirely eliminated in the foreseeable future. The needed reduction of structural unemployment will be difficult. It will require vigorous and sustained efforts. But it can be done if we are willing.

Unemployment in excess of 4 percent is aggregative rather than structural or frictional. Reduction in the unemployment rate to 4 percent cannot be achieved this year, but it can and should be responsibly achieved during 1973 by an appropriate combination of monetary, fiscal, and price-incomes policies together with a vigorous beginning on needed structural reforms.

This Committee views with alarm recent suggestions that full employment can be equated with an unemployment rate greater than 4 percent. This position is totally unacceptable.

An unemployment rate no higher than 3 percent remains an appropriate long-run target for the United States. If the necessary structural and institutional reforms are undertaken, a combination of a rate of unemployment below 3 percent and an inflation rate (as measured by the GNP deflator) no higher than 2 percent can be achieved and sustained.

Because we are presently so far from the long-range employment goal, a specific interim target should be established. A 4 percent unemployment rate represents an appropriate interim target. The Administration should establish such a target and make available their estimate of when it can be reached.¹

MONETARY AND FISCAL POLICY

The year 1971 was a year of uncertainty and disappointment as the predicted economic recovery failed to materialize. Financial markets generally reflected this uncertainty. The fiscal 1972 budget which was announced in January of last year called for a small surplus if the economy were operating at high employment. In addition, the pace of monetary expansion in late 1970 had slowed perceptibly. Prices and wages were still rising rapidly while unemployment had reached a recession level of 6 percent. Hardly any analyst outside the Executive Department considered the Administration's optimistic economic forecast to be in the realm of probability.

Review of 1971 Developments

Monetary policy in early 1971 called for a substantial easing in financial markets. The money stock (currency and demand deposits) expanded at a rapid annual rate of 10 percent in the first half of the year; and interest rates, particularly short-term rates, continued their downward path from the historical highs reached in mid-1970. However, the expansionary thrust of monetary policy was not achieving its hoped-for effect of sparking an economic recovery. Business spending on plant and equipment actually declined in real terms during 1971.

Businessmen continued to shift from short-term to long-term financing to further insulate their firms from the liquidity bind which in 1970 brought many to the edge of bankruptcy. Consumers also built up their liquidity, and their savings rate was maintained at the record high rate of 8 percent of disposable income.

As the year 1971 developed, the budgetary outlook became somewhat more stimulative, largely as a result of congressional decisions. Principal elements in this shift were postponement of a scheduled social security tax increase, increases in social security benefits, and a rise in military pay. Thus the prospective small budget balance at full employment earlier envisioned for fiscal 1972 was turned into a deficit approaching \$8 billion.

In contrast to this more expansionary prospect for fiscal policy, monetary policy tightened as inflation continued into the summer.

¹ Senator Humphrey does not join in this recommendation.

The rapid money growth of the first part of 1971 virtually ceased; and both long- and short-term interest rates again moved upward. During the second half, the money stock was virtually constant, rising at an annual rate of less than 1 percent from July through December.

Despite this lack of increase in the money supply, short- and long-term interest rates again began to decline in late summer. Such reductions should have been considered a reasonable development if there is any validity to the proposition that interest rates were maintained at their very high levels because of inflationary expectations. If lenders and borrowers confidently expected that the price-wage controls introduced in August would be effective in controlling inflation, it would have been reasonable to expect interest rates to fall even more than they actually did.

That the money supply remained virtually stable in late 1971, despite renewed efforts of the monetary authorities to achieve some expansion, was one of the more puzzling phenomena of 1971. The apparent explanation is that the fears and uncertainties which plagued the economy in early 1971 were not allayed or resolved by the New Economic Policy announced in August. Business firms and consumers remained hesitant to commit additional resources until there was more positive evidence that the economy was once more on the road to healthy economic growth without inflation.

The single most encouraging sector of the economy in 1971 was the housing industry. With the need for housing large and rising, the increased flow of savings-type deposits made mortgage financing considerably more available in 1971, and mortgage interest rates throughout the year were lower, except for the period in mid-1971 when money market conditions generally tightened. It should also be noted that the federally sponsored or supported housing agencies came to the aid of housing, particularly during the period when financial markets tightened in the middle of the year.

The private financial picture at year-end was generally more favorable than that which has prevailed over the last several years. Total household holdings of deposits increased in 1971 at a rate more than double that of the previous year. This was partly accomplished by disposal of U.S. Government securities and also by increasing indebtedness of individuals. These aggregate data conceal differing patterns among various groups and individuals. Obviously, for example, there is little, if any, reason to believe that the poor and the unemployed shared in the generally improved financial developments of 1971. The fact that consumer spending was still lagging at year-end and the saving rate was still high suggests strongly that increased saving has flowed largely to those with high incomes, who in general tend to save a relatively large proportion of their income gains.

The improvement in the financial position of business was also evident in 1971. Although the increase in liquid asset holdings was not so large as in the previous year, corporate businesses had greatly improved their balance sheet structure with debt consolidation proceeding at a continuing rapid rate.

While interest rates at year-end were off noticeably from the previous year, long-term rates were still high in historical perspective. FHA mortgage rates, for example, were still at 7.6 percent down from 8.9 percent 12 months earlier, and from 9.3 percent at the peak

in 1970. Even more significant was the fact that they were less than one-half of a percentage point under the level prevailing in August when the new program was initiated, and they were above rates achieved just prior to the tightening of monetary policy last spring.

For many people, particularly small businessmen, homeowners and consumers, interest rates continue to remain excessively high, and there is little indication that the responsible authorities have in mind any concerted program to increase the availability of credit on more reasonable terms to these borrowers. In spite of pronouncements of improvement in credit availability and in spite of our wage-price program, the fact remains that many consumers continue to pay exorbitant interest rates, ranging as high as 36 percent per year, and that the Administration shows only great indifference to this problem.

Persistently high residential mortgage interest rates become a matter of even greater concern when they are viewed against Federal Reserve Board recommendations ostensibly aimed at improving the availability of home loan funds during periods of tight money and high interest. The Board has recommended that lenders provide mortgages with variable interest rates subject to up or down adjustment depending on market conditions; removal of the interest rate ceilings of FHA and VA backed residential mortgage loans; and eventually ending the interest rate ceiling on consumer time and savings deposits.

These recommendations must be carefully scrutinized. The fact that mortgage interest rates remain near historically high levels despite the fact that mortgage lenders have a surplus of loan funds should raise questions as to what remedies should be applied. Obviously, increasing the cost of money to lenders, as is suggested by eliminating interest ceilings on deposits, would tend to make more loan money available, but at the cost of excluding increasingly large numbers of moderate and middle income families from the housing market. A sharp case in point is the 1969-1970 experience. Mortgage interest rates rose sharply through 1969. When rates exceeded 9 percent at their peak in early 1970, housing starts fell almost to the 1 million unit mark. During this period, studies showed that one-third of all the households in the Nation with incomes above the level qualifying them for Federal mortgage interest subsidies were priced out of the housing market because mortgage payments would have exceeded 25 percent of their incomes, a ratio which would have prevented them from being able to afford other essential items necessary to maintain an adequate standard of living.

Monetary Policy in 1972

The Economic Report of the President suggests that with some stimulative fiscal policy in the current period, and an accommodative monetary policy, private demands will pick up strongly in the second half-year and more than make up for the proposed decrease in fiscal stimulus after mid-year.

Just what monetary policy should be over the next year is not spelled out in the Economic Report, but the Administration's GNP forecast implies an expansive monetary policy. If their predicted 9 percent increase in money GNP is to be realized, the money supply must also grow about 9 percent or else there must be a substantial

pickup in the velocity of circulation. While some increase in velocity can be reasonably anticipated, fairly rapid money growth will also be needed if recovery is not to be choked off by rising long-term interest rates.

Chairman Burns of the Federal Reserve Board said the Board would act constructively to assist the economy toward a path of restoring full employment in a reasonably fast time period, but just what that would mean was not clear. It was also implicit, if not explicit, in his testimony that he thought long-term interest rates were still too high. But it also seemed evident from his testimony that monetary policy would not *directly* act to bring long-term rates down, and that Federal Reserve policy would continue to emphasize stimulative efforts in the short-term markets which would presumably in time be felt in lower long-term interest rates.

Another point stressed by Chairman Burns and other witnesses was that long-term interest rates should fall if the wage-price control apparatus succeeds in lowering inflationary expectations. The most recent price developments—with wholesale and retail prices bulging upward following the post-freeze adjustments—is cause for concern that the abatement of inflationary expectations may still be some distance off.

Monetary actions should be sufficient to accommodate an expansionary fiscal policy. Certainly, if we have any hope to achieve the 9-plus percent growth in money GNP in 1972 predicted by the Administration, the money supply growth target should be at the upper limit of the 2-6 percent range recommended by this Committee for more normal circumstances. Equally important is the necessity that the monetary authorities have regard for the impact—or lack thereof—of monetary policy on interest rates. Long-term interest rates are still too high for sustained economic growth. The Federal Reserve should develop appropriate policy tools to achieve lower long-term interest rates, particularly those on home mortgages and on State and local bonds.

Fiscal Policy in 1972

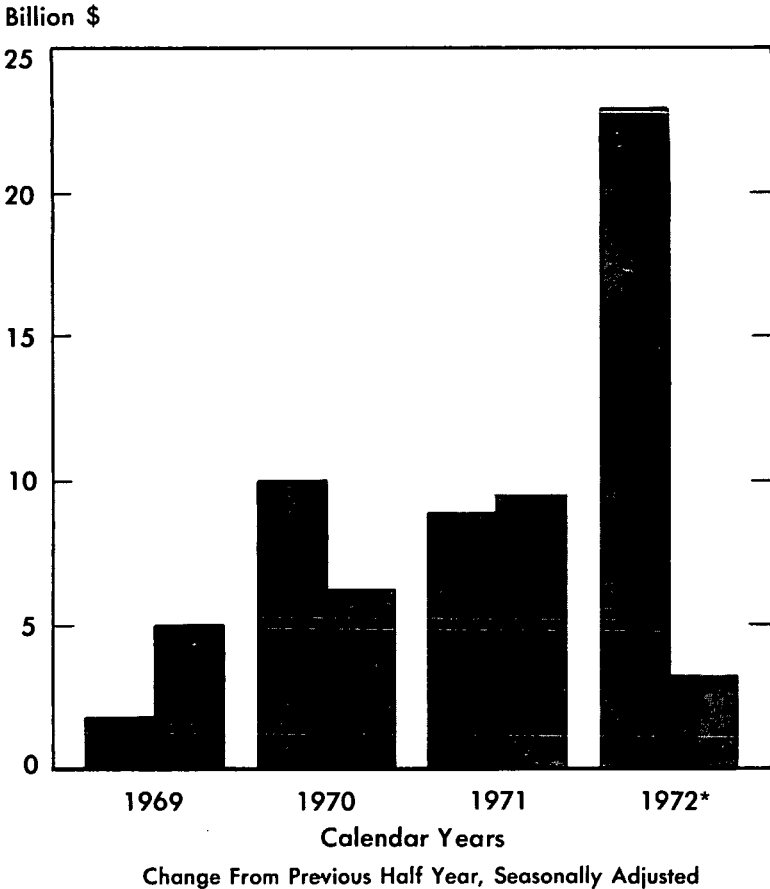
The Administration's budget recommendations are inadequate in three major respects. First, the proposed pattern of expenditures would lead to large and poorly timed changes in the amount of economic stimulus provided by the budget. Second, the composition of recent and proposed changes in both taxes and expenditures is not designed to produce the needed expansion of civilian employment. Third, it is questionable whether the proposed expenditure pattern can, in fact, be achieved.

Timing.—The Administration has estimated that there will be a \$38.8 billion deficit in fiscal 1972 and a \$25.5 billion deficit in fiscal 1973. When adjusted for the revenue loss and increased expenditure caused by high unemployment, the estimated budget deficit is \$8 billion in fiscal 1972, and there is a small surplus in fiscal 1973. When examined by half years, the shifts in the budget position are large and sudden. As shown in Chart 3, the planned increase in Federal expenditure in the first half of calendar 1972 is more than twice that

of any recent half year, while the second half of 1972 would show the smallest increase of any half year since the first half of 1969. The change in the full employment surplus by half years (NIA basis) is shown in Table 3.

CHART 3

Federal Expenditures (NIA Basis)



*Estimate by BEA

TABLE 3.—FULL EMPLOYMENT EXPENDITURES AND RECEIPTS (NIA BASIS)

[In billions of dollars, seasonally adjusted annual rate]

Half years	Expenditures	Receipts	Surplus
1971: II	223.8	227.7	3.9
1972: I	244.8	235.4	-9.4
II	250.1	246.1	-4.0
1973: I	257.6	256.7	-0.9

Source: Council of Economic Advisers.

Even if the proposed spurt of spending in the first half of this calendar year should be achieved, there is great danger that it will be poorly planned, wasteful, and probably ineffective in creating jobs. The move toward restraint after June 30 is undesirable. The Administration expects that the private sector will pick up the main burden of stimulus as the full employment budget moves toward balance. In our view, this development is based far more on hopes than on any tangible evidence.

Composition.—The composition of the budget surplus or deficit is as important as its overall size—if not more so. In short, some deficits can be more stimulative than others. The Administration's budget for fiscal 1972, in our view, is less stimulative than suggested by the size of the estimated deficit for two reasons:

(1) 80 percent of the deficit arises from the shortfall of revenues below their full employment level and from the increase in expenditures on unemployment compensation, welfare, and related items caused by the high unemployment.

(2) Another 10 to 12 percent of the deficit arises from tax changes enacted in 1971. One of these was the new investment credit, which will reduce revenues by approximately \$2 billion. Since the credit can be claimed on all new investment, the revenue loss is quite large relative to any *addition* to investment which may be induced by the credit. In the case of the new personal income tax cuts, the impact has been temporarily offset by an increase in tax withholding rates.

Realism.—In addition to basic questions about the effectiveness of the Administration's scenario for recovery we have doubts about the realism of their spending estimates. It is doubtful that the sharp increase in spending which the budget implies for the first half of calendar year 1972 will actually be achieved, especially since the Administration estimates are based on assumed quick enactment of controversial legislative proposals.

Restoration of full employment, which should be the primary objective of public economic policy, requires measures that will put people to work quickly and generate increased demand. At the same time, responsible planning for the future requires that we make neither permanent sacrifices of revenue nor shortsighted commitments to large and inflexible permanent expenditure programs. We propose two expenditure programs which would have the effect of putting people to work now, but the cost of which would diminish as full employment is approached. The first of these is a program of counter-cyclical aid to States and cities. The second is a substantially expanded program of public service employment. Without these programs, or similar ones, it seems probable not only that unemployment will

remain above 5 percent throughout this year, but that unemployment will continue far too high in 1973. With these programs, and with the attendant boost to consumer confidence and to private employment, unemployment can be reduced to 4 percent during 1973. Furthermore, unemployment can be reduced in a noninflationary manner because we would be putting people to work providing needed public services. We would not be creating skill shortages or other inflationary bottlenecks within the private sector.

Both of these programs were recommended by this Committee last August. Had they been adopted at that time, the country would now be far closer to full employment than it is.

The Administration's budget policy recommendations should be rejected on three fundamental grounds:

- (1) **The switch from a full employment deficit in fiscal 1972 to balance in 1973 will not achieve sustainable high employment.**
- (2) **The realism of the budget estimates is questionable.**
- (3) **The composition of proposed tax and expenditure changes is not designed to have maximum job-creating effect.**

Fiscal policy must remain stimulative for as long as necessary to restore full employment. At the same time, commitment to large future expenditures which cannot later be controlled must be avoided. Fiscal stimulus should be provided through expenditures which directly create jobs now and which will decline as the unemployment rate declines. Two major new programs are required:

- (1) **A substantially expanded public service employment program.**
- (2) **A system of counter-cyclical Federal payments to State and local governments designed to compensate these governments for the shortfall in their own revenues caused by high unemployment. The size of these payments would vary with the amount of unemployment. No payment would be made when the unemployment rate was below some specified level.²**

THE LONGER TERM BUDGETARY PROSPECT

The longer term prospect afforded by the Administration policies is even less reassuring than the short-term. Our revenue base has been reduced so as to render it incapable of adequately serving the emerging needs in the public sector. As indicated in more detail in chapter III, our tax system is riddled with loopholes and special advantages for the favored few with the result that vast potential revenues are lost to the country.

There is urgent need for action to reform the tax system and begin the restoration of our eroded tax base. Obviously this will prove an

² Senator Bentsen does not concur in this recommendation absent a full examination by the Committee of the potential problems of such a program.

extensive and time-consuming undertaking. We believe, however, that there is enough information and knowledge available to begin the long trek toward a broader and more equitable tax base.

Accordingly, we recommend that action be taken forthwith to eliminate enough of the most egregious and least defensible loopholes to provide an increase in revenues of approximately \$10 billion in fiscal 1974 and of a somewhat lesser amount in fiscal 1973.

SOCIAL SECURITY

Another problem arises from the increasing reliance placed on regressive payroll taxes. As discussed in the next chapter, the social security financing system should be reformed to make it more progressive.

We believe a substantial increase in social security benefits is needed immediately. The Administration proposals for social security include a 5 percent increase in benefits; an increase in the tax *base* to \$10,200 retroactive to last January; and a reduction in the increase in the tax *rate* already scheduled under existing law for January 1, 1973. Presently the combined employee-employer tax rate is 10.4 percent; under the Administration proposal, it would rise to 10.8 percent next January; but under existing law, if not changed, it would rise to 11.3 percent.

Even with the Administration-proposed changes from existing law, the social security system will take in more in receipts than it will pay out in benefits in fiscal 1973. Benefits need to be increased more than 5 percent. Five percent means an increase of only \$3.50 per month for those receiving the minimum benefit for single individuals. A larger increase in social security benefits can be soundly financed without increasing the tax rate at this time.

Social security benefits should be increased substantially more than the 5 percent recommended by the Administration. No increase in the tax rate in 1972 or 1973 is necessary to finance such a benefit increase.

PRICE-INCOMES POLICY

For many years, this Committee has consistently advocated the use of a price and incomes policy as a regular, continuing aspect of total economic policy. Therefore, we wish that we could commend the efforts at price and wage control which the Administration has undertaken since last August. Unfortunately, these policies are so late in being adopted, so complicated in their design, so weak in their administration, and so modest and vague in their goals that we are compelled to be severely critical and to recommend an immediate sweeping revision of policy.

Delay in the Adoption of Price-Wage Policy

When the present Administration first took office, excess demand had generated a genuine problem of inflation, acknowledged both within and outside the Administration. Rather than strengthen the anti-inflation efforts of the previous Administration by continuing the

“jawboning” efforts of persuasion or by reinstating voluntary price-wage guidelines, the new Administration pointedly rejected the use of any type of incomes policy. It turned instead to a policy of restraining the economy as the means of controlling inflation. At first the Administration, and many private observers, believed that inflation could be brought under control with only a modest rise in unemployment. In fact, the inflation, greatly strengthened by the Administration’s promise to avoid guidelines or controls, proved intractable. Encumbered by their negative commitment to avoid price and incomes policies, the Administration continued to let unemployment rise in the mistaken belief that this would work against inflation.

Rising unemployment is simply not the most effective weapon against the cost-push type of inflation with which we have been faced since at least the beginning of 1970. It was a mistake for the Administration to abandon incomes policies when they first took office; it was a greater mistake for them to delay a reversal of policy until after we had suffered high unemployment for over a year. The great human costs of high unemployment which we are still paying and will continue to pay for many more months are a legacy of the unconscionable 2½-year delay in adopting an incomes policy.

Complicated Design and Weak Administration

The present control machinery gives every evidence that it is going to prove less effective than it should be. The prime reason is its failure to concentrate on the sectors where control is needed and only those sectors. In most sectors of the economy, the forces of competition are adequate to keep prices responsive to demand and supply conditions. In some sectors, characterized by big business and by large labor unions, competition is not adequate. Both prices and labor costs can increase in the face of slack demand. Intense price or cost pressure can also arise in sectors subject to sudden sharp demand changes and/or supply shortages due to restricted entry. The construction and health care industries offer examples of this latter problem. The purpose of a price and incomes policy is to substitute for competition; to make prices and costs in these particular sectors behave as they would under competition. There is no need for a facade of controls covering the entire economy.

A massive legal framework designed to administer compulsory peace-time controls encompassing almost the entire economy is proving to be unworkable. There is no need for such a sweeping program. If we are to have controls, they should be concentrated on the limited sectors of the economy where they are needed.

This view was supported by witnesses at our Annual Hearings. Dr. Gardner Ackley, for example, argued for the termination of “all or nearly all compulsory controls over retail prices, rents, most personal services, and at pre-retail levels for a broad range of less important manufactured and processed goods, where effective competition prevails. . . . These are simply not the areas where cost-push inflation originates. Prices in these areas reflect the *effects* of cost-push inflation. But if the sources of that inflation are controlled, so will be its reflection in these prices.”

The present policy of elaborate efforts to rule on thousands of price decisions and hundreds of wage contracts simply means that the limited staff resources of the Price Commission and the Pay Board are spread too thin. Staff time is frittered away on decisions of no importance, while far too little attention can be given to the few big price and wage decisions which are of fundamental importance to effective inflation control.

A vital corollary of this is that the powerful enforcement value of public opinion is being lost. The most effective enforcement machinery available is public outrage when major pricing decisions are not in the public interest. But when the public is confronted with a barrage of information on price changes, with no indication of those which are important and those which are trivial, public opinion does not become effectively concentrated on the crucial changes. Indeed, faced with so many price changes and with the difficulty of evaluating which are justified and which are not, the public is, as Dr. Ackley put it, increasingly realizing that current retail price controls and rent controls are "essentially meaningless." The public is therefore beginning to believe "that the entire price-wage control effort is a fraud."

Given the very long time during which this Administration has been purporting to "fight inflation," first by creating unemployment and finally in recent months by imposing controls, given the high costs we are paying, the amount of progress which has been achieved is pitiful. The estimate that after controls have been in existence for well over a year and after unemployment has been near 6 percent for 2 years, the inflation rate will still be near 3 percent is a virtual admission that the control policy does not mean much.

The present price-wage control program is overly elaborate in its coverage, but the inflation goal is unduly modest and lacks specificity. The control system is too complex to be administered efficiently. De-control of large segments of the economy and a concentration of effort on only those sectors of the economy characterized by definite market power would enhance the chances for reducing inflation.

A Price-Incomes Policy for the Future

One unfortunate aspect of the ineffectiveness of the present poorly designed control system is that it might invite the conclusion that no price and incomes policy can be effective; that, indeed, such a policy is apt to be worse than nothing. We reject this conclusion.

We vigorously support efforts to make the U.S. economy more competitive and more efficient. Much can and must be accomplished in this direction, and we detail our recommendations in the remaining sections of this chapter. Nonetheless, it would be foolish to suppose that all elements of monopoly and all structural rigidities can be removed from the U.S. economy. Price and incomes guidelines will continue to be needed as one aspect of a total policy to restore and sustain noninflationary full employment.

It is unfortunate that the Council's Economic Report fails to make clear this continuing need. Indeed, it states that price-wage controls are expected to "fade away, leaving no permanent change in the system except the eradication of inflationary expectations."

As we return to full employment, it is vital that we do so without introducing new inflationary forces. This will require price-incomes guidelines as well as vigorous efforts to improve the structure of the economy. We will need an effective price-incomes policy even more next year than this year. We will continue to need it in subsequent years.

The present system of cumbersome mandatory controls should be abolished as rapidly as possible. It should be replaced by a permanent mechanism for the administration of a largely voluntary price-incomes policy. The real challenge to our ability to control inflation will come when the economy again approaches full employment. Attention should be focused *now* on getting ready to meet this challenge.

This Committee has repeatedly recommended the establishment of a board or agency to administer price-incomes policy on a continuing basis. We reiterate this recommendation and stress the following:

- **Policy should be focused on those sectors of the economy where market power seriously interferes with the price-regulating forces of competition.**
- **Labor, business, and consumer groups must participate in policy formulation.**
- **Price-incomes policy must have full backing from the President.**
- **It must be regarded as a continuing part of overall economic policy and must be coordinated with fiscal and monetary policy.**
- **The maximum degree of voluntary compliance must be sought. However, some limited enforcement power will be needed in the near term.**

POLICIES FOR IMPROVEMENT OF THE PRICE STRUCTURE

Achieving full employment with reasonable price stability will require vigorous Federal policies to improve the structure of product and labor markets. One essential thing the Federal Government must do is to initiate a comprehensive program for correcting government regulations and procedures that artificially inflate costs and prices. Such a program is needed both to achieve substantive improvements in economic performance and to add credibility to other aspects of the anti-inflation effort. In addition, the Federal Government must pursue an active anti-trust policy to maintain competition in the private marketplace.

The Committee has been unable to learn what the Administration's long-run policy is for correcting government-induced structural problems. Following a promising section title in the President's Economic Report, "Inflation and Unemployment in the Long Run," we are told that structural problems may and may not exist. The significance of Federal Government activities in creating these structural problems is not even mentioned. The extent of the Council's action for correcting structural problems is to say that it "will be making an intensive study of them in 1972."

While it is always useful to have additional studies, and certainly they are needed in this area, it is difficult to understand why specific actions to correct known structural defects cannot proceed while studies are in progress. This is especially so in view of the fact that the President, with great fanfare in June of 1970, established the Regulations and Purchasing Review Board "to determine where Federal purchasing and regulations drive up costs and prices." The Board was given a broad charter, which we are told is still in effect under the New Economic Policy, to review and evaluate all Federal activities that may contribute to rising costs and prices.

In a start toward fulfilling this charter the Regulations and Purchasing Review Board developed a list of Federal activities that appear to contribute to inflation. The Board's list includes government building acquisition, the Renegotiation Act, transportation regulation, import restrictions on oil, meat and other commodities, the Jones Act, the Buy American Act, the Davis-Bacon Act, Federal procurement, utility rate setting, and so on. As these examples illustrate, and as other such lists could confirm, many of the Federal Government activities that encourage higher costs and prices are well known. What is lacking is a comprehensive policy for reducing these government induced market distortions.

The Regulations and Purchasing Review Board itself, after making its original inventory of problem areas, and evaluating certain cases like the Jones Act and the Buy American Act, took almost no action to correct these problems.

When the Committee questioned former members of the Board on its effectiveness, there was agreement that the Board had not lived up to its promise and had not come up with any specific recommendations. Dr. Hendrik Houthakker, for example, gave this evaluation of why the Board had failed: "I think it is fair to say that the failure of this Board was one of the many reasons why the Administration was finally forced into the August 15 program. I think the speech which the President made in June 1971 was recognition of the adverse impact of various limitations of competition on our free enterprise system. But when it comes to the point of reform, most of the programs investigated turned out to be so strongly entrenched there wasn't much you can do about them."

It appears, then, that lack of knowledge about government induced structural problems is not as great as the lack of will to act. This should not be tolerated because it is clear that our overall goals for full employment and price stability cannot be achieved without fundamental structural reform.

We urge the Administration and Congress to act vigorously to reform government programs and activities that significantly contribute to inflation. Wherever import quotas, regulatory policies, government procurement policies, stockpile reserves, Federal subsidies, and/or other policies are found to artificially restrict market supply, or otherwise unnecessarily inflate prices, they should be eliminated or redesigned to be compatible with fulfillment of the Employment Act.³

It is also well known that structural inflation can result from a decline in competition as particular private markets become highly concentrated. A high degree of economic concentration will generally

³ Senator Humphrey does not join in this recommendation.

mean that prices are rigid downward, but less so upward. In addition, highly concentrated industries have little resistance to wage and cost pressures because it is easy for them to raise prices to cover the higher costs. In these industries prices are not primarily determined by competitive market forces but are "administered" by the firm to meet "target-rates-of-return" and other firm objectives.

It is the responsibility of the Federal Government to prevent the deterioration of competition in private markets by active anti-trust policies. But this Administration has not seen fit to be the advocate for competition. As in the case of the Regulations and Purchasing Review Board, the Administration has indicated the importance it attaches to anti-trust policy by not even mentioning it in the Economic Report. We reiterate the conclusion of the President's Cabinet Committee on Price Stability in 1969, with which we concur:

We recommend vigorous enforcement of the anti-trust laws as essential for reducing further the inflationary effects of discretionary power. Only to the extent that we maintain effective market competition can we continue to place primary reliance on private decisionmakers in our quest for high employment, rapid economic growth, and price stability.

MANPOWER AND EMPLOYMENT POLICY

Achieving the goal of full employment with relative price stability is contingent upon effective government programs to improve the structure of labor markets and of job opportunities. The Federal Government has a responsibility to help prepare individuals for specific job situations, to promote a general upgrading of skills throughout the economy, and to assure that job opportunities are available for those who want jobs.

The Manpower Development and Training Act of 1962 provided the basis for a government effort to ease structural changes in the economy for the worker. The program has admittedly encountered some difficulties but the major scope of manpower programs and the lack of previous experience account for many of the problems.

Structural problems arise in labor markets when changes in the composition of economic activity force some workers out of their jobs. Defense cutbacks in 1969 and 1970 and the slowdown in the commercial airline industry have displaced significant numbers of aerospace workers in recent years, for example. Yet shifts away from one sector of production should not be used, as they have been in the last two years, as a justification for tolerating large increases in unemployment. This same principle applies to workers who are displaced from their jobs as a result of import competition. A government policy which promoted strong economic growth, accompanied by adequate manpower programs, would have avoided the severe unemployment problems of the past two years.

As in the past, we continue to strongly advocate a comprehensive government program to deal with unemployment whether it is due to inadequate private demand, technological change, shifts in government expenditure patterns or the inequality of economic opportunity.

While structural economic changes often require retraining programs for displaced workers, these programs will be successful only if job opportunities are maintained and expanded. There is some value in retraining as a means of upgrading the general level of skills in the economy, but the Federal Government would be avoiding its responsibility if it simply trained workers for jobs that do not exist. The social and economic costs of manpower programs which do not result in employment for the trainee far outweigh any advantage. Moreover, it is wrong to raise the aspirations of the unemployed or disadvantaged by providing training but failing to provide job opportunities. Achieving our goal of full employment with price stability is contingent on availability of jobs whether in the public or private sector. The Government's responsibility for job creation cannot be divorced from manpower training efforts. Skill training that is not accompanied by a job opportunity is grossly unfair to the individual and costly to the Government.

We strongly recommend, while continuing to stress the need for manpower programs, that training programs be tied more closely to provision of job opportunities. The Government is responsible for assuring that job opportunities are available for those who wish to work. These job opportunities may be stimulated through growth of aggregate demand in the private sector and through expansion of the public sector. We cannot overemphasize our belief that job training must be accompanied by jobs.

Given economic conditions that prevailed in 1970 and 1971, aggregate demand in the private sector was insufficient to stimulate enough employment opportunities for a continually growing labor force. Since the prospects for a significant increase of private demand in 1972 are not particularly strong, government intervention in labor markets is warranted. The limited Public Service Employment Act which was passed last year has thus far provided over 140,000 jobs, but even if all the funds available for the current year are spent, only around 25,000 more persons can be hired.

In the absence of new policies which foster job creation, not only must we anticipate that the unemployment rate will still be above 5 percent at the end of this year, but that it may remain well above 4 percent throughout 1973. There is no need to accept this continuing high unemployment. The public sector of our economy has important unmet needs. Willing workers are available. The administrative machinery set up under last year's Act is capable of handling a larger program.

As stated above in the Fiscal Policy Section, the public service employment program should be substantially expanded.

The program should also be expanded to include limited funds for the purchase of the materials and equipment which will be required. It is not possible to estimate precisely the necessary size of the program or its exact cost. The mere existence of a meaningful government commitment to directly expand employment would be a great spur to confidence and to private job creation. In any case, a willing worker put to work in useful employment is a gain to society, not a cost. It would be foolish to argue that we cannot afford to put people to work.

Employment Outlook for Teenagers and Young Adults

If manpower programs are to continue to serve a useful purpose, they must be responsive to basic changes in economic conditions. The late sixties and early seventies have witnessed rapid growth in the number of young people seeking jobs. Again we must stress that the changing composition of the labor force is not a valid reason for accepting permanently higher levels of unemployment. Instead, manpower programs addressed specifically to these labor groups must be instituted.

In the case of unskilled teenagers entering the labor force, programs which combine work and training must be expanded. Providing opportunities for employment among teenagers may be difficult because they are only part-time workers or because they may move to several different jobs before accepting permanent employment. As a result many employers are reluctant to hire young people. It is especially important that adequate programs be developed to assure training and a positive initial job experience for young people who are just entering the labor force.

Furthermore, it is important to note that the demographic conditions which were an underlying factor in the large influx of teenagers during the late 1960's have diminished somewhat. The great majority of the baby-boom era population is now becoming a part of the 24-35 age group. Creating job opportunities and providing training for these young adult workers whose early work experience may have occurred in a high unemployment period is especially important.

The Committee urges that training and employment programs for teenagers and young adults continue to be strengthened and that these programs be flexible enough to accommodate changing economic conditions.

Equal Employment Opportunity

Despite the specific wording and intent of the 1964 Civil Rights Act to eliminate job discrimination on the basis of sex, race or creed, inequality of job opportunity remains a serious problem. Elimination of discriminatory hiring practices is desirable not only from a social and human standpoint, but it would aid greatly in easing pressures on labor markets. The Equal Employment Opportunity Commission was created as part of the 1964 Act, but unfortunately it was not empowered to enforce the provisions against discrimination. We applaud the recently passed legislation which would permit the Commission to file suit against employers, whether private, educational or government, that discriminate on the basis of sex, race or religion.

Equal employment opportunity for all remains an unmet goal. The stronger legislation recently passed by Congress must be vigorously enforced.

The Employment Service

As originally conceived the Federal-State Employment Service was to provide job placement through a matching of job slots with job applicants. While this concept is an attractive one in principle, in practice the Employment Service's performance has been disappoint-

ing and inadequate. During the last ten years, the number of people placed through the Employment Service has actually been declining from 6.7 million in 1962 to 5.8 million in 1968 and to 4.6 million in 1970. In the last several years, funds have been provided in the Budget for computerization of job placement services—for establishment of job banks. While it is still premature to judge the effectiveness of job banks, early reports suggest that they have provided job listings rather than job matching services. There are several possible alternatives available for strengthening the Employment Service. These include Federalization, better State and local control in conjunction with manpower planning councils, or more direct Federal budget control by use of a contract grant system. These and other possibilities must be explored in order to make the Employment Service a viable tool in easing structural problems in labor markets.

Testimony given during the Committee's annual hearings suggested that the Employment Service is especially unresponsive to the needs of minority groups and has in some cases seriously discriminated against Blacks and Spanish-speaking groups. According to a recent report by the Urban Coalition, the difficulties of dealing with the Service have resulted in mistrust, hostility and discouragement among the disadvantaged. As a consequence "more individuals are dropping out of the labor force and are adding to the very problem that manpower programs were designed to solve."⁴

The difficulties of dealing with the Employment Service are compounded for job seekers who do not speak English. This is a further deterrent for Mexican-Americans and other minorities who vitally need placement services. The staffs of State employment offices should be expanded to include more personnel who speak foreign languages.

The Employment Service must be strengthened considerably in order to better perform its job-matching function. Studies of alternative reforms should be undertaken with a view to insuring that adequate placement assistance be provided for all those seeking help, including minority groups. The Employment Service must acquire sufficient personnel who speak Spanish and other languages so that inability to speak English will not be a barrier to the use of job placement services.

STRENGTHENING ECONOMIC STATISTICS

The formulation of economic policy will be haphazard and subject to more than the normal margin of error if the economic statistics which support policy decisions are not sufficiently accurate. Our Federal statistical programs are among the best in the world, yet there are important areas of the programs where significant improvements need to be made. This Committee has long and vigorously supported a continued upgrading of existing statistical programs and the funding of new initiatives. We are glad to see that the new budget proposes additional funds for improving the national income accounts.

The credibility of the interpretation of our statistics is equally as important as their accuracy. Public confidence in government eco-

⁴ "Falling Down on the Job: The United States Employment Service and the Disadvantaged," prepared by the Urban Coalition and the Lawyers' Committee for Civil Rights Under Law, June 1971.

conomic policy, which has been one missing ingredient in the last few years, is closely related to credible economic data. Every Administration, including the present one, seeks to place the best possible interpretation on data as it is released. Political analysis of previously released data is to be expected. But when this politicizing of statistics is accompanied by apparent efforts to restrict public access to professional technical explanation of the statistics, public confidence in the statistical programs cannot help but be affected.

While the extent of an administration's political comment on statistics remains its own prerogative, this Committee vigorously protests recent attempts to downgrade the technical non-partisan initial release of data. Early in 1971, the Administration cancelled the Bureau of Labor Statistics press conferences on the price and employment situation. These press briefings, which did not supplant the political comment of appointed Administration officials, were conducted by professional technicians who gave a nonpartisan objective explanation of the data to the press and public. For many years press briefings on employment and prices had been conducted by the BLS professional staff, and this practice was consistent with the recommendations made in 1962 by the President's Committee to Appraise Employment and Unemployment Statistics (also known as the Gordon Committee).

The Gordon Committee emphasized that "the need to publish data in a nonpolitical context cannot be overemphasized. By and large, this has been the case—the collection and reporting of the basic data have always been in the hands of technical experts. Nevertheless, a sharper line should be drawn between the release of the statistics and their accompanying explanation on the one hand, and the more general type of policy-oriented comment which is the function of officials responsible for policymaking on the other."

By cancelling the monthly press briefings, the Administration has failed to comply with this recommendation and has seriously eroded the credibility of our entire statistical program.

The Bureau of Labor Statistics press briefings on the monthly price and employment statistics should be restored and similar technical briefings should be initiated for other major economic statistics.

We recognize that while we benefit from one of the best statistical programs available continued refinements must be undertaken if the quality of our data is to be preserved. Changing economic conditions and the availability of more sophisticated statistical procedures warrant a reevaluation of our current data. It is generally recognized, for example, that data on the geographic, age and sex composition of unemployment is essential for development of adequate job creating and training programs to meet needs of different labor groups. In cases where particular data series were inadequate, the continued growth of the economy has emphasized even more their weaknesses.

Aside from the issue of confidence in our employment and unemployment data related to cancellation of the BLS press briefings, there is the question of the statistical reliability of these data. Private economists and the Administration have recently raised serious points relating to the collection of data and to the items which should or

should not be included in the official definition of employment and unemployment. The Gordon Committee served a useful function in the early 1960's in developing a consensus definition of labor force data. We noted with concern that the President's Commission on Federal Statistics, which deliberated for over a year before making its report in late 1971, failed to address itself to the critical areas of employment and price statistics.

Given the changing economic conditions and evolving needs of policy makers over the last 10 years, we favor an in-depth study be again conducted to air the issues and make recommendations for improving employment statistics. Among those questions to be addressed are the measurement of discouraged workers, whether or not these workers should be counted as unemployed, and how age and sex shifts in the labor force should be reflected in the data. The increasing importance of State and local data cannot be overemphasized. With increasing frequency, economic aid measures, such as extended unemployment compensation, are tied to State unemployment data. There is some doubt about the reliability and comparability of data collected by individual States. The employment study group should also address this question of better State unemployment data.

Such a study cannot be completed in a very short period of time. The Gordon Committee deliberated for the better part of a year before making its recommendations; and the issues have not become less complex over the last 10 years. If a committee were appointed shortly it could be required to report in 1973. This would also insure that the political pressures of an election year would not impinge on the committee deliberations. A committee made up of nonpartisan, nongovernment experts would best serve the interests of all for an in-depth and impartial study.

We recommend appointment of a nonpartisan, nongovernment committee to evaluate our present labor force statistics; the committee should make its recommendations in approximately one year.

In the past three years, this Administration has repeatedly emphasized the importance of reducing inflation.

While the Committee has no intention of discounting the importance of price stability, we stress the need for accurate measurement of price trends. Statistical experts have questioned the comprehensiveness of present price statistics and the merits of the methodology that is presently employed.

We recommend that a committee be appointed to evaluate the methodology and scope of our present price statistics. This committee should make its recommendations in approximately one year and should be nonpartisan and nongovernment in nature.

These two areas in which we suggest specific studies do not, of course, cover the range of needed improvements in our statistics. Our measures of national income, monetary variables, housing activity, business investment, foreign trade, consumption—to name but a few of the other statistical programs—are in need of careful and continuing review and improvement if we are to have adequate information for economic policy implementation.

III. TOWARD MORE EQUITABLE AND EFFECTIVE FEDERAL PROGRAMS

The priorities of government should reflect choices that serve the most pressing needs of the people. This has not been the case with the priorities pursued by the present Administration. Major deficiencies include renewed emphasis this year on larger expenditures for national defense, space, and public works, last year's unbalanced tax proposals, continuing failure to control subsidies and outmoded government programs, and the absence of a commitment to policies that will enable the poor to share in the benefits of our economy. This chapter will discuss these issues primarily in the context of civilian priorities, while the following chapter will focus on the same issues as they are relevant to national defense.

We lay special emphasis on the goal of establishing an optimum distribution of income and wealth in this country because this is what determines the extent of economic independence and well-being in our society. Although other conditions are necessary to insure that our market economy serves society, the economy will be basically inefficient and unjust if it has the wrong distribution of economic benefits.

In the United States, as of 1969, the richest fifth of the population received 41 percent of the income while the poorest fifth received 6 percent. The average income of the richest 20 percent of all families was about seven times that of the poorest 20 percent of all families. Furthermore, the distribution of wealth has been even more unequal than the distribution of income. In a Federal Reserve study done in the early 1960's, the wealthiest 20 percent of the population owned about 75 percent of private assets, while the poorest 25 percent had debts at least as great as their assets.¹ There is no indication that this situation has changed.

The appropriateness of this distribution of income and wealth is a question that can only be resolved by the President and Congress. One of the major functions of Government is to make collective judgments on what is a just distribution of economic benefits. As the subsequent sections of this chapter will show, this Administration's priorities do not serve to equalize the share of all citizens in these benefits. It is also to be regretted that the Congress has not placed sufficient emphasis on this objective.

We urge both the Congress and the Administration to place greater emphasis on improving the distribution of income and wealth in this country. Government tax policies and expenditure programs should be designed to serve that purpose.

¹ Federal Reserve Bulletin, "Survey of Financial Characteristics," March 1964, Washington, D.C.

PRESSING NEED FOR TAX REFORM

Despite the fact that the fiscal year 1972 deficit may approach \$40 billion, that tax burdens are becoming more regressive, and that the long-run revenue projections of the Federal Government indicate we will not be able to finance essential public programs, neither the President's Economic Report nor the Budget provide recommendations to reform the Federal revenue system. We do not accept the assessment of the Secretary of the Treasury that these matters can be postponed.

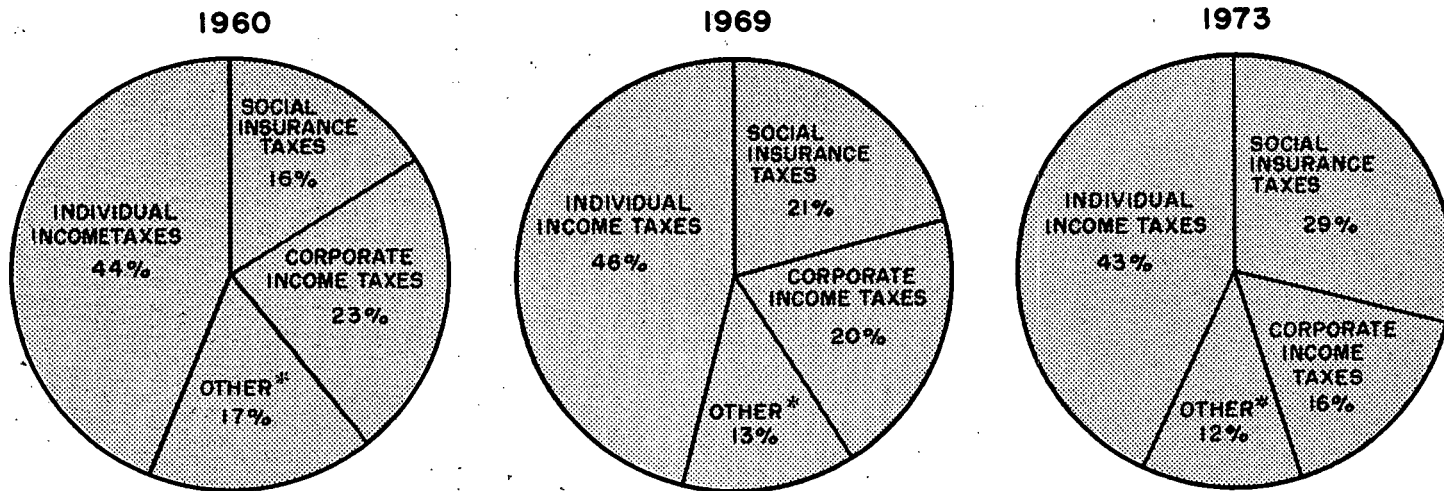
The fundamental purpose of taxes is to obtain the resources needed to pay for governmental activities. Considerable effort has gone into designing a progressive tax system—at least at the Federal level—which places a proportionally greater burden on those who have greater ability to pay. In general, this effort to make taxes progressive has been one of the most positive elements of our Federal tax system. It has enabled the Government to obtain needed levels of revenue and to do so in a way that distributed the burden of taxes fairly.

The tax system is used for other purposes, however, such as stimulation of economic growth, stabilization of overall economic activity, and as an incentive to encourage the use of resources in one direction rather than another. This latter use of taxes has by now proliferated to such an extent that the Federal tax system has lost much of its revenue-producing potential and its reputation for fairness. Many wealthy individuals continue to go tax free. The composition of overall revenues has shifted to regressive payroll taxes rather than the more progressive income taxes. Special tax provisions have expanded in the direction of favoring high income and wealthy individuals. Finally, some individuals below the poverty line are still required to pay Federal taxes.

One indication of the unfairness of the tax burden can be seen in the shifting composition of the Federal tax system away from the relatively progressive individual and corporate income taxes. Chart 4, showing Federal receipts by source for fiscal years 1960 and 1969 and Administration estimates for fiscal 1973, illustrates this trend. Individual income taxes drop as a share of the total tax burden from about 46 percent in fiscal 1969 to an estimated 43 percent in fiscal 1973. At the same time, corporate income taxes, which in 1960 provided 23 percent of total revenue, drop from 20 percent in 1969 to an estimated 16 percent in 1973. Taken together, this represents about a 7 percent decrease in the most progressive Federal taxes in only 4 years. During the same time social insurance taxes rose from almost 21 to an estimated 29 percent, or approximately 8 percent. Thus, the effect of the revenue changes from fiscal 1969 to fiscal 1973 has been to shift the tax burden away from the relatively progressive income taxes to the more regressive payroll taxes.

CHART 4

PERCENT OF FEDERAL BUDGET RECEIPTS, BY SOURCE



* Other includes excise taxes, estate and gift taxes, customs duties and miscellaneous receipts.

Table 4 lists the major tax changes that have occurred since 1969 and their effects on revenues in subsequent years. The revenue loss associated with these changes might not be of concern if the reduced revenues were strengthening the income and spending power of poor and average income citizens. In fact, the specific tax reductions, although providing some tax relief to poor and average income taxpayers, on balance benefit business firms and upper income taxpayers.

TABLE 4.—ESTIMATED REVENUE EFFECT OF THE 1969 TAX REFORM ACT, ADR AND THE REVENUE ACT OF 1971

[In billions of dollars]

	Fiscal years—			
	1970	1971	1972	1973
1969 Tax Reform Act:				
Individual income tax.....	-0.1	-2.4	-5.8	-8.6
Corporate income tax.....	+1.3	+3.0	+3.7	+4.0
Total, 1969 Act.....	+1.2	+ .6	-2.1	-4.6
Asset Depreciation Range (ADR)¹.....		- .3	-1.0	-1.9
1971 Revenue Act:				
Individual exemptions and deductions.....			-2.7	-2.6
Job development credit.....			-2.5	-3.6
Domestic international sales corporation.....			0	-.1
Repeal of auto and truck excise taxes.....			-2.5	-2.3
Total, 1971 Act.....			-7.7	-8.6
Grand total.....	+1.2	+ .4	-10.8	-15.1

¹ The revenue loss estimates for the ADR provision are corrected to take into account congressional modifications made in conjunction with the 1971 Revenue Act. Congress reduced the liberal depreciation guidelines provided by administrative action in January 1971, by disallowing full depreciation for assets in the 1st partial year of their use (referred to as the 1st-year convention). This reduced the revenue losses attributable to the ADR provision to the estimates provided in the table above.

Source: Office of the Secretary of the Treasury, Office of Tax Analysis, and Joint Economic Committee.

The 1969 Tax Reform Act reduced some of the special provisions in the income tax law, such as the depletion allowance, repealed the investment tax credit, and significantly lowered general tax rates for individuals. In terms of fiscal 1973 revenues, the effect of the Act is to increase corporate income taxes by about \$4 billion and reduce individual income taxes by about \$8.5 billion. The primary beneficiaries of these tax reductions are middle-income taxpayers, although modest benefits accrue to low-income groups.

This trend was reversed with revenue changes initiated by the Nixon Administration. The Asset Depreciation Range (ADR) provision, instituted by the President in January 1971, permitted business firms to accelerate depreciation claims by 20 percent. Although subsequently modified and reduced by Congress, this provision lowers fiscal 1973 revenues by about \$1.9 billion. Last August the Administration proposed tax changes which, with modifications, became the Revenue Act of 1971. Of the total \$8.6 billion reduction in tax receipts estimated for fiscal 1973 as a result of the provisions of this Act, \$3.7 billion will be direct reductions in business tax payments, \$2.3 billion will be excise tax reductions which will primarily provide additional stimulus to the auto industry, and only \$2.6 billion will be reductions in general individual income tax liabilities.

Taken together, the tax changes since 1969 will erode 1973 Federal revenues by about \$15 billion. Although some of the tax reductions in

the 1969 Tax Reform Act benefit middle and low income taxpayers, these have to a great extent been offset by subsequent tax reductions benefiting business and upper income taxpayers. The net effect of these Federal tax changes has been to maintain a system of special provisions whose benefits are distributed primarily to the wealthy.

For example, the largest share of special benefits in the individual income tax accrue to the higher income classes. In a forthcoming study prepared for the Joint Economic Committee, Dr. Joseph Pechman and Dr. Benjamin Okner have identified \$77 billion of special provisions in the individual income tax law and distributed the benefits of those provisions by income class.² As may be seen in Table 5, the low segment of the income distribution scale with annual incomes below \$5 thousand, containing 18 percent of the families, and receiving 3.9 percent of adjusted gross income, receive only 1.4 percent of the benefits of the special provisions in the income tax law. Even the average families, those with an annual income between \$5 and \$10 thousand, and comprising 28 percent of the total families, receive only 8.5 percent of the tax benefits. At the upper end of the income scale, however, we see that about 1 percent of the families, who receive 9 percent of the adjusted gross income, also receive approximately 24 percent of the special benefits of the tax system. Moreover, 47 percent of the total tax benefits are received by the 8 percent of families having incomes in excess of \$25,000.³

TABLE 5.—FAMILY DISTRIBUTION OF EXPANDED ADJUSTED GROSS INCOME AND FEDERAL INCOME TAX BENEFITS BY INCOME CLASS, 1972

[In percent]

Expanded adjusted gross income class (in thousands)	Families	Expanded adjusted gross income	Income tax benefits
Under \$5.....	18.2	3.9	1.4
\$5 to \$10.....	27.5	15.9	8.5
\$10 to \$15.....	24.9	23.7	14.8
\$15 to \$20.....	14.9	19.7	16.0
\$20 to \$25.....	7.0	12.0	12.4
\$25 to \$50.....	6.3	15.6	22.5
Over \$50.....	1.2	9.2	24.3

Note: Details may not add to 100 percent due to rounding.

Source: Data are derived from Joseph Pechman and Benjamin Okner, "Individual Income Tax Erosion By Income Class", in "The Economics of Federal Subsidy Programs: A Compendium of Papers, pt. 1," forthcoming. Expanded adjusted gross income represents an income base that has been expanded to include certain forms of income, such as realized capital gains, which are not included in conventional measures of adjusted gross income. Income tax benefits represents what the study refers to as the "increase in tax liabilities," which is the additional taxes that would be paid if all special provisions in the income tax law were eliminated.

Despite the distorted distribution of tax benefits, the erosion in the income tax system might be acceptable if the special provisions

² The \$77 billion includes all special provisions of the income tax law that reduce the comprehensive income base defined by the authors. The \$38 billion of tax subsidies included in the Joint Economic Committee staff study referred to on page 43 of this report included only those corporate and individual tax provisions designed to alter particular private market incentives. Differences also arise because of variability in estimation techniques and because the Pechman-Okner study is based on 1972 projected income levels while the staff study uses 1970 data.

³ For additional details on the Pechman-Okner study see "Individual Income Tax Erosion by Income Class," in *The Economics of Federal Subsidy Programs: A Compendium of Papers*, Joint Economic Committee, forthcoming.

efficiently achieved the specific social or economic goal toward which they are aimed. A somewhat distorted distribution of benefits might be the price that must be paid for an oil depletion allowance to stimulate oil exploration or for an excess depreciation provision to stimulate the production of rental housing. In fact, there is no body of significant evidence showing that these special tax provisions achieve their specific objectives, let alone evidence showing that they achieve their objectives efficiently.⁴ In recent testimony before the Subcommittee on Priorities and Economy in Government, Professor Stanley Surrey made the following evaluation of the evidence and analysis available to justify these special tax provisions:

I think you can also say that less critical analysis is paid to these tax subsidies than almost any direct program that the Congress considers and these tax subsidies simply tumble into the law without any supporting studies; they are propelled by cliches, debating points and scraps of data that are passed off as serious evidence. A tax system that is so vulnerable to this injection of extraneous, costly and ill-considered expenditure programs is simply in a very precarious state from the standpoint of the basic goals of tax fairness.⁵

Finally, the erosion of the income tax system makes it very difficult for the Federal Government to maintain its long-run revenue obtaining capabilities. The long-term projection of full employment revenues and expenditures contained in the budget shows a positive budget margin of only \$5 billion through fiscal 1976. Such a small margin in future years means that the Government faces a serious fiscal crisis. The Federal Government will either have to hold discretionary expenditure increases to \$1.25 billion a year, operate with full employment deficits for the foreseeable future, establish additional taxes, or aggressively pursue tax reform.

The rapid growth of the payroll tax indicated above reflects both the accomplishments achieved and the problems to be faced with the social security system. The payroll tax has grown rapidly because it is the financial basis for retirement income support, protection against disability, aid to the survivors of deceased workers, and medical services.

⁴ Senator Bentsen notes that the percentage depletion allowance was reduced by the Tax Reform Act of 1969 from 27½% to 22% and that capital expenditures for domestic exploration for oil and natural gas fell \$600 million between 1969 and 1970 with figures not yet available for 1971. Exploratory wells drilled fell from 9701 in 1969 to 7693 in 1970 and fell again to 6922 in 1971. Total wells drilled fell from 34,053 in 1969 to 29,467 in 1970 and fell again to 27,300 in 1971. The total footage drilled fell from 160.9 million feet in 1969 to 142.4 million feet in 1970 and to 128.3 million feet in 1971. In that the nation is currently experiencing significant short falls in domestic production of natural gas relative to demand and is producing domestic petroleum reserves at close to capacity while requirements for such products are increasing, any further change in tax policy relating to exploration and development of such reserves should not further discourage investment in these activities.

⁵ "The Economics of Federal Subsidy Programs" hearings. Subcommittee on Priorities and Economy in Government, Joint Economic Committee, Part I, Jan. 14, 1972.

Social security has been one of the great achievements of the Nation. But these significant achievements should not blind us to the reality that the payroll tax is a regressive tax. The present payroll tax, establishing a flat tax rate on earned income up to \$9,000, places a proportionately larger burden for the financing of social security on the lower and middle-income wage earners. For the working man making \$9,000 a year, the direct tax rate is 5.2 percent, while, for the individual making \$50,000 a year the direct tax rate is about 0.8 percent. In addition, the payroll tax applies without regard to the number of dependents of the taxpayer. Finally, since the payroll tax is levied beginning with the first dollar earned, it is exacted from workers who are below the poverty level. Although these inequities have been serious since the inception of this tax, the increased reliance placed upon the payroll tax aggravates the regressivity. Suggestions have been made for reform, and Congress and the Administration should carefully consider these proposals.

In addition to taxes on income, our society has generally supported progressive taxes on property transferred from generation to generation in order to prevent the continued accumulation of great wealth. At the Federal level, we have pursued this objective by establishing steeply progressive estate and gift taxes. The estate tax, for example, begins at 3 percent on the first \$5,000 of the taxable estate and rises to 77 percent on a taxable estate in excess of \$10,000,000. Like the income taxes, however, these taxes have become so filled with special provisions that the effective rates are quite low. Of the total Federal estate tax returns filed in 1966, for example, the average rate was 26 percent on estates with an average value of \$270,000. As a result, the Federal estate and gift taxes have provided only about 2 percent of total Federal revenues.

Taken together, the above weaknesses in the Federal revenue system are quite serious and require remedy.

We urge the Administration to provide to the Congress by this summer detailed evaluations of at least one-third of the special provisions in the individual and corporate income tax laws, so that Congress can decide whether the provisions fairly distribute their benefits and efficiently achieve their specific objectives.

The social security tax system should be made more progressive.

The Federal estate and gift taxes should be re-examined to determine if they might be suitable as additional revenue sources.

In the future, the Department of the Treasury should provide the Congress with detailed analytical studies of proposed special provisions in the tax law prior to enactment. In addition, the Department of the Treasury should provide analytical evaluations of the same provisions periodically thereafter, beginning no later than three years after enactment.

MAJOR EXPENDITURE PRIORITIES IN THE 1973 BUDGET

As in past budget messages, the Administration again this year argues that American priorities have been dramatically reordered toward greater emphasis on human resource programs relative to defense programs. As evidence, it compares the share of budget outlays allocated to human resource programs (45 percent) to the share of outlays allocated to national defense programs (32 percent). Human resource programs, as defined by the Administration, include the functional budget categories of income security, education and manpower, health, and veterans benefits and services. The measure of national defense expenditures is the functional category of the budget called national defense.

The Administration's presentation of how priorities are changing is misleading. In the first place, the category human resources, which excludes such areas as housing and environment programs but includes Civil Service retirement, cannot serve as any truly adequate guide on what programs are aimed at fulfilling pressing human needs. Second, about 80 percent of the programs in the human resource category are relatively uncontrollable in that their growth is fixed by previously enacted law. In no sense can these expenditure increases reflect new Administration priorities.

In order to understand the major priorities advocated by the President in FY 1973, one should not focus on total spending in each functional category, but primarily on increases in new obligational authority. Requests for new authority measure the future commitments for new and expanded programs the President is asking the Congress to fund in the fiscal year under consideration. These commitments, along with estimates of the lifetime costs of new programs, provide a reasonably complete view of what priorities the President is presenting to the Congress. Furthermore, it presents Administration priorities in a budgetary context that allows congressional review and alteration.⁶

Table 6, which summarizes the major shifts in obligations between fiscal 1972 and 1973, shows approximately how the composition of the budget will change. Total new obligational authority is estimated to increase by about \$21 billion, or 8 percent, from \$249.8 billion to \$270.9 billion. There are no major program decreases from the fiscal 1972 budget, a fact that is itself notable, so that this overall increase of \$21 billion represents the total budget resources to be devoted to new or significantly expanded programs in fiscal 1973 and future years.

The most striking aspect of the priorities reflected in Table 6 is the large increase in funding requested for national defense. In addition to that, the Administration is requesting increased spending authority in the defense-related areas of military security assistance, the space shuttle, and veterans benefits. On the civilian side, the major

⁶ No measure of Presidential priorities is by itself completely satisfactory. Unfortunately, full lifetime cost of new programs is often not contained in the budget. The space shuttle for example, would eventually cost many billions of dollars, but this is nowhere made clear in the budget. The information contained in the budget is not adequate for a thorough analysis of expenditure priorities. Requests for new obligational authority also has the weakness that previously authorized but unused spending authority can be used to rapidly accelerate outlays in any particular fiscal year. The President may in this way rapidly expand a program in a given fiscal year without requesting new authority from Congress. It is significant that the President cannot *initiate* a new program in this manner, however.

Administration proposal is general revenue sharing. The \$3.5 billion social security increase largely reflects Congressional initiatives as embodied in the pending H.R. 1 legislation.

TABLE 6.—Major changes in new obligational authority in fiscal year 1973

[Billions of dollars]

Department of Defense, Military	6.3
Military Security Assistance ¹	.5
Veterans Benefits	.2
Space Shuttle	.2
General Revenue Sharing	5.3
Welfare Reform	.5
Emergency School Assistance	.5
Medicare ²	.5
National Educational Institutions ³	.2
Public Works ⁴	.3
Civilian Research and Development	.4
Social Security Increases	3.5
Other	2.7
Total	21.1

¹ Includes conventional military assistance and related economic supporting assistance that is not included in Department of Defense estimates of military assistance.

² Since budget authority for these trust funds equal receipts, and since trust fund outlays are determined by the number of beneficiaries, outlays instead of budget authority is shown for this item.

³ Includes new funding for the National Foundation for Higher Education and the National Institute of Education.

⁴ Includes additional new funding for the Corps of Engineers and the Bureau of Reclamation.

Source: Estimated from data in *The Budget of the United States Government, Fiscal Year 1973*.

The issue of general revenue sharing was fully discussed by this Committee in last year's Annual Report. We too place high priority on aid to States and cities, but we find many aspects of the Administration's proposed solution unsatisfactory. One important cause of the current financial difficulties of States and cities is the recession of the past two years. In Chapter II of this Report, we discuss the need for immediate counter-cyclical aid to State and local governments.

We seriously question whether a large increase in defense spending will in fact contribute to our national security. This we discuss in detail in the chapter on national security.

Many other aspects of the priorities reflected in this year's budget are disturbing. In last year's budget, the President provided a table called "Selected Economies and Reforms in the 1972 Budget," and admonished that, all too often, "all Federal activities continue unless vigorous efforts are made to curtail them." The failure to significantly reform any existing programs in this year's budget indicates a retreat. Resource misallocations cannot be corrected unless we are willing to cut back as well as to expand. In previous Reports, this Committee has identified numerous areas of unjustified expenditure, such as unnecessary urban superhighways and grandiose public works.

The Administration's own projection of the future budget situation makes it clear that unless we do cut back on some existing

programs, major tax increases will be required to provide even minimal steps toward meeting growing public needs.

The Administration's budget presentation, with its emphasis on the relative shares of total spending going to defense versus human resources, merely obfuscates serious analysis of expenditure priorities. Uncontrollable increases in trust fund expenditures are discussed as if they reflected deliberate Administration decisions to reallocate resources toward social programs.

The Administration technique of explaining the shift in budget priorities is unsatisfactory. An analysis of major controllable program increases, as well as major recommended program decreases, should be regular budget features. Requested increases in new obligational authority by program should be more prominently shown in the budget and more fully justified.

In addition to the immediate decisions Congress must make on the President's budget, the Congress should give additional attention to the more rational setting of the Nation's long-run priorities. Too often, major priority decisions are made under short-run pressures to do *something* to stimulate the economy and decrease unemployment. The fiscal program proposed by the Administration last August as part of the New Economic Policy represented a poor choice of tax and expenditure measures, designed to encourage the use of additional resources in automobile production, defense spending, export subsidies, and increased private investment, while postponing welfare reform and aid to States and cities. Further, the Administration proposed these new priorities suddenly at a time when the state of the economy had so worsened that there was no longer adequate time for full consideration of alternatives. The result has been that the setting of specific priorities was done in altogether too precipitous a fashion. It is important that this does not happen again.

Sudden requests for emergency legislation without adequate opportunity for review make it impossible for Congress to rationally set national priorities. The Administration should by the coming summer provide Congress with a proposed list and accompanying analysis of high priority programs which could be initiated or expanded in the event that Congress decides additional measures are needed to promote economic recovery.

FEDERAL SUBSIDY PROGRAMS

Much of the growth in the Federal Government has consisted of activities that the private sector could not do, but which were deemed essential to the general welfare. The Government has provided for the national defense, maintained a monetary system, funded the public debt and maintained a fiscal policy, regulated international trade, and collected revenues to finance these activities and the general administration of government.

A less obvious but quite important government activity takes the form of subsidies to producers and consumers to alter their behavior in particular private markets. In this case the Government does not take over the activity, and run it as a public function for the general welfare, but instead provides financial assistance to special groups in

the private sector to get them to do things that, it is argued, are in the public interest. The full significance of such subsidies in the American economy is not known, but it appears they are quite important because they change private market incentives, reallocate resources within the private sector, change the structure of private markets, alter the distribution of income, and cost the taxpayer a great deal of money.

Moreover, to the extent that subsidies are not carefully scrutinized and evaluated, they may waste national resources, cause costs and prices to rise, and allow special interest groups to become entrenched beneficiaries of the public dollar. Despite the obvious significance these subsidies have for the overall performance of the economy, the Nation has paid scant attention to this area in its past policies and in the analysis contained in this year's Economic Report and Budget.

The Committee, concerned for some time about the lack of public information and analysis of these special benefit programs, has initiated a series of studies and hearings in this area.⁷ The first publication in this series, a Committee staff study entitled "The Economics of Federal Subsidy Programs," attempted to determine the pervasiveness of major subsidy programs as a prelude to further investigations by the Committee. The result of that study was an estimate that the fiscal year 1970 gross budgetary cost of Federal subsidy programs was approximately \$63 billion. Table 7 provides a summary view of the financial forms these subsidies take as well as their area of direct economic impact. As one can see, the Federal Government grants subsidies in cash, special tax advantages, credit assistance, and benefits-in-kind such as housing or food. The direct impact of these subsidies is scattered throughout the private market system, including the areas of agriculture, food, medical care, manpower, education, international trade, housing, natural resources, transportation, and commerce and economic development. It is probably no exaggeration to say that subsidies are the dominant form of government intervention into the private incentive structure of particular private markets.⁸

TABLE 7.—MAJOR FEDERAL SUBSIDIES, FISCAL YEAR 1970
(In millions of dollars)

Function	Form				Total
	Cash payment	Tax	Credit	Benefits-in-kind	
Agriculture.....	3,879	880	443	1,593	5,202
Food.....				4,617	1,593
Medical care.....	973	3,150	NA		8,740
Manpower.....	1,991	550			2,541
Education.....	1,976	785	434	409	3,604
International trade.....	106	420	623	34	1,183
Housing.....	195	5,680	2,550		8,425
Natural resources.....	330	1,970	22	712	3,034
Transportation.....	300	10		362	672
Commerce and economic development.....	2,051	15,635	59	1,518	19,263
Other.....		9,400			9,400
Total.....	11,801	38,480	4,131	9,245	63,657

¹ The individual totals of each financial form are rounded up so that the total cost is approximated at \$63,000,000,000.

Source: *The Economics of Federal Subsidy Programs: A Staff Study*, the Joint Economic Committee, Jan. 11, 1972.

⁷ The Joint Economic Committee in 1960 published a subsidy study entitled "Subsidy and Subsidy-Like Programs of the U.S. Government" and updated that study in 1965.

⁸ For additional details on the staff study and a list of the additional study papers to be published, see *The Economics of Federal Subsidy Programs: A Staff Study*, Joint Economic Committee, January 11, 1972.

Although the staff study did not evaluate specific subsidy programs, it did provide some preliminary findings on deficiencies in the overall operation of the subsidy system. These findings were substantiated and elaborated upon in the first set of hearings on subsidies held by the Subcommittee on Priorities and Economy in Government of the Joint Economic Committee. In brief, they were:

- Much of the information necessary to understand and evaluate Federal subsidies is hidden from public scrutiny. Special efforts are made by subsidy proponents to give subsidy programs other labels such as tax incentive, loan, and cost sharing. Public documents of accountability such as the budget have been completely inadequate as a tool for controlling these special benefits. To a large extent this lack of information is the root cause of other deficiencies in our subsidy system.

- This absence of information on subsidies has kept the general public from knowing their pervasiveness and cost. As indicated earlier, the staff study identified \$63 billion as the budgetary cost of Federal subsidy programs in fiscal 1970, which is a conservative estimate of the full cost of subsidy programs. Unfortunately, such a cost accounting is not available on a regular basis.

- Federal subsidies are not comprehensively organized by objectives and areas of economic impact. This makes it almost impossible to determine what subsidies are supposed to do, if they achieve their purpose, to what extent subsidies overlap, the magnitude of subsidy payments to each sector of economic activity, and the relationship of program objectives to other national goals.

- In terms of their direct impact, there appears to be a bias toward producer rather than consumer subsidies. From the data available, it also appears that the distribution of subsidy benefits tends to favor higher income groups. This is especially true of tax subsidies.

- There has been no serious effort by the Federal Government to evaluate subsidies that are wasteful or outmoded. The result has been that subsidy programs are maintained indefinitely and piled one on top of another.

Neither the Executive nor Congress has developed adequate information to insure control over Federal subsidies in order to rectify the above deficiencies.

Federal subsidy programs should constantly be reevaluated to insure that their objectives are still important, that they operate efficiently, and that they distribute their benefits equitably. We urge the Congress and this Administration to immediately initiate a critical review of major subsidy programs in order to eliminate or redesign wasteful, unfair, and outmoded subsidies. To assist in this review, we recommend that the General Accounting Office undertake annual monitoring and selected evaluation of major subsidy and special benefit programs.

The need to evaluate Federal subsidy programs is painfully demonstrated by the section 235 home ownership and section 236 rental assistance programs. Under these programs, the Federal Government provides interest subsidies to the low-income home owners or the owners

of rental dwellings occupied by low-income families who could not afford such housing if the full cost of mortgage financing were applied to their mortgage payments or monthly rental. The subsidies provided by these programs can cover all but one percent of the mortgage loan, and the mortgage itself is insured by FHA.

Last year the Department of Housing and Urban Development indicated the scope of these programs when it revealed to the House Appropriations Committee that the Federal Government had a potential maximum liability of \$15 billion on the 611,000 Section 235 units and \$20 billion on the 570,000 Section 236 units—a total of \$35 billion—for which commitments had been made at that time. Program commitments have continued since then, and it can be conservatively estimated that the maximum total has now reached a least \$40 billion. The degree of Federal commitment, of course, may be diminished somewhat for those home owners and renters who are able to accept a greater portion of the interest costs in their housing payments as their incomes increase.

Investigations by the staff of the House Banking and Currency Committee and the House Government Operations Committee have disclosed widespread abusive practices among lenders, real estate speculators, and appraisers involved in these and other Federally assisted and insured housing programs. Meanwhile, in many cases the home owner has been victimized.

IV. DEFENSE AND NATIONAL SECURITY

DEFENSE SPENDING AND UNEMPLOYMENT

President Nixon, in his Economic Report, states that unemployment was reduced from the 6 percent level in the sixties by a war buildup and that it must be reduced from that level in the seventies by the creation of peacetime jobs. The President goes on to state that "the unemployment problem has been intensified by the reduction of over 2 million defense-related jobs and by the need to squeeze down inflation." Similar statements can be found in the Economic Report of the Council and in the speeches and congressional testimony of other Administration officials. The Administration position appears to be that the low level of unemployment that prevailed during the late sixties was brought about by the war buildup while the high unemployment that currently prevails has been caused by the winding down of the war. This argument has an appealing symmetry that might be persuasive were it not for the facts.

Unemployment in the Sixties

The facts are that the sixties began with a high rate of unemployment generated in the recession of 1960-1961. Unemployment was 6.7 percent in 1961. But in the next three years, prior to the war buildup, the unemployment picture brightened considerably. By 1964, unemployment was at 5.2 percent and the following year it dropped to 4.5 percent. The spurt in defense spending did not occur until 1965. Although defense expenditures went from \$47 billion to \$51 billion from 1961 to 1962, they rose only slightly in 1962, 1963, and 1964. In the year 1964-1965, defense spending was actually cut by \$4 billion, reducing the total from \$54.2 billion to \$50.2 billion. By the mid-sixties, in other words, defense spending was close to where it was in 1961, while unemployment had declined sharply. It is true that defense spending rose rapidly after 1965 and that unemployment subsequently went down from 4.5 percent to a low of 3.5 percent. Undoubtedly, increased defense spending after 1965 was a major factor in the further lowering of the jobless rate. However, what happened in the defense sector after 1965 obviously could not have influenced the earlier unemployment rates. The unemployment picture had improved drastically from 1961 through 1965, before the war buildup. Statements that the improvement would not have occurred were it not for the war simply do not square with the available data.

Post-War Experiences

The other side of the Administration's argument is that just as the war buildup brought unemployment down, so have the defense cut-backs contributed to the recent rise in joblessness. Some Administration spokesmen have made even more extreme statements to the effect

that this Nation has never experienced full employment except during times of war. One inference of such assertions is that a large increase in unemployment is to be expected whenever defense spending is reduced. Some critics, with considerable support from the analysis put forth by this Administration, have gone further and charged that the United States depends upon defense buildups for economic growth and prosperity, that without the stimulus of war and preparations for war, our economy would be continually plagued with high unemployment and unsatisfactory growth rates. The Committee firmly rejects both inferences as inconsistent with historical facts and as distortions of the way our economic system works. The American economy will become inextricably tied to defense expenditures only if the political leadership makes it so.

The facts are that the economy has demonstrated its capacity to maintain low unemployment while defense spending was being significantly reduced. Following World War II, from 1945 through 1948, defense spending dropped from over \$80 billion to about \$12 billion and defense purchases of goods and services declined from \$73.5 billion to \$10.7 billion. Throughout that period, unemployment remained under 4 percent and was 3.8 percent in 1948.

It is true that consumer demand had been accumulating throughout the war as a result of shortages, controls and high income, and that when the war ended consumer and business spending rose sharply. The release of pent-up demand thus acted as a stimulant to the economy, accounting in large measure for the low unemployment rates experienced in the 1945-1948 period. In this sense the post-World War II period is distinguishable from the present. Nevertheless, unemployment did remain low during that period.

Analysis of the post-Korean period shows that there were serious unemployment problems following the initial military cutback. From 1953 to 1954 defense spending and defense purchases dropped sharply and were accompanied by an unemployment rise from 2.9 percent to 5.5 percent. However, from 1954 to 1955 there was another sharp drop in defense spending and defense purchases, and unemployment went down in that year from 5.5 percent to 4.4 percent. We are not attempting to say that defense reductions have not imposed economic problems, including unemployment problems in the past. Statements by the Administration suggest that defense reductions will inevitably lead to increased unemployment. We believe unemployment does not have to rise when defense spending is curtailed. Measures can be taken to offset changes in government spending—whether those changes occur in defense or any other program—and to create jobs when necessary.

Current Administration Policy

The Administration could and should have anticipated the need to expand job opportunities during the period when defense spending was declining. The Council demonstrates in its Report that a net reduction of about 2 million persons in defense-generated employment occurred as a result of the drawdown of troop levels in Vietnam, the steady flow of veterans out of the Armed Forces, and the decline of defense contract awards. These were all easily predictable consequences

of the decision to wind down the war; a decision that was made by the Administration.

Obviously, the Administration did foresee those consequences and decided to allow them to happen. It has been common knowledge that the Administration "game plan" called for some rise in unemployment as the price to be paid for anti-inflationary measures. Government spokesmen have not attempted to hide this aspect of economic policy, although it has been down-played. A former member of the President's Task Force on Inflation stated to the Committee that both the Council and the Task Force believed it was "inevitable that stabilization could only be achieved at a price in terms of unemployment . . ." It was hoped that there would be only "a little extra unemployment" for a period of 3 years.

Of course, unemployment is never little for those who are involved. In this instance it is not little by any measure. One of the groups to be hit hardest is veterans. Unemployment of male Vietnam veterans, 20-29 years of age, stood at 8.4 percent at the end of 1971.

The policy of increasing unemployment through a policy of defense reductions and inaction turned out to be a tragic miscalculation and a serious error in judgment. Arthur Okun, former Chairman of the Council of Economic Advisers, stated to the Committee: "The Administration chose deliberately and consciously to use the defense cutback as a vehicle for fiscal restraint in order to fight inflation and worked hard to insure that it was not offset by increased civilian expenditures."

The Committee takes note of the large increase proposed for defense this year. The Administration is requesting \$85.4 billion in new obligational authority, including a \$6.3 billion increase for military programs. Table 8 shows total defense requests and appropriations actions for the fiscal years 1970-1972. Without commenting on the merits of this year's request, we can observe that an \$85 billion defense budget is hardly consistent with the Administration's claim that it has successfully managed the transition to a peacetime economy. We can also observe that Presidential elections will be conducted in the fall and this is a year when it could be tempting to want to reduce unemployment through the stimulus of rising defense spending. In our judgment, using the defense budget as a vehicle for fiscal expansion would be as unjustified as using it for purposes of fiscal restraint.

TABLE 8.—APPROPRIATIONS REQUESTED VERSUS APPROPRIATIONS ENACTED

NATIONAL DEFENSE FUNCTION, FISCAL YEARS 1970-72

[Dollars in thousands]

Function	Classifications	1970		1971		1972		
		Requested	Enacted	Requested	Enacted	Requested	Enacted	Pending
051	Department of Defense—Military.....	80,382,885	74,297,588	73,518,143	71,358,061	75,751,937	72,633,863	2,077,456
057	Military assistance.....	975,000	350,000	1,462,500	1,390,000	1,215,000	900,000	-----
058	Atomic Energy Commission.....	2,365,953	2,222,769	2,388,500	2,307,260	2,338,202	2,294,380	22,300
059	Defense-related activities:							
	Office of Emergency Preparedness.....	3,260	3,200	3,386	3,360	3,314	3,314	-----
	HEW: Emergency health.....	4,000	4,000	3,755	4,030	4,203	4,203	-----
	GSA: Property management and disposal service.....	21,976	20,296	24,462	27,639	29,800	30,296	-----
	Selective Service System.....	76,754	75,348	79,197	78,197	82,235	82,235	-----
	Subtotal, defense-related activities.....	105,990	102,844	110,800	113,226	119,552	120,048	-----
	Total national defense function ¹	83,829,828	76,973,201	77,479,943	75,168,547	79,424,691	75,948,291	2,099,756

¹ This table does not include permanent appropriations or deductions for offsetting receipts which become available without appropriation action by the Congress. Therefore, it will not agree with functional totals that appear in the budget.

Source: Office of Management and Budget.

The defense program should not be used for purposes of stimulating the economy and creating jobs. The only legitimate function of the defense program is to provide the military requirements essential for national security.

INADEQUATE JUSTIFICATION FOR DEFENSE PROGRAMS

There appears to be a growing tendency to use major components of the defense program for nonmilitary purposes or to justify them on grounds other than our own military requirements. This tendency can be seen in the military assistance program with respect to those foreign countries that receive aid not because we have a direct security interest in the military capabilities of those countries against specific threats, or even because we wish to obtain rights to use bases and other military privileges in those countries, but rather because we have a general political interest in the maintenance of the status quo. Thus, Morton H. Halperin, former Defense Deputy Assistant Secretary for Policy Planning and Arms Control, who testified last year before the Subcommittee on Economy in Government, said that military aid has been used with only limited success as a political instrument for such purposes as gaining and maintaining influence within the military establishments of various countries, pre-empting other countries from replacing the United States as the major influence with the military establishments of certain countries, restraining regional arms races, and "to further other diplomatic and political objectives."¹ The point is that such activities are political in nature.

A number of our most expensive weapons programs were first justified as necessary in order to "match" what the other side had or what we thought they had or were trying to have. The idea of matching the Soviet Union played a large part in our decision to develop an ABM, a MIRV capability, a new air defense system, a step-up in surface ship construction, and a new fleet of nuclear submarines. We went forward with ABM and MIRV production at least partly because we wanted to be able to use those programs as "bargaining chips" in our international negotiations. We are not saying that Soviet capabilities are not relevant to our own needs, or that the programs referred to were not required. We are saying that the relationship between Soviet capabilities and our needs is complex, and that this complexity has often not been recognized in the sketchy rationales presented to Congress for new weapons systems initiatives. Because of the enormous costs and the economic impact of these programs, we are concerned that decisions regarding them be made in the Department of Defense only with strict regard to our real military requirements.

We are confident that Congress will want to scrutinize all expensive defense programs with special care to ascertain whether the purposes they are intended to serve are worth the costs.

Congress needs to scrutinize with special care Administration requests for new major weapons systems and other defense programs that have been justified on inadequate military grounds.

¹ "Economic Issues in Military Assistance," Hearings before the Subcommittee on Economy in Government, Joint Economic Committee, January-February 1971.

DEFENSE SPENDING AND WASTE

Defense contracting for weapons and other hardware continues to be one of the most wasteful and mismanaged programs in the Federal Government. Large sums, running into billions of dollars, are spent on programs that are prematurely moved from the drawing board to the development stage, only to be later canceled before they emerge from development. In the decade 1960-1970, projects totaling \$6.8 billion were canceled by the Department of Defense before completion of development. Weapons that are completed often cost several times more than the original estimates, fail to satisfy contract specifications, and are delivered months or years late. An analysis of 45 selected weapons currently being built reveals they will exceed original cost estimates by more than \$35 billion, after adjusting for changes in quantities.

The Committee recognizes that not all cost over-runs on weapons programs are avoidable or unnecessary. Unforeseen difficulties do occur, inflation may increase costs, and changes may become desirable or necessary because of advances in technology. But spokesmen for the Department of Defense and the contractors tend to exaggerate these and other factors in an effort to excuse poor performance. Our weapons have become noted for electronic frills and gold-plating, for being excessively priced, overcomplicated, and underachievers.

Procurement Policies

Government procurement policies and practices often add to the problems and the costs of defense contracting. Procurement officials have been slow to enforce the Government's contractual rights, to insist on a dollar's worth of value for a dollar's cost, and to protect the taxpayers' interests in the billions of dollars spent on weapons programs annually. For example, more than \$14 billion in government-owned property remains in the hands of private contractors, although the Department of Defense has formally adopted a policy of significantly reducing the amount. Studies by the General Accounting Office and this Committee show that the Department of Defense neither maintains utilization records nor a complete inventory of this property. A number of abuses have been uncovered including unauthorized use of government-owned property for commercial purposes.

Equally serious is the problem of the "bail-out." A bail-out occurs when a contractor who cannot perform according to the terms of his government contract is permitted to deliver less than he agreed to deliver or to increase the original price. The Government bails the contractor out by agreeing to less than full performance under the original contract specifications or higher costs or both. As a result of these and other practices, vast subsidies are being given to the defense industry. Of course, not all defense contractors engage in these practices and there are many dedicated government officials who see it as their responsibility to get the best job for the least cost. Nevertheless, the contract system today is on the verge of a shambles. As the former Deputy Secretary of Defense said not long ago, defense procurement is a mess.

Support Costs and Manpower Utilization

The Committee is concerned over high and rising support costs in the Department of Defense and the problems of manpower utilization. Support to combat ratios are excessively high. A study of Army Tables of Organization and Equipment (TO&E) shows that in the 16,000 man combat divisions, less than 7,500 soldiers are assigned to direct combat duties, and in the 48,000 man Division Force Equivalent, it is probable that less than 25 percent are assigned to a legitimate combat role. Of the more than 420,000 Army troops in Vietnam in 1969, less than 200,000 were performing in combat or combat-related roles. A typical 16,000 man Army infantry division contains about 11,000 officers and noncommissioned officers and 5,000 private soldiers, or about 2 officers and noncommissioned officers for every 1 private soldier. Yet relatively few of the officers and noncommissioned officers are assigned to jobs as combat troop leaders. About 60 cents out of every defense dollar goes to manpower and related costs. The need to eliminate the fat in this area is imperative.

Another serious support problem concerns the number of active bases and installations excess to the needs of the Department of Defense. While it is difficult to zero in on this aspect because of the lack of publicly available studies comparing the number, size, and location of bases to the military force structure, it is widely conceded that there are too many bases. The former Deputy Secretary of Defense said in December that the closing of unnecessary bases would result in savings of an estimated \$1 billion annually.

DOD needs to do a better job of eliminating waste and mismanagement throughout the military establishment. Large cost over-runs and gold-plating of weapons systems, excessive support costs, and mishandling of military assistance are undermining our defense program. Defense spending should be reduced. A tighter, leaner, and smaller defense budget will strengthen our real national security.

TOTAL COSTS OF NATIONAL SECURITY

The essence of the Federal budget should be clearly defined and itemized breakdowns of government expenditures so as to render a full, accurate, and understandable accounting to the public of how tax dollars are spent. The defense portion of the budget document falls far short of this goal for at least three reasons: (1) Large amounts of foreign military assistance expenditures are excluded from the budget category called "National Defense;" (2) the budget definition of defense-related activities is too narrow; and (3) the format for the "National Defense" category was changed this year, making it more difficult to comprehend.

Military Assistance

Military assistance provides an extreme example of budgetary obfuscation. The line item called "Military Assistance" in the budget seriously understates the true costs of military aid to foreign govern-

ments. In 1971, for example, the budget shows \$1 billion in military assistance funds were spent for national defense. In fact, further analysis shows actual costs for this program total about \$6 billion. The disparity occurs because on close examination the \$1 billion accounted for under "National Defense" turns out to be only the portion of foreign military aid known as the Military Assistance Program (MAP). Most military assistance is handled outside of the formal MAP structure through related programs.

The largest single portion of non-MAP military aid is the Military Assistance Service Funded Program (MASF). This program, totaling \$2.4 billion in 1971, is funded through the Department of Defense. MASF is not itemized under "National Defense." To locate this major outlay one must look under the table called "Summary of the Department of Defense Budget Program" where it appears as "Support of Other Nations." Other major components of military aid, foreign military credit sales, and economic supporting assistance are to be found under the budget category "International Affairs and Finance," where Department of State and related activities are located. An item of military aid bearing the unlikely title "Food for Peace" is also found under "International Affairs and Finance." Until the hearings conducted by this Committee into "Economic Issues in Military Assistance,"² the magnitude of military aid was not generally known.

We do not say that any of the items of military aid enumerated cannot be found through a careful reading of the budget. However, the fragmented way they are handled and the sometimes misleading titles given to the various programs would make it difficult for even an expert budget analyst to see the full range of military assistance. Indeed, some aspects of the program defy analysis. The costs of transferring arms, equipment, and real property to recipients of military aid are still not completely known.

Defense-Related Expenditures

A major difficulty with the budget category "National Defense" is that it does not include all the items of expenditure that can be related to defense requirements. "Defense-related" expenditures are defined to include the Selective Service System, emergency preparedness activities, stockpiling of strategic and critical materials, and expansion of defense production. Outlays for the Atomic Energy Commission and military assistance are carried as separate line items.

We believe a much broader view needs to be taken of what the Federal Government spends each year for the overall purpose of national security. For example, most of the expenditures under the budget category "International Affairs and Finance" are directly related to national security, and a number of other programs, in whole or in part, are similarly intended or would not be undertaken but for the requirements of national security. Two major items of expense, the veterans' program and most interest on the national debt, are legacies of past wars and defense programs.

² Ibid.

The National Security Budget

Last year we incorporated these programs into a table called the "National Security Budget." It was our hope that presentation of such an expanded view of defense and defense-related activities would begin a dialogue and encourage the Executive Branch to adopt or modify the concept for this year's presentation of the budget. Unfortunately there has been little dialogue and no action.

On the contrary, this year's budget moves in the opposite direction, away from the objective of a full accounting of the costs of national security. Until this year, the National Defense category in the part of the budget set aside for discussion of Federal outlays by function included a single table containing line items for Department of Defense-Military, military assistance, atomic energy, and defense-related activities. Department of Defense-Military was broken down into separate components, such as military personnel and procurement; military assistance was broken down into two components; and defense-related activities were divided into four components. That table does not appear this year, although pieces of it can be found on various pages. A similar table can be found in the back of the budget in the midst of the "Summary Tables." We believe this year's presentation is more difficult to read and understand.

The lack of response of the Executive to the proposed National Security Budget can perhaps be appreciated by an examination of this year's breakdown (Table 9). It will be seen that when all readily identifiable security-related costs are included, they amount to well over \$100 billion annually. It should also be noted that recommended budget authority takes a dramatic leap upward, both for DOD-Military and total National Security. Recommendations for increases in budget authority can be taken as an indicator of the Administration's intent to increase actual outlays.

TABLE 9.—NATIONAL SECURITY BUDGET*

[In millions of dollars]

	Outlays (fiscal years)							Authority 1973
	1965	1968	1969	1970	1971	1972 estimate	1973 estimate	
Defense, military assistance and defense related activities:								
DOD military ¹	46,173	77,373	77,877	77,150	74,546	75,000	75,900	81,656
Military assistance ²	2,469	1,237	1,355	1,186	2,045	1,790	1,649	3,021
Atomic Energy.....	2,625	2,466	2,450	2,453	2,275	2,358	2,422	2,563
Space Research and Technology.....	5,093	4,721	4,247	3,749	3,381	3,180	3,191	3,378
U.S. Arms Control and Disarmament Agency.....	7	11	10	11	10	9	10	10
Renegotiation Board.....	3	3	3	4	5	5	5	5
National Security Council.....	1	1	1	1	2	2	3	3
Stockpiles.....	16	19	18	15	23	28	23	23
Expansion of defense production.....	60	51	166	-15	-188	-27	-32	-----
Selective Service.....	43	57	65	75	81	81	80	80
Emergency Preparedness.....	17	12	11	4	13	8	8	8
Deductions for offsetting receipts.....	-124	-116	-138	-118	-89	-218	-692	-692
Subtotal.....	56,383	85,835	86,065	84,515	82,104	82,216	82,567	90,055
Payments for past wars and defense program:								
Veterans Benefits.....	6,080	6,882	7,640	8,677	9,776	11,127	11,745	12,441
Interest ³	8,577	10,308	11,843	13,734	14,707	15,050	15,871	15,871
Subtotal.....	14,657	17,190	19,483	22,411	24,483	26,177	27,616	28,312
Programs justified on grounds of national defense:⁴								
Ocean shipping ³	253	227	236	239	321	349	351	410
Impacted area school aid ³	263	380	299	492	395	388	359	323
Subtotal.....	516	607	535	731	716	737	710	733
Total, national security.....	71,556	103,632	106,083	107,657	107,303	109,130	110,893	119,100

* 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.

¹ DOD military excludes DOD civil outlays which totaled \$1,200,000,000 in 1965; \$1,300,000,000 in 1968; \$1,300,000,000 in 1969; \$1,200,000,000 in 1970; \$1,400,000,000 in 1971; \$1,700,000,000 in 1972 (estimated); \$1,800,000,000 in 1973 (estimated); and \$1,800,000,000 in new obligational authority for 1973.

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. Total obligational authority for this program is shown in the budget as \$2,400,000,000 in 1971; \$2,400,000,000 in 1972 (estimated); and \$2,200,000,000 in 1973 (estimated).

³ Includes 75 percent 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.

Costs of the War in Southeast Asia

Once again, for the third year in a row, the budget fails to break out separately the costs of the war in Southeast Asia. In our report last year, we urged that the Administration resume the practice of discussing the costs of the war in the budget, and we repeat that recommendation. Congress and the public have a right to expect a full and formal accounting of this source of major government expenditures, including breakdowns for Vietnam, Cambodia, and Laos. It is disconcerting, to say the least, to find the costs of the war expunged from the budget while spokesmen for the Department of Defense feel free to discuss the figures in press conferences, as was done on January 22, 1972, in a conference conducted by the Secretary of Defense and two of his principal assistants.

The defense budget document is woefully inadequate as a public accounting of the true costs of national security.

The budget should be expanded to include:

1. **The total costs of military assistance.**
2. **Outlays for programs of all agencies other than DOD that are related to current military programs, or are justified on the grounds of national security, or are in payment for past wars or military programs.**

The costs of the war in Southeast Asia should be specifically identified in the budget document.

THE COUNCIL OF ECONOMIC ADVISERS

We are most disappointed with the failure of the Council of Economic Advisers to focus on the problems of defense spending and its impact on the economy. The Employment Act of 1946 gives broad authority to the Council to formulate and recommend national economic policy, to gather and analyze information concerning economic developments and trends, and to appraise the various programs and activities of the Federal Government in the light of the basic policy declared in the Act, namely, "to promote maximum employment, production, and purchasing power." Nowhere in the Employment Act is it stated that the Council should concentrate on civilian programs and activities of the Government to the neglect of military programs and activities of the Government.

A fair reading of the Council's reports suggests that it has long neglected the economic impact of defense spending and other activities related to national security. This year the Council in its report almost entirely ignores this important side of the economy. Only in a few paragraphs is defense spending discussed at all, and then to buttress the Administration's argument that defense cutbacks have contributed to the increased unemployment. We believe that the Council in failing to come to grips with the problem of defense has transformed itself into a Council or Economic Advisers for Civilian Affairs. To begin with, the Council ought to immediately conduct in-depth studies of some of the more pressing questions raised by the defense program.

Earlier we referred to the high costs of military manpower and the problem of manpower utilization. A serious related problem con-

cerns the military retirement program. In 1969, outlays for retired military personnel were \$2.4 billion. By 1971 they had risen to \$3.4 billion and are estimated to be \$4.3 billion in 1973. In view of the uniqueness of the military retirement program, this large and rising cost of defense ought to be carefully studied.

The relationship of defense spending and inflation has been a continuing source of confusion and controversy. Spokesmen for the Department of Defense attribute a large portion of increased expenditures to rising wages and prices. Others allege that defense policies are a major contributing factor to those same rising wages and prices. The truth is not known with any degree of precision and, in line with the Council's great concern over inflation, we would think it would want to understand the problem. These and other matters, including the effects of defense spending on the balance of payments, literally cry out for objective analysis. The Council can perform a great service to the Nation by broadening the scope of its activities to include defense and national security.

The CEA should pay greater attention to the impact of defense spending on the economy. The Council's continued neglect of this important problem, as evidenced by the inadequate discussion of defense spending in the Council's reports, is a source of continuing concern and disappointment to the members of the Committee. The Council should conduct studies and report its findings at the earliest possible time on:

- 1. The extent to which defense spending and procurement practices contribute to inflation.**
- 2. The impact of inflation on defense spending.**
- 3. The effects on our balance of payments of the costs of military bases and facilities in foreign countries, and the deployment of troops in Europe, Asia, and other areas of the world.**

THE OFFICE OF MANAGEMENT AND BUDGET

The Office of Management and Budget poses a more difficult problem. The budget review process differs for the Department of Defense and the other agencies in the Executive Branch. Briefly, after the budget of a typical civilian agency is submitted to OMB, spokesmen for the agency are required to explain and defend the request at the offices of the budget examiners. Following an informal hearing, the examiners independently scrutinize the agency's submission and make a recommendation to the President. The President later makes known his decision on that agency's request. If the agency disagrees with the decision, it must appeal to the President.

The defense budget is reviewed in an entirely different and, in our judgment, a less effective manner. For one thing, spokesmen for the Department of Defense are not required to appear at the offices of the budget examiners to answer questions about the defense request. Instead, the budget examiners are required to go to the Pentagon to conduct their review. Second, the budget examiners are required to

conduct a "joint review" of the defense request, assisted or accompanied at each stage of the review by officials of the Department of Defense. The difference between the independent review of civilian agencies and the joint review of the Department of Defense is significant because at the completion of the joint review, the budget office forwards its recommendations to the White House, provided they are concurred in by the Department of Defense. If there is disagreement over any aspect of the proposed defense budget, the budget examiners must forward their recommendations regarding the area of disagreement as a separate document. The tendency is for the Department of Defense to be more successful in having its proposals approved by the President than are the civilian agencies.

We recognize the political aspects of this problem. In a sense, the joint review procedure only reflects the different relationships between the Department of Defense, the civilian agencies, and the White House. The Department of Defense, being by far the largest and most powerful agency in the Federal Government, is likely to have substantial influence at the highest policy levels no matter what budget review procedure is employed. But a vigorous and concerted effort by the Office of Management and Budget to analyze the substantive issues in the defense program and to identify the areas of waste and inefficiency can have a profound and salutary effect on defense budget requests. The Committee is not satisfied that OMB is devoting sufficient manpower and resources to this problem.

One indication of OMB's failure is the amount of identifiable fat in the present defense program. We have already discussed a number of areas where excessive defense spending exists. In our judgment, OMB needs to upgrade its defense review activities and do a better job of ferreting out and challenging wasteful programs. A dollar spent on defense should be as carefully scrutinized as a dollar spent on civilian programs.

The Office of Management and Budget should concentrate more of its efforts and resources on reviews of the proposed budget requests of the Defense Department so as to identify and recommend elimination of unnecessary and wasteful expenditures.

V. INTERNATIONAL ECONOMIC ISSUES ¹

Last year the Executive conceded that existing policies were untenable and, on August 15, launched a new international economic policy. This reversal occurred in response to the first annual U.S. trade deficit of this century and massive speculation against the dollar. While the initial stage of these new international policies was unnecessarily unilateral and protectionist, they did succeed, on December 18, in bringing about the first essential contribution to a viable new international economic order—the realignment of exchange rates among industrial nations.

Ultimate success in monetary reform or liberalizing trade, however, is not yet assured. The dollar remains inconvertible, foreign monetary authorities are obliged to hold more liquid dollar assets than they would prefer, no new mechanism to assure prompt exchange rate adjustment has been agreed upon, the activities of the International Monetary Fund (IMF) are hampered by the aftereffects of our August 15 initiative, protectionist sentiment remains dangerously high in the United States, and no permanent improvement in our international competitive position has been achieved. Solutions to all of these problems must be put into effect before the new international economic policy can be deemed a success.

The United States now stands at the most critical juncture in its international economic relations since the end of World War II. Our continued leadership in the evolution of a unified international monetary system and in the gradual reduction of all types of barriers to trade is now dubious. As a consequence of an excessively narrow definition of the national self-interest or of an attempt to maximize our bargaining leverage in negotiations, the United States may yet produce the dissolution of the international monetary system that has been arduously constructed over almost three decades. In addition to the risk of a monetary breakdown, the threatened enactment of protectionist legislation would reverse the course of trade liberalization that began in 1934. In recent history, the United States has been the nation exercising primary leadership in carrying forward international monetary reform and trade liberalization. Whether the pace of these constructive developments could continue in the future without U.S. leadership is questionable.

INTERNATIONAL TRADE POLICY

A number of factors have contributed to the burgeoning of protectionist sentiment, tinged with isolationism, that has occurred in the United States during the past few years. Perhaps most important as explanations for the change in attitude are the persistent high unemployment rate, at about 6 percent, and the progressive deterioration in the U.S. trade balance that led to a deficit of nearly \$3 billion in

¹ Senator Humphrey states that he is in strong disagreement with some of the dogmatic conclusions stated herein.

1971. Also important as contributing factors are the Vietnam War and social discontent at home, which have undermined our confidence in the ability of the United States to successfully exert its capabilities abroad. Another element is the almost total lack of data and consequent wide misunderstanding regarding the domestic employment and balance-of-payments consequences of direct investment abroad by major American corporations. All of these tendencies toward protectionism have been intensified by Administration actions that tended to legitimize the use of trade restrictions as a solution to job losses and trade deficits. Imposition of a 10 percent import surcharge and the threat to invoke the Trading with the Enemy Act to limit imports of synthetic textiles and apparel set examples that make legislators more likely to advocate trade restrictions and make the launching of any new U.S. initiative in trade liberalization far more difficult.

Countering Protectionism

These recent examples set by the Administration and the increasing threat that some protectionist measures might secure congressional approval demand that the President emphatically reject a restrictionist approach to the solution of U.S. international economic difficulties and offer a constructive alternative policy course. The adoption of trade restrictions by the United States would cause other nations to take similar action immediately. The outcome would be a general reduction in the volume of trade—and employment—with no promise of an improvement in the U.S. net trade balance. Not only would consumers lose by being denied quality imports at competitive prices, but well-paid workers in export industries would also find that foreign demand for their products had substantially diminished. Of course, some additional jobs would be created in import-competing industries to supply goods substituted for those that had been denied access. But these new jobs would generally pay less than those lost in more sophisticated export industries and would have an uncertain future, since they would depend upon the continued maintenance of import restrictions.

Leadership from the President is essential to counter the threat posed by growing protectionist sentiment. Now that most short-term trade issues with other industrial nations have been resolved following the December agreement to realign exchange rates, the President should articulate for the information of the Congress and the general public his strategy in pursuing more comprehensive trade liberalization. Japan and Western European countries have indicated their willingness to begin comprehensive trade negotiations next year. To conclude any agreement, the Executive will need statutory authority granted by the Congress. An essential first step in obtaining such authority from the Congress is the presentation of comprehensive, detailed information on the economic consequences for the United States of tariff and nontariff trade barriers, of multinational corporate investment overseas, of dumping by other countries, and of enlarging the European Economic Community. Only with this type of information can the Congress be assured that the outcome of any new trade negotiation is fair to the United States. As a second step, to eliminate the uncertainty about what authority the President will request and to counter

the impression that the introduction of additional restrictions is an appropriate solution to lagging American competitive abilities, the President should speak out clearly and detail his policy.

The solution to the international trade problems of the United States is not to be found in quotas or similar restrictions limiting imports. Any suggestion to adopt such techniques as a general solution should be emphatically rejected. Instead, the Administration should articulate a forward-looking trade strategy and accompanying schedule for implementation.

The dollar devaluation agreed to in December assures the United States of an immediate gain in its competitive position vis-a-vis foreign producers. But differences between nations in the pace of inflation, rates of productivity growth, and consumer preferences as incomes rise may gradually erode this gain. The United States, moreover, will continue to extend financial assistance to developing countries and export capital throughout the foreseeable future. To insure a liberal trade policy and to maintain overall zero balance in the face of financial outflows, the United States needs substantial earnings from net sales abroad of goods and services.

Exchange Rates and Productivity

Two essential contributions to maintaining an appropriate balance between the goods and services account and financial outflows are frequent adjustments of exchange rates and effective methods for raising the productivity of American workers. Exchange rates must be altered more promptly and gradually than has been the practice in the last decade. Delay has caused rate changes to be larger and more disruptive than would otherwise have been necessary. Even with appropriate exchange rate flexibility, however, our ability to provide continuing increases in the standard of living for Americans and to exercise economic leadership throughout the world will be undermined if productivity here does not grow more rapidly than it has in recent years. The Administration has announced its intention to undertake a major effort to stimulate the rate of productivity growth. This program should be pressed forward as quickly and energetically as possible. It should strive for legitimate increases in productivity and not rely upon subsidies or tax loopholes to compensate with public resources for the competitive failings of American industry.

Restructuring the U.S. Economy

One aspect of U.S. domestic economic growth and our pattern of investment abroad warrants special investigation. Through either the licensing of patents or direct investment overseas, U.S. corporations have tended to export much of our most advanced technology. This outflow of technology has apparently been stimulated somewhat by existing tax codes. On the other hand, we have tended to subsidize, protect, and otherwise prop up labor-intensive industries that are less advanced technologically and pay relatively low wage rates. We should consider the formulation of a national industrial development program that

would plan for the creation of new industries with a competitive advantage based on the application of recent technological innovations. Such new enterprises would help raise the skill and wage levels of American labor and create job openings for workers in labor-intensive industries now facing import competition. To succeed, such a program would require the full cooperation of business and labor in its planning and implementation. To fail to achieve such a restructuring of American industrial capabilities implies that developing countries will not be able to find a satisfactory market in the United States, standards of living here will not improve as fast as they otherwise might, and the position of the United States in world economic leadership will gradually be assumed by other countries.

The appropriate solution to U.S. trade and balance-of-payments problems lies in the prompt adjustment of exchange rates and in effective policies to strengthen competitiveness through efficient management, increased worker productivity, and shifts in the composition of output toward those industries in which the U.S. has a comparative advantage.

THE GOALS OF CURRENT MACRO-ECONOMIC POLICIES

Foreign observers have criticized current monetary and fiscal policies in the United States for producing excessively low interest rates and for generating an excessively large Federal budget deficit. These policies have been cited as responsible in part for the slow rate of short-term capital flows back to the United States following the December agreement on exchange rate realignment.

The classical case for currency devaluation applies to a country that is suffering from excessively high aggregate demand and consequent inflation. While the present rate of inflation in the United States is still higher than would be desirable, it has come down from the pace a year ago. The price freeze contributed to this improvement. On the other hand, unemployment has stubbornly remained near the unacceptably high level of 6 percent and recovery from the low of the recent recession has been sluggish. Therefore, under these circumstances, monetary and fiscal policies must be directed essentially to reducing unemployment and stimulating a faster recovery of production. As the economy expands, short-term interest rates will rise, and increased revenues will diminish the budget deficit.

Especially at this time when unemployment is at an intolerable level and the strength of the recovery from the previous period of stagnation is in doubt, monetary and fiscal policies must be used primarily to increase employment and to insure an adequate rate of domestic economic growth.

CONTINUING INTERNATIONAL MONETARY REFORM

The August decision to terminate free gold convertibility for the dollar and the December agreement to realign exchange rates and increase the dollar price of gold were only the first steps in a series of fundamental reforms of the international monetary system. The com-

munique that the Group of Ten Ministers issued on December 18 stated "that discussions should be promptly undertaken, particularly in the framework of the IMF, to consider reform of the international monetary system over the longer term." The outstanding issues mentioned as topics for negotiation included the maintenance of stable exchange rates, convertibility, the role of gold and other reserve assets, the supply of reserves, exchange rate flexibility, and the control of short-term international capital movements.

Treasury Delay

Since December the attitude of the U.S. Treasury in pursuing these discussions and in devising appropriate interim arrangements on behalf of countries continuing to acquire dollars has been unnecessarily hesitant and defensive. The United States cannot assume any general commitment of dollar convertibility before our balance of payments has improved substantially, before an international agreement has been reached to guarantee prompt adjustment of exchange rates, or before excess official dollar balances have been immobilized. On the other hand, there is no valid reason to insist that the United States can afford no expenditure of reserves for any purpose or that intensive discussions on top priority issues be delayed.

The suspension of dollar convertibility has severely hindered the ability of the International Monetary Fund to discharge its normal responsibilities. A number of countries holding substantial dollar reserve balances would like to repay outstanding loans from the Fund. But the IMF already holds a surfeit of dollars, and according to its by-laws, cannot accept more of that currency in repayment of outstanding obligations. If the Fund continued lending while at the same time debtors were prevented from repaying, the IMF would eventually deplete its stock of strong currencies that can be used to help nations experiencing payments deficits.

Other Fund members have offered usable currencies in exchange for dollars if the United States will also spend its reserves to buy two or three hundred million outstanding dollars to facilitate repayment by the United Kingdom and other debtors. If the world is to enjoy a smoothly functioning, unified international monetary system in the future, a strong, effective IMF will be needed as the focus of that system. In addition, a limited expenditure of reserves by the United States to facilitate the repayment of debts and strengthen the IMF would be an indication of American commitment to a unified monetary system and of confidence in the ultimate strength of our own balance of payments.

Preconditions of Convertibility

Although no date for a general resumption of dollar convertibility can be specified at this time, the Treasury can immediately begin discussions on essential prerequisites of convertibility. Such prerequisites include a guarantee that surplus nations will increase the foreign exchange value of their currencies more promptly than they have in the past and help prevent chronic deficits on the part of the United States or other countries. Because the United States occupies such a signifi-

cant position in international trade and finance and because the dollar will most likely continue to be used as the chief intervention currency throughout the foreseeable future, this country cannot expect to enjoy precisely the same freedom in exercising initiative to alter dollar exchange rates as other countries do in modifying the external value of their currencies. However, before any return to general dollar convertibility, it is essential that the United States, insofar as it is possible, be given the same latitude to adjust the exchange value of our currency that other countries enjoy.

Another issue that must be settled before convertibility is restored is that of the dollar overhang in the hands of foreign monetary authorities. Liquid dollar liabilities to foreign central banks now total over \$50 billion. Some portion of this amount, but not all of it, is excess reserves that the foreign authorities were obliged to acquire and hold as an alternative to either letting their exchange rates appreciate more or imposing exchange controls. A reflux of short-term funds to the United States can be expected as short-term interest rates rise with a quickening pace of economic activity and as our balance of payments strengthens. However, foreign central banks will almost certainly continue to hold more dollars than they require for intervening in the exchange markets. Some arrangement must be formulated, therefore, to immobilize superfluous dollar balances. These excess reserves could either be used to purchase long-term U.S. Treasury obligations or they could be deposited with the Fund in order to establish central bank "checking account" balances to be used in the settlement of payments surpluses and deficits. The particular mechanism that is preferable to the United States is not particularly dependent upon the amount of dollars to be immobilized. Thus, on this issue also, the Treasury could outline its preferences and begin negotiations immediately.

A willingness on the part of the United States to negotiate and to make a modest expenditure of reserves facilitating the normal functioning of the IMF would indicate our confidence, contribute to a lessening of uncertainties in exchange markets, and help discourage other nations from implementing exchange controls if they are obliged to purchase additional dollars. Foreign countries cannot be expected to absorb dollars indefinitely—and will not—if they are uncertain about how these dollars may be used in the future. Moreover, it is far more likely that exchange controls will spread, that current transactions as well as capital movements will be obstructed, and that currency blocs will evolve in an atmosphere of acrimony if the United States refuses to assume a position of leadership. Given the present structure of the international monetary system, the United States bears a unique responsibility. Timidity and procrastination on our part will tend to sour international economic and political relations. The United States could easily pay larger costs and suffer more rigorous adjustments in an acrimonious international environment than if we acknowledge our cooperative responsibilities.

Negotiations on fundamental reform of the international monetary system should begin immediately. An appropriate initial focus for these discussions is how to guarantee sufficient exchange rate flexibility in the future. Without the assurance of a responsive and effective exchange rate mechanism, the United States can hardly

restore dollar convertibility. The second order of business might be the discussion of the terms under which excessive liquid dollar balances now in the hands of foreign central banks can be immobilized. If these issues can be resolved, two major obstacles to the restoration of dollar convertibility will have been overcome.

Substituting SDRs for Dollar Reserves

Dollar reserves held by foreign monetary authorities have grown from less than \$10 billion at the beginning of 1960 to over \$50 billion today. But after the events of 1971, foreign officials will view with apprehension any further accumulation of dollar reserves. Moreover, the U.S. Treasury is eager to shed some of the constraints that result from use of the dollar as a reserve asset. For at least three reasons, therefore, special drawing rights (SDRs) should replace the dollar as the primary source of future additions to the reserve stocks of Fund members. First, the acceptability of the dollar as a medium for settling payment imbalances has been impaired. Second, equity demands that the United States submit to essentially the same balance-of-payments discipline as other countries and not finance external deficits by obliging the monetary authorities of other countries to accept additional dollars. Third, as the reserve-asset role of the dollar is curtailed, the United States will enjoy an increased capacity for altering dollar exchange rates. The consensus of the delegates at the annual meeting of the International Monetary Fund last fall and the Group of Ten meeting in December was that special drawing rights should assume the reserve-asset functions previously fulfilled by the dollar.

As the chief source of additional reserves, special drawing rights will necessarily be distributed in even larger amounts during coming years than they have been in the past. Since this multilaterally created money will constitute a generalized claim on the output of any IMF member, it is important that they be distributed in a way that does not exacerbate the disparity of incomes that exists between industrial and developing countries. The large majority required to agree upon any SDR distribution assures that these assets will not be created in excess of what a broad consensus of IMF members interpret to be a legitimate need for reserves. Moreover, the bulk of newly distributed SDRs will eventually find their way into the reserve balances of industrial nations regardless of the distribution formula. The issue that arises, therefore, relates to the transitional impact on wealth and real incomes of any particular distribution formula. Over the long run, the real welfare and security of the industrial world will be fortified if developing countries share fully in the evolution of the international monetary system. In addition to benefitting from this system, poor nations can also contribute to it. A variety of mechanisms can be employed to distribute SDRs in a way that will increase real resource transfers from the industrialized to the developing world. The issue of which mechanism to select is far less important than that there be one.

In the future, special drawing rights issued by the International Monetary Fund should replace the dollar as the

primary source of additions to the global stock of reserves. As more SDRs are distributed to insure a sufficient supply of international money, special attention should be devoted to injecting these assets into the system through a mechanism that will enable an increase in transfers of real resources from industrialized nations to developing countries.

Limiting the Role of Gold

The role of gold in the international monetary system is gradually diminishing. This evolution is appropriate since the contribution that gold can make to the usefulness and stability of the system is shrinking. Special drawing rights now provide the same guarantee of a constant value and have the further benefit of a small interest return. Although the dollar was theoretically convertible into gold, the presence of gold as a monetary reserve did not prevent other industrialized countries from being forced to accumulate undesired amounts of reserve currencies. The members of the IMF now have the collective ability to create reserves as needed rather than expend real resources to purchase gold. In the future, the introduction of more gold into the system, rather than the distribution of additional SDRs, would imply a real resource transfer to gold producers that at least in part would substitute for a similar transfer to developing countries.

Gold is a useful store of value only in the event of a collapse of the International Monetary Fund and the demonetization of special drawing rights. While some governments will invariably want to be insured against all eventualities, the quantity of monetary gold reserves now in the system is more than adequate to serve this function. As part of any comprehensive international monetary reform, therefore, the existing IMF agreement to purchase gold from South Africa under certain circumstances should be terminated.

The quantity of gold reserves in the international monetary system should not increase.

Short-Term Capital Flows

In 1971 huge outflows of short-term funds from the United States put intense downward pressure on the exchange value of the dollar and consequent upward pressure on the value of several foreign currencies. Although troublesome for monetary authorities at the time, the bulk of these flows was in fact not destabilizing, since they were tending to push rates toward a realignment that would be tenable over the long run. The decision in December to widen the range of permissible exchange rate fluctuations from 1 to 2¼ percentage points on either side of parity, which increased the potential losses of speculators, was a constructive move toward effective control of international short-term capital flows.

The widening of exchange rate margins has apparently had the unexpected effect of slowing the return flow of short-term funds to the United States following the exchange rate realignment. Holders of other currencies have been reluctant to buy dollars when the dollar might become substantially cheaper on exchange markets in the immediate future. This temporary disadvantage will eventually be over-

come as the balance-of-payments position of the United States strengthens and as short-term interest rates rise in this country with an increasingly rapid expansion of economic activity.

In the future international flows of short-term capital should not be permitted to threaten a structure of exchange rates that is appropriate for producing a zero net balance on current and long-term capital accounts. In addition to the wider margins, continued use of the swap mechanism among the Federal Reserve and other central banks and persistent efforts to coordinate economic policies among the major industrial nations can help keep short-term capital flows within proper limits.

Widening the band within which exchange rates may fluctuate has apparently helped curtail international flows of short-term capital. The U.S. monetary authorities should cooperate with their counterparts abroad to the maximum extent feasible in swap mechanisms and in policy coordination to help maintain international short-term capital flows within appropriate bounds.

DEFENSE BURDEN SHARING

When the new international economic policy was enunciated on August 15, one demand in the list of negotiating issues presented by the United States was to request a more equitable distribution among our allies of the costs of mutual defense. Since that time the Japanese and the European members of NATO have agreed to increase their weapons purchases from the United States, assume a larger proportion of the costs of maintaining bases, and have pledged a variety of other contributions. Discussions are continuing with Canada.

Unfortunately, our allies have still not fully implemented the policy that is generally agreed upon in principle, i.e., that no nation's balance of payments should either benefit or suffer as a result of that country's contribution to the mutual defense. In most instances, rigorous implementation of this guideline would require that our allies make some annual cash payment to the United States. While pledges to increase arms purchases in this country have been the normal technique for reducing the balance-of-payments costs to the United States of mutual defense, this approach suffers from the twin disadvantages of prompting other countries to buy weapons they do not legitimately need and of discouraging what may be a desirable degree of national self-sufficiency in weapons production.

Given agreement among the United States and its allies on the force composition and levels required to satisfy mutual defense needs, each nation should make its desired contribution of troops and arms. Balance-of-payments surpluses and deficits resulting from these contributions should then be offset through cash payments. In the event that our allies are unwilling to fully compensate the United States for our contributions of troops and arms to the mutual defense, the logical alternative would be to reduce the U.S. contribution to a level consistent with the financing burden that our allies are willing to bear.

Canada, Japan, and the European allies of the United States should promptly implement the guideline that no nation's balance of payments either benefit or suffer as a result of its contributions to the mutual defense.

SUPPLEMENTARY VIEWS OF VICE CHAIRMAN PATMAN

With some minor exceptions, I agree with the overall findings and recommendations of the report. As a document, it should serve as a good roadmap to both Congress and the Nation as a whole in terms of disclosing current economic shortcomings and providing recommendations for immediate action to overcome these problems.

As it should, the report deals at some length with the President's economic stabilization program and points up blatant failures which, taken in their entirety, will surely serve to defeat the purposes this unprecedented project is supposed to serve. The economic stabilization program is described as unprecedented because it marks the first time in the nation's history that extensive controls have been imposed on what is a peace-time economy. The only other relatively recent examples of economic controls and regulations of this scope occurred during World War II and the Korean War, when demand for goods and services so far outstripped the supply as to make price and wage stabilization an unquestioned necessity.

I have no question about the need for control and regulation under current economic conditions. I do have many questions about the manner in which the economic stabilization program is being administered and these are largely reflected in the criticism the report itself aims at the program.

But I think there are other questions that have arisen as a result of our stumbling economy and the use of regulatory authority provided under the Economic Stabilization Act, as amended. These questions are directed at the very structure and function of our economic system and the system's continual failure to adequately meet the social priority needs of the nation.

For example, when inflationary forces have been temporarily stemmed and most if not all controls are finally removed, what essential changes if any will have been achieved in terms of reducing the number of poverty stricken people in the nation? How much additional money will be available for rural and urban development, for education, for health, for public works and facilities? How, in fact, will the allocation of credit be altered so that the net effect will be to provide a greater share of the nation's wealth to those who are most in need? Those holding the reins of economic stabilization have admitted that their task is to fight inflation, to return the nation to the stable status quo of the mid-nineteen sixties. I have no argument with this intention, but I am convinced that this should be the beginning rather than the end of efforts to realign the economy to better serve the best interests of the people.

In what I consider to be an all too casual reference, Federal Reserve Board Chairman Arthur Burns himself referred in his testimony to the Committee to the need to examine the concentrated economic power of major corporations and large unions from the point of view of being

immune from common competitive market forces which tend to hold inflationary tendencies in check.

Obviously, it is not enough simply to check corporate economic power from becoming even more concentrated. If competition in their markets is to be restored, then the power of large corporations must be deconcentrated by requiring divestiture of major components which would then operate as separate competing units.

But even if corporate economic power were significantly diminished, would the nation's wealth be shared by a significantly larger number of people than is now the case? Again, would there be fewer poverty stricken, more public works and facilities, better schools and teachers and better health care? I doubt it.

Left essentially unchanged, is there any assurance the structure of our economic system will successfully reverse the disastrous patterns of the past two decades, which have left large areas of rural and central city urban America economically devastated? Is there any real hope that the largest single investment made by our government, defense expenditures, will be funneled into depressed urban and rural areas rather than continually sustaining a relatively small number of corporate giants?

Will we abandon devices like the investment tax credit, so readily embraced as a crisis tool theoretically designed to promote industrial expansion and job opportunities but which in reality is most often used by those who need it least? The most extensive use of the investment tax credit has been among the largest of the nation's business and industrial entities which have huge resources to sustain themselves. Indeed, Detroit auto manufacturers were quoted in the press as being all but indifferent to the prospect of re-instatement of the investment tax credit during the period it was being proposed by the Administration. They made it clear that their investment decisions were based on market feasibility and little if anything else.

How long shall we continue to allow the nation's housing and public works and facility needs to be victimized by economic cycles nourished by Federal Reserve tight money-high interest policies? Secretary of Housing and Urban Development George Romney is currently pointing with pride to the fact that low and moderate income housing starts are at last approaching the national housing goal. No emphasis is placed on the fact that our current housing achievements are made possible by an overabundance of mortgage funds resulting from lack of consumer confidence and spending in an otherwise dormant economy. Why must housing boom only when the rest of the economy is in a recession? Even the brightness of the housing picture has been drastically diminished because Federally assisted housing for low and moderate income families is being provided against a background of scandalous abuses by housing speculators and unscrupulous lenders who have defrauded both the homebuyers and the taxpayers to the point where Government housing programs in some areas border on the edge of collapse.

Why is it that while money market rates have substantially dropped for the nation's largest borrowers, interest rates for most of the nation's borrowers, the homebuyers and those who make installment purchases and seek consumer loans, have remained virtually unchanged from historically high levels?

I raise these questions in an effort to point out that both the public and private sectors of our economic system are not meeting the needs of a vast section of the population and to ask whether the existing system is really designed to do so. If it is not, what structural changes are needed to retain the private competitive nature of the system and at the same time make it adequately responsive to our most pressing social problems?

This is not to say that the system remains static. Changes are constantly occurring. Proposals to slightly alter the structure of the nation's financial institutions in terms of regulation and restrictions are expected to be made to Congress next year. But will these proposals result in any real change in the allocation of credit to priority areas? Nothing so far revealed in these proposals holds out the assurance that interest rates will be reduced to reasonable levels for most of the nation's borrowers. Nothing has been proposed in the way of protecting the housing, and state and municipal bond markets from periodic starvation. No suggestion is made that a new lending vehicle, such as a national development bank for priority purposes, be established to sustain a flow of investment funds into areas where the need is urgent.

The time is long past when tinkering with the fringes of our economic system should serve to satisfy anyone who is genuinely concerned with the nation's social problems. Both Congress and the Administration should proceed to launch an extensive evaluation of the structure of our economic system to determine where and how it should be altered to better serve the people. This effort should begin with the legislative committees and the Administrative agencies that have responsibility for fiscal and monetary policy. Private financial institutions which control the flow of most of the nation's credit should be called on to provide all necessary information.

If our national concern with the way the economy functions is to end with the close of the economic stabilization program, then we will have done nothing more than admit there are basic, crucially important faults in the system, and leave it at that. Such a posture is indefensible.

The overall evaluation of the economic system which I advocate should include the following subject areas:

- Should the Federal Reserve Board be reorganized?
- Should Federal bank supervisory agencies be reorganized?
- What methods should be utilized to promote more competition among financial institutions as a way of providing adequate funds at reasonable rates for all the nation's borrowers?
- What additional steps should be taken to stem the growing concentration of financial resources through bank mergers, bank holding company growth and acquisitions, trust department activities and bank management of pension funds?
- What policies and actions should be devised to reduce if not eliminate conflict of interest among lending institutions and those with whom they have substantial business relationships?

One of the basic items going to consideration of the Federal Reserve Board should be Open Market Committee support of the Federal securities market. Deficits totaling \$65 billion have been projected by the Nixon Administration for this year and next year. The prospect of heavy Treasury borrowing in the months ahead is inescapable. By the same token, the heavy demands on the money market imposed by such borrowing will have a large and damaging effect unless handled in the right way. Interest rates could be triggered upward and

the result would be a return to the historically high interest rates of 1969 and 1970, especially in terms of the cost of money for homebuyers and state and municipal governments.

The only certain way of avoiding another return to these disastrous conditions is to require the Federal Reserve Open Market Committee to support the Federal bond market. It can do this by coordinating market sales and purchases between the Open Market Committee and the Treasury in order to establish and maintain a floor of reasonable interest rates.

Every taxpayer in the nation will directly benefit from such a policy because it will mean a reduction of interest on the national debt. Equally important, an effort to hold down interest rates in the Federal securities market will have a direct effect on all other interest rates, thus benefiting both large and small borrowers. Unless market interest rates are held down, the regulations and restrictions imposed on the public through the economic stabilization program will have been for nothing and there will be little hope of sustained economic recovery.

Such an approach to the market by the Federal Reserve Open Market Committee is far from being an untried concept. During the 1930's and 1940's, Federal securities were sold and purchased in this way and interest rates on long-term Federal bonds did not exceed 2.5 percent. But in 1953 this approach to the market was abandoned, with the result that the Americans have paid nearly \$500 billion in excess interest on the public and private debt since that time.

A graphic illustration of the fact that the Federal Reserve can exercise its authority to manage the public debt in a way which will protect the interests of the American people by holding interest rates on Federal securities at a minimum is given below. The schedule shown is a remarkable example of how the interest rate on the public debt was held at a minimum by the Federal Reserve during the 14-year period, 1939-1952, a time when extreme inflationary pressures were exerted due to the demands of World War II and the Korean War, and also a time of stringent deflationary conditions following the end of World War II. In effect, it was a time when the nation's economy was made to run the gamut of economic extremes, yet the average interest on long-term government bonds for these 14 years was only 2.36 percent.

TABLE I.—*Yields on long-term Government bonds, by years, 1939 to 1952*
(percent per annum)

Year:	Yield
1939	2.36
1940	2.21
1941	1.95
1942	2.46
1943	2.47
1944	2.48
1945	2.37
1946	2.19
1947	2.25
1948	2.44
1949	2.31
1950	2.32
1951	2.57
1952	2.68
Average	2.36

The Federal Reserve policy of managing the interest rate on the public debt was abandoned during the Eisenhower Administration and the result is clearly shown in the schedule below. During the 19-year period, 1953-1971, the interest rate on long-term government bonds was 4.35, which is 84 percent more than the average of the previous 14 years.

TABLE II.—*Yields on long-term Government bonds, by years, 1953 to present (percent per annum)*

Year:	Yield
1953	2.94
1954	2.56
1955	2.84
1956	3.08
1957	3.47
1958	3.43
1959	4.08
1960	4.02
1961	3.90
1962	3.95
1963	4.00
1964	4.15
1965	4.12
1966	4.65
1967	4.85
1968	5.26
1969	6.12
1970	6.58
1971	5.74
Average	4.35

The effect of abandoning the low-interest policy on the total public debt is shown below. During the 23-year period, 1951-1973, the actual and projected interest rate on the national debt averaged 3.45 percent, a figure which is 46 percent greater than the average that prevailed in the 1939-1952 period. Consequently, the interest paid on the national debt, \$269.3 billion, from 1951 to 1973 is \$165.5 billion greater than would have been the case had the interest rate been held to the average of the previous 14 years. The total excess of \$165.5 billion came directly out of the taxpayers' pocket.

TABLE III.—EXCESS INTEREST RATES ON FEDERAL DEBT, 1951-73

(Dollar amounts in billions)

Fiscal year	Total Federal debt	Total interest paid	Computed annual interest rate	Computed interest cost at 1951 rate
1951.....	\$255.3	\$5.7	2.23	\$5.7
1952.....	259.2	5.9	2.27	5.8
1953.....	266.1	6.6	2.48	5.9
1954.....	270.4	6.4	2.36	6.0
1955.....	274.4	6.4	2.33	6.1
1956.....	272.8	6.8	2.49	6.1
1957.....	272.4	7.3	2.67	6.1
1958.....	279.8	7.8	2.78	6.2
1959.....	287.8	7.8	2.71	6.4
1960.....	290.9	9.5	3.26	6.5
1961.....	292.9	9.3	3.17	6.8
1962.....	303.3	9.5	3.13	6.8
1963.....	310.8	10.3	3.31	6.9
1964.....	316.8	11.0	3.47	7.1
1965.....	323.2	11.8	3.65	7.2
1966.....	329.5	12.6	3.82	7.3
1967.....	341.3	14.2	4.16	7.6
1968.....	369.8	15.6	4.21	8.2
1969.....	367.1	17.7	4.82	8.2
1970.....	382.6	20.0	5.22	8.6
1971.....	409.5	21.6	5.27	9.1
1972 ¹	455.8	22.1	4.84	10.2
1973 ¹	493.2	23.4	4.74	11.0
Total.....		269.3	² 3.45	165.5

¹ Estimated.² Average.

Note: Excessive interest on national debt—\$103,800,000,000.

Source: Budget of the United States for fiscal year 1973.

The full impact of abandoning the Federal Reserve low interest rate policy of 1939-1952 is only partially reflected in excess interest paid on the national debt since that time. The purchase and sale of Federal securities occupies so large a position in the money market that the interest rates applying to these securities strongly influence virtually all other interest rates in the nation, up or down—for good or bad. There is in fact a strong relationship between rates applying to the Federal debt and those applying to the private debt. It therefore is possible to compute not only the excess interest paid on the Federal debt from the Eisenhower Administration to date, but the excess interest paid on the private debt as well. Using the average interest applied to both the public and private debt in 1952 and comparing that with actual interest paid on the combined public and private debt since then, discloses that the American people paid \$497.2 billion more than would have been paid under the low-interest rate policies that prevailed during previous years. The total savings equals an amount large enough to wipe out the Federal debt entirely and leave the Federal government with a surplus.

TABLE IV.—EXCESSIVE INTEREST CHARGES ON THE PUBLIC AND PRIVATE DEBT, 1953 THROUGH 1971
 (Dollar amounts in billions)

Year	Net public and private debt	Interest paid	Interest costs figured at 1952 average	Excess interest paid
1953.....	\$581.6	\$21.7	\$20.5	\$1.2
1954.....	605.9	23.5	21.4	2.1
1955.....	664.9	25.8	23.5	2.3
1956.....	698.3	29.5	24.7	4.8
1957.....	728.3	33.6	25.8	7.8
1958.....	769.1	35.5	27.2	8.3
1959.....	831.4	40.3	29.4	10.9
1960.....	872.4	44.2	30.9	13.3
1961.....	929.8	46.8	32.9	13.9
1962.....	997.1	52.5	35.3	17.2
1963.....	1,071.7	58.7	37.9	20.8
1964.....	1,153.7	65.2	39.8	25.4
1965.....	1,245.6	72.4	44.1	28.3
1966.....	1,341.4	81.9	47.2	34.7
1967.....	1,442.7	89.9	50.8	39.1
1968.....	1,584.5	104.9	55.8	49.1
1969.....	1,722.7	120.6	60.6	60.0
1971.....	1,839.7	135.6	64.8	70.8
1971.....	1,950.0	156.0	68.8	87.2
Total.....				\$497.2

¹ Estimated.

SUPPLEMENTARY VIEWS OF SENATOR FULBRIGHT

While other responsibilities have prevented me from actively participating in the recent hearings and deliberations of the Joint Economic Committee, I do support the general tenor of the Committee's recommendations.

I want particularly to emphasize my agreement with the recommendations on reordering priorities and eliminating military waste. We have spent billions of dollars on unwise and unnecessary military items while frequently neglecting serious domestic needs and our true national security. We have not given adequate consideration to the entire question of the impact of our massive defense outlays and defense activities on the economy and society.

I strongly concur with the statement that, "The defense budget document is woefully inadequate as a public accounting . . ." I feel that the budget figures as presented to the Congress and the public are highly misleading in many respects, particularly in regard to the actual amount spent for military and military-related purposes. The figures in the Committee's Report make clear that, despite contrary claims by the Administration, the military budget is still growing and still dominates the overall budget.

I am pleased that the Committee has given emphasis to this point, and I hope that the Report and its recommendations will stimulate both the Administration and the Congress to focus on these vital issues. If we continue to avoid these questions, we only delude ourselves.

SUPPLEMENTARY VIEWS OF REPRESENTATIVE BOGGS

I am in general accord with the views expressed in the Majority Report and hasten to commend my associates on the Joint Economic Committee both for the hard working and thorough way in which they went about exploring the President's economic policy recommendations and for their impressive competence in appraising it. Regrettably, my duties as Majority Leader did not permit me to participate fully in the hearings and, for this reason, it would not be appropriate for me to take a position on each and every recommendation in the Report.

At the same time, I want to take this opportunity to emphasize the fundamental conclusion that the misguided economic policies of the Administration have cost this country some \$125 billion in lost production during the past two years and brought about a situation where 5 million people are out of work. What is more, had it not been for the programs put through at the initiative of the 92nd Congress, the situation would have been far worse.

In the circumstances, I feel it incumbent on me to set forth briefly in these supplemental views the legislative record of the 92nd Congress aimed at the goal of restoring to this nation the full employment enjoyed prior to January 1969 and toward ending the unhappy and unprecedented combination of escalating inflation and plunging employment which has been our lot during the past two years.

When this Congress convened in January 1971, we found the nation's economy in disarray. The legacy of full employment bequeathed President Nixon by the outgoing Democrats in January 1969 had been dissipated and replaced in two years by an additional two million jobless Americans. After witnessing a steady growth of the economy throughout the Kennedy-Johnson years we were now faced with an industrial plant operating below 75 percent of capacity and an annual GNP \$74 billion below its potential.

The costs to the nation of this deliberate slowdown have been enormous. Far from bringing down prices as intended, Administration policies produced an unprecedented combination of inflation and recession. The cost of living was 12 percent higher in January than it had been two years before, and unemployment was approaching the ten-year high of 6 percent where it has stayed throughout the year. The number of Americans living in poverty increased in 1970 for the first time in a decade, and welfare rolls also hit all-time highs.

Because this nation obviously could no longer afford inaction, the 92nd Congress extended the authority it had given the President in 1970 to control wages and prices, and urged him once again to act immediately. The Congress approved emergency employment legislation and accelerated public works authorization to get the Federal government into the attack on joblessness.

And after the President finally adopted our recommendations on August 15, we expeditiously enacted tax relief to stimulate the econ-

omy and a further extension of the economic stabilization legislation to give full latitude to the Phase II proposal. The Congress strengthened and refined both these measures to provide balance and equitable treatment for all Americans.

A partial list of the measures passed by the 92nd Congress demonstrates the extent and character of our actions up to now.

Cost of Living Stabilization Act.—On its own initiative the Congress kept the Economic Stabilization Act of 1970 operative through April 30, 1972, despite the President's repeated disclaimers that he would not invoke the wage-price control mechanism it authorized. However, when the continuing poor performance of our economy led to the August 15 unveiling of the New Economic Program, the President requested a further extension of the controls, and we complied by making the Act operative until 1973 while including additional provision for standby authority to control interest rates.

Emergency Employment Act.—With persistent unemployment the most troublesome aspect of our sluggish economy, we enacted several bills to give the job market a shot-in-the-arm. The Emergency Employment Act authorizes \$2.25 billion over the next two years to reimburse State and local governments for placing the unemployed in public service jobs—in health, education, sanitation, public works, environmental control. It provides for special consideration for Vietnam veterans and earmarks funds for unemployed professional and technical personnel. And, when unemployment hovered consistently at the six percent level throughout 1971 we expedited a separate \$1 billion appropriation in early August to get the Act immediately implemented.

Accelerated Public Works.—Another major Congressional initiative aimed at our pervasive unemployment problem would have authorized \$5.5 billion for a program of accelerated public works projects, extension of the Public Works and Economic Development Act, and the Appalachian Regional Development Act. The \$2 billion that was earmarked for job creation in speeded-up public works projects proved unacceptable to the President, however, and drew a veto which the Senate sustained. With such Administration intransigence toward the highest unemployment in a decade, we were forced to re-draft a compromise bill to extend Appalachia aid and EDA, with only \$500 million for unemployment in accelerated public works. Though we passed this legislation on August 5, the President did not order its implementation until December, and then only in a most parsimonious manner.

Revenue Act.—To provide stimulation for a lagging economy we approved \$15.8 billion in personal and business tax relief. These tax breaks included a seven percent investment tax credit for industry and speed-up of personal tax exemption and deduction increases scheduled for subsequent years. The final product due to Democratic Congressional efforts gave a far greater measure of tax relief to those in the low and moderate income brackets than would have the President's original proposal.

Small Business Loan Ceiling Increase.—To ease problems faced by small businessmen during recessionary times, we increased SBA's outstanding loan ceiling from \$2.2 billion to \$3.1 billion for regular and displaced loans, trade adjustment loans, prime contracts and opportunity loans though fiscal 1972.

Unemployment Compensation.—In a bill amending the administration of the Federal unemployment tax collection system, we authorized the payment of an additional 13 weeks of unemployment compensation to individuals who have exhausted their benefits in States with a jobless rate over 6.5 percent.

Conventional text book wisdom of our era has it that, in areas of paramount legislative importance, the President proposes and the Congress disposes. Like so many unexamined maxims dealing with human affairs, this, when tested against the practical experience of the 92nd Congress, proves to be less than the entire truth. This Congress, certainly in the economics sphere, to an extent unwitnessed probably for half a century, has been the innovator, the proposer; the President and the entire Executive Branch, by way of contrast, have played the passive role of reactor or receiver, sometimes opposing, sometimes accepting with great reluctance economic reforms emanating from Capitol Hill. The current combination of inflation and recession would be much worse had the Congress relied on the Administration's recommendations alone and failed to enact on its own initiative the economic legislation placed on the statute books during the past year.

The Congress will not allow continued high unemployment and underutilization of productive ability to further pile up the mass of lost potential. We will stand ready during the year to expand public employment further, to enact emergency grants to State and local governments to tide them over the recession, to build additional necessary public facilities, and thereby meet basic needs while providing additional employment, and take any other steps necessary to restore our economic well being.

MINORITY VIEWS
on the
1972
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 1972 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.

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I. INTRODUCTION

On August 15, 1971, President Nixon startled the nation and the world with a series of bold measures to deal with the problems of unemployment, inflation and our unfavorable balance of payments position. In so doing he won the plaudits of the overwhelming majority of business, labor and financial leaders both here and abroad, as well as those of the American people.

Seven months after inauguration of the Administration's New Economic Policy there has been substantial progress on each of these fronts. Nevertheless, we must recognize that problems still remain. In our view, the primary task of economic policy this year will be to continue to reduce unemployment and inflation while at the same time our economy continues to expand. As the current debate over what constitutes "full employment" suggests, the measures we need to take in order to carry out this primary task will require more than merely stimulating aggregate demand. During this very crucial period, policy makers must display considerable objectivity both in examining the sectors and causes of present unemployment and in prescribing remedies.

In the international area the problems of dollar convertibility and the establishment of a more stable, permanent basis for a reformed international monetary system will present challenges at least as great as those which faced the draftsmen at Bretton Woods.

As this Annual Report goes to press, virtually all economic forecasters are predicting significant gains for the economy in 1972. Nevertheless, a degree of caution understandably carries over from the uncomfortable period of scaling back an overheated economy. In this delicate setting, those who speak out on economic affairs can have almost as much influence as a mere recitation of economic events themselves. This places a responsibility on those who would criticize present policy to avoid negativism and offer realistic alternatives in specifics rather than generalities.

II. REVIEW OF 1971

PRIOR TO AUGUST 15

By the end of the first four months of 1971 the index of leading indicators had posted its sixth consecutive monthly advance, and the latest Conference Board consumer survey indicated that consumers were stepping up their buying plans. Housing starts had reached a record rate of just under 2 million per year, retail trade was running ten percent ahead of the 1970 figures, and civilian employment on a seasonally adjusted annual basis had chalked up a two month advance of 5.7 percent. There was considerable debate as to the advisability of injecting extra stimulus into the economy. News articles at the time revealed that economists and political leaders from both parties could be counted on each side of the fence.

There was also disagreement over the use of more direct wage and price policies. Some favored wage and price controls; however, others cited the difficulty of administering controls and the lack of a sufficient sense of urgency among the American people, whose voluntary compliance was necessary to make controls effective. Two additional arguments against more direct wage-price policies were that consumer prices were rising at a less than three percent rate for the year, and that significantly increased productivity gains suggested a less inflationary environment for the current policies. The "current policies" included many elements of a mature incomes policy: for example, the Construction Industry Stabilization Committee, a system of inflation alerts, and revised government procurement policies.

One area in which there seemed to be little disagreement was that of international monetary policy. Although the outlook for the U.S. balance of payments was very cloudy, there was general agreement among central bankers that the solution to the problem rested as much with other countries as with the United States. When Germany was forced to float the mark in early May, most central bankers looked upon the immediate solution to the crisis as being in the hands of Germany rather than the United States.

The difficulty for economic policy at that time derived from the fact that we were in a new economic environment. Unemployment still hovered at unacceptable levels at a time when there had not been a sufficient reduction in consumer prices. Especially puzzling to economists was the fact that the savings rate was at a historical high, indicating that additions to consumer income could not be the only solution to expanding the economy. Business borrowing was directed in large part toward increasing liquidity, so that activity in the financial markets could not necessarily be interpreted as a sign of plans for markedly increased business investment. A complicating factor was that an unduly expansionary monetary policy in this state of affairs was likely to produce a flight of interest-sensitive funds from the United States and thus aggravate our balance of payments. In this setting of uncertain economic signals alongside clear signs of

progress there was ample cause to wait until the indicators gave proof positive of the need for a change in policy.

By mid August it was clear that the favorable trends indicated in the first quarter were not going to produce the hoped-for growth. Nor did the price behavior create much cause for optimism. The second quarter GNP figures showed an economy moving at a rate insufficient over the long run to absorb new entrants to the labor force. While the record of price inflation continued to be better than in the previous year, the improvement was not sufficient to calm fears of a continuing inflation. Even more disturbing was the fact that our merchandise trade balance (excluding military) deteriorated sharply during the second quarter, posting a slim deficit on a seasonally adjusted basis for the period. This gave speculators yet another reason for hedging on a revaluation of other currencies, and the very severe pressures against the dollar in foreign exchange markets resulted ultimately in a loss of reserve assets by the U.S. in early August of more than \$1 billion.

THE NEW ECONOMIC POLICY

On August 15, 1971, President Nixon made a nationwide radio and television address concerning the state of our nation's economy. In the wake of an economy disrupted by war, overexpansion and inflation, he made the following comments:

Prosperity without war requires action on three fronts: We must create more and better jobs; we must stop the rise in the cost of living; we must protect the dollar from the attacks of international money speculators.

We are going to take that action—not timidly, not half-heartedly, and not in piecemeal fashion. We are going to move forward to the new prosperity without war as befits a great people—all together, and along a broad front.

This speech inaugurated the President's New Economic Policy.

President Nixon announced at that time the means he intended to employ in solving each of the major economic problems he identified as facing the nation—unemployment, inflation and international monetary disequilibrium. First, he described the fiscal measures that would generate more employment. The Job Development Credit and the Accelerated Depreciation Range were designed to stimulate investment in new equipment, which would generate new jobs and increase productivity. The elimination of the automobile excise tax and the speed up in the reduction of personal income taxes were designed to encourage consumer demand in an effort to expand the economy and thereby create more jobs.

Next, to cope with inflation, the President announced an immediate 90-day wage-price-rent freeze to halt inflation and break the back of the inflationary expectations which played a large role in keeping the inflationary spiral moving upward. The President announced at that time the establishment of the Cost of Living Council, which he commissioned to set up a program which would establish economic stabilization after the 90-day freeze was over.

The President's third major effort was to suspend the convertibility of dollars into gold and other reserve assets; and, as a temporary

measure to strengthen the U.S. balance-of-trade position until an international monetary agreement was worked out, to impose a 10 percent surcharge on all imports to the U.S.

Assessment of the NEP.—The President's efforts towards international economic stability have been productive. They were clearly a major impetus to the resolution of an international monetary crisis which existed during the summer of 1971. (The international economy is fully discussed in Section V below.) Additionally, the surcharge on imports into this country, originally designated a temporary measure, was eliminated because of progress in finding a solution to our international trade problems.

With respect to the problem of unemployment, we note that every member of the Administration who testified before this Committee during its Annual Hearings this year deplored the unemployment rate that has existed during the past year. Each of them—Chairman Stein of the Council of Economic Advisers, Treasury Secretary Connally, Labor Secretary Hodgson and Director Shultz of the Office of Management and Budget—described the steps being taken by this Administration to reduce the rate of unemployment significantly by the end of 1972. Each of these leaders supported an expansionary monetary and fiscal policy to generate demand for goods and services and thereby the need for more workers to produce them. Each approved the realignment of international exchange rates as a means of improving the United States balance-of-payments position and increasing employment by raising our exports relative to our imports. A time lag must be expected, however, before these policies can be expected to bear fruit.

Secretary Hodgson, in particular, discussed in detail the expanded Federal manpower programs, including those geared towards unskilled youth, programs to aid veterans returning from Vietnam and the Technology Mobilization and Re-employment Program to help displaced scientists and engineers find jobs. We are spending approximately \$10 billion annually for manpower programs and unemployment compensation—about \$2,000 for each unemployed person. The programs to reduce unemployment are the most difficult to evaluate at this time, mainly because they do not lend themselves to the immediacy of results that characterize efforts to control inflation and stabilize the international monetary situation.

It was only in December of last year that Congress, in the Revenue Act of 1971, passed a modification of the fiscal measures requested by the President last August to stimulate growth in the economy, make American manufacturers more competitive with foreign manufacturers and generate new jobs. If Congress implements the full employment budget recommended by the President, this, along with the other measures announced in August, should enable the goal of 5% unemployment by the end of 1972 to be reached.

The third aspect of the President's New Economic Policy has been the most visible component of his program. The economic stabilization plan, beginning with the Phase I "freeze" has produced results in the battle against inflation, and at the same time remains consistent with efforts to reduce unemployment.

The failure of jawboning and voluntary restraints in the form of the wage-price guidelines practiced by the Democratic administrations in the early 1960's and similar experiences in various other industrial

countries convinced the President and his economic advisers that repetition of such measures would be inadequate to solve the nation's economic problems. The decisive move to halt increases in wages and prices for 90 days was designed to discourage inflationary expectations which had become a built-in obstacle to efforts to combat inflation. Lastly, the Administration was well aware that an absolute "freeze" would generate inequities. It wanted to use the period of the "freeze" to develop a more flexible and more equitable transition to wage and price stability.

Phase I: The Freeze .

Because the freeze required complete surprise to prevent anticipatory action and windfalls, little planning and no organizational preparation could be carried out prior to August 15th. The element of surprise was important to deter anticipatory wage and price increases that would undoubtedly have evolved had such action been alluded to prior to its implementation. It is clear that this was accomplished.

The Office of Emergency Preparedness (OEP) was charged with the responsibility for administering the freeze. Operating under the direction of the Cost of Living Council (CLC), which the President established as the coordinating body of the economic stabilization program and which made all policy decisions during the period of the freeze, the OEP responded swiftly and efficiently in discharging the difficult tasks of disseminating information concerning the rules and regulations of the freeze and responding to the reports concerning violations. The dissemination effort was aided by the widespread publicity received by all policy decisions concerning every aspect of Phase I.

Though over 6,000 requests for exemptions to the freeze were received by the OEP, the CLC, which ultimately decided all exemptions, allowed only five individual exemptions during the entire period of the freeze. During the same period, the Internal Revenue Service, working as the compliance-enforcement office for OEP, checked 46,000 complaints of alleged violations of the freeze and spot-checked another 85,000 in conjunction with routine income tax audits.

Opinion polls disclosed that the freeze was overwhelmingly popular among the American public which was pleased that decisive action had been taken to stop inflation's erosion of real incomes. This support is documented by the high degree of compliance the IRS found in its spot checks, and in the small number of cases (35) referred to the Justice Department for willful violations of the freeze.

During the period of the freeze, the Consumer Price Index rose at monthly rates of less than half those of the prefreeze period, 3.8 percent between January and August as compared to 1.7 percent between August and November. Wholesale prices rose even more slowly than consumer prices, and industrial wholesale prices actually declined between August and November by 1.8 percent. Clearly the freeze achieved its primary goal of quickly reducing the rate of inflation.

Phase II: More Flexibility

The rigidity of a program such as the freeze is obviously unworkable in the long run in a dynamic economy such as ours. The President made it clear from the beginning that the freeze would be a temporary

measure used for the specific purposes of effectively breaking the inflationary spiral until a more workable, equitable program could be developed and effected.

Such a plan was announced by the President on October 7, 1971, in another nationwide address. At this time, he introduced the Price Commission and the Pay Board as the organs which would oversee Phase II of the New Economic Policy. The Cost of Living Council's policymaking role was modified in Phase II; it maintained its function as coordinator and disseminator of information as well as its responsibilities for program coverage and classification. It was clear that the two new bodies would have the final say in determining pay adjustments and price changes consistent with the objective of attaining an inflation rate of between 2 and 3 percent by the end of 1972. Advisory bodies were established to aid the Pay Board and Price Commission in areas where particular problem issues were likely to occur. The committees on Interest and Dividends, Health Services Industry, State and Local Government Cooperation, National Commission on Productivity, the Rent Advisory Board and the Construction Industry Stabilization Committee all provide expert input when needed by the Pay Board and Price Commission to make decisions which are as objective and equitable as possible.

Because of the rigidity and stringency necessary in Phase I, certain inequities were bound to affect individuals or groups within the economy. In extending the Economic Stabilization Act of 1970 to April 1973, Congress adopted amendments which were designed to rectify major inequities arising from the freeze during Phase I. Wage and salary increases scheduled to take effect after the freeze by contracts entered into before August 15, 1971, were authorized to be paid unless "unreasonably inconsistent" with the Pay Board standards. Likewise, wage and salary increases which were scheduled to take effect during the freeze by virtue of contracts negotiated prior to the freeze were allowed retroactively unless judged "unreasonably inconsistent" with Pay Board standards. The retroactive payment of wage and salary increases provided for by law or contract prior to August 15, 1971, where prices had been advanced, productivity increased, taxes raised, or appropriations made of funds which had otherwise been raised or provided for to cover such increases were ordered regardless of Pay Board standards. Employer contributions to pension, profit-sharing, annuity and savings plans, as well as contributions to group insurance and disability and health plans were not to be included in the Pay Board standards for approved increases in wages and salaries unless found to be "unreasonably inconsistent". Finally, wage increases to individuals whose earnings were substandard (less than \$1.90 an hour) or who were members of the working poor were not to be limited by Pay Board standards for approving wage and salary increases. These are examples of the elimination of inequities experienced during Phase I.

By these actions, Congress acknowledged the necessity of upholding the validity of such contracts as fundamental to obtaining the support of labor and management for the stabilization effort. It also recognized that the economically disadvantaged should not be placed at further disadvantage in anti-inflationary efforts.

The Price Commission announced its goal of holding average price increases in the economy to a rate of 2.5 percent per annum, consistent

with the overall goal of the Administration to get inflation down to between 2 and 3 percent by the end of 1972. It plans to do this by requiring firms to justify price increases on the basis of costs and to maintain some restraint on profit margins of firms which increase prices. The Pay Board's general standard for average wage increases was announced as 5.5 percent per year based on productivity improvement and cost-of-living trends. The 1972 *Annual Report of the President's Council of Economic Advisers* states:

The standards announced by the Pay Board and the Price Commission imply the following arithmetic: If compensation per hour of work rises by 5.5 percent per annum, and if output per hour of work rises by 3 percent per annum, labor costs per unit of output will rise by approximately 2.5 percent per annum. If prices rise in the same proportion as labor costs, which are the largest element in total costs for the economy as a whole, then prices will also rise by 2.5 percent, a rate within the range of the goal set by the CLC.

The standards set by the Price Commission and Pay Board, according to the CEA Report, imply a minimum growth in output per man hour—or productivity as it is called—of 3 percent per year. This growth in productivity is imperative if we are to meet our goal of holding down costs and prices and regain our favorable balance of trade. However, in the past several years the United States has not met the average annual rate of 3 percent which had prevailed for most of the past two decades. In the second half of the 60's, productivity in the United States averaged only 2.1%, well below the previous average annual rate.

In writing the Economic Stabilization Act Amendments, the Congress recognized the importance of productivity as a factor in reaching our national goal of holding inflation to between 2 and 3 percent. First, it made the commitment that all rules, regulations and orders issued under the Economic Stabilization Act Extension should be designed to encourage labor-management cooperation for the purpose of achieving increased productivity, and it instructed the Executive Director of the National Commission on Productivity to be consulted in the formulation of policies, rules, regulations and orders under the Act—which by definition include all policy decisions of the Pay Board and Price Commission. Second, the Congress exempted from Pay Board standards salaries paid in conjunction with existing or newly established employee incentive programs which are designed to reflect increases in employee productivity. These amendments were offered by Senator Percy. Third, under the aegis of Senator Javits, Congress put into legislation the Executive Order of the President which created the National Commission on Productivity. The Act authorizes the sum of \$10,000,000 for use by the Commission in pursuance of increasing our nation's productivity. (The importance of productivity in restoring stability to the United States economy is discussed in detail in Section III.)

By the week ending March 7, 1972, the Price Commission had approved price increases for 2,017 pre-notifying companies. The average rate of these increases was 3.1 percent, slightly more than the standards established by the Commission. However, the price increase of total sales (including those of pre-notifiers) averaged only 1.6

percent, well below the 2.5 percent standard declared by the Price Commission.

The Pay Board as of February 25th has consented to 1972 wage increases for its prenotifiers who have filed since the end of the freeze. The average increase of agreements negotiated prior to November 13, 1971, was 4.3 percent; for those negotiations concluded after November 13, the average increase in wages and salaries was 3.7 percent. These averages are well below the Pay Board's general standard of 5.5 percent.

In addition to the progress made by the Price Commission and the Pay Board, it is encouraging to note that the pressure on the IRS as recipient of wage-price complaints has substantially subsided in recent weeks. We may conclude that the degree of voluntary compliance is substantial, as it was in the case of the freeze. If this were not true, the IRS offices would undoubtedly be inundated with complaints and reports of alleged violations.

In analyzing Phase II, it must be remembered that the ultimate objective of Phase II is to reduce the annual rate of inflation to 2 to 3% by the end of 1972. However, as Dr. Herbert Stein, Chairman of the Council of Economic Advisers, declared in his testimony at the Annual Hearings of the Joint Economic Committee:

We are not so naive as to think that for the first time in history we have devised a price-wage control system that is perfectly effective, fair and efficient. But we do think the system that has been set up has accomplished a great deal and will accomplish a great deal more.

Once controls have served their purpose and economic stability has been restored, we will return to an economy guided by the principles of the free market mechanism.

Already the Cost of Living Council has made strides in the direction of eliminating controls. The CEA Report, as well as the Economic Stabilization Program Quarterly Report, list all of the items which were decontrolled from the beginning of the program in August until December 31, 1971. Since that date, the CLC has announced a number of other items which are now exempt from the controls program. In accordance with the title in the Economic Stabilization Act Extension which says that "wage increases to any individual whose earnings are substandard or who is a member of the working poor shall not be limited in any manner, until such time as his earnings are no longer substandard or he is no longer a member of the working poor," the Council has declared that workers receiving less than \$1.90 an hour are exempt from the Pay Board controls.

The CLC also excluded from price controls most State and local government fees and charges, fees and charges for securities traded on exchanges regulated by the Securities and Exchange Commission, luxury apartment units which rent for \$500 per month or more, owner-occupied apartments (single or multiple family) of under four units, fees and charges of nonprofit educational institutions, and, most recently, retail firms with sales under \$100,000 per year. The CLC is eliminating from controls those segments of the economy which it judges are not contributing to or which have negligible impact on inflation.

III. OUTLOOK FOR 1972

Our economic goal in 1972 is to achieve strong economic growth in a condition of high employment and low inflation. In mid-1971, President Nixon, seeing that our economy was not moving towards this goal satisfactorily, set this nation on a bold new economic course. The New Economic Policy has achieved substantial success in setting the stage for healthy growth with price stability in 1972. We believe that 1972, with the cooperation of the Congress and in the absence of unforeseen major problems, will be, to use the President's phrase, a "good year."

PROJECTED GROWTH IN 1972

One basic measure of performance of our economy is annual Gross National Product. Therefore, in any attempt to foresee what lies ahead for the economy, we must look to GNP. We find it quite encouraging that public and private economists are in substantial agreement regarding probable growth of GNP during 1972. In 1971 there was a substantial spread between the general consensus of private forecasts for GNP in 1971 and the Administration target. This difference reflected both the uncertainty of economic conditions in early 1971 and the fact that the private forecasters were stating their opinions of the "most probable" GNP performance in 1971, while the Council of Economic Advisers was stating a "feasible target" for GNP which would be consistent with moving significantly towards an economy of noninflationary full employment by yearend.

For 1972, the Council of Economic Advisers has projected that GNP will increase approximately \$100 billion to around \$1145 billion. This increase of almost 9.5 percent over the level of GNP in 1971 represents a projected real increase in GNP of around 6 percent and an increase in the GNP price deflator of around $3\frac{1}{4}$ percent. The consensus of a large number of private economists and econometric models for 1972 GNP is about \$1140 billion. These forecasts generally project real growth between 5.5 and 6.5 percent and inflationary growth of between 3 and 4 percent. It is generally agreed that the difference between the consensus of most private forecasts and the Administration forecast is not of any real significance.

As indicated in the Council's Report, GNP forecasts made by the Council were qualified in the past by the warning that these forecasts should be viewed only as the mid-point of a range of plus or minus \$5 billion around the forecast. This warning was appropriate when GNP was about \$500 billion per year. As the Council notes, the "equivalent band of uncertainty for today's larger numbers would be plus or minus \$10 billion." Indeed, a former Chairman of the Council of Economic Advisers in the Johnson Administration predicted 1972 GNP of \$1140 billion, with real growth of approximately 5.5 percent, and stated before this Committee that the difference between his

forecast and the Administration's forecast "is well within the range of forecasting error." We welcome these private and public statements of the approximate nature of economic forecasting. Such statements are a happy contrast to the claims of a decade ago regarding the ability of government economists to forecast and to "fine tune" the economy.

We find this consensus among economists as to probable 1972 GNP encouraging because we believe it stems from increasingly strong performance in various sectors of the economy since August 15, 1971. During the 4th quarter of 1971, GNP increased sharply, with real growth rising at an annual rate of 5.8 percent and inflationary growth held to 1.7 percent as a consequence of the President's wage-price control policies. During the month of January, housing starts were recorded at a seasonally adjusted annual rate of more than 2.5 million, up 4.8 percent from December, 1971. This growth continued the strong upward trend in housing starts which took place during the final months of 1971. It is reasonable to expect that demand for housing will remain high because of the age distribution of our population and the backlog of unmet housing needs. Additionally, the well-established downward trend in mortgage rates should have a very favorable effect on housing construction during 1972. During 1972 the Council has projected total private housing starts at 2.2 million units. We believe that this projection is a perfectly sound one, given the present favorable economic conditions in the housing industry.

There is also good reason to expect personal consumption expenditures in 1972 to be strong. Earned income is expected to grow substantially, and this growth will be supplemented by increases in social security benefits. Additionally, because of abnormally high savings rates in 1971, the buying potential of consumers is strong. Modest tax cuts which consumers will enjoy during 1972 will also increase their disposable income. Finally, increasing consumer confidence, which has been slow in starting, is expected to accelerate economic growth further.

On the output side, we may expect strong performance in industrial production during 1972. Since August, 1971, industrial production has been rising at an annual rate of about 6 percent. As a reflection of rising business confidence that economic performance will be good in 1972, the Department of Commerce-Securities and Exchange Commission survey taken in late January and February, 1972 indicates that businesses are planning a 10.5 percent increase in 1972 over 1971 in total outlays for new plant and equipment. This survey compares very favorably with the Commerce-SEC survey taken in November and December, 1971, which projected a spending increase of 9 percent in 1972. Accompanying these expenditures, we believe it reasonable to expect business inventories to expand during 1972, given the low level of inventory investment during the past two years and the favorable sales prospects expected in 1972. In fact, inventory investment during the fourth quarter of 1971 showed a substantial rebound from the net disinvestment during third quarter 1971.

FISCAL POLICY

An expansive fiscal policy will supplement the stimulation which the economy will receive during 1972 from steady growth in the private sector. The stimulus contained in proposed Federal expenditures

for 1972 can perhaps best be evaluated by comparison to 1971. Between calendar year 1971 and 1972 total Federal expenditures will increase \$29 billion in the national income accounts, or 13 percent. Additionally, tax reductions will total approximately \$3.7 billion. In terms of the full employment budget we will see a swing from an excess of receipts over expenditures in 1971 of \$5.5 billion to an excess of expenditures over receipts of \$6.5 billion in calendar year 1972—an overall swing of \$12 billion between the two years.

As for the fiscal year budgets, the 1972 fiscal year budget is expected to result in a deficit of \$38.8 billion (on a full employment basis, this deficit would total \$8.1 billion). The 1972 budget was originally projected to be in approximate balance on a full employment basis and to show an actual deficit of \$11.6 billion.

There are several reasons for the difference between the original projections and present expectations. First, because of the lower-than-expected level of economic performance, a shortfall in the originally estimated revenues to the Federal Government during fiscal 1972 is expected in the amount of \$15.4 billion (exclusive of tax changes). Additionally, the Revenue Act of 1971, enacted as part of the New Economic Policy in order to stimulate the economy, is expected to result in net tax reductions totaling \$4.4 billion. Higher than projected Federal spending is expected to total \$7.4 billion. A substantial deficit is projected for fiscal year 1973, but the budget is in balance in full employment terms. (The projected deficit of \$25.5 billion arises from a shortfall in revenues from what would be available to the Government at full employment.)

The size of these deficits is a matter for concern, regardless of how appropriate the deficits may be in immediate economic terms. Therefore, we believe it of vital importance that the Congress act on President Nixon's request that a rigid ceiling be imposed on fiscal year 1973 expenditures, but reserving to itself the right to reallocate expenditures if necessitated by the ceiling. Enactment of such a ceiling would serve several purposes. First, the American people must be assured that the Federal budgetary process is not careening along out of control, but that the large budget deficits have been an appropriate response to pressing economic problems arising during the transition from a wartime to a peacetime economy. Second, it would force both the Executive and Legislative branches to keep the overall budgetary picture in perspective. Absent such a ceiling, there is a great temptation to focus on specific programs within the budget without keeping clearly in mind the place of the programs in the total spending process. Yielding to this temptation results in loss of control over expenditures, something that has happened in the Congress all too frequently in recent years.

In past Minority Views, we have described how the appropriations process can be improved (e.g., zero base budgeting, the establishment of a Congressional Office of Goals and Priorities). We believe that such suggestions can be useful in implementing a spending ceiling.

MONETARY POLICY

What should the course of monetary policy be during the coming months? We are assured by the Chairman of the Federal Reserve that the Fed will supply adequate funds to support the current eco-

conomic recovery, but will not be the architect of a new round of inflation.

Some analysts have questioned the ability of monetary policy to generate much additional demand in the early stages of economic recovery. We note, for example, that Chairman Burns stated on several occasions at last year's annual hearings that banks were "full of money" and "hunting for customers" at a time when, in retrospect, the rate of economic growth was not especially rapid. Projections developed by the Joint Economic Committee indicate that the largest single stimulus to economic recovery at times such as this can be a sharp revival of consumer confidence, which suggests that the primary role of monetary policy at this point in the business cycle may be to provide a favorable climate for economic growth based primarily upon private sector growth and an expansionary fiscal policy.

During 1972 the Fed will face the difficult task of balancing the need for a monetary policy adequate to fund strong economic growth against the need to restrain inflation. To supply the liquidity needed by an expanding economy, and avoid so large a rise of interest rates as to choke off the expansion, will require substantial growth in the money supply. Much of our budget deficit during calendar year 1971 was financed by foreign governments rather than through Federal Reserve operations. By reinvesting officially held dollars in special U.S. Treasury issues, foreign governments accumulated \$10.8 billion of the U.S. Federal debt from January to December, at a time when the total Federal debt rose \$23.5 billion. To the extent we are successful in improving our official settlements balance during 1972 we cannot expect this pattern of Federal debt financing to repeat itself.

On the other hand, the Fed must take care that our monetary policy does not have the effect of increasing inflationary pressures and reducing the impact of our comprehensive anti-inflationary policies. The sacrifices and efforts of the last few years in the fight against inflation have been too great to jeopardize our growing hard-won success by inappropriate monetary policies.

Under these circumstances we cannot presume to recommend a specific rate or range of monetary expansion. We are confident that during 1972 the Fed will show its accustomed flexibility in reconciling the problems of achieving our goals of economic expansion, a complementary interest rate structure vis-a-vis other major countries, the avoidance of strains in the financing of Federal debt and the avoidance of renewed inflationary pressures.

PRICE-WAGE CONTROLS ¹

The price-wage control system which went into effect last August made great contributions to the sharp reduction in inflationary growth during the last half of 1971. We believe that this progress will continue in 1972.

Price-wage control systems have generally broken down after varying periods of time because of excess demand for various goods

¹ Congressman Blackburn comments that philosophically he is opposed to wage and price controls and feels that they set a dangerous precedent for the economy; however, it is obvious that President Nixon's freeze and now Phase II were needed in order to break the psychology of inflation which had been gripping the economy.

and services. This demand places the control system in direct opposition to market forces. Our present control system was not imposed at a time of excessive demand, or during what has been called a "demand-pull" inflationary period. Instead, we had a "cost-push" situation, which was the consequence of expectations, ideas and attitudes built up during the period from 1965 on. In testimony before this Committee last month, several economists indicated that, given our recent inflationary history, only a system of mandatory price-wage controls of the type now in effect could successfully reduce inflationary psychology and expectations within a reasonable time period. The alternative approach was to endure unacceptably high unemployment levels for a period of four or five years, which, as President Nixon has said, is a price we are unwilling to ask the American people to pay.

With controls, we hope to eliminate this inflationary psychology and at the same time work to reduce our present unemployment level through healthy economic growth. Over the course of controls, if all goes well, expectations and attitudes will become ones of "price stability," at which time controls will be removed. We believe such ultimate removal to be essential, inasmuch as a system of permanent controls is inconsistent with the operation of a free market system, in which market forces are able to act efficiently in setting wages and prices and in allocating resources. In our present situation, we believe that it will be appropriate gradually to decontrol various sectors of our economy as it becomes apparent that certain sectors may be decontrolled without an inflationary impact. The Administration has already removed a number of areas from control as appropriate during the last several months. As this policy of gradual decontrol continues, the remaining controls will be strengthened. This strengthening will result both from the ability of the staff engaged in administering the control system to concentrate more heavily on the remaining controlled areas and the probable favorable effects on public support which will result from partial decontrol.

EMPLOYMENT AND UNEMPLOYMENT

As the President has said, "The great problem [in 1972] is to get the unemployment rate down from the 6 percent level where it was in 1971." We have already made substantial progress towards this goal; between December 1971 and February 1972, the unemployment rate, as seasonally adjusted, dropped from 6.0 to 5.7 percent. We believe that the Administration's fiscal policy for 1972, including manpower programs, and the price-wage control system will enable us to reduce the unemployment rate of 1971 even more by yearend.

The unemployment rate resisted reduction rather stubbornly during late 1971, at a time when our economy was showing increasing strength. This strength was reflected in large part in rapid growth in total employment. During the second half of 1971 new jobs in the economy increased by almost 1.5 million. In spite of this, the unemployment rate remained relatively steady. This stability in unemployment in the face of economic growth resulted principally from a larger than normal growth in the labor force during late 1971, which was based upon several factors. First, as job opportunities improved, more people, especially women and young persons, were drawn into

the labor force. Second, the number of persons released from the armed services and the reduction in draft calls operated to increase the civilian labor force at a faster than normal pace.

Moreover, throughout 1971 the unemployment situation was aggravated, as it has been for the last several years, by the elimination of large numbers of both military and civilian defense related jobs. In 1971 approximately 2 million fewer persons were employed in defense than in 1968. There were 700 thousand fewer jobs in 1971 than in 1970. In addition to the general nationwide effect on unemployment, these reductions have caused sharp geographical variations in the incidence of unemployment. At the same time that these defense jobs were being eliminated, we did not have a rapidly expanding nondefense sector in the same geographical areas which could absorb the released workers. At the end of World War II, when we were converting from a wartime to a peacetime economy, as we have been again in recent years, there was a tremendous pent-up demand for goods and services. This demand permitted the rapid assimilation of persons released from defense work into the nondefense civilian labor force. Because the American people were not deprived of goods and services during the Vietnam war as they were during World War II, the winding down of the war in Vietnam has not released strong domestic demand and, therefore, not caused a rapid expansion in nondefense employment.

In addition to these factors which had substantial effects on our labor force and unemployment rates in 1971, and which will continue to have some effect in 1972, recent years have seen significant structural changes in our labor force and in the composition of the unemployed category which affected employment and unemployment in 1971 and which will continue to do so in years ahead. If we wish to reduce the unemployment level to the lowest possible point which is consistent with noninflationary growth, we must be aware of and deal with these structural changes, which were forcefully presented to this Committee during its recent hearings. The extent of these changes is apparent by comparing the composition of the labor force in 1949 and 1971, two years in which the unemployment rate for all workers was an identical 5.9 percent. In 1949 male workers aged 25 years and over comprised almost one-half of the total work force. These workers generally have the highest level of skill and experience and the greatest attachment to the labor force. By 1971 males aged 25 and over comprised less than 30 percent of the work force. In 1949 females totaled slightly less than 30 percent of the work force; in 1971 they comprised over 44 percent. Additionally, young males aged 16 to 19 totaled under 10 percent of the work force in 1949, but 13.8 percent in 1971. For various reasons which will be of critical importance to policymakers, both women and young males generally have a higher overall unemployment rate than older male workers. As the proportion of the total work force comprised of young men and women has increased, their overall higher unemployment rates have raised the general unemployment rate for all workers as a percent of the total labor force. As a result of these changes, there is great need for special measures to assist women and inexperienced young workers entering the labor force in finding jobs. We no longer have a nationwide problem of there being insufficient jobs for experienced, skilled workers.

The extent of the difficulties caused by the structural changes in our labor force may perhaps be highlighted by looking at unemploy-

ment of workers aged 19 years and less. In 1971, these young workers had an unemployment rate of 16.9 percent, as compared with 4 percent for adults aged 25 and up and 3.2 percent for married men (which had dropped to 2.8 percent by February 1972, the lowest level since August 1970). In 1962 the unemployment situation for teenagers was just over three times as high as for workers aged 25 years and over. Beginning in 1963, this ratio began to exceed 4 to 1. For the years 1963–1971, the average ratio of unemployment of young persons to unemployment of workers aged 25 years and up was 4.7 to 1. Testimony before this Committee indicated that this rise in teenage unemployment relative to overall unemployment is probably attributable to a number of factors, including the rapid rise in the number of teenage workers as a result of the post World War II baby boom, reduction in the size of our armed forces, the elimination due to technological advances of many unskilled jobs previously filled by young workers and, finally, the large number of students among the young labor force.

Given the rapid growth in the number of young persons seeking employment and the probable continuing decrease in the number of unskilled and other entry level jobs which these young persons traditionally fill, we believe it imperative that a number of new approaches to enable young workers to be more employable be considered. One is increased emphasis on technological and vocational skill training for young persons, as opposed to the present strong emphasis on a college education for virtually everyone, regardless of students' personal inclinations or abilities. We must avoid educating too many people for jobs that will not open up—especially at a time when our changing technology requires increasing numbers of workers with specific technical skills.

A second approach is one which has been urged by the Administration, namely, the provision of a lower minimum wage for teenagers to encourage their employment in certain types of jobs, mainly unskilled. The Council of Economic Advisers suggests in its Report that the rising level and the expanded coverage of the minimum wage in recent years may have been a strong factor in the upward trend in the teenage unemployment rate. We feel that a rise in the present minimum wage for adult workers, while holding the rate at the present level for teenaged workers, might well have very favorable effects on teenage employment. However, we question whether any rise in the minimum wage during 1972 is appropriate.² We heard with great

² Senator Javits believes that the minimum hourly wage should be raised to \$2.00 promptly. In his view, such an increase is necessary to enable low-paid employees to keep pace with the increased cost of living (an increase to \$2.07 would be required to make up fully for the erosion in real income suffered by workers receiving the minimum wage of \$1.60 since 1966). Senator Javits believes that our past experience demonstrates that increases in the minimum wage have not had the disemployment effects predicted by some economists; nor have they been a significant cause of inflation, especially when the increases occurred during periods of economic recovery, such as we are now experiencing. Finally, Senator Javits believes that an increase in the minimum wage to \$2.00 would be fully consistent with the express provisions of the Economic Stabilization Act exempting workers with "substandard earnings" from the stabilization program. The Cost of Living Council, acting pursuant to those provisions, has established the exemption rate as \$1.90 per hour, and Senator Javits believes even that rate should be revised upward to reflect more accurately the intention of Congress in approving the exemption.

interest testimony from noted economists of varying political persuasions before this Committee in recent months on the probable economic effects of raising the minimum wage in 1972. Not one felt that such a rise is advisable now.

MANPOWER POLICIES AND PROGRAMS

In addition to the stimulative effects on the economy which we expect from the Federal budget in general and the price-wage control system, we believe that the Administration's manpower policies and programs will have a strongly positive effect on the economy and employment during 1972. In fiscal 1972 expenditures in the unified budget for unemployment compensation and for manpower programs will exceed \$10 billion. If unemployment in this fiscal year should approximate 5 million persons, this would amount to more than \$2000 per person. Manpower programs, which have a long history, have been substantially expanded in the last three years. In fiscal 1973 the Federal Government expects to spend \$5 billion on Federal manpower programs. This is exclusive of unemployment insurance and is approximately 20 percent more than will be spent on these programs in fiscal 1972.

In addition to the continuing manpower programs in which nearly a million young people were enrolled in fiscal 1971, such as the Neighborhood Youth Corps, the Concentrated Employment Program and Job Opportunities in the Business Sector (JOBS), during 1971 a number of programs aimed at specific sectors of our population with high unemployment were instituted. These programs will continue in 1972 and we expect them to have a highly favorable effect on employment.

In the last two years the number of male Vietnam era veterans in our civilian population increased by over 1.3 million. During 1971, a number of programs were launched by the Administration to aid these veterans in finding jobs. Project Transition, which is a discharge counseling, training and placement program, was stepped-up. Also, in the private sector, more than 100 Job Fairs, which aim at bringing veterans and prospective employers together, were held in cooperation with the National Alliance of Businessmen. These Job Fairs resulted in the placement of approximately 320,000 veterans in the second half of 1971. Additional substantial placement is planned for 1972.

On a second front, the Administration has taken strong steps to reduce unemployment and meet various public needs. Under the Public Employment Program, which was authorized by the Emergency Employment Act of 1971, the Federal Government subsidizes a large part of the cost of adding new employees to State and local government payrolls. A number of steps were also taken in the area of defense-related civilian employment, which has been greatly reduced in the last few years. The Technology Mobilization and Re-employment Program and related programs, which were expanded rapidly during 1970 and 1971, will be increased further during 1972, and should have a very favorable effect on some of the high regional unemployment rates attributable to these defense employment reductions. The use of modern data processing techniques by the U.S.

Employment Service in providing job information has also made a strong contribution to reducing unemployment. The computerized listing of job openings, which are known as Job Banks, has expanded rapidly and now covers most of the major labor markets in the United States.

In addition to the ongoing large manpower programs and the specialized programs which have been instituted in the last year or so, the President has recommended to Congress a series of special revenue sharing programs, including the Manpower Revenue Sharing Act. We share the President's sense of urgency regarding special revenue sharing for manpower programs. We believe that consolidation of most manpower programs into a single large program, the elimination of most of the narrow categorical grants, and the shift of decisionmaking from the Federal level in Washington to State and local governments would make our manpower efforts much more effective by providing the flexibility needed to ensure that training opportunities and job placements are made available where they are needed most. The Manpower Revenue Sharing Act would furnish this flexibility by authorizing services such as classroom instruction in both remedial education and vocational skills, on the job training with both private and public employers, and job opportunities which would include both work experience and short-term employment for certain age groups and temporarily unemployed persons, as well as transitional public service employment.

IV. USE OF RESOURCES

PRODUCTIVITY

The problem of our nation's productivity is of great concern this year, as it was last year, to the Minority Members of the Joint Economic Committee. In response to the drastic decline in the rate of increase in U.S. output per manhour beginning in 1969, last year's Minority Views contained two major recommendations. One suggested the establishment of a permanent National Commission on Productivity operating primarily through regional and local organs which would grapple with the issues involved in productivity performance at the grassroots level. This recommendation was enacted as part of the Economic Stabilization Act Amendments of 1971 (Public Law 92-210), which gave legislative sanction to the National Commission on Productivity and authorized the Commission to spend \$10 million in pursuit of improved productivity in the United States.

Additionally, the 1971 Minority Views recommended that the nation channel its capital into pursuits promising higher productivity. In the fiscal year 1973 budget message, President Nixon responded to that recommendation in increasing by \$1.4 billion—to a total obligation of \$17.8 billion—funds committed to strengthening U.S. technology through research and development. The need for more research and development (R&D) is emphasized clearly in a chapter of the 1972 Annual Report of the Council of Economic Advisers. The Report, outlining the rationale for government participation in R&D, explains that firms are reluctant to undertake large R&D commitments because "although an investment in R&D may produce benefits exceeding its costs from the viewpoint of society as a whole, a firm considering the investment may not be able to translate enough of these benefits into profits on its own products to justify the investment."

The Office of Management and Budget asked the National Science Foundation to study the relationship between R&D and economic growth and production. The conclusions of that study were that the contribution of R&D to economic growth is positive, significant and high and that the United States is under investing in the civilian sector of R&D for the needs of our economic growth and production. Hopefully, the funds the President has made available will help to remedy this situation.

Suggestion has been made to form an R&D production review board—half comprised of scientists and half of union, management and public members—which would review and evaluate research proposals that may be of interest to the Federal Government. Its range might cover research into governmental activities such as the TVA or military arsenals, as well as the efficacy of grants to private industrial or employee relations departments to encourage innovation and evaluation of new productivity techniques.

The establishment of a Productivity Commission and increased Federal R&D expenditures are only a beginning. Productivity is also a function of labor and the management of labor. In a country that has the resources and capabilities to ensure a good life for all of its people, productivity has become a major issue because the price individuals pay for goods and services varies directly with levels of human output. Inflation—erosion of buying power—occurs when the costs of production increase at rates higher than output. The more each individual contributes to total output, the less it costs each to satisfy his wants and needs. If costs, including labor costs, rise sharply, the price will not be affected if productivity is also rising at the same or a greater rate. However, this has not been the case in the United States since 1965, and the country has paid dearly for the poor productivity performance it has experienced. This is demonstrated by the rise of the Consumer Price Index over the past three years, and a sharply eroded position in international trade.

Notwithstanding that labor productivity has been increasing at an above average rate now that we are on the upswing of a business cycle, the uncomfortable fact is that the increase is insufficient to match the average use in labor costs and is also clearly insufficient—as we point out below—to keep pace with productivity gains in other countries.

1.

There are four main reasons why it is imperative that the U.S. consider the improvement of its productivity as a major national priority in the year 1972. First, and foremost, continued growth in productivity is the only long term guarantee to provide the goods and services we need for ourselves and future generations. In last year's Minority Views we pointed out that only small amounts of unallocated resources are available to us over the coming five years to fulfill new needs and desires. Optimizing of these resources means that more productive means of utilizing them must be found.¹

Second, we know that productivity improvement is the only permanent hedge against paying inflated prices for the goods and services we desire—i.e., the only way to achieve rising *real* incomes and stable prices. Since 1965, employee compensation has been rising at significantly higher rates than during the preceding eight years. Yet, during this time, output per manhour has improved only minimally or, during some quarters not at all—conditions which explain a good part of the recent inflationary experience and the fact that real wages have been limited.

Third, improvements in the quality of goods and services produced are paid for most cheaply by productivity gains. We should not measure productivity in a way that ignores the quality of the product or service we are measuring is not ignored. For example, environmental controls for clean air and clean water will probably increase the cost of producing the same number of cars or the same amount of paper.

¹ Congressman Blackburn points out that higher growth of productivity would allow us to meet more of our public needs without scaling back private consumption or investment demand. The productivity issue is more complex than implied here: the volume of allocated resources will increase substantially, and these could be used to meet new needs by changing taxes, shifts in consumption preferences, for example.

The only way these costs will not be passed on to the consumer is through rises in productivity in the production of these higher quality products. Similarly, improvements in the quality of community services can be paid for without raising taxes only if we can improve our productivity in such services as trash collection, education, etc.

Finally, increased productivity is an essential ingredient in the ability of the U.S. to compete in international trade. The table below shows that over the past five years U.S. productivity performance has lagged behind that of other leading industrial nations.

AVERAGE ANNUAL PERCENT CHANGE, 1966-71¹

Country	Output per man-hour	Compensation per man-hour	Unit labor costs	
			National currency	U.S. dollars
United States.....	2.3	6.4	4.0	4.0
Belgium.....	6.6	9.2	2.4	2.7
Canada.....	4.1	8.4	4.1	5.4
France.....	6.3	10.8	4.3	1.5
Germany.....	5.1	10.3	5.0	8.0
Italy.....	4.8	11.8	6.7	7.0
Japan.....	13.8	17.1	2.8	3.5
Netherlands.....	9.2	11.7	2.3	2.9
Sweden.....	7.6	10.8	3.0	3.3
Switzerland ²	6.8	8.2	1.2	2.0
United Kingdom.....	4.5	9.8	5.0	1.9

¹ Preliminary figures.

² Wage earners only.

Source: Bureau of Labor Statistics.

The implications of this phenomenon for our price competitiveness are obvious. Candor compels us to admit that reduced productivity was a factor in our trade deficit last year. As we explain in Section V, America must improve its balance of trade.

2.

What can be done to improve productivity in the United States today and in the years to come? Gains in productivity are the result of improved uses of capital, labor and management practices.

It has been suggested that increased productivity is solely a function of monetary incentives directly reflecting the increased output. However, a problem with this suggestion is that it denies the consumer the dividend of lower prices.

Most research seems to indicate that many factors—including monetary incentives—influence workers' desires and abilities to produce more. It is helpful to look at several ideas that have been proposed.

Upgrading the skills and education of our labor force is an obvious step towards improving productivity. Growth in the productive services per laborer is mainly a consequence of new or additional skills. Board rooms are full of persons who began their careers on the factory floor; nevertheless, it is also surprising to discover instances where the inherent ambition of workers for self improvement and education is not recognized. We must eliminate, or at least greatly reduce, the differential between the most productive and the least productive worker in any given field.

More mobility and flexibility in the labor force would allow easier transitions from low to more highly productive plants, firms and even industries. At present, the rigidity attached to employment in any given plant illustrated by the loss of vested pension rights, seniority, etc., in case of job transfer impedes the worker from making his contribution where it would be most effective.

Job conditions and employment security also are thought to influence workers' productivity. These factors help determine how much effort he is giving. Socially, people who are happy and secure function better than those who are not; this applies to their work as well.

Management must encourage productivity improvements by rapidly adjusting to technological change. In some cases, business management will need the help of labor management. As examples, featherbedding and other work rules which impede productivity gains must be changed. On the other hand, business management must be prepared to pay relocation allowances, in-plant transfers, early retirement benefits and other measures to secure job security and seniority—all of which reduce the pressure on unions to institute or maintain such rules which inhibit increased productivity. This so-called productivity bargaining should be encouraged by Federal Government labor mediators.

Job redesign is another important element in increased productivity. Job redesign could mean a program which eases the physical burdens of older workers and shifts them to younger employees who are better able to cope with more strenuous tasks. Or, it may mean devising aptitude tests to see where each employee best fits into the scheme of a large corporate enterprise. Since people usually want to work at what they do best, this benefits both the employer and the worker.

Union and management cooperation are vital to the cause of increasing productivity. It must be clear to workers that increased productivity does not mean to work faster or harder but to work "smarter". We must educate everyone to understand that increased productivity benefits all.

A program recently initiated by Chrysler Corporation illustrates excellent union-management cooperation. The aim of the Chrysler "Job Enrichment Program" is to involve workers in plant level decisions, solicit their suggestions about work at the plant, and motivate them by making their work more interesting. Since each plant operates its own program, the means of increasing productivity are developed at the grassroots level. Some examples of what these programs involve include: when foremen are on vacation, workers run their own departments; assembly line workers test drive the cars that they have assembled; workers now form teams with foremen and engineers to solve quality problems. The results of this program so far, as reported both by management and labor, are that workers have a new sense of identification with the firm. Communications between management and labor have improved, which itself has led to improved productivity, and absenteeism is abating.

The humanistic improvements which have been mentioned or alluded to are not the only means of giving impetus to improved output for workers. Incentives can play a large role in increasing output per manhour. There are several productivity incentive plans which have

been devised. Both the Scalon Plan and the Rucker Plan call for cooperative relations between union and management utilizing employee participation in solving problems of efficiency. Most of the increased productivity would result from employees' ideas on solving production problems. Gains in a firm's productivity would be shared by management and workers.

Another type of employee incentive program is the Kaiser Plan. It insures job security to employees by providing those displaced by technological improvements with replacement jobs or Employment Reserve funds at previous levels of income for varying periods until new jobs for them are found. Additionally, employees receive 32.5% of any reductions in per-unit cost of steel products; part is received in a monthly bonus and part is placed in reserve to match wage and benefit gains negotiated by other steel producers.

3.

The preceding section deals with some of the methods that can be used directly to stimulate productivity—primarily in the manufacturing sector of our economy. However, the productivity issue is larger than this. National attention must be focused also on productivity in the service and governmental (Federal, State and local) sectors. Productivity in the services sector of the economy has traditionally been lower than that of the manufacturing sector. The problem is compounded as services are becoming an increasingly larger part of our country's total output. A basic problem is our inability to measure productivity accurately in many service industries. Answers in the services area are in short supply, but an important concern of the National Commission on Productivity will be to define key problems and raise potential solutions. In the services area, we are much more limited in our ability to add capital equipment to produce increased output—although it does appear automatic data processing has had and will continue to have a tremendous impact in this area.

Virtually all governmental activity is service-oriented. Increased productivity does not mean how quickly a grant application can be processed, so much as it means how many applications can be processed by one person or one unit. Such services require some amount of qualitative judgment. Thus, increased productivity can arise from reducing the need for qualitative judgment by substitution of quantitative norms where possible, by determining who should render service and when it should be performed. This is a deep, complex problem, but one with which the Administration is already coming to grips. The President has submitted to Congress a major plan for reorganizing the executive department. His hopes are that by restructuring the bureaucracy, it can be made to function more responsively and efficiently, thus providing better services to the American people.

At the local level, there is a deep need for cooperation and exchange of information between governmental bodies. As more effective means of providing community services are discovered, the new information and technology should be made available to other localities which could take advantage of the newly-developed skills.

4.

The real key to productivity lies in one word: flexibility. A pragmatic approach is the only one that offers solutions to a multitude of varied problems. Programs in individual plants must be geared to the priorities of its workers. A doctrinaire approach will not pay off. For example, one factory that was geared to an "efficient" assembly line production approach, found that workers' productivity increased when they were allowed to see an item through several stages of manufacture. Its employees produced more when they viewed themselves as artisans instead of as assembly line robots.

Similarly, in trying to develop a national productivity policy the Federal government may have to be flexible and shift from its conventional thinking about trusts and monopolies in the interests of productivity. There may be instances where productivity is impeded by current barriers to consolidation and exactly the opposite may be true where monopoly, oligopoly or price-supported industries now exist.

A discussion of productivity should also mention the gains which can be made by means of investments in social overhead—e.g., public health and education—which have a significant effect on aggregate productivity even though the effect is not direct. Projections demonstrate that the percentage of the U.S. labor force with a high school education will double in the 30 years between 1950 and 1980. Clearly this will be a more productive labor force, but the "return" in increased productivity from this investment in education is something which we imperfectly understand. By the same token, there is a "return" from investment, for example, in air pollution equipment, in the form of reduced incidence of lung disease and a consequent increase in the amount of output per man.

ENERGY

In recent years our use of energy has risen dramatically. In these views we do not wish to recount the problems which this growing usage has created; the President's 1972 Economic Report describes our energy situation, problems, and alternatives comprehensively. Instead, because of our deep concern over the difficulties in reconciling continuing economic growth and a high level of material well-being with preserving a safe, enjoyable environment for all Americans, we wish to direct our attention to President Nixon's energy message to the Congress of June 1971, and to the initiatives contained in that message.

One of the most fertile fields in the search for ways in which to produce clean energy for a growing America, and thus to strike that reasonable balance between our environmental concerns and rapidly expanding energy needs² which the national interest requires, is that

² We are in the midst of an energy crisis today, as the blackouts and brown-outs, natural gas restrictions, and other fuel shortages of recent years attest. Without a comprehensive, well-directed energy policy, this crisis is sure to worsen. According to the Chairman of the Federal Power Commission, electrical energy usage will almost triple between now and 1990. Growth of the electric utility industry during the next 20 years may require the construction of 40 new hydroelectric installations of 100 megawatts or more, approximately 50 new pumped storage hydroelectric installations of 300 megawatts or more, and about 90 fossil and 156 nuclear steam-electric plants on new sites.

of research and development. In his message to the Congress, President Nixon listed several areas in which new technological breakthroughs are possible, along with programs aimed at achieving these breakthroughs. Sulphur oxides constitute one of our major environmental pollutants; almost all of these oxides are produced as byproducts of energy generation. Our resources of low sulphur fuels are clearly inadequate relative to demand. Common sense as well as economics dictates that efforts be made to reduce the amount of sulphur emissions from conventional fossil fuels. **We support the Administration proposals for Federal funding, in partnership with industry, of research and development of a suitable range of cleaning techniques for removal of sulphur oxides. Successful development of these techniques would enable us to utilize our large resources of high sulphur fuels economically while protecting the environment from excessive sulphur oxide discharges.**

Along the same lines, one of our best hopes for meeting our requirements for large amounts of clean energy lies with the fast breeder nuclear reactor. These reactors utilize nuclear fuel very efficiently and are capable of producing large amounts of energy with a much smaller environmental impact than results from usage of our present fossil fuel plants. **We believe that Federal expenditures towards development of fast breeder reactors with low, environmentally safe levels of thermal and radioactive discharge are a sound investment in our future national energy producing capacity.**

A third high priority research and development project regarding clean energy is that of coal gasification, which would enable us to convert our very large reserves of coal into the cleanest of fossil fuels, namely, natural gas. In addition to this project, the Federal Government is giving continuing support to other research and development efforts, including controlled thermonuclear fusion, coal liquefaction, magnetohydrodynamic power cycles and use of solar energy. **Because of our rapidly growing energy needs, we believe that these are all feasible avenues of approach and worthy of Federal support, so that the partnership of Government and industry can continue in working to meet our Nation's energy needs.** As the President said in his energy message last June, "the key to meeting our twin goals of supplying adequate energy and protecting the environment in the decades ahead will be a balanced and imaginative research and development program."

In addition to research and development efforts, there are, of course, other ways of increasing our clean energy supplies. **We support the Administration's program aimed at making the energy resources on certain Federal lands available for our needs in an environmentally acceptable way.** This comprehensive program includes outer continental shelf leasing, development of our oil, shale and geothermal energy resources and location and development of additional natural gas fields. Supplementing these efforts are the programs providing energy source imports from such secure areas as Canada, the provision of a satisfactory long-term supply of nuclear fuels and, finally, and perhaps most importantly, the development of conservation measures in the use of the energy produced.

We applaud President Nixon's emphasis on the importance of having each individual American aware of the cost of the energy which he uses. As the President points out, we use energy so lavishly today in

part because its price does not reflect its full social cost. Consumers of energy do not pay the environmental costs of energy production, although these costs are a real part of production costs. To help meet one aspect of this problem, the Department of Housing and Urban Development recently issued new standards for insulation in Federally insured houses. These standards, applicable to single family structures, require insulation to reduce maximum permissible heat loss by about one-third for a typical home. In his message the President estimated that **the fuel savings resulting every year from the application of these new standards will, on the average, equal the cost of the additional required insulation.** The Secretary of Housing and Urban Development is now revising standards applicable to Federally insured apartments and other multi-family structures. These standards will reduce maximum permissible heat loss by about 40%. Savings in fuel costs over a five year period will on the average total more than the increased construction costs which will be required by the new standards.

On the industrial side, and along the line of making the cost of energy reflect more accurately its true social cost, the President proposed last February the establishment of a sulphur oxides emissions charge. This charge would build the cost of sulphur oxide pollution into the price of energy and would additionally provide strong incentives to reduce these emissions.

The need for a coherent overall governmental program regarding energy is apparent when we consider that the energy industries account for approximately one-fifth of all of our investment in new plant and equipment. Aside from the environmental and social aspects inherent in our present energy problems, the pure economic importance of the energy industry is very great. In the past many Federal governmental programs dealing with energy have been fragmented, with responsibility for various aspects of these programs being lodged in a number of agencies throughout the Federal Government. **We believe that President Nixon's proposal that all important Federal energy source development programs be consolidated in the proposed Department of Natural Resources is a sound one. Under such consolidation, the responsibility for the overall Federal energy effort would be centralized. This centralization would help insure that our total energy resources would be utilized as effectively as possible. If the extensive Federal executive branch reorganization proposed by the President is not to be acted upon during 1972, we believe that serious consideration should be given immediately to centralizing Federal energy efforts in an Office of Energy Policy in the executive branch.**

ENVIRONMENTAL QUALITY

In recent years the level of environmental consciousness in the United States has risen rapidly. Demands for increased environmental protection and restoration have accompanied this rise. **In our opinion, the Federal Government under President Nixon's leadership has led the way in proposing and implementing enlightened environmental policies and programs. During 1971 the Administration proposed environmental programs in areas as diverse as regulation of toxic substances, noise control, preservation of historic buildings, power plant siting and control of ocean dumping. Throughout 1971 these**

measures were the subject of Congressional consideration and hearings. We believe it is appropriate that the Congress take more cooperative action in 1972. These programs are essential if we are to implement a comprehensive plan for improving the environment. At the same time, we believe that the Congress must also lay the groundwork in 1972, through hearings and other Congressional action, for the enactment of enabling legislation in the areas outlined by the President in his environmental message to the Congress last month.

In his February 1972 message the President made a number of proposals which complement some of the initiatives which he presented to the Congress more than a year ago. These programs include action in the area of pollution control, by means of a Toxic Wastes Disposal Control Act, control of sediment from construction activities, an emissions charge on sulphur oxides, and certain clean energy research and conservation approaches; in the area of technology, through advanced pest management, and noise control and air pollution research; in improving land use and protecting our wilderness areas, by means of wetlands protection, limitation of use of poisons on public land, creation of new Wilderness Areas, etc. There are also important proposals for greater international cooperation with regard to environmental matters. These proposals include establishment of a United Nations Fund for the Environment and greater measures to control marine pollution.

A number of these initiatives by the President have already been effected through Executive Order under existing legislative authority. A number of others require cooperative legislative action by the Congress. Because of the large number of programs and their comprehensive nature, it is not possible here to discuss in detail the President's 1971 and 1972 environmental initiatives. **What we do wish to emphasize most strongly is the need for Congressional action on these proposals as promptly as is consistent with the orderly legislative process. As we have said, the Congress has been investigating the 1971 proposals for more than a year, in most cases. We believe that 1972 is an appropriate year for action.**

SURFACE FREIGHT TRANSPORTATION

In many respects our nation's transportation system has been overregulated for many years. The history of this regulation and of the social and economic costs which it entails are discussed in some detail in both the 1971 and 1972 Economic Reports of the President and in our views on the 1971 Report. In 1971 the Administration proposed to relax the regulation of one of the most important parts of our transportation system, namely, surface freight transportation.

We believe that modernization of regulations would make a positive contribution towards creating more competitive conditions in surface freight transportation. As we said in our views last year, in the trucking industry numerous regulations contribute to filling our highways with empty and partially loaded trucks, causing great economic waste. These regulations include the regulation of backhauls, restrictions on commodities hauled, restrictions against mixing regulated and non-regulated commodities and restrictions on service to points intermediate to points to which service is certified. These technical restrictions have resulted in a situation in which only slightly more than half

of all regulated trucks have full loads in both directions, resulting in low productivity. Regulation of both minimum and maximum freight rates charged by common carriers, including establishment of rates based upon the value of the transported freight ("value of service") instead of in relation to the cost of providing service, has also been very wasteful, preventing free market forces from reducing or increasing prices according to relative supply and demand.

We believe that allowing common carriers greater rate flexibility cannot fail to have favorable effects upon competitive conditions in, and the health of, the surface freight transportation industry. We also note with interest the recent proposals by the Department of Transportation to the Civil Aeronautics Board regarding domestic air fares. We believe that greater flexibility is also indicated for domestic air transportation.

HEALTH AND MEDICAL CARE

In many ways the United States does not measure up to the rest of the world in the quality of its health services. We have fewer physicians in proportion to our population than Argentina or Germany. Our infant mortality rate exceeds that of Sweden, the United Kingdom and Japan. Perhaps more disturbing, our average life expectancy is less than the average of the 22 Organization for Economic Cooperation and Development countries.³

Persons concerned with public health problems point out disturbing trends which should be dealt with in formulating health policy. Our sheer affluence has generated increasing amounts of wastes and pollutants whose health implications are only gradually being discovered. Our ability and propensity to travel has evidently outpaced our ability to manufacture safer highways and motor vehicles, as the 25 percent rise in the auto accident death rate from 1960 to 1969 attests. The marked decline in the number of general practitioners, who have traditionally provided basic health care for American families, has created a seriously uneven distribution of medical services, especially in rural areas. Although the national average is one physician to every 630 persons, the rate in one third of all the counties in America is one to every 1,800 persons. And in more than 130 counties, covering more than eight percent of our land area, there are no physicians. Finally, we cannot ignore the sharp upward trends in related statistics which bear upon our national health; the rate of outpatient psychiatric services and the rate of drug addiction are examples.

The cost as well as the quality of medical care is also a subject which merits national concern. During the decade of the 1960's the medical component of the Consumer Price Index (CPI) rose at a faster rate than any other. Between 1967 and 1970, a time when inflationary pressures were more severe, the cost of medical care services rose 24.2 percent, compared with the overall CPI increase of 16.3 percent.

³ Congressman Blackburn is very concerned about the accuracy and implications of the comments in this section on the quality of health and medical care in the United States. Regarding physicians, Mr. Blackburn points out that it is difficult to get a consistent measure of physicians per capita across countries. By most measures the U.S. does very well, and in quality our doctors are probably tops. Lack of doctors hardly seems to be our problem; misuse of doctors for tasks that can be handled by midwives, nurses, etc. may be a problem.

These statistics illustrate a point which has important economic as well as public health consequences: we simply cannot assume that rising incomes and per-capita wealth will necessarily produce superior health services for all Americans. As yet we have not devised an efficient health services delivery system which would ensure quality medical care for all persons. Also, we have fallen short in exploring fully the effects which our modern life has on our national health.

Several trends and developments suggest in part the future course of medical care in the United States. As the Economic Report of the President points out, public financing of medical services has become an increasingly large part of total outlays. Twenty-six percent of total outlays were so financed in fiscal year 1966, compared with 37.9 percent in fiscal year 1971. There is also a trend from direct private payments to payments by third parties or by health insurance plans. User payments have declined from 86 percent of total private payments in 1950 to 58 percent in 1971.

Government efforts to control pollution, crack down on unsafe products and improve the state of highway safety have a direct bearing on national health. We commend the Administration for recognizing that a comprehensive approach to public health demands improvements in such areas as well as in the purely medical fields.

Other Administration initiatives which deserve mention are the commitment to cancer research, which resulted in the National Cancer Act of 1971, and the vastly increased efforts to find a cure for sickle cell anemia.

This description of developments in national health forms the basis for recommendations which we believe should become guidelines for the economic aspects of health policy.

We affirm that a national health system must assure access to quality medical care at fair cost for all Americans. One problem which our health statistics point out is the wide disparity in the health of persons in low and high income areas.⁴ Access will in some cases require insurance plans so as to enable users to pay the high costs of medical services; in other cases it will require the construction or reorganization of medical care delivery systems so that physical access to care will be facilitated.

We believe the control or reduction of medical costs must be a priority task for Government in the years ahead. Testimony before this Committee in recent years has pointed out that in some respects public health planning has proceeded oblivious to the economic consequences, and that as a result there has been a serious mismatch of demand and supply. Also, sophisticated equipment developed as a result of the strides being made in medical research has made the cost of even routine medical service more expensive. In part, a solution to the problem of medical costs lies in a judicious use of selective Federal subsidies—to medical training institutions and research projects, for example. In part, also, an attack on rising medical costs must be made by developing new approaches to the organization of delivery systems. We commend the President for recognizing this problem fully in his national health policy message last year.

⁴ Congressman Blackburn questions the accuracy of this sentence. The very poorest states do seem to have worse health but beyond that the relation may go the other way. Some of the richest states have worse health than the middling states (the mid-west has the best).

The effectiveness of national health programs can only be determined accurately if we have the statistics to reflect the inputs and outputs of medical care. At the present time we know too little about the effects which dollar expenditures for drug prevention can have on the rates of addiction, or which spending for air pollution control can have on respiratory and other diseases caused by air pollution. Only by knowing the opportunity costs of certain types of health expenditures can we improve the quality of health care with the scarce resources at our disposal. The Joint Economic Committee is particularly well suited to give this area the study it deserves.

V. AGRICULTURE AND RURAL DEVELOPMENT

A review of the economic situation of agriculture for 1971 discloses that the farmers of our nation continued to receive less than a fair share of the national net income.

It is vital for not only the Administration and the Congress to understand this economic fact of life, but for the consuming public to understand it as well.

If the family farmer is to remain the backbone of American agriculture—and we believe he should—this situation must improve. While the future of the nation's agriculture will be determined far more by what farmers do for themselves than by what government does for them, government programs will continue to be needed for some time into the future as a means of assuring a continued ample supply of quality food and fiber to meet our domestic and export requirements. Moreover, our system of "people's capitalism" implies a continued measure of *direct* government activity—rural development, pesticide control, marketing and quality regulation, credit assistance, and conservation, for example. And, *indirectly*, government action with respect to exports, imports, inflation, dock strikes and transportation will continue to affect the economic condition of our agricultural producers.

No segment of American industry has increased its productivity as dramatically as has agriculture. Unlike other areas of industry, however, the rewards of increased productivity have not been shared by those who have been responsible for such progress. This can go on only so long before risk capital, managerial skill, and labor will move elsewhere. And if this ever happens, the American consumer will pay a heavy price.

THE 1971 AGRICULTURAL ECONOMY

The agricultural sector of our economy experienced some of the same problems as the rest of the economy in 1971. However, the cyclical nature of farm prices showed a contrast to 1970, when grain prices generally rose as the year progressed and livestock prices declined. The reverse was true in 1971.

Realized gross farm income in 1971 was up \$2 billion from the previous high of 1970, setting a new record at \$58.6 billion. However, farm production expenses of \$42.9 billion in 1971 were also up \$2 billion over the previous year. Thus, the realized net income of \$15.7 billion for the farming industry was the same as in 1970.

Net farm income nationally rose sharply in the second half of 1971, and if this trend continues, projections show that realized net income for 1972 will exceed the 1971 level by \$1.5 to \$2 billion.

The nation had an estimated 2,876,000 operating farms during 1971, a 2% decline from the previous year. Based on this figure, average realized net income per farm was \$5,468 in 1971—\$94 more than in 1970 and \$31 more than the record set in 1969.

For people who live on farms, the share of their income which is derived from nonfarm sources continued to increase slightly in 1971 (from 47.7% to 48.2%). The Secretary of Agriculture testified before our Committee that nonfarm income is a greater proportion of total income for farm operations which sell a low volume of farm products, although nonfarm income is not limited to these smaller farms. Operator families on many of the larger farms also receive substantial amounts of income from nonfarm sources.

In 1971, aggregate personal income of the farm population totaled \$28 billion, up \$500 million over 1970. Of this, \$14.5 billion was from farm sources and \$13.5 from nonfarm sources. On a per capita basis, disposable personal income (after taxes) of the farm population reached a new high of \$2,692 in 1971, about \$150 higher than in 1970. The per capita disposable income of nonfarm people, however, made an even greater rise than that experienced by farm people, to a level of \$3,623. Thus the ratio of average disposable income of farm people to nonfarm people was about 74 percent in 1971, slightly below the 75 percent of the previous year. This is still a marked improvement over the 55 percent of 1960, however.

Looking at the agriculture balance sheet, farm assets increased \$16 billion in 1971 (a 5 percent rise), reaching a total of \$335 billion at the end of the year. The value of farm real estate (up 4 percent) accounted for over half the rise in total assets. Total farm indebtedness (including Commodity Credit Corporation loans) continued its upward climb to a total of \$65.5 billion, an increase of \$4.4 billion. This was up 7 percent from 1970, almost double the 4 percent rise from 1969 to 1970 but still under the average of 9 percent per year during the preceding decade. Debt per farm, however, rose from \$20,896 in 1970 to \$22,775 in 1971, an increase of 9 percent, substantially above the 5 percent increase in 1970.

Although interest rates were down, particularly in the latter part of 1971, farmers continued to be reluctant to make long-term debt commitments. Nationally, the farm debt to asset ratio has increased steadily over the past 20 years, from 9.4 percent in 1950 to 18.8 percent in 1970 and 19.5 percent at the beginning of 1972. Since as many as a third of the farms have no debt at all, the debt to asset ratio of indebted farms would be substantially higher.

The larger increase in assets over liabilities resulted in an \$11.7 billion, or 4.6 percent, increase in proprietors' equities. The 1970 increase was only 2.6 percent.

When proprietors' equities are compared with total realized net income, it can be seen that the farmer's return of his net farm equity was slightly less than 6 percent. Thus, the average farmer, in effect, received little or no return on his labor and managerial skills—another clear indication that farmers have not shared fairly in the national net income.

THE COST-PRICE SQUEEZE

The cost price squeeze continued to plague the nation's farmers in 1971. While the index of prices received by farmers was 112 percent of the 1967 base (compared to 110 percent in 1970), the index of prices paid stood at 120 percent of the 1967 base (up from 114 percent in 1970). The result was a decline in the parity ratio from 72 in 1970 to 70 for 1971 as a whole.

Several new developments in the general economy did favorably affect farm costs in 1971. The wage-price freeze from mid-August to mid-November had a dampening effect on the prices of most inputs of nonfarm origin. Prices of inputs of farm origin were not directly affected; neither were interest rates, which generally did not increase from mid-August levels. Phase II of the President's program to reduce inflation also set limits on the amount that prices of nonfarm inputs can rise.

A principal factor in the increase in farm production expenses in 1971 was higher prices for purchased feed. Expenditures for purchased feed rose 7 percent over the 1970 level, compared to an average annual change of slightly less than 3 percent during the 1966-70 period. Corn prices were higher in early 1971 because blight infestation and dry weather reduced yields and supply in 1970. Expenditures for fertilizer, insurance, seed, and pesticides all rose more than the average annual change from 1966-1970.

The Secretary of Agriculture testified before our Committee that a somewhat smaller increase in farm production expenses can be expected in 1972. Plentiful supplies of feed grains and hay will hold down expenditures for purchased feed by keeping unit prices at or below 1971 levels. Also Phase II should slow the rise in the price of nonfarm origin production items.

As already noted, 1971 seemed to be the reverse of 1970 in grain and livestock price performance. In 1970, grain prices generally rose as the year progressed, due primarily to a short corn crop brought on by blight and drought damage; and livestock prices, particularly hogs, generally declined. In 1971 because of a smaller land diversion in view of threatened corn blight, which did not materialize, along with a favorable growing season, the corn crop reached 5,540 million bushels—about 35 percent larger than the short crop of 1970. Sorghum grain and barley crops were also up substantially, and wheat production for 1971 was a record 1,640 million bushels—20 percent above a year earlier. As a result, U.S. average corn prices, which were at a level of \$1.43 per bushel (U.S. average) last June fell to a seasonal low of 97¢ per bushel in November.

On the other hand, hog farmers cut back on farrowing, with the December 1971-May 1972 pig crop estimated to be 9 percent smaller than a year earlier. After reaching a low of around \$15 per hundredweight (average at seven major markets) in December 1970, prices of slaughter hogs have slowly moved upward, averaging \$18.50 per hundredweight for 1971 as a whole, still \$3.50 below the average for all of 1970. However, by January of this year prices had reached nearly \$28.00.

Cattle prices also strengthened during 1971. Choice steers at Omaha rose from about \$29 per hundredweight in January to nearly \$34.50 in December, averaging \$32.50 for the year—\$2 above the average for 1970. In early February of this year, choice steers at Omaha were approaching the \$37 level, one which had not been reached for 20 years.

The strong livestock prices, particularly for cattle, have caused some consumers, who are not familiar with the need for such prices to offset the low prices of previous years, to call for raising meat import quotas or putting raw agricultural commodities under price controls.

It is interesting to note that when producers' prices are low, no one suggests that the farmer's cost of production should also go down. Of course, the farmer's costs of production do not go down when his prices

go down, and he needs cyclical, strong prices to offset low prices so he can stay in business. Moreover, increasing meat import quotas or establishing a price ceiling on agricultural products would not significantly help lower consumer prices.¹ A recent study published by the Department of Agriculture for the years 1947-1949 to 1970 ("Farm-Retail Spreads for Food Products") demonstrates that the major increase in consumer prices comes from the spread between the wholesale price received by the packer and the retail price paid—rather than the spread between the farmer's price and the wholesale price. Since 1967 (the base period for many government statistics), the price of food has risen less than most of the other main components of the Consumer Price Index. In 1971 the retail food price index rose 3 percent, a considerably smaller rise than the 5½ percent increase in retail food prices for 1970 and smaller than the 4.3 percent increase in retail prices represented by the entire Consumer Price Index. On the other hand, the index of prices received by farmers for all livestock and livestock products decreased almost 2 percent from 1970 to 1971. The American housewife in 1971 bought her quality food with only 16 percent (compared to 16.5 percent in 1970) of her family's take-home income, the lowest percentage ever, in any country.

Farmers received only 38 cents of the dollar consumers spent for market basket foods in 1971, compared to 39 cents in 1970 and 52 cents in 1947. In the case of meat products, particularly, the above-cited study reveals that, generally, retail prices have been more stable than corresponding farm prices. Thus, when farm prices increased, retailers generally did not increase their retail prices as much; and when farm prices declined, retail prices did not decline as much. Some of us have requested the Department of Agriculture from time to time to put pressure on retailers to try to correlate their retail price movements more closely with farm price declines, and Department officials have done so—with some, but not enough, success. Consumer groups should join in this effort.

From all of this, the conclusion is inescapable: consumer price increases in recent years have largely been the result of increased costs after the product has left the farmer's hands and before it is sold to the consumer. We believe that the consumers of this country should be made aware of this and that substantially increasing meat import quotas or placing a ceiling on the prices of raw agricultural products would not only fail to reduce consumer prices significantly, but would be unfair to producers who have not been sharing fairly in the national net income.

¹ Senators Javits and Percy, and Representatives Widnall, Conable, Brown, and Blackburn, state, "We feel that the wording of this section as it relates to meat imports does not provide a fully equitable balance between the interest of the consumer and those of the producer. We note that the Director of the Cost of Living Council in a public statement made February 12 recognized the connection between the meat import quota system and the significantly higher prices the American consumer has been paying for beef in recent months. At that time, Director Rumsfeld announced that the Administration might ease quota restrictions to allow more imported meat to enter the country as a means of slowing the rising spiral of retail meat prices. Mr. Rumsfeld asserted further that higher import levels of manufactured meat would also exert downward pressure on prices of steaks and other cuts of meat. On March 8, President Nixon issued an Executive Order that suspended certain provisions of the Meat Import Act of 1964 to allow an increase in meat imports subject to the quota provisions of the Act. We hope that these measures of the Administration will indeed curb the rising spiral of retail beef prices."

THE AGRICULTURE ACT OF 1970

No economic report on agriculture would be complete without a discussion of the Agriculture Act of 1970—one of the major economic forces affecting the agriculture sector of the economy. That Act signaled a changing trend in national farm policy toward greater flexibility and a wider range of decision-making for farmers in their farming operations. And it should be noted that the minority members of this Committee had consistently recommended that farm programs, to follow the 1965 Act, should move toward a strong market economy rather than a government payment and regulated economy and that they should achieve a fair share of the national net income for our farm population.

The greater flexibility and wider range of decision-making provided for in the 1970 Act was 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. But, as the unexpected overproduction of 1971 crop corn demonstrated, good intentions can go astray. Nevertheless, few believe that the 1970 Act should be condemned on the basis of a single year's experience. Surveys show that a majority of farmers welcome the freedom to grow the crops they choose to grow, and it would seem that demands for return to the rigid bases and allotments established under previous farm legislation are premature.

A year ago, because of the experience with corn blight in 1970 and the threat of repetition of the disease in 1971, there was widespread fear of a short crop of corn, with resultant high consumer prices, particularly for meat. This fear was clearly revealed in the grain futures market. Because of these fears and because the Department of Agriculture determined that, if it should err, error should be on the side of abundance, rather than underproduction, a required set aside of only 20 percent of the feed grain base was prescribed for farmers volunteering to enter the program. A combination of little blight damage and very favorable growing conditions resulted in a record national yield per acre of 86.8 bushels and a total corn crop of 5.5 billion bushels, accompanied by abnormally low corn prices. These prices were further depressed for many weeks because of dock strikes which prevented the movement of grain to export terminals.

We do not believe that, under the circumstances, either the government or the farmers should be blamed for guessing wrong. The situation could have been worse for the nation, as a whole, if the guess had been the other way and we had had two short crops in a row with not enough food and feed grains to meet our domestic and export needs. The questions now are how to prevent a recurrence of overproduction, reduce the present surplus, and help the corn producers through this period of low prices.

The Department of Agriculture's feed grains program for 1972 is a step in the right direction and is designed to reduce production sufficiently to cause a reduction in carryover stocks. The target is a feed grain set aside of at least 38 million acres, more than double the 18 plus million acres set aside in 1971. In order to achieve this, the Department early this year announced an additional option under which producers can earn an increased rate of payment on additional set aside acres.

Changes announced by the Department of Agriculture in the 1972 feed grains and wheat programs will require higher payments to participating farmers, and such additional income, coupled with stronger grain prices expected to result from reduced production and a reduced amount of grain not under seal, is expected to improve the net income picture for 1972, as discussed earlier.

We recognize that the Department's activities in responding to the 1971 surplus production have not satisfied everyone. There continue to be those who favor high price supports and rigid production controls. Not only would this reverse the policy determined by the Congress with passage of the Agriculture Act of 1970, but it would place our grain exports in jeopardy. If the support price were so high as to not meet competition for foreign markets, we would have to subsidize our exports—and this would be in violation of the General Agreement on Tariffs and Trade. We note that the Senate Agriculture Committee rejected a proposal calling for a 25% increase in price supports, which would have cost the government \$2.5 billion over the proposed budget. The Committee also rejected a proposal by Senator Miller calling for a 10% increase in price supports, which would have cost the government \$1 billion over the budget. The Administration opposed any increase in price supports, but fairness demands that we call attention to the fact that the Department of Agriculture has taken some actions to relieve the low market price situation: extension of period for keeping 1969 through 1971 crops under loan until May of 1973 (which has greatly reduced the amounts of so-called "free-grain" for marketing); distress loans for ear corn stored on the ground or in temporary facilities; and a greatly-expanded facility loan program to help farmers build on-farm storage facilities. Also, the end of the dock strikes restored the 9¢ to 10¢ loss in grain prices which had occurred because of closure of ports for export shipments.

The present corn surplus situation is similar to that which existed during the crop year 1967–1968 when the excess 1967 crop production brought prices to a low level. For example, the average mid-month prices (all grades) received by Iowa farmers for November and December of 1967 were 95¢ and 99¢ per bushel, respectively; and for all of 1968 the average was \$1.01 per bushel. Democrats obviously are in no position to criticize this Administration on the basis of their record of performance.

AGRICULTURAL TRADE

Agricultural exports during 1970 reversed a downward trend of the previous three years and set a record of \$7.3 billion. In 1971 a new record was set, as agricultural exports reached a new high of \$7.7 billion, 6 percent above 1970. This gain raised the agricultural trade balance to \$1.9 billion from the \$1.5 billion the previous year as the inflow of dollars from farm product sales further exceeded the outflow from farm product purchases. The picture would have been even brighter had it not been for the dock strikes.

Increases for cotton (up 57 percent over 1970), soybeans (up 8 percent), soybean meal (up 17 percent), inedible tallow (up 20 percent), dairy products (up 37 percent), meats and meat products (up 15 percent), and hides and skins (up 6 percent) were mainly responsible for the new record. Partly offsetting these gains were reductions in feed

grains (down 9 percent), wheat (down 2 percent), rice (down 18 percent), poultry products (down 3 percent), and tobacco (down 4 percent). The dock strikes were responsible for the decline in wheat and feed grains exports.

The 1971 increase in dollar exports arose primarily from higher prices received as a result of larger foreign demand and limited supplies of major commodities such as soybeans, soybean meal, cotton, and inedible tallow. The overall volume of agricultural exports was relatively unchanged from 1970.

Agricultural imports for 1971 increased one percent to \$5.8 billion, just slightly over the record of \$5.77 billion set in 1970. Much of the increase was due to higher prices rather than an increase in volume. Two of the most important items as far as American farmers are concerned—dairy products and meat and meat products—both declined on a volume basis from 1970. Imports of dairy products in 1971 were equivalent (fat solids basis) to 1.3 billion pounds of milk, about a fourth less than in 1970. This decline was due primarily to new dairy import quotas in 1971 and to reduced world supplies of dairy products. Imports of red meat totaled 2,317 million pounds (carcass weight equivalent) in 1971, 3 percent less than in 1970, when they were at a record high of 2,387 million pounds. This decline was due primarily to the President's imposition of the 10 percent import surcharge at the time of the wage-price freeze.

The following tables illustrate the trends in agricultural exports and imports over the past few years.

TABLE I.—AGRICULTURAL IMPORTS, CALENDAR YEARS 1964-71

Commodity	[In millions of dollars]							
	1964	1965	1966	1967	1968	1969	1970	1971
Supplementary:								
Animals, live.....	56	117	118	80	113	119	157	138
Dairy products.....	62	73	118	115	101	101	125	114
Meat and meat products..	483	525	619	664	764	861	1,010	1,047
Sugar, cane.....	458	441	502	587	641	638	725	763
Tobacco, unmanu- factured.....	89	130	127	129	142	128	139	152
Wool, apparel.....	115	157	157	102	110	85	59	31
Other.....	675	627	986	1,019	1,167	1,157	1,393	1,445
Total.....	1,938	2,070	2,627	2,696	3,038	3,089	3,608	3,690
Complementary:								
Coffee (green, roasted)...	1,027	1,064	1,069	964	1,144	896	1,165	1,177
Cocoa beans.....	131	139	122	147	136	168	201	181
Rubber, crude natural....	201	182	177	170	188	275	231	211
Wool, carpet.....	90	71	72	38	48	43	31	35
Other.....	357	384	424	437	470	486	533	533
Total.....	1,806	1,840	1,864	1,756	1,986	1,868	2,161	2,137
Grand total.....	3,744	3,910	4,491	4,452	5,024	4,957	5,770	5,826

Source: Economic Research Service, U.S. Department of Agriculture. May not add due to rounding.

TABLE II.—AGRICULTURAL EXPORTS, CALENDAR YEARS 1964-71

[In millions of dollars]

Commodity	1964	1965	1966	1967	1968	1969	1970	1971
Cotton, excluding linters.....	682	486	432	464	459	280	372	584
Dairy products.....	224	196	126	121	143	121	127	174
Feed grains, excluding products.....	855	1,135	1,334	1,054	926	860	1,064	971
Fruits and preparations.....	279	313	315	310	277	323	334	351
Soybeans.....	567	650	767	772	810	822	1,228	1,325
Tobacco, unmanufactured.....	413	383	482	468	524	540	517	497
Vegetables and preparations.....	158	155	176	164	173	192	206	212
Wheat and flour.....	1,532	1,183	1,534	1,206	1,100	830	1,111	1,089
Other.....	1,638	1,728	1,715	1,776	1,816	1,968	2,300	2,492
Total.....	6,348	6,229	6,881	6,365	6,228	5,936	7,259	7,695

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

TABLE III.—SHARE OF U.S. AGRICULTURAL PRODUCTION EXPORTED, FISCAL YEARS 1964-71

[In percent]

Commodity	1964	1965	1966	1967	1968	1969	1970	1971
Wheat, including flour equivalent.....	75	55	65	56	49	34	41	53
Rice, rough basis.....	62	54	55	64	64	48	60	62
Nonfat dry milk.....	62	44	37	24	20	25	24	26
Dried edible beans.....	49	17	17	18	16	17	21	20
Tallow.....	44	40	37	40	38	38	36	41
Soybeans ¹	41	48	43	39	40	38	50	53
Hops.....	41	43	42	40	36	39	30	32
Rye grain.....	34	6	11	16	12	5	2	9
Cotton.....	32	30	20	48	55	26	29	36
Dried prunes.....	30	27	37	35	28	29	31	20
Lard.....	28	18	9	9	9	10	16	20
Dried whole milk.....	28	17	21	16	16	23	22	18
Tobacco, farm sales weight.....	26	25	29	38	32	38	37	35
Cottonseed ²	23	32	19	6	5	7	32	23
Raisins.....	21	25	23	24	38	27	28	39
Dried edible peas.....	20	60	65	82	74	84	70	79
Grain sorghums.....	17	24	36	39	23	14	16	24
Barley, grain.....	17	14	19	11	8	3	4	18
Flaxseed.....	11	27	15	32	25	36	16	11
Corn, grain.....	11	15	17	12	12	12	13	12
Cattle hides.....	45	56	41	41	36	42	45	44
Lemons and limes.....	9	17	21	19	18	19	21	24
Variety meats.....	9	10	10	10	9	10	10	11
Almonds.....	16	12	16	13	15	12	23	25

¹ Includes bean equivalent of soybean oil for export.² Includes seed equivalent of cottonseed oil for export.

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

The importance to the American farmer of our agricultural export markets cannot be overemphasized. Exports take the production of one out of four cropland acres. In the last fiscal year, exports took more than half of all the rice, wheat and soybeans sold by U.S. farmers. This is an enviable record, but we believe that we can do better. As was pointed out in our Minority Views last year, this will require maintaining and expanding our present export markets, keeping a steady flow of exports uninterrupted by domestic labor disputes, and carrying out our trade policies in such a manner as not to invite retaliation from our foreign customers.

We have commented in previous minority views on the Common Agricultural Policy (CAP) of the European Economic Community (EEC) and the implications for American agriculture of the expansion of that market. The CAP involves a number of complicated governmental control schemes, including minimum import prices and variable import levies designed to bring prices of imported commodities up to the high EEC domestic support prices. Export subsidies are paid so that surpluses can be dumped on world markets at reduced prices. Expansion of the CAP to the United Kingdom, Ireland, Denmark, and Norway, which signed a Treaty of Accession with the EEC on January 22, 1972, could have an adverse impact on the total market for U.S. agricultural products.

The enlarged EEC will be the world's largest trading block. Its importance for U.S. exports is shown by the fact that the "Ten" accounted for 27 percent of total U.S. exports and 29 percent of U.S. agricultural exports in 1970. Still more importantly, they accounted for 34 percent of U.S. commercial farm exports in 1970. Also, although the EEC has increased its purchases of U.S. soybeans and bean products (which are not subject to the variable levies) at an annual rate of 10 percent per year since 1955-56, U.S. agricultural exports which *are* subject to the variable levy have declined since the mid 1960's. (U.S. exports of these same products to the EEC had been increasing in the period from the mid 1950's to the mid 1960's.)

As a result of the negotiations last year on realignment of international currencies, the U.S. and the EEC in February of this year announced an agreement to initiate and actively support multi-lateral and comprehensive negotiations within the framework of GATT, beginning in 1973, on international economic relations, including all elements of trade. Several short-term concessions were made by the EEC, including the addition of an extra amount of wheat to its planned stockpiles, a reduction in tariffs on oranges and grapefruit, and an agreement to consult with the U.S. while developing a common tax policy on tobacco products which will not discriminate against U.S. tobacco. However, of even greater significance to U.S. agriculture is the commitment to long-term negotiations which will cover agricultural as well as industrial trade. Such negotiations will be taking place while the EEC is in the process of enlargement, and they will offer an opportunity to minimize any adverse effects on our trade resulting from expansion of the EEC. At the same time, such negotiations could assist world trade generally through further reductions in trade barriers.

We commend the Administration for reaching this historic agreement. We have been calling for trade negotiations which will deal with agricultural as well as nonagricultural trade barriers for some time now, and we urge the Administration to negotiate vigorously at these upcoming sessions to insure improved market access for our agricultural commodities. In view of the importance of agricultural trade to the U.S., tangible results in trade terms for these products are essential to any successful negotiations.

The following tables indicate the trends in agricultural trade with our major trading partners.

TABLE IV.—U.S. IMPORTS, CALENDAR YEARS 1964-71

[Dollar amounts in millions]

Year and area	Total imports	Agricultural imports	Agricultural imports as percent of total imports	Year and area	Total imports	Agricultural imports	Agricultural imports as percent of total imports
1964	\$18,600	\$4,082	22	FROM UNITED KINGDOM—Con.			
1965	21,283	4,087	19	1969	2,129	35	2
1966	25,360	4,491	18	1970	2,186	51	2
1967	26,733	4,452	17	1971	2,461	55	2
1968	33,066	5,024	15	FROM JAPAN			
1969	35,863	4,957	14	1964	1,763	40	2
1970	39,756	5,770	15	1965	2,401	37	2
1971	45,546	5,826	13	1966	2,948	37	1
FROM EEC				1967	2,994	32	1
1964	2,831	258	9	1968	4,044	37	1
1965	3,316	270	8	1969	4,849	37	1
1966	4,098	306	7	1970	5,852	38	1
1967	4,441	331	7	1971	7,244	46	1
1968	5,849	362	6	FROM CANADA			
1969	5,787	363	6	1964	4,227	176	4
1970	6,574	436	7	1965	4,813	234	5
1971	7,530	423	6	1966	6,106	240	4
FROM UNITED KINGDOM				1967	7,099	201	3
1964	1,132	23	2	1968	8,918	226	3
1965	1,403	24	2	1969	10,345	244	2
1966	1,761	30	2	1970	11,025	323	3
1967	1,710	28	2	1971	12,723	314	2
1968	2,016	32	2				

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

TABLE V.—U.S. EXPORTS, CALENDAR YEARS 1964-71

[Dollar amounts in millions]

Year and area	Total exports ¹	Agricultural exports	Agricultural exports as percent of total exports	Year and area	Total exports ¹	Agricultural exports	Agricultural exports as percent of total exports
1964	\$26,156	\$6,348	24	TO UNITED KINGDOM—			
1965	27,135	6,229	23	Continued			
1966	29,884	6,881	23	1969	2,278	361	16
1967	31,142	6,380	20	1970	2,478	411	17
1968	34,199	6,228	18	1971	2,311	438	19
1969	37,462	5,936	16	TO JAPAN			
1970	42,590	7,259	17	1964	1,894	720	38
1971 ²	43,497	7,695	18	1965	2,042	876	43
TO EEC				1966	2,312	942	41
1964	4,481	1,416	32	1967	2,665	864	32
1965	4,904	1,476	30	1968	2,924	933	32
1966	5,264	1,564	30	1969	3,462	934	27
1967	5,582	1,460	26	1970	4,610	1,214	26
1968	5,994	1,367	23	1971	4,012	1,073	27
1969	6,875	1,269	18	TO CANADA			
1970	8,325	1,586	19	1964	4,653	3 615	13
1971	8,292	1,829	22	1965	5,486	4 620	11
TO UNITED KINGDOM				1966	6,487	5 626	10
1964	1,445	448	31	1967	7,053	6 556	8
1965	1,537	390	25	1968	7,936	7 595	7
1966	1,645	471	29	1969	8,956	8 710	8
1967	1,929	424	22	1970	8,806	8 826	9
1968	2,132	374	18	1971	10,101	10 761	8

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.¹⁰ Includes \$163,000,000 in transit shipments.

Source: Economic Research Service, Department of Agriculture.

The Public Law 480 program continues to play an important role not only in our foreign policy but in our efforts to open up new markets for American products. Because of increased cereal production in developing countries and legislative restrictions on country eligibility, exports in 1971 remained at the previous year's level of about \$1 billion. Although exports under P.L. 480 did not help our balance of payments problem, they did mean a market outlet for \$1 billion worth of our farmers' crop production. While the program now accounts for only about 15 percent of our total agricultural exports, it is highly important for certain commodities. For example, in fiscal year 1971, P.L. 480 shipments accounted for more than a third of our total wheat exports, nearly a fourth of the cotton, half the rice, more than 40 percent of the soybean oil, and nearly 90 percent of the nonfat dry milk. Also, P.L. 480 has assisted in the development of some of our important cash agricultural markets, such as Japan. We believe that the program has been most useful and urge that it continue to be funded at or near present levels.

The Department of Agriculture also administers several commercial export assistance programs, including export payments and sale of commodities from CCC inventory at competitive world prices. The

latter program was used in connection with the sale of feed grains to the Soviet Union in November of 1971. We commend the Department for its initiative in the Russian grain sale and we encourage continued use of these programs to open potential new markets and maintain our present competitive position.

No matter how many new export markets are opened up or how large the existing markets are, if we cannot provide a continuous flow of exports, the American farmer will suffer because he is much more dependent on exports than the operators of most other businesses. U.S. farmers were seriously injured in 1971 by the work stoppages at the West Coast, Atlantic and Gulf ports of this country. The Secretary of Agriculture has estimated that the dock strikes at these ports reduced U.S. farm exports during the shutdowns by over \$700 million from year earlier levels.

Normally, the East and Gulf Coasts account for about two-thirds of our total agricultural exports. During the October–November 1971 period, these ports exported substantially less than half the agricultural products exported during the same period the previous year (\$400 million compared to \$917 million). The strike impact was especially severe in October on exports of soybeans and corn from Gulf Ports. Corn exports were down from \$67 million to \$9 million and soybeans were down from \$95 million to about \$16 million. It is estimated that the work stoppages depressed corn prices by 9 cents per bushel and soybean prices even more.

Diversionsary movements to open ports during the strike, anticipatory shipments off the East and Gulf Coasts before the strike, and heavier than normal shipments following the strike helped in reducing the losses. However, it is abundantly clear that many of the losses will be permanent, because some of our normal customers have shifted procurement to our competitors. Thus, the impact of these strikes will also be felt in lost sales for the future.

FARMER BARGAINING POWER

As shown by the statistics in the early part of this section, farmers, as a group, are not sharing fairly in the national net income. Federal farm programs are helpful in enabling farmers to achieve a more equitable share, but the 1971 experience clearly indicates that additional authority could be useful. We believe that improved bargaining power for farmers through their producer associations could be helpful in improving farm income in certain types of commodities. However, where the futures market sets the current price of commodities—as in the case of major grains—bargaining legislation would not seem to be appropriate.

While there may be honest disagreement over the way or ways to provide farmers the opportunity to achieve better income, everyone can agree that we must preserve the family commercial farm as the backbone of a healthy American agriculture. One of the best ways to do so is through an enlarged and strengthened farmer cooperative movement, which would lay a foundation for improved bargaining power. If we do not move in this direction, then indeed the large corporate farming enterprises could well take over and relegate the family commercial farm to a chapter in American history books.

The basic question involved in bargaining legislation is the proper role of the Federal government. However, it would be well to point out

that any improvement in bargaining power for farmers could be completely undercut by unsound fiscal, monetary, and foreign-trade policies of the federal government. When it comes to the marketing of farm commodities, we believe the proper role of the Federal government should include establishment of conditions which insure that our basic free market system will function with fairness to both consumers and producers. "Fairness" implies a balance of economic power. We do not believe the farmers of this nation wish to see a government-dominated market structure established as the vehicle for obtaining better prices for their production. Any such mechanism could well lead to the destruction of the present voluntary associations of producers.

RURAL DEVELOPMENT

Last year in our Minority Views we included, for the first time, a section dealing with rural development. We believe the increased interest in rural development is a recognition of the interdependence of urban and rural areas and the fact that many of the problems of the cities are an outgrowth of problems in rural America.

Despite variations in the character of rural settlement, rural areas share common problems associated with the provision of, and access to, adequate public and private services and employment under conditions of comparative sparsity of population. Such basic rural similarities and rural-urban differences show no sign of disappearing.

We believe it is imperative to implement a national policy of bringing about a more efficient and commonsense geographical distribution of our continually growing population and economic wealth. Although achieving such a goal of balanced economic and population growth will not be easy, we must move. This necessarily means the development of plans at levels close to the people, because the people concerned must believe in them if they are to be carried out.

We realize that there are a number of different legislative proposals pending before the Congress to strengthen and improve our rural areas. In considering these, we believe that there are basic principles which should guide our action. We must treat the problems of rural America as part of a general strategy for balanced growth. The flow of power to the federal government must be reversed and more of the decision-making power returned to State and local officials who are closest to the people. We must provide adequate resources and credit to attract greater private involvement in rural development. Finally, we must develop rural America in such a manner as to protect agriculture and the environment.

We applaud the Administration for the high priority it continues to give to rural development and hope that the Congress will give the Administration's proposals its close and active attention.

CONCLUSIONS AND RECOMMENDATIONS

1. The Administration, Congress and the consuming public should work together to understand and help solve the problems of the farm economy.

2. Adequate farm income is still a major concern for a large part of the farm sector. The average farmer receives an inadequate return for his investment, labor and managerial skills.

3. Inflation and low farm prices aggravate the cost-price squeeze. The Administration's economic policies have been helpful in holding down the costs of inputs of nonfarm origin, but more cooperation is needed from the Congress.

4. An abnormal increase in meat import quotas or placing a ceiling on prices of raw agricultural products would not get at the major cause of high consumer prices. The Department of Agriculture and consumer groups should put pressure on retailers to correlate their retail prices more closely with farm price declines. The spread between the prices farmers receive and the prices the consumer pays should be narrowed.

5. The Department of Agriculture should make absolutely sure that under the wheat and feed grain programs enough land is taken out of production to reduce production sufficiently to reduce surplus stocks.

6. Agricultural exports are of vital importance to U.S. farmers. The Administration should negotiate vigorously in future trade talks to achieve adequate concessions insuring market access for our agricultural commodities and minimizing the adverse effects of expansion of the EEC. We should formulate our own foreign trade policies to contribute to the expansion of world trade.

7. Action should be taken to prevent repetition of the terribly costly dock strikes which hindered the orderly flow of agricultural exports to foreign markets.

8. The P. L. 480 program should be continued at or near current levels. The Department of Agriculture should continue to use commercial export assistance programs to open potential new markets and maintain our present competitive position.

9. Improved bargaining power for farmers could be helpful in improving farm income in the case of certain commodities. Any mechanism to achieve such increased bargaining power should strengthen voluntary associations of producers and insure that our basic free market system will function with fairness to both consumers and producers.

10. Rural development is vital to both urban and rural people and to a balanced economic and population growth. Elements of a rural development program should include:

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

b. Increased credit and funding for programs designed to strengthen the public and private services of rural areas (e.g. water and sewer systems, health services, housing, transportation, and utilities) to provide a base for economic growth;

c. Awarding of federal contracts and establishment of federal installations in rural areas and communities;

d. Strengthened manpower training programs in rural areas;

e. Expanded and improved administrative organizations for rural area planning and development; and

f. Return to the States and local governments of a portion of the federal revenues to be used for rural development projects.

VI. THE UNITED STATES IN THE WORLD ECONOMY

1971 was a watershed year for the international economy. Pressures which had been gathering for more than a decade broke through the restraining influence of time-honored agreements to produce what some have called the end of the Bretton Woods system. In turn, the events which started on August 15 and led to the Smithsonian accord in December are but the first step in a series of adjustments which will substantially change the system of international exchange and payments as we know it today.

On August 15, as part of the New Economic Policy, the President announced the suspension of dollar-gold convertibility and the imposition of a temporary ten-percent import surcharge. These actions were designed to protect the dollar at a time when speculative pressures could have plunged the world into a major monetary crisis. During the autumn, negotiations among the Group of Ten countries resulted, on December 18, in an agreement on new exchange rates.

Under the terms of the so-called Smithsonian accord, the Group of Ten countries also agreed to broaden the band on either side of the new exchange rates to $2\frac{1}{4}$ percent, and to undertake discussions promptly on longer term reform of the international monetary system. The specific items slated for discussion were the role of gold and reserve currencies, SDR's, flexibility of exchange rates, measures to deal with movements of liquid capital, international liquidity and the proper division of responsibilities for defending stable exchange rates. As part of the exchange-rate package, the United States agreed to bring a dollar devaluation proposal to Congress, and to drop the ten-percent import surcharge and the "buy-American" provision of the investment tax credit.

In retrospect this break with the past seems only a logical step to protect America's interest in the face of an intractable balance-of-payments problem and the increasingly uncomfortable position of our creditor trading partners. Symbolic of our position was the fact that our balance of trade deteriorated sharply in 1971, posting the first annual deficit in this century. Nevertheless, it is easy to forget the resistance which had been built up during the Bretton Woods years to any major change in the system. Notwithstanding the practical impossibility in recent years of our pledge to exchange gold for officially-held dollars at \$35 per ounce, this pledge was repeated in one form or another by the last three administrations.

That the actions of August 15 were necessary—and that further reform is equally necessary—is abundantly clear. Balance-of-payments deficits over the course of more than two decades had become virtually impossible to control, despite the best intentions and efforts of Government to reverse the trend. There was a growing realization that the major cause behind this state of affairs was the fact that we had entered a new stage of international economic relationships based upon competition among equals rather than upon Marshall Plan-era

diplomacy. Perceptive analysts pointed out that we were using policies developed at a time when our international competitive superiority was considered axiomatic. Our attitudes toward the dollar, the gold-dollar link and our place in the international monetary system had followed from this premise.

The result was a long series of balance-of-payments deficits, and an accumulation of dollars in foreign hands that exceeded any estimate of our ability to make good on the pledge of dollar-gold convertibility.

In the first half of 1971, our balance-of-payments position deteriorated rapidly, notwithstanding the fact that price and cost trends among the Group of Ten countries implied an improved picture over the coming years. Our deficit in official reserve transactions reached more than \$22 billion on an annual basis during the first three months of 1971. Speculative funds added significantly to the burden of foreign central banks, which wished to prevent accumulations of official dollars on the one hand and to prevent major changes in exchange rates on the other. The accumulated strains on the monetary system became particularly severe in April and May, leading to currency floats by Germany and the Netherlands, par value changes by Austria and Switzerland, and a tightening of exchange controls by other major European countries.

It is to the Nixon Administration's credit that it refused to take refuge in antiquated doctrine, and instead recognized the realities of the international situation in taking the actions it did in August to December of 1971. By the same token, it is clear from the President's Economic Report that the Administration is maintaining a refreshingly open mind on the subject of further reform of the international monetary system.

INTERNATIONAL MONETARY REFORM

Until last August the most significant development in the Bretton Woods system had been the conclusion of the agreement on Special Drawing Rights (SDR's) in 1968. That agreement, which took the form of amendments to the International Monetary Fund charter, provided a mechanism for creating international liquidity adequate to meet the needs of world trade and intergovernmental transactions. In theory, it diminished the necessity for countries wishing to strengthen their reserve position to do so at the expense of other countries. The SDR facility also provoked forward-looking thinkers to encourage the use of reserve creation for the direct benefit of developing countries, for whom the lack of foreign exchange reserves is an important bar to a higher standard of living.

In practice, the SDR facility has proven technically workable. Transactions involving SDR's among IMF members have totaled an equivalent of \$2.3 billion since the facility was made operational, in January 1970. Although there has been some discussion in the United States whether the level of SDR creation was sufficient—or excessive, as some other countries have implied—no country has blamed SDR's for the events leading up to August 15 or declared that we should do away with SDR's in the future. Economists generally agree that the facility has blunted the natural tendency of countries to pursue reserve policies by means of international payments restrictions and balance-of-payments credits (e.g., swaps, IMF drawings). There is similar

agreement that SDR allocations have made reserves available to many countries which have not attracted short-term capital.

However, the limitations of the SDR facility were also demonstrated during 1971. We discovered that the facility was inadequate to the task of controlling the volume of international reserves. We also discovered that the distribution of SDR's did not always correspond to the need of recipient countries for increased reserves; the major changes in reserves during 1971 were in several cases the result of short-term capital movements rather than deliberate reserve creation. It is clear, therefore, that the SDR facility must be supplemented by effective measures to control excessively large international flows of capital.¹

Perhaps the two most significant factors influencing capital flows are the level of actual, or anticipated, exchange rates on the one hand, and the relative level of interest rates among countries on the other. IMF rules generally require a country to intervene in the exchange markets to keep the value of its currency from breaking through the "band" around par. However, experience has shown that speculative hedging against a currency revaluation can force a government to absorb extremely large flows of hot money, mostly dollars. Distortions also can take place when interest-sensitive funds seek out currencies promising greater yields.

Government transactions in other countries—for example, foreign aid transactions and military equipment purchases—have direct balance-of-payments consequences. Private capital movements which are influenced by market, as opposed to exchange or interest rate factors also have a considerable effect.

This indicates that any significant reform of the international monetary system must resolve many issues on an integrated and comprehensive basis. Testimony during the Annual Hearings of this Committee demonstrated that the Administration shares this view. **We support the Administration's efforts to use August 15th as the basis for developing a new system which—unlike Bretton Woods—will be able to respond to the new conditions of the international economy.** On specific items we have the following comments:

(1) *Exchange rate adjustments.*—In the past few years, exchange rate adjustments have taken place only as a matter of last resort, and as such have encouraged the build up of speculative pressures. In addition, the system has given a bias to devaluations over revaluations. Until recent years, devaluations outnumbered revaluations by over two to one. **We support a system of smaller and more frequent changes in par, to the extent such are needed to discourage sudden shifts of international capital. We also support an exchange rate system which will bring equal influence to bear upon persistently surplus countries as**

¹ Congressman Blackburn states: The inability to control the volume of international reserves is not inherent in the SDR facility itself but in the reserve-currency system into which SDR's were introduced. A similar consideration applies to the maldistribution of new reserves: if it is regarded as desirable to distribute new reserves in proportion to IMF quotas, as is now done with SDR's, then the problem lies not in the SDR facility itself but in the coexistence of the dollar as a reserve asset. Thus, even if we can control "excessively large international flows of capital," new reserves will continue to be distributed in a less than "optimal" fashion as long as the dollar continues as a reserve asset.

well as deficit ones. Realizing the connection that exists between reserve creation and a reduction of pressure on a currency to devalue, we support a level of reserve creation which—taken together with other reforms—would remove the bias toward devaluation which existed in the Bretton Woods system.²

(2) *SDR distribution.*—With regard to artificial reserve creation, we further recommend that the IMF explore whether the formula for SDR distribution should be reformed and revised to ensure that it is best serving the national interest of the U.S. in providing maximum possible promotion of U.S. exports and domestic employment.

(3) *Coordination among monetary authorities.*—It is clear that close coordination of monetary authorities is crucial to the smooth and efficient functioning of any international monetary system. Problems of interest rate policies, the investment of foreign exchange reserves, and capital controls (e.g., the Federal Reserve's Voluntary Foreign Credit Restraint Program) all require implementation with full knowledge of the reaction of affected governments. While we are satisfied with the fact that consultation among the Group of Ten central banks does occur at regular intervals, we would also support efforts to make the process more formal and more open. In this context the analogy of the Federal Open Market Committee, wherein reports are issued three months after each meeting, is useful.

(4) *Defense burden sharing.*—We continue to support the efforts being made by the Administration to have the burden of defense costs distributed more equitably among our allies.

(5) *Gold.*—There is almost universal agreement among economists that the role of gold in the future international monetary system will be diminished. The United States provided the first major step in this direction when it suspended dollar-gold convertibility on August 15, and we support the Administration's intention not to resume full convertibility. Our experience has shown gold to be a less than ideal medium as a basis for the international monetary system. The resources which need to be devoted to mining monetary gold are by definition wasted when one considers that another reserve asset, SDR's, can be created by an accounting entry. Gold production bears no relation to the needs of the world monetary system, and will probably continue to be outpaced by those needs. The existence of a two-tier market for gold, while it has served us adequately since its origins in the emergency situation of March 1968, nevertheless places strains on a gold-based system whenever speculative pressures arise in the private gold markets. Finally, we have learned that the present system unnecessarily imposes problems of diplomacy into the workings of reserve management, as the case of South African sales of gold to the IMF illustrates.

² Congressman Blackburn asks: Do we want to create enough reserves to remove all pressure on deficit countries to eliminate balance of payments disequilibrium? There are other ways of mitigating the devaluation bias, e.g. rules or presumptions have been proposed by some economists under which surplus countries would have the same responsibility to revalue as a deficit country would have to devalue.

(6) *The dollar*.—Perhaps more clearly understood is the fact that the role of the dollar will undergo substantial change during a reform of the international monetary system. Before August 15, the dollar was not only the vehicle currency for international trade but was also the intervention currency of governments and the most widely used reserve currency. By suspending the convertibility of the dollar into gold and other reserve assets, the President began a process of reform which, according to virtually all economists, will change the role of the dollar as a reserve currency.

History will probably note that this and further reforms are overdue, and that the rationale for maintaining the dollar as the underpinning for the international monetary system disappeared with the emergence of a fully reconstructed and competitive Europe and Japan. We agree with this assessment. However, we appreciate as well the considerable problems which must be overcome before a suitable role for the dollar can be defined and agreed upon. The chief problems are the disposition of foreign-held dollars in excess of U.S. monetary reserves (the "dollar overhang"), and the restoration of convertibility for the dollar.

A solution to these problems, as well as the problems of gold, demands a sophisticated appreciation of what can be accomplished in the long versus the short term. We believe the progress made to date demonstrates the wisdom of the President's August moves. The fact that Congress has reacted swiftly to the President's request for a change in the par value of the dollar demonstrates the clear national interest which was served by the exchange rate adjustments negotiated in the Smithsonian agreement. We believe the next step must be to carry out that part of the Smithsonian accord which calls for prompt negotiations to consider reform of the international monetary system over the long term.

In concluding a discussion of gold and the dollar we would like to emphasize the potential that exists for utilizing international monetary reform as a vehicle for promoting capital flows towards developing countries. While such a device presents technical difficulties, we believe its significance is too great to be ignored.

INTERNATIONAL TRADE AND FINANCE

If there is one thing the American people learned from the events of August 15, it is the close connection that exists between the arcane science of international monetary procedures and the more down-to-earth subjects of exports, imports, wages, prices and jobs. Perhaps the man in the street can be excused from taking an avid interest in dollar convertibility, wider bands, or international liquidity creation, but when the suspension of dollar convertibility and the currency realignments of the Smithsonian agreement are tied directly to progress on the trade front and to domestic jobs—as the President made clear since last summer—the interdependence of all these becomes pretty complete.

We have already pointed out that the events of August–December 1971 call into question the role of the dollar as the world's major reserve currency. As one of the witnesses at the Annual Hearings stated :

As things stand now, no country can know for certain whether it will be able one year from now to use its dollar reserves to make payments to Europe or, if so, at what approximate rate of exchange. If the U.S. balance of payments recovers quickly, the European countries may not object to a moderate increase of their dollar holdings, even if the dollar is not convertible in any form. On the other hand, if there is a sharp increase of their dollar holdings, some of them may decide not to accept more dollars, even if this means abandoning their dollar exchange rates. Or if they continue to accept dollars, it may be only in connection with trade, while other payments go through a free market at fluctuating exchange rates.

As the above statement demonstrates, the events of 1971 also call into question the ability of the system to absorb persistent United States balance-of-payments deficits in the future.

In short, by abandoning the gold-dollar link, we may have freed ourselves from some of the burdens of being the world's major reserve currency, but we also freed ourselves from some of the benefits as well. In the future, we shall have no choice but to develop policies which guarantee long range balance-of-payments equilibrium. The implications of this state of affairs for our trade policy are clear.

There is a respectable body of economic opinion which questions whether our trade account need play a leading role in restoring such equilibrium. The income from investments, so the argument goes, should be enough to offset the outflows in our trade and other balance-of-payments accounts. This pattern is the logical outgrowth of America's transformation to a "mature creditor nation" from one which had to rely upon exports of goods and services to maintain balance-of-payments equilibrium.

Although trends suggest that the "mature creditor nation" theory has some substance, today's figures show that we cannot afford continuous trade deficits. As the Economic Report of the President points out, the surplus in U.S. net investment is insufficient to compensate for other factors (e.g., mutual security costs, foreign aid, pensions to citizens living abroad) which the national interest demands. Therefore, we agree with the conclusion in the Economic Report that for the present "a trade surplus will be required if our goal is external balance."

There are indications that our trade position can be significantly improved over the coming 24 months. The currency realignment reached at the Smithsonian agreement will result in a weighted, average appreciation of other Group of Ten currencies vis-a-vis the dollar of approximately 13 percent: the realignment with Japan, with whom our trade deficit has been the largest, is almost 17 percent.

With regard to trade agreements, negotiations were successfully concluded in 1971 establishing a tariff quota for imports of stainless steel flatwear and voluntary export restraints for wool and man-made

fiber textiles and for meat. The International Wheat Agreement was re-negotiated during the year.³ Substantial progress was made during 1971 toward an agreement with Japanese and Common Market steel producers for extending their voluntary export arrangements on steel.

During 1971 Japan liberalized a variety of its import restrictions as a result of bilateral discussions with the United States. As the year ended, we were engaged in negotiations over short-term trade problems with the European Community, Japan, and Canada. Agreement was reached with the first two early in 1972, including agreement to engage in further negotiations in 1973. It is our hope that these will be major negotiations, which will get into the serious business of non-tariff trade barriers.

Among the closely related activities in 1971 affecting international trade was the establishment of a high-level group by the Organization for Economic Cooperation and Development to examine trade problems in long-term perspective and propose possible solutions. Within the framework of the General Agreement on Tariffs and Trade (GATT), the United States and other countries made substantial progress toward the solution of specific trade problems, notably in the development of a code for industry, technical, and other types of standards. The United States also initiated GATT examination and review of the preferential arrangements which have been developed by other countries and an examination of the future role and function of the GATT.

In 1971, in fulfillment of Secretary Rogers' pledge to the developing nations of the world, the Administration initiated consultations with Members of the Congress with a view to the early introduction of legislation to grant developing countries generalized tariff preferences on a wide range of products. The European Common Market, Japan and Norway have already extended such preferences to the developing world.

We share the judgment that Secretary Rogers put forward in his 1971 foreign policy report that "1971 was not an appropriate time to submit legislation for these preferences." We would ask our friends in Latin America and other developing countries of the world to understand that the delay in submitting this important legislation reflects the serious economic problems of our country rather than a lack of intention to develop a system of generalized trade preferences which will benefit them.

On the legislative front, the passage of the Administration's DISC proposal, which we supported in an earlier Annual Report, marks a breakthrough in the development of incentives for export. By enacting P.L. 92-126 (The Export Expansion Finance Act of 1971), the Congress provided the Export-Import Bank with the flexibility Exim needs to assure that U.S. exporters can offer competitive financing on their export sales. The same legislation also exempted export credits from the Fed's Voluntary Foreign Credit Restraint program.

³ Unlike the previous agreement, which contained minimum prices that caused so much evasion and controversy, the new agreement merely provides for negotiations with respect to minimum prices. This enables the United States to protect our producers by refusing to agree to such prices unless there are appropriate safeguards.

Administrative decisions in the anti-dumping, countervailing duty and adjustment assistance areas show that these features will continue to be important parts of our trade policy. As we point out below, however, we believe that there is substantial room for improvement in our adjustment assistance mechanism.

The above paragraphs indicate the breadth of measures available to the Government for improving our trade balance and for minimizing the burden of adjustment. However, it should not be assumed that each constitutes a totally effective means. Nor should we take for granted the long-run necessity for such a wide range of measures, given our traditional commitment to free trade. The extent we have had to resort to voluntary agreements limiting the imports of various commodities, for example, indicates in some cases the shortcomings of the adjustment assistance provisions of the 1962 Trade Expansion Act.

The above discussion leads us to the following conclusions about policies for regaining a healthy trade balance and for minimizing the burden of adjustment:

(1) The primary element of a national trade policy should continue to be the pursuit of the goal of expanded trade. Over the long-run, this will do more to create jobs at home than any other measure. Thus, we applaud the progress being made by the Administration to bring about the liberalization of trade restrictions and to commence comprehensive negotiations on reducing nontariff trade barriers. We do not believe that a solution to our trade balance can be found in the imposition of overall quantitative trade restrictions, such as are provided in the Hartke-Burke bill, discussed below.

(2) Our best defense against further deterioration in our trade balance lies in improving our price competitiveness through increased productivity. Year-to-year gains in productivity in this country, while they compare favorably with prior U.S. experience, still fall far short of the performance being turned out by our major trading partners overseas. Our detailed views on productivity are contained in Section IV of these views.

(3) We are not convinced that our adjustment assistance programs are being used to best advantage. At the outset we need better information as to the effectiveness of these programs: how quickly affected persons are being rehired, the effect of plant and worker adjustment assistance programs on communities, the feasibility of establishing an "early warning" system for identifying entities in need of adjustment assistance, the costs and benefits of the present form of adjustment assistance compared with more comprehensive forms. We commend the President for his initiatives in this field and await his legislative recommendations.

(4) Notwithstanding the necessity of the December 1971 currency realignments, the international monetary system is not yet developed so that the U.S. can use changes in the par value of the dollar as a major tool of trade policy. Therefore, a program of export expansion must rely upon more conventional means. In this regard, we applaud the achievements of

the Export-Import Bank, in being able to increase the amount of Exim-financed exports by 137 percent over the past two years. Of particular note is the way the Bank has successfully revised its medium-term discount program which, in the three years prior to June 30, 1969, had only attracted 21 banks for \$460 million in exports, whereas in the two fiscal years since then has attracted 102 banks for \$1.2 billion in exports. With regard to the short-term discount facility authorized by the Export Expansion Finance Act of 1971, we trust that the added flexibility to Exim's operations will not be encumbered by administrative restraints, and will thus provide the support intended by Congress.

(5) One of the major elements in our trade deficit lies in the travel account. Americans spend \$2.6 billion more abroad than foreign visitors spend in this country. We affirm, as we have done on several past occasions, our opposition to solving the travel account imbalance by restricting the travel of Americans abroad. However, we cannot help but notice that our efforts to attract foreigners to these shores is modest compared with the efforts of other countries to promote tourism—consisting chiefly of Americans—to theirs. Therefore, the Administration is to be commended for requesting a significantly increased appropriation for the U.S. Travel Service at a time when budget stringency is being practiced in other quarters. This represents a realistic use of opportunity costing. We affirm our support for the full appropriation being requested by the Administration.

(6) While we admire the Administration's successful efforts to obtain voluntary export restraints by other countries for such commodities as wool and man-made fiber textiles, we would prefer that such a program be accompanied whenever possible by a vigorous effort to improve the productivity of the U.S. industry being protected. Only in this way can the voluntary quota system be prevented from becoming a permanent feature of our trade policy. We share as well the misgivings of the Council of Economic Advisers that the voluntary quota system fosters noncompetitive practices abroad, which in the long run can make severe inroads on our trade position.

A major issue in trade proposals being made this year is the activities of the multi-national corporation. Alternately praised and maligned, the MNC has been said by some to have been responsible for much of the speculative pressure against the dollar in 1971. Perhaps more seriously, it is also blamed for "exporting jobs" through the use of foreign subsidiaries and the transfer of U.S.-developed technology to them. According to critics, the MNC is assisted by the fact that present tax and tariff provisions encourage this kind of activity. A bill submitted by Senator Hartke and Representative Burke would establish a broad quota system and substantially curb the MNC activities alleged to be at fault.

The keystone of the issue is, of course, jobs. One economic rationale cited by supporters of the Hartke-Burke bill is that existing jobs now threatened by imports would be protected by the bill and that the import substitution effect of the quotas would generate additional employment; in other words, passage of the bill would produce more jobs.

We disagree strongly both with the Hartke-Burke proposal and with the arguments used to support it.

We are painfully aware of some instances where plants have closed because their production was transferred overseas, with the product being exported back to the United States, and we cannot be so naive as to think that the range of services presently available to those affected are an adequate substitute for the jobs they once held. On the other hand, we believe that the Hartke-Burke proposals being offered to "cure" the situation are worse than the disease. Recent studies have made it clear that when a multinational corporation invests in manufacturing operations overseas, this is done in 90 percent of the cases to retain foreign markets and to overcome trade barriers—the alternative being to totally lose the business to foreign competition. Less than 10 percent of the production of foreign affiliates of United States firms overseas is imported into the United States.

The American working man would be the chief loser in a broad system of quotas. Passage of the Hartke-Burke bill would set off a trade war of such proportions as to constrict international trade and threaten a worldwide depression. The implications of this phenomenon for the domestic employment picture are immense. At the least, the bill would jeopardize the jobs of the more than 2½ million Americans employed in export activity. It would "export" those jobs, which are generally in high-wage industries, while providing insufficient new jobs through import substitution effects.

At the present time, the foreign trade sector of the U.S. economy is estimated to be generating more than 750,000 jobs, taking into account the job displacement represented by imports. We believe this performance can best be improved through the multilateral liberalization of trade restrictions, which as we have mentioned above, is already being charted by the Administration, through increased productivity at home, and through the improvement of adjustment assistance programs.

Nor is the attack on other forms of MNC activity warranted. A recent empirical study concludes that from 1960 to 1970 the rate of growth in domestic employment and U.S. exports has risen much more rapidly in MNC's than in the nation as a whole, and that decisions to locate plants abroad have been based primarily upon the need to preserve foreign markets or overcome trade barriers; in many cases, component parts are manufactured here. As for curbs on transfers of technology, we are reminded that substantial amounts of foreign technology (e.g., radial tires, cassette tape recorders) have come from abroad; it is, therefore, a two-way street. Finally, we note that many barriers to international trade have an inflationary effect.

One aspect of MNC activity which merits examination is the way in which their operations influence U.S. balance-of-payments statistics. Preliminary analysis has shown that a substantial proportion of the "errors and omissions" sector of our balance-of-payments accounting—the largest sector, accounting for \$11.4 billion of the liquidity deficit last year—results from financial flows generated by or through MNC's. While we strongly support efforts being made by our Administration to quantify the various components of our balance-of-payments accounting more precisely, there is merit also in an international approach to the problem

of developing statistics describing MNC activity. We urge the Administration to seek international standards for developing such statistics, using the IMF as a forum.

FOREIGN AID

The foreign assistance programs of the United States faced their most critical tests in 1971 since the inception of the program. The Congress did not act on the President's message of April 21 proposing the reform of our foreign assistance programs, and then the Senate defeated the House-passed AID authorization bill on October 29.

While the AID program was quickly revived and passed the Senate by a large margin less than two weeks later, this legislation contained very large cuts in the overall requested authorization level for economic, security and military assistance. The magnitude of these cuts calls into question U.S. efforts to provide assistance to developing countries in the amounts that correspond both to their needs and to our own long-term political and economic interests.

We accept the premise that changing economic conditions both at home and abroad call for a new definition of the United States role in providing foreign economic assistance. We note that there is now increased burden sharing among the industrialized nations of the world in providing development assistance, that nations other than the United States are now supplying more than half of all such assistance, and that their contributions are growing. We also note that international institutions such as the World Bank group, the regional development banks, and the United Nations Development Program are promoting an effective and multinational development effort.

We urge that the responsible committees of the Congress give priority attention to the President's recommendations for restructuring the aid programs of the United States toward the end of re-molding these programs to better meet the new realities of the 1970s.

As the President has stated in his annual foreign policy report to the Congress:

Our wealth, our humanitarian traditions, and our interests dictate that we have an active foreign assistance program. The world looks to us for help in this area, and it is right that we should respond. I am prepared to work with the Congress to that end.

ADDITIONAL VIEWS OF SENATOR JAVITS

DOMESTIC ECONOMIC ISSUES

Except where footnoted, I agree with the Minority Views of this report and support the Administration in its very difficult task of managing our economic recovery. In a number of respects, however, I believe the points of emphasis established by the Minority to be misplaced.

There is no getting around the fact that the economic progress made to date, while commendable, is insufficient to meet our goals of full employment and a healthy business environment. The Administration's growth projections can be accounted for almost entirely by the Administration's own projections of productivity gains and additions to the labor force, leaving very little promise of substantial reductions in unemployment over the near future. The Administration's fiscal policy expressed in aggregate terms is appropriately stimulative; however, a closer look at the numbers reveals a jump in the amount of the budget which is uncontrollable, and a serious "locking in" of increased federal spending for future years, especially in authorizations for the military.

Under these circumstances, we urgently need to set employment goals as a first step, and to adapt our fiscal policy and goals for business growth to meet them. As a means towards achieving substantially reduced unemployment during the coming year, we need a greatly expanded public sector jobs program and a reform of the existing manpower programs so as to ensure suitable job opportunities for those being trained. Recent studies have pointed out the shortcomings of present manpower policies, which concentrate chiefly on the supply side (e.g., training) while not paying enough attention to the demand side of the labor market, which includes efforts to reduce racial and sex and ethnic discrimination. We must bring our manpower policies up to date, and in this regard a sophisticated public sector jobs program should be made the basis for our efforts.

There is ample room for improvement in the management of Federal spending. Congress should seize the spirit of concern which has been expressed at the large budget deficits—both actual and proposed—to rationalize the appropriations process. Establishment of a Congressional Office of Goals and Priorities Analysis, which I have proposed in legislative form, is needed at this time.

Our efforts to contain inflation cannot succeed so long as structural barriers to improve productive efficiency continue. The Government should make a special effort at this crucial time, in conjunction with the National Commission on Productivity and the Regulations and Purchasing Review Board, to pinpoint those government activities which result in higher prices and reduced government efficiency.

I dissent from the Minority Views on the subject of minimum wage legislation. In my view, a prompt increase in the minimum wage to \$2.00 is essential to help those at the bottom of the wage scale to keep pace with the rising cost of living. Past experience demonstrates that such an increase is noninflationary during recovery periods such as the present.

INTERNATIONAL ECONOMIC ISSUES

For the third year in a row, neither the budget submitted by the Administration nor the Economic Report of the President breaks out separately the costs of the Southeast Asian war. The Administration, unfortunately, is not providing the Congress and the American people the complete economic facts concerning our continuing and tragic involvement in Vietnam. I urge the President, in the years ahead, to provide the Congress and the American public with a full and formal accounting of our Southeast Asia expenditures. I think that it is widely recognized that these expenditures in the past have played a major role in contributing to the inflationary pressures that are still present in the American economy, to the continuing weakness of the U.S. dollar and to the deficit position of our Government. Since the war has been wound down impressively and hopefully will soon be concluded, such public disclosures clearly would be in the Administration's interest.

Turning to the international economic issues which today have such a profound effect on the American domestic economy, it is my view that the reform of the international monetary system should be pursued with the same urgency as was the interim agreement on currency realignments concluded on December 17-18, 1971. The passage of time will strengthen no nation's bargaining position—rather it may further weaken the delicate financial relationships between nations of the free world which are an integral part of the economic well-being of the free world. In turn, the issue of the continued economic well-being of the free world is an integral part of our national security.

I urge the Administration immediately to take the minimal steps needed to provide the mini-convertability that is necessary to maintain the orderly functioning of the International Monetary Fund. I am pleased to note that the Administration appears to be showing some signs of flexibility on this issue. But I also urge the Administration to take positive, open steps to make good on its Smithsonian pledge to open prompt negotiations looking towards the long-term reform of the international monetary system. These negotiations must be concerned with the future role of gold and SDRs within the international monetary system, the role of the dollar as a reserve currency, the immobilization of the excessive dollar balances now in the hands of foreign central banks, the possible linkage between future SDR creation and development assistance and most importantly, the building of sufficient exchange rate flexibility into the international monetary system.

In constructing such a new international monetary system, we must be wary of those who would favor a division of the world into several rival major currency and trading blocs. Unfortunately, the evolution of the European Common Market to date gives pause to those of us

who favor an open trading world based on the principle of most-favored nation treatment. Within the Common Market, preferential trading relations in open contravention of this principle are being maintained if not strengthened.

Our vision of the future should leapfrog the regional trading bloc concept which seems to be gaining ground and rather focus on a new round of trade negotiations in 1973, looking towards the establishment of a free trade area of industrial products combined with a freer trade in agricultural products. This would require modification of the present Common Agricultural Policy of the European Common Market.

If this vision is not pursued and if the information of regional monetary and trading blocs continues to gain, all countries of the free world will suffer in terms of economic growth. I would urge our European friends to think twice before putting into concrete, arrangements whose net effect will be to encourage the United States, Japan, Canada, New Zealand, Australia, Latin America and selected other countries of the Pacific to turn inward and to construct the same kinds of *discriminatory* tariff and non-tariff barriers now increasingly rising in Europe.

The world has an unparalleled opportunity to construct a new and viable international economic order that would work enormous benefits to all countries of the free world. We must seize this opportunity, otherwise economic regionalism will be upon us, with all that this means militarily, politically and economically. And once the forces of regionalism and protectionism take hold, they will be exceedingly difficult to undo. The decisions we make today will probably mould the world for the rest of this century. Perhaps the moment will soon be at hand to convene a summit conference of the heads of Government of the major nations of the free world to decide what should be the economic shape of the free world for the rest of this century.

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 March 28. 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 year is summarized below.

FULL COMMITTEE

Economic Prospects and Policies

The combination of inflation and unemployment which the Nation experienced in 1970 prompted the Committee to hold six days of special hearings on the economic situation commencing January 22. Testimony was received from State and local officials, a Member of Congress, former government officials, academicians, representatives of business, labor and banking, and other experts.

February 1971 Economic Report of the President

On February 5, the Committee began ten days of hearings on the 1971 Economic Report of the President receiving testimony from the Council of Economic Advisers, the Director of the Office of Management and Budget, members of the Cabinet and other officials of the executive departments, Members of Congress, economic experts from universities and research groups, and representatives of business. Part 3 of the printed hearings contains statements from leaders of banking, business, labor, agriculture, and private research groups commenting on the President's Report.

The 1971 Joint Economic Report

The Annual Report of the Joint Economic Committee (S. Rept. 49) was filed with the Congress on March 30, the March 1 deadline having

been extended by P.L. 92-2. The Report also contains a statement of Committee agreement, joint views on international economic issues, minority and other views.

Current Labor Market Developments

In April the Committee began the first in a series of monthly hearings on the employment-unemployment situation. The Administration's action in eliminating the traditional monthly press conferences at which top technical experts discussed the unemployment figures led the Committee to institute these hearings. Witnesses at the first hearing were the Commissioner of the Bureau of Labor Statistics and a former Commissioner. At subsequent monthly hearings testimony was received from the Commissioner of BLS, academic experts, government officials, and, at the July 2 hearings, five unemployed persons.

The 1971 Mid-Year Review of the Economy

Six days of hearings were held in July on the mid-year review of the state of the economy. Testimony was received from the Majority Leader of the Senate, the Chairman of the Council of Economic Advisers, the Chairman of the Board of Governors of the Federal Reserve System, and outstanding economists with expert knowledge in the fields of housing, monetary and fiscal policy, and wage and price developments.

The Committee released its report on the mid-year review on August 16. This report also contains supplemental and minority views.

The President's New Economic Program

As a result of the President's August 15 announcement of a wage-price-rent freeze, suspension of dollar convertibility and proposed tax and expenditure changes, the Committee held fifteen days of hearings in August and September. Witnesses were government officials, a Member of Congress, leading economists, former officials who had previously administered wage and price controls, business and labor leaders, consumer spokesmen, and other experts.

Federal Statistical Programs

A one-day hearing was held in October on the status of Federal statistical programs and the reorganizations which are being undertaken to improve the structure of Federal statistical activities. Testimony was received from the Chief Statistician of the Office of Management and Budget. The record of this hearing is included in the committee's publication entitled "Current Labor Market Developments, Part 2."

Phase II of the President's New Economic Program

In November the Committee undertook a review of the economic implications of Phase II of the President's inflation control program, having as witnesses the Chairman of the Price Commission and the Chairman of the Pay Board.

Report on Crude Oil and Gasoline Price Increases of November 1970: A Background Study

On November 3, the Committee released a background study on crude oil and gasoline price increases. This study analyzes the April 1971 report to the President by the Director of the Office of Emergency Preparedness. The report to the President is reprinted in this study as an appendix to the staff analysis.

The Economics of Federal Subsidy Programs

On January 11, 1972, the Committee issued a staff study on Federal subsidy programs representing a first step in setting forth the analytical principles and the factual data necessary to understand and evaluate Federal subsidy programs. The study undertakes to cover the range of subsidies, as well as to analyze individual subsidy programs, and forms a part of the continuing review by the Subcommittee on Priorities and Economy in Government of public economic policy. This study was prepared by Mr. Jerry J. Jasinowski of the Committee staff and Dr. Carl S. Shoup who served as consultant to the Committee.

SUBCOMMITTEE ON PRIORITIES AND ECONOMY IN GOVERNMENT

Following the hearings in January and February of 1971 on "Economic Issues in Military Assistance," the title of the Subcommittee on Economy in Government was changed to the Subcommittee on Priorities and Economy in Government so as to include the Subcommittee's continuing concern with priority aspects of government expenditures, in addition to the economic effects of such expenditures.

Economic Issues in Military Assistance

Five days of hearings were held in January and February on the economic aspects of military assistance. Questions pursued were: How much does the United States spend annually on grant and loan programs and what are the total amounts of cash and credit sales from the United States to foreign countries? How are the costs and benefits of military assistance measured and what are the economic impacts?

Witnesses heard were Members of Congress, the Comptroller General of the United States, officials of the Defense and State Departments, former government officials, and representatives of private research institutions.

The Acquisition of Weapons Systems

Part 3 in this series of hearings was held on April 28 and 29. Testimony focused on defense profits, the impact of the Truth in Negotiations Act, government-owned property in the hands of contractors, cost over-runs on major weapons, and related issues in defense contracting.

Part 4 of these hearings was held on May 24 and 25, continuing the investigations of the above subjects, and also including an inquiry into shipbuilders' claims against the Government.

Continuing the inquiry into the acquisition of weapons systems, part 5 of these hearings was held in September, concentrating on contractors' claims against the Government and the production of the C-5A.

Witnesses at the above hearings were the Comptroller General of the United States, officials of the Defense Department, the Chairman of the Renegotiation Board, representatives of the tool and die industry, an executive of Lockheed-Georgia Company, and a former employee of Lockheed.

Economy in Government: Automatic Data Processing Equipment

In May the Subcommittee released its report based on previous hearings entitled "Economy in Government Property Management—Procurement of Data Processing Equipment." This report centers upon

the phenomenal growth in the use of automatic data processing equipment by the Government and the adequacy of existing policies for the efficient procurement and management of these resources.

The Economics of National Priorities, Part 1

For the third consecutive year the Subcommittee conducted its annual inquiry into national priorities. Three days of hearings were held in June, concentrating on the alleged shift in national priorities from a war-time to a peace-time economy, and questions concerning the composition of the Federal budget and the allocation of the country's resources. Testimony was received from former Administration officials, academic experts and representatives of private research organizations.

The Economics of National Priorities, Part 2

On August 9, 10, and 11, hearings were held on the relationship of Russian and Chinese economic strength to their military budgets. The purpose of the hearings was to determine what level of defense spending is needed both to protect the United States against the actual military threat which these two countries pose and to reorder our priorities in order to keep ourselves economically strong and free. In addition to testimony received from former Ambassador W. Averell Harriman, the Subcommittee heard from representatives of the State Department, and academic experts.

Economic Analysis and the Efficiency of Government, Part 6

As a part of the Subcommittee's continuing study of economic analysis and the efficiency of government, a two-day hearing was held in July on the specific issue of "Economic Incentives To Control Pollution." A Member of Congress and experts connected with major conservation organizations testified before the Subcommittee.

Oil Prices and Phase II

Three days of hearings held in January 1972 examined oil import quotas, the tax treatment of oil, the application of the antitrust laws to the oil industry, and procedures for leasing Federal off-shore oil lands. Witnesses were government officials, a Member of Congress, industry spokesmen, and experts from private research groups.

The Economics of Federal Subsidy Programs, Part 1

In connection with the Committee's release of the staff study on subsidy programs, three days of hearings were held in January 1972 on the multi-billion dollar Federal subsidy system. The purpose of the hearings was to focus attention on the billions of dollars in subsidy programs, estimate their individual cost, gather information on their benefits and determine whether they achieve the purpose they are designed to meet. Testimony was received from a Member of Congress, former administration officials, experts in the field of subsidies, and representatives of private research groups.

Members of the Subcommittee on Priorities and Economy in Government are Senator William Proxmire, Chairman; Senators John Sparkman, Hubert H. Humphrey, Charles H. Percy, and James B. Pearson; Representatives Wright Patman, Martha W. Griffiths, William S. Moorhead, Barber B. Conable, Jr., and Clarence J. Brown.

SUBCOMMITTEE ON ECONOMIC PROGRESS

The Subcommittee continued review of a number of issues including energy requirements in the United States as related to long-term growth, investment in human resources, and financing requirements of communities.

Members of the Subcommittee on Economic Progress are Representative Wright Patman, Chairman; Representatives Martha W. Griffiths, William S. Moorhead, Clarence J. Brown, and Ben B. Blackburn; Senators William Proxmire, J. W. Fulbright, Lloyd M. Bentsen, Jr., James B. Pearson, and Charles H. Percy.

SUBCOMMITTEE ON INTER-AMERICAN ECONOMIC RELATIONSHIPS

The Subcommittee carried on a continuing staff review of major economic developments in Latin America and their implications for United States policy. In view of the obvious relation of inter-American economic matters to the hearings conducted and continuing study by the Subcommittee on Foreign Economic Policy, no hearings were held during the year by this Subcommittee.

Members of the Subcommittee on Inter-American Economic Relationships are Senator John Sparkman, Chairman; Senators J. W. Fulbright, Abraham Ribicoff, Lloyd M. Bentsen, Jr., Jacob K. Javits, and James B. Pearson; Representatives Hale Boggs, Martha W. Griffiths, Barber B. Conable, Jr., and Ben B. Blackburn.

SUBCOMMITTEE ON URBAN AFFAIRS

Regional Planning Issues

As a part of the study begun in 1970, the Subcommittee held eight days of hearings in May to explore all of the issues involved in regional planning and the relationship of planning efforts at the State and local levels to the various Federal departments. Testimony was received from experts on various aspects of regional planning.

Restoration of Effective Sovereignty To Solve Social Problems

On December 6, the Subcommittee released a report based, in part, on the extensive studies and hearings of the Subcommittee over the past four years and previous hearings and studies by the Joint Economic Committee. This report suggests challenging ways to solve regional and urban problems by improving relations between the vast Federal bureaucracy, State and local agencies and the people they serve. Also included in the report are minority views.

Members of the Subcommittee on Urban Affairs are Representative Richard Bolling, Chairman; Representatives Henry S. Reuss, Martha W. Griffiths, William S. Moorhead, William B. Widnall, Clarence J. Brown, and Ben B. Blackburn; Senators Abraham Ribicoff, William Proxmire, Hubert H. Humphrey, Jacob K. Javits, and Charles H. Percy.

SUBCOMMITTEE ON ECONOMIC STATISTICS

The Subcommittee continued its staff review of Government statistical programs and examination of the extent to which its long-standing recommendations for improvement of the system were being car-

ried out. No hearings were held but the Subcommittee participated in the main Committee's inquiry into circumstances surrounding the cancellation of the press conference on the monthly unemployment statistics and related matters.

Members of the Subcommittee on Economic Statistics are Senator Abraham Ribicoff, Chairman; Senators J. W. Fulbright, and Jack Miller; Representatives Richard Bolling, Martha W. Griffiths, Clarence J. Brown, and Ben B. Blackburn.

SUBCOMMITTEE ON FOREIGN ECONOMIC POLICY

A Foreign Economic Policy for the 1970's

Beginning in December 1969, the Subcommittee has conducted hearings aimed at developing a broad understanding of factors involved in the formulation of a foreign economic policy for the 1970's. In June, the Subcommittee held the seventh in this series, focusing on "U.S. Foreign Economic Policy," receiving testimony from eight officials of the Executive branch.

Members of the Subcommittee on Foreign Economic Policy are Representative Hale Boggs, Chairman; Representatives Henry S. Reuss, William S. Moorhead, William B. Widnall, Barber B. Conable, Jr., and Clarence J. Brown; Senators John Sparkman, J. W. Fulbright, Abraham Ribicoff, Hubert H. Humphrey, Lloyd M. Bentsen, Jr., Jacob K. Javits, Jack Miller, and Charles H. Percy.

SUBCOMMITTEE ON INTERNATIONAL EXCHANGE AND PAYMENTS

The Balance of Payments Mess

Five days of hearings were held in June to appraise the U.S. balance-of-payments position, to investigate the sources of the dollar flows into Germany during the latter part of April and early May, and to examine the need for exchange rate realignment. During these hearings the Under Secretary of the Treasury for Monetary Affairs, testified that current policies were adequate to keep the U.S. balance-of-payments deficit within acceptable limits and that by no means was dollar devaluation necessary. Other witnesses, who included the president of the German Institute for Economic Research and outstanding academic specialists, generally agreed that existing policies were inadequate.

Action Now to Strengthen the U.S. Dollar

On August 7, the Subcommittee released its report, with minority views. This report argued that the U.S. balance-of-payments problem could be overcome only through a general realignment of exchange rates among industrial nations and that, if necessary, the United States should initiate this process by suspending dollar/gold convertibility and allowing the dollar to float in exchange markets. On August 15, the President announced his new economic policy. As the initial step in this policy, the Treasury gold window was closed and the dollar was cut free to float in exchange markets.

Members of the Subcommittee on International Exchange and Payments are Representative Henry S. Reuss, Chairman; Rep-

representatives Hale Boggs, William S. Moorhead, William B. Widnall, and Barber B. Conable, Jr.; Senators William Proxmire, Hubert H. Humphrey, Lloyd M. Bentsen, Jr., Jacob K. Javits, and Charles H. Percy.

SUBCOMMITTEE ON FISCAL POLICY

Study of Welfare

In May, Congress appropriated a special fund to be used by the Subcommittee for a comprehensive two-year study of this Nation's system of welfare related programs. The study is aimed at providing factual information and analytical studies which Congress will need in this field over the next decade. The first hearings and study papers are expected in March 1972, and the total study is expected to be completed on or before June 30, 1973.

The study will cover the multitude of Federal and non-Federal programs which directly or indirectly provide a supplement to privately earned incomes either through cash grants or in-kind goods and services. The study will include the administration of these programs, their effectiveness in achieving their objectives, and the effects of welfare programs in combination on family structure, continuance or elimination of welfare need, employability, the structure of the labor market, and related issues.

Long-term Economic Implications of Current Tax and Spending Proposals

The Subcommittee held four days of hearings in May on the possible long-range implications of fiscal policy proposals being discussed. The purpose of the hearings was to determine what could be the overall economic effects of any one or several of the proposals being adopted in the years through 1976. Testimony was received from former officials in the Executive branch, academic experts, and representatives of banking, labor, and private research organizations.

The Economics of Recycling Waste Materials

The increasing concern with the effect of waste discharge on the quality of our environment and the doubts as to the adequacy of sources of virgin materials as inputs of production led to two days of hearings in November on the economics of recycling waste materials. Witnesses were Members of Congress, representatives of materials industries, environmental protection administration officials, and a private expert.

Members of the Subcommittee on Fiscal Policy are Representative Martha W. Griffiths, Chairman; Representatives Hale Boggs, William S. Moorhead, Richard Bolling, William B. Widnall, and Barber B. Conable, Jr.; Senators William Proxmire, Abraham Ribicoff, Hubert H. Humphrey, 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 1971.

Allied Social Sciences Association—Annual Meeting.

Brookings Institution.

Business Council.

Conference Board.

Conference on Research in Income and Wealth.

Data Resources, Inc.—Outlook Conferences and Technical Seminars.

International Council on Social Welfare.

International Monetary Fund/International Bank for Reconstruction and Development—Annual Meeting.

Resources for the Future.

Wharton Econometric Forecasting Seminar.

The Executive Director and other professional staff members made addresses or presented papers to the following:

Airline Finance and Accounting Conference.

Allied Social Sciences Association—Annual Meeting.

American University.

American University—Urban Affairs Institute.

Brookings Institution—Seminar on Congress and Economic Policy.

Canadian Parliament.

Committee on Taxation, Resources, and Economic Development—Tenth Annual Conference.

Conference Board—Economic Forum.

Defense Economic Analysis Council—Symposium on the Relevance of Economic Analysis to Decisionmaking in the Department of Defense.

Federal Statistics Users Conference.

George Washington University Law School.

Georgetown University.

Grinnell College.

Health Manpower Training Conference on The U.S. Congress—Resource Allocation.

League of Women Voters, Seattle, Washington.

McGraw-Hill—Informal Conference.

National Association of Manufacturers.

National Association of Tax Administrators.

National War College.

New York State Council of Economic Advisers.

North Carolina State University.

Society of Government Economists.

U.S. Civil Service Commission, Berkeley, California—Executive Seminar.

U.S. Civil Service Commission, Kings Point, New York—Executive Seminar.

University of South Carolina.

University of Wisconsin—Congressional Conference on the Crisis in Our Economy.

Washington Cooperative League.

The Executive Director conducted a seminar on public law and economic policy at the George Washington University Graduate School of Law. 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:

Austria
Belgium
England

France
Japan

Student Interns

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

ADDITIONS TO COMMITTEE STAFF

During 1971 Ross F. Hamachek joined the staff as an economist and Walter B. Laessig was appointed minority economist.

DISTRIBUTION OF COMMITTEE PUBLICATIONS

In 1971 the Joint Economic Committee distributed approximately 273,000 copies of current and previous years' publications. During that time 31 new publications were issued.

In addition, the Superintendent of Documents sold in excess of 100,000 copies of current and past years' publications. This figure does not include the approximately 10,000 subscriptions to the Committee's monthly publication, *Economic Indicators*, sold by the Superintendent of Documents.

SUBCOMMITTEE MEMBERSHIP

PRIORITIES AND ECONOMY IN GOVERNMENT

SENATORS

William Proxmire, *Chairman*
John Sparkman
Hubert H. Humphrey
Charles H. Percy
James B. Pearson

REPRESENTATIVES

Wright Patman
Martha W. Griffiths
William S. Moorhead
Barber B. Conable, Jr.
Clarence J. Brown

ECONOMIC PROGRESS

REPRESENTATIVES

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Martha W. Griffiths
William S. Moorhead
Clarence J. Brown
Ben B. Blackburn

SENATORS

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J. W. Fulbright
Lloyd M. Bentsen, Jr.
James B. Pearson
Charles H. Percy

INTER-AMERICAN ECONOMIC RELATIONSHIPS

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SENATORS

Abraham Ribicoff
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 Abraham Ribicoff
 Hubert H. Humphrey
 Lloyd M. Bentsen, Jr.
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 Charles H. Percy

INTERNATIONAL EXCHANGE AND PAYMENTS

REPRESENTATIVES

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