THE 1974 ECONOMIC REPORT OF THE PRESIDENT

HEARINGS

BEFORE THE

JOINT ECONOMIC COMMITTEE CONGRESS OF THE UNITED STATES

NINETY-THIRD CONGRESS

SECOND SESSION

PART 5

INVITED COMMENTS

Printed for the use of the Joint Economic Committee

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THE 1974 ECONOMIC REPORT OF THE PRESIDENT

The letter appearing below was sent to the following organizations: Ad Hoc Coalition on Housing, The American Bankers Association, AFL–CIO, American Life Insurance Association, Chamber of Commerce of the United States, Committee for Economic Development, Common Cause, Communications Works of America, Community Council of Greater New York, Conference of Mayors, Conference on Economic Progress, Conservation Foundation, Consumer Federation of America, Consumers Union of the U.S., Inc., Cooperative League of the U.S.A., Corporate Accountability Research Group, Council on Economic Priorities, CUNA International, Inc., Federal Statistics Users Conference, Financial Executives Institute, Friends of the Earth, Independent Bankers Association, Investment Bankers Association, Investment Company Institute, League of Cities, League of Women Voters, Machinery and Allied Products Institute, Movement for Economic Justice, National Association of Counties, National Association of Manufacturers, National Association of Mutual Savings Banks, National Association of Security Dealers, National Consumer Congress, National Farmers Union, National Federation of Independent Business, Inc., National Federation of Independent Unions, The National Grange, National League of Insured Savings Associations, National Organization for Women, National Planning Association, New Jersey Tenants Organization, New York Chamber of Commerce, Public Interest Economics Center, Sierra Club, Taxation With Representation, United Automobile, Aerospace and Agricultural Implement Workers of America (UAW), United Mine Workers of America, United States Savings and Loan League, Urban Coalition, Mr. Jerry Voorhis, and Mr. Andrew F. Brimmer. These organizations were invited to submit their views or comments on the text and recommendations contained in the 1974 Economic Report of the President. Twenty-two organizations submitted statements and their views were considered by the Joint Economic Committee in preparation of its report on the President's Economic Report.

CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,
Washington, D.C., February —, 1974.

Dear Mr. ___________: Under the Employment Act of 1946 the Joint Economic Committee has the responsibility of filing each year a report containing its findings and conclusions with respect to the recommendations made by the President in his Economic Report. Because of the limited number of days available for hearings, the Committee is requesting a number of leaders of business and finance, labor, agriculture, consumer, and environmental organizations to submit statements for the record on the economic issues facing the Nation. These statements will be made a part of our hearings on the Economic Report in a printed volume containing such invited statements.

At the request of Chairman Wright Patman I therefore invite your comments on the economic issues which concern the Nation and your own organization.

Under separate cover I am sending you a copy of the 1974 Economic Report of the President, filed February 1, 1974.

We would like to distribute copies of your statement to the members of the committee and the staff, and would therefore appreciate your sending 30 copies by Friday, March 15, 1974, to Mr. Michael J. Runde, Administrative Assistant, room G-133, Dirksen Senate Office Building, Washington, D.C.

Sincerely,

JOHN R. STARK,
Executive Director.

AMERICAN BANKERS ASSOCIATION

The 1974 Economic Report of the President is another in the series of reports to the Congress on the current state of the Nation's economy. It is also accompanied by a report from the Council of Economic Advisers which reviews in greater depth the economic issues now confronting the country. As might be expected, the report emphasizes the gains which have occurred over the last year. And there have been some gains. The dollar is stronger now and the international payments position of the United States has improved. In addition, the report contains a clear and concise statement of the issues still to be resolved. Special attention has been given to the energy crisis, agriculture, income distribution, and international financial developments. This report, like its predecessors, reflects a high degree of professional competence in the analysis and presentation of the basic economic issues confronting us.

High on the list of issues confronting us is the problem of inflation; a problem which, as the report says, has confronted us for 8 years. The report concedes frankly that "many programs have been launched to stop it—without durable success." The American Bankers Association shares the concern of the Council with the dangers of inflation and wishes to emphasize the necessity of undertaking measures to curb it.

The American Bankers Association has in commenting on previous issues of the Economic Report warned of the dangers of inflation and stressed the necessity of adopting measures to deal with it. We feel that the policies adopted so far have been inadequate. We recognize, as does the report, that this will be a long and hard struggle but we believe that it is worth the effort. The 1974 Economic Report admits that those who would fight inflation must be prepared to stay the long course. After reciting all of the virtues of fighting inflation and emphasizing the dangers of inflation, we feel that the report has not recommended any new medicine, or even an increased dosage of the old medicines.

Instead, the report turns to a recital—no doubt substantially correct—of the real gains achieved over the last 8 years. And for the following year, the hope is expressed that a modest slowdown in business early this year will reduce the rate of inflation. In view of the Council's own admission that the battle against inflation has so far achieved no durable success, it may be unduly sanguine to assert that a slowing in the rate of inflation will follow the decline in business.

As a general rule, restrictive fiscal and monetary measures are usually called upon to curb inflation. However, both the budgets for this year and for next year show that the Government anticipates 2 more years of deficits. With prices rising, with speculation increasing, and with inflationary fears mounting, a budgetary deficit of any size is probably not desirable. More restrictive fiscal policies may be in order. This is especially true since the modest decline in business now expected may result in a larger budgetary deficit than is forecast in the President's message.

The report furthermore notes that because of lags between monetary policy and its effect upon economic activity, the influence of "monetary policy on the economy during 1974 will largely result from the monetary expansion during the second half of 1973 and the first half of 1974." Monetary policy is admittedly a highly complex subject, but the American Bankers Association believes that an easy money policy is not appropriate at a time when we are trying to curb inflation.

Admittedly, these are difficult choices to make. A restrictive monetary and fiscal policy might bring about an unacceptably high level of unemployment. On the other hand, we are reasonably certain that expansionary fiscal and monetary policies will exacerbate inflationary trends. The American Bankers Association believes that it is necessary to reexamine the long-run effects of inflation upon the economy as compared with a lower level of business activity needed to curb it. Moreover, we feel that the tools that have been employed over the last 8 years to curb inflation should be reappraised. Such a reexamination may reveal new ways of using these old tools more effectively, or disclose new tools to achieve this objective. We understand clearly the difficulties confronting this—or any other—administration in trying to develop a healthy economic climate. Those who stand on the sidelines are frequently accused of giving advice that is not helpful. We believe, however, that efforts to curb inflation should be pursued with vigor, because in our judgment over the long run this will tend to restore the health of the American economy. If we permit inflation to run unchecked we undoubtedly will bring widespread economic maladjustments.

One measure that could be adopted to lessen inflationary pressures is the removal of the existing legal restrictions on the operations of free markets such as the Robinson-Patman Act and the Davis-Bacon Act. The American Bankers Association is of the opinion that governmental efforts should be directed toward removing controls placed on the economy by the existing phase IV program and to avoid in the future another experiment with wage-price controls.

In making these comments about the Economic Report, we do not wish to downgrade it. Indeed, to reemphasize there is much in this report that has great merit and many of our economic problems are analyzed with great perspicacity. The American Bankers Association does, however, believe that the fight against inflation should have an even higher priority than we feel is assigned to it in the current Economic Report.

AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS

By I. W. Abel, *Chairman, Economic Policy Committee*

The AFL–CIO is pleased to have this opportunity to present our views on the Economic Report of the President and on the state of affairs of the national economy.

The recent midwinter meeting of the AFL–CIO Executive Council and its Economic Policy Committee devoted considerable attention to economic developments.

We are deeply concerned about the deterioration of the American economy. Today it is in the worst shape since the Great Depression of the 1930's. Inflation has accelerated sharply, accompanied by an energy crisis and another recession. Prices of food and fuel are soaring out of sight. Workers' buying power is declining. The living standards of American families—especially middle- and low-income famil'es with children—are being severely undermined by skyrocketing prices generally and, in particular, by the prices of food. Layoffs and cutbacks of working hours are spreading. Unemployment is rising rapidly. Public confidence in the Government's ability to manage economic problems has dropped to an alarming low point.

The energy crisis underscores the growing danger to the American economy of the increasing dependence on foreign oil imports, encouraged by the lavish Government subsidies for the foreign operations of the huge, multinational oil companies.

The soaring prices of farm products and crude materials—based essentially on massive, unregulated exports of such commodities in short domestic supply—reveals the inflationary jolt of the devaluations of the American dollar. The administration has sacrificed the American price level and the living standards of the American people for a temporary improvement of the balance-of-payments accounts, without a workable solution to halt the deterioration of the U.S. position in the world economy.

Basic problems in the domestic economy and in international economic relationships have not been handled. Instead, the administration has engaged in gimmickry and rhetoric, which fail to solve growing problems and which contribute to the loss of confidence.

Following are the AFL–CIO's views on these and related issues, with specific recommendations for Government action to forestall an economic tailspin and to move America forward again.

The National Economy in Early 1974

The second recession of the Nixon administration has begun.

Industrial production declined in December and January, bringing it down to about the level of mid-1973, and it is still falling. Unemployment is rising rapidly. Living costs are soaring. The living standards of the American people are being undermined. Housing is in a depression.

The Government has not leveled with the American people and has no plans to meet this crisis.

This decline is based on the complex economic mess that developed in 1972–73, which has been compounded severely by the energy crunch.

The energy crunch has aggravated America's economic troubles which developed during the previous 2 years, as a result of the Nixon administration's economic policies. The economy was already in a slowdown, with the danger of a recession and continuing rapid inflation, before the onset of the energy emergency.

Homebuilding was declining sharply; auto sales in October were down; the buying power of workers' weekly take-home pay was also moving down; interest rates were close to or higher than the record levels that brought on the money crunch and recession of 1969–70; the cost of living in October was up 7.9 percent from a year before and it was continuing to rise; there was a sharp drop in consumer confidence. That was before the energy emergency.

The energy crunch is resulting in sharp increases in fuel prices, as well as widespread cutbacks in production, employment, and working hours—with uneven impacts in the different industries, sectors, and occupations. Since October 1973, the national economy has been facing the double threat of an oil-crunch slowdown and price pressures on top of the economic slowdown and continuing rapid inflation that were already underway.

By December and January, the economy was in a general recessionary decline, with both rapidly rising unemployment and soaring living costs.

The Nixon administration's policies have resulted in accelerating inflation since the summer of 1972. This stepped-up pace of rising prices was touched off by the huge Russian grain deal in July 1972. It was made far worse by the devaluations of the American dollar, which resulted in large-scale exports of farm products and crude materials—such as steel scrap, copper scrap, waste paper, and fertilizer —which are in short domestic supply. The devaluations also boosted the prices of imports.

The administration's adoption of restrictive monetary and fiscal policies, at the beginning of 1973, were the wrong approach. These policies could not possibly stem the inflationary tide. But they brought interest rates to record levels and slowed the economy, at the same time as the buying power of workers' take-home pay declined. Moreover, rising interest rates added to inflationary cost and price pressures throughout the economy.

The administration's shifts from phase 2 to phase 3, freeze 2 and phase 4 did nothing to halt the accelerating rise of living costs. They continued the so-called stabilization program's record of unfairness and imbalance. Moreover, they generated uncertainty and a further decline of public confidence in the Government's ability to deal with economic problems.

The energy crunch, which was superimposed on this weakened condition, is resulting in added inflationary pressures, layoffs, cutbacks in weekly working hours, and reduced living standards.

The result has been:

Housing starts, hit hard by high interest rates and inflation, fell sharply after the early months of 1973, By January, they were down 40 percent from January and February 1973, and building permits were down 37 percent.

Sales of new American-made autos, which have been hit by the energy crunch and the decline of workers' buying power, were down sharply in January and February from a year before. Auto production in January was down 31 percent from January 1973, and in February it was down 32 percent from year-before levels.

The buying power of the average worker's weekly take-home pay has been declining since October 1972. By January, it was down 5.8 percent from the level reached 15 months before.

In sharp contrast, corporate after-tax profits shot up an estimated 27 percent in 1973, following a 16 percent increase in 1972 and a rise of 21 percent in 1971.

The cost of living, as measured by the Consumer Price Index, in January, was up 9.4 percent from a year before—the sharpest 12-month rise since 1947–48, except for early 1951 after the outbreak of the Korean war. Retail prices of food—the largest item in the family budget of most Americans—soared 19.5 percent between January 1973 and January 1974, squeezing the living standards of most American families.

Further increases of retail prices are indicated by the 20.3 percent rise of wholesale prices in the past year, the renewed sharp rise of wholesale food prices and the surge of prices for gasoline and fuel oil. It is estimated that the consumers' energy bill, alone, will be up about $20 billion in 1974, in addition to price boosts for food and other consumer goods and services.

Unregulated huge exports of goods in short supply and the Government's failure to regulate and curb excessive speculation and profiteering in the commodity exchanges brought tremendous increases in the spot prices of basic farm products and crude materials. The cash spot-price of wheat, for example, shot up from $1.60 a bushel in mid-April 1972 to $2.57¼ 1 year later and to $5.76 on March 1, 1974; soybeans went from $3.54¾ per bushel to $6.64¾ and $6.32 in that same period of time; corn shot up from $1.25 per bushel to $1.65 and $3.21; steel scrap soared from $35 a ton to $44.50 and to $125; cotton jumped from 38.9 cents per pound to 41.8 cents to 71.1 cents. Such price boosts are pressing on skyrocketing costs and prices, all along the line to the retail store and the consumer.

Industrial production dropped six-tenths of 1 percent in December and eight-tenths of 1 percent in January.

The real volume of retail sales, in January, after accounting for increased prices, was substantially less than in January 1973.

The number of employees on nonfarm payrolls dropped almost 260,000 in January 1974, The average workweek in private, nonfarm industries fell to the lowest level since these figures were first reported on a monthly basis in 1964.

Unemployment shot up 630,000 between October 1973 and January 1974—from 4.1 million or 4.6 percent of the labor force to 4.7 million or 5.2 percent. The Labor Department's report that unemployment remained about the same in February may be due to a statistical quirk, since manufacturing employment continued to drop and there was a rise in the number of people receiving unemployment insurance payments.

The Federal Reserve's monetary policy shot interest rates up sharply. The prime interest rate, which commercial banks charge on loans to the largest corporations, was 9½ percent in the beginning of February—a full percentage point higher than the prime rate of 1969–70 that resulted in the recession and money crunch. During February there were indications that the Federal Reserve may have moved away somewhat from its restrictive policy and the prime rate declined to 8¾ percent at the end of February. But there was no clear indication of a continuing policy of monetary ease and a continuing, rapid decline of interest rates.

The Survey Research Center of the University of Michigan reports that "the pervasive lack of confidence in the Government and its economic policy, together with the widespread opinion that the inflation problem won't be easily solved, has led to great pessimism about the long-run outlook."

The national economy is in a mess—a general recessionary decline, rising unemployment and the continuation of soaring inflation, with no relief in sight.

What is needed, above all, is a candid public appraisal of these difficulties by the administration—to establish the foundation for restored public confidence in the Government's ability to face up to economic problems and to deal with them fairly and equitably.

The AFL–CIO believes these Government measures are required immediately to get the economy on the road to balance and health:

1. Congressional action is needed to minimize the disruptive effects of the energy emergency on the operations of the economy and particularly on jobs. Additional action is needed to adopt a genuine excess profits tax and to eliminate the lavish loopholes of special tax privilege for the oil industry—to assure that no group is permitted to profit from the energy emergency, while the overwhelming majority of Americans suffer inconvenience, hardship, job losses and reduced living standards. The basis for congressional legislation and administration action must be fairness, equity, and evenhandedness across the board.

2. We urge the Congress to enact legislation to provide extended unemployment insurance payments for the long-term jobless so that workers displaced by the energy crunch will not be left without any income in an economy of high unemployment.

3. We call on the Congress to appropriate sufficient funds for a large-scale public service employment program. Massive Federal grants to the States and local governments are needed to create jobs for the unemployed in providing the multitude of unmet public services required by the American people.

4. A special program of Federal grants to States, local governments, and Federal agencies is needed to accelerate short-term public works construction and repairs in areas of high unemployment.

5. The national economy requires Federal Reserve Board action to provide a sufficient expansion of money and credit, at lower interest rates, to encourage the expansion of job opportunities.

6. We urge the Congress to direct the Federal Reserve System to allocate a significant portion of available bank credit, ar reasonable interest rates, for housing and community facilities and to curtail

the flow of credit for such activities as conglomerate takeovers, land speculation, and foreign subsidiaries.

We also call on the administration to substantially increase its expenditures for middle- and low-income housing—to meet the need for adequate housing and boost homebuilding in this period of steep decline.

7. We urge the Congress to adopt the minimum wage bill the President vetoed in 1973—to raise the minimum wage and extend the Fair Labor Standards Act's coverage to millions of low-wage workers who are not protected by that law. We urge enactment of that bill without any discriminatory subminimum for youth—to provide a uniform floor for the wages of workers, regardless of age, sex, race, creed, or color.

8. The administration's so-called stabilization program has been unfair, unjust and inequitable from its inception on August 15, 1971. The rise of living costs has accelerated sharply and profits and interest rates have skyrocketed, while only workers' wages have been held down. It is better that there be no controls program whatsoever, rather than one that is inequitable and based on the perpetuation of special privileges.

9. Increases in the buying power of workers' wages and salaries are essential—to provide workers with a share in the benefits of industrial progress and to establish the foundation for improved living standards.

10. Tax justice is essential to establish a fair and equitable method for obtaining needed Federal revenue. Elimination of major loopholes in the Federal tax structure can raise as much as $30 billion of additional revenue for the expansion of public facilities and services and the reduction of the relative tax burden on middle- and low-income taxpayers.

11. Export controls on agricultural and crude material products, in short supply, should be established and maintained, until inflationary shortages are ended and pressures on the prices of such products subside. The Federal tax subsidy for export companies should be suspended for the export of commodities in which there are price-raising supply problems. Effective government regulation of the commodity markets—including margin requirements—is needed to curb excessive price-boosting speculation and profiteering.

12. We urge Congress and the administration to adopt and pursue a comprehensive policy to halt the deterioration of America's position in the world economy—to stop the export of American jobs and undermining of the Nation's industrial base, to regulate the export of American technology and capital, to eliminate the tax and other incentives that encourage U.S. companies to establish and expand their operations in foreign countries and to curb the rising tide of imports that displace American production.

The So-Called Stabilization Program

Thirty months of the Nixon administration's so-called stabilization program have proven its complete and utter failure. It has done nothing to curb inflation. As a stabilization effort, it is a fraud.

Living costs are now soaring at a yearly rate of over 9 percent—twice as fast as before the administration began its game plans, freezes, and phases. Wholesale prices are zooming six times faster.

The controls program has been unfair, unjust, and inequitable from its very beginning on August 15, 1971. Workers' wages, alone, have been held down. Profits, interest rates, and prices have skyrocketed.

Since February 1966, the AFL–CIO has reiterated its willingness to cooperate with an emergency program of economic controls on the condition that they were evenhanded, fair and equitable, with equal sacrifice from all segments of the economy.

However, the record of the past 30 months makes it perfectly clear that the Nixon administration will never institute a program of evenhanded controls, based on the principle of fairness, justice, and equal sacrifice.

There can be no justification whatsoever for a 5.5 percent standard for wage increases in the face of living costs that are rising almost twice as fast. In fact, economic justice would dictate that workers' wages reflect at least increases in the cost of living plus productivity.

The administration's control program has created economic imbalance, confusion, and chaos. This unfair and unjust program should be ended now. The present legislation, which gave the President power to control the economy, expires on April 30, 1974. It should not be renewed in any former guise.

The Government should deal directly with the basic causes of inflation and injustice, such as: tax bonanzas to business and the wealthy, which produce an inflationary lack of balance in the economy; the unregulated and frequently subsidized huge exports of farm products and crude materials in short domestic supply; the essentially unregulated commodity exchanges, where excessive speculation and profiteering have added to soaring cost and price pressures; the export of capital and technology which lead to the deterioration of America's position in the world economy and inflationary devaluations of the dollar; and high interest rates that raise costs and prices.

The Energy Crisis

The truth about the energy emergency is hidden from the public by the veil of secrecy of the giant oil companies.

Except for what the oil industry wishes to report on its operations, there is no hard information available to the public on the degree of the present oil shortage, the extent of expected shortages this year, the size and location of inventories and the size of domestic reserves. Moreover, there is no independent Government audit of the oil industry's reports.

Fifty years after a Senate committee, chaired by Senator Robert M. LaFollette, Sr., recommended legislation requiring oil companies to provide the Government with valid and comprehensive statistics concerning their operations, the Federal Government still depends on unverified industry assertions.

As a result, the public has been presented, in these past 4 months, with confusing and widely varying estimates of the energy emergency. Whatever the facts are about this situation, the American people have not been given the truth.

However, there are some clear, unfortunate facts:

A serious, long-term energy shortage has been developing, with growing dependence on foreign sources and foreign-flag shipping of crude oil and petroleum products. The development of technologies for alternative sources of energy has lagged, while the giant oil companies have emphasized crude oil and refinery investments in foreign operations, with the aid of lavish U.S. tax breaks, and they have also accumulated large percentages of U.S. coal, uranium, and oil shale reserves.

The present oil shortage is one aspect of this developing, long-run energy problem. It was brought to a head by the Arab bloc embargo of oil shipments to the United States and cutback of their crude oil output. But there were temporary and spotty shortages in the winter of 1972–73 and in the spring-early summer of 1973, before the Arab bloc's action, and more widespread shortages were expected in 1974. Prices started to shoot up months before the Arab oil bloc's action.

The United States depends on oil to meet about one-half of its energy needs, at present. The use of oil and petroleum products rose from less than 11 million barrels a day in 1963 to nearly 16.4 million barrels a day in 1972. In 1973, it was about 17 million barrels a day. By 1974, it probably will be down somewhat from the 1973 level, after accounting for voluntary conservation an Government allocation measures to reduce the use of petroleum products, as well as the impact of staggering price increases.

However, U.S. domestic production and capacity of crude oil and refined petroleum products leveled off at about 11 million barrels a day in 1970. Since 1970, with demand rising, the United States depended, to a growing degree, on imports.

There has been little new refinery capacity added in the United States in the past 5 years. The companies have been building refineries in foreign countries—geared, in part, to meet the very sharp increases in foreign demand for petroleum products, with higher prices than in the United States and wide profit margins.

This emphasis of the major oil companies on foreign investment—exploration, drilling, and crude oil production, as well as refining—has been encouraged and subsidized by lavish loopholes in the Federal tax structure. According to the Chase Manhattan Bank, the oil companies' investment outlays in foreign operations, which were about equal to their outlays for similar operations in the United States in 1963, soared to $6 billion more than in U.S. operations by 1973—60 percent greater investment expenditures in foreign countries than in the United States.

By 1973, imports of oil and petroleum products amounted to about one-third of U.S. use. They increased from 19 to 22 percent of American consumption between 1963 and 1969 and then shot up to about 33 percent in 1973.

The amount of crude oil and petroleum products imported directly from the Arab oil-producing countries has been small. In 1973, it was only about 5½ percent—mostly crude—of the total volume of approximately 17 million barrels a day of crude oil and products that were used.

However, in the past few years, the United States became increasingly dependent on imported refined petroleum products, with significant amounts refined from Arab-area crude oil, although the refineries are in the Caribbean, Europe, eastern Canada, the Bahamas, and elsewhere. The increasing amount of imports of refined products included a growing volume of products that were refined from crude oil of the Arab oil-producing areas. In 1973, the direct and indirect imports from the Arab oil-producing areas were perhaps as much as about 10 percent or possibly more of American consumption.

America's rapidly growing dependence on foreign imports of crude oil and petroleum products, since 1970, made the United States increasingly vulnerable to the blackmail of the Arab oil bloc in mid-October—to embargo shipments to the United States, cut crude oil output and sharply boost their charges on each barrel of crude from wells in the Arab oil-producing areas.

There are shortages of gasoline and other petroleum products in many areas at present, for consumers and industrial users, regardless of how much of the current emergency is actual or manipulated.

Consumers are paying more money for less gasoline and petroleum products in addition to more money for less food—a situation that is reducing living standards, with particular adverse impacts on low- and middle-income families. In the 12 months between December 1972 and December 1973, retail prices of fuel oil and gasoline skyrocketed 46.8 and 19.7 percent, respectively. In that same period, the wholesale price of crude oil rose 27.5 percent, while the price of refined petroleum products, at wholesale, jumped 125 percent—a clear indication of profiteering and further substantial price hikes for consumers.

Consumers have been affected by inconveniences and hardships, as well as staggering price increases.

Shortages have resulted in widespread plant shutdowns, production cutbacks, layoffs, curtailed working hours and economic dislocation. The number of unemployed jumped from 4.1 million or 4.6 percent of the labor force in October to 4.7 million or 5.2 percent in January and the Labor Department reported that the number of jobs eliminated by energy shortages in the past several months "was substantial."

Several thousand independent gasoline stations have been forced out of business in the past year, hitting small businesses and their employees.

The Federal tax code provides the oil companies with depletion allowances and intangible drilling cost writeoffs for their foreign operations, as well as dollar-for-dollar subtraction of foreign tax payments and royalties which are disguised as taxes from their U.S. income tax liabilities. These lucrative loopholes have encouraged and subsidized foreign oil operations and foreign-flag shipping, at the expense of American production and employment, and have enabled the giant, multinational oil companies to pay effective U.S. income tax rates as low as 2.7 percent in 1972.

The staggering price increases and tax loopholes contributed to fabulous oil company profits in 1973—much greater increases than the substantial 27 percent rise for all U.S. corporations and a greater rate of return on net worth. Profits shot up sharply in the October–December quarter of the year, despite the Arab oil bloc's embargo against the United States cutback of crude oil production and boost of charges per barrel of crude oil. Twenty-two large oil companies, according to Treasury Department estimates, reported combined after-tax profits of $9.1

billion in 1973, up 52.7 percent from 1972 and producing a 15.1-percent rate of return on net worth. Of the five largest, Exxon reported that its after-tax profits in 1973 increased 59.3 percent; Mobil's were up 46.8 percent; Texaco, 45.4 percent; Standard Oil of California, 54.2 percent; and Gulf, 79 percent.

In an article in the New York Times of February 10, 1974, Charles L. Schultze, Director of the Budget in the Johnson administration, wrote: "Price increases for oil will add about $20 billion to the consumer's energy bill in 1974. Perhaps one-third of this will flow abroad. Most of the remainder will flow into oil company profits."

No soothing rhetoric from the Nixon administration can ease the tremendous burden of hardship, job losses, reduced living standards, and general economic dislocations imposed on the American people, while the giant oil companies amass increases in their cash flow that are beyond belief.

The American people deserve a frank and open assessment of this situation from the administration. They also deserve Government measures to assure the American people that Government programs to deal with this emergency will be based fully on the principle of equality of sacrifice.

Most Americans should not be forced to sacrifice, while a few are allowed to profit excessively from the emergency. The American people can respond to difficulties now, as they have in the past, if they are provided with a candid appraisal of the situation and with fair and equitable Government measures to cope with it.

Therefore, the AFL-CIO advocates the following measures:

1. We urge the Congress to establish adequate Government machinery to provide the public with verified information on the oil industry and its operations. To assure that the companies will provide the necessary information, the Federal chartering of all major oil corporations should be required, with Federal standards for disclosure.

2. Federal legislation to provide extended unemployment insurance payments for the long-term jobless is essential. Also required are adequate Federal appropriations for a large-scale public service employment program to create jobs for the unemployed in providing needed public services. Federal funds for an accelerated public works program are needed in areas of high unemployment. Such measures can help to prevent the energy emergency from plunging the national economy into a tailspin.

3. The Government's allocation program must be based on a fair and equitable sharing of petroleum products, to minimize economic disruption and job losses. We insist that those who are placed in charge of the Government machinery established to meet the energy emergency have no hint of conflict of interest through direct or indirect connections with energy industries. Such Government machinery must contain procedures for the review of complaints from workers and their representatives.

4. We call on the Congress to eliminate immediately the depletion allowance and intangible drilling tax breaks provided the oil companies on their foreign operations, as well as the tax credit for foreign income tax payments and royalties disguised as taxes against the U.S. tax liability permitted all corporations. We also urge the phasing out of

the special loopholes the oil companies enjoy on their domestic operations.

We reiterate our demand for a genuine excess profits tax on the unconscionably high profits of corporations. The so-called "windfall profits tax" of the administration is a phony and would again penalize the consumer.

5. Proposals to deregulate natural gas at the wellhead, which would simply boost prices and profits, must be defeated.

6. The administration, in its efforts to avoid gasoline rationing because of the President's personal objections, has permitted unconscionable increases in gas prices, intolerable hardships to those unable to buy gasoline when they need it and an unfair, inequitable method of distribution which has caused long lines at gas stations in some areas while others experience no shortages whatsoever.

We dislike rationing as a way of life but equitable, evenhanded rationing is much to be preferred over rationing by taxation or high prices. Rationing by the high-price route would mean hardship for workers while the wealthy could afford all the gas they needed for pleasure without regard for need or equity.

7. We again urge the Congress to review the performance of America's oil industry in meeting the energy needs of the American people, at reasonable prices, and to determine whether or not this industry is in fact a public utility, which should be subject to interstate regulation by the Federal Government.

8. We support the investigations of the Federal Trade Commission and several State governments into the monopolistic practices, including joint ventures and interlocking relationships, of the oil and natural gas companies and their ownership of large percentages of coal, uranium, and oil shale reserves. We call on the Congress to enact legislation to require the integrated, giant oil companies to divorce the marketing of petroleum products in the United States from the production, refining, and transportation of oil. The separation of these integrated operations from the wellhead to the service station would benefit the independent refiner and marketer, as well as the consumer.

9. We again urge creation of TVA-type fuel development agencies, including oil shale, to develop and expand energy sources and provide cost yardsticks for the benefit of consumers.

10. We believe that authority for relaxation of environmental standards must be kept to the minimum necessary to meet the energy emergency. Any easing of environmental standards should be considered on a case-by-case basis and should be spelled out within specific limits.

11. The long-range energy needs of America and the stability of the national economy require immediate measures to secure America's self-sufficiency through development of varied and alternative energy sources and technologies. We strongly recommend enactment by Congress of legislation that would mobilize the Nation's scientific and technological resources through a 10-year, $20 billion crash program to expand existing and develop alternative energy resources—including advanced nuclear power technology, oil shale development, improved utilization of coal resources, electric power technology, conservation of fuels and energy, and modes of transportation. Such legislation should provide specific protections against monopolization of the development of alternative energy sources.

12. A massive rebuilding of the American-flag tanker fleet is an essential part of reducing this country's dangerous dependence on foreign petroleum imports, transported in foreign-flag vessels. We support legislation to require that 20 percent of oil imports be transported on privately owned U.S.-flag vessels, to the extent that the vessels are available at fair rates, and that this reserved share increase to 25 percent after mid-1975 and to at least 30 percent after mid-1977.

13. We once again propose the creation of a statutory Council on National Energy policy. There should be created a single national Federal energy agency which would combine various scattered Federal program functions.

Tax Justice

Events of the past few months have shockingly and graphically illustrated the inequities of the Nation's tax structure and the urgent need to close loopholes and enact an excess profits tax.

Some 80 million Americans are now going through the annual task of filing their income tax returns. The chore has always been laborious, but the tax avoidance examples set by the President of the United States, the recently resigned Vice President of the United States, and the Nation's multinational oil giants have made the task more maddening than ever before.

On December 8, 1973, the White House reluctantly published President Nixon's tax returns and provided American citizens a lurid, shocking example of how those with wealth and privilege can manipulate the tax laws to avoid their fair share and heap the burdens on those who can least afford them.

Those returns revealed:

In 1970, the President of the United States, on an income of $262,942, paid $792.81 in Federal income taxes—about the same amount a worker with three dependents paid that year if he earned $8,250.

According to the Internal Revenue Service, in 1970 there were 24 persons with incomes in the $200,000–$500,000 range who paid Federal income taxes of $800 or less. The President was among that group.

In 1971, the President paid $878.03 on a reported income of $262,385, the same as a worker with three dependents earning $9,250.

For the first 4 years of his Presidency, President Nixon's income tax payments amounted to 7 percent of his income. A working family pays about 10 percent.

Eleven days after his personal tax records were made public, the President announced a tax proposal to deal with oil company energy crisis profiteering. In his message, President Nixon stated, "It just isn't fair, for example, for millions of Americans to make sacrifices in order to deal with the crisis we confront and for a few to make excess profits or what we would call windfall profits."

What was proposed, however, was not a tax on profits—"windfall," "excess," or otherwise. It was an excise tax on barrels of crude oil—designed to be borne by the consumer and to pave the way for further oil price increases and even greater oil company profits.

The Federal income tax is a system of self-assessment. Its success depends on the honesty of the American people and the faith and confidence they have in their Government. Political scandal, gross economic mismanagement, and the clear threat of a deep recession have put confidence in Government at an alltime low.

Workers and consumers are searching for some sign that their Government is interested in their welfare and willing to act accordingly. Action on the tax front would provide such a signal.

Specifically, the AFL-CIO calls for:

Immediate enactment, retroactive to January 1, 1973, of an excess profits tax. The tax should be similar to that which was in effect during the Korean stabilization period and should contain appropriate provisions to prevent hardship cases and assure that smaller companies are not unfairly burdened.

Complete and immediate elimination of depletion allowances and intangible drilling cost writeoffs on foreign-produced oil. The current writeoffs cannot be justified on any grounds whatsoever. There is no reason to permit such writeoffs for foreign wells and there is certainly no reason for permitting such writeoffs to increase as a result of foreign oil countries' actions to increase prices.

Foreign income taxes should be treated as deductible costs of doing business rather than the present practice of crediting them dollar-for-dollar against the company's U.S. income tax liability

The foreign tax credit has encouraged oil companies, as well as other multinational firms, to invest abroad heavily at the expense of domestic operations and American jobs. This abuse which calls upon U.S. taxpayers to subsidize the oversea operations of U.S. corporations must be ended.

Eliminating the credit would end a major tax loophole. It would aid efforts to obtain independence in energy and to develop a rational trade policy for the United States. In addition, the present practice of allowing "excess" foreign tax credits to accumulate, in order to avoid payment of future U.S. income taxes, must be ended.

Immediate elimination of the tax deferral privilege which permits U.S. corporations, operating through subsidiaries, to pay no income taxes on the profits of their foreign subsidiaries until such profits are brought back home—which may be never. Such income should be taxed in the year in which it is earned just like the income of domestic corporations and American workers.

Enactment of provisions to assure that losses on foreign operations cannot be used to wash out income from sources that would otherwise be subject to U.S. taxes.

Speedy phaseout of percentage depletion and the loophole which permits the immediate writeoff of "intangible" drilling costs on domestic operations. Eliminating these loopholes would mean that the capital investment costs of oil and gas companies would be written off over a period of time—just as the investment costs of most other U.S. industries.

Finally, we call upon the 93d Congress to act as swiftly as possible to fully complete the unfinished business of achieving tax justice.

The many devices, gimmicks, and loopholes such as the half-tax on capital gains, fast depreciation and investment credit, which rig the tax structure against workers and the public interest must be ended.

The unfairly high share of the cost of Government borne by low-, moderate-, and middle-income taxpayers must be reduced. And the Federal Government must have the funds necessary to meet its responsibilities in eliminating the present gaps in essential public facilities and services and to provide for the future health and well-being of the Nation.

International Trade and Investment

The international economic structure has been seriously shaken. Normal trade patterns are being shattered. National currencies are in disarray. Nations with once-comfortable trade balances are desperately seeking larger export markets to earn the price of oil for industrial survival.

Much of the blame can be laid to the staggering price increases levied by the oil-producing nations, which have further fueled a global inflation carrying with it the possibility of worldwide recession and unemployment of crushing proportions.

These events have made the administration's so-called Trade Reform Act of 1973 totally obsolete. Its provisions bear no relation to the events of the day. Indeed, the bill passed by the House late last year and now pending before the Senate Finance Committee is worse than no bill at all. A total reexamination of U.S. trade and investment needs is in order, utilizing the realities of the seventies—particularly 1974—and abandoning the dead and unworkable dogmas of the past.

The energy crisis comes on the American economy at a time when it already is in deep distress, much of it traceable to the Nation's misguided and misapplied foreign trade and investment policies. The American worker, consumer, and businessman are all suffering from a deepening erosion of the U.S. industrial base. A tide of imports has wiped out more than a million jobs as products and whole industries have been engulfed. The export of technology and capital at reckless rates have funneled American production and productivity abroad, costing the U.S. economy not only badly needed new jobs and job opportunities but the benefits of more efficient production means. Multinational corporations, manipulating U.S. tax laws, have transferred jobs and production overseas at the expense of the American economy, costing the Nation badly needed tax revenues.

The administration's trade bill fails to address itself to these problems. In addition to granting the President unprecedented and sweeping new powers which he could use to permanently alter the structure of foreign trade and the structure of the U.S. economy, the bill contains these serious deficiencies:

It provides no specific machinery to regulate the suffocating flow of imports or to curb the export of materials in short supply at home.

It does not deal with the export of U.S. technology and capital to other parts of the world where corporations—mainly American-based multinationals—can maximize profits and minimize costs at the expense of U.S. jobs and production.

It does nothing to close the lucrative tax loopholes for multinationals which make it more profitable for them to locate and produce abroad.

It does nothing to repeal items 806.30 and 807 of the Tariff Code, which encourage U.S. firms to locate abroad and take advantage of low-wage foreign production and a special low-tariff rate on goods exported to the United States.

It fails to assure action against unfair trade practices of other nations.

It does not assure adequate U.S. responses against new and old barriers to U.S. products raised by other nations, particularly at a time when nations of the world are reexamining these barriers with an eye to greater self-protection.

It encourages the entry of goods from low-wage nations of the world at special or zero tariffs.

It insures the further heavy erosion or stunted growth of badly hit U.S. industries such as steel, apparel, chemical and allied products, rubber, shoes, stone, clay and glass, autos, aircraft, and electronics.

It ignores the fact that America's industrial base and productive strength have been weakened by current foreign trade and investment policies, and makes no provision for restoring the Nation's critically needed industrial health.

For these reasons Congress should reject the bill now before it and write a new trade bill which will contain legislative provisions that are comprehensive, flexible, and realistic.

The new legislation should:

1. Regulate U.S. imports and exports as a means of establishing an orderly flow of international trade. Specific flexible legislative machinery is needed to control imports. This flexible mechanism should also be applied as a restraint on the excessive exports of farm goods, crucial raw materials, and other products in short supply domestically. Exports, imports, and U.S. production should be linked in relation to needs for supplies, production and job opportunities in the United States.

Shortages of raw materials in the United States and new demands by countries which have those raw materials have led to new problems. Many raw material producers are requiring companies to use those raw materials within their borders. This interchange has led to a new threat to the American industrial system. As long as the United States has a policy of freedom of investment abroad and other countries have policies to seek their own rapid industrialization, the shortages of raw materials here will be used as an excuse to help industry to move abroad and further undermine production facilities within the United States.

Interwoven into this problem is the recent change in the value of each nation's money. The value of the yen, the franc, and other currencies have become lower. Many countries are competing to export as much as possible to improve their balance of trade and balance of payments. Imports from any part of the globe into the United States can shoot up very rapidly and the United States has no system to prepare for the rapid influx of any product from any part of the world.

2. Modernize trade provisions and other U.S. laws to regulate the operations of multinational corporations. Regulation of multinational firms, including banks, is necessary because these concerns are the major exporters and importers of U.S. farm products, crude materials, and manufactured products. They use U.S. tax, trade, and other laws in combination for their worldwide advantage. They export production facilities, money, and jobs, and juggle prices and credit to maximize their own worldwide company advantage. They license the newest technology for use abroad and combine in joint ventures with foreign companies and governments regardless of the impact on the U.S. need for jobs, production, or supplies.

3. Eliminate U.S. tax subsidies and other advantages for corporations investing abroad. Specifically, the tax laws should eliminate tax deferral of income earned abroad and foreign tax credits. These provisions allow U.S. corporations to pay no income on the profits of their foreign subsidiaries until these profits are brought home—if ever—and the foreign tax credit permits corporations to credit taxes paid foreign governments, dollar for dollar, against their U.S. tax liability. These provisions contribute to the export of jobs, the erosion of the U.S. industrial base, the denial of needed raw materials and components for U.S. production and job needs, and encourage foreign governments to change their rules to the disadvantage of the United States. The present provision in the tax laws allowing the establishment of Domestic International Sales Corporations (DISC's) should also be repealed. This provision now gives the largest multinational firms and banks windfall tax breaks on their exports.

The annual cost to the U.S. Treasury of these tax loopholes amounts to at least $3 billion in needed revenue.

4. Repeal flagrant incentives and subsidies to encourage U.S. firms to move or expand abroad. These are items 806.30 and 807 of the Tariff Code, which encourage the foreign production and foreign assembly of goods for sale in the United States. These provisions are used to shift production to cheap labor markets for the profits of the multinational corporations. Imports under these provisions have risen from $1 billion in 1967 to $3.4 billion in 1972; in the first 10 months of 1973, imports under these provisions were 55 percent higher than in the like period of 1972.

5. Reexamine and limit the operations of the Export-Import Bank which provides loans at interest rates much lower than those paid by American businesses, consumers, and home buyers. These loans help U.S.-based multinationals expand foreign branches and assist foreign governments, including the Soviet Union and other Communist countries, in getting America's newest production facilities. Particular emphasis should be given to the impact on U.S. jobs, and potential cost to the U.S. taxpayer.

6. Clear provisions should be written into new legislation to regulate exports of capital and new technology. Other nations are demanding only the newest kind of U.S. technological facilities and U.S. firms are licensing or producting America's newest inventions abroad with the help of U.S. and foreign governments.

7. Multilateral trade agreements with other nations, such as the textile multifiber agreements, should be administered in keeping with the flexible machinery devised to regulate imports and exports.

This flexible machinery would be a safeguard against a misunderstanding of America's intent and assure continued U.S. sovereignty over its trade ahd other domestic laws.

8. Since almost any Federal, State, or local law can be considered a nontariff barrier to trade, any legislative provision to authorize negotiation on nontariff barriers should be limited and should require specific congressional approval for the removal of any barrier, with full information about the products affected. U.S. tax laws, consumer protection laws, and other social legislation, including occupational health and safety standards, should be barred from such negotiations.

9. New provisions are needed to speed and assure action against foreign dumping of products on the U.S. market—the sale of these goods at a price artificially lower than in home countries—or other subsidized imports into the United States. These provisions should emphasize U.S. producer and worker needs and rights to participate in proceedings.

10. Clear labeling on imports of products and components to mark the country of origin of the product and the components within it is needed. Advertisers also should be required to designate the country of origin of products they handle. All consumer protection legislation should be strictly enforced on imports.

11. Trade with Communist countries should not be viewed as ordinary commercial exchange. The United States should end the extension of low-interest loans and insurance of private loans by U.S. Government agencies to Communist countries. Senate legislation must contain the restrictions on Soviet trade written into the House bill over the opposition of the administration.

12. The need for improved U.S. statistics on imports, exports, and production has become urgent. Neither the U.S. Government nor interested U.S. producers and workers can obtain adequate statistics in sufficient detail on the impact of imports or exports of industrial commodities. A comprehensive system of reporting on investment abroad, licensing of production, and other technology flows is needed. Firms which operate within the United States should be required to segment their United States and foreign production in reporting to Government agencies.

The energy crisis has demonstrated that overdependency on foreign sources of any material can be costly and perhaps fatal. It also has demonstrated that nations, when faced with a choice, are quick to act in their own self-interest. And it has graphically demonstrated that multinational corporations hold corporate allegiance above national allegiance. New trade legislation must recognize these factors.

AMERICAN LIFE INSURANCE ASSOCIATION

This statement is submitted on behalf of the American Life Insurance Association, a national trade association with a membership of 365 life insurance companies which account for over 90 percent of the legal reserve life insurance in force in the United States. The total assets of the life insurance business presently aggregate over $253 billion which represents the savings that have been entrusted to our companies by millions of policyholders. We welcome the invitation of the Joint Economic Committee to present our views on the economic issues that affect our policyholders and confront the Nation.

The Need To Control Inflation

In our view, the foremost economic problem confronting the American public today is inflation. Prices have soared in recent months by amounts that would have been unthinkable only a short time ago. Purchasing power of wages and salaries throughout the Nation has been sharply eroded by an accelerating advance of consumer prices. During the past 5 years the Consumer Price Index has risen by more than 30 percent, despite the presence of price controls since 1971. In the past 12 months alone, consumer prices have increased by 9.4 percent.

A primary concern within our business is the need to conserve the purchasing power of the billions of dollars of insurance protection and savings accumulated through the purchase of life insurance. To protect the economic value of these funds over future years, and to avoid the disruptive effect which inflation can have on everyday household spending, it is imperative that first priority be given to economic policies that will bring down the inflation rate to tolerable levels.

It is a fundamental principle of our economic system that rising prices are caused by an imbalance between demand and supply. In the past, excess demand typically has been the factor that forced price levels higher, especially during periods of rapid economic expansion. We are now faced with a new situation, unique in the period since World War II, in which supply shortfalls and actual declines in the availability of some products are the basic cause of the highest inflation rates in recent history. These shortages, most notably in petroleum and other energy sources, have also held down output and employment. Dislocations in the automotive industry, domestic airline schedules, and travel-related businesses have been well publicized, but other sectors are also experiencing difficulty in obtaining essential materials, with resulting bottlenecks and production slowdowns.

Under present conditions it is essential that we scrupulously avoid policies that would stimulate total demand and drive prices still higher. Instead, we must concentrate on measures to improve supplies and increase output to achieve a better balance with demand and reduce the pressure on prices. The policies pursued in this critical year will determine our success or failure in holding back inflation in 1975 and beyond.

Outlook for Business Activity in 1974

In appraising the outlook for the economy, the Council of Economic Advisers (CEA) has projected a gross national product of about $1,390 billion in 1974, an increase of about 8 percent over 1973. According to the CEA, most of the rise will be attributable to inflation at the rate of 7 percent, as measured by the GNP price deflator. In our view, the inflation rate in 1974 is more likely to reach 7½ percent, with the consumer price index advancing even more rapidly—a most disheartening prospect for the American public. In the final quarter of 1973, the GNP inflation rate soared to an 8.8-percent annual rate, with a strong likelihood of a similar percentage in the first quarter of 1974. If we are to succeed in lowering the pace of inflation during the balance of this year, it is of the utmost importance that we avoid stimulative policies that will add to upward price pressures, in the face of supply-induced constraints on the output of goods and services.

The energy shortage, dramatized by the Arab oil embargo, already has produced layoffs and other side effects in a number of industries. It may never be possible to trace the full effects of energy shortages radiating through almost every sector of economic activity, but the overall impact clearly has been to intensify the economic slowdown.

In projecting the most probable path for economic activity in 1974, the CEA expects real output to be approximately flat and perhaps declining for an interval in the first half of the year, followed by a rise "by somewhat more than the normal trend rate" during the second half. In our view, the economy faces a serious business setback in the months immediately ahead, primarily induced by shortages and adjustments to reduced supplies of petroleum. We are less optimistic than the Council of Economic Advisers about the strength of recovery in the second half, which will depend importantly on the future availability of oil from foreign sources.

Federal Budgetary Policy

An important key to the course of inflation in 1974 and 1975 will be the role of Federal budgetary policy in stimulating or restraining demand. In the Budget Message of the President for the fiscal year ending June 1975, total Federal receipts are estimated at $295 billion with proposed budget outlays of $304.4 billion, leaving a projected deficit of $9.4 billion. The proposed budget outlays represent an 11-percent increase over fiscal 1974, which in turn is estimated to show an 11-percent increase over fiscal 1973.

Repeated increases of this magnitude are, in our view, a clear threat to the objective of curbing inflationary pressures. We would urge that the $304.4 billion spending total proposed for fiscal 1975 should be considered by the Congress an as upper limit, rather than a base figure on which further spending may be added by new legislative programs. A preferable course of action would be for the Congress to examine the $304.4 billion total with a critical eye, to disclose instances of excessive spending and hopefully reduce outlays in areas of lesser current priority.

We are particularly alarmed over recent statements by administration spokesmen that they are prepared to increase Federal spending beyond the $304.4 billion figure in order to support the economy. In the present situation, efforts to speed up Federal payments or slow tax collections from the public at large would clearly aggravate the present high rate of inflation by increasing demand without adding to supply. We believe strongly that budgetary policy should act as a restraining influence until it becomes possible for the supply of petroleum and other critically short commodities to reach a better balance with the present level of demand. In a traditional business downturn where insufficient demand is the basic cause of declining output, fiscal stimulus through budget deficits may serve to restore economic growth. But larger deficits are not an appropriate corrective for a downturn created by insufficient supplies of essential raw materials such as petroleum.

The budget message presents an alternative "full employment" budget for fiscal 1975, showing federal receipts $16 billion higher and Federal outlays about $1 billion lower than in the actual budget. This calculation attempts to estimate the level of receipts if the unemployment rate were at 4 percent, rather than the higher percentage actually expected in 1974. On this basis, the "full employment budget" shows a surplus of $8 billion rather than the $9.4 billion deficit actually projected for fiscal 1975 and it is argued that the economic impact of the budget is one of "moderate restraint."

In our view, the use of a 4-percent unemployment assumption as a measure of "full employment" is unrealistic in our present economy. As the budget message notes, a 4-percent rate today would mean much tighter labor markets than ten years ago, in view of the changing composition of the labor force. The Council of Economic Advisers, in a special analysis of unemployment statistics in the economic report, states that a condition of "maximum employment" was approximately met in 1973, when the average unemployment rate was 4.9 percent rather than 4 percent. We would recommend that analysis of budgetary effects which rely upon outdated and unrealistic assumptions of "full employment" should be discarded. If a more realistic unemployment assumption were used, the fiscal 1975 full employment budget would be in deficit, thus exerting an expansionary influence rather than moderate restraint. Accordingly, any additions by the Congress to the $304.4 billion spending total presently projected would heighten the fiscal stimulus and further aggravate inflationary pressures.

The budget message also refers to the growing percentage of projected outlays that are "virtually uncontrollable" by reason of prior budgetary commitments and legislative decisions. The ratio of such "uncontrollables" has moved unrelentingly higher, from 59 percent in 1967 to about 74 percent in fiscal 1975. This development should be a matter of deep concern to the Congress. Federal spending can be described as "uncontrollable" only in the short run of a year or two. In the longer run, the responsibility for these locked-in spending commitments lies squarely and directly with decisions made by the Congress in earlier years. All too often, programs have been authorized with small beginnings which rise in an irreversible pattern to major dollar outlays within 3 to 5 years. We are presently burdened with far too many spending commitments which have seriously reduced the flexibility needed for effective budget control. The presence of these commitments also curbs our ability to undertake new initiatives that may have a much higher current priority than the "hang-over" programs now described as "uncontrollable."

We have been gratified to witness during the past year a growing awareness within the Congress of the need to coordinate appropriations and determine funding priorities within an overall budget strategy. After several months of thoughtful study by the Joint Study Com mittee on Budget Control established in late 1972, and further review of the problem within the House and Senate, new legislation providing for improved congressional control over budgetary outlays and receipts has passed the House (H.R. 7130) and is soon to be considered by the Senate (S. 1541). This legislation could have far-reaching consequences in achieving a better management of Federal budgetary policy and its effects upon inflation and the economy. We strongly support the objectives of this legislation and urge its speedy enactment.

Federal Reserve Monetary Policy

Monetary policy represents the other major means by which Government policy affects total demand in the economy, either by encouraging or restraining the growth of money and credit. As in the case of fiscal policy, we believe that monetary policy should exert a restraining influence on the expansion of money and credit during 1974 to avoid aggravating inflationary pressures. We believe that the primary objective of monetary policy should be to check the high rate of inflation. In our view, the growth of the money supply in 1974 should be held below the rates of expansion permitted in the last 2 years. We are in agreement with the statement by Federal Reserve Chairman Arthur F. Burns before the Committee on Appropriations of the House of Representatives on February 21, 1974, when he said:

> In the current economic slowdown, the task of monetary policy will not be the same as in a classical business recession, when a considerable easing in the supply of money and credit can be expected to provide the financial basis for the subsequent recovery. This year, our nation's capacity to produce may actually decline, or at best rise at an abnormally low rate. A great deal of caution will therefore be needed in framing monetary policy. An easier monetary policy can be only a marginally constructive influence when economic activity slows because of a shortage of oil.

Our financial markets have become extremely sensitive to both the rate of inflation and the rate at which the money supply is expanding. A more rapid rate of monetary expansion is now seen as the forerunner of greater demand pressures and higher inflation. In turn, a rise in inflationary expectations not only reduces the inflow of savings to thrift institutions and curbs the amounts available for long-term financing, but also raises the "inflation premium" on bond and mortgage rates in the financial markets. Thus, high rates of monetary expansion have led ultimately to higher long-term interest rates on home mortgages, corporate bonds, and Federal securities by reason of the inflation factor in the saving-investment process.

There are pressing needs ahead to expand plant facilities and capital equipment in order to improve capacity and increase the supplies of goods. Capital formation of this kind relies on private savings flows in the last analysis. Ongoing inflation at high rates will damage incentives to save and retard the growth of productive capacity. Thus, long-run considerations of economic growth in output and employment support the view that monetary policy should not seek to counter the current slowdown through an easier credit policy that would aggravate inflation. Our first objective should be to bring inflation under control in order to permit a resumption of balanced growth.

FUTURE OF WAGE AND PRICE CONTROLS

Serious misgivings have developed since last summer about the effectiveness of controls under phase 4, along with a growing belief that such controls have become counterproductive. In some instances, price ceilings have served to limit the supply of goods reaching the market, leading to shortages which are difficult to correct in a brief period and ultimately bringing upward pressure on prices. We believe that the present system of wage-price controls has outlived its usefulness and we therefore recommend that the Economic Stabilization Act be allowed to expire on its termination date of April 30, 1974.

At the same time, we recognize the possibility of opportunistic developments in the wage and price area once the controls are allowed to expire. The administration has proposed that the Cost of Living Council be continued in a "watchdog" capacity to monitor future wage negotiations and price adjustments and to hold public hearings on developments which threaten further inflation. We support this proposal as a necessary followup during the months immediately after the expiration of formal controls.

For the longer term, there is a strong likelihood that inflationary forces will remain active in the economy for a considerable period of time and a less temporary approach will be needed to guard against inflationary influences. In early 1971, prior to the imposition of mandatory wage-price controls, the life insurance business recommended to the Joint Economic Committee the establishment of a continuing independent governmental Commission on Inflation to study the causes, the consequences, and the remedies for inflation, and to report regularly or on an ad hoc basis to the Congress and to the public. This proposal was made in the belief that the public at large, as well as the Congress and the executive branch, should be kept closely informed of those decisions or actions, public or private, which lead to increases in wage costs in excess of productivity growth, and in other costs and prices. With the likely expiration of mandatory controls within the next few weeks, we again recommend strongly the establishment of a continuing Commission on Inflation.

The Commission, though lacking enforcement powers, would study policies and actions of both public and private organizations from the single point of view of their implications for inflation. Such a Commission should not be called upon to balance various policy goals as the operating departments and agencies of Government must do. Rather, it should conduct such studies as it considers most fruitful, and issue whatever reports it deems appropriate, from the standpoint of preventing inflation.

While inflation in the nature of things is a concern of many governmental agencies, including particularly the Council of Economic Advisers, the Treasury, and the Federal Reserve Board, there is presently no agency with a responsibility to study inflation and publicize actions, policies, and developments that are clearly inflationary in nature. Such a Commission as we are proposing, if its members have sufficient stature and do their job, could have a far-reaching impact on both public and private actions. A high level Commission of distinguished members would serve as an effective supplement to sound budgetary and monetary policies without which inflation cannot be brought under control.

Concluding Comments

With inflation running at the highest rates in several decades, there can be little doubt that policies to control inflation deserve the highest priority today. The corrosive effects of accelerating prices have already been felt by the American wage earner through a reduction in the purchasing power of his income and the future value of his savings. Expectations of future inflation have escalated sharply within the past year, now that we have witnessed price increases well beyond the outer limits we once thought possible. Recent talk about "double digit" inflation rates is no longer considered outlandish and the experience of many foreign countries demonstrates that this possibility cannot be ignored.

These prospects carry the dangers of a self-fulfilling prophesy in which current decisions as to spending and saving, borrowing and investing, are governed by an overriding concern about rising prices. On the wage front, anticipation of higher consumer prices, piled on top of the price increases of recent months, could bring on more forceful wage demands and a renewed surge of "cost push" inflation later this year and into 1975. This factor alone argues strongly for policies to achieve a lower inflation rate and forestall a cumulative upward spiral of wages, costs, and prices.

There is a natural concern about the recent rise in unemployment, which has been concentrated in those areas and industries affected by petroleum shortages for which political factors, rather than economic forces, have been responsible. Hopefully, the Arab oil embargo will be lifted within a fairly short time period. But more expansive budget policies or a faster growth in the money supply will not restore jobs to workers whose layoffs resulted from the oil shortage. While hardships for many have been created by the energy-induced slowdown, even greater hardships for the entire American public would result from further inflation prompted by stimulative policies. The path to fuller employment and a resumption of stable growth lies in economic policies designed to hold back demand until critical shortages can be overcome and a better demand-supply balance can be achieved.

We appreciate this opportunity to present our views on these critical issues.

ANDREW F. BRIMMER*

From time to time, I have attempted to keep abreast of economic trends and developments affecting the black community along with other major groups in the national economy. Statistics on employment for 1973 as a whole have recently become available. On the basis of these data, I have just completed an assessment of the broad experience of blacks in the labor market last year. The following conclusions emerged:

The demand for labor remained strong throughout most of 1973; and (despite the reduced growth of output after the first quarter), labor markets tightened as total employment expanded rapidly and unemployment declined moderately.

In this environment, the employment situation among blacks improved markedly in 1973—after several years of disappointing performance. Employment rose substantially during the year, at a faster pace than job growth in the economy as a whole.

On the other hand, the black civilian labor force also expanded rapidly. The labor force participation rate for blacks edged up in 1973 (after remaining unchanged throughout 1972). The gain last year reflected an increased willingness on the part of blacks to enter the labor market as a result of the improved employment prospects.

This expansion of the black labor force moderated declines in unemployment. After dropping sharply early in the winter, the jobless rate for black workers was little changed during the remainder of the year.

Black workers also raised their share of jobs in higher skilled occupations and in high-wage industries in 1973. There was also some decline in their participation in low wage sectors.

These conclusions are amplified in the following discussion.

CIVILIAN LABOR FORCE

The black civilian labor force expanded rapidly in 1973 due to an increase in participation as well as continued large increases in the working age population (see table 1, attached). As one would expect, adults accounted for the great bulk of the labor force growth as participation rates edged up slightly and population expanded rapidly. However, teenagers continued to enter the market in large numbers, and their labor force increased significantly. Their white counterparts also recorded substantial growth.

Last year was the first year the overall participation rate for blacks has increased since the mid-1960's. Most of the advance was attributable to an increase in participation among black women and young

*Member, Board of Governors of the Federal Reserve System. I am grateful to Ms. Diane W. Sower of the Board's staff for assistance in the preparation of this report. However, the views expressed are my own and should not be attributed to the staff. Nor should they be attributed to my colleagues on the Board.

workers. Among adult men 20 years or older, the rate was basically unchanged. Yet, this represented a departure from the sharp drops that have been evident in recent years.

TABLE 1.—PARTICIPATION RATES, BY AGE AND RACE, 1963-73, SEASONALLY ADJUSTED

	Black [1]				White				Black as percentage of white			
	Total	Male 20 and over	Female 20 and over	Both 16–19	Total	Male 20 and over	Female 20 and over	Both 16–19	Total	Male 20 and over	Female 20 and over	Both 16–19
1963	63.0	83.9	49.9	41.7	58.2	84.4	37.0	45.7	108.2	99.4	134.9	91.2
1964	63.1	84.1	50.6	40.4	58.2	84.2	37.5	45.0	108.4	99.9	134.9	89.8
1965	62.9	83.7	51.1	40.1	58.4	83.9	38.0	46.5	107.7	99.8	134.5	86.2
1966	63.0	83.3	51.6	42.2	58.7	83.6	38.8	49.1	107.3	99.6	133.0	85.9
1967	62.8	82.9	51.6	42.9	59.2	83.5	39.8	49.2	106.1	99.3	129.6	87.2
1968	62.2	82.2	51.4	41.9	59.3	83.2	40.4	49.3	104.9	98.8	127.2	85.0
1969	62.1	81.4	51.9	41.9	59.9	83.0	41.5	50.6	103.7	98.1	125.1	82.8
1970	61.8	81.4	51.7	40.5	60.2	82.8	42.2	51.4	102.7	98.3	122.5	78.8
1971	60.9	79.9	51.8	37.5	60.1	82.3	42.3	51.6	101.3	97.1	122.4	72.7
1972	60.0	78.4	51.1	39.0	60.4	82.0	42.7	54.3	99.3	95.6	119.7	71.8
1973	60.3	78.5	51.3	40.2	60.9	81.7	43.5	56.2	99.0	96.1	117.9	71.5

[1] Negro and other races.

Source: U.S. Department of Labor, Bureau of Labor Statistics.

Participation was up for young black men 18 to 24, but it continued to edge down among men 25 to 44 years old (table 2). Among white men, participation rates rose in the younger age groups—16 to 24—and for men 25 to 34 years but edged down in the older age groups. The rapid rise in labor force participation among white women continued in 1973 with all of the gain accounted for by younger women and those in the 25 to 44 age groups. Participation of black women also increased, particularly in the younger age range.

In 1973, there were 10 million black workers holding jobs or looking for employment (table 3). They represented 11.4 percent of the labor force—a slightly larger fraction than in the previous year. Over the four quarters of 1973, the total civilian labor force rose by 2.7 million (to 88.7 million). This gain was composed of an increase of 330,000 for blacks and 2.4 million for whites. Thus, blacks accounted about 12 percent of the total expansion.[1]

TABLE 2.—CIVILIAN LABOR FORCE PARTICIPATION RATES BY DETAILED AGE AND RACE

	16 to 17	18 to 19	20 to 24	25 to 34	35 to 44	45 to 54	55 to 64	65+
Black male: [1]								
1960	45.6	71.6	90.4	96.2	95.5	92.3	82.5	31.2
1961	42.5	70.5	89.7	95.9	94.8	92.3	81.6	29.4
1962	40.2	68.8	89.3	95.3	94.5	92.2	81.5	27.2
1963	37.2	69.1	88.6	94.9	94.9	91.1	82.5	27.6
1964	37.3	67.2	89.4	95.9	94.4	91.6	80.6	29.6
1965	39.3	66.7	89.8	95.7	94.2	92.0	78.8	27.9
1966	41.1	63.7	89.9	95.5	91.1	90.7	81.1	25.6
1967	41.2	62.7	87.2	95.5	93.6	91.3	79.3	27.2
1968	37.9	63.3	85.0	95.0	93.4	90.1	79.6	26.6
1969	37.7	63.2	84.4	94.0	92.7	89.5	77.9	26.1
1970	34.8	61.8	83.5	93.7	93.2	88.2	79.2	27.4
1971	32.4	58.9	81.5	92.9	92.0	86.9	77.8	24.5
1972	34.1	60.1	81.5	92.7	91.4	86.1	73.6	23.6
1973	32.4	61.1	83.6	91.8	90.9	87.5	69.4	22.4

See footnotes at end of table, p. 1005.

[1] The changes noted throughout the text cannot be derived directly from the data in tables 3 and 4. The changes indicated for 1973 have been adjusted to reflect the change in population control made by the Bureau of Labor Statistics and introduced in March 1973. For an explanation of the adjustments see "Employment and Earnings," April 1973.

TABLE 2.—CIVILIAN LABOR FORCE PARTICIPATION RATES BY DETAILED AGE AND RACE—Continued

	16 to 17	18 to 19	20 to 24	25 to 34	35 to 44	45 to 54	55 to 64	65+
Black female:								
1960	22.1	44.3	48.8	49.7	59.8	60.5	47.3	12.8
1961	21.6	44.6	47.7	51.2	60.5	61.1	45.2	13.1
1962	21.0	45.5	48.6	52.0	59.7	60.5	46.1	12.2
1963	21.5	44.9	49.2	53.3	59.4	60.6	47.3	11.8
1964	19.5	46.5	53.6	52.8	58.4	62.3	48.4	12.7
1965	20.5	40.0	55.2	54.0	59.9	60.2	48.9	12.9
1966	23.6	44.0	54.5	54.9	60.9	61.0	49.1	13.0
1967	22.8	48.7	54.9	57.5	60.8	59.6	47.1	13.0
1968	23.3	46.9	58.4	56.6	59.3	59.8	47.0	11.9
1969	24.4	45.4	58.6	57.8	59.5	60.8	47.5	11.9
1970	24.3	44.7	57.7	57.6	59.9	60.2	47.1	12.2
1971	21.9	41.4	56.0	59.2	61.0	59.4	47.1	11.5
1972	21.4	43.9	56.7	60.1	60.7	57.3	43.9	12.8
1973	23.9	45.1	58.0	62.7	61.6	56.1	44.7	11.4
White male:								
1960	46.0	69.0	87.8	97.7	97.9	96.1	87.2	33.3
1961	44.3	66.2	87.6	97.7	97.9	95.9	87.8	31.9
1962	42.9	66.4	86.5	97.4	97.9	96.0	86.7	30.6
1963	42.4	67.8	85.8	97.4	97.8	96.2	86.6	28.4
1964	43.5	66.6	85.7	97.5	97.6	96.1	86.1	27.9
1965	44.6	65.8	85.3	97.4	97.7	95.9	85.2	27.9
1966	47.1	65.4	84.4	97.5	97.6	95.8	84.9	27.2
1967	47.9	66.1	84.0	97.5	97.7	95.6	84.9	27.1
1968	47.7	65.7	82.4	97.2	97.6	95.4	84.7	27.3
1969	48.8	66.3	82.6	97.0	97.4	95.1	83.9	27.3
1970	48.9	67.4	83.3	96.7	97.3	94.9	83.3	26.7
1971	49.2	67.8	83.2	96.3	97.0	94.7	82.6	25.6
1972	50.2	71.1	84.3	96.0	97.0	94.0	81.2	24.4
1973	52.7	72.3	85.8	96.3	96.8	93.5	79.0	22.8
White female:								
1960	30.0	51.9	45.7	34.1	41.5	48.6	36.2	10.6
1961	29.4	51.9	46.9	34.3	41.8	48.9	37.2	10.5
1962	27.9	51.6	47.1	34.1	42.2	48.9	38.0	9.8
1963	27.9	51.3	47.3	34.8	43.1	49.5	38.9	9.4
1964	28.5	49.6	48.8	35.0	43.3	50.2	39.4	9.9
1965	28.7	50.6	49.2	36.3	44.3	49.9	40.3	9.7
1966	31.8	53.1	51.0	37.7	45.0	50.6	41.1	9.4
1967	32.3	52.7	53.1	39.7	46.4	50.9	41.9	9.3
1968	33.0	53.3	54.0	40.6	47.5	51.5	42.0	9.4
1969	35.2	54.6	56.4	41.7	48.6	53.0	42.6	9.7
1970	36.6	55.0	57.7	43.2	49.9	53.7	42.6	9.5
1971	36.4	55.0	57.9	43.6	50.2	53.7	42.5	9.3
1972	39.3	57.4	59.4	45.8	50.7	53.4	42.0	9.0
1973	41.7	58.9	61.6	48.5	52.2	53.4	40.8	8.7

[1] Negro and other races.

Source: U.S. Department of Labor, Bureau of Labor Statistics.

TABLE 3.—CIVILIAN LABOR FORCE,[1] 1963–73, SEASONALLY ADJUSTED

	Black[2]				White			
	Total	Male 20 and over	Female 20 and over	Both 16 to 19	Total	Male 20 and over	Female 20 and over	Both 16 to 19
1963	8,003	4,381	3,042	580	63,830	39,841	19,430	4,559
1964	8,170	4,427	3,138	605	64,621	40,178	19,959	4,784
1965	8,321	4,457	3,219	645	66,137	40,401	20,469	5,267
1966	8,499	4,467	3,301	731	67,276	40,319	21,130	5,827
1967	8,649	4,503	3,375	771	68,699	40,850	22,100	5,749
1968	8,759	4,535	3,446	778	69,976	41,317	22,820	5,839
1969	8,955	4,579	3,574	802	71,778	41,772	23,838	6,168
1970	9,198	4,726	3,664	808	73,520	42,564	24,616	6,440
1971	9,322	4,773	3,769	781	74,790	43,088	25,030	6,672
1972	9,584	4,847	3,888	849	76,958	43,961	25,822	7,175
1973	10,075	5,049	4,066	909	78,689	44,490	26,647	7,552
1972:								
Q1	9,500	4,789	3,875	836	76,316	43,635	25,577	7,104
Q2	9,545	4,847	3,867	836	76,759	43,871	25,767	7,121
Q3	9,587	4,868	3,862	857	77,276	44,090	26,023	7,163
Q4	9,690	4,879	3,950	861	77,459	44,213	25,920	7,326
1973:								
Q1	9,820	4,927	4,019	874	77,792	44,265	26,132	7,395
Q2	9,946	5,035	3,990	921	78,510	44,352	26,632	7,526
Q3	10,105	5,076	4,105	924	78,856	44,511	26,879	7,466
Q4	10,232	5,158	4,154	920	79,648	44,815	26,959	7,874

[1] Thousands of persons age 16 and over.
[2] Negro and other races.

Source: U.S. Department of Labor, Bureau of Labor Statistics.

TABLE 4.—EMPLOYMENT,[1] 1963-73, SEASONALLY ADJUSTED

	Black[2]				White			
	Totals	Male 20 and over	Female 20 and over	Both 16 to 19	Totals	Male 20 and over	Female 20 and over	Both 16 to 19
1963	1,740	3,979	2,757	404	60,622	38,272	18,499	3,850
1964	7,383	4,088	2,855	440	61,922	38,799	19,047	4,076
1965	7,643	4,190	2,979	474	63,445	39,232	19,652	4,562
1966	7,877	4,249	3,033	545	65,021	39,418	20,427	5,176
1967	8,011	4,309	3,134	568	66,361	39,984	21,263	5,113
1968	8,169	4,356	3,229	584	67,750	40,503	22,052	5,195
1969	8,384	4,416	3,365	609	69,518	40,978	23,032	5,508
1970	8,446	4,461	3,412	573	70,183	41,093	23,521	5,569
1971	8,403	4,428	3,442	533	70,716	41,347	23,707	5,662
1972	8,628	4,518	3,546	564	73,074	42,362	24,554	6,158
1973	9,131	4,762	3,734	634	75,278	43,183	25,494	6,602
1972:								
Q1	8,484	4,438	3,524	522	72,309	41,962	24,332	6,015
Q2	8,624	4,507	3,544	573	72,772	42,212	24,439	6,121
Q3	8,546	4,533	3,525	588	73,399	42,542	24,721	6,136
Q4	8,733	4,590	3,588	555	73,810	42,720	24,725	6,365
1973:								
Q1	8,940	4,649	3,680	611	74,270	42,873	24,945	6,452
Q2	9,047	4,729	3,680	638	75,062	43,015	25,490	6,557
Q3	9,191	4,786	3,773	632	75,559	43,281	25,727	6,551
Q4	9,348	4,884	3,805	659	76,287	43,582	25,828	6,877

[1] Thousands of persons age 16 and over.
[2] Negro and other races.

Source: U.S. Department of Labor, Bureau of Labor Statistics.

EMPLOYMENT

Overall employment rose substantially in 1973, increasing 3.7 percent over the year after posting a healthy 2.9 percent gain the previous year (table 4). Jobs among blacks increased by 400,000 to a total of 9.3 million, an increase of 4.6 percent. Gains occurred among both adults and teenagers, who had recorded an employment decline the year before. Black men registered large job gains which probably reflected the strong performance of the manufacturing sector in 1973. Factory employment—hard hit by the 1970 recession—did not start to recover until late 1971, after which it rose steadily in the subsequent 2 years. The 1973 rise was more than twice that registered the year before. Much of the gain was concentrated in the metal and metal using industries where black adult men are heavily represented. Employment also expanded considerably among adult white men, but their 2.2 percent rate of increase was well below the 3.8 percent gain of their black counterparts.

Employment opportunities for black women also picked up during the year as the number of jobs held by them rose to 3.8 million, for an increase of 3.7 percent. The number of white women holding jobs expanded by 4.7 percent over the year. Teenage employment also rose substantially. Among young black workers an 18 percent gain pushed teenage employment above levels recorded in 1969. The number of jobs held by them had remained substantially below these peak levels for 3 years. Young white workers also fared well in the tightening labor market as their employment increased by about 8 percent. This strong employment picture probably reflected the continued expansion of the service-producing industries where many women and young workers are concentrated, many in part-time jobs. These industries added nearly 1.8 million workers to their payrolls in 1973 with the largest gains occurring in the trade and the service industry.

Unemployment

Joblessness among blacks declined moderately during 1973, after rising in the 2 previous years. At the end of 1973, about 884,000 blacks were unemployed, compared with 957,000 a year earlier (table 5). This represented a decline in joblessness by roughly 7½ percent for blacks as a group. Among black men, the decline was 5 percent; it was 3½ percent among black women, and 15 percent among black teenagers. These decreases in joblessness were smaller than the decreases experienced by whites overall. For the latter group as a whole, the drop was 8½ percent; it was 17 percent for white men; 5½ percent for white women; but there was about a 10-percent increase for white teenagers.

The unemployment rates among blacks declined moderately during 1973 after rising in the 3 previous years. The largest relative improvement occurred among black teenagers whose unemployment rate dropped to about 30 percent after averaging over 33 percent in 1972 (table 6). At the same time, unemployment increased over the four quarters of 1973 among white teenagers as their labor force growth outstripped employment expansion. However, their unemployment rate—at about 12.6 for the year as a whole—was less than half the jobless rate of black youth. After averaging about 6.8 percent in 1972, the unemployment rate for adult black men edged down during 1973 to about 5.7 percent, the lowest since the 1970 recession. Unemployment among adult white men also declined significantly, and their jobless rate decreased from the 3.6 percent level of 1972 to about 2.6 percent in 1973. Joblessness among adult women of both races declined moderately; the unemployment rate for black women averaged 8.2 percent and for white women, about 4.3 percent in 1973.

TABLE 5.—UNEMPLOYMENT,[1] 1963–73, SEASONALLY ADJUSTED

	Black [2]				White				Black as percentage of total		
	Total	Male 20 and over	Female 20 and over	Both 16 to 19	Total	Male 20 and over	Female 20 and over	Both 16 to 19	Civilian labor force	Unemployment	Ratio percent unemployment to percent labor force
1963	863	402	285	176	3,208	1,569	931	708	11.1	21.2	1.91
1964	787	339	283	165	2,999	1,379	912	708	11.2	20.8	1.86
1965	678	267	240	171	2,691	1,169	817	705	11.2	20.1	1.80
1966	622	218	218	186	2,255	901	703	651	11.2	21.6	1.93
1967	638	194	241	203	2,338	866	837	635	11.2	21.4	1.91
1968	596	179	217	194	2,226	814	768	644	11.1	21.0	1.89
1969	571	169	209	193	2,260	794	806	660	11.1	20.2	1.82
1970	752	265	252	235	3,337	1,371	1,095	871	11.1	18.4	1.66
1971	919	345	326	248	4,074	1,741	1,324	1,010	11.1	18.4	1.66
1972	956	329	342	284	3,884	1,599	1,268	1,017	11.1	19.8	1.78
1973	894	287	332	275	3,411	1,307	1,153	950	11.3	20.8	1.84
1972:											
Q1	1,016	351	351	314	4,007	1,673	1,245	1,089	11.1	20.2	1.82
Q2	921	335	323	263	3,987	1,659	1,328	1,000	11.1	18.8	1.69
Q3	941	335	337	269	3,877	1,548	1,302	1,028	11.0	19.5	1.77
Q4	957	289	362	306	3,649	1,493	1,195	961	11.1	20.8	1.87
1973:											
Q1	880	278	339	263	3,522	1,392	1,187	943	11.2	20.0	1.79
Q2	899	306	310	283	3,448	1,337	1,142	969	11.2	20.7	1.85
Q3	914	290	332	292	3,297	1,230	1,152	915	11.4	21.7	1.90
Q4	884	274	349	261	3,361	1,233	1,131	997	11.4	20.8	1.82

[1] Thousands of persons age 16 and over.
[2] Negro and other races.

Source: U.S. Department of Labor, Bureau of Labor Statistics.

TABLE 6.—UNEMPLOYMENT RATE, 1963-73, SEASONALLY ADJUSTED

	Black[1]				White				Black as percentage of white			
	Total	Male 20 and over	Female 20 and over	Both 16 to 19	Total	Male 20 and over	Female 20 and over	Both 16 to 19	Total	Male 20 and over	Female 20 and over	Both 16 to 19
1963	10.8	9.2	9.4	30.3	5.0	3.9	4.8	15.5	2.04	2.29	1.80	1.80
1964	9.6	7.7	9.0	27.3	4.6	3.4	4.6	14.8	2.09	2.26	1.96	1.84
1965	8.1	6.0	7.5	26.5	4.1	2.9	4.0	13.4	1.98	2.07	1.88	1.98
1966	7.3	4.9	6.6	25.4	3.4	2.2	3.3	11.2	2.15	2.23	2.00	2.27
1967	7.4	4.3	7.1	26.3	3.4	2.1	3.8	11.0	2.18	2.04	1.89	2.39
1968	6.7	3.9	6.3	24.9	3.2	2.0	3.4	11.0	2.09	1.95	1.85	2.26
1969	6.4	3.7	5.8	24.1	3.1	1.9	3.4	10.7	2.06	1.95	1.70	2.25
1970	8.2	5.6	6.9	29.1	4.5	3.2	4.4	13.5	1.82	1.75	1.57	2.16
1971	9.9	7.2	8.7	31.7	5.4	4.0	5.3	15.1	1.83	1.80	1.64	2.10
1972	10.0	6.8	8.8	33.5	5.0	3.6	4.9	14.2	1.96	1.88	1.80	2.38
1973	8.9	5.7	8.2	30.2	4.3	2.9	4.3	12.6	2.09	1.97	1.91	2.39
1972:												
Q1	10.7	7.3	9.1	37.6	5.3	3.8	4.9	15.3	2.02	1.92	1.86	2.46
Q2	9.6	6.9	8.4	31.5	5.2	3.8	5.2	14.0	1.85	1.82	1.62	2.25
Q3	9.8	6.9	8.7	31.4	5.0	3.5	5.0	14.3	1.96	1.97	1.74	2.20
Q4	9.9	5.9	9.2	35.5	4.7	3.4	4.6	13.1	2.11	1.74	2.00	2.71
1973:												
Q1	9.0	5.6	8.4	30.1	4.5	3.1	4.5	12.8	2.00	1.81	1.87	2.35
Q2	9.0	6.1	7.8	30.7	4.4	3.0	4.3	12.9	2.05	2.03	1.81	2.38
Q3	9.0	5.7	8.1	31.6	4.2	2.8	4.3	12.3	2.14	2.04	1.88	2.57
Q4	8.6	5.3	8.4	28.4	4.2	2.8	4.2	12.7	2.05	1.89	2.00	2.24

[1] Negro and other races.

Source: U.S. Department of Labor, Bureau of Labor Statistics.

The total black unemployment rate, at 8.9 percent was about twice the aggregate white rate in 1973. This was a slightly higher ratio than in the 4 previous years.

There was a decline in discouraged workers in 1973. The number who wanted a job but did not think they could get one declined by about 44,000. Blacks accounted for 80 percent of the decline. At the end of 1973, they comprised less than one-fifth of the discouraged workers compared with the one-fourth average over the previous 2 years.

Industry Employment

The industry distribution of black employment in 1973 can be traced in table 7. The largest proportion—excluding government—of black jobholders were employed in manufacturing with the heaviest concentrations in metals, machinery, transportation equipment—all sectors where demand was strong in 1973—and in food and apparel. Their share of factory employment climbed to 10.7 percent. This fraction was in line with their representation in the work force, and represented an improvement from the 10 percent share in 1972. Outside manufacturing, the proportion of black workers employed in services was high, although slightly lower than in 1972. This was mainly a reflection of movement out of private household employment; although black jobholders were still overrepresented in both household and other service fields. In trade, blacks were under-represented. Moreover, for them, job growth in this sector was primarily in the low wage field of retail trade.

TABLE 7.—EMPLOYED PERSONS BY INDUSTRY AND RACE, 1973

[In thousands]

	Percentage distribution		Black employment by industry
	Total percent	Black [1] percent	Percent
Total number			
Total percent	100.0	100.0	10.8
Agriculture	4.1	3.4	8.9
Mining	0.7	0.3	4.0
Construction	5.9	4.8	8.8
Manufacturing	24.6	24.3	10.7
Durable	14.6	13.8	10.2
Ordnance	.2	.2	10.4
Lumber	.8	1.4	18.0
Furniture	.6	.6	11.0
Stone, clay and glass	.8	.9	12.8
Primary metals	1.6	2.0	13.9
Fabricated metals	1.7	1.5	9.5
Machinery	2.6	1.4	5.6
Electrical machinery	2.6	1.9	8.2
Transportation equipment	2.6	3.1	13.0
Instruments	.6	.3	6.4
Miscellaneous	.6	.5	8.4
Nondurable	10.0	10.5	11.3
Food	2.1	2.5	13.0
Tobacco	.1	.4	44.6
Textiles	1.1	1.6	15.2
Apparel	1.6	2.1	13.8
Paper	.9	.7	8.6
Printing	1.5	.7	5.2
Chemicals	1.3	1.3	10.7
Petroleum	.3	.2	8.7
Rubber	.8	.8	10.9
Leather	.4	.3	7.9
Transportation and public utilities	5.7	5.2	9.9
Trade	19.8	13.9	7.6
Wholesale	3.8	2.5	7.1
Retail	16.0	11.4	7.7
Finance, insurance and real estate	5.3	3.2	6.7

See footnotes at end of table, p. 1011.

TABLE 7.—EMPLOYED PERSONS BY INDUSTRY AND RACE, 1973—Continued

[In thousands]

	Percentage distribution		Black employment by industry
	Total percent	Black [1] percent	Percent
Services	17.8	22.7	13.8
Private household	1.9	6.4	36.8
Miscellaneous	15.9	16.3	11.1
Government	21.4	29.4	14.8
Federal	2.7	4.5	18.1
State and local	2.6	2.6	10.7
Other government (not specified)	16.1	22.3	15.0

[1] Negro and other races.

Source: U.S. Department of Labor, Bureau of Labor Statistics (based on unpublished tables).

One way of looking at the changing structure of black employment is to group the industries into "high-wage," "mid-wage," and "low-wage" industries, defining the groups by the industry's average weekly earnings. Table 8 shows these groupings together with black workers' share of the industry's employment over time. This is an approximate measure of upward job mobility among black workers. Overall, black workers increased their share of employment in high-wage industries in 1973 to 9.3 percent from 8.9 percent in 1972. Moreover, as the total number of workers employed in high-wage industries increased 5 percent in 1973, the number of high-wage jobs held by blacks jumped about 10 percent. In the midwage industries, blacks increased their share from 8.9 percent to 9.6 percent, reflecting a 15 percent gain in employment in 1973. In low-wage industries, the black share, at 10.6 percent, was essentially unchanged from 1972.

TABLE 8.—INDUSTRY EMPLOYMENT, BY WAGE LEVEL AND RACE, 1968, 1972, AND 1973

Industry	Earnings index [1]	Black [2] share of employment		
		1968	1972	1973
High wage		8.8	8.9	9.3
Construction	166.07	10.0	9.2	8.8
Petroleum	152.63	7.4	11.1	8.7
Primary metals	147.78	14.0	13.9	13.9
Transportation equipment	147.19	10.4	11.6	13.0
Transportation and public utilities	142.14	7.9	9.1	9.9
Mining	137.79	3.0	4.5	4.0
Machinery	134.01	4.4	5.6	5.6
Chemicals	129.79	8.1	8.8	10.7
Paper	123.96	7.9	8.6	8.6
Printing	122.90	6.2	5.0	5.2
Fabricated metals	122.21	8.3	8.2	9.5
Stone	121.65	11.3	11.0	12.8
Mid wage		9.8	8.9	9.6
Wholesale trade	112.49	7.7	6.6	7.1
Instruments	109.42	5.0	4.8	6.4
Electrical equipment	108.05	7.7	7.7	8.2
Food	107.21	12.2	11.2	13.0
Rubber	107.95	8.7	9.0	10.9
Lumber	100.96	21.9	19.4	18.0
Low wage		11.3	10.5	10.6
Tobacco	97.44	26.3	33.8	44.6
Finance	92.80	6.5	6.6	6.7
Furniture	90.13	10.7	10.2	11.0
Miscellaneous durables	88.37	9.4	8.4	8.4
Textiles	83.11	9.5	13.4	15.2
Services	79.39	16.0	14.1	13.8
Leather	73.79	8.6	8.3	7.9
Apparel	68.96	10.9	11.5	11.4
Retail trade	65.79	7.7	7.4	7.7

[1] Average weekly earnings of production workers in the indicated industry as a percentage of production worker weekly earnings for total private nonfarm economy, 1973.

[2] Negro and other races.

Source: U.S. Department of Labor, Bureau of Labor Statistics (black employment shares based on unpublished data).

Among high-wage industries, black workers increased their representation in 1973 in transportation equipment, chemicals, fabricated metals, and in stone, clay, and glass industries. Ground was lost in construction, in petroleum, and mining. Outside of manufacturing, black workers increased their share of employment in transportation and public utilities and in some of the mid-wage industries—especially food and rubber.

Among the low-wage industries blacks moved out of the service industries, reducing their job share somewhat. However, there was some countertendency to increase their share of industry employment in tobacco, retail trade, and textiles. Thus, in summary, while the extent to which black workers were better off in their employment gains cannot be ascertained, the analysis does indicate that blacks did make significant employment gains in the relatively high-wage industry jobs during 1973.

Occupational Distribution

The distribution of blacks among occupations in 1973 is shown in table 9. Comparison with data for 1972 indicated that there was a noticeable advancement in the range of jobs held by blacks. Over the year, black workers' share of white collar jobs increased to 7 percent—still well short of their representation in all occupations—but an improvement over the 6.6 percent they registered in 1972. The gain was attributable to a relative increase in the number of blacks in all of the white collar occupations. Yet, the movement into professional and technical jobs and managerial positions was particularly noticeable.

TABLE 9.—EMPLOYMENT BY MAJOR OCCUPATION AND RACE, 1972 AND 1973

	1972			1973		
	Total, percent distribution	Black,[1] percent distribution	Black, as a percent of total	Total, percent distribution	Black, percent distribution	Black, as a percent of total
Total employed	81,702	8,628	10.6	84,409	9,131	10.8
Total percent	100.0	100.0		100.0	100.0	
White collar	47.8	29.8	6.6	47.8	31.1	7.0
Professional and technical	14.0	9.5	7.2	14.0	9.9	7.7
Managers, office and property	9.8	3.7	4.0	10.2	4.1	4.3
Clerical	17.4	14.4	8.7	17.2	14.9	9.3
Sales	6.6	2.2	3.6	6.4	2.3	3.9
Blue collar	35.0	39.9	12.0	35.4	40.8	12.5
Craftsmen and foremen	13.2	8.7	6.9	13.4	8.9	7.2
Operatives	16.6	21.3	13.6	16.9	22.2	14.2
Laborers	5.2	9.8	20.2	5.1	9.7	20.5
Service	13.4	27.2	21.4	13.2	25.3	20.8
Private household	1.7	6.8	40.6	1.6	5.7	38.4
Other service workers	11.7	20.5	18.5	11.6	19.6	18.4
Farm	3.8	3.0	8.6	3.6	2.8	8.4
Farmers and Farm Managers	2.1	0.6	3.3	1.9	0.7	3.7
Laborers and Foremen	1.7	2.4	15.1	1.6	2.1	14.2

[1] Negro and other races.

Source: Bureau of Labor Statistics, U.S. Department of Labor.

Among the blue collar occupations, black workers were still disproportionately represented in the lowest paying laborer jobs, and the proportoni did not change over the year. However, blacks did increase their share of the relatively higher paying jobs as craftsman and operatives. Black workers remained heavily overrepresented in the low paying service occupations. On the other hand, during 1973 there was a strong movement out of private household employment and a consequent decline in their share of service jobs. In 1973, black workers continued to leave the lower paying agricultural jobs, but there was a slight increase in their sha e of farm proprietor occupations.

In summary, while blacks made real progress during 1973 in obtaining higher paying jobs, their occupational concentration remained in the relatively low-skill, low-paying jobs.

Outlook

Although 1973 showed a substantially improved employment picture for black workers, the outlook for 1974 is far from optimistic. Slowdowns in production growth combined with the onset of energy shortages have resulted in layoffs in a number of industries and a rise in joblessness since November. The unemployment rate fo· black workers has increased by 1.2 percentage points since the recent low in October to 9.6 percent in January. Much of the increase has occurred among adult black men. As cutbacks continue in manufacturing, trade, and services industries—sectors where black workers are heavily represented—the employment situation is likely to worsen.

Therefore, it appears that remedial steps will become necessary for a large group of workers in 1974. Higher funding of the public employment program, extensiou of unemployment insurance benefits, and special retaining programs are under consideration by Congress. If enacted in time, these measures would undoubtedly be helpful in easing the impact of employment reductions.

CHAMBER OF COMMERCE OF THE UNITED STATES

By CARL H. MADDEN, *Chief Economist*

The Chamber of Commerce of the United States welcomes the opportunity to comment on the "Economic Report of the President" and the "Annual Report of the Council of Economic Advisers."

THE ECONOMY: POLITICIZING THE OUTLOOK

The term "recession" is becoming politicized amid forecasting uncertainty special to a year of energy problems, market distortions, and inflationary excesses. Whether 1974 brings one rather than two quarters of negative real growth is less important than recognizing basic underlying changes.

Perhaps a technical recession can be averted if consumer and business confidence combine to avoid an inventory cycle, maintain strong business investment demand, and if an easy monetary policy and an easing of raw commodity inflation promote such confidence, among other things.

All that a more pessimistic forecast requires, however, is that second-half prices of basic commodities keep rising, the oil embargo drags on, pulling down business confidence and new car sales, and housing remains depressed in an atmosphere of credit stringency.

A series of surprises has chastened economic policymakers and forecasters. The strong growth that policymakers sought through an election year time frame brought surging inflation led by skyrocketing food and fuel prices. A growth in real terms of 14 percent since August 1971, adding 1 new job for every 12 then existing—a boom bigger than any since 1945–47—mandated alarming price rises and multi-phased peacetime controls now destined for needed termination.

The national chamber has recently called for the unconditional end of all wage-price controls. Controls hold down supply and stimulate demand, thereby adding to shortages. The administration favors continuing controls on health care. This is ill advised. What is needed rather than controls is legislation to improve the health care system. The national chamber in 1970 convened a special committee on the Nation's health care needs which conducted an intensive study of health care policy, ranging beyond the scope of many national legislative proposals. The committee's recommendations, all of which except policy proposal IX were subsequently approved in a referendum taken of the chamber's voting members, appear in a 30-page white paper, which is attached to this statement. Essentially these recommendations support increasing the supply of health services through:

- More and better health care personnel;
- Better responsibility, accountability, and coordination of health care;
- More responsibility on the part of community hospitals;
- Improvement of hospital efficiency/cost controls; and
- Improvement in health-delivery systems.

Reality has eluded economic forecasters. The loss of policy integrity during Vietnam war financing left a bigger legacy of inflationary psychology and induced wage-cost excesses than realized, making the economy more vulnerable to a second round of inflation than expected. Then, the poor crop year of 1972–73 followed the Russian wheat sale to draw down the buffer stock of U.S. farm commodities. And the United States suddenly, but not without earlier warning from business and scientists, fell heavily dependent on imported crude oil when excess capacity of our Southwestern fields dried up. Fueled by policy excesses, inflation burned.

Since the 1930's, policy and forecasting models have reversed Say's Law, which held that supply creates its own demand. Now, we realize that demand does not necessarily create its own supply. Aggregative economic policy, despite all its trappings, is not enough. Indeed, a major danger lies in viewing the present slow-up as "just another cycle."

Pessimism over limits to growth raise questions about the longer term cost of food, a slower rate of productivity gains in farming in the face of higher fertilizer and energy costs, possible adverse long-term weather trends, and a persistent and strong world food demand accompanying population growth. On the other side, slackened world demand will ease shortages of industrial commodities, and if capacities rise, supplies will grow faster. This year's crop outlook, barring bad weather, is very good. And the worst of the price rise in energy should be over. Thus, it is possible that forces now or soon to be at work could abate inflationary pressures in the second half of 1974.

The Policy Prescription: Look at Supply

If we are to avert high and permanent inflation, however, policy should rely on economic analysis that examines supply as well as demand. Past testimony and statements of the Chamber of Commerce of the United States have emphasized the need to raise levels of real investment in the United States, that have been inadequate, compared to competitor nations, for much of the past decade.

In an environment of sharply limited short-term supply conditions, the danger of "dumping money" into the economy through excessive fiscal and monetary stimulation is exactly to create high and permanent inflation. It is spending as usual while inflation burns, a real risk of "budget-busting" and monetary immoderation.

The issue is that of an economic strategy to achieve more productive investment, both tangible and intangible, to gain higher productivity, construed broadly in social, economic, and environmental terms. The world is moving through an accelerating revolution of science. It is nowhere near its zenith. Science broadens its scope to worldwide environmental oversight that promises deepened understanding of resource management. Science offers promise of rapid progress in analyzing major systems such as world weather, health systems, urban systems, social systems, national urban growth systems, and the like. Communications advances seem to be only in their infancy, with some forecasters predicting that in the next 30 years the speed of communications will increase 1 millionfold.

Prospects, not well understood, are favorable for shifting capital from less efficient to more efficient processes for satisfying wants through energy and materials management techniques only now being formulated and developed. The issue of an economic strategy is therefore broader than a pursuit of energy sufficiency. It is different from goals oriented planning and priority setting. The issue is to consider potentialities for future gains in human welfare through structuring incentives for an enterprise economy to shift from the industrial to the postindustrial mode, in which more productive investment creates new economic processes, new industries, and new forms of want satisfaction.

Subjects Needing Exploration

The "Annual Report of the Council of Economic Advisers" has some novel and worthwhile new features, especially the chapters on income distribution and the international economy. But there are several national economic policy questions not discussed that in our estimation should be treated in subsequent reports. Although not exhaustive, the following listing should be at least suggestive.

1. The Council and this committee might examine inflation as a sociopolitical phenomenon. The economic mechanisms of inflation are well known, but the political and social trade-offs, the reasons for them, the integrity of political mechanisms, and the potential for their improvement have been neglected, here and abroad.

2. A study in depth is needed of worldwide supply conditions and prospects for fuels, minerals, and foodstuffs in relation to growing aggregate world demand under the pressure of both worldwide inflation and rising "third world" demand. The study should distinguish between short-term adjustments to sudden or sharp changes in either demand or supply, and on the other hand, long-term developments and changes that require underlying adaption in the economy.

In this regard, the Joint Economic Committee might well investigate the impact of wage-price controls on shortages of fuels, raw materials, and foodstuffs. The shortages problem for petroleum products in the United States contrasts sharply with the absence of waiting lines and shortages in countries around the world that have refrained from imposing arbitrary price ceilings.

3. The Joint Economic Committee could devote a major effort to developing a permanent competence in longer term anticipatory understanding of the major potentialities for future social and economic development. The idea would be to develop competence to examine a variety of possibilities, as in the fields of invention and technology, to indicate the kinds of developmental progress that are underway, and to consider some of the implications to society, along with a rough timetable of anticipated progress. Such competence would allow estimates, for example, of the "Promise of the 1975–85 Decade," and so on.

4. A concomitant effort would be to analyze and project the future needs for capital, both social and economic. It is surely strikingly clear that capital shortages are a worldwide phenomenon. They are, of course, related to worldwide inflation. And they no doubt are related as well to Government policies and promises inconsistent with resource supplies. Such an investigation would be directed toward the development of appropriate policy to insure an adequate supply of capital to satisfy demands.

5. Further study is needed of the contours desired for a world economic environment suitable for stable and environmentally balanced economic growth consistent with equity among nations of conflicting ideologies. The issue is not so much the technicalities of monetary, trade, and investment mechanisms as it is the avoidance of the ominous trend toward isolationism, economic autarky, and increased restrictions on the development of trade and investment. The worldwide rise in the price of gold is a clear symptom of rising disorder and declining confidence in world monetary arrangements and developments. We are in the midst of rapid changes that involve the underlying resource bases and, more fundamentally, the social organization of economic activities. Successful monetary mechanisms require basic accord concerning the workings and effects of the international economic system. As a second attachment to this statement, there is the text of a talk, "Developing a Healthy World Business Climate," which discusses more fully some of the issues involved in creating a healthy world economic environment.

Summary

National preoccupation with short-term energy problems and the current business slowdown threatens to conceal basic longer term issues. One of these issues is the shortage of industrial raw materials caused by simultaneous overexpansion of all industrial economies in 1972–73. Such shortages can recur unless national economic policies anticipate them. A second and related issue is the need for more and better incentives for supply increasing investment. A major lesson of the past year has been the inflationary consequences of encouraging consumption while discouraging production, through ill-advised economic control programs, regulatory disincentives to business investment and overexpansive fiscal and monetary policies.

The Council of Economic Advisers and the Joint Economic Committee would make a valuable contribution to national economic policy development by carefully examining inflation as a social and political problem; the effects of controls on shortages of fuels, raw materials and foodstuffs; the likely future demand for capital, and related longer range issues that tend to be overlooked in popular discussion of economic problems.

[The attachments referred to in the text follow:]

[Attachment A]

IMPROVING OUR NATION'S HEALTH CARE SYSTEM: PROPOSALS FOR THE SEVENTIES

Introduction

Health care, at issue before the Congress in 1971 in six major proposals, vitally affects U.S. business as well as all Americans. Business is the single largest private consumer of health care and has long played a role of leadership in assuring the health of the American people. The Chamber of Commerce of the United States has made two major studies of health care recently, one of problems and the other of proposals. Its long-range study group, the council on trends and perspective, analyzed major health issues of the 1970's in a report approved by the chamber's board and published in 1968.[1] Its special committee on the Nation's health care

[1] Report of the council on trends and perspective, "Major Health Issues of the Seventies," economic analysis and study group, Chamber of Commerce of the United States, 1968.

needs, established in 1970, has examined major proposals. Gsnerously assisted by leading health care experts, and armed with the results of extensive research prepared for the businessmen's steering committee on social problems of New York State Gov. Nelson A. Rockfeller, the national chamber's special committee conducted an intensive study of health care policy, ranging beyond the scope of many current legislative proposals. The committee's recommendations, adjudged appropriate for consideration as chamber policy by the national chamber's board in February 1971, represent the informed and mature judgment of conscientious business leaders selected for their experience in corporate decisionmaking who are concerned about the Nation's health care, its accomplishments, and improvement.

By 1970, Americans were concerned with improving the Nation's health care system, among our largest and fastest growing industries. U.S. business was also concerned. It has a large stake in health care. The largest single private buyer of health care, U.S. business spends $13 billion a year for health insurance, medicare and medicaid, and other health care benefits for its employees and their dependents. As a leadership group in the society, business has a major interest in and responsibility for the health and well-being of the American people.

No one should question the historic accomplishments and high standards of the U.S. health care system. There is wide recognition of our world leaderhip in health related sciences, our unmatched urban medical centers, the superb training of medical and health care leaders, our distinguished medical schools, and the human dedication and discipline of our leaders in the healing arts.

Yet, few would deny that by 1970 important issues were emerging that justify concern to improve health care in the Nation. Spiraling health care costs, shortages and maldistribution of health care personnel and facilities, new emphasis seen possible on health maintenance and the prevention of illness, advancing technology—all of these issues have contributed to the spreading debate.

What are the problems of health care? What are the alternatives facing the Nation? How can we assure that the desire of Americans for quality health care can be met without losing the benefit of past accomplishments? These are questions that preoccupied the business leaders of the national chamber.

The Problems

In its 1968 study[2] of the health care problem, the Chamber's Council on Trends and Perspective reported several findings:

(1) Health care expenditures have been the fastest rising item in the Consumer Price Index, and sharp cost rises especially in hospital charges, are expected to continue.

(2) Despite rising wealth and income, dramatic medical advances, and improving medical technology, the United States lags behind other western nations in indexes of health such as infant mortality. Surveys generally indicate an excessive rate of illness, disability, and infant mortality among groups at the poverty level.

(3) U.S. health expenditures per person are among the highest in the world, and health care personnel are among the best trained in the world; but the United States faces critical challenges stemming from resentment of higher health care costs, inadequate facilities, personnel shortages, and maldistribution, inadequate health insurance coverage, and inadequate health care for the poor.

(4) Examination of the health care complex reveals poor planning of hospital and other health facilities, use of highly trained health care personnel to perform services requiring lower skills, not enough use of existing advanced technology to improve medical delivery systems in hospitals, fragmentation of health services, and insufficient data on every aspect of the workings of the system.

(5) Greater emphasis can and should be put on preventing illness and disability, on public education about the value of preventive services, on orienting services toward the health of the "total" person, on continuous planning for needed improvement in and more effective use of health facilities in communities, and on a rational system of reporting experience to allow objective analysis of varying approaches and evaluation of progress.

[2] The study report was based on a synthesis of major points developed in several specially commissioned background papers studied by the Council, Council consultations with health authorities, oral presentations to the Council by leading health experts, and the Council's own evaluation of the health issue. The special committee on the Nation's health care needs, starting with the Council's report, examined the subject of health care in greater depth and based its conclusions upon the further information it developed.

The problems of health care are systems problems. They relate to the way the total health care complex, looked at as a whole, produces desired results:

Goals.—What should the U.S. health system aim to do?
Personnel.—What kinds of personnel are needed?
Control.—How should decisions about health services be made?
Delivery.—How can delivery of care be improved?
Cost.—How can rising costs be contained?
Financing.—How should needed care be paid for?

It is a mistake to think that the health care issue is primarily one of financing alone. Indeed, provision of financing to meet existing needs and increased desires for health care, without other needed changes, is a good way to "break the system", to overload it to a breaking-point.

Goals

POLICY PROPOSAL I. MAINTENANCE OF HEALTH, AND MEDICAL CARE

In general.—The Nation's goal for the health care system should be to assure access to quality care for all Americans at reasonable total costs for services provided, in a manner that maximizes the advantages of individual freedom of choice and of flexibility to adjust to changing needs. This goal should be achieved through our current systems rather than through any governmental system.

This system should strive to deliver comprehensive care, including health maintenance, primary, specialty, restorative and health-related services in extended care facilities.

Maintenance of health.—There should be a national program educating all Americans on ways and means to maintain and promote good health, including prevention of disease and the role and content of proper nutrition.

Goals define purposive action and energize creative effort, for society as for a business. New goals for health care can now be sought because both achievements and gaps of the past are now illuminated by new knowledge and new conditions.

Standards and spending

Our present health care system developed historically to give "sick care" not "well care." Its philosophy has not changed to conform to present capabilities in health care technology and organization, nor to changed health hazards created by our highly organized urban life.

Health standards, as a result, have not risen commensurate with expenditures. Total spending on health in 1969 of $60.3 billion made up 6.8 percent of gross national product (GNP), compared to 4.5 percent 20 years ago, but life expectancies have scarcely risen and for males, in some age groups, have declined. Even though we spend a rising share of output on health care, 49.1 percent of American civilians in a recent year had one or more chronic diseases or impairments, and 46.9 percent of prospective military draftees were rejected for physical impairments.

In general, indices of the health of Americans do not compare favorably with other industrial countries. The United States appears to rank 13th among industrial countries in infant mortality.[3] Infant mortality among blacks is appreciably higher than among whites. Despite great improvement in the recent past for all industrial countries in reducing the percentage of mothers who die in childbirth, the United States has slipped in the rankings among these countries. The United States is 18th among industrial countries in life expectancy. It is 16th among industrial countries in the death rate of males in their middle years. In all instances, during the past 15 to 20 years, the United States ranking worsened. This is true despite the high percentage of our total output compared with other industrial nations that we spend on health care, the highest level of income in the world, and the high competence of our medical profession.

Experts will disagree about how to interpret specific comparisons of health indices among different industrial countries. Sweden with its small homogeneous population is no larger than New Jersey. Experts also rightly point out that the fast pace of life in our competitive and highly mobile, urban society, and the increasing trend toward loss of life and injury on our highways, rather than the quality of health care, may contribute to lack of progress in measurable aspects of health. But after all the qualifications of the experts are entered and taken into account, there remains the question as to whether or not the United States is slipping behind other industrial nations in the accomplishments of its health care system as a whole. Our direction seems to be away from, not toward, being the best in the world.

[3] Infant mortality is measured differently in various industrial countries.

Reasons accomplishments lag

The reasons health accomplishments lag behind spending are the gap between health of poor and nonpoor, the maldistribution of health care personnel, their increased specialization, and the change in causes of illness and death.

Convincing evidence shows that the poor receive less health care and suffer poorer health and reduced life expectancy. There are 25 million people in our population of 203 million who lack comprehensive medical coverage. The hazards of urban poverty, of course, extend beyond the reach of health care alone; yet, greater access to health care, and improved delivery of care available, could help. Many rural poor lack access to health care or means to purchase it. Poor people suffer higher than average infant mortality, incidence of illness, and chronic disability, but obtain lower than average immunization, medical and dental service, or physician's visits. Chronic illness among the poor is about three times the average.

The Nation's physicians are concentrated in urban areas. In mid-1969, metropolitan counties had 146 physicians per 100,000 population; bordering counties had 77, and isolated counties had 75. Although rural residents may have special needs because of age, or lack of income, health services are less available to them. Even in urban areas, though, health care is less available in poor neighborhoods or is not delivered, despite availability. Nonwhites make more use of emergency rooms and hospital clinics but less use of physician's visits than whites. And because of physician shortages in nonwhite urban neighborhoods, hospital utilization rates are higher for the urban poor than for the middle class.

Access to health care is reduced by the rising tendency of doctors to specialize, which reduces availability of general care. Among the Nation's more than 300,000 physicians, only 15 percent are general practitioners. Although the number of physicians has grown 25 percent faster than the total population, one-third of physicians today are engaged in medical research, teaching, public health, and industry. As a result, the number of doctors caring for patients declined by 10 percent relative to population between 1950 and 1965.

The cause of death has changed dramatically since 1900 because of medical advances; yet, paradoxically this has reduced the ability of the present system to provide access to health care. In 1900, the leading causes of death were acute, communicable diseases—influenza, tuberculosis, and gastritis—having a death rate of 540 per 100,000 people and accounting for one-third the deaths. In 1960, the three top killers were diseases of the heart, cancer, and stroke, which caused 620 deaths per 100,000 people and 65 percent of all deaths. The conquest of acute disease has gone along with a lag in adapting to the care needed for new causes of death. New knowledge, moreover, of the value of early detection of cancer, the role of diet and exercise in heart disease, and of maternal and infant malnutrition in mental retardation is difficult to inject into health care for nationwide, organized emphasis.

While health accomplishments lag behind our investment of resources in health care, evidence grows that greater systematic emphasis on health maintenance and illness prevention would achieve cost savings; that is, would increase the productivity of the health care system. One estimate holds that hospital admissions from urban inner-city poor neighborhoods could be cut by as much as 80 percent by preventing disease. While health insurance today encourages hospitalization, with resulting expensive care, a shift to health maintenance and illness prevention might reduce time lost from work because of acute illness, currently an average of 8.2 days per person. And growing evidence that infants, deprived both before and after birth of protein, suffer brain and central nervous system as well as bodily damage, stands in contrast to data showing that in large U.S. cities an average of 20 percent of infants 6 to 36 months old suffer nutritional anemia.

To increase the productivity of health care, achieve cost savings, and above all to improve the prospects of health for all Americans, new goals are needed for the health care system. Health cannot be assured, but access to health care can be a goal. The assurance of such a goal is empty unless quality care is available and deliverable. Access to quality care at exorbitant cost is evidence of a malfunctioning in the supply of health care, and supply must rise to bring costs down. Freedom of individual choice, both by recipients and suppliers of health care, is a basic human value and an assurance against deterioration in quality or invasions of privacy.

The goal of the health care system should lay emphasis on comprehensive rather than episodic care, to achieve quality assurance and cost advantages; at the same time the system should deliver primary, specialty, and restorative care, and health-related services in extended care facilities. Evidence to be discussed later is available to support the emphasis on the goal of comprehensive care and health maintenance.

To achieve public awareness and understanding of the value of new health care goals, a much higher priority should be given to promoting and maintaining good health, including the vital role of nutrition in health maintenance, for all Americans. The society does not lack the intelligence, ingenuity, means, or resources to develop and administer a national program devoted constructively and forcefully to ways and means of maintaining good health and preventing illness and disability; it can be done if we will do it.

PERSONNEL

POLICY PROPOSAL II. MANPOWER GOALS, DEVELOPMENT, AND UTILIZATION

Goals.—The development of more and better health manpower during the current decade should be sought by subscribing to several goals, including:

- Establishment of several new university health science centers, and of more university health education centers;
- Encouraging university health science centers to help coordinate and guide health manpower education and to cooperate in developing better systems for delivery of health care;
- Development and expansion of education and/or training programs for physician's and dentist's assistants and associates;
- Acceleration of medical and dental education;
- A large increase in entrants' places in medical and dental schools; and
- Positive efforts to increase admissions to medical and dental schools for women and minorities.

Manpower development.—To provide access to health care for those in rural areas and in the inner cities, the Federal Government should make loans to students for costs of education in the health professions and skills, with the provision that such loans would be forgiven if such persons will deliver their services for a period of time in some area of manpower or service shortage.

To attract and retain an adequate supply of qualified professionals in the fields of preventive and early disease detection, these individuals should be accorded special recognition and levels of compensation commensurate with their education and experience.

Utilization.—Detailed State licensing for various professions in the health field is expensive, restrictive and often unnecessary. Licensing of paramedical personnel such as physician's assistants or other health professionals would seriously restrict the supply and the effective use of such personnel in the delivery of health care. Physicians and hospitals should be licensed to employ such personnel if they are qualified or certified as qualified.

The price of any product or service for exchange in markets depends on the relationship between the demand and supply. In competitive markets a rise in price rations the supply among those able to pay—but equally important, the price rise stimulates an increase in supply. Resources are drawn into production of the desired good or service to bring about a new, higher balance between demand and supply and price falls back. In competitive markets a rise in price induces an increased supply which restores a lower price.

Economics and the supply of health care services

Economic analysis throws important light on the issue of health care personnel and the price charged for their services. The mistaken and callous view that complex human beings and their activities can be interpreted exclusively by economic analysis has caused much mischief. Equally mischievous, however, is the view that since "human labor is not a mere commodity," such labor services may not be examined for economic tendencies at work in their demand, supply, and pricing.

Health care services do respond to economic influences. They respond to restrictions in supply, whether appropriately or inappropriately set by such factors as length of training, licensing requirements, cost of training. Restrictions of cost and length of training, licensing, professional standards and the like limit supply relative to what it otherwise might be and extend the period in which supply could respond to increase in demand.

Recent health care legislation such as medicare and medicaid, through provision of financing, effectively increased demand for health care. With supply restricted and slow to respond, the sudden increase in demand accelerated price increases. Setting goals such as proposal I, however, requires that access to quality care be provided "at reasonable cost." The goal requires that careful attention be given by the Nation to goals of personnel development and utilization, to the supply of health care manpower. If demand for health care rises further through increased provision for financing but supply is slow or lacking in response, the price of health care services will continue to soar. Even if demand rises are kept in bounds, if health care services are sufficiently restricted in supply for whatever reason, prices will keep rising.

It is crucial to realize that health care services are not offered in a competitive market. Demand for health care, generally, is reluctant demand; the consumer of health care services is usually necessitous and does not specify amount or price of needed care. Also, the supply of health care services is in general limited by state laws setting complex licensing requirements, by self-regulatory standards of health care professions, and by the shortage of medical school places compared with the number of qualified applicants. The result is that until lately health care services for the nonpoor, viewed in their economic aspect, have been a peculiar mixture of supply which contains powerful nonprice restrictions and monopoly elements. For the poor, health care services have been at times "free" but at the discretion of suppliers and at times of inferior quality. Dissatisfaction with the evident irrationalities in the manpower supply situation has been rising on the part of health care personnel, including physicians, and on the part of patients, both poor and nonpoor. In any event, health care manpower should be expanded in supply without loss of quality, flexibility, or freedom of choice, so as to keep costs reasonable for society and for consumers of health care.

Some hold that the Nation is now short by 50,000 physicians and 150,000 technicians, but such numerical estimates can easily be subject to wide ranges of error depending on the philosophy, organization, distribution, and administration of the delivery of health care. Yet, the case for mal-supply of health care personnel is convincing on the facts. Of the 273,502 active, non-Federal physicians in the United States as 1970 began, 82.5 percent were engaged in delivering care to patients, and 10.9 percent were in other professional activities such as medical teaching, administration, and research. Increasing specialization between 1960 and 1967 added 50,000 specialists and subtracted 6,000 general practitioners. Uneven geographical distribution provided New York State, for example, with 200 physicians per 100,000 people and Mississippi with 69 per 100,000; but even so, some lower income neighborhoods of New York City found "private physicians as hard to find * * * as in backward rural counties of the South." Foreign trained doctors make up 15 percent of all U.S. practicing physicians and in 1967 made up 24 percent of all new additions to the U.S. medical profession.

Traditional notions of the facts about doctor-patient contact are out of date. The trend, even in high income areas of high physician/population ratios, is toward superficial contact. A recent Kentucky study showed median patient-physician contact of 4.7 minutes. Although the physician works an average of 60 hours per week, many patients encounter long delays in getting appointments for routine care; many spend costly and valuable time in crowded waiting rooms; weekend care more and more shifts to often overcrowded and ill-equipped hospital emergency rooms.

Our 101 medical schools take 10,800 entrants per year, about one-half the qualified entrants, of which around 40 percent are from families with incomes above $15,000, among the highest one-eighth of income receivers, and another 20-plus percent from families earning between $10,000 and $15,000. Although women make up four-fifths of health services personnel, only 6 percent of physicians and surgeons are women. Blacks, making up 11 percent of the population, comprise 3 percent of U.S. physicians; and the majority of black medical students are enrolled in two major medical schools, Howard University and Meharry Medical College.

As an industry, the health care system is among our largest and fastest growing. Though the supply of health manpower (nonphysician) has increased sharply, demand keeps outstripping capacity. A recent U.S. Government study claims a need by 1975 for 1 million more health workers. Another U.S. Government study claimed a shortage existed in 1965 of 257,000 hospital workers. Many programs exist now for training technical health care personnel, but strict State licensing requirements limit employment of graduates. Federal loans to medical and other health care students have forgiveness provisions for practice in supply-short areas.

Policy implications

It seems plain that employers should adopt goals to develop more and better health care manpower during this decade. The goals stated in policy proposal II were developed through careful consultation and study. Medical and dental education needs expanding in number of entrants and needs accelerating to cut length of training. The Nation needs more doctors and dentists, male and female, white and nonwhite, trained at home. The country should not tolerate the drain of talent from other, less affluent countries that is represented by foreign training of 15 percent of our total supply of physicians, while at home half of qualified applicants are denied admission to our medical schools. A shift to 3-year medical education in 1973–74 by all existing medical schools would increase student places in 1966–77 by 4,500 without incurring construction costs, a saving of nearly two-thirds of construction and operating costs in universities. Eliminating the intern year would also be possible. There is considerable evidence that courses are duplicated between college and the first 2 years' curriculum in many medical schools.

Costs of medical school education appear to be threatening to go out of control. Many medical schools are in dire financial straits, with total costs per student running at $10,000 per student per year and counting research at between $18,000 and $20,000. Yet some doctors and students claim that medical schools emphasize research and specialization for too much and neglect education or training for family care.

University health science centers are needed to serve their community by providing continuing education for all health manpower occupations. Such centers can provide manpower (1) to analyze social and economic aspects of medical and dental care, (2) develop needed personnel to help physicians, (3) develop through cooperation with local community colleges and high schools training programs for allied health workers. Doctors spend too much time now on routine tasks, including 25 percent of their total time on business (bookkeeping, billing, ordering supplies, et cetera). About 30,000 medical corpsmen leave the military each year but rarely continue in medicine. Health science centers can and should serve as centers of knowledge about social and environmental barriers to delivery of health care in urban gehttos and rural slums.

Licensing of health professionals

Concerning utilization recommendations in policy proposal II, the health care industry is one of the major regulated industries of America, subject to complex State licensing statutes set following the 1910 Flexner Report and scarcely changed since except by additions of numerous fields. While health care means of delivery have changed rapidly, licensing requirements have remained constant, along with the outdated machinery of bureaucracy to administer them.

Meanwhile, rising malpractice suits with larger and larger judgments force doctors to practice "defensive medicine," involving the patient in paying piecework rates through cumbersome "fee-for-service" for separate billing of batteries of tests and examinations in hospitals which could be carried out by doctors' assistants in clinics.

The future of health teams, however, depends on developing such assistants—called "paramedical personnel"—whom doctors are willing to use and whom patients are willing to accept for routine testing and examination. While the law will not hold a physician liable for negligence of an independent technician, the physician who uses an assistant is held liable for his negligent acts under general laws of agency. Thus, the law encourages the physician "contracting out," to practice defensive medicine, and wasteful, expensive care; but the law discourages physician-supervised office care.

Present licensing laws prevent effective use of paramedical personnel, without necessarily improving quality of care. The licensing of physicians and hospitals to employ paramedical personnel who are qualified or certified as qualified would remove the organization of physician care from outmoded legal straitjackets, while increasing the flexibility of health care delivery, a step physicians themselves would welcome.

Control

POLICY PROPOSAL III. RESPONSIBILITY, ACCOUNTABILITY, AND COORDINATION

Council of Health Advisers.—There should be established in the Executive Offices a Council of Health Advisers to advise the President. Its responsibilities should include, but not be restricted to, making continuing studies on manpower and facilities needed to achieve the Nation's goals in health.

Planning Council.—Areawide health care planning councils should be adequately staffed with competent personnel so they can operate efficiently. Business should support and participate in the work of such councils. Employers should consider refusing financial aid to any health care facility that does not accept decisions of such councils.

In the United States today, there is no group which objectively appraises the structure and functioning of the Nation's health care system or its performance in relation to its goals. A Council of Health Advisers to the President could perform that function, by analogy to the effective, three-man Council of Economic Advisers which, since 1946, with a small (15-man) professional staff, analyzes and reports on the economy each year. A Council of Health Advisers could also study the current health care information system. To understand continuously what is happening in health care will require improving the health care statistical system. The Council would not duplicate or dominate cabinet departments concerned with health but would provide the President with policy analysis, development, and evaluation.

In the local society of 1900 health services centered on family units; in today's urban society health care focuses on community needs. Today's health care complex, called by some analysts a "nonsystem," involves some 8,000 hospitals and their 1.6 million beds divided among voluntary "tax-free" institutions, Federal, State, and municipal-owned hospitals, private (for-profit) institutions, and Veterans' Administration hospitals.

As an institution, the hospital in the United States is a curious mixture of philanthropic, professional, voluntary, or profit-making activity and has been peculiarly subject to cost escalation. Hospital costs, the fastest rising component in the Consumer Price Index, rose from $48.15 per patient-day in 1966 to well over $70 in 1971 and are still rising. Rising hospital costs stem from rising wages, expensive technology, and increasing numbers of staff per patient. But they also stem from needless duplication of expensive equipment and lack of cost-conscious management compared with other institutions.

Present hospital organization creates an inter-hospital competitive spirit of professional pride which leads to installing exotic equipment with too little regard for cost or availability elsewhere in the community. The internal organization of hospitals creates uncompromising institutional autonomy, absence of marketplace discipline, passivity to changes in management methods, and lack of clear managerial authority.

What is needed is better comprehensive health care planning in communities. A relatively new concept, comprehensive community health planning has been stimulated by Federal legislation, in the Hill-Burton Act in 1946, the regional medical program (Public Laws 89–239) in 1965, and the partnership for health program (Public Law 89–749 and 90–174) in 1966–67. These laws authorized State health planning offices and advisory councils and local, areawide planning agencies. Besides such technical aid to comprehensive health planning, the Federal Government also provides categorical grants. Progress of local agencies varies widely; vast regions of the Nation lack agencies, while some metropolitan areas are well organized.

Despite its risks, comprehensive community health care planning is vital. The risks of comprehensive local planning ar related to its virtues: pressure for coordination can stalemate action or polarize opinion, as can indiscipline or inexperience among leaders. Authoritarian control risks damage to viable pluralistic arrangements and partisan political decision. Even so, the job of reducing duplicated facilities, fostering joint utilization of administrative services, and reducing wasteful competition for professional prestige can be done more effectively with leadership than without it.

Business, as a major consumer of health care, has a big stake in getting results which avoid wasteful costs. Coming soon are developments such as regional complexes of medical services; computerized, centralized, intelligible health records; sophisticated equipment to aid and check diagnosis; centralized purchase; and the like. These developments require cooperation between the community of organized consumers and professionals producing health care, if the society is to control the social institutions which serve them.

POLICY PROPOSAL IV. HOSPITALS AND HOSPITAL TRUSTEES

Hospitals.—Hospitals in any area have a joint and several responsibility to help meet that community's health care needs. Community hospitals should meet local and State needs without wasteful duplication of facilities and needless expenditure of funds. To continue receiving exemption from a variety of taxes, each nonprofit hospital should regularly publish detailed financial statements and information such as contractual terms for compensating services of specialty groups in the hospital discounts extended for hospital care received by staff and other hospital personnel, or by participants in a health plan, and should accept overall decisions by areawide planning councils.

Hospital trustees.—Employers should be encouraged to obtain or develop training programs for those of their employees who are or will be board members or trustees of health service units (hospitals, medical centers, health service planning agencies, and so forth).

The voluntary hospital has evolved from the almshouse of more than 200 years ago, where people went to die, to the quasi-public utility of today, where people go to get well. But society has not fully assimilated the profound change. A look at the present status and past history of the hospital as an institution makes this clear. Total hospital beds in general medical and surgical hospitals rose from 812,000 in 1963 to 934,000 in 1968, but because hospitals were growing larger in size, the total number dropped from 6,710 to under 6,539. About 8 out of 10 hospitals today are general hospitals, giving both surgical and nonsurgical care; the others give specialty or long-term care. About half the Nation's 7,991 hospitals are voluntary, nonprofit institutions; 35 percent are owned by Government (Federal, State, or local), and 16 percent are profitmaking.

First established in Philadelphia in 1751, the hospital as an institution in its early years grew mainly as a place for medical schools to practice clinical medicine and was chiefly under voluntary sponsorship, outside either public or church auspices. Today, voluntary hospitals are granted tax-exempt status by the Federal Government as "charitable" organizations, in the legal sense of "an implied public trust constituted for some public benefit." The Internal Revenue Service sets standards for tax-exemption.[4] It generally accepts, as voluntary, any community hospital supported partly by public contributions and/or public grants from a city, county, or State. And it grants tax exemption because the voluntary hospital * * * is formed for the purpose of furnishing hospital facilities to all persons in the community at the lowest possible cost and necessarily accepts patients who are unable to pay for hospital facilities in order to retain the support of the community."

Though legally nonprofit, voluntary hospitals in recent years have earned rising net incomes, from $91 million in 1961 to $400 million in 1969, a 340 percent increase. Prohibited from paying dividends, the nonprofits have had large sums to use for adding to facilities and modernizing. Profitmaking hospital net income rose, 1961 to 1969, from $19 million to $70 million, or 268 percent.

The history and law concerning voluntary hospitals both imply that these institutions are vested with a public trust and tinged with a public interest. Tax exemption standards require operating "at the lowest possible cost," which should imply avoidance of wasteful duplication of facilities and needless expenditure of funds. The public interest, which requires detailed public reporting of, for example, utility operations such as telephone and power companies, should by analogy require such reporting from voluntary hospitals. Just as the public interest becomes engaged in the operating plans of regulated utility corporations, so the public interest has a stake in the health care palnning of voluntary hospitals as their plans are related to national and community needs.

Employers, as major purchasers of health care through employee benefits and taxes, have a strong interest in developing leadership capacities among their employees who serve as board members of health service units. Such employees represent not only the public interest but the consumer interests of necessitous buyers of health care financed by employee benefit plans or taxes partly paid by employers. Employers also have an interest, as explained later on, in including among the leadership capacities of employee trustees an understanding of the special problems of effectively providing the urban poor with access to quality health care.

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[4] As follows: (1) The hospital must be organized as a nonprofit charitable organization for the purpose of operating a hospital for the care of the sick; (2) it must be operated to the extent of its financial ability for those not able to pay for the services rendered and not exclusively for those who are able and expected to pay; (3) it must not restrict the use of its facilities to a particular group of physicians and surgeons, such as a medical partnership or association, to the exclusion of all other qualified doctors; (4) its net earnings must not inure, directly or indirectly, to the benefit of any private shareholder or individual. See U.S. Treasury Department, Internal Revenue Bulletin, Cumulative Bulletin 1956: January-June, 1956, p. 203-204.

POLICY PROPOSAL V. DELIVERY SYSTEM

The Federal Government, through incentives, and employers and insurance carriers should encourage expansion and improvement of existing methods for providing health care services, and the development of new delivery arrangements.

Through health care benefit programs, employers should enable employees to have a choice of delivery arrangements, such as prepaid group practice where available.

Urban hospitals, as community health care centers, should expand their out-patient service facilities and should develop neighborhood centers for screening and referral of patients.

Improving the productivity of the health care industry, without sacrifice of quality, is crucial to assuring access to quality care for all Americans at reasonable cost. The reason is clear. The demand for health care is certain to rise. Hardly any service is generally more basic to people than good health. The rising affluence of our society and its concern for quality, the rising educational level of our people, the increase in active recreation, the emphasis of our culture on youth and vitality, the growth in our aged population, and the special health problems of the poor all make health and health care a source of both necessitous and discretionary spending, and lack of spending a source of disability and illness. Yet, as noted above, health and health spending are not necessarily coequal, nor does spending, in and of itself assure good health. The issue is the effectiveness of health care, not the total amount spent for it.

Organization of delivery system

This issue goes to the organization of health care. The term "delivery system" refers to the way a particular arrangement for giving care to people is put together and how it functions. In business, a firm gives thought to its "production system" or its "purchasing system" to make them more effective. In health care, thought can be given to "delivery systems" to make them more effective.

In the present delivery system, with its general emphasis on treating the sick, the physician is the usual "entry point" for most people in getting access to care. The care is provided in a variety of ways—in doctors' offices, through home visits, in hospital emergency rooms, or through normal "in-patient service," or through "out-patient service," or in neighborhood clinics, or in nursing homes. The physician, still, is the heart of the system because he "screens" patients to determine whether care is needed, examines, performs or orders tests, prescribes regimens including drugs, performs or refers treatment, and determines when the patient is "cured" and released from treatment.

Yet, among health care personnel the services of the doctor are in the scarcest supply, relative to demand; they are costly; and the supply of doctors is slow to respond to an increase in demand because of the cost, length, and difficulty of training, the barriers of licensing and certification, and professional standards. Measures to increase the effectiveness of doctors without sacrifice of quality would be highly cost-effective.

Personal and economic considerations largely determine the distribution of doctors among specialties, regions, urban or rural areas, and among types of practice. The issue, in analyzing delivery systems, is whether the present organization of health care delivery gives doctors personal and economic incentives which bear some average correspondense with the Nation's and the community's health care needs.

Judging from the amount of ferment and debate now occurring on these questions, a strong argument can be made that further thought and experiment in new kinds of health care delivery systems are badly needed by the society and therefore should be encouraged by groups such as employers. A strong argument can also be made for a pluralistic, indeed competitive, approach to providing for the diverse needs of the American people for health care.

Group and solo practice

The contrast of solo, fee-for-service practice with prepaid group practice illustrates the need to positively stimulate new delivery arrangements but also to avoid easy or quick judgments that any one mode of delivery gives "the answer."

In solo, fee-for-service practice, health care easily becomes "sick care." Piece-work rates of payment probably tend to give incentives to doctors to maximize treatment procedures, if economic reasoning from large bodies of industrial evidence is valid, and for patients to minimize contacts with doctors. The doctor performs most of the services, including routine testing, and he also devotes significant time to the "business" of his office. In treating patients with hospitalization insurance, the doctor realizes that, to collect, the patient must be hospitalized. Again, economic incentives tend to push both doctor and patient towards at least erring on the side of hospitalizing the patient when in doubt.

Group practice contrasts with solo, fee-for-service practice as a system for delivering health care. Group practice, involving about 12 percent of today's practicing doctors—either in individual clinics or under prepaid group arrangements such as the Kaiser Permanente Plan, the Health Insurance Plan of New York, or Group Health in Washington, D.C. Prepaid group plans now cover about 8 million persons.

Kaiser, the oldest and largest group plan, was formed during the depression years to provide health care to isolated construction workers and their families (about 200,000 people) on a prepayment rather than the usual fee-for-service arrangement. Today the plan covers about 2 million subscribers in 6 States. Care is provided through an integrated system of outpatient centers, 51 clinics, and 22 hospitals by 2,000 physicians and 13,000 nonphysician employees. The plan provides comprehensive care at an annual cost of about $100 per person.

Through prepayment, subscribers set total annual income for the health care group. Thus, the incentive is established in managing the group to promote and maintain health, including incentive for early detection of disease, in order to reduce the frequency of costly hospital treatment. Group members, on the other hand, have no economic incentive to delay examination or treatment. The key features of the Kaiser plan are (1) the prepayment charge for plan members; (2) voluntary enrollment with subscriber-choice of at least one other health care plan—Blue Cross-Blue Shield or commercial insurance; (3) autonomous operation of each group; (4) turnover of subscriber income to doctors and hospitals; (5) necessity to live within budgeted income but choice as to disposition of surplus; (6) services from a group.controlled hospital base; (7) full-time salaried doctors; and (8) doctor responsibility for decisions affecting quality of care.

In group practice, incentives are given to economize the time of doctors subject to their assumption of responsibility for quality of care. Doctors need not "screen" routine cases, or perform tests, or spend time on business arrangements, or treat patients in hospitals in order to assure claims against insurors, or err on the side of providing unneeded hospital care or unduly lengthened stay by a patient in the hospital. As an abstract delivery system, the group practice concept gives subscribers and doctors economic incentives to maintain health and economize treatment. Conversely, fee-for-service practice gives patients incentives to avoid treatment and doctors incentives to provide it. The tremendous growth of health insurance, both private and government, which shifts the main burden of payment for care to third-party insurors, however, weakens the economic incentive of patients served by the dominant delivery system to avoid treatment in hospitals.

Problems in the delivery of care

The present delivery system, in fact, faces several problems: (1) the dramatic increase in recent years of hospital utilization, (2) the trend toward specialization among physicians, and (3) the lack of access to health care for many people.

During the 1960's the demand for use of hospitals rose dramatically, mostly from a rising use of hospital outpatient facilities plus longer stays in hospitals by patients. From 1961 to 1969, outpatient service demand rose 75 percent. Inpatient admission rose 20 percent, but the average length of stay by patients in hospitals increased by 12 percent to 8.3 days per patient.

The reason was an astonishing increase of approximately 65 million people who became eligible for major financing of their stays in hospitals through private health insurance and the public programs of medicare and medicaid. The growth of private health insurance for hospital benefits from 1960 to 1968 added 32 million people, from 120 million to 150 million. Medicare in 1966 made 20 million elderly people eligible for federally financed hospital care and by 1969 medicaid added 15 million people from low-income families. By 1969 only half of hospital expenses were paid from private pocketbooks, down from 64 percent in 1966.

Meanwhile, increasing specialization of doctors has had adverse impacts on access to medical care. The trend to specialization stems basically from the explosion in technology. But it also is influenced by economic incentives in the present delivery system, where usually the fees and income of general practitioners are lower and those of various specialties are ranked higher depending on cost, length, and difficulty of training and professional certification. To illustrate, at yearend 1969, the Nation's supply of doctors is about 303,000, and 9 out of 10 are non-Federal. Of non-Federal doctors (274,000), about 9 out of 10 care for individual patients. Of doctors caring for patients, 22 percent (55,000) are in general practice, 23 percent (57,000) are medical specialists, 30 percent (73,000) are surgeons, and 26 percent (63,000) are in other specialties. As mentioned earlier, between 1960 and 1967 increasing specialization added 50,000 specialists but reduced general practitioners by 6,000. And although numbers of doctors grew 25 percent faster than the population between 1950 and 1965, the number of doctors caring for patients declined by 10 percent relative to the population.

General practitioners, in fact, are critical of the recently prevailing philosophy of medical education in the Federal Government and in medical schools, which, they argue, in general seems to neglect analysis of the social environment in which health care is demanded. Thus, the vast majority of medical students were science majors in college, and few had undergraduate education in the arts and humanities, while few medical school curricula provide opportunity for study of the social-economics of medicine or health care. What's more, Federal financial aid to medical education, which expanded rapidly during the 1950's and 1960's, seems to have involved the strategem of providing such aid indirectly through research grants. The strategem, however, inadvertently gave powerful economic incentives for faculty to give first priority to specialized research. This generated a leadership style or model for students of the research-minded specialist rather than the style of the "family specialist" who would focus specialized disciplines in a better organized and more humane fashion on health care oriented to family, neighborhood, community, and national circumstances and need.

As a generality, medical education seems to reflect as a result the educational philosophy of the 19th century German university in an era striving for synthesis of specialized modes through systems analysis, process-oriented management, and institutional renewal in many areas of social life. In commenting on the explosion of knowledge, the eminent physicist Robert Oppenheimer observed, "This world of ours is a new world, in which the unity of knowledge, the nature of human communities, the order of society, the very notions of society and culture have changed and will not return to what they have been in the past." Health care education, when viewed as the inculcation of the art of healing, plays a crucial role in determining the leadership model for such a new world. Some thoughtful general practitioners seem to be saying to present-day medical education in this perspective, "Physician, heal thyself." Cognizant, however, of the damgers of over-generalization, the business leaders made no recommendation about health care education, though they did see apparent problems.

Delivering health care to the poor

According to health care experts, under existing arrangements, including the hangover of "charity" concepts in voluntary hospitals, the urban poor too often reject health care services that are available in what are sometimes the finest quality urban medical centers. There is at the same time evidence that the supply of doctors in private practice in urban poor neighborhoods is rapidly dwindling. For example, in one small section of the Bronx in New York City, between 1945 and today, while the population increased from 45,000 (largely white) to 65,000 (blacks and Puerto Ricans), the number of full-time doctors dropped from 67 to 3.

At the same time, scattered evidence suggests but does not show conclusively that neighborhood centers for screening and referral of patients, adapted in style to familiar surroundings and manned in important part by paraprofessional personnel familiar with the neighborhood and its people, but also operated as a function of a nearby hospital, can effectively deliver to poor people humane and high quality health care.

The conclusion suggested is that urban hospitals, acting as community health centers, should sharply expand their out-patient service facilities and should develop genuine neighborhood centers for screening and referral of patients. The supply of black, Mexican, and Puerto Rican paraprofessional personnel should be expanded as rapidly as possible. Otherwise, much talent and empathy with the poor, which able and willing neighborhood residents possess, will go on being wasted for lack of practical understanding and organization leadership in urban hospitals.

Without doubt the single most urgent and most challenging aspect of improving the existing health care delivery system, when considered objectively and factually, is the lack of access by the urban and rural poor to quality care at reasonable cost. The reluctance of the urban poor to make use of complex, imposing, and impersonal facilities available in some inner city neighborhoods is a classic symptom of the urban poor documented by generations of sociological and psychological evidence as well as by an ample literature of black and other minority group poetry, novels, and drama. The increasing deterioration of central city neighborhoods in some cities, the welfare mess, the long-time evidence, now growing, of social disease, crime, and narcotics traffic and addiction are classic symptoms of social disorganization of a scope reaching far beyond health care alone. In fact, the delivery of health care is only one dimension in a complex of elements comprising the syndrome of poverty. Other dimensions are housing, family life, education, jobs, transportation, and crime. It is unfair and naive, as many experienced inner-city health care administrators point out, to expect that either health care financing or the availability of conventional facilities will effectively deliver health care to people so situated.

Yet, because the social costs of ill health, as well as other social costs, are mounting in such neighborhoods at disturbing rates, the need for practical, effective, commonsense approaches to each element of the poverty syndrome gains urgency. Business leadership, like other forms of leadership in the society, stands challenged by present circumstances in the Nation's major central cities The test of any new health care delivery system will be its proven ability to give access to quality health care even-handedly to poor and nonpoor. In the later 19th century the social task in burgeoning cities was to supply public health measures and sanitation as public goods to keep cities running, and growing. Today, the present task of the society is to come up with practical, effective, commonsense ways to provide opportunity to the poor, including genuine access to quality health care at reasonable cost. The effort is worthwhile in dividends of social benefit that might offset mounting social costs.

New arrangements for delivering health care to the rural poor are also needed. As mentioned earlier, health services are less available to rural than to urban residents, and even less available to the rural poor. The ratio of 75 doctors per 100,000 people in isolated rural counties, or of 69 per 100,000 in Mississippi, stands in stark contrast to New York State's 200 per 100,000. In 1969, there were 134 counties in the country with no active non-Federal physician, an increase of 36 counties since 1963.

In considering the delivery of health care to rural residents, and particularly to the rural poor, the problem appears to be one of purpose, leadership, and organization rather than technology or cost. It may also be a problem of organizing a delivery strategy, by analogy to organizing a marketing strategy in business. There was little evidence available that much systematic, professional study has been made of technical organizational or operations analysis issues in this field. For example, the question arises as to whether emergency facilities in rural areas might be combined more effectively for both automobile accident victims and rural residents. Technology is not lacking, as demonstrated by emergency facilities and techniques highly organized by military physicians using helicopters in Vietnam. Delivery arrangements combining emergency care for rural residents and travellers could be organized by regional hospital centers to provide effective communication and avoid duplication. Likewise, mobile clinics operating from such regional hospital centers could provide health maintenance and preventive care. Indeed, effective, mobile delivery arrangements for emergency and health maintenance care, it would seem, might have application in cities and suburbs as well. To our knowledge, little study has been made of the delivery system possibilities—little operational analysis has been completed—on these subjects.

Pluralism or wholesale reform?

Some people want wholesale reform of health care delivery systems. They argue that Americans cannot get adequate care unless the present horse-and-buggy health care delivery system is drastically restructured and reorganized. They contend that doctors cannot otherwise be attracted to places of health care deficit. They believe that incentive programs, such as loan programs, can only result in the poor treating the poor. They believe a fairer approach is a temporary physician draft of medical graduates. These people think that to foster competition between delivery systems will only result in delaying needed change because of the attitude of the health care profession. They fear that competition will only perpetuate the duplication of facilities. They believe that such competition puts consumers of health care at a disadvantage because they are often poorly advised about the nature and quality of health care and are incapable of making informed choices.

Above all, these people have concluded, a wholesale change from the present health care delivery system to prepaid group practice could cut from 10 percent to as much as 40 percent of waste from the estimated $63 billion spent in 1969 on health care in the Nation. One calculation by a business analyst suggests that a group system for all Americans could have reduced spending in 1969 from $63 billion to $47 billion and could have effectively eliminated today's shortage of doctors, as well as sizably reducing the utilization of expensive hospital facilities.

These views, at the least, emphasize the concern and impatience of people with the present delivery arrangements, a concern that can be easily shared. These views also amount to a warning that, unless the effectiveness of health care delivery is quickly and definitely improved, then the extension of financial access to health care for all Americans risks a complete breakdown of the existing delivery system which will then require replacement. Despite this threat, the preponderant evidence clearly indicates that the access goal of proposal I is now feasible in principle when combined with other appropriate steps to be taken in the health care system. What's more, the preponderant evidence is that the American people in this age of rising affluence, rising education, and quality consciousness strongly believe that today's and tomorrow's society can and should get the access goal, even if it means imposed change which some will view as more or less drastic. The American people, in short, believe that quality health care should be accessible to all and they intend to demand it.

Evolution, not revolution

Even so, there are convincing arguments for evolutionary change in delivery systems rather than for a national leap to the conclusion that any one delivery mode gives "the answer" now to providing delivery of health care.

The most basic argument for a pluralistic approach to health care delivery is a technical argument. There is no one system that will meet the diverse needs of the American people for health care. The founder of the first prepaid group plan, Dr. Sidney Garfield, holding this opinion, insists that Kaiser subscribers always have an effective choice of delivery systems.

For the U.S. medical and health care profession, for the consumer, and for the society, freedom of choice is preferable because it is more effective in human terms. For the consumer, it allows personal privacy, escape from "the system," and discretionary power to purchase. Some people, for their own private reasons, may wish to look after their health or lack of health as they choose, whatever may be professional opinion. In considering freedom of choice for people, hardly anything is more personal than health, and biological life itself. The business analyst who calculated the savings possible from an instant and complete change to group practice went to great lengths to emphasize his skepticism of their realism except as an illustration of the implications of hypothetical assumptions. The fact is that today significant numbers of families enrolled in prepaid group plans also go outside this system to obtain care at their discretion.

Freedom of choice for the physician is also crucial in human terms. Established doctors throughout the country who care for the sick and work abnormally long hours to do so have invested hard intellectual and physical effort over a lifetime as well as investing their professional judgment in private, fee-for-service practice. To expect such people of intelligence, education skill, experience, and energy—and people possessing essential services—to discard their practice overnight is to display unacceptable ignorance of human motivation. To require such change is to promote ineffectiveness of health care. Freedom of choice, however, does allow younger doctors starting out in practice, or others, to innovate. Says Garfield, "Medical school faculties should point out the advantages and disadvantages of all methods of practice to these young men so that they can choose wisely."

Freedom of choice has value in human terms for society. John Stuart Mill in his "Essay on Liberty," found the basis for individual freedom of thought and opinion in promoting mental well-being and reducing error. Freedom of choice has an analogous social value that innovative delivery systems must meet the of survival in practice rather than by fiat. It therefore has the economic value of avoiding expensive societal errors resulting from unintended results of a sweeping change imposed by law. Unintended results in many programs set by law for the Nation illustrate the risk: public housing, urban renewal, farm subsidy, and interstate highway system. It can be argued that medicare and medicaid, by dumping on the existing delivery system billions of dollars in increased demand for health care services of 35 million families in 3 short years, was almost irresponsibly erroneous, however well intentioned. Objective analysis of market behavior could yield no other result than anticipation of a powerful upward thrust to the price of health services. Political leadership that perceives the resulting rise in the taxpayer cost of medicare and medicaid solely as "gouging" piles irresponsibility on top of irresponsibility.

Freedom of choice as a societal value, finally, gives time for adjustment. Some criticism of existing delivery arrangements seems to imply no genuine anticipation of change, as for example concern that doctors may not be attracted to health care deficit areas. Ambiguous and inconclusive results of programs to deliver health care to the urban poor, sponsored by the Office of Economic Opportunity, cause skepticism that, of itself, prepaid group practice can reach the urban poor. There is no magic in prepaid group practice for the rural poor. Time is needed to see whether newer approaches, such as the Health Care Corporation, or the Medical Care Foundation, can give sufficient organizational unity and flexibility for serving the existing market, to innovate an operational mode for improving delivery to urban poor, rural poor, and victims of emergencies. Geographically, the health care market today is a metropolitan and megalopolitan market. Geographically, the metropolitan community of today consists of inner city, central city, suburbs, exurbs, and hinterland, and may spill over innumerable outdated political boundaries and even State boundaries. The "business" of health care delivery, like any other business, has to be structured to serve its market. There is room for competition, flexibility, and diversity in such a venture, and there is reason in the size of the market to expect competitive innovation in mode of delivery.

POLICY PROPOSAL VI. EFFICIENCY AND CONTROL OF COSTS

Business should encourage:

(1) All hospitals, extended care and nursing home facilities to adopt uniform accounting practices, financial reporting and costfinding systems;

(2) All hospitals to establish arrangements to review and monitor (peer review) the appropriateness of such items as hospital admissions, duration of stay, and treatment prescribed;

(3) All hospitals, extended care and nursing home facilities to accept reimbursement for services on a prospective, rather than on a retroactive ("costplus") basis, providing suitable methods can be devised;

(4) Physicians to accept reimbursement for "usual and customary charges" as payment in full for services rendered; and

(5) Each hospital to charge the same prices for the same services, regardless of the kind of benefit protection of the patient.

Employee benefit programs should:

(1) Be broadened to encourage health care in the least expensive manner; and

(2) Require deductibles and copayment for services received, where feasible.

The large increase in demand for health services in the 1960's dramatically highlighted the need for increased efficiency and control of costs. The prodigious increase in spending between 1950 and 1967, from $11.1 billion to $43.9 billion, or nearly 300 percent, came 48 percent from inflation, 18 percent from population growth, and 34 percent from quality improvements, greater use, and other factors. Medical costs rose faster than the Consumer Price Index and hospital costs topped the index items. The rise of private insurance and the advent of medicare and medicaid, resulting in only half of hospital expenditures coming from the pocketbook of patients, relaxed economic incentives to economize both treatment and use of hospitals.

Cost problems

The result was cost problems for hospitals which future rises in demand will make worse. Responsible medical experts estimate that as many as 30 percent of hospital admissions are unnecessary. The same illnesses could be treated outside the hospital. Patients go to hospitals—understandably—to collect on insurance. The problem is that actuaries and insurance authorities, according to these experts, "are notoriously short on flexibility, and therefore, prepaid medical care insurance is still strongly biased toward payment for in-hospital services." Also, physicians find it more convenient, timesaving and financially rewarding to see patients in hospitals. Also, social agencies exert pressure to lengthen hospital stays of some patients to fill voids in social and economic programs. And medical education has conditioned medical graduates to believe that only hospital care assures highest quality.

Another problem of costs is that Blue Cross and private health plans, in paying hospitals for patient care, reimburse hospitals for costs after care is delivered. No incentive is given the hospital to operate efficiently because virtually all its costs are covered.

Professional competition in using very expensive facilities and equipment is a third problem. Open heart surgery is one example. According to one hospital director, such surgery requires a team of 12 doctors, nurses, and technicians on constant standby. Unless 50 such operations are performed a year, the health team's skills deteriorate. But of 800 hospitals equipped to do open heart surgery, one-third don't have one operation a year, let alone 50.

Finally, hospital accounting procedures, financial reporting requirements, and cost finding techniques are inadequate. Reporting standards vary all over the lot. Hospitals lack even the discipline other industries must face which borrow from banks or float securities through investment bankers or are regulated by an agency.

Methods to contain costs

Discussion with top flight hospital administrators revealed that there is a real need for all community, nonprofit hospitals to follow uniform accounting practice and reporting techniques and cost-finding procedures. Cost per patient-day varies widely among hospitals in the same community. Many nonprofit hospitals report sizeable net income. At present business, the largest single private purchaser of health care services, does not know what it is getting for its money, and the only way to find out is to get a look at the figures.

To control costs, deductible and copayment provisions in health insurance policies are essential. The reason is obvious: without his personal involvement the patient has no real concern about costs. In a world of competing demands for resources, to remove personal involvement of the insured is to arrange for him to squander resources to his own loss in the enjoyment of these resources in other uses.

To control costs, coverage of health insurance should be redesigned to reduce drastically the unneeded use of hospital beds and facilities. Coverage of outpatient facilities, deductible for hospital admission, payment of identical fees for specified treatment in or out of hospitals—these are illustrative of measures needed.

To control costs, hospitals should not be permitted to charge, as they do, merely because of differences in benefit protection, different prices to various patients for the same services. This is an unjust hangover from the "charity" concept in which hospitals weighted paying patients with part of the cost of welfare payments, in effect levying a private tax on paying patients—the least appropriate taxpayers—to cover "charity cases."

To control costs, insurance carriers and Blue Cross could play a far more active rule in controlling costs. Walter J. McNerney, President of Blue Cross, believes his organization should support areawide planning, include strong incentives in contracts to support efficiency and economy, and finance prepaid group practice as an alternative form of care. Employers should encourage such moves promptly.

To control costs, operational analysis by hospitals should quickly become widespread. One hospital director has in effect a "predicted length of stay profile" for each diagnosis, to use in measuring a doctor's performance. He requires a prospective rather than a retrospective hospital utilization review to be carried out, so that each discharge can be measured against the predicted length of stay for that diagnosis. He suggests greater reward for doctors whose performance results in lowering community costs. The average length of stay in his hospital is much lower than surrounding institutions. These illustrations suggest the scope for applying to the hospital costsaving operational analysis familiar to industrial engineers for a generation or more.

To control costs, some move must be taken by the society soon to deal with the more frequent malpractice, suit being brought against both doctors and hospitals, sometimes "with a long tail," that is, long after treatment has been given. The consequence is over-elaboration of examination and testing by doctors and hospitals as they respond by practicing "defensive" medicine. The committee was concerned about the malpractice issue and wishes to express its concern, though it did not formulate a specific policy proposal.

The recommendations of policy proposal VI reflect a general condition characteristic of the behavior of the hospital and other health care institutions as a group, together with their supporting professionals and insurors. The condition is that these groups are only beginning to adjust their conduct to the idea that Americans are changing their values and consciousness respecting health care. Health care professionals have practiced in an environment that is a curious mixture of philanthropy, science, humanitarianism, and professional decorum—with perhaps a dash or two of obscurantism. But with the tremendous pressures on employers of rising employee benefits, the increasing financing of health care by tax dollars, and the large increase in the demand for resources by the society for other social purposes, the pressure of more cost effectiveness in the organization and operation of health care services will keep rising. Consumerism—a concern for higher standards of organizational economizing—is gathering force in the health care industry.

FINANCING

POLICY PROPOSAL VII. FINANCING SERVICES

The Federal Government should provide health insurance protection to replace medicaid for those on public welfare, and others below the poverty income line who are not covered by employer plans or medicare, or who are unemployed.

POLICY PROPOSAL VIII

Every American should be protected against the risk of being pauperized by catastrophic expenses of illness. Private program, supplemented by a public program is necessary, financed by Federal appropriations, should be developed to achieve this objective.

POLICY PROPOSAL IX

All employers, public and private, should be required to provide all their employees a minimum basic health benefits package, including ambulatory and out-patient care.

POLICY PROPOSAL X

The self-employed should receive the same tax treatment for health insurance premiums as employees do under employer-financed group plans.

POLICY PROPOSAL XI

In assuring access to health services for all Americans, the Federal Government should not provide such care directly, purchase health insurance protection from private carriers for everyone, nor initiate a federalized national health insurance system.

To assure access to quality health care for all Americans at reasonable cost" (proposal I) requires new means of financing health care. To see why, it is helpful to review what and how the U.S. people pay for health care.

Who pays what for health care

The United States spends more than $67 billion a year on health care, about 6.8 percent of the entire gross national product, a rise from 4.6 percent of GNP in 1950 and 5.3 percent in 1960. This is more than the Nation spends on Social Security or formal public and private education. It is more than the Nation spends on defense less Vietnam. From 1950 to 1969, total health expenditures rose fivefold in size, an average of 8.8 percent a year, and in the last 3 years, an average of 12.2 percent. Per capita spending on health care doubled during the 1960's. Of the total dollar spent on health care in fiscal 1969, 43 cents went to hospitals, 23 cents went to doctors, 12 cents to drugs, 9 cents to dentists and 13 cents to other spending. Since 1950, the share of the health care dollar going to hospitals rose from 35 cents to 43 cents, while the share to doctors dropped from 25 cents to 23 cents.

Despite the rising share of U.S. total spending that is going to health care, financial access to care is not available to all Americans. By 1970, of the 203 million people in the United States, about 88 percent of the civilian population—175 million people—had some protection against inpatient hospital expenses, 80 percent—162 million—had some coverage against surgical expenses, 67 percent—135 million—had regular medical expense insurance, and only 35 percent—72 million—were covered for major medical expenses. Put another way, in 1968, among the 177 million people under 65, not in institutions or the Armed Forces, 20.5 percent had no hospital insurance, 21.9 percent had no surgical insurance, 34.5 percent had no in-the-hospital medical expense insurance, 50 percent lacked insurance to cover X-ray or laboratory charges incurred when not in the hospital, 57.5 percent had no insurance for visits to doctors' offices or care at home, 61 percent had no insurance against the cost of prescribed drugs, and 97.5 percent had no insurance against dental expenses.

Some 40 percent of the Nation's health care bill is now paid by government—Federal, State, and local—through (1) health programs for Government employees (2) servicemen and their dependents, (3) veterans, (4) medicare and medicaid, and (5) State and local hospitals. Of the non-Government portion of the Nation's health bill, private health insurance provided through Blue Cross, Blue Shield, and commercial insurors together pays about one-third. Individuals pay the other two-thirds out of their pocketbooks.

Federal Government experience with medicare and medicaid has been unhappy. Also, the growth of "third party" payment of medical bills through Blue Cross, Blue Shield, and group insurance has inflated health care costs. Government forecasts of medicare spending were too low, but forecasts for medicaid were worse. By 1972, with 48 States enrolled, medicaid costs are estimated at $7 billion. Medicaid should be considered along with welfare costs, rapidly mounting in major cities and States and subject to administrative tangles and abuses as well as great disparities among the States and regions. Insurance "third party" groups have inflated costs by being content to serve largely as conduits for funds, a sort of automatic "cost-pass-through" mechanism without hard scrutiny of costs or charges.

Proposals for access to care

From the background of present circumstances concerning the State of the health care system as portrayed herein, including its financing, here are thumbnail sketches of six major proposals before Congress in 1971 for financing care (see appendix A for analytical comparative summaries of plans).

(1) The Health Security Act (Representative Griffiths and Senator Kennedy) would provide Federal health insurance for all U.S. residents, financed through a Health Security Trust Fund, to give virtual cradle-to-grave coverage. The national health insurance for all residents would be financed by new taxes: 50 percent from general revenues, 36 percent from a new tax on employer's total payrolls of 3.5 percent, 12 percent from a 1-percent tax on employees' wages and on unearned income up to $15,000 a year initially; and 2 percent from a tax of 2.5 percent on self-employment income up to $15,000 a year to start with.

(2) "Ameriplan"—The American Hospital Association—would provide a nationwide universal health insurance program for all with delivery of health services provided through new organizations called Health Care Corporations. Three "package" plans would be provided: (a) a Standard Benefits Plan of basic hospital, physicians' and related care, (b) a plan covering Catastrophic Illness and Health Maintenance, and (c) a Supplemental Benefits plan. The Standard Benefits package must be purchased by everyone, from health insurance carriers and the "Blues"; Health Maintenance and Catastrophic Benefits are sold only by the Health Care Corporations to those with Standard Benefits; and Supplemental Benefits are for optional purchase. Under Ameriplan those who can afford, will pay; Government pays for others. It is a three-part financing plan: (1) general revenues for all the care of the poor and near-poor; (2) a payroll tax on all workers and employers to pay for the aged and the Catastrophic and Health Maintenance benefits; and (3) direct private payments for the Standard Benefits Package and Supplemental Benefits.

(3) A catastrophic illness proposal—Senator Russell Long—would provide Federal costsharing only in illnesses that result in "catastrophic" costs. Since medicare and medicaid already cover the poor and those 65 and over, all other workers covered by Social Security would get the benefits with the exclusion of the first 60 days of hospital care, and the deduction of the first $2,000 of expenses per family per year. The plan would cover 80 percent of the cost of covered care and services. The plan would be financed by payroll taxes imposed on both employers and employees paid into a separate trust fund.

(4) "Medicredit"—the American Medical Association—would provide financing of health care through an income tax credit for buying private health insurance. Those with little or no tax liability would receive a certificate or voucher to be used in buying insurance. The amount of the credit would vary depending on income tax liability, the amount of the credit decreasing as income tax liability increased. Medicare for the aged would be retained but medicaid for the poor would be replaced by the certificate system. Since the cost of Medicredit would be financed by a loss in Federal revenue, the loss would either be recouped by other taxes, an increase in the national debt, or Federal expenditures less than they would have been without the loss.

(5) A two-part plan for workers and the poor—the Nixon Administration—would require all employers to provide minimum health insurance to workers and their families, including catastrophic cost protection. Free health insurance would be provided for poor families and a graduated premium charge would be levied for near-poor families. Medicare and medicaid would be continued for the

aged, blind, and disabled. Employers would pay eventually for 75 percent of the cost of the basic plan for their employees.

(6) "National Health Care Act"—the Health Insurance Association of America—would make comprehensive health care insurance available to all. Employees would get a 100 percent income tax deduction of premium costs, the Federal Government would pay the costs of the poor, and the near-poor would pay for some costs, depending on income, while the Federal Government paid the rest of their costs. Benefits would be provided through State pools of private health insurors. The cost would be borne by the Federal Government to the extent of deductions by a loss of revenue, either offset by other revenues or by reducing spending relative to what it would otherwise be.

The financing proposals

The proposals for financing health care services (policy proposals VII–XI) may be weighed separately, but they should be considered in relationship with one another to examine how they are directed to meeting the national goal for the health care system, "to assure access to quality care for all Americans at reasonable total costs for services provided, in a manner that maximizes the advantages of individual freedom of choice and of flexibility to adjust to changing needs" (policy proposal I).

As a floor of protection against the risks of catastrophic financial loss from illness, policy for the Nation should protect all Americans against the risk of being pauperized by illness. Most costs of illness are manageable, but some can mount to many thousands of dollars. Although the incidence of such catastrophic illness is rare, the effect on a family is devastating. If all Americans are to have financial access to health care at reasonable cost, the notion of health care "charity" and the funds available to health care institutions for "charity" should be and will be limited. Catastrophic illness costs are an insurable risk, and personal and social benefits are produced in preventing individual large losses—with resulting social losses—by risk-sharing, through Government if necessary.

The poor, who today too often lack both financial and operational access to health care at reasonable cost, have Federal-State assistance for health care through medicaid. Under consideration of 1971 in the Congress as well is the revision of the welfare laws to increase the Federal role in the welfare system. Thus, the principle of Federal aid to the poor in cash and in services is now firmly established as national policy; indeed, the debate is now over how much more responsibility the Federal Government should assume.

The evidence is persuasive, however, in the skyrocketing costs and the abuses of medicaid that it is providing neither quality care nor care at reasonable total costs. Medicaid rules create serious work disincentives because benefits are cut off at fixed income levels even if a family's health care needs are high. Program coverage varies greatly among States while health care costs very among families without regard to their location. The burden on State governments of financing medicaid is onerous because of its design. And the design of medicaid actually discriminates in favor of the poor against the nonpoor by financing care which the economizing incentives of nonpoor families would cause them to abstain from. Medicaid should be replaced by Federal health insurance protection for welfare and other poverty families not covered by employer plans or medicare, or who are unemployed.

The choice of providing financial access to quality health care for employed nonpoor Americans and their families at reasonable cost and with freedom of, choice and flexibility lies between provision of such access by Government, by employers, or by individual American families. Already, however, employers of a substantial proportion of the labor force provide various amounts of health care insurance protection among employee benefits costs. Business firms, as a group the largest single private consumer of health care, have strong financial incentives to buy health care protection at reasonable cost. Business firms also have technical managerial skills and abilities which allow them, on behalf of their employees, to monitor and evaluate the reasonableness of health care costs. Public employers have similar incentives.

Given the prospect of rising income levels and the trend toward employer provision of noncash benefits—employee benefits—as a rising proportion of direct labor costs, the prospect seems likely for employed, nonpoor Americans to gain health care insurance protection through work compensation if the responsibility for providing access to health care remains theirs.

Therefore, to assure a floor of protection to access which is equal among various regions and between urban and rural areas, and to assure quality care at reasonable cost with freedom of choice and flexibility, national policy should require all employers, public and private, to provide their employees with a minimum basic health benefits package. Ambulatory and out-patient care should be included to avoid excessive and expensive use of hospital facilities because treatment coverage is limited to hospital care.

To provide access to all Americans of quality health care, then, includes (1) a program for all Americans, through Federal funding if needed, of protection against catastrophic illness; (2) Federal health insurance protection replacing medicaid for the welfare poor, the nonworking poor, and the unemployed poor; (3) a basic health protection package for families of employed Americans provided by all employers, public and private; and (4) for the self-employed, the same tax treatment for health insurance premiums as employees receive under employer-financed group plans.

The choice of providing financial access to health care for all Americans through direct Federal provision of care, through Federal purchase from private carriers of insurance protection for everyone, or through a national Federal insurance system should be rejected. Proponents of Federal national health insurance argue that only a national health insurance program financed by the Federal Government can resolve the health care system's problems. They hold that only the Federal Government, with its concentrated power, can marshal the funds and enforce the guidelines needed to attack the total health care problem—personnel, control, facilities, delivery system, cost. Control of such insurance by an independent board assures response to changing conditions, they argue. These proponents themselves, however, reject direct Federal purchase of insurance from private carriers or direct Federal provision of care.

There are strong arguments, however, against having Government establish a national Federal insurance system. Most people in the United States prefer personal financial responsibility for their own needs and are able to meet them. The tradition has yielded personal motivation, self-respect, accomplishment, and satisfaction, and it has contributed to U.S. standards of living and the quality and extent of public goods such as education. Most people prefer the freedom and privacy which comes from the desire for personal financial responsibility. National health insurance would encounter the disillusionment of raising demands and then sobering expectations—as in the case of medicare and medicaid—as its promises had to be curbed by the shortages of facilities and manpower and rapidly escalating costs. The problem with the health care system is not a dollars problem, it is a manpower-facilities-organization problem. To load the system with sudden demand is as irresponsible as to delay needed reforms in the supply and provision of service.

What is wanted, as this study shows, is increased competition and flexibility in the supply of service, increased adaptation of personnel and facilities to today's society, and increased vigilance by many purchasers of health care to insist that the interests of health care consumers are protected. The threat of national health insurance is a gradual loss of these possibilities as the monoply power inherent in a centralized control system generates an expert bureaucracy which stultifies adaptation and change.

COMPARATIVE SUMMARY OF KEY PROVISIONS OF MAJOR HEALTH PROPOSALS-92ND CONGRESS

	HEALTH SECURITY ACT H.R. 22 (Griffiths, D. Mich.) S3 (Kennedy, D. Mass.) AFL-CIO	NATIONAL HEALTH INSURANCE PARTNERSHIP Aministration Proposal No bill introduced
Concept and Eligibility	Government universal insurance program financed by employer/employee payroll tax and general funds, for all U.S. residents. Would replace Medicare and Medicaid; eliminates private insurance industry participation.	A national program covering all Americans, with requirement that employers provide health insurance protection for employees and their dependents that meets federal standards. Federal health insurance for low income families with children not covered by employer plans.
Benefits	Comprehensive health benefits; nearly unlimited physician/hospital services, and dental care to age 15. Some limits on nursing home & mental health care/drug use. No cost-sharing by beneficiaries.	Employer-employee plans must include inpatient hospital and physician services, diagnostics, child & maternity care, family planning and catastrophic protection. Maximums on deductibles and coinsurance. Special family health plan for welfare families includes similar benefits.
Manpower	Restructures existant resources; promotes new sources through grants, loans, education subsidies. Emphasis on training health professionals for primary health care teams/group practice. Incentives to place manpower where needed; aid disadvantaged	Incentives for medical professionals to relocate in low income areas; subsidies to medical schools, student loans to increase health professionals -- with forgiveness provision for practicing in underserved areas. Creation of National Health Service Corps to work in scarcity areas; subsidies to train para-medical personnel.
Facilities	No specific provisions; gradual change through regional/state planning. Incentives favor organization of group care facilities over solo practitioners.	Encourages creation of Health Maintenance Organizations (HMO's) favoring group medical practice and prepaid care; establish Health Education Centers in underserved areas. Federal money, through planning grants and loan guarantees, made available to initiate HMO's, plus funds to create Health Education Centers.
Effect on Delivery System	Sponsors would: increase availability of services; priority to ambulatory care under comprehensive organizations; strengthen planning & budget controls; increase consumer representation; provide group practice incentives & discourage fee-for-service practice.	Improves delivery system by encouraging formation of HMO's, providing comprehensive services on a fixed-fee basis.
Evaluation and Cost Controls	Sets national standards for participating individual & institutional providers. Program is pre-budgeted at all levels; costs expected to rise on controlled, predicted basis under state & regional review. Plan equitable distribution of resources throughout nation & reduction of costly inpatient services; elaborate judicial review.	HMO's will operate on a budgeted basis, offering incentives for better preventive care and efficiency. Cost-sharing by subscribers, stress on illness prevention, designed to contain costs & demand for services. Proposes greater regulation of health insurance industry. Employers would absorb most rising medical costs.

COMPARATIVE SUMMARY OF KEY PROVISIONS OF MAJOR HEALTH PROPOSALS-92ND CONGRESS

	HEALTH SECURITY ACT H.R. 22 (Griffiths, D. Mich.) S3 (Kennedy, D. Mass.) AFL-CIO	NATIONAL HEALTH INSURANCE PARTNERSHIP Administration Proposal No bill introduced
Impact on Public and Private Programs	Repeals Medicare & most of Medicaid services; eliminates need for employers to provide employee health insurance (but "savings" go to employees). Eliminates participation of private insurance carriers (regarded as non-essential).	Medicare and Medicaid retained for aged and disabled. Private insurer role, and Federal regulation of the health insurance industry, will increase. Employers required to provide health insurance for their employees.
How Administered	Run by Health Security Board under HEW; includes advisory council with majority consumer representation. Regional offices empowered to develop area & local priorities & funding; local offices act as citizen ombudsman. States focus on audits/inspections.	Employer-employee plans underwritten and administered by private insurance carriers under Federal regulation. FHIP and Medicare are federally-run, using insurance carriers as fiscal intermediaries. Residual Medicaid is federal-state administered.
Estimated Costs	Sponsors claim startup of $53 billion (in fiscal 1974) before controls become effective; Administration estimate is $77 billion.	Employer-employee premium costs for health insurance could rise from present $13 billion to $20 billion by 1974 according to federal officials. Cost of Family Health Insurance Plan estimated at $1.2 billion. (1st year)
Financing	Through payroll taxes and federal general revenues including 3.5% employer wage tax, 1% on wages and unearned income and 2.5% self- employment tax. Employee tax ceiling: $15,000 to start; employers' tax levied on entire payroll.	Employers must pay at least 65% of total premiums through 1975, increasing to 75% in 1976. Family Health Insurance Plan (FHIP) financed from general funds of treasury with government paying full cost for those with income below $3000, with premium payments on sliding scale between $3000-$5000.

	NATIONAL HEALTH CARE ACT H.R. 4349 (Burleson, D. Texas) Health Insurance Association of America	AMERIPLAN American Hospital Association No bill introduced
Concept and Eligibility	Standard benefit package for poor, near-poor, and indigent uninsurables, with policies purchased from private insurance carriers, and premium costs federally subsidized. All others are covered by purchasing individual or group health insurance, and by Medicare.	A nationwide health insurance program available to all, regulated by state & federal government. Delivery of medical services would be through Health Care Corporations -- either public or private, serving specific geographic areas with a defined population.
Benefits	Uniform benefits guaranteed the poor, available to near-poor, uninsurables. Provides basic and catastrophic insurance benefits -- ultimately would be comprehensive; federal standards set for group plans.	Three packages available: Standard Benefits - which all must have, sold by insurance carriers & the "Blues"; Health Maintenance and Catastrophic Benefits - sold only by corporations to those with Standard Benefits; Supplemental Benefits-optional.

COMPARATIVE SUMMARY OF KEY PROVISIONS OF MAJOR HEALTH PROPOSALS-92ND CONGRESS

	NATIONAL HEALTH CARE ACT	AMERIPLAN
	H.R. 4349 (Burleson, D. Tex.) Health Insurance Association of America	American Hospital Association No bill introduced
Manpower	Improved federal student loans to train health professionals (doctors, nurses, lesser skilled); grants to train ambulatory care teams and for service in underserved areas.	Health Care Corporations are responsible for identification, recruitment and training of personnel. Responsible for quality and competence of manpower through cooperation with recognized medical authorities (accreditation, licensure), education institutions (development and training), and for peer review.
Facilities	Provides grants and loans to build or modernize comprehensive ambulatory care centers.	Health Care Corporations develop own needs under state supervision.
Effect on Delivery System	Federal grants and loan guarantees for ambulatory health care centers to reduce use of hospitals; loans and grants to promote education and get manpower where needed.	Reorganizes the delivery system by making HCC's directly responsible for provisions of all care at community level-with hospitals as "hub" of the system. Emphasis on preventive care.
Evaluation and Cost Controls	Contains deductibles and co-payments to control over-utilization; provision for state review of provider health care charges; provides authority to withhold funds for expansion of projects deemed unsound; peer review of treatment and fees.	Provision to evaluate services through peer review and community participation; copayments and limitations on service under Standard Benefits Package discourage over-utilization and contain costs. States control HCC charges and professional fees.
Impact on Public and Private Programs	Medicaid would be absorbed into state reinsurance pools, underwritten by carriers. Scope of employer plans should broaden to include ambulatory care, because of tax penalty for noncompliance.	Medicare and Medicaid would be replaced. Private health insurance industry would be regulated by a National Health Commision.
How Administered	Secretary, HEW sets federal standards monitoring operation of state-regulated, privately insured pools; payment under federally-supported programs subject to peer review and, in the case of health care institutions, based on State Health Care Institutions Cost Commissions.	Federally administered through new independent National Health Commission, to set standards and insurance benefits. State Health Commissions regulate Health Care Corporations -- locally responsible for providing comprehensive (maintenance, primary, specialty, restorative, health related) care.
Estimated Costs	Health Insurance Association of America (sponsor) estimates $3.4 billion 1st year (1970 est.).	No estimate available.
Financing	State-federal payments (full premiums for persons on public assistance; partial for those of limited income). Individual and/or employers meet costs of their own private plans.	Those who can afford, will pay; government pays for others. Provides 3-part financing: 1) general revenues for all care of poor & near-poor 2) payroll tax on all workers and employers to pay for aged and Health Maintenance and Catastrophic benefits 3) direct private payments -- for Standard Benefits Package and Supplemental Benefits.

COMPARATIVE SUMMARY OF KEY PROVISIONS OF MAJOR HEALTH PROPOSALS-92ND CONGRESS

	HEALTH INSURANCE ASSISTANCE ACT - MEDICREDIT H.R. 4960 (Fulton, D. Tenn.) S. 987 (Hansen, R. Wyo.) American Medical Association
Concept and Eligibility	A system of income tax credits for all U. S. residents to offset cost of private health insurance. Participation is voluntary, but automatic for the poor.
Benefits	Establishes minimum benefits for approved insurance plans; catastrophic illness protection. Outpatient and physicians' services. Limited hospital care. Unlimited extended coverage after expending a percentage of net-taxable income.
Manpower	No provisions.
Facilities	No provisions.
Effect on Delivery System	Proposal contains no provisions to change present delivery system
Evaluation and Cost Controls	Insurance policies will contain deductible/copayment features to control overutilization of hospitals' and physicians' services. Insurance carriers are subject to state control and must form "risk pools".
Impact on Public and Private Programs	Medicaid would be absorbed; Medicare would continue. No marked change in current role of private health insurers.
How Administered	Federal control through a National Health Insurance Advisory Board, empowered to set minimum benefits and set standards for state use in approving plans and carriers.
Estimated Costs	1970 cost estimated at $8 billion by AMA and $15 billion by Administration.
Financing	By insurance premiums for those able to buy (with tax credits scaled to income) and federal subsidation,through general revenues,of low income groups having zero income tax liability.

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[Attachment B]

DEVELOPING HEALTHY WORLD BUSINESS CLIMATE

By CARL H. MADDEN, *Chief Economist*

Has the United States lost its competitive edge in world trade? By one measure, our trade balance, it may have. Last year we experienced the first annual trade deficit in this century: $4.6 billion. But partly because of dollar devaluations, so far this year we have been running a surplus at half that rate. Although the short-term future is clouded by the fuel shortage, which may inhibit the production of exports and raise the prices of imports in the next few years, projections by Hendrik Houthakker are optimistic for exports in particular and our balance of payments as a whole. For next year he projects a $10 billion export surplus, for example, and by 1979 a $21 billion surplus. The computer model used for these projections assumes continued growth with some inflation both in this country and in its major trading partners. According to other computer models used by Dr. Houthakker and his colleagues, the effect of energy shortages on overall output and the price level will not be serious over the next decade, but they do foresee "temporary dislocations due to energy shortages during the next few years." These conclusions are based on the high price sensitivity of both fuel supply and fuel demand which, it is contended, have not been taken sufficiently into account by such groups as the National Petroleum Council. In Dr. Houthakker's opinion the Council overestimates the future demand for energy. According to the calculations of Dr. Houthakker and his colleagues, the imposition of an additional 7½ cent excise tax on gasoline on July 1, 1973 would have reduced consumption in 1975 by about 7 percent, thus keeping it at the 1973 level.

THE ENERGY PROBLEM—SHORT AND LONG-TERM ASPECTS

Experts tell us that in the next 3 to 5 years we will continue to have energy shortages, especially of fuel oil. The Arabian states are behaving like an international cartel, not only by setting higher prices for their oil but also by discriminating among markets. It is clear that we can no longer safely depend on Arabian oil to fill the energy gap created by the rising proportion of our oil demand met by imports. Oil imports accounted for 27 percent of our consumption last year and will account for about 33 percent this year. Imports are estimated to rise to at least 50 percent of our requirements by the end of the decade. Much of these imports would have come from the Middle East.

Over the next decade we face, not an energy crisis, but a collection of problems. Energy is supplied and responds to demand through a network of markets that have been upset by three main developments.

The first disturbing development is the very rapid increase in the demand for energy imposed by our current technology and high rate of economic growth. Energy consumption in the United States is eight times the world average and has been growing 7 percent yearly.

The second development is the extremely slow absorption of environmental costs into the supply prices of energy.

The third, and probably the most important development, is the distortion of the market mechanism by public policy.

Regarding the first development: For two decades after World War II electric power generation costs were greatly reduced by building larger and more efficient plants. But after 1965 capacity did not keep pace with demand, partly because nuclear power came on line more slowly than expected, and partly because the post 1965 inflation ballooned construction costs.

Regarding the second development: environmental costs have been imposed not only in the form of more stringent operating standards but also in the form of opposition to new generating plants, especially nuclear plants. Construction of any plant can be challenged in the courts under the National Environmental Policy Act and, where a court has felt uninformed about environmental impacts, the safest procedure has been for it to stop planned construction.

Regarding the third development: public utility regulation has held prices down to the level of historical costs which, in an inflationary period, understate true costs. As a result, power has been artificially cheap, misleading business and consumers into more power-intensive investments, Moreover, in the oil industry since August 1971 price ceilings on both crude and refined oil have discouraged expansion of refinery capacity. There have been no new refineries in this country in the past 3 years, although some are now underway.

Energy from coal and natural gas has been adversely affected by the same kinds of influences as have affected electric power and oil. A further complicating factor in the case of gas has been the tremendous increase in demand for it because it is a clean-burning fuel.

In the longer term the United States is in a good position to bring the supply and demand for energy into balance through contraction in demand and realization of new sources of supply. The most important single source of additional energy supplies is oil imports from the Caribbean and from the Persian Gulf About three times as much new capacity is being developed every year in the Persian Gulf as 10 years ago. In round numbers oil reserves in the Persian Gulf area are 220 billion barrels—excluding Saudi Arabia's 140 billion barrels—5½ times our domestic reserves. The international oil cartel, OPEC was formed in February 1971 at Tehran with the cooperation of the United States which mistakenly saw it as a means of guaranteeing a steady and increasing flow of oil to itself. As is true in all cartel arrangements, unless the current Arabian boycott is complete, as times goes on, it may become less effective because of the temptation for non-Arabian producers to divert shipments from non-American to American customers, attracted by higher prices.

In addition to stepping up our imports of non-Arabian oil, over the longer term we will be in a position to develop a national energy supply policy by devoting more resources to energy research and development. The President's announcement in early July and reaffirmation in early November of a $10 billion R. & D. energy research program should speed up the development of clean energy. This would include synthetic oil and gas from coal—of which we have one-third of the world's known supply—and research into other sources of energy besides nuclear power, such as oil shale, strip mining, geothermal energy, and solar energy. The utilities are pushing new technologies, such as magnetohydrodynamics

(MHD) to supplement nuclear breeders in the 1980's, MHD offers thermal efficiency as high as 60 percent, compared to 40 percent for fossil-fuel plants and 33 percent for fission-powered plants.

In both the short and long run decontrolling prices in the energy industry—including natural gas, which Congress still controls—will stimulate production and limit demands for energy.

Regardless of the economic adjustments that will have to be made in the next few years because of the fuel shortage, the long-run prospects for continued growth and development of the world economy will depend in large measure on the willingness of nations to relax existing barriers to trade and investment. The nationalistic reaction of Western Europe to the reduced flow of oil from the Middle East does not augur well for such cooperation. It is only being realistic to recognize the present danger of a general backsliding into the beggar-my-neighbor policies of the leading nations in the 1930's which led to a downward spiral of successive contractions in world output, incomes and employment, culminating in a worldwide depression.

If this dismal outcome is to be avoided, national policy in all the industrialized nations, including the United States, has to face up to the question: Shall we protect declining industries that are being subjected to intensified foreign competition or shall we by various incentives, ease the necessary shifts of capital and manpower from such industries into those in which we enjoy a comparative advantage, thereby contributing to continued world economic growth?

For a long time business has been trying to tell the country that our Federal tax system, by penalizing savings and investment more than in other industrial nations, slows the growth and updating of our lagging stock of capital and so retards productivity in the economy and makes us less competitive internationally.

Economic growth requires investment, but in the period 1960–71 the United States lagged behind all major industrial nations in the share of total otuput allocated to capital formation. Linked to these developments, productivity gains were less than half the average in 10 major industrial nations, 2.9 percent compared to the other nation's average of 6.1 percent.

Moreover, prospects for productivity gains in the 1970's in the United States are slightly below historical trends because of several factors: a continuing shift from high productivity goods production to lower productivity services, slower emigration from farms, a leveling of research outlays and a lesser emphasis on science, engineering and business in formal education.

Nations Have Become More Interdependent

The world fuel shortage is only one graphic current example of an overwhelming fact, the more industrialized each country becomes, the more dependent it becomes on its trading partners.

Powerful forces are remolding the world economy, new technology, widely diffused through international business, has promoted international division of labor in the industrialized West. Burgeoning multinational corporations have accelerated this development. And rising expectations have made less developed nations impatient to share the West's affluence. But at the same time, the economic gap between the affluent West and the underdeveloped countries has widened as population growth in these countries has outstripped their capacity to produce.

From the end of World War II through the sixties much of the world depended on a continuing flow of food, raw materials, and capital equipment from the United States and other New World countries. During that period the United States accounted for 85 percent of total export surpluses in the Western World, with the bulk of our exports being financed through our own dollar credits.

In the fifties, when the Marshall plan and other postwar reconstruction plans were being implemented, Europe and Japan were still hastily rebuilding their wartorn economies and the U.S. economy was the strongest in the world. Today our competitive strength is challenged by Japan and the enlarged European Economic Community which now accounts for half of world trade in industrial products.

By 1970 world trade had increased to five times its 1950 level, but the increase primarily benefited the Common Market and Japan. The Common Market's share of the vastly expanded postwar trade volume just about doubled, from 15 percent in 1950 to 28 percent in 1970. Japan's share rose from 1 percent to 6 percent. Japan's record of export growth has been unparalleled, an annual growth rate of 19 percent over the 1950–70 period. In sharp contrast, the United States' share of world exports has declined from 16 to 14 percent.

During the 1950–70 period, there were many parallels between the leading economic position of the United States and Britain's earlier heyday when the machine processes of the Industrial Revolution gave her technical and economic superiority. Like Britain in earlier times, the United States has led in the development of world trade and investment. But the strength of nationalistic sentiment among the underdeveloped countries precludes any organization of trade and investment by the United States along 19th century British lines. In the 19th century, the world trading system rested on a division of labor between advanced industrial creditor countries and backward raw-material producing debtor countries. Today the trading system is being refashioned, not through colonialism, which perished with the first World War, but through increasing internationalization of business and production under the aegis of the multinational corporation.

International trade has gone through two phases in the last century. Its first phase in the first half of the 19th century was the exchange of European manufactures for nonmanufactured goods from the rest of the world. From about 1860, Western European capital began to flow into construction and operation of ports, railroads, and plantations all over the world. Production was then developed on a large scale for export to Europe. Mining, together with tea, cocoa, coffee, sugar, rubber, jute, and indigo plantations, tin smelters in Malaya and refrigerated meatworks in Argentina swelled the volume of world trade. This outpouring of capital and organizing skills raised both exports and imports, but the colonial world became dependent on the West. The ending of this colonial dependence has ushered in the second phase of international trade—industrial nations' dependence on imports of vast amounts of industrial raw materials and energy sources that are only available in quantity from developing countries. The "have" nations are becoming the "have nots" as their dependence on raw material producing areas, like the Middle East, increases.

Of all the diverse forces affecting economic growth and international interdependence today the most powerful and pervasive is applied science, including the science of management. The vehicle for worldwide technological diffusion is international business enterprises, sometimes taking the form of foreign branches or subsidiaries of firms headquartered in industrialized countries, at other times taking the form of joint enterprises representing several different industrialized countries. These companies have interpenetrated each other's markets as well as the markets of the less advanced countries. Productivity cannot be expanded in countries such as India and China unless capital, technical skill, and organizing ability are provided them. But these productive requirements can no longer be furnished on the old colonial terms. The nationalistic leaders of the third world are highly sensitive to majority control of their industry by foreigners and are moving, as in Latin America, the Middle East, and even in industrialized nations like Canada, to vest such control in the hands of their own nationals.

To the extent that the world trading system still rests on a division of labor between advanced industrial creditor nations and backward raw material producing debtor countries, it must be refashioned. There will always be scope for territorial division of labor. But increasingly world division of labor will be based on advantages in natural resources rather than organization of technical knowledge over which the dominant white race can hardly expect to enjoy a permanent monopoly. Of all human skills the organization of technical knowledge is not only the most productive but also the most readily transferable.

THE "MIXED ECONOMY" IS GOING INTERNATIONAL

Four major developments have internationalized "the mixed economy": national economic planning, new forms of business enterprise, the opening up of trade between the communist and noncommunist world and greater capital flows between countries. The national plans now being drawn up in some of the underdeveloped countries, such as China, lean heavily on the Russian experience, especially in the priorities of development, the location of strategic industries and, above all, in the training of technicians. If necessary, these underdeveloped countries, like Russia in the past, will endure a transitional period of forced savings to accumulate the capital necessary for modernization and, like Russia today, they can be counted on to add increasingly to world trade. Private enterprise must be prepared to accept and work within the new political order.

Internationally, new forms of business enterprise have arisen. U.S. corporations have poured capital into the petroleum rich areas of the Middle East. The Rockefeller interests have created new industries in Latin America with the assistance of national governments and the participation of local interests. It has become standard practice among many corporations to secure investment of local foreign capital in branch operations abroad and to recruit and train local management.

But the major challenge to the resourcefulness of the Western World lies in Asia, including Russia. The challenge is to bring Asian countries more fully into the world trading system. The circuits of world trade and the multilateral clearing of payments cannot be restored until Asian nations can utilize the technical skills and organizing skills of the scientific West. This is largely the problem of putting to work the productive capacities of corporate enterprise in ways acceptable to the nationalism of the underdeveloped countries. The expansion of productivity in Asia is the key to continued growth in the triangular goods and payments flows among the United States, Europe, and Asia.

We are beginning to see an accelerated "reverse flow" of direct dollar investment not only from West Europeans but particularly from the Japanese, stimulated by the cheapening of our dollar by as much as 46 percent compared to the mark and 27 percent compared to the yen. It is entirely possible that before long some American writer will produce a book entitled "The European Challenge," comparable to Jacques Servan-Schreiber's decade-old "The American Challenge," which warned that American firms threatened to take over West European industry. What has happened to this dire prediction? Rather than becoming dominantly American, investment in Western Europe has become more internationalized through consortia and similar arrangements.

In a recent year, of a gross world product of $3 trillion, about one-third was produced by the United States, one-third by other noncommunist industrial nations, and one-third by the communist nations and the developing countries. The share of gross world product (GWP) accounted for by U.S. based multinational enterprise was only 15 percent in 1970. However, the percentage of GWP contributed by all multinational companies is growing at the rate of 10 percent per year. At this rate multinationals will generate one-half or more of GWP in less than 30 years.

The administration, through its trade bill, hopes to be able to negotiate lower tariffs and reduce nontariff barriers erected by our trading partners, especially Western Europe and Japan. If successful, the stimulus to our exports resulting from dollar devaluation will be reinforced, but so will imports, which are already destined to go up because of rising incomes and especially, our growing dependence on foreign sources of energy.

How the United States Can Meet the Productivity Challenge

If it is true that the dollar was overvalued in the 1968–71 period, as many economists contend, this factor in itself would have depressed exports and increased imports. Now, apparently, this overvaluation has been eliminated and, in contrast, the dollar may be somewhat undervalued, thereby stimulating exports and restraining imports. But this fact should not blind us to the need continuously to find ways to upgrade our productivity, for productivity in the last analysis is the key to economic progress. Ever since the first Peter Peterson report on our foreign economic policy appeared in December 1971, the administration has stressed the role played by productivity in our balance of payments.

Productivity offers the greatest potential for raising per capita output and living standards, because while natural and human resources are limited and subject to diminishing returns, there is almost no limit to the scientific and technological frontier that largely shapes productivity gains. In the opinion of John Kendrick, an international authority on this subject, the higher rates of productivity in the Common Market countries and Japan than in the United States in the 1968–71 period mostly represented catching up with our advanced technology while we were developing new technologies. Our national economic policies must encourage widespread exploitation of these new technologies if we are to remain competitive.

In this connection we must not fall into the trap of over emphasizing a favorable trade balance in our foreign economic policies at the risk of overlooking the changed character of international business. This business is based increasingly on comparative advantage unhampered by political boundaries. For example, sales by American subsidiaries located abroad stimulate foreign economies and raise foreign incomes and employment which, as a feedback into our economy, raise our exports, incomes, and employment. The same is true of foreign direct investment in the United States. Unquestionably, the resulting new patterns of industrial and employment growth will not be the same as in the 19th century or the early decades of the 20th century. But even in a closed economy the development of new productive methods, new products, new human skills, and exploitation of new natural resources would have changed the relative importance and comparative efficiencies of major industries. Good examples are the development of nonferrous metals and plastics as competitors for steel, of truck and air freight for the railroads, of synthetic fibers for wool and cotton and of electronic communication for the more conventional types. Over the long run new technology creates employment, not unemployment. Our jobless rates are no greater today than they were 50 or 100 years ago, despite the fact that there has been literally a technological revolution. Moreover, there is just no magic way to get productivity advance without investing more heavily in R. & D. and in more modern plant and equipment.

We must step up our real outlays for R. & D. which began leveling off in the mid-1960's. Basic research provides the pool of knowledge from which applied research draws. Unless this pool is constantly replenished we are in danger of losing our technological leadership. Our major foreign competitors have set up large organizations to research methods of increasing productivity. In Europe the French and German productivity councils were started under the Marshall plan in the 1950's; and a Japanese productivity center was started in 1953 at the urging of the United States. In contrast, our 20-man National Commission on Productivity after more than 3 years, following a very slow start, has just commenced to show some results by sparking a program for measuring productivity in the Federal Government and for increasing efficiency in State and local governments.

Indeed, some people have argued that the most crucial productivity problems are found in Government, which has shown the least concern for worker procudtivity. Another generation of Government neglect of productivity could impose a heavy burden on business and the economy. Not only is productivity lagging in the public sector, but little is being done to correct it. In industry, on the other hand, the powerful forces of competition provide strong incentives to innovate. Unless urban government in particular gets out of its rut of complacency, the sharply rising demand for labor-intensive urban services will produce either an explosive increase in costs or a shortage of such services. Modernizing its management techniques, upgrading its talent and expanding the role of commercial suppliers are essential for all levels of government, but especially for states and localities. A useful service that the Productivity Commission could perform is to act as the national policy focal point for examining all of our national laws affecting productivity—especially tax laws—to see where improvements might be made.

More favorable tax treatment has induced higher rates of private capital formation in other industrial countries than in the United States. At a 48-percent tax rate and with straight-line depreciation, the corporate income tax alone more than doubles the rate of return required to justify capital investment. West Germany, Britain, Belgium, Canada, and Japan all place a lesser tax burden on capital formation than does the United States, despite the investment tax credit and accelerated depreciation features of our corporate tax law.

Conclusions

The answer to our international economic problems lies only partially in improvement of our trade balance. One of our principal goals must be to encourage the development of foreign markets for our products, whether produced domestically and exported or produced by U.S. firms located abroad. The multinational corporation is an efficient means of acquiring and maintaining these markets. By internationalizing the production process, foreign operations of multinationals have become the single largest customers of U.S. exports and the largest supplier of vital energy imports.

Continued foreign direct investment by U.S. multinationals is essential to foreign market access and position. If our multinationals are hampered by higher taxes or controls on technology, exports or investment abroad, they will be handicapped as they try to compete with the growing presence of foreign-based MNC's If we ever could claim to be self-sufficient, we most definitely can no longer make that claim. A healthy world business climate is one in which the maximum opportunities for comparative advantage can be enjoyed with the greatest possible mobility of resources and high-technology enterprise. Productivity raising investment is all the more important in view of environmental protection laws and regulations that add to unit production costs but do not get into our output measures.

Certainly there will be costs of reallocating resources as production patterns change by industry and by location; but society in the long run will be further ahead by encouraging resource reallocation and absorbing reallocation costs rather than reducing productivity through ill-advised protectionist measures, such as import and export controls.

These underlying economic principles are recognized by the official negotiators in the current and upcoming international discussions on trade, money, energy, and defense, but quid-pro-quo's and trade-offs will have to be effected if world trade and investment are to continue to grow. This was the theme of the second Peterson report, which was submitted to the President last June, but has not been made public. The report's thesis is that the United States must avoid a showdown with Europe and Japan and seek mutual concessions in the four related areas of monetary arrangements, trade agreements, energy needs, and the sharing of defense burdens. The idea of such a broad linkage in negotiations on these subjects drew a favorable response last July at a meeting in Copenhagen of the foreign ministers of the Common Market countries. The ministers agreed to prepare concrete proposals for discussions with the United States on a new "Atlantic Charter." The notion of a new Atlantic Charter was proposed by Henry Kissinger last April as a framework for linking economic and political issues. But at present the nine Common Market countries have a joint negotiating position only on trade matters.

There is no unanimity within the administration on the issues of money, trade, energy, and defense. At one extreme the State Department opposes tough bargaining on economic issues that might strain diplomatic and defense relations with allies. At the opposite extreme Treasury wants to use the trade negotiations as leverage for monetary reform. The interests of other departments fall somewhere between State and Treasury. For example, Agriculture wants to attack the Common Market's protectionist agricultural policy to widen markets for our agricultural exports. There are no easy solutions to these questions, but the need is urgent for finding and cultivating common grounds for effective compromises.

The ideal world business climate would be one in which the world economy would be as open and free from political and social impediments as our domestic market—an economy in which labor and capital would be free to move from low-productivity to high-productivity employment. Attainment of such a high degree of resource mobility can hardly be expected in the near future; but the growing economic interdependence of nations is a powerful long-term force at work persuading trading nations that there are mutual advantages to be gained from an improved international monetary system, less protectionism and a higher rate of technological innovation than at present.

The United States faltered in its world economic leadership during the unhappy Vietnam era. It lost the momentum gained during the Kennedy Round of trade liberalization as we repeated the error of the British after World War I and kept our currency officially overvalued at a time when heavy Vietnam spending was pumping billions of dollars into world money markets. But there are signs of an approaching agreement on reforming the world monetary system, especially the joint statement issued by the United States and six leading European nations last November 14 ending the two-tier gold market. This was an important step toward eliminating gold from its central role in the present system.

Another favorable sign is the apparent defeat of the protectionist coalition that sponsored the Burke-Hartke bill, especially organized labor, which fears the competition of foreign labor.

A third favorable sign is the growing emphasis on our need to raise productivity if we are to remain competitive. So long as the dollar was undervalued following the Smithsonian agreement in December 1971, our exports enjoyed an artificial competitive edge, reflected in an improved trade balance since then. But that artificial advantage may have disappeared by now, since the trade-weighted average devaluation of the dollar on November 14 was only 6.32 percent. If this artificial stimulus to exports has disappeared, Hendrik Houthakker's expectation of a high and rising export surplus in this decade may not be justified in the presence of other factors. The principal additional factors are those bearing adversely on our productivity, ranging all the way from discriminatory tax laws to anticompetitive labor union practices and higher costs of imported raw materials, including fuel. The "Days of Wine and Roses" are over in our export relations. National economic policy should recognize this fact. If American business is given the opportunity to show what it can do, freed from governmentally imposed restraints, it can once again lead the world in exports and foreign-based sales by U.S. corporations. Failing this, we may never recapture the high percentage of world exports we formerly enjoyed.

COMMITTEE FOR ECONOMIC DEVELOPMENT

By PHILIP M. KLUTZNICK, *Chairman, Research and Policy Committee*

I appreciate this opportunity to comment on the economic report of the President and the annual report of the Council of Economic Advisers on behalf of CED's Research and Policy Committee. As you know, our committee has presented testimony on the two reports ever since these annual reviews were initiated. We are greatly pleased to share our views with you again this year.

The challenges that confront economic policymakers this year are exceptionally difficult, given the simultaneous emergence of rampant inflation and lagging demand and the extraordinarily complex domestic and international problems related to the energy situation. The Council should be commended for approaching these problems with considerable candor and for recognizing the importance of contingency planning. My comments will focus primarily on the considerations that should underlie such contingency planning; on the role of wage-price policies; and on some of the longer range structural reforms that deserve high priority if sound economic growth without inflation is to be restored. In addition, I shall comment on a number of the new program initiatives announced by the administration as well as on international economic issues.

FISCAL AND MONETARY POLICIES

The Council's economic projection for 1974 envisages 1 percent growth in real GNP, a 5½ percent average unemployment rate, and a 7 percent price rise. Underlying this projection is the assumption that there will be changes in direction within the year, with no net real growth experienced in the first half but more than 4 percent real growth in the second. Price increases are expected to ease later in 1974, following very pronounced bulges in price levels in the early part of the year.

Quite clearly, this projection is subject to an unusual degree of uncertainty. Indeed, developments since the publication of the economic report suggest that price increases may already have been higher and the weakening of economic activity greater than the Council initially envisaged. Of course, both the high rate of price increase and the rise in unemployment have to a considerable extent been associated with shortages of energy and other supplies that have had a concentrated impact on selected product and geographical areas. I can testify from personal knowledge, for example, that materials as well as energy bottlenecks have become a very real problem for various types of construction activity. It is thus not yet clear to what extent significant changes in the supply situation would affect the underlying course of demand.

One possibility is that with an end of the oil embargo and an easing of energy and related shortages, there will be a marked resurgence of consumer and business confidence as well as spending. Even now, I find the continuing strength of capital spending very impressive. It seems clear, moreover, that over the years ahead, there will be enormous demands for capital expenditures in various areas of the economy, particularly in energy-related industries; and growing realization of this prospect should in itself tend to strengthen business sentiment. Together with the expected very sizable expansion of Government outlays, the factors I have cited could conceivably lead to a stronger upturn in activity later this year than the Council projects.

Of course, an improved supply-demand balance in both the energy and agricultural commodity areas, plus the beneficial effects on domestic price levels resulting from dollar appreciation, might bring about a significant easing of inflationary pressures. Nevertheless, there are clearly substantial risks that a rapid resurence of demand could result in significantly greater-than-projected inflation, especially if it should turn out that a substantial share of the current weakening in activity is attributable to supply bottlenecks and shortages of capacity. These considerations highlight the dangers of overstimulating the economy.

Another possible course of events—and one that appears to me as the more likely contingency as of this moment—is that the economy will show a more pronounced weakening than the Council anticipates, involving a sharper than projected downturn in the first half of the year and inadequate or no recovery in the second half. Among the factors that could produce this result are the following:

(*a*) Automobile demand might not pick up as much as forecast in the second half of the year, particularly if there are continued dislocations and uncertainties related to the gasoline shortage.

(*b*) It seems doubtful that housing demand and activity will register the kind of upturn normally associated with credit easing, given consumer uncertainties about the energy situation, the fact that there was considerable overbuilding of middle and upper income units in the past few years, and the impediments to construction stemming from various shortages. With only very limited "unfreezing" of funds for new construction of subsidized units for lower income families, moreover, public construction of housing units is scheduled to proceed at a relatively slow pace.

(*c*) The sharp rise in the prices of energy and food could lead to substantial discouragement of the consumption of other products. Thus, to the extent that earnings generated by oil price increases are not directly plowed back into the U.S. income stream, the higher oil price tends to have the same dampening effect on overall demand as a tax on consumers that is not used for new Government spending. It is not clear that CEA's projections have taken full account of this deflationary factor, which might amount to as much as $20 billion.

(*d*) Similar deflationary effects of higher oil prices on other oil-importing countries will add to the weakness of their economies and reduce their purchases from us. The resulting reduction in our net exports could be very substantial, particularly if the dollar continues to appreciate.

(*e*) Capital outlays might not hold up as well auring 1974 as is suggested by current surveys of spending plans, particularly if supply shortages interfere with production schedules.

(*f*) Although a very sizable increase in Federal spending is projected in the new budget, actual Federal spending has recently been lagging behind budget projections, and it is questionable whether spending in the remainder of the current fiscal year can be stepped up as fast as planned.

Clearly, the contingency plans needed to cope with the uncertainties I have outlined will have to be directed both at averting or counteracting a serious weakening in the economy and at minimizing the risks of inflation. The Council indicates that it is developing such plans. However, it has provided few specifics as to what they might contain.

In my view, more intensive public exploration is desirable, both with respect to the time when added action may have to be taken, and to the types of action required. Clearly, there are risks in widespread discussion of such plans. To the extent that they are directed at providing greater fiscal stimulus, they may overly whet the public's appetite for spending or tax reduction measures that may not turn out to be necessary. Nevertheless, if adequate and well-considered action is to be taken in time, careful advance preparations are required that should involve the Congress, the public as well as the administration.

As regards timing, the Council notes there is relatively little that changes in fiscal and monetary policies that might be adopted now could do to affect the course of economic events in the first half of 1974, given the time lags between initiation of policy measures and their impact. It does not, however, stress the corollary point: that contingency measures to deal with emerging signs of significant deviations from the CEA forecast would have to be initiated soon to have an effect during the second half of 1974. In my view, the administration and the Congress should give explicit joint consideration now regarding the conditions and point in time that would call for initiation of contingency measures.

What about the types of contingency measures that should be considered? In line with the views we expressed in our 1972 policy statement, "High Employment Without Inflation," we believe that strong efforts should be made to assure that stimulative measures do not overshoot their mark and thus add to future inflation. Hence, we favor the greatest feasible use of measures that are self-limiting or easily terminated when no longer needed. Wherever possible, moreover, increases in spending should be concentrated in the areas that have the highest social priority.

These principles suggest that it would be desirable to use the following approach if additional stimulus through larger expenditures became appropriate. Unemployment insurance benefits should be substantially strengthened and extended. Considerable emphasis should be placed on signficantly enlarged public service employment programs that would be automatically phased down once the volume of unemployment declines to specified levels. In addition to the self-limiting feature, these types of expenditures have the advantage of being directly pinpointed toward the alleviation of unemployment; in the aggregate, they are thus likely to prove less costly than other means in achieving this objective. I also believe that consideration might be given to special forms of aid to States and localities that would be designed to help offset the shortfall in their revenues attributable to the weakness of the economy.

As discussed further below, there is, in addition, a strong case on both short term and longer range grounds for stepping up assistance to low income housing. We also favor acceleration of defense spending that can be clearly justified on national security grounds. However, we believe it is important to guard against any tendency to relax scrutiny of program additions in this area merely because they would have favorable near-term employment effects and because such programs can often be expanded more quickly than many nondefense activites.

If increased use of "self-limiting" expenditures, together with appropriate actions in the monetary area, should not be enough to provide the needed stimulus, some action in the tax area might also be desirable. We would, however, urge great caution in resorting to such a step because of the need for assuring an adequate future revenue base. Thus, tax cuts used to cushion an economic downturn should, where possible, be of a type that can be reversed relatively promptly when the economic situation improves.

CED has in the p st advocated changes in personal and corporate income tax rates to counteract tro g cyclical forces. We have also stressed, however, that the appropriate form of tax change should be decided by the Congress in the light of circumstances. While the Research and Policy Committee has traditionally held that tax adjustments for stabilization purposes should not involve changes in relative tax burdens, I believe that in the very unusual situation now facing us, the most suitable type of tax reduction—if such a reduction is needed at all—is likely to be one that would ease the tax burden on lower and middle-income taxpayers, that is, the groups that are hardest hit by the regressive impact of sharply higher energy and food prices. In this connection, consideration might, for example, be given to a temporary reduction in the social security tax rate, or to a temporary income tax credit of a stated amount. Such measures would not only be appropriate on equity grounds; they might also help lessen the intensity of wage demands and the risk of an accelerated wage-price spiral. Of course, adoption of one or more of these tax changes might also be desirable on longer-term grounds; but if tax cuts are made for such reasons, they should normally be linked to equivalent actions to restore permanent revenue or reduce outlays.

The possible need for tax changes to counteract cyclical developments gives new emphasis to our long-held view that better procedures are required to permit prompt action to institute such changes. In our 1969 policy statement, "Fiscal and Monetary Policies for Steady Economic Growth," we called for giving the President discretionary authority to raise or lower ncome taxes by specified amounts. However, the particular technique used for achieving greater fiscal flexibility is less important than getting the desired results. An alternative to our proposal would be the establishment of standby congressional procedures that would facilitate rapid action in the tax area when required.

L:t me emphasize, finally, that no contingency strategy is likely to be satisfactory unless greatly improved procedures are instituted to give the Congress and the executive branch effective control over the budget process. Our strong views in this area were most recently expressed in the July 1973 statement by our program committee, "Improving Federal Budget Control." We are encouraged by the progress toward basic reforms in the Congressional budget process that now appears to be underway. t is vitally important, however, that the reforms which are finally adopted give the Congress really meaningful control over all aspects of Federal spending and revenues and do not dilute this control through various exceptions and options for backdoor spending. We urge, moreover, that the needed reforms be instituted as p.omptly as possible.

Wage-Price and Structural Measures

In our 1972 statement, "High Employment Without Inflation: A Positive Program for Economic Stabilization," we called for: (*a*) selective phasing out of compulsory wage-price controls as soon as feasible; (*b*) continuing governmental monitoring of wage-price developments and efforts by a Presidential board to secure adherence to responsible wage and price behavior on a voluntary basis; (*c*) greatly increased stress on structural measures to increase supply, productivity, and competitiveness; and (*d*) continuation of standby authority for compulsory controls as long as necessary.

I was glad to note that the Council will be expected to serve as a focal point for efforts to reduce the inflationary impact of the Federal Government's own operations. The need for such an arrangement was strongly urged in our 1970 statement, "Further Weapons Against Inflation," in which we called for the creation of an agency that would act as "public defender of the price stability objective within the Government." We hope, too, that the Council will serve as an important catalyst for concerted efforts to increase productivity at all levels of Government, a subject which our committee is currently studying in depth.

The Council's report stresses the very limited effectiveness of wage-price controls under the conditions of supply shortages and commodity inflation which prevailed in 1973, though it notes that "the operation of controls during 1971 and 1972, bringing about a good balance in the structure of wages, may have helped to avoid a repetition in 1973 of the kind of wage spiral the country was experiencing before August 1971." However, there is almost no discussion of the new types of wage-price problems that may come to the fore in 1974. In some respects, 197[illegible] is likely to resemble 1971 when high and rising unemployment accompanied high inflation rates.

We are particularly concerned with the possibility that the recent very large increase in living costs caused mainly by the sharp climb in energy and food prices might trigger a renewed wage-price spiral. The enlarged earnings from these higher prices have accrued to a few industries only and partly flow to foreign producers. Hence, most U.S firms are not able to provide full compensation for the rise in living costs to their employees without raising their own prices further In this situation, there could be a case for a somewhat more active governmental role in wage-price matters than the Council seems to envisage, though hopefully only within the context of a voluntary income policy

To permit a prompt response to contingencies, however, it would seem desirable to retain at least limited standby authority for compulsory controls. If such authority were to be provided, however, great care would have to be taken that any reimposition of controls on particular industries only be permitted on the basis of a "due process" procedure that provides adequate opportunity for business, labor and the public to present their views at appropriate hearings.

NEW PROGRAM INITIATIVES

The President's economic messages this year include important new program initiatives in the areas of welfare reform, housing, health-care and higher education. We welcome the general thrust of these initiatives, which closely parallel the proposals that our committee had made in a series of recent policy statements.

Welfare reform.—The administration's new welfare reform proposals will apparently call for direct cash assistance to assure a minimum income to those in need, whether the need results from inadequate earnings or inability to work. The new program, unlike the earlier family assistance plan, is expected to cover single persons as well as family members. At the same time, the program will provide for strong work incentives. All of this is in accord with the recommendations made in our 1970 policy statement, "Improving the Public Welfare System."

Housing.—The new housing program basically favors direct cash assistance for housing low income families and calls for stepped-up experimentation with such programs. At the same time, it partially reverses the earlier suspension of existing programs to subsidize construction of low income housing. Both of these steps were recommended in our 1973 policy statement, "Financing the Nation's Housing Needs."

In our view, however, the overall level of assistance for low-income housing is still far from adequate in relation to needs, particularly since it will take considerable time before any housing allowance program can be implemented on a wide scale. We believe that a further "unfreezing" of subsidies for the building of new homes is needed to avoid a serious shortfall in the availability of housing for moderate and low-income families over the next few years.

Health care.—Our April 1973 statement, "Building a National Health Care System," called for universal national health insurance coverage as well as for major steps to improve the organization and delivery of health care and to overcome the severe inflationary problems of the industry. While somewhat less comprehensive than our proposed program, the administration's plan would also offer a basic level of national health care protection through a three-part system based on employer-coverage, existing Federal programs such as medicare, and a third category covering low-income and high-risk groups on an income-related basis. We believe that such a three-category approach, implemented on a carefully-phased basis, represents the best means of moving toward the goal of greatly improved health care for all while at the same time making optimum use of existing institutional mechanisms. Unlike the Administration's plan, however, our proposals would not limit eligibility for the third category to low-income and high-risk individuals but would make it available to all persons not eligible for other arrangements.

Higher education.—Our 1973 policy statement, "The Management and Financing of Colleges," stressesd the desirability of increasing the proportion of Federal aid that is given to students directly rather than through institutions, and of enlarging the scope of Federal student loan and guarantee programs. We welcome the proposals along these lines that are contained in the President's Budget and Economic Report.

Let me emphasize that our support for new programs in each of these areas is not merely based on a recognition that they represent a needed response to urgent social needs. It also reflects our strong conviction that basic reforms are required to assure that these needs will in the future be met in a much more rational, effective, and economic fashion than has been the case to date.

INTERNATIONAL ECONOMIC POLICIES

We fully agree with the Council's emphasis on the need for new or strengthened arrangements for international cooperation in the monetary, trade, and investment fields. In our view, it would be hard to overstress the urgency of achieving solid progress in these areas.

This note of urgency was already sounded in our July 1973 policy statement, "Strengthening the World Monetary System," in which we indicated that "major questions remain as to whether cooperation will in fact persist or give way to a series of competitive depreciations of major currencies and uncoordinated proliferation of national controls over trade and capital movements. In the absence of a clear indication that there is fundamental agreement on the rules of the game and basic willingness to abide by a central authority that will enforce these rules, the danger remains very real that the world will be moving toward a system of economic warfare among increasingly separated regional trading blocs." Since then, the dramatic oil price increases by a number of producing countries have made these dangers much more apparent and imminent.

As regards world monetary arrangements, our 1973 statement emphasized that exchange rates should henceforth play a substantially larger role in balance-of-payments adjustment than under the Bretton Woods regime, but that a need for some official intervention in exchange markets would remain, We concluded that the essential needs of sound international trade and finance could be met either by a system of managed floats or by adjustable parities subject to frequent and relatively small adjustments. The more important task, we stressed, was to develop a clear set of internationally agreed-upon rules to govern whatever kind of exchange rate system might be emerging, and to assure that adequate rules also existed with respect to the use of controls on trade and capital movements. We further urged that the focal point for cooperative monetary arrangements whould be a strengthened International Monetary Fund.

It is encouraging that the focus of international monetary discussions has moved in the directions we have urged. There is now a wide recognition that a high degree of international cooperation is needed to avoid a spread of beggar-thy-neighbor policies among the industrial nations—a threat posed by the fact that these countries as a group are running large payments deficits vis-a-vis the oil producers, and by the possibility that these deficits may serve as a serious depressant on domestic economic activity in these countries.

One element of a successful solution must clearly lie in the development of adequate arrangements through which the extremely large foreign exchange earnings that are accruing to the petroleum-producing countries as a result of the oil price increase will be invested or otherwise respent in ways most conducive to a high level of international economic activity and viable balance-of-payments relationships. Private market mechanisms should be able to accomplish much of this task, provided they are allowed to function effectively. In this connection, we strongly applaud the recent termination of U.S. capital controls. This step should facilitate the ability of our capital markets to attract funds from the oil-producing countries and elsewhere and to permit the orderly channeling of such funds into productive uses, both within the United States and abroad.

Additional steps would, however, also appear to be needed to facilitate the orderly recycling of funds that are now flowing to the oil-producing countries. Such steps might well include the creation of new types of credit facilities within the International Monetary Fund. As was pointed out in our 1973 statement, a case for establishing such a facility exists quite apart from the special problems posed by the accumulation of large international reserves by the oil producers.

A need also exists for new bilateral and multilateral arrangements specifically designed to assist the flow of funds from the oil-producing to the less-developed countries. At the same time, there is an urgent need to assure an adequate flow of development assistance from the industrial countries. In this connection, we consider it highly important that the United States take prompt action to meet its obligations toward the International Development Association.

Paralleling the need for international cooperation in the monetary and investment areas is the urgent requirement for significant progress in the current international trade negotiations. To make such progress possible, it is essential that the President be given prompt and adequate authority to conduct such negotiations.

There are numerous areas in which international agreement on trade matters will be required. In the context of the present international economic turmoil, for example, it will be especially important to agree on appropriate measures to minmize serious disruptive effects on both producers and consumers stemming from the extraordinarily large recent shifts in world trading and financial relationships. Thus, as the Council's report points out, there is a clear need for internationally-agreed rules to govern "safeguard" arrangements that are designed to provide temporary assistance to producers faced with problems of sudden and large import increases.

Equally important in a world of greatly increased supply scarcities, however, will be the development of intergovernmental arrangements that assure reasonable access to raw material supplies. Such arrangements, in turn, will need to incorporate multilateral rules governing cases where countries employ limitations on exports as a safeguard for domestic consumers who might otherwise be exposed to extremely large price increases.

Finally, there are numerous ways in which cooperative international action can help to resolve the longer-range problems in the fields of energy and raw materials that have recently come to the forefront of public attention. Our committee is currently giving intensive study to this subject and it is our hope that we shall soon be able to make a constructive contribution to the emerging dialog in this area.

As I indicated at the outset of this statement, the convergence of a series of unusual events and trends has made the present time an exceptionally hazardous one for economic policymaking. Effective policies will thus require a high degree of alertness—and ability to respond—to shifts in the underlying balance of economic forces as well as to the emergence of new influences. This is why the principal emphasis in this statement has been on the need for adequate contingency planning, and on the importance of equipping our economic officials with sufficient authority to put these plans into prompt effect if they are needed.

COMMUNICATIONS WORKERS OF AMERICA

By JOSEPH A. BEIRNE, *President*

As president of the Communications Workers of America representing over 550,000 working people throughout this country, I welcome this opportunity to express the concern of thousands of our members over the economic issues currently facing the Nation.

In the last few years, the U.S. economy has encountered an unusual number of problem or "crisis" situations. It appears that as soon as one problem is resolved a new and more serious one emerges. In mid–1970, for example, the administration publicly agonized about keeping labor's demands under control, balancing the Federal budget and strengthening the dollar in world trade. At that time, we were in the face of rampant inflation, growing unemployment, recurrent balance of payment deficits, and the first recession in 10 years. Since then, there has been moderate success in solving some of these problems.

The Federal budget appears to be in balance as revised estimates for the calendar year 1973 show a surplus of receipts over expenditures reaching nearly $1¼ billion. Unemployment has been marginally reduced from an average of 5.9 percent reached in 1971 to 4.9 percent last year, a level which is high compared to the sub 4-percent levels reached in the last 3 years of the Johnson administration. In the third quarter of 1973, the United States realized its first balance-of-payments surplus in 3 years. But these achievements have not brought about the economic stability that we enjoyed in the decade of the 1960's. Instead, the Nation's current economic problems are clearly the worst in decades.

Headlining today's problems are an extraordinary array of shortages and supply dislocations, with the "energy crisis" attracting the most attention. Many economists are indicating that the economy may be sliding into a recession with unemployment rising over 6 percent. But the persistent high rate of inflation remains to be our central problem and most difficult test as high prices continue to flare up in different areas for new and different reasons.

Throughout the decade of the sixties, inflation rose at an annual rate of 3.1 percent, as measured by the yearly average Consumer Price Index. During this period, it was generally considered that inflation and other maladies of the business cycle could be minimized through responsible fiscal and monetary measures. But since 1968, such traditional measures have been either misused or have been inadequate in an effort to stabilize the economy. Therefore, the question that arises is whether the anatomy of new business cycles have mysterious origins, as the administration would have us believe, or do political considerations tend to be a guise for irresponsibility?

Inflation in Retrospect

Some of the mysteries of our current problems can be better understood by reviewing economic conditions of the last few years. Inflationary pressures began when we were taking on the heavy financial burdens of the Vietnam war without increasing the rate of growth in revenues. Therefore, sizable deficits occurred in the Federal budget which, in turn, fueled rapid economic expansion.

In an effort to slow down the torrent of demand, surcharges on corporate and personal income taxes were levied. The new surcharges quickly diminished federal deficit spending, and by the first quarter of 1969 Federal receipts over expenditures showed a surplus. But demand had a good head start, and subsequently fiscal measures did not prove to be a short-run solution for inflation. To counteract the hesitancy and short-run ineffectiveness of fiscal policy, monetary policy was tightened severely in late 1968 and this posture of stringency continued through 1969.

By mid-1969, inflationary pressures were buoyed by consumer spending. But the rigid restraints were starting to effect the growth of the economy. Even though the Federal budget was locked into large expenditure obligations, the surcharges were allowed to expire in June 1969. By the end of 1969, the United States entered into its first recession in a decade, and yet inflation remained with us.

What Went Wrong?

The repeated failures of traditional policies raise questions on whether or not new currents in the economy are causing them to be ineffectual. Although there may be some merit to these questions, there are valid explanations on why the traditional policies did not work during this time period.

The predominant reason is that the administration did not use fiscal and monetary measures in the same manner or degree that they were so successfully used in the early sixties. Large deficit spending was allowed to continue for too long a duration. In an attempt to compensate for the delay in policy, the largest budget surplus in 20 years was permitted to accumulate. But apparently a timelag of policy action cannot be compensated for by more stringent policy. Consumption habits were deeply instilled and, therefore, the consumer simply changed his or her savings ratios. The overcompensations of fiscal restraint did, however, cause a slowdown for the rest of the economy, sliding it into a recession.

Demand Builds Up Again

As unemployment increased and industrial production decreased in 1970, policy was initiated to stimulate the economy. But again the administration overcompensated in both fiscal and monetary policy. By the end of the year, the United States was engaging in its largest deficit spending since World War II. Monetary policy was also one of expansion as the money supply (demand deposits and currency) grew over 6 percent during 1970. The policies brought us out of recession, but also it refueled the inflationary pressures. Prices were moving upward faster than had been experienced in a decade. Something had to be done. Finally President Nixon ordered a 90-day freeze and subsequently wage and price controls.

Wage and Price Controls

Wage and price controls are not a solution to inflation. Control measures are only useful as a temporary mechanism to hold back inflationary pressures until proper policy can be devised and take effect. For a year and a half, controls were moderately successful in reducing price increases.

But proper monetary and fiscal policy had not been implemented. Throughout 1971, the Federal budget was out of control showing increasing deficits each quarter. In 1972, the deficit spending had been significantly reduced, but it still was at the heated pace of spending that occurred during the Korean war. This fiscal policy was especially risky because of a great surge of business expansion in Japan and Europe.

Monetary policy also fortified demand during the last three years. The Federal Reserve permitted the money supply to grow at unprecedented rates, 7 percent from 1970 to 1971, 6.5 percent from 1971 to 1972, and 7.4 percent from 1972 to 1973. This was a higher rate of growth than any 3-year period since the end of World War II.

Both Herbert Stein, Chairman of the Council of Economic Advisers and Arthur Burns, Chairman of the Federal Reserve Board, have since conceded that the 1972 policies, in retrospect, can be considered overly expansionary. Both, as can be expected, blame each other as the greater villain. There is little doubt that the administration lacked coordination and careful planning, adding up to risky, imprudent policy.

New Inflationary Surprises

The herky-jerky, overreactive economic policies of the Nixon administration are not the only rudiments of our current inflationary pressures. The prolonged demand along with other events caused critical shortages which in turn brought about a predominant upward pressure on prices.

By late 1972, all major European countries and Japan were in unison riding on top of their own respective business booms. This provided a powerful external demand factor for U.S. goods, creating an overwhelming total demand. The administration was rudely reminded that economic policy should be devised in respect to external factors as well as domestic factors.

Food Shortage

In the 15 years preceding 1968, food prices rose only 1.2 percent per year, as measured by the food index of the Consumer Price Index. The food supply had always been bountiful in the United States. The average American worker saw food expenses as a shrinking portion of his budget. But early last year, food spending became the dynamic sector of consumer prices.

In late 1972, an already tight world food supply was radically depleted when bad weather in several countries reduced world grain production. The Russian crop failures included their most important staples, expecially in grains and potatoes. The failure of the anchovy catch in Peru put further pressures on soybean supplies. The peanut crop in India and Senegal was poor, reducing a significant source of meal.

The shortfalls exerted substantial pressure on U.S. grain and soybean supplies, which were under duress for a variety of reasons. The main restraint of U.S. agricultural supplies stemmed from outdated agricultural policies. For most of the last two decades, we have enjoyed the problems of oversupply in farm crops. Lacking any foresight, the basic policy of the Department of Agriculture in 1972 remained to be one of keeping prices up by holding down supply. Thus, in a time of world wide grain shortages, the United States had an enormous amount of good farmland idle from cultivation.

The United States was also guilty of poor management in its dealings with the Soviet Union. When their wheat crop failed in 1972, the Soviet Union made a major shift in policy by going to the world market to get wheat for their domestic needs.

Soviet buyers entered the world market by expressing interest in U.S. corn and soybeans, and they were able to purchase large quantities of grain at very low prices. Their final purchases amounted to nearly 20 million metric tons of grain from the United States, representing about 20 percent of all grain stocks held by the United States at the end of the year. The effects of these massive purchases pushed up the prices of wheat over threefold.

At the time of the sale, the U.S. Department of Agriculture had no mechanism to oversee, or even keep tabs on, foreign grain orders. Therefore, a system that could warn regulatory officials that a major concentrated purchase plan was being pursued by the Soviets, simply did not exist. Under, what was apparently the strong endorsement of the White House, a handful of American grain companies contracted to sell vast quantities of U.S. grain reserves. The administration not only encouraged the sale of dangerously large amounts of domestic grain, but through U.S. export subsidies it allowed windfall profits to be reaped by the private grain traders. Furthermore, the credit terms arranged by the administration for the Soviets could not, by any stretch of the imagination, be termed politically astute or commercially profitable.

The repercussions of poor Federal agricultural policy reverberated throughout every household in America. Food prices soared over 19 percent in 1973. Acute shortages occurred in the supermarket, especially in meat products.

The Oil Shortage

The present "energy crisis" is another example of poor management by the Nixon administration. Since the late 1960's Arab-United States relations gradually deteriorated. Yet, as these relations continued to worsen, the United States became more dependent on Arab oil. But the administration did nothing to prepare us for possible cartel actions such as price fixing, production controls and embargo.

Prior to the 1970's, the quantity of foreign crude oil was imported at a ratio of 12.2 percent of domestic production, as restricted by the mandatory oil import program created by Presidential proclamation in 1959. In early 1970, it became necessary for President Nixon to raise the restriction on oil imports by Executive order. As domestic crude oil production relative to demand decreased, it became increasingly necessary to raise the level of imports. The responsibility for the "balancing wheel" function for providing refineries with adequate levels of crude oil feed stocks rested with the Oil Policy Committee, Department of the Interior Office of Emergency Preparedness.

Warning Signs of the Shortage

In the last 3 years, there have been several warning signals that a serious energy shortage could materialize. In 1970, the oil-producing Arab countries formed the Organization of Petroleum Exporting Countries (OPEC) to work as an effective international cartel. The following year, major American oil companies were set back by the oil producing countries demanding and receiving ownership in the petroleum operations taking place in a number of countries. On March 1, 1972, Saudi Arabia persuaded the Arabian American Oil Co. to turn over 20 percent ownership. This was considered a major achievement for OPEC.

A combination of discouraging developments indicated inevitable shortages of crude oil such as the lack of crude oil on spot market, shrinking domestic stocks of crude oil, increasing allowed productions in oil States, stepped up import rates considerably higher than those of recent years and heavy demand for import tickets at high prices. By mid-1972, it was necessary for allowable production rates to be increased to 100 percent at certain reservoirs in Louisiana. Late the same year, it became evident that allowable imports and domestic production could not meet demand, and America endured a heating oil shortage. Among the contributing factors to that shortage were: (1) Low distillate inventories entering the final quarter of 1972; (2) tight crude oil feed stocks with crude oil imports not being increased in the final quarter of 1972 to the level permitted; and (3) refineries operating at 89 percent of capacity instead of 92 percent of capacity.

By mid-1973, it became apparent that we might also suffer a gasoline shortage. Darrell Trent, Acting Director of the Office of Emergency Preparedness announced April 5, 1973, that he was deeply concerned over both the current stock of inventories and production of gasoline by American oil refineries. Soon after that announcement, several large oil companies reflected the intensifying shortage of gasoline when they began allocation plans of their own. Phillips, for example, reduced sales to its customers by 10 percent based on purchases made the previous year.

Administration Inaction

Despite these and many other clear warnings of upcoming shortages, the administration was extremely slow and impotent in its actions. An excellent example of the lack of leadership and decision was provided by the establishment by the President of a Cabinet level Oil Policy Committee in February 1970, in response to a recommendation by the President's Task Force on oil imports. The Oil Policy Committee was chaired by the Director of the Office of Emergency Preparedness until the spring of 1973. A useful forum for presentation of views was provided, but the authority of the Chairman was derived from a White House press release. With this kind of vacuum, it is a small wonder that the kind of strong measures the situation demanded were never launched.

Major Recommendations for 1974

Our most serious economic problems today have been persistent ones throughout the tenure of the Nixon administration. These chronic problems have considerably weakened our country in respect to our stature abroad as well as our fundamental quality of life here at home. There must be immediate responsible action to relieve us from rampant inflation, high unemployment, and critical commodity and energy shortages. The following are our major recommendations:

(1) *Tax reform.*—In the last 10 years, the distribution of Federal budget receipts by source has changed considerably. For example, corporation income taxes contributed to 21 percent of Federal revenues in 1964, but its share dropped to 16 percent last year.

Additional revenue will be needed to counterbalance large Federal deficit spending that is expected to occur this year. These revenues can be obtained by eliminating major tax loopholes of special benefit for corporations and wealthy families.

(2) *Manpower.*—Unemployment has been a chronic problem for the Nation since 1969. The unemployment rate soared from 3.5 percent in 1969 to an average of over 5 percent for the last 4 years. It is imperative that an effective national-in-scope manpower program be immediately implemented. It should be a comprehensive program with consolidations and coordination of all manpower activities under a central administration. The principal objective must be that of job creation, but training must also be included if the program is to have any value. There must also be special manpower aid to depressed areas which would provide specialized training and job assistance.

(3) *Farm and food policy.*—Our inflation in food prices can be directly related to the administration's faulty agricultural policy. CWA strongly recommends that restrictions on the use of farmland be ended. We also recommend that income guarantees be made effective for working farmers as incentive to increase production.

(4) *Antitrust.*—The checks and balances inherent in a competitive system are being distorted by flagrant antitrust violations. Much of our inflationary pressures can be attributed to administrative pricing policies among giant monopolies. CWA recommends a congressional review of the present antitrust policing system with the purpose being to devise a new and more effective mechanism which would expedite penalties for violations.

(5) *Energy.*—The present "energy crisis" underlines the necessity for a comprehensive national energy policy. We support the creation of a statutory Council on National Energy Policy. A National Energy Agency should be created with authority to establish a mandatory nationwide oil and gas allocation plan and require oil companies to report on reserves and distribution systems.

CONFERENCE ON ECONOMIC PROGRESS

By LEON H. KEYSERLING*

Part I. GENERAL COMMENTS ON 1974 CEA REPORT

In part I of my presentation, I make some general comments about the 1974 Annual Report of the Council of Economic Advisers. These comments reveal that I am fundamentally in disagreement with much of the basic analysis, and what may be called the basic economics, of the Advisers' Report. I disagree with much of what the report contains, and am even more concerned about what it leaves out. Essentially, the report does not respond to the challenge of the Employment Act of 1946. The report is short on goals responsive to that act, and short on policies to achieve appropriate goals. For these reasons, it seems unnecessary that, in this part I of my comments, I go into much refinement or detail.

In part II of my presentation, I set forth in considerable detail my own analysis of the economic situation and needed policy actions. This in itself will serve to explain, amplify, and reinforce my general criticism of the Economic Advisers Report as set forth in part I.

Chapter 1 of CEA Report—Economic Problems and Policies

This chapter commences by stating that "For eight years economic policy and the news about the economy have been dominated by inflation. The story has been a frustrating one."

This is a correct statement, with respect to the preoccupation of the CEA, and perhaps of economists in general. But it also reveals the most important reason why so much has gone wrong. For preoccupation with inflation, instead of rational attention to it in the context of many other problems, is astigmatic and has also turned out to be self-defeating.

The movement of prices is highly important, but prices are not an end in themselves. Prices are merely one of the mechanisms whereby resources and incomes and economic activity are allocated toward the three great purposes of our economic system. These three objectives are reasonaly full use of our growing resources at optimum economic growth, adequate attention to the priorities of our needs, and social justice. The preoccupation with price trends per se has caused terribly costly neglect and mishandling of these three great purposes.

Moreover, the preoccupation with price inflation has ironically yielded far more price inflation than would have resulted from the treatment of the price problem in a fuller perspective. Indeed, it is again apparent from this first chapter of the 1974 CEA Report that adequate analysis or explanation of the persistent and accelerating

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inflation is hardly attempted. Surely, the poverty of the analysis is evidenced by the intimations on page 21 of the report—and elsewhere therein—that wage trends should be assigned first degree responsibility for the excessive inflation. This viewpoint is at once refuted by responsible empirical study, and most especially with respect to the most recent year.

The mistaken analysis and misdirected emphasis of the CEA Report is further revealed in chapter 1 by the treatment of the energy problem, concentrating as it does on the volume of oil imports as affected by Arab action commencing very late in 1973. It is true that this Arab action has serious consequences. But it is totally wrong not to stress that many aspects of the oil shortage, other energy shortages, food shortages, transportation shortages, housing shortages, shortages in health and educational services, and other specialized shortages have been accumulating for many years. And it is equally wrong not to recognize that these specialized shortages reflect in the main the same erroneous economic approaches which have yielded the tremendous and long-enduring shortages in jobs and national production, when measured against our full and growing capabilities.

Surely, this first chapter of the CEA Report offers no penetrating analysis of the causes of the long-enduring deficient performance of the U.S. economy, when measured against our capabilities and needs; and without such analysis, correct and adequate remedial action cannot be forthcoming.

Insofar as any such analysis is even sketchily suggested, it focuses considerably upon the need to stimulate private investment. But a meaningful analysis of long-term trends to date makes it clear that the central barrier to adequate private investment has been gross deficiencies in ultimate demand in the form of private consumption and private outlays combined. Consequently, the CEA does not direct its concern as to how this ultimate demand may be expanded adequately, but instead repeats its unwarrantedly bearish position in this factor.

The CEA's treatment of goals for 1974 is in my view utterly indefensible, and ignores both the national interest and the sound declared purposes of the Employment Act of 1946. It seems to me a thorough abdication of responsibility that the CEA should view with equanimity the forecast that the economy in 1974 as a whole will register a real growth rate of only about 1 percent compared with 1973. This may be a correct forecast as to what is likely under national policies now in being and those proposed. But it is an entirely incorrect attitude as to what national policies should be proposed and effectuated to forestall or ameliorate this dismal outlook.

In fact, the fiscal and monetary and other policies outlined in this chapter appear designed to bolster rather than to counteract this dismal outlook. For the CEA admits that the economy could be brought rather quickly toward movement in a direction conducive to fuller resource use—the 1-percent growth rate would actually carry it further away from full resource use—by available policies, but that such policies should not be attempted because they would increase inflationary pressures. Again, such a position not only neglects priorities of need, but also continues to espouse a theory of inflation repudiated by the very fact that inflation has been accelerating so rapidly even during the most recent times when the economy has been moving to stagnation and then to recession, with increasing resource disuse. And the same phenomena stagflation, was obvious during several earlier periods before blatant shortages were in being.

As I have already stated, the detailed materials in support of my criticism of the first chapter of the CEA report will be set forth in part II of my presentation.

Chapter 2 of CEA Report—Developments and Policy in 1973

This chapter of the CEA annual report is a competent accounting of what actually happened in 1973. But it fails completely to recognize the import or challenge of the highly unfavorable developments within the year, and it fails to make any meaningful analysis of the reasons for these unfavorable developments. Certainly, an economy which moved from a rather high rate of real economic growth at the beginning of the year to a stagnation rate of growth later in the year, and then to recession or clear warning of recession by the end of the year, was trending very unfavorably. And doubly so, when the acceleration of price inflation negated the honored theory of the CEA economists—and many others—that the economic slackening which the national policies abetted would reduce the pace of price inflation. Certainly, these highly unfavorable developments on all fronts called for a reconsideration and drastic revision of the content and nature of national economic policies, instead of bringing forth a ringing affirmation of these policies and their continuation with only slight variation.

Specifically, the statement on page 47 of the report that "total output approached the ceiling early in the year" is not substantiated be revealed facts in the report, nor by the actual situation. Neither the rate of unemployment early in the year, nor the amount of idle capacity early in the year, justifies the statement that total output was approaching a ceiling. Nor is there justification on the same page 47 for the statement that "the price rise accelerated and demand for output was stimulated in anticipation of future shortages and price increases." If that had been true, why did price inflation accelerate further, even before the energy crisis, when total output was obviously moving further and further away from the ceiling? The same comment applies to the statement on page 49 of the CEA report that, at the start of 1973, "the real increases were unsustainable in terms of the economy potential to produce. * * *"

The treatment of housing, on page 53 of the report, is grossly defective and excessively abbreviated. No mention is made of the tremendously adverse impact of the extraordinary decline in housing starts upon the economy at large. The implication of the report, to the effect that the housing decline was to be expected and not to be vigorously resisted, is entirely unjustified. The essential housing problem is to make real and rapid inroads against the unacceptable type of housing in which one-fifth to one-fourth of the American people live, with the damaging effect of this upon urban conditions in all their aspects. The failure to recognize that this problem even exists is a salient illustration of the CEA's lack of attention to those national priorities which should be a first concern of national economic policy.

The statement on page 53 of the CEA Report that "consumer demand rose sharply from 1972 to 1973 under the influence of higher income" is technically true, but misleading and far too complacent. The real task of the CEA is to analyze whether consumer spending and incomes, as major components in GNP, rose nearly rapidly enough to avoid stagnation and recession, and to have a restorative influence upon economic performance. The fact is that consumer income and spending trends fell far short, and increasingly short, of these desiderata.

The CEA also neglects the problem that a large part of the increase in consumer incomes was supported by social security benefits, financed by undesirable payroll taxes which had repressive and regressive effects. Correspondingly, the discussion on the trends of the rate of saving neglects the all-important problem of the unfavorable distribution of saving, as affected by the unsatisfactory distribution of income.

The statement on page 57 of the report that "the 3.3 percent rise in employment was the largest December-to-December increase since 1955" is another one of those euphoristic statements which palpably ignores the fact that the rise in employment was not large enough to prevent continuance of a level of unemployment intolerably high, and not in accord with any possible concept of "maximum" employment.

The discussion of productivity and potential output, commencing on page 62 of the CEA Report, does not exhibit sufficient concern about the unsatisfactory rate of productivity growth during 1973. Far more important, in its discussion of factors relative to this unsatisfactory rate of productivity, the report slights what I regard to be the main point—that the unsatisfactory rate of productivity growth has recurrently been due to the size of the "gap" between the actual performance of the economy and potential performance at reasonably full resource use. I shall develop this point, as well as other points I make in this part I, much more fully when I come to part II.

The statement on page 65 of the CEA Report that "during 1973 prices rose more rapidly than at any time since the Korean war" is misleading. It is true that prices rose with extreme rapidity for a very short period during the Korean war, following the unexpected entry of China. But the average annual rate of inflation of consumer prices during 1947–53 was only 3 percent, while the average annual rate was more than 5 percent during 1969–73. The 3-percent average was attained despite a 7.8-percent rate of inflation from 1947 to 1948, due mainly to conditions created during World War II and the premature abandonment of controls. The annual rate of inflation during 1947–53 was reduced from 7.8 percent in the first year to 0.8 percent in the final year, while the rate of inflation rose from 5.9 percent to more than 7.4 percent from the first to the last year of the period 1969–73. This, despite the fact that average annual unemployment was only 4 percent and the average annual rate of real economic growth 4.9 percent during 1947–53, contrasted with 5 percent and 3.7 percent, respectively, during 1969–73. Further still unemployment declined from 3.9 percent to 2.9 percent from the first to the last year of the period 1947–53, and rose from 3.5 percent to 5 percent from the first to the last year of the period 1969–73. These comparisons in themselves reveal the utterly erroneous character of the current CEA's explanation of the causes of inflation, which is to the effect that inflation is accelerated as the economy moves closer to full resource use, and abated when the economy moves further away from full resource use.

Beginning on page 68 of the CEA report, the position is taken that a quickening in the rate of increase in money compensation per man-hour led to sharply rising unit labor cost, and that this contributed substantially to price inflation in the private nonfarm economy. This is a gross misinterpretation of what really happened, and completely absolves the price managers from any responsibility for price increases which led to profit trends which are certainly excessive in relationship to the performance of the economy at large. Actually, real money wage rates lagged behind productivity gains, and this is the appropriate test of whether wage rate changes were a major factor in inflation. Insofar as the money wage rate increases merely reflect increases in the cost of living, this was wages chasing prices, rather than the reverse. The long-maintained bias of the CEA against wages and consumer income and spending has been not only unfair and unwarranted, but also highly injurious to needed economic adjustments.

The effort of the CEA to show that profits did not tend to be too high in this context, and maybe to imply that they were too low, is not sustainable.

What I have just said about wages and profits is fortified in detail in part II of my presentation.

Chapter 3 of the CEA Report—Inflation Control Under the Economic Stabilization Act

This long chapter in the CEA report is a careful and rather exact description of what actually happend to prices under the various stages of the economic stabilization program. It includes a frank admission that the controls did not restrain roaring price inflation in 1973, but this is accompanied by posing, without attempting to answer, the question of whether there would have been more or less inflation without the controls in 1973.

The CEA discussion strongly intimates that the controls did not succeed in 1973 because they were not developed to deal with a shortage situation. But the energy crisis caused by Arab action did not occur until the very end of 1973; and the Council does not explain why, if there were shortages before such Arab action which explained the inffectiveness of the controls, these shortages had not been foreseen long ago by the Council, and actions taken to overcome them or to counteract their impact upon prices.

Much more important, the CEA substitutes an unanswered question as to whether or not the controls were desirable in 1973 for any meaningful analysis of whether a different or better set of controls might not have worked better in 1973. The CEA discussion at large is thus apologetic and defensive. After all, controls worked very well during World War II and the Korean War, under conditions (and, in World War II, shortages) far more difficult than in recent years.

There are at least two reasons why the controls worked so badly in 1973, neither of which the CEA touches upon.

The first reason is that the controls in 1973 were a part of a series of actions whereby the Government had at least four different systems of controls within a rather short period of time, and sometimes instituted a new system accompanied by the statement that the Government did not really believe in it much and was going to abandon it soon. Frequent shifts in the nature of a controls program may be workable and desirable when the controls are definitive and all-inclusive. This might be sensible "fine tuning." But as the recent controls, aside from the freeze, were limited in nature and depended so largely upon the acceptance and cooperation of functioning economic groups, the controls could not possibly succeed when these groups could at no time have any certainty that the controls would not be changed again before they could be digested. Neither controls nor any other economic policy can work well when the Government makes it clear that the Government itself does not know what it is trying to do, or why.

There is a second and even more important reason why the controls did not work as they should, even when they worked as their managers wanted them to, and this applies not only to 1973 but also from the initiation of the freeze. This even more important reason does not seem even to reside within the consciousness of the CEA. The purpose of controls is not simply to hold down price increases, or to hold down wage rate increases. The purpose of controls is to help to allocate resources and incomes in a manner constant with economic balance, and social equity as well. For these kinds of controls, the specific terms of the controls must be set in the model of a balanced tableau for the economy at large, pointed toward fulfilling the three great purposes of growth, priorities, and justice. The controls worked well during World War II, and also during the Korean war, because this procedure was followed.

But there has been no such procedure in recent years, and the controls have been only one example among many of inconsistent and misdirected policies. This situation was so extreme that there were times when the controls "worked worst when they worked best," that is, worked worst when their quantitative objectives came closest to being attained. For during the freeze and thereafter, the terms of the controls were undoubtedly biased on the price increase and profit and investment side, and correspondingly biased against the consumption and wage side. This is not really surprising, in that it reflected the clearly revealed basic economics—and nowhere more clearly than in the current CEA Report—of those imposing the controls. The freeze and phase II worked "well," in terms of the objectives of those imposing them. But they aggravated the economic imbalances, and contributed to the stagnation and oncoming recession.

This is no argument against controls per se. But it is an argument against ill-devised controls, not perceptive of their real purposes, and conducted with isolated disregard for their real purposes.

Chapter 4 of the CEA Report—Energy and Agriculture

The discussion of energy in the 1974 CEA Report is thoughtful in several respects, and contains a number of useful ideas and proposals. Nonetheless, I view the discussion seriously vulnerable, in that it steers away from rationing, and apparently relies entirely upon rising prices to allocate energy in short supply. Everyone should know by now that, while rationing is unpleasant, it is a sounder economic and fairer socially way of allocating essential commodities in very short supply than excessive and uncontrolled price increases.

But my criticism of the treatment of the energy shortages in the CEA Report goes far beyond this. The report treats these shortages as largely the result of recent and unforeseeable developments, and does not recognize adequately for how long these shortages have been developing. Nor does it recognize the key responsibility of the CEA and of the Economic Reports of the President to undertake the long-range planning required to assure an adequate supply of energy, and other necessities such as food, in the perspective of an economy which is growing at an optimum rate at reasonably full resource use.

The CEA Report is replete with suggestions as to what other instrumentalities of Government should do about energy shortages, and it is true that the detailed processing of such matters must be assigned to agencies other than the CEA itself. But the CEA cannot thus easily escape its own responsibilities. The long-range economic and social budget which CEA should develop should deal not only with the overall economy, but also with components as important as energy, housing, transportation, educational and health service, et cetera. For while the specialized agencies are claimants in their respective fields, only an agency such as the CEA can reconcile these claims. And only an agency such as the CEA can be fully aware of the impact upon the Nation and people at large, if any specialized claim is neglected or excessively serviced.

There is little or no evidence in the current CEA Report that its members are awake to the plenary mandate which the Employment Act of 1946 embodies. Over the years, the CEA has concentrated mainly upon fiscal policies, and to a lesser degree upon monetary policies, while it has neglected the task of integrating these with other eminently important economic and related social programs and policies. It would seem unthinkable that, during recent years, the CEA has paid such scant attention to housing, the social insurance programs, farm programs, transportation programs, and several others which need to be treated in unison if we are to have a reasonably integrated economic and related social program and policy, and not merely a medley of disconnected, inconsistent, and improvised programs and policies.

The extensive treatment of agriculture in the CEA report is something new, because this vital subject has been ignored or lamentably slighted in previous CEA reports. But the views expressed in the report repeat a lot of long enduring errors. For example, the report states on page 128 that, while the problem of farm production shortages has arisen since 1972, the problem from the 1930's to 1972 in agriculture was "excess productive capacity and the adjustment of resources to that condition." This is an erroneous position in almost all regards.

We may have had farm surpluses related to effective demand, just as we had job surpluses in the general economy relative to effective demand. But over the decades our production of foods and fibers has been inadequate to prevent millions of American families from suffering malnutrition and millions of others from having an inadequate diet to meet the needs of an economy maintained at reasonably full resource use and to maintain the level of agricultural exports which would be in our own interest and make the contribution we should toward the reduction of poverty and toward economic development in many other parts of the world.

In this connection, the table on page 129 of the CEA 1974 Report is rather misleading. It shows the surpluses of nonperishable commodities over many years in ratio to total utilization within 1 year. But it neglects the fact that, year by year, the production of farm commodities in each year has been very little in excess of actual utilization in that year—quite apart from the fact that defects in distribution have prevented the yearly utilization from approximating the real need. As I have pointed out in various published studies, if the so-called surpluses in agriculture were properly measured, they would be shown to be infinitely smaller than the surpluses in other parts of the economy, and infinitely less costly, when measured by idle plant and idle manpower.

The fundamental and tragic errors in national farm policy over the decades have brutally driven millions of farm families off the land and into the cities where, instead of being productively absorbed, they have accounted for close to half of the total unemployment and welfare costs in urban areas. In this connection, it does not make sense for the CEA to take the position that farm policy has been none of its business. For how can it not be a prime function of the CEA to deal with an aspect of the economy which imports so much for the performance of the economy as a whole and the well-being of the people?

Beginning on page 133 of the 1973 CEA Report, the discussion of agricultural policy for the future makes some good points, but is sterile indeed with respect to the really dominant problem. The dominant problem is still that farm per capita income suffers from grievous disparity, and that the public services available to farm families and others in the rural population suffer from comparable grievous disparity. Instead of making a lot of really secondary technical points, the CEA should dedicate itself, within the contours of a meaningfull long-range economic and social budget, to exploring and answering these questions: (1) How much food and fiber should be produced, looking 5 or 10 years ahead? (2) What farm resources, human and other, are needed toward these ends? and (3) What incomes and public services for farmers are needed to achieve these purposes, and also to do justice to this portion of our population?

Attention to these matters would not require a vastly larger CEA. For the CEA needs only to identify the questions and set the standards, and can and should assign to the specialized agencies the detailed work. But without this kind of central guidance from the CEA, the specialized agencies, even with their hordes of economists and other specialists, are unable to ask the right questions, much less to provide the right answers.

Chapter 5 of the CEA Report—Distribution of Income

Not many years ago, a report of the CEA declared pridefully that it was "neutral on the subject of income distribution." The current report may seem to have risen above this, in that it offers a great deal of new and useful information on the subject of income distribution.

This is all to the good. Nonetheless, the report is seriously defective in its treatment of the income distribution problem, in that it treats it largely as a social or equitable problem, and largely overlooks the fact that rapidly improved income distribution is at the very heart of the problem of regaining and maintaining reasonably full resource use at acceptable low levels of unemployment of plant and manpower and other productive resources.

The report correctly observes that income distribution has improved most rapidly during periods of high real economic growth and reasonably full resource use, and improved less rapidly or gotten worse during periods of low economic growth with large idleness of resources. But this tends to put the cart before the horse. It would be more revealing and more indicative for policy, to say that the improved distribution of income is in itself a sine qua non for optimum economic performance.

Similarly, in the treatment of the poverty problem, the CEA is correct in observing that poverty has been reduced most rapidly under conditions of high real economic growth and reasonably full use of resources. Here again, it would be more revealing and indicative to observe that the rapid reduction of poverty is itself a sine qua non for a fully healthy economy, in terms of viable equilibrium. Until that position is reached, we will never have that interpenetration of purely economic and social objectives which is essential to adequate achievement in either field.

These defects in the CEA approach do much to explain why the CEA has become so preoccupied with price trends per se that it has downgraded attention to the far more important issue of improved income distribution. In fact, experience indicates that a rising price level, induced in part by vigorous programs to improve income distribution, is far preferable—if that were the choice—to a stable or more slowly rising price level attained by regressive policies. The price level was extraordinarily stable between 1922 and 1929, and look what happened thereafter. In the long run, just because the economy has moved upward and downward and sideways, and registered so dismal an average economic performance and tolerated so much idleness of plant and manpower, income distribution has changed very little in the long run, as the CEA report observes. But the CEA does not recognize that this is just what is most wrong in the American economy, even on purely economic grounds—quite apart from recognizing that we are a rich enough economy to do social justice.

If the CEA could overcome these defects of commission and omission, it would advocate policies drastically different from those which it now espouses. It would not advocate the acceptance of rising unployment and negative economic growth, on the spurious ground that this would help to restrain inflation. Instead, it would recognize that income distribution is most adversely affected by these developments, and similarly it would recognize that this kind of bloodletting does not establish a sound base for optimum performance on any front.

The proposals which the CEA advances for a continuation of the attack upon poverty are conventional and inadequate. They consist mostly of a discussion of established programs. They do not recognize that entirely new and immensely larger efforts are needed. Reading between the lines, the CEA bows to the conventional view that these needed efforts cannot be "afforded" by the economy in its present position. But in fact, doing what needs to be done in this area should be first and foremost on the agenda for lifting us out of our current position, and breaking out of the rigid cycles of upturn, stagnation, and downturn.

As in the case of the food problem and energy problem, the details of an adequate war against poverty, and toward improved income distribution, should be an integral part of the recurrent CEA reports and the Economic reports to the President. The liquidation of poverty and improved income distribution are at the very core of the economic problem in America, and not something to be treated as a cold and scholastic appendge, with little sense of urgency, and little by way of the needed policies and programs.

Chapter 6 of the CEA Report—The International Economy in 1973

This chapter of the CEA report is in some respects the best, in terms of technical and conventional analysis. But it focuses upon the balance of payments as the great issue. This results in an excessive preoccupation with that issue, having unfortunate consequences analogous to those resulting from the excessive preoccupation with price movements per se which I have already discussed.

The central purpose of the international transactions of the United States is not to maintain a favorable balance of payments, but rather to achieve the levels and types of exports and imports which are most compatible with optimum economic growth, reasonably full resource use, and the servicing of our great domestic priorities, with due allowances for the contribution which we should make to the progress of peoples elsewhere, especially in the underdeveloped lands.

If these purposes are sought and achieved, it is not essential that the United States maintain a favorable balance of payments, Indeed, there is considerable force in the argument that the position of the United States in the world economy is such that we should run a substantially unfavorable balance of payments for many years ahead. The difficulty occasioned to us by large unfavorable balances has not been that these are intrinsically evil, but rather that the mechanisms for the handling of international transactions have not been sufficiently improved and modernized. What the CEA report says about such improvements and modernization is, in my view, far too tentative and limited.

A long-range program related to the volume and composition of our imports and exports should be developed, and made an integral part of the long-range economic and social budget which I advocate for continuous development by the CEA. There are many reasons for this. We cannot evolve a successful international policy without a successful domestic policy, and the two interrelate in ways too obvious to mention. Likewise, we cannot develop a successful domestic farm policy, without integrating it with our international economic policies. Nor can we develop a successful energy policy without integrating it with our international economic policies. Our own agencies in the international field are flying substantially blind, when they do not receive guidance from an overall agency such as the CEA, in terms of the relevancy of what we seek internationally to what we seek domestically.

In summary of what I have said thus far, our national economic and related social policies are based upon wide ranges of wrongful analysis. Equally important, they are not integrated and consistent. And above all, they are not responsive in the slightest to the vast potentials of our economy and our people, nor to the urgent needs which the achievement of these potentials would serve. They seek, and often erroneously, to alleviate difficulties after they appear, and not to reach out creatively and in time toward the great goals we should pursue. They thus fail to recognize the great challenge of the Employment Act of 1946.

In the following part II, I set forth alternative analyses, objectives, and policies, responsive in my view to the aims of the Employment Act and to the imperative needs of today and tomorrow.

Part II. My Own Analyses of the Economic Situation, and of Needed Policy Actions

In this part II, I offer my own analyses of the economic situation, and of needed policy actions. This serves two purposes. It amplifies and fortifies my criticisms of the CEA Report in part I. And it offers materials which I hope will be helpful to the Joint Economic Committee and to some others.

1. The Unsatisfactory Economic Performance, 1953–73

The deficient economic growth record

The desirable or optimum average annual rate of real economic growth is the rate needed to maintain reasonably full use of our growing productive resources. These resources include manpower and plant, natural resources, financial mechanisms and organizing abilities, brains and skills, free institutions, etc. The needed rate of real economic growth during any period is best determined by practical or empirical observation of growth rates in the past, with due allowance for accelerating trends in productivity and know-how under the incentives afforded during periods of reasonably full resource use.

The average annual rate of real economic growth was 4.7 percent during 1922–29, 4.5 percent during 1947–50, 5.1 percent during 1950–53, and 5.1 percent again during 1960–66. Viewing other factors also, it is conservative to conclude that an average annual growth rate of about 4.4 percent in real terms was needed and attainable during 1953–73.

But the average annual rate of real economic growth was only 3.6 percent during this 20-year period. Moreover, the economy did not grow steadily at this rate. The average annual rate was only 2.4 percent during 1953–60, only 3.3 percent during 1966–69, and only 3.6 percent during 1969–73, and the annual rate was only 2.4 percent from the first to the fourth quarter of 1973. In other words, the economy during these two decades has gone through four complete cycles of inadequate "boom" or upturn leaving us short of reasonably full resource use even at its peak, stagnation period, and period of absolute recession. The economy is now moving from the second to the third stage of a fifth such cycle.

The needed growth rate during the years ahead is not based upon the 4.4 percent figure cited above. During 1973–75, the needed growth rate is estimated at about 8.4 percent to restore reasonably full resource use by the end of 1975. Thereafter, taking account of the new technology and other factors, the needed average annual growth rate during 1975–80 is estimated at about 4.7 percent (see my chart 1 attached).

The deficient output record

Due to the inadequate rate of real economic growth, there has been a growing "gap" or deficiency in actual total national production (GNP), measured against reasonably full output. In 1953, this "gap" was only 0.4 percent or $2.2 billion, measured in 1970 dollars. But in 1973, the "gap" was 14.9 percent of $197.7 billion. And in the fourth quarter 1973, the "gap" was 15.6 percent or $210.8 billion (annual rate) (projections from 1953; see again chart 1).

The high unemployment record

Officially recorded unemployment depicts full-time unemployment as a percentage of the civilian labor force. But the true level of unemployment includes also the full-time equivalent of part-time unemployment, and the concealed unemployment in the form of those who are not participating in the civilian labor force—and therefore not counted as unemployed—because of scarcity of job opportunity. Even this true level of unemployment does not measure the underutilization of fully employed workers when there is large slack in the economy, which reflects itself in reduced productivity gains.

In my work for many years, a full-time unemployment rate of 2.9 percent and a true unemployment rate of 4.1 percent is regarded as consistent with maximum employment. The full-time unemployment rate was below 1.0 percent at times during World War II, but this probably involved excessive strain. On the other hand, the notion that unemployment rates very much higher than those espoused in my work are necessary or desirable to avoid excessive inflation is economically unsound and socially undesirable, for reasons which will be disclosed fully later on in my discussion.

In 1953, full-time unemployment was 2.9 percent, and the true level was 4.9 percent. Unemployment has been higher in every year since, and very much higher in most years. In 1966, after 5 years of relatively high economic growth which did not restore reasonably full resource use, full-time unemployment was 3.7 percent, and the true level was 6.1 percent. In 1973. full-time unemployment was 4.9 percent, and the true level was again 6.1 percent. By January 1974, full-time unemployment was 5.2 percent, and the true level 6.6 percent (see again chart 1).

The immense cost of the deficient performance

The cost of the deficient economic performance may be quantified by comparing the actual performance with the performance which would have resulted if reasonably full resource use at the average annual real economic growth rate of 4.4 percent had been maintained.

The total national production "gap," during 1953–73 as a whole, was more than $1:824 trillion, measured in 1970 dollars; for 1969–73, it was 922 million; and in the fourth quarter 1973 alone, it was at an annual rate of almost $211 billion.

The role of wages and salaries in the economy at large will be discussed in detail later on in the discussion. Suffice it at this point to note that, viewing the three periods above, the deficiencies in wages and salaries were more than $1.03 trillion, $457 billion, and more than $113 billion, respectively.

The true level of unemployment, in excess of the level consistent with maximum employment, was 48.5 million man-years during 1953–73, 10.8 million during 1969–73, and 1.8 million in fourth quarter 1973 alone.

It is also vital to note how the foregoing deficiencies in economic performance have affected the great priorities of our domestic needs which depend upon public outlays. On the basis of the increased tax collections which would have resulted from optimum economic performance, governments at all levels would have had about $471 billion more, again measured in 1970 dollars, available for these domestic priority outlays during 1953–73 as a whole; more than $275 billion additional available during 1969–73; and more than $80 billion additional available (annual rate) during fourth quarter 1973 (see chart 2).

One explanation is necessary with regard to the foregoing demonstrations. When it is stated that total national production in fourth quarter 1973 was running at an annual rate of almost $211 billion below maximum production, this does not mean that the annual rate of national production in that quarter would have needed to be increased that much to restore maximum production. This is because the stated figure is merely an estimate of where we would have been in fourth quarter 1973 if we had grown at an optimum rate from 1953 forward. For this purpose, the figure is entirely valid, and tremendously significant. But by fourth quarter 1973, our productive potentials were very much lower than they would have been if we had had a fully healthy economy from 1953 forward. Thus, the increase required, as of fourth quarter 1973, to restore reasonably full resources use was probably somewhere in the rough neighborhood of $100 billion—which was bad enough.

The prospects ahead, under current national policies

The full significance of this staggering waste of our full potentials cannot be appreciated without examining their import for the future. Without drastic changes in national and other economic and related social policies—and these changes are not yet on the way—it appears unlikely that the growth record during 1973–80 will be significantly different from that during 1953–73. In that unhappy event, the results are estimated as follows:

The forfeiture of total national production, again measured in 1970 dollars, is estimated at about $1.678 trillion for 1973–80 as a whole, and about $324 billion for 1980 alone. The forfeitures in wages and salaries are estimated at more than $866 billion and more than $171 billion, respectively. The forfeitures in Government outlays at all levels for goods and services are estimated at more than $234 billion and more than $43 billion, respectively. And the forfeitures in man-years of employment opportunity are estimated at 16.5 million and 2.6 billion, respectively (see again chart 2). The employment forfeitures are in much smaller ratio to the total national production forfeitures during the period ahead than during the past, because of the much higher productively and much higher earnings per employed worker.

2. *The Core Maladjustment: The Investment-Consumption Imbalance*

The superficial prevalent approach: neglect of sound distribution

The prevalent approach in national economic policy has been to try to increase total purchasing power when the economy is too slack, and to reduce total purchasing power when the economy is alleged to be overstrained. This theory would be sound if actual purchasing power were roughly in accord with actual spending. But for this to occur, the purchasing power must be properly distributed, in accord with considerations of economic balance. If purchasing power is not properly distributed, there is a gap between purchasing power and actual spending, in the form of more saving than is absorbed by current investment. And this results in less actual spending than is needed to use our resources fully, with consequent deficiencies in output and jobs.

The investment-consumption imbalances

The persistent lack of attention to the distribution problem has been the core cause of the "roller-coaster" prosperity, moving repeatedly from inadequate upturn to stagnation to recession. In each period of upturn, investment in the plant and equipment which add to production capabilities has increased very much more rapidly than ultimate demand in the form of total private consumer expenditures plus total public outlays for goods and services. Public outlays, although commonly called investment, are really ultimate demand or public consumption. This is because the preponderance of these public outlays are for purposes other than creating production goods.

Whenever the relatively excessive investment in production capabilities has become sufficiently severe in the form of actual or prospective "excess" capacities, such investment has been cut back very sharply. And these cutbacks, superimposed upon the larger and more enduring deficiencies in ultimate demand, have brought on the periods of stagnation and recession.

Practically every major economic policy has contributed to these imbalances. The Federal tax policy has done so for many years, by becoming much less progressive in nature, thus favoring investors as against consumers. The prevalent monetary policy of tight money and fantastically high interest rates has contributed to the imbalances, by favoring those who invest as against those who consume. The various attempts, direct and indirect, to "guide" or "control" prices and wages have had the same effects, because of their erroneous composition. And voluntary adjustments in the private economy have moved in the same wayward direction. The detail errors in these various policies will be described more fully as the discussion proceeds.

In short, the towering central problem of the U.S. economy is faulty income distribution, and yet almost no concern about this has been made manifest in the evolution of basic economic and related social policies.

The empirical evidence of the imbalances

The conclusion just reached is so important that the empirical evidence in support of it should be set forth rather fully.

From the first three quarters of 1955 to the first three quarters of 1957, from the first half of 1959 to the first half of 1960, and from the first half of 1961 to the first half of 1966, the three "boom" periods registered a real growth rate in investment and plant equipment extraordinarily more rapid than the real growth rate in ultimate demand. During these three periods, the real total growth in such investment was 8.5, 13.5, and 11.2 percent, respectively, while the growth rates in ultimate demand were only 2.7, 2.5, and 5.2 percent, respectively. During the two recession subperiods within the longer period cited, investment was cut back very drastically, but this was in response to the deficiency in ultimate demand rather than to inadequate prices or profits per unit of output and sales.

From the first half of 1966 to the fourth quarter of 1970, a mixed period including recession, ultimate demand grew considerably faster than investment, but not enough faster to restore balance and induce reasonably full resources use. And from fourth quarter 1970 to fourth quarter 1973, a period of inadequate upturn followed by stagnation and oncoming recession, investment grew 6.1 percent, while ultimate demand grew only 4.4 percent. This most recent period made manifest in glaring form the failure to apply correctiveness in the relative growth rates of investment and ultimate demand.

This analysis does not imply that investment in plant and equipment was adequate in the long run. Indeed, from 1953 to 1973, there was an annual average deficiency of $8.7 billion, measured in 1970 dollars, in such investment. But this deficiency did not occur because of repressive treatment of investment by national policy, nor because of inadequate prices or returns per unit of output; it occured despite excessively favorable treatment of such investment and prices and returns per unit on the high side, because of the deficiency in ultimate demand and the neglect of this by national and other economic policies (see chart 3).

The point is further developed by other types of empirical examination. During the "boom" or upturn period 1960–66, with all measurements in constant dollars, total national production advanced 34.9 percent, private consumer spending 32.2 percent, and Government outlays at all levels for goods and services 33.4 percent. Meanwhile, private investment in plant and equipment advanced 60.1 percent, which was a clearly nonsustainable rate in view of the relatively slow advances in ultimate demand. These unbalanced relative trends were abetted by distortions in income trends. Wages and salaries advanced only 33 percent, labor income including fringes only 34.1 percent, farm proprietors' net income only 23.6 percent, and transfer payments only 32.2 percent. But corporate profits advance 46 percent, personal interest income advanced 65.4 percent, and personal dividend income advanced 41.3 percent.

The period 1969–73 as a whole witnessed the inevitable reaction to these unbalanced trends. The real average annual growth rate was only 3.6 percent. Stagnation and recession occurred. It was only to be expected, during such a period, that ultimate demand would grow more rapidly than investment in plant and equipment, and that wages and salaries would grow more rapidly than corporate profits. But even during this period, such investment and profits grew relatively too rapidly, compared with ultimate demand and wages and salaries, so that economic balance was not restored. And toward the end of this period, the imbalances became even worse, as depicted below.

From third quarter 1972 to third quarter 1973, again measured in constant dollars, total national production grew 5.6 percent, private consumer spending grew 5.1 percent, and Government outlays for all goods and services grew 2.3 percent. But private investment in plant and equipment grew 11.3 percent. And while wages and salaries grew only 4.5 percent, and total labor including fringes only 4.4 percent, corporate profits grew 16 percent. The increases of 11.1 percent in transfer payments and of 29.4 percent in farm proprietors' net income did not nearly compensate for the gross lag in wages and salaries and labor income, in terms of the development of adequate ultimate demand. Moreover, the transfer payments did not add much to an ultimate demand, because they were financed mainly and unfortunately out of regressive payroll taxes. These respective trends brought stagnation and prospective recession (see chart 4). This analysis runs only through third quarter 1973 because the data on profits for fourth quarter 1973 were not available as of the time of preparation of these comments. But carrying the analysis through fourth quarter 1973 would not change the picture substantially.

Under the circumstances, nothing could be clearer than this: To avert or ameliorate the recession which is now in the making, if it is not already here, and to initiate vigorous progress toward restoration of reasonably full resource use as soon as feasible, the major concentration of all policies must be upon the adequate enlargement of consumer incomes and of the wage rates which are the major factors in the imperative advance.

3. The lag in Consumer Income and in Wage and Salary Income

The previous discussion makes it clear, by one method of approach, that the lag in consumer spending and income, of which wage earners' spending and income are the largest portion, has been the central explanation of the highly unsatisfactory economic performance during the past two decades, and especially during the most recent years. It is now desirable to quantify this conclusion in a somewhat different way. These quantifications are based upon full prosperity economic models which, as is well known, I have been developing and adjusting from year to year, and which have turned out to be reasonably correct (in the light of actual developments) as to full prosperity needs.

The deficient growth rate in private consumption and ultimate demand

Expressed in constant dollars, the needed average annual growth rate in private consumer spending was 5.3 percent during 1960–73. But the actual average annual growth rate was only 4.4 percent during this period, only 4.1 percent during 1966–73, and only 2.6 percent from fourth quarter 1972 to fourth quarter 1973. The deficiency in private consumer expenditures came to more than 51 percent of the deficiency in total national production during 1960–66, more than 43 percent during 1966–73, and almost 47 percent in fourth quarter 1973.

We have already noted that the deficiency in ultimate demand includes both private consumer spending and public outlays at all levels for goods and services; it is also true that these public outlays, apart from national defense, are primarily supplements to consumer incomes and living standards. The deficiency in ultimate demand came to more than 74 percent of the total national production deficiency during 1960–66, more than 72 percent during 1966–73, and more than 84 percent in fourth quarter 1973.

The deficiency in gross private investment came to less than 26 percent of the deficiency in total national production during 1960–66, less than 28 percent during 1966–73, and less than 16 percent in fourth quarter 1973. Further, more than half of the investment deficiency in recent years has been due to inadequate residential construction which in turn has been due to erroneous national policies which have impacted most heavily upon the housing conditions of lower-middle and low-income families. Less than half of the deficiency in gross private investment has been due to deficiencies in the private investment adding to production capabilities and, as earlier stated, this deficiency has been induced by the deficiency in ultimate demand (see chart 5).

Inadequate consumption growth due to inadequate income growth

It is not true, although it is frequently asserted, that inadequate consumer spending has occurred because consumers as a whole have saved too much and spent too little. The truth of the matter is that the basic reason for inadequate consumer spending has been inadequate consumer income. However, it is also true that, at any given level of consumer income, saving has been too high and spending too low because too large a portion of the total consumer income has flowed to those in the upper ranges of the income structure who save relatively large portions of their income, while relatively too little income has flowed to those lower down in the income structure who spend relatively large portions of their income and save less.

The trends in total private consumer spending and in total personal income after taxes demonstrate conclusively that both spending and income have been too low. Measured in constant dollars, the average annual rate of increase in total private consumer spending declined from 4.8 percent during 1960–66 to 4.1 percent during 1966–73, and to only 2.6 percent from fourth quarter 1972 to fourth quarter 1973. The respective figures for total personal income after taxes were 5.1, 4.1, and 3.2 percent. The much more rapid growth in income than in spending during the most recent period clearly indicated the gravity of income maldistribution.

For the period 1960–73 as a whole, it is estimated that the deficiency in private consumption of $790 billion, measured in 1970 dollars, was based fundamentally on a deficiency of $1.154 trillion in total consumer income before taxes (see chart 6).

The role of the deficiencies in wages and salaries

The next step in the quantitative analysis is to portray how much the deficiencies in wages and salaries have contributed to the deficiencies in total consumer income before taxes. For the period 1953–73 as a whole, with all measurements in 1970 dollars, the annual average deficiency of $49.1 billion in wages and salaries came to more than 75 percent of the $64.8 billion average annual deficiency in total consumer income before taxes. In 1973, the wage and salary deficiency of $105.4 billion came to more than 81 percent of the $129.3 billion deficiency in total consumer income before taxes. And in fourth quarter 1973, annual rate, a wage and salary deficiency of $113.2 billion came to almost 83 percent of the $136.5 billion deficiency in total consumer income before taxes (see chart 7).

4. The Lag in Wages and Salaries Behind Productivity Gains: The Significance of the Productivity Potential

One of the most commonly accepted propositions, among economists and national policymakers, is that real wage and salary increases should be kept closely in line with gains in productivity or output per man-hour. There are some imperfections in this position which will be treated later on in the discussion. But first of all, it is desirable to compare the trends in productivity or output per man-hour with trends in real wages and salaries.

The wage and salary lag, by conventional measurements

In the total private nonfarm economy during 1960–73 as a whole, the average annual rate of advance was 2.8 percent for output per man-hour, and 2.7 percent for wage and salary rates per man-hour. This would seem to indicate a rough balance, although (as will later be shown) the wage and salary rate gains were improperly repressed in response to repression of productivity gains due to the excessive slack in the economy. In any event, it is far more important to note the trends during the subperiods within 1960–73.

During 1960–66, the average annual rate of increase was 3.4 percent for productivity or output per man-hour, and only 2.7 percent for wage and salary rates. The tremendous lag in wage and salary rates during this period of "boom" or upturn was naturally the main cause of the deficiency in total wages and salaries which did so much to prevent full economic restoration, and to bring on the very inferior economic performance from 1966 forward.

During 1966–73, when the average overall economic performance was very deficient, the average annual rate of increase in output per man-hour fell to 2.3 percent. The average annual rate of increase in real wage and salary rates was held at the somewhat higher figure of 2.7 percent. This was not nearly good enough for reasons which will be discussed when I come to consider the growth in the productivity potential, as distinguished from the actual growth in productivity.

From fourth quarter 1972 to fourth quarter 1973, the average annual growth rate in productivity or output per man-hour in the total private nonfarm economy was only 0.8 percent. This happened despite the fact that the real economic growth rate during this period was somewhat higher than the average during 1966–73. The reason was that continuation of a sorely deficient rate of real economic growth during the later period added to the problem of unused resources which always has an adverse effect upon productivity gains. But during this period from fourth quarter 1972 to fourth quarter 1973, something even worse happened. Instead of the rate of increase in real wage and salary rates increasing more than the very small rate of increase in productivity gains, there was no real improvement at all in wage and salary rates. From the viewpoint of the wellbeing of the entire economy, this was one of the most unfavorable developments on record. It tremendously aggravated the deficiency in total wages and salaries, the main factor in pulling the economy downward toward absolute recession.

The situation has been even worse in total manufacturing. During 1960–73, the average annual rates of advance were 3.7 percent for productivity, and only 2.1 percent for wage and salary rates. During 1960–66, the average annual rates of advance were 3.8 and 2 percent, respectively. During 1966–73, the average annual rates of advance were 3.5 and 2.1 percent, respectively. And from fourth quarter 1972 to fourth quarter 1973, the rates of advance were 2.3 percent and minus 0.2 percent, respectively.

These respective trends in manufacturing show the ridiculous bias of the hue and cry, especially in manufacturing, that wage gains have been excessive, and have been the reason why prices have moved so rapidly upward (see chart 8).

The productivity potential and its significance

Thus far, the data presented have compared the trends in real wage and salary rates with the trends in actual productivity. But although this comparison is in line with the thought and action in national and other policies bearing upon wage adjustments, it is entirely fallacious. For it is economically injurious to adjust real wage and salary rate increases to the extraordinary repressed productivity gains which result from severe economic slack. The clear consequences of doing this is to aggravate and compound the economic slack, by developing wages and salary trends which are entirely inconsistent with economic restoration, or with any viable model for an economy at reasonably full resource use. Instead, real increases in wage and salary rates should be adjusted to the growth rate in the productivity potential, which means the indicated growth rate in actual productivity which would occur under conditions of reasonably full resource use.

It is no sound argument that an economy "cannot afford" wage and salary rate gains of this size when the economy is in fact repressed, and when actual productivity gains are correspondingly reduced. Such an argument is rather akin to arguing that public spending should be reduced when we are suffering from severe economic slack, because the economy "cannot afford" more public spending. This line of argument defies the very meaning of economic restorative policies, which should be designed to bring every major component of the economy into line with what such component should be in a fully healthy economy, or should be in an economy moving vigorously toward that goal.

Nor is there any merit in the argument that the wage and salary rate policy herein recommended should not be applied to private industry, when private industry is suffering from the profit consequences of a stagnating or recessionary economy. For even during such periods, within the two decades under review and certainty during the most recent years, prices and profit margins per unit of output have been high enough if not too high. If the absolute level of profits have at any time been too low to induce an adequate level of private investment to meet the requirements of a soundly performing economy, the appropriate expansion of ultimate demand, in the form of private consumption and public outlays, would quickly restore the needed level of profits, and indeed the tendency would be these profits to become too high in terms of economic balance throughout the economy.

The trends in the productivity potential

With these considerations in mind, let us now look at the record with respect to the productivity potential in the U.S. economy. Viewing the entire U.S. private economy, it appears that advancing technology, increased labor skills, and other factors have tended toward an accelerating growth rate in productivity under conditions of reasonably full resource use. The actual average annual productivity growth rate rose from 0.5 percent during 1910–20 to 2.4–2.5 percent during 1920–40, and to 3.1 percent during 1940–55. (It was 4.1 percent during 1947–53.) The productivity growth rate sank to 2.3 percent during the poor economic performance years 1955–60, and then rose to 3.8 percent during the "boom" or upturn years, 1960–66. It then fell to an average of somewhere in the neighborhood of 2 percent during the years 1966–71, which were characterized on the average by very poor economic performance. But during the period of brisk recovery from first quarter 1971 to first quarter 1973, the average annual productivity growth rate shot up to 4.3 percent. Then, from first quarter 1973 to fourth quarter 1973, a period of stagnation and oncoming recession, the average annual rate of productivity gain was minus 0.7 percent.

From the foregoing data, it appears conservatively that the growth rate in the productivity potential for the U.S. economy at large was about 3.2 percent during 1950–55, and about 3.7 percent during 1955–73. It is in accord with these estimated gains in the productivity potential that real wage and salary rate gains should have been adjusted during the years mentioned (see chart 9).

Under the wage price guidelines or "controls," as first applied during the Kennedy-Johnson years and then under the Nixon administration, the alleged objective has been to achieve real wage and salary rate gains in the neighborhood of 3 percent, this purporting to be roughly in line with nationwide productivity gains. But due to the deficiencies in the application of the policy, it is clear that the gains in real wage and salary rates have lagged seriously behind the 3 percent figure. And they lagged much more behind the growth rates in the productivity potential which constitute the proper standard for real wage and salary rate gains.

5. *Significance of Erroneous Fiscal and Monetary Policies*

The erroneous policies with respect to wages and salaries, already depicted, have been gravely aggravated by erroneous fiscal and monetary policies. These also have contributed to income maldistribution, added to the investment-consumption imbalances, and reinforced the trends toward "boom," stagnation, and recession. Wage earners have been the major victims of all this.

The general errors in tax reductions and concessions during the 1960's and 1970's

During the 1960's and on into the 1970's, the Federal Government, with the main impetus stemming from the executive branch, engaged in an orgy of ill-considered and unwise tax reductions and concessions. The practical consequence has been to feed the fat and starve the lean, by redistributing after-tax income in nonprogressive directions, and by reallocating resources and economic activity in a manner highly contributory to the economic imbalances already discussed. Thus, in the overall, these tax reductions, while avowedly designed to stimulate the economy, have at best given it a brief shot in the arm; in the longer run, they have intensified the maladjustments leading to periodic stagnation and absolute recession. Simultaneously, by the choice of misdirected tax cuts in lieu of well-directed Federal spending, the great priorities of our domestic needs have been dangerously underserved, with immense damage to the people at large.

The nonprogressive nature of the tax cuts, 1964–73

The data on this subejct are very revealing. Those with incomes below $3,000, who comprised 16.1 percent of the tax return in 1969, received only 7.9 percent of the total tax cuts during 1964–73. Those with incomes between $3,000 and $5,000, who comprised 14.8 percent of the tax returns, received only 12.9 percent of the tax cuts. In contrast, those with inocmes between $5,000 and $10,000, who comprised 35 percent of the tax returns, received 38.4 percent of the tax cuts. Those with incomes between $10,000 and $20,000, who comprised 28.8 percent of the tax returns, received 29.6 percent of the tax cuts. Those with incomes between $20,000 and $50,000, who comprised 4.7 percent of the tax returns, received 10.3 percent of the tax cuts. And those with incomes over $50,000, who comprised only 0.6 percent of the tax returns, received 0.9 percent of the tax cuts.

It is no excuse for the misdirection in this tax cutting that there is "more room" for tax cuts among the higher income brackets because they have higher incomes, and pay more in taxes in relationship to their incomes. Despite this, it would have been feasible and highly desirable to concentrate more of the tax cuts lower down in the income structure. Other things being equal, tax cuts for everybody are desirable. But other things being as they actually were, neither economic nor social conditions justified large and repeated tax cuts for those with high incomes, and maybe not even for those in the upper middle income groups (see chart 10).

The tax cuts aggravated the investment-consumption imbalances

Still another reason why the pattern of the tax cuts was economically unsound was that they allocated relatively too much to the investment function, and relatively too little to the consumption function. Taking as an example the 1971 tax cuts, their short-run effects during 1971–72 were to allocate $4.5 billion to the investment function, and only $3.4 billion to the consumption function. Their permanent effects, as of 1973 and thereafter, were to allocate $7.4 billion to the investment function, and only $2.7 billion to the consumption function. The complete misdiagnosis of the economic situation and our economic needs, represented by such a pattern of tax cuts, has already been discussed fully (see chart 11).

The excessive tax cuts estopped adequate increases in public spending

The repeated decision to put so much into tax cuts, and so little into increased Federal spending, was abysmally wrong. Tax cutting was a far less efficient method than increased public spending, with regard to stimulating the economy, because a substantial portion of the benefits of tax cuts were saved instead of being spent, and doubly so because of the nonprogressive nature of the cuts. Relatedly, the undue emphasis upon tax cuts for investors aggravated the investment-consumption inbalances. Besides, a substantial portion of the tax cuts created excessive aftertax investment income, even in relationship to domestic outlets for investment. Consequently, an excessive portion of investment was directed overseas, to the detriment of our balance of payments.

And it is obvious that tax cuts, especially in the nature of those undertaken, contributed very little toward serving the great priorities of our domestic needs, which primarily supplement the living standards of wage earners and others who are not in the high income structure. The alternative of increased public spending could and would have been directed toward these purposes. To illustrate, the massive tax cuts of 1964 had an immediate annual value in the neighborhood of $20 billion, and this value increased year by year as the tax base grew with a growing economy. At least half of these 1964 tax cuts should have been directed instead to increase public spending for priority needs. This would also have helped to correct the investment-consumption imbalance, in that (as earlier stated) public spending is mostly ultimate consumption.

The massive tax cuts of 1964 provided a brief stimulus to the economy, as $20 billion thrown into the streets would have done. But within a couple of years, the results were renewed stagnation, and thereafter the substantial beginnings of roaring inflation as stagnation progressed and ended in recession.

The excessive scarceness in the money supply, and its adverse impact upon economic growth

It would be too cumbersome and complex, for the purposes of my comments, to undertake a comprehensive examination of the trends in the prevalent monetary policy and its effects. But enough can and should be said to make the errors transparently clear.

During 1953, third quarter 1973, as earlier stated, the average annual rate of real U.S. economic growth was only 3.6 percent, or seriously deficient. During the same period, the average growth in the nonfederally held money supply averaged annually only 3.5 percent. This establishes a strong initial case that the supply of money has in general been made too tight. It will not do to argue that the trends in the money supply have merely been responsive to the real performance of the economy, and not affected it. For the money managers themselves have frequently admitted that, at times, they deliberately tightened the money supply to repress the economy in the name of fighting inflation.

It is well known that the scarcity approach to the money supply has been extreme during particular years, and this has contributed mightily to the damaging downward movement in the rate of real economic growth. The growth rate in the nonfederally held money supply was only 2.2 percent from 1954 to 1955, only 1.3 percent from 1955–56, and minus 0.7 percent from 1956 to 1957. The real growth rate of the economy was only 1.8 percent from 1955 to 1956, only 1.4 percent from 1956 to 1957, and minus 1.1 percent from 1957 to 1958. From 1958 to 1959, the growth rate in the money supply was only 1.1 percent, and from 1959 to 1960 minus 0.6 percent, and the real economic growth rate was only 2.5 percent from 1959 to 1960, and only 1.9 percent from 1960 to 1961. From 1965 to 1966, the growth rate in the money supply was only 2.2 percent, and from 1966 to 1967 the real economic growth rate was only 2.6 percent. From 1968 to 1969, the growth rate in the money supply was only 3.2 percent, and from 1969 to 1970 the real economic growth rate was minus 0.4 percent. From second to third quarter 1973, the growth rate in the money supply was lower than from third quarter 1972 to third quarter 1973 as a whole, and the real economic growth rate dropped to 3.4 percent from second quarter 1973 to third quarter 1973, compared with 5.6 percent from third quarter 1972 to third quarter 1973 as a whole.

The fantastic rise in interest rates, and their adverse impact upon the economy

The application of the prevalent theory to the growth rate in the money supply has forced interest rates up fantastically; relatively minor undulations in these rates have not affected much the long-term upward trend. Comparing 1952 with October 1973, the cost of money rose 2.13 to 6.81 percent on U.S. Government 3–5 year issues; from 2.96 to 7.60 percent on Aaa corporate bonds; from 2.19 to 5.05 percent on high-grade municipal bonds; from 3.49 to 9.24 percent on short-term bank loans to business; from 2.33 to 8.92 percent on 4–6 month prime commercial paper; and from 4.29 to 9.18 percent on FHA new home mortgage yields.

The immense increases in the cost of money has had very uneven impacts upon various sectors of the economy, adding to the economic imbalances which explain the "roller-coaster" prosperity with all of its injurious effects. Thus, the rising cost of money has had very little effect upon investors in the key sectors of big industry. This is because these key industries have relied more upon retained earnings than upon borrowings, which have constituted a small fraction of their total investment funds, and also because they have been able to pass on to others through price increases those rising costs which they have experienced. Simultaneously, the rising cost of money has been extremely hurtful to small business, wage earners, families, homeowners, and other consumers. Nothing has been more regressive socially and more repressive in the overall than the rising cost of money.

The direct costs to borrowers of rising interest rates: the excess interest costs

In the overall, from 1952 to 1972, the average interest rate on the Federal public debt rose 106.9 percent. This imposed an additional interest cost upon the Federal public debt of $60.3 billion, all of which was an excess interest cost because the policy resulting in these increases was unwarranted and unjustified on all scores. In 1972 alone, the excess interest charges imposed upon the Federal public debt were almost $8 billion. And furthermore, these excess interest costs increased the size of the Federal public debt and of the Federal budget deficits. They did not only directly, but also because they contributed to the deficient economic performance with its adverse impacts upon revenues at existing tax rates.

It is strange indeed that those very economists who assert that the Federal deficits have been a primary cause of inflation maintain at the same time that a monetary policy which has added so much to these deficits has been antiinflationary.

The rising cost of money upon Federal borrowings has necessarily affected the cost of money on all other types of borrowings, because recognized margins are maintained among these various types. From

1952 to 1972, the average interest rate on the total public and private debt rose 119.3 percent, and this imposed excess interest costs of $570.9 billion for the period as a whole. In 1972 alone, the excess interest cost on the total public and private debt was $84.9 billion (see chart 12).

Preferable uses of amount involved in excess interest costs: enlarged incomes, especially among the poor

The following examples are merely illustrative of preferable uses of the amount involved in the excess interest costs, without implying that the total amount should have been channeled in the directions indicated, although a very substantial part of it should have been so channeled.

If the $570.9 billion of excess interest costs during 1953–72 had instead flowed to increase the incomes of American families, they would have provided more than $11,500 to each family of four, and more than $1,600 to each family of four in 1972 alone. On a *per capita* basis for the entire population, the excess interest costs were equivalent to almost $2,900 for the period as a whole, and to more than $400 in 1972 alone.

To take a related example, the excess interest costs of $570.9 billion, during the period 1953–72 as a whole, averaged $28.5 billion annually. If this amount had instead been directed toward increasing the incomes of all families living in poverty with incomes below $4,000 with average income of $2,405 in 1971, it would have provided $4,130 more of income to each of these families in each year of the entire period under review. If channeled to all families with incomes below $3,000, with average income of $1,836 in 1971, it would have provided $6,477 more to each of these families in each year. And if the total amount had been channeled to families with incomes below $2,000, with average income of $1,159 in 1971, it would have provided $13,571 more to each family in each year.

The immediately foregoing example demonstrates that only a fraction of these excess interest costs should have been channeled directly toward the liquidation of poverty. In fact, it is generally estimated that only somewhere in the neighborhood of $13 billion of income supplementation would be needed annually to lift out of the poverty cellar all of the American families imprisoned therein. And far less than this amount would be required, if the tight money policies and other prevalent policies had not prevented the maintenance of reasonably full employment and production, which in itself is by far the greatest factor in the reduction of poverty (see chart 13).

Preferable uses: the great priorities of our domestic public needs

With respect to the great priorities of our domestic needs, which are financed by the Federal budget, let us now examine the implications of having available for these great purposes the excess interest costs imposed upon the Federal budget by the prevalent economics in its monetary aspects.

On a calendar year basis, the annual average excess interest cost in the Federal budget was $5,519 million during 1964–72. And on a fiscal year basis, during the years 1964–74, annual average Federal budget outlays for education were $4,719 million, for health services and research $10,902 million, for housing and community development $2,871 million, for public assistance and welfare services $7,028 million, and for manpower programs $1,912 million. In calendar 1973, the excess interest costs in the Federal budget were in the range of $8 billion. As proposed originally by the President in the 1975 fiscal budget, outlays for education were $8,195 million, for health services and research $26,282 million, for housing and community development $5,667 million, for public assistance and welfare services $17,894 million, and for manpower programs $3,342 million.

How truly disheartening it is to contemplate how much the sorely deficient level of outlays for these Federal vital domestic public purposes could have been increased, if the Federal budget had not been burdened with the economically unsound and morally indefensible excess interest costs (see chart 14).

The foregoing is highly relevant to wage policy proper. For the shortchanging of essential public services means that, for economic and social reasons, an even more "liberal" wage policy is needed than if this short-changing were not in effect and in prospect.

6. Goals for the U.S. Economy, 1975 and Fourth Quarter 1975

One important point I have already developed is that national and other policies bearing upon wage adjustments have not related these adjustments to the real needs of the economy. And they can hardly do so, when policies in general have not been based upon consistent and adequate goals for the economy at large, but instead have been improvised at random, and hardly related to the requirements for full economic restoration. For this and other reasons, as in many previous materials I have furnished the JEC, it is necessary to set forth goals for the economy at large, and the related goals for wage and salary adjustments in general. These goals are based upon the requirements for achieving reasonably full resource use by the fourth quarter of 1975. All of the goals have been reconciled within my model for the economy at large, already referred to.

Goals for the economy at large, including wages and salaries

Projected from a 1973 base, civilian employment should be up 6.7 percent by 1975, and 7.8 percent by fourth quarter 1975. This would reduce the volume of unemployment by 28.6 percent in 1973, and 34.6 percent in fourth quarter 1973. The target is full-time or official by reported unemployment of about 2.9 percent, and a true level of unemployment of about 4.1 percent.

Total national production in real terms should be up 17.5 percent by 1975, and 19.5 percent by fourth quarter 1975. As a proper component in this objective, consumer spending in real terms should be up 12.5 percent by 1975, and 14.5 percent by fourth quarter 1975.

Total wages and salaries in real terms should be up 16.4 percent by 1975, and 18.6 percent by fourth quarter 1975. Part of this would reflect additional employment, and part of it would reflect productivity gains.

In an economy moving at appropriate speed toward full restoration, productivity or output per man-hour should be up 11.8 percent by 1975, and 12.8 percent by fourth quarter 1975. This is much higher than the long-term growth rate in the productivity potential, as must be the case in a vigorous recovery movement. The growth in employment, plus the growth in productivity, would exceed the growth in total national production, due to the changes in working hours and other factors in the composition of the labor force.

Real wage rates should rise by 10.4 percent by 1975, and 11.3 percent by fourth quarter 1975. Wage rate gains are projected at a slightly lower rate than the growth in productivity, so as not to move real wage growth too far out of line with longer-term sustainable trends (see chart 15).

The goals will seem excessive and unattainable to those who have never adjusted their thinking to a genuinely restorative economic effort. Because we did what we needed to do during World War II, the rate of real average annual economic growth was about 9 percent. To be sure, this was from a low base, but it is also true that more than 13 million potential workers were drawn into the Armed Forces.

7. *The Prevalent Economics Foments Price Inflation and a New Approach To Restraining It*

The theory and practice of the prevalent economics is so thoroughly ingrained, among university teachers and practitioners and policymakers, that they usually do not deem it necessary to defend it. But when they do make the attempt, the defense converges upon this erroneous proposition: The economy experiences more price inflation when it gets near to reasonably full employment and production, and experiences less price inflation when idle resources move further and further below reasonably full use. Thus, every deliberately contrived effort to slow down an upturn before reasonably full resource use is achieved, and many repressive efforts even when the economy is in stagnation or recession, are avowedly undertaken to hold back the real economic performance in the name of restraining inflation. This makes restraint of price increases the paramount objective of the policymakers. And this is very wrong.

Particular price levels are not a paramount economic objective: the true function of prices

Let us start by assuming, contrary to the empirical evidence which will soon be discussed, that the cause-of-inflation thesis oflthe scarcity economists, sometimes related to the so-called Phillips curve, is correct. Even on this assumption, sacrificing the three great and ultimate purposes of our economic system to curb price inflation is indefensible in practice. For these three great and ultimate purposes do not relate to prices per se. Rather, they are (1) to maintain the rate of real economic growth which yields reasonably full employment and production, these being ultimate values in themselves, and the absence of these being far more costly than any differences in the price level which are deemed to result from varying rates of real economic performance; (2) to meet the great priorities of our domestic and international needs; and (3) to do social justice. Neither given price levels nor given trends in prices can properly be classified as a fourth great purpose in this ultimate sense.

To put this another way, the prevalent economics mistakes the true function of prices in our economy. No particular price levels, and no particular trends in prices, are desirable per se. The true function of prices and profits, of wages and other forms of income, and of public fiscal and monetary and other economics policies, is to allocate incomes and resources in the manner most conducive to fulfillment of the three great and ultimate purposes of economic system. Experience, in general, indicates that the balance or adjustments essential to these three great purposes may be achieved under a stable, rising, or falling price level, and whatever price trends promote these great purposes are desirable price trends.

To take the most telling example, an extraordinary stable price level during 1922–29, except for falling farm prices, did not prevent the "Great Crash." It came because, even under a stable price level, the cost reductions due to productivity gains were translated excessively into profits and investment, instead of being shared adequately with workers, farmers, and other consumers. In consequence, our ability to produce grew enormously out of line with ultimate consumption, and this always spells trouble.

In short, the prevalent economics during recent times has been utterly wrong, in attempting to give primacy to the attainment of so-called price stability. Moreover, as will shortly be shown, the approach has also aggravated inflation greatly.

To illustrate further why any particular degree of price stability should not be accorded this primacy, let us look at it this way: If the amount of price inflation we have actually suffered in recent years had been accompanied by policies and programs designed successfully to matintain optimum economic growth and reasonably full employment and production, to meet the great priorities of our domestic and international needs, and to do social justice, the bargain or "trade off" would have been one of the finest the policymakers ever made (again, as will soon be pointed out, fulfillment of these primary objectives would have yielded far less price inflation). But when this actual amount of price inflation during recent years has been accompanied by policies deliberately and "successfully" designed to thwart and neglect these great purposes of our economic life, this amount of inflation has been stupid, cruel, and indefensible. It is manifestly immoral, for example, to make millions of breadwinners and their families suffer the ignominy, income losses, and the other evils occasioned by massive unemployment, even if such action enabled the affluent and rich to buy luxuries and necessities at a somewhat lower price than would otherwise be the case.

The prevalent theory of price inflation is standing on its head: the empirical evidence against it

But all the foregoing is only the beginning of the sorry story, with respect to the means attempted by the prevalent economics to restrain price inflation. For directly contrary to the prevalent theory, higher economic growth and fuller use of manpower and other resources have meant less price inflation, while stagnation and recessions have usually meant more price inflation. The experience record on this has now endured for more than two decades.

During 1952–55, the real annual economic growth rate averaged 3.5 percent, and officially recorded full-time unemployment averaged 4 percent. Menawhile, the average annual rate of inflation was only 0.3 percent for consumer prices, minus 0.2 percent for wholesale prices, and only 1.1 percent for industrial prices.

Then came the period 1955–58, when the average annual rate of real economic growth was only 0.8 percent. Officially recorded full-time unemployment averaged 4.9 percent, and the annual rate within this period rose from 4.4 percent in the first year to 6.8 percent in the last year. Meanwhile, the average annual rates of inflation were 2.6 percent for consumer prices, and 2.5 percent for wholesale and industrial prices.

During 1958–66, the average annual rates were 4.9 percent for real economic growth, and 5.4 percent for unemployment, and unemployment declined from 6.8 to 3.8 percent. Cocurrently, the average annual rate of inflation was 1.5 percent for consumer prices, 0.7 percent for wholesale prices, and 0.6 percent for industrial prices.

Then, during 1966–69, the average annual rate of real economic growth declined to 3.3 percent. Unemployment averaged 3.6 percent, and declined only from 3.8 percent in the first year to 3.5 percent in the last. The average annual rate of inflation was 4.1 percent for consumer prices, 2.2 percent for wholesale prices and 2.5 percent for industrial prices.

During 1969–73, the average annual rate of real economic growth remained at the deficient level of 3.6 percent. Unemployment averaged 5 percent, and rose from 3.5 to 4.9 percent, comparing the first and last year within this period. The average annual rate of price inflation was 4.9 percent for consumer prices, 6.2 percent for wholesale prices, and 4.6 percent for industrial prices.

The utter bewilderment and confounding of the prevalent economics came during the period from first quarter 1973 to fourth quarter 1973. Measured at an annual rate, the real rate of economic growth was at the stagnation level of only 2.4 percent, and unemployment averaged 4.9 percent, declining only from 5 percent in the first quarter to 4.7 percent in the third. Meanwhile, the average annual rate of inflation was 9.3 percent for consumer prices, 16.2 percent for wholesale prices, and 13.7 percent for industrial prices (see chart 16).

To cap the climax, the informed forecasts are now to the effect that the stagnation will become worse, and most likely end in an absolute recession, sometime in 1974. As usual, the price forecasts are strangely "optimistic," but to date they have been more optimistic than reality. Even so, consumer price inflation is forecast to run somewhere between 6 and 8 percent, with even more inflation in the other sectors.

It might hopefully have been anticipated that, at long last, the scarcity economists would have abandoned their discredited theory as to the causes of price inflation, and accordingly abandoned the repressive economic measures which they have applied. Not so. Instead of admitting that their cause-of-inflation theory has been thoroughly discredited, they still aver that it is marvelous. But they now have revised upward their estimates as to the amount of unemployment which we should tolerate, or even encourage, in order to curb price inflation. A fine example of this is the man reportedly slated to be the next Chairman of the Council of Economic Advisers.

The wise choice, guided by experience

The author of this study is ready to admit that the data and correlations which he has offered above are not absolutely conclusive. Different periods might possibly be selected for the exercises, even though those actually selected are entirely reasonable. More refined analysis might yield slightly different results, but not substantially so.

But the enduring evidence is overwhelming: There is no justification whatsoever for the prevalent thesis, translated into practice, that we should sacrifice so much by way of the three great purposes of our economic growth for so dubious a cause-of-inflation theory, completely unproved even if not completely refuted by all experience. It would be better to move forward with what we need to do to fulfill these three great purposes.

It may possibly be true, although the author of this study doubts it, that contrived departures from a reasonably well-performing economy might at times temporarily abate some price inflation. It may also be true that vigorous efforts toward economic restoration, which are now so imperative, might at times temporarily augment inflationary pressures. But a longer view should be taken. "Fine-tuning" has proved itself a flop. In the long run, it appears incontestably true that an economy maintained at reasonably full resource use, and fulfilling its obligation toward priorities and social justice, would average less net price inflation than the "roller-coaster prosperity" induced by the egregiously wrong theory of the causes of inflation now for so long in vogue.

Toward a revised theory of the causes of inflation based upon the empirical evidence

It is not by accident nor fortuitously that the prevalent theory as to the true causes of price inflation have been so thoroughly repudiated by the relevant empirical evidence. There are many theoretical explanations of what has actually happened.

First, an economy with contrived and serious shortages generates clear tendencies toward more inflation. We should by now recognize this, especially in view of the current and prospective inflationary impact of the food and energy shortages.

Second, the rate of gain in productivity or output per man-hour, when the economy is in stagnation or absolute recession, is only one-third to one-fifth as large as when it is reasonably near full resource use. This increases per-unit costs of production, and results in large price increases, whether justifiable or not in view of profit margins. To put this in another way, large departures from reasonably full resource use mean an inefficiently operating economy, and inefficiency breeds inflation.

Third, aside from farm prices and some others, prices are no longer determined by "supply and demand." They are instead "administered" prices fixed by the deliberate policy decisions of business managers. All relevant experience shows that these managers, in pursuit of predetermined profit goals, and in order to cover the higher costs resulting from deficient volume, lift their prices more rapidly in the face of inadequate sales than in the face of a full volume of sales. Whether the managers are "right" or "wrong" in so doing is beside the point.

In economics classes 75 years ago, the students were told that the holder of 10 apples would increase the price if there were 11 buyers and decrease it if there were 8 buyers. The professors, including even Paul Samuelson to a degree, still say this today. But if the holder of the apples controls the supply, and if people want or need to buy them, he will increase the price more when there are 8 buyers than when there are 11 buyers, in order to cover costs and achieve profits. This observation of commonsense, confirmed by experience, has not found its way into the thinking of the prevalent economics.

Fifth, the pernicious policy of tight money and fantastically high and usually rising interest rates, also pursued in the name of fighting inflation, is very inflationary per se. This is because the rising cost of money operates like other rising costs. If the rising cost of money is experienced by business firms in the "administered" price areas, they translate this into rising prices charged against the industries and consumers to whom they sell. Insofar as the rising cost of money is experienced directly by consumers in their buying, they tack this rise in the cost of living on to their wage demands, and this, rightly or wrongly, is claimed to be inflationary. If consumers are in a position where they cannot take this compensatory action, they merely suffer the inflation. Also, the prevalent money policy helps to stunt real economic growth, and this in itself is inflationary.

Sixth, the business uncertainties, spawned by the "roller coaster" prosperity, add greatly to inflationary pressures. Price increases are engineered to "counter" these uncertainties. Thus, the assurance, through performance, that there is full commitment to sustained full prosperity would do most to dispel the motivations toward undesirable price increases.

8. *Comments About Housing*

In part I of my comments, I referred to the insignificant treatment of housing in the 1974 CEA Report. I now reinforce this comment with my own analysis.

High promise and poor performances

The deficiencies in our housing supply, both quantitative and qualitative, are perhaps the best illustration of the interdependence of economic and social considerations.

The Housing Act of 1949, with bipartisan support, established the goal within a decade of "a decent home for every American family in a suitable living environment." Almost a quarter century later, despite the advantage of our increased economic capabilities and organizing skills, we have not moved appreciably closer to this goal. And in terms of the unfavorable impact of bad housing upon urban conditions generally and municipal costs, it is a salient feature of the housing neglect that our urban areas have been subjected to a progressive decay.

There have been many studies of the influences of bad housing upon the one-fifth to one-fourth of our population (according to the criteria applied) who live in bad housing, in terms of its effects upon morale, health, social behavior, and civic behavior and attitudes. In view of these available studies and their wide currency, I will not develop this aspect further. But there has been relative neglect of the impact of the deficient housing performance upon our general economic performance, in terms of investment, employment, and production opportunity. Accordingly, I shall now concentrate upon these aspects.

The deficient trends in housing starts

In 1950, a relatively banner year for housing, there were 1,952,000 housing starts. The rate declined to 1,500,000 in 1969, and to 1,469,000 in 1970. The number moved upward to 2,058,000 in 1971, and to 2,379,000 in 1972. It then declined to 2,080,000 (estimated) in 1973.

And the seasonally adjusted annual rate was only 1,642,000 in October 1973. Thus, the average annual rate of housing starts during the past 5 years has been immensely below the average annual goal of 2,285,000 during 1973–80, and 2,500,000 in 1980 alone. These goals have not been developed by me; they are the official goals of the Government itself.

The seriously deficient nature of this housing performance cannot be fully appreciated, without examining the composition of the housing starts. Only so-called public housing relates closely to the needs of the poor and deprived, who occupy most of the bad housing. In 1950, there were only 44,000 public housing starts. During each year from 1969 forward, the total was very much lower, with only 22,000 in 1972, and only 15,000 estimated for 1973. The seasonally adjusted annual rate in October 1973 was only 29,000. Moreover, very little housing is built for those in the lower middle-income group, and far too little even for those in the middle-income group. The extraordinarily high concentration of housing starts among those in the upper middle-income and high-income groups is not only socially wrong. It also explains the recurrent "saturation" of the housing market for these groups, which in turn explains the extraordinary erratic trends in housing starts, and their serious consequences for the economy at large.

This record, combined with the most recent actions of the President with respect to housing, make a mockery of the official goals for housing performance (see chart 17).

Many erroneous national economic policies on many fronts have contributed to the poor record. This applies not only to housing policy proper, but also to tax and spending policies, and to those other policies which affect income distribution and overall economic performance. But it will suffice, at this point, to refer explicitly only to the prevalent monetary policy. Roughly speaking, the excess interest costs imposed on housing mean that, if a family with an income of $7,500 buys a new $15,000 home, it will pay excess interest costs over the customary life of the mortgage equivalent to a full year of its annual income after taxes. The practical result is that most families in middle-income groups simply cannot buy. And when they do, what could be more inflationary than the excess costs imposed upon them?

The job scarcity in contract construction

The highly unsatisfactory housing performance has contributed directly to a much higher rate of unemployment in contract construction than in other sectors. Viewing averages for 1953–73 as a whole, unemployment was 10.6 percent in contract construction, compared with 5.3 percent in manufacturing, and 4.9 percent in the total economy. In 1973 alone, unemployment was 8.9 percent in contract construction, compared with 4.4 percent in manufacturing, and 4.9 percent in the total economy. The uniquely high unemployment in contract construction explained also a substantial part of the unemployment in other areas, because the deficient rate of housing starts had adverse effects upon the demand for all those types of products which enter the home, and upon the construction of those neighboring facilities which serve the home (see chart 18).

The housing scarcity contributes powerfully to scarcities throughout the economy

Measured in 1970 dollars, the construction deficiency during the period 1953–72 is estimated at $214.9 billion. Viewing the ramifying effects of this deficiency, it is estimated that it accounted for a loss in total national production of $429.8 billion. The construction deficiency thus entailed a Federal revenue loss of $86.9 billion, and a State and local property tax loss of $16.5 billion. The resultant loss of man-years of employment was 9.9 million.

The final step in this exercise is to project the consequences during 1973–80, without drastic changes in national economic and social policies. For the period as a whole, the deficit in residential and related commercial construction is estimated at $75.2 billion. The attributable loss is $150.4 billion for total national production, $30.1 billion for Federal revenues, and $3.9 billion for State and local property taxes. The resultant man-years of work lost is 2.6 million (see chart 19).

By comparing the foregoing with the overall deficiencies depicted on an earlier chart, one can easily discern the profound significance of the maltreatment of housing.

9. *Comments on the "Energy Crisis"*

In part I, I suggested the inadequacy of the CEA discussion of the energy problem. I now offer my own analysis.

The "energy crisis" exists on a very wide front

The "energy crisis," and its serious impact upon our entire economy, merit much more explanation than has thus far been forthcoming. The Middle East difficulty does not nearly account for the size of this "crisis." Our oil imports attributable to that region, in ratio to our total oil supply, are large. But they are not large enough to be fraught with so much damage, if we ourselves had not committed so many errors on so many fronts for so many years. In addition to factors cited below, we could have had enough reserve oil capacity, if we had looked ahead and planned, to reduce the consequences to us of troubles in the Middle East, or elsewhere, which were not unimaginable even though not clearly predictable.

This is a proper moment to note that growing and then serious energy shortages, in areas other than oil, were highly visible for a number of years before 1973. Due to insufficiencies of plant and other facilities, there were electricity shortages, and dimouts and blackouts in some important areas. In the case of natural gas, there were actual and growing inadequacies of plant and pipelines—generally ignored, and partly "concealed" by the deficient level of performance and demand in the economy at large—for a long period before the critical shortage of gas as a commodity set in and was recognized. Today, efforts to increase the availability of natural gas, through imports and domestic exploration, are restrained considerably by the awareness of limited plant and pipelines; and even such commodity increases as are actually achieved will accentuate the inadequacy of plant and pipelines.

Such are the bitter fruits of the prevalent approach, and it is highly indicative that these other manifestations of the energy shortages have been relegated to the rear as the oil "crisis" has emerged.

Long-term shortcomings in the public utility regulatory process: too little capital, too high money costs, and erroneous price policy

During many years of appearances before Federal and other regulatory commissions, I have challenged the prevalent policies and decisions which have not looked ahead to growing nationwide energy requirements, have not responded to the need for a U.S. economy growing stably and at an optimum rate—toward which energy itself is a vital contributing factor—and have pursued the practice of too little and too late. The traditional regulatory approach has been to allow a utility the rate of return needed to cover the cost of capital actually used. But the capital actually used has fallen far short of the amounts essential to serve the growing needs of a growing nation. And this nondynamic approach is more the fault of the public regulatory bodies than of the utilities themselves, for adequate expansion of energy supply is a matter of nationwide concern, and requires concerted action beyond the scope of individual utilities in their own future planning.

More specifically, the regulatory commissions have not protested, or done so only in muted tones, against the scarcity ravages of the prevalent monetary policy. For example, among the major electrical utilities, the embedded cost of debt capital—the average cost on outstanding long-term debt—rose from 3.13 percent in 1953 to 5.47 percent in 1971—later comprehensive data not available—with very much higher interest costs on current borrowings. The excess interest costs, during the period cited, cost the electric utilities $4.037 billion, and the end is not yet (see chart 20).

This money-cost extravaganza has hurt the utilities more than any other major industry except housing. This is because the ratio of long-term debt to total capitalization is almost twice as high among the utilities as in manufacturing, and almost three times as high as in motor vehicles and equipment. And the excessive costs of debt capital have also entailed excessive costs of equity capital among the utilities.

The general price inflation has also worked with special severity among the utilities. From 1966 to 1972, consumer prices rose at an average annual rate of 2.9 percent, wholesale prices 1.9 percent, and industrial prices 1.8 percent. But the prices received by the utilities at large rose at an average annual rate of only 1.7 percent. These utility price disparities, that with the Consumer Price Index being by far the most significant, have also appeared in later years. The price lag among the utilities has not been compensated for by a relatively higher rate of technology progress. This is indicated by the profit trends among the utilities, as set forth below.

The above-described price policy among the regulatory commissions is not beneficial to the consumer in the long run. For the shortages of utility capacities and services will average more utility price increases in the long run than would have resulted from a more farsighted regulatory policy. This is already becoming very apparent.

Deficient income, plant and equipment, and service among the utilities

The foregoing factors have conspired to produce adverse income trends among the utilities. Among the public utilities in general, the average annual growth rate in per unit revenues declined from 2.3 percent during 1953–60 to 1.7 percent during 1960–72. The average annual trends in income before taxes were down from 7.7 to 1.8 percent, and in income after taxes were down from 8.5 to 3.3 percent. These adverse trends are expressed in current dollars; in real dollars, the trends were much worse. This occurred despite a much higher real economic growth rate, and a much higher physical volume of utility sales, during the later period than during the earlier period (see chart 21).

In view of these adverse trends, the growth rate in utility investment in plant and equipment has declined. For the utilities generally, the average annual growth rate in real terms for such investment dropped from 13.7 percent during 1947–53 to only 4.5 percent during 1953–72. Even allowing for the extraordinarily high growth rate during the earlier period, due to restraint during World War II and other factors, the growth rate during recent years has been highly unsatisfactory. Some of the serious current shortages are proof of this (see chart 22).

Due to trends toward inadequate plant and equipment, the services offered by the utilities to industrial and household consumers has increasingly fallen short of the need, and even of the effective demand. Hence, voluntary programs to curtail use, in many parts of the country, for a number of years past. Among the utilities generally during 1947–53, the average annual increase in physical sales was 8.8 percent, while the average annual growth rate in real total national production was 4.9 percent. During 1970–72, when the figure for real total national production was only slightly lower at 4.6 percent, the figure for utility sales was greatly lower at 5.5 percent. The sharply declining ratio of the growth rate in utility sales to the growth rate in total national production cannot be viewed without deep concern (see chart 23).

The proper approach to growth in utility sales and capacity

What has just been said is valid, even though, in absolute terms, the growth rate in utility sales has been sustained at a higher rate than the growth in total national production. Because of new technologies, rising industrialization, and several other factors, the growth rate in utility sales should be increasingly higher in ratio to the growth rate in total national production. Further, as earlier indicated, the deficient growth rate in utility sales or service to the public has been partly "hidden" by the deficient performance of the economy at large.

Nor should utility capacities merely follow general economic trends. When the general economy is "down," it is neither in the interest of the overall economy nor in the interest of the users of utility services that utility investment should also slow down accordingly. Rather, it is wise that the growth in utility investment, geared to long-range needs, should exert a "countercyclical" effect.

To put the matter in a nutshell, the utility regulators have looked too much at the past, and have not nearly enough planned for the future in a long-range perspective.

Overcoming the "energy crisis" requires a much broader perspective, and a much wider range of national effort

But even the regulatory bodies deserve partial exoneration, because they have been impeded in their tasks, and also have taken their cure, from what the general national policymakers have been saying and doing. An adequate supply of energy is too vital to be the sole responsibility of the specialized regulatory commissions, or of private enterprise alone, where there is no regulation although maybe there should be, as in oil.

The "energy crisis" cannot enduringly be overcome by the measures now in being or under active consideration, for they are both inadequate in themselves and far too narrow in perspective. Immediate and drastic steps should be taken to reverse the tight monetary policy and exorbitantly high interest rates. Moreover, the Council of Economic Advisers, as part of its statutory duty—honored mainly in the breach—to set long-range goals for the overall economy and propose policies accordingly, should simultaneously have been doing and should now do the same thing for a sector of the economy as essential as energy, and for some others as well. If CEA had been doing this, instead of dribbling away with hackneyed, delimited, and unsuccessful "solutions," such as advocating more unemployment and more scarcities to "fight inflation," and had so advised the President, then he would not have slighted the energy problem for so long, and would not now be pressed to show so much dramatic interest in it—inadequate and improvised in the 11th hour.

And if the CEA had been doing its full job, the shortage of energy would not have had as adverse "psychological" effects, under conditions of general economic health, as it is having under conditions of economic stagnation and prospective recession. The scarcity economists should now change their ways; not seek to use the energy crisis as an excuse for many of the results of their own mistakes.

The priorities problem and the "energy crisis"

Much more attention to our great domestic priorities ranks very high on the list of about-faces now required in national economic policy. We could even conserve energy, and end the "crisis" sooner, by taking vigorous measures to allocate more of our resources and production efforts away from the gadgets and superfluities which we need least and which require relatively large amounts of energy to make them available, and toward those grossly neglected social services which we need so much and which require relatively less energy to make them available. Rationing of oil consumption among those using oil, while temporarily essential, would not be nearly enough. To be sure, such allocations would involve a sounder conception than we now employ, as to the real purpose of the Federal budget, including both spending and taxation.

What is recommended would represent an infinitely wiser national policy than the proposals to cut the use of energy by methods which would help the privileged and hurt the many—for example, indiscriminate price increases to "reduce demand," or the talked about imposition of nonprogressive taxes. Learning from bitter experience, it is now high time to much better.

10. Comments About the Agricultural Situation

I shall now reinforce in detail my criticism of the treatment of the agricultural problem in the 1974 CEA Report.

The "farm problem" has been, and still is, underconsumption, not overproduction

From 1953 forward, the economists in power developed the doctrine of farm "overproduction" and farm "surpluses." By 1973, it was forcefully brought home to the American people that we suffered from a shortage of food, and this pushed farm prices sharply upward for a while. But the people have not yet been informed that at no time since 1953 has there really been general overproduction of food. All along, there have been shortages in ratio to total needs, as will be discussed in this chapter. Similarly, there have never been substantial farm commodity surpluses in the overall—even when measured against actual demand as distinguished from total needs—although it is true at times that poor adjustments in the composition of farm output have temporarily caused some excessive surpluses of some farm commodities. The right course would have been to alter the composition of farm products, not to repress the total.

In general, the real trouble has not been overproduction of farm products, but rather underconsumption. This underconsumption has stemmed from the maldistribution of income and the insufficiency of total consumer income, which have been detailed earlier in this study. A year or so ago, the scarcity economists rubbed their eyes in bewilderment, when it was revealed for the *nth* time that millions of American families of low income were still suffering from malnutrition; and there are far too many in a somewhat higher income group who do not enjoy a sufficiently varied and attractive diet. The same comments apply substantially to fiber consumption for clothing In addition, our industries would use far more farm products, under conditions of sustained reasonably full production and employment. More exports of farm products are also desirable and attainable

The brutal deflation of the farm population, and its impact upon adequate growth in farm output

Based upon the erroneous thesis of excessive farm output and excessive farm surpluses, the economists in power during the past two decades have sought to solve an imagined problem by the brutal deflation of the farm population through the brutal repression of farm income growth. While our total population grew from 160,184,000 in 1953 to 208,837,000 in 1972, the farm population shrank from 19,-874,000 to 9,500,000, or from 12.5 to 4.5 percent of the total population. A considerable part of this shrinkage was sound and in accord with longer term trends. This is because farm productivity or output per man-hour has generally increased rapidly enough to enable farmers to perform their service to the Nation with a constantly declining labor force in ratio to the total labor force. But a very large part of the shrinkage was highly undesirable, and was not consistent with adequate farm output.

Farm acreage for crops harvested declined from 348 million in 1953 to 298 million in 1972. This drop of 14.5 percent was much too large.

Due to farm productivity advances, total farm output grew 42.8 percent in real terms from 1953 to 1972. Meanwhile, total national production grew 91.3 percent in real terms. A large part of this growth disparity was entirely appropriate. As incomes and living standards rise, and as industrialization and technology advance, it is to be expected that farm output shrink in ratio to total national output. But a large part of the disparity has been due to trends toward a level of farm output far below our needs.

The brutual repression of farm income growth

The instrument used for the brutual deflation of the farm population has been income-growth repression. This has occurred mainly through defaults in a national farm policy intended to protect the farmer against the fact that his prices are determined by the "law of supply and demand," while most other prices are "administered" by business managers who can protect themselves.

The total personal income of the farm population from all sources rose from $19.8 billion in 1953 to $33.2 billion in 1972, a gain of 67.7 percent. But a large part of this increase was due to income received by farmers from sources other than farming. Over the same period of time, personal income from farm sources rose only from $13.4 to $17.7 billion, a gain of 30.1 percent. These measurements are in current dollars. Measured in constant dollars, farm income from farm sources declined very greatly. Meanwhile, again measured in current dollars, total personal income in the United rose from $288.2 to $935.8 billion, a gain of 224.7 percent. The predominant cause of this tremendous disparity in the trends was the huge decline in the ratio of the farm population to the total population, some of which was proper and some of which was improper, as earlier indicated. But much of it was due to the repression of farm income growth, even with regard to the actual farm population.

Because of the huge change in the population ratios, it is more illuminating in some ways to use per capita income figure. In 1972, the per capita personal income of the total farm population derived from all sources was $3,495, and that derived from farm sources was only $1,842. In 1972 also, the per captia personal income in the United States at large was $4,481, and among the nonfarm population was obviously higher. It should be noted, in this connection, that there are, on the average, more workers per farm family than per nonfarm family.

The immense disparity of income suffered by farm people is even more unjust, in view of their productivity record. From 1953 to 1972, productivity or output per man-hour on the farm increased about 200 percent. In the private nonfarm economy, it increased only 62.7 percent.

The discriminatory treatment of farm income is accompanied by discrimination in other respects. The public services made available to farm families, and to other rural families, are very much below those made available elsewhere. This is partly because local and State services are adversely affected by the low revenues in consequence of low incomes, and very largely because the Federal Government has not adopted adequate "equalization" programs to give relatively greater help to the less fortunate areas of the country.

Price parity for farmers, a goal without realization

The concept of the farm price parity ratio was originally designed, through basic legislation, to prevent farmers from being much worse off than others because of the fact that their prices are determined in a "free market" over which they had no control, while the prices for most other commodities and services are fixed by those who offer them to the public. In essence, price parity, as farmers like others live by their incomes, not by their prices. Thus, a price parity ratio of 100 was regarded as that relationship between the prices received by farmers and the prices paid by farmers which would represent rough equalization of price treatment, and therefore of income treatment. The so-called Government price support program was conceived to achieve this parity, by the "support" acquisition of farm commodities.

Due to the passage of time during which the price parity ratio concept was not properly adjusted to various economic changes, even 100 percent price parity (when achieved) has come nowhere near to approximating income parity for farmers. Even beyond this, nothing like 100 percent price parity has been maintained. The price parity ratio dropped from 93 in 1953 to 79 in 1972. It is true that the ratio rose to 107 on August 15, 1973, in the face of acute shortages, but it was down to 95 on February 15, 1975. Far more significantly, the price parity ratio averaged only about 82 during 1953–73 inclusive.

Farm prices and prices at the consumer level

The prices received by farmers are not to be confused with the prices paid for food by consumers at the retail level. Over the years, there has been a great widening of the "farm-to-market spread" between what the farmer receives and what the consumer pays. Some of this has been due to improved packaging, processing, and marketing services, and so forth. But a considerable part has been due to excessive price increases in the "administered" areas, more at the intermediate level than at the ultimate retail level. Retail "margins" are competitive and very small.

Even so, the consumer, over the year, has made a very good bargain in the purchase of food, and some part of this bargain has been unjust to the farmer. Today, the portion of the American family's spending for food is much lower in ratio to its total spending than it was years ago, although this is not as true of low-income families as for those higher up in the structure. Finally in this connection, as we have very recently learned, the prices paid by the consumer would be lower, if not for the contrived and unwise food shortages in consequence of the prevalent economics.

We now have a situation where relatively few nonfarm families in the United States are poor unless the breadwinner is unemployed, or unless they are senior citizens whose insurance or other payments are inadequate. But an unusually large part of the farm population remains poor even while working hard. Scarcity economics has hit farm people harder than others.

How injustice to the farmer has hurt the economy and the people at large

Apart from the economic and social injustice of mistreatment of the farm population by economists in power, the adverse impact upon the economy and the people at large has been very serious. Agriculture and the Public Interest, prepared by me and issued in February 1965 by the Conference on Economic Progress, made findings which have remained pertinent during the more recent years, with some variations. During the years immediately preceding 1965, the farm income deficiency accounted for about one-fifth of the deficiency in total personal income which explained so largely the deficiencies in economic growth, total production, and total employment. The deficiency in farm investment accounted for much more than one-fifth of the deficiency in gross private domestic investment. Viewing these two factors and others, the farm deficiency accounted for from one-fifth to one-fourth of the deficiencies in total national production.

Beginning with 1953, the economists in power told us that the millions of farm families driven off the farms by the repressive treatment of farm income, and by cutbacks in farm acreage, would find a happy haven of jobs and opportunity in urban areas. It is amazing that this prospect should have been offered. For it was apparent throughout that job opportunity in private industry was declining, and that the expansion of jobs in the services and in Government was not increasing sufficiently to counteract the industrial trends in full.

In consequence, a tragically large portion of the farm families driven into urban areas have entered the ranks of the unemployed and the lists of those on welfare. At least one-third, and perhaps much closer to one-half, of the total excessive unemployment in urban areas has been due to the "happy" migration of farm families to the cities. If there had been adequate farm production program in accord with our true needs, a substantial portion of these uprooted farm families could have been usefully and rewardingly employed on the farm. Further, it would have been better and less costly for everyone, if most of those who could not have been employed on the farm had been benefited by programs designed to find other useful employment for them in the areas where they originated.

Scarcity versus abundance in farm production

Let us now return to the subject of farm production scarcity versus farm production abundance. The 1965 Conference on Economic Progress study, referred to above, exploded the false thesis of the excessive farm "surpluses." It pointed out that, as of 1964, the true level of unemployment was 8.3 percent of the civilian labor force. The total national production deficiency was 11.8 percent. Steel capacity was 21 percent idle, and automobile plants 13.7 percent idle. In the same year, the portion of current farm output not currently consumed was only 0.6 percent. And 1964 was not an atypical year, in terms of such comparisons. It is thus clear that the surpluses in other sectors of the economy have enormously exceeded the "horrendous farm surpluses." Indeed, we have usually not had an adequate reserve of farm products, quite apart from lacking enough output to meet real domestic needs fully and well, and to export adequately.

As earlier stated, a large part of the brutal deflation of the farm population, and the brutal repression of farm income, has been due to underconsumption. The 1965 study referred to above made these findings, as to 1964: Measured in 1963 dollars, the deficiency in total U.S. private consumer expenditures was $395 billion. Consistently, the deficiency in food outlays, measured in terms of a satisfactory diet for all American families, was $124 billion, and the deficiency in consumer outlays for clothing and shoes was $40 billion. And these two deficiencies, in themselves, reduced total farm income by $55 billion, and net farmers' operating income by $25 billion.

The need for long-range and integrated planning

The corrective measures needed over the years, and needed now, call for a considerable degree of long-range planning in the development of national farm policy. The economists on the Council of Economic Advisers may assert the claim that they have had very little to do with such policy. But they should have. Their practical neglect of this problem is but one illustration of their improperly limited range of concern. Confining themselves predominantly to fiscal and monetary matters (and not dealing appropriately with these), they have blatantly neglected many other equally important aspects of national economic and social policy. In fact, one of the very reasons why they have fallen so far short in what they attempted is that all basic national economic and related social policies should be coordinated and integrated in an overall perspective. The failure to do so is not in accord with the mandate of the Employment Act of 1946.

Some parts of this failure are almost inexplicable. How could those on the Council of Economic Advisers, immediately concerned with the unemployment problem, have overlooked the dire unemployment consequences of the brutal transfer of so large a part of the farm population to urban areas? The "farm problem" is really an American economic problem.

Based upon the economy of abundance, we need a totally new approach to the "farm problem," which can be attempted only in the context of a totally new approach to the entire U.S. economic and social problem.

11. *Comments on Transportation*

It is highly significant that the 1974 CEA Report does not stress the high importance of the transportation problem. For this reason, I now offer my comments.

The long-enduring shortage of railroad transportation

After the recognition of the "energy crisis" in 1973, it dawned upon many that railroad services were in short supply. And if they had been in adequate supply, it would have been feasible to shift a great deal of traffic carriage to a form of transportation which is relatively economical in terms of fuel. But it was not nearly enough to recognize in 1973 that railroad service was in short supply, because it takes a long time to expand these services substantially.

The railroad shortage, moreover, has been of very long duration. It has been aggravated by the intrustion of scarcity economics into the thought and action of the regulation of the railroads by public process. It has been further aggravated by the tendency to pay more attention to the desires of the more fortunate than to the needs of the less fortunate.

Those in the lower income brackets would be much better off with adequate mass transportation between where they live and where they work. But those in relatively higher income brackets have preferred to clog the roads with automobiles, although by now it is highly doubtful that this has made even them better off than if they had used mass transportation facilities. An important factor in all this has been the dedication of relatively excessive resources to the construction of beautiful and encircling throughways around cities, and from the cities to the suburbs. This has "convenienced" those who can afford to live in the suburbs and commute to work in the central cities; it has been detrimental to the lower income people in the central cities who have seen the public services they most need progressively starved by overspending on these magnificent throughways.

The record before the Penn-Central merger

By far the most telling and dramatic example of the application of the scarcity economics to the rail transportation problem has been the farrago involved in the merger of the Pennsylvania and New York Central Railroads, and the sorry aftermath of this merger. Because of its highly illustrative nature, an account of this merger, the largest in U.S. business history and maybe the most unwise, is set forth in this chapter. I am perhaps in an unusually good position to offer this account because, for more than 5 years, as an economist before the Interstate Commerce Commission and as a lawyer before the Supreme Court of the United States, I opposed the Penn-Central merger.

During 1953–61, the average annual real economic growth rate of the U.S. economy was at the extremely low level of 2.4 percent. In portions of the areas served directly by Penn and Central (indirectly, they served the entire Nation through various linkages), the growth rate was even lower, notably in parts of New England and Pennsylvania. Penn and Central responded to this by slashing their locomotive tractive power, freight car carrying capacity, and employment in ranges of 24 to 26 percent. This rendered them incapable of carrying even the volume of traffic which would have been available to them if their capacities had been larger. They attained this situation by the approach of deliberately avoiding what they considered to be the less profitable forms of traffic, especially passenger traffic, and concentrating more and more upon what they considered to be the more profitable types of traffic. In addition, instead of trying to increase their volume by becoming more price competitive with other modes of traffic, their prices in 1961 were 37.6 percent higher than in 1947.

Even if the application of these two aspects of scarcity economics had been beneficial to Penn and Central, it was very detrimental to the services offered by the two roads, and to the public served. Many communities were deprived of railroad service entirely. Passenger traffic, and "commuter" traffic above all, were affected most seriously. And these trends were intolerable because, in terms of the applicable legislation and commonsense, the primary obligation of the railroads is to serve the public. If they run into financial difficulties in so doing, those financial measures should be adopted which enable them to continue to serve. But the irony of the matter was that the scarcity policy of Penn and Central greatly aggravated their financial difficulties. Their after-tax incomes trended downward during 1953–61, and reached a deficit of $9 million in 1961.

The processing of the Penn-Central merger

These adverse trends in income led to ever-increasing agitation by these two railroads, and by other parties, to the effect that the two roads were approaching "bankruptcy," and that only a merger could save them and thus be helpful to the public. There was almost no effective voice speaking in the public interest, in opposition to this agitation. Thus, very early in the 1960's, the Penn-Central merger proposal came before the Interstate Commerce Commission.

The essence of this merger proposal was just what might have been expected under the circumstances. The two railroads offered the ICC examiners, hearing the case, a projection that the average annual U.S. real economic growth would be only 3 percent during 1961–70. They forecast that revenue ton-miles carried by the two roads would decline from the 1961 level by 6.5 percent by 1965, and by 9.2 percent by 1970. They forecast that, in the absence of substantial reductions in cost to be achieved through further slashing in facilities and services, their after-tax incomes would decline further from the deficit level in 1961. They therefore proposed that the central feature of the merger would be the "saving" of an estimated $80 million, largely through further drastic slashes in facilities and services.

The Interstate Commerce Commission examiners, when they issued their opinions approving the merger in the mid-1960's, did not even fulfill their statutory obligation to make an independent and objective examination of rail service requirements. Instead, they accepted and incorporated into their opinions, lock, stock, and barrel, the projections made by Penn and Central. Their subservience to the thinking of the two railroads was complete.

When, in 1966, the Interstate Commerce Commission itself approved the action of the Examiners, the actual course of events to that date had utterly discredited their findings. Revenue ton-miles carried by the two roads in 1965 were 22 percent above 1961, and those estimated for 1966 were 43 percent above the forecast for 1970. (My projection in 1961 for 1965, at the examiners' hearings, was less than 1 percent off the mark.) This was substantially due to the fact that the average annual real U.S. economic growth rate during 1961–65 was 5.4 percent, contrasted with the 3 percent forecast made by the two railroads and accepted by the examiners. (In 1970, actual revenue ton-miles carried by the two roads, despite an economic recession in that year, were 84 million, contrasted with the forecast of 64 million made by the two railroads and accepted by the examiners.) Instead of the further decline in income after taxes from the 1961 base, as forecast by the two railroads and accepted by the examiners, actual income after taxes was $75.5 million in 1965, and was estimated at $100 million in 1966.

Planning for economic calamity

Thus, the Interstate Commerce Commission, when it approved the merger in 1966, already knew that the forecasts made by the two railroads and accepted by the examiners were as wrong as rain in all respects. Nonetheless, the ICC took the position that developments from 1966 to 1970 might be so adverse as to justify on the average these forecasts for the period 1961–70. There was no basis whatsoever for this absurd position of the ICC.

In fact, the opponents of the merger pointed out to the ICC that this could happen only if the volume of revenue ton-miles carried declined by about 30 percent from 1966 to 1970, which was within the realm of probability only if the average annual U.S. real economic growth was less than 1 percent during these years. The opponents also pointed out that this could only happen if we suffered within 1966–70 an economic downturn roughly comparable to the Great Depression. The opponents of the merger also pointed out that, in any event, the ICC had no mandate nor justification for predicating estimates of needed railroad service upon so catastrophic an outlook, but instead was mandated by legislation and by commonsense to predicate needed railroad service in the future upon the assumption of at least a reasonably healthy economy. And still further, the opponents of the merger pointed out that predicating the needs of future railroad service upon such a catastrophic assumption would be in furtherance of such an event, because of the importance of railroad investment, employment, and services to the economy at large.

Action on the merger by the Supreme Court

The approval by the ICC of the Penn-Central merger came before the Supreme Court of the United States in the October term of 1966. The opponents of the merger presented to the Court the materials and developments set forth above. But these opponents were small and weak in number. The proponents of the merger were legion, and were strengthened by the continuing agitation, by all of the media, to the effect that the merger was imperative to avoid bankruptcy. The U.S. Department of Justice, which has opposed the merger in a 288-page brief before the ICC, vigorously supported it before the Supreme Court, with no revealed reason for the strange change, and, in fact, the two roads were much better off in 1966 than they had been when the Justice Department first decided to oppose the merger. Some of the earlier opponents of the merger were apparently "bought off" by the two railroads, or affected by changed "political" conditions. The merger was also supported by six other railroads appearing before the Supreme Court, apparently interested in the size of the "settlements" which the merger would make available to them, and also imbued with the philosophy of scarcity of railroad service.

Nonetheless, the Supreme Court at this stage, by a vote of 5 to 4, sent the merger back to the ICC for further review. Nothing that happened during this review corrected any of the earlier errors made by the Commission, nor indicated any reconstruction in its thought or approach. Yet, when the merger came back to the Supreme Court again, it was finally approved by a unanimous vote. The opinion of the Court was based in the main upon the proposition that the Court should not interfere with the judgment of the specialized regulatory bodies. But the very reason for Court review is to interfere with these judgments when the process of the regulatory body has been blatantly inadequate, and manifestly not in accord with statutory mandates such as those for adequacy of service. It may have been that the Court was distracted by the complex issues involved in appropriate adjustments for the other six railroads. It may even have been that some members of the Court were sincerely impressed by the almost universal agitation for the merger as the road to salvation. And some members of the Court may even have been imbued with aspects of the prevalent economics.

Developments subsequent to the merger

Not much needs to be said about what happened immediately after the merger. Facilities, jobs, and service continued to be slashed. The result was the bankruptcy predicted by the opponents of the merger if such practices received the stamp of Government sanction.

Then, the Federal district judge, appointed to oversee the bankruptcy, named a group of trustees to manage the bankruptcy. One of these was the president of a railroad which had made manifest somewhat the same railroad philosophy as the managers of Penn and Central. One of them was a former dean of the business school of a leading university, who for many years had been a frequent consultant to the railroad industry, and a defender of its views. One of them was the president of a great department store, whose presumptive knowledge of railroad problems was evidently derived from the toy department in his store. All in all, despite one significant exception, the trustees were singularly devoid of experience or records which indicated due knowledge of an attention to the dominant public interest.

As might have been expected, the trustees proceeded, with much help from Penn-Central, to put the stamp of approval upon those very aspects of scarcity economics which had done so much to bring on the trouble among the two roads prior to the bankruptcy. Facilities, jobs, and service were further slashed. But again, as had earlier been predicted by the opponents of the merger, this carried matters from bad to worse. And Penn-Central turned to the Government for rescue.

Even with this history and the lessons it should have taught, there seems to have been not much change in the approaches applied to date. The Congress has taken a greatly increased interest in the railroad problem, and various pieces of legislation have been approved or brought under active consideration. But in the main, these have continued to adhere to the theory that salvation will come through scarcity of rail services. And the President's proposals for rail relief is the most glaring example of the scarcity approach.

The default of general national economic policies

It is interesting to note, in these connections, that President Kennedy established a special group, including the Council of Economic Advisers, to study the Penn-Central merger proposal and the railroad merger problem in general, and to make a report accordingly. This report set forth some interesting, and for the most part valid, criteria for use in dealing with railroad mergers. But there is little or no evidence that the Government followed up on these, and, as earlier indicated, the Department of Justice, in the end, vigorously supported the Penn-Central merger. In general, the Council of Economic Advisers did not take an active interest in the Penn-Central merger nor in other railroad mergers, and later on it appeared to approve of, or at least to be acquiescent about, the Penn-Central merger. The ultimate viewpoint of the Council was that this problem was not really within the area of its knowledge and concern.

Nothing could be more fallacious than this viewpoint. There can be no sufficiently integrated and comprehensive national economic policy, unless the Council of Economic Advisers deals, quantitatively as well as qualitatively, with all major aspects of national economic and related social policies. This does not mean that the Council should become an overblown agency with an immense staff. It should certify specialized problems to the specialized agencies, and assign their detailed examination to the much larger staffs of such agencies. Indeed, without this, the specialized agencies have no adequate perspective, within which to design their research programs and their other activities.

12. Comments on National Defense

Although national defense outlays are noneconomic in purpose, the issue of national defense has been increasingly subjected to economic considerations. Hence, the following comments seem appropriate.

General principles for national defense outlays

In an economy where the brains and the will are available to maintain reasonably full employment and production, national defense outlays are neither necessary nor desirable for economic or social reasons. In fact, national defense outlays represent, in the main, a demand upon our resources without corresponding benefits of an economic or social nature. Nonetheless, it is obvious that huge national defense outlays are unavoidable in the kind of world in which we live today, and will live for the foreseeable future. This observation should not prevent us from striving constantly to help fashion the kind of world in which national defense outlays will no longer impose the burden which they do now, and will continue to impose in the near future.

Nor should this observation prevent us from striving, by all available means, for true economy in national defense. This requires constant reappraisals of the international situation. It requires vigilant reexamination of the relative effectiveness of and need for various types of forces and weaponry. The proposition that it is better to have too much than too little by way of national defense, like all sound propositions, should not be overdone.

But when all of this has been said, it is very difficult for the informed citizen, or for one in my position, to determine what the magnitudes of our national defense outlays should be at any given point in time. The informed citizen may, although not without considerable difficulty, formulate a reasoned opinion as to the international situation, which perhaps may be as sound as his reasoned opinion on the other matters discussed in this study. It is much more difficult for even the informed citizen to form a reasoned judgment as to desirable weaponry, and as to the size and composition of our defense forces. This is not to say that the informed citizen should not form and express views on this subject; that is a duty in a democracy. But it does mean that a high degree of responsibility and discretion in these matters must be allowed to the official experts in this field, and to the President and the Congress. After all, we do live in a representative democracy, even though these representatives are not always right. The citizen is not always right, either.

The current confusion and division regarding national defense

Having said this, it remains true that the prevalent economics has led the Nation and the citizen dangerously astray, with respect to the entire matter of national defense. It has done this by asserting that our national defense outlays have imposed an excessive and undesirable burden upon the economy, and contributed greatly to inflationary pressures. This can hardly be the truth, in view of the actual situation pertaining during the past two decades, as depicted earlier in my comments. The total demand upon our resources has been far short of our reasonably full capabilities, and the excessive inflation has been due to causes not based upon economic overstrain.

It is equally dangerous that the prevalent economics has led the Nation and the people to believe that the gross neglect of our great domestic priorities has been caused by, or made necessary by, excessive national defense outlays. This is incorrect, for the economic reasons stated above. It is also incorrect because the gross neglect of these great domestic priorities existed long before we got into Vietnam, and are persisting with a vengeance now that we have gotten out of Vietnam.

The "successful" effort to establish this kind of "competitive" relationship between national defense and the great domestic priorities has wrought incalculable damage. It has confused and misled a large portion of our young people. It has divided the Nation into two hostile camps, those not willing to give the great domestic priorities precedence over national defense, and those not willing to give national defense precedence over these great priorities. So long as this condition exists, we cannot achieve the degree of accord essential to many of our great purposes as a nation and a people.

The confusion about priorities

These immensely costly errors derive from a salient feature of the prevalent economists. Not only have they substituted the damaging philosophy of scarcity for the rewarding philosophy of abundance; in addition, this very process has led them to forget the very meaning of priorities, and thus not only to short-change the great domestic priorities, but also to assume a defective stance regarding adequate national defense outlays in their totality.

For the very meaning of priorities is that they should come first. Especially in an economy as powerful and productive as ours, there is room and to spare for the full vindication of these priorities, even if it were true that our resources were being so fully used that we could not do as much of everything as we ought to do. And, indeed, we can never do as much of everything as we would like to do.

Under conditions when the choice really is (1) to short-change either national defense and/or the great domestic priorities, or (2) to restrain the scores of billions of dollars of superfluous, expendable or postponable, and at times even deleterious production and consumption, we should unhesitatingly elect the second course, and not the first. We recognize the need for this in the presence of the current "energy crisis," although we are not dealing with it nearly as well as we should. But the prevalent economists have not recognized this with respect to national defense or the great domestic priorities. As to the latter, the main manifestations of the default have been set forth throughout this study.

Defense implications of the international situation

The current and foreseeable international situation calls insistently for revaluation of the prevalent thought and action regarding national defense. Day by day, we should strive for a just and lasting peace, everywhere. We should encourage a meaningful détente with the Soviet Union, and a rapprochement with China, as first steps in this direction. But the behavior pattern of the Soviet Union in the Middle East, and many other actions on its part, do not leave room for complacency, despite a tenuous détente.

These Soviet actions are carrying forward, with great vigor, the intent of the Soviet Union to gain effective control of the oil supply in the Middle East directly or indirectly; to gain dominant strength in various strategic waters, including the Mediterranean; and to make vulnerable the coast of China and outflank the western democracies. Even if the problem of the relationship between the Arabs and Israel did not exist, there is no reason to believe that these purposes of the Soviet Union would not proceed anyway. This entire process poses a great and increasing threat to the United States and its allies.

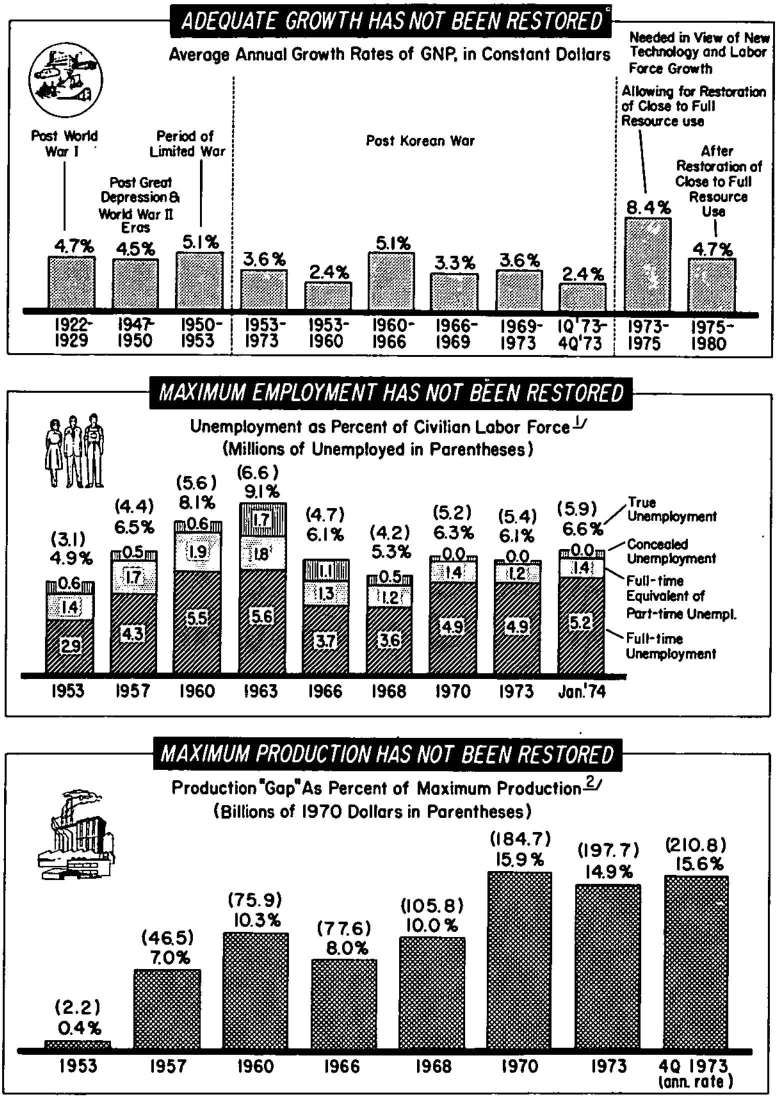
The Soviet Union respects and relies upon strength, and a less kind term would be brute force. This is perilous to us because, according to most of those in the best position to know, the Soviet Union is building its military forces, weapons, and technology at a pace which augers clear superiority over the United States within a period of time not long in the life of nations. The widespread theory that it makes no difference who is "stronger," on the ground that each of the two great powers has the ability to decimate or destroy the other, is of limited validity. Technologically, it is possible for one to reach the point where it alone can destroy the other. And in any event, it is entirely feasible for one to reach the point where it can bully and blackmail the other in limited strategic confrontations, even though each retains the good sense not to try to destroy the other.

Under these circumstances, while striving earnestly and by all means toward a meaningful détente, culminating in a true and lasting peace, it is essential that the United States make every effort meanwhile to maintain at least equality of military forces with the Soviet Union, or even better to maintain some superiority, and also to take account of the needs imposed by other aspects of the worldwide situation. It is correct that, in the long run, an "arms race" and nothing more is a hopeless concept leading toward final disaster. But the baby should not be thrown out with the bath water, and we should keep our guard high until we can safely relax. That time is not now.

[The charts referred to in the text follow:]

Chart I

BASIC U.S. ECONOMIC TRENDS, 1953-1973



1/ In deriving these percentages, the Civilian Labor Force is estimated as the officially reported Civilian Labor Force augmented by concealed unemployment. Thus, some of the percentage figures on full-time unemployment vary very slightly from the official reports, which do not take account of the augmented labor force. Full-time unemployment of 2.9% and true unemployment of 4.1% would be consistent with maximum employment. All data relate to persons 16 years of age and older. Components may not add to total, owing to rounding.

2/ Maximum production, 1973, equates with average annual growth rate of 4.4%, 1953-1973.

Basic Data: Dept. of Commerce; Dept. of Labor

Chart 2

COSTS OF DEFICIENT ECONOMIC GROWTH U.S. ECONOMY, 1953-1973

(Dollar items in billions of 1970 dollars, except average family income)

1953-1973 1/

Total National Production (GNP)	Man-years of Employment 2/	Personal Consumption Expenditures	Gov't Outlay for Goods and Services
1953-1973: $1,824.2 1969-1973: 922.0 4Q 1973: 210.8	1953-1973: 48.5 Million 1969-1973: 10.8 Million 4Q 1973: 1.8 Million	1953-1973: $841.1 1969-1973: 403.4 4Q 1973: 98.4	1953-1973: $471.1 1969-1973: 275.5 4Q 1973: 80.2
Private Business Investment (Incl. Net Foreign)	**Average Family Income (1970 Dollars)**	**Wages and Salaries**	**Unincorporated Business and Professional Income**
1953-1973: $512.0 1969-1973: 243.1 4Q 1973: 32.2	1953-1973: $16,349 1969-1973: 6,694 4Q 1973: 1,612	1953-1973: $1,034.3 1969-1973: 457.0 4Q 1973: 113.2	1953-1973: $154.5 1969-1973: 72.1 4Q 1973: 21.3

1973-1980 3/

Total National Production (GNP)	Man-years of Employment 2/	Personal Consumption Expenditures	Gov't Outlay for Goods and Services
1973-1980: $1,677.9 1980: 323.9	1973-1980: 16.5 Million 1980: 2.6 Million	1973-1980: $1,028.3 1980: 206.0	1973-1980: $238.4 1980: 43.4
Private Business Investment (Incl. Net Foreign)	**Average Family Income (1970 Dollars)**	**Wages and Salaries**	**Unincorporated Business and Professional Income**
1973-1980: $411.3 1980: 73.4	1973-1980: $13,570 1980: 2,588	1973-1980: $866.5 1980: 171.3	1973-1980: $97.6 1980: 17.3

1/ All deficits are calculated from a 1953 base, in that growth rates since then have averaged far too low. 4Q 1973 figures are at annual rates.

2/ Based upon true level of unemployment, including full-time unemployment, full-time equivalent of part-time unemployment, and concealed unemployment (nonparticipation in civilian labor force) due to scarcity of job opportunity.

3/ These deficits are projected from a 1972 base, writing off the cumulative deficits 1953-1972

Basic Data: Dept. of Commerce; Dept. of Labor

Chart 3

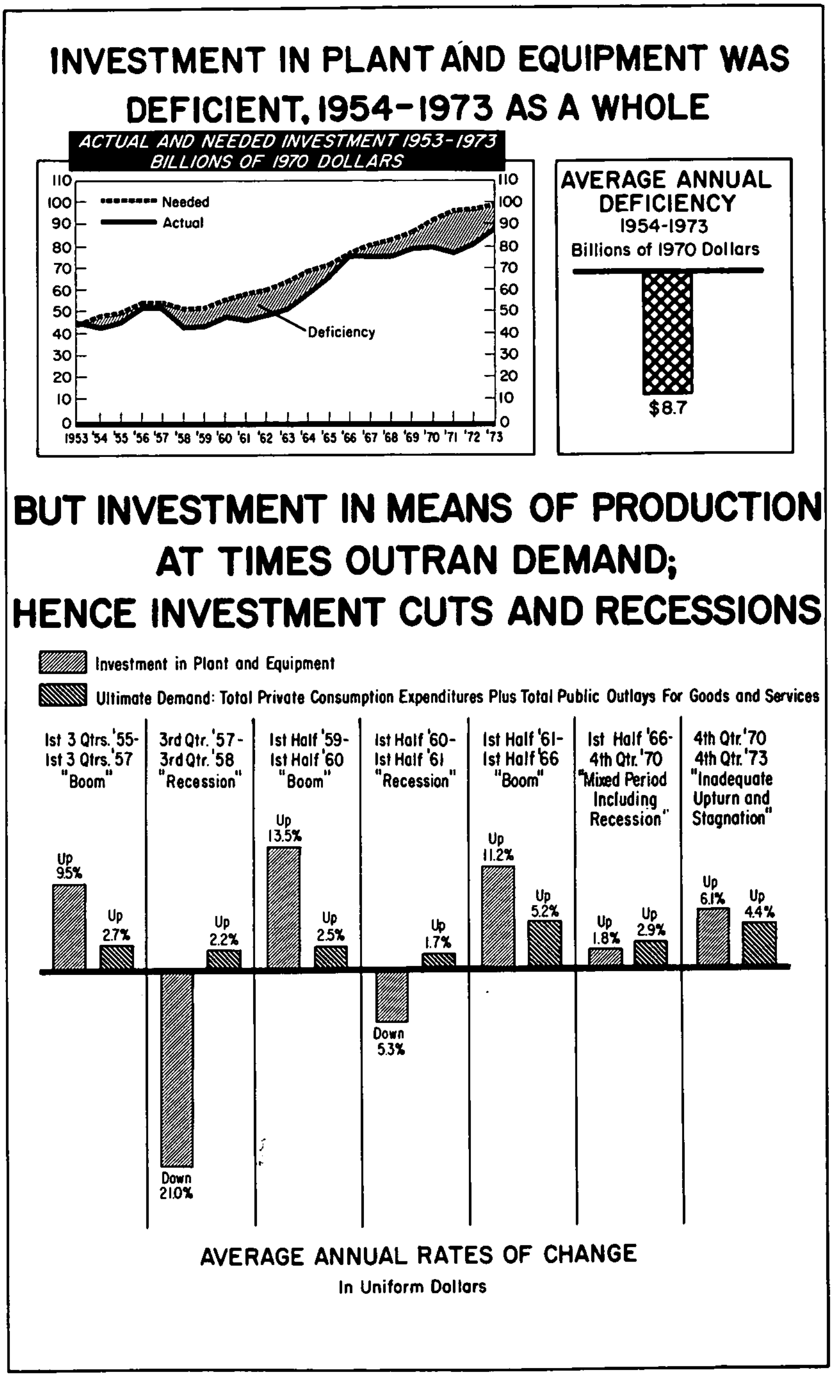
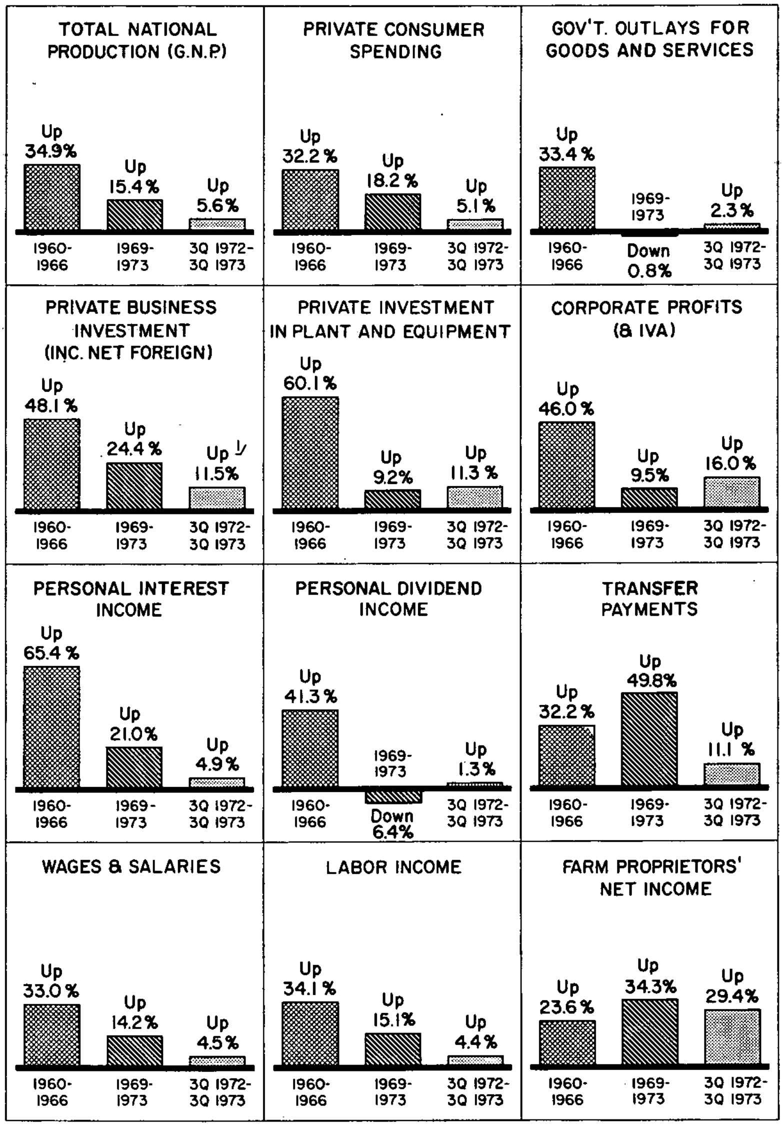

INVESTMENT IN PLANT AND EQUIPMENT WAS DEFICIENT, 1954-1973 AS A WHOLE
ACTUAL AND NEEDED INVESTMENT 1953-1973
BILLIONS OF 1970 DOLLARS
Needed
Actual
Deficiency
0 10 20 30 40 50 60 70 80 90 100 110
1953 '54 '55 '56 '57 '58 '59 '60 '61 '62 '63 '64 '65 '66 '67 '68 '69 '70 '71 '72 '73
AVERAGE ANNUAL DEFICIENCY
1954-1973
Billions of 1970 Dollars
$8.7
BUT INVESTMENT IN MEANS OF PRODUCTION AT TIMES OUTRAN DEMAND; HENCE INVESTMENT CUTS AND RECESSIONS
Investment in Plant and Equipment
Ultimate Demand: Total Private Consumption Expenditures Plus Total Public Outlays For Goods and Services
1st 3 Qtrs.'55-1st 3 Qtrs.'57 "Boom"
Up 9.5%
Up 2.7%
3rd Qtr.'57-3rd Qtr.'58 "Recession"
Down 21.0%
Up 2.2%
1st Half '59-1st Half '60 "Boom"
Up 13.5%
Up 2.5%
1st Half '60-1st Half '61 "Recession"
Down 5.3%
Up 1.7%
1st Half '61-1st Half '66 "Boom"
Up 11.2%
Up 5.2%
1st Half '66-4th Qtr.'70 "Mixed Period Including Recession"
Up 1.8%
Up 2.9%
4th Qtr.'70-4th Qtr.'73 "Inadequate Upturn and Stagnation"
Up 6.1%
Up 4.4%
AVERAGE ANNUAL RATES OF CHANGE
In Uniform Dollars

Chart 4

COMPARATIVE GROWTH, U.S. ECONOMY, 1960-1966 1969-1973, AND 3Q 1972-3Q 1973

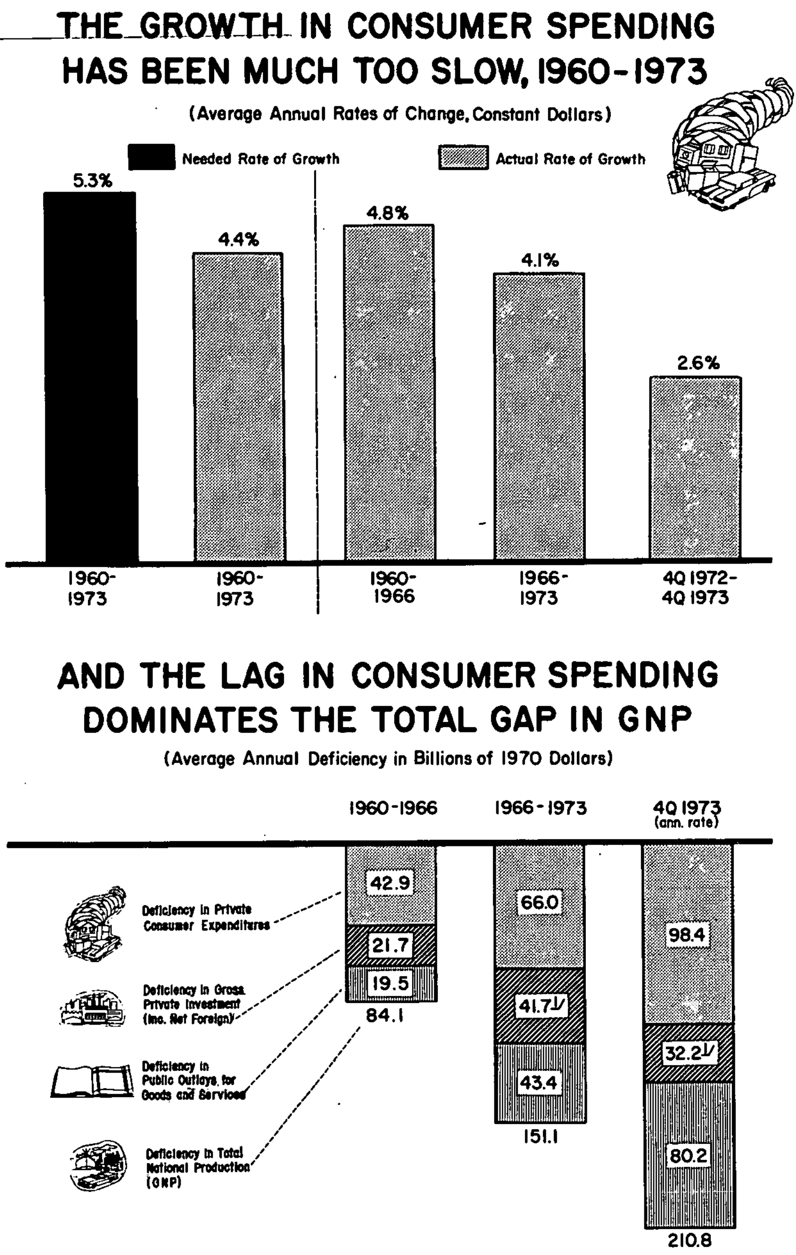
Total Percentage Changes, in Constant Dollars



1/ Excluding Net Foreign, 4.8%

Source: Dept. of Commerce, Bureau of Economic Analysis

Chart 5



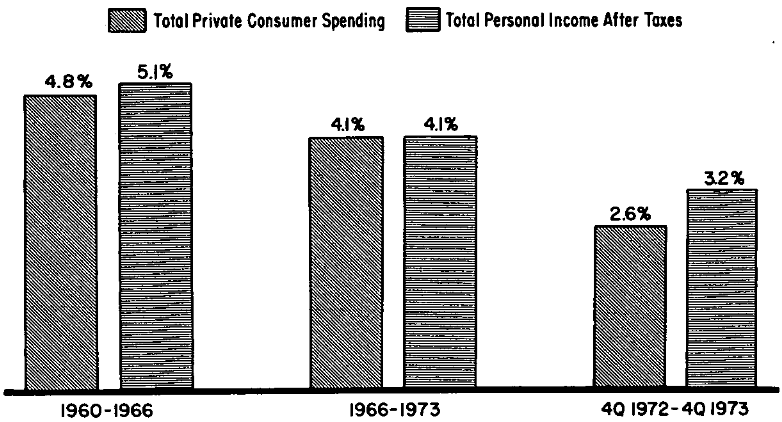
1/ More than half the investment deficiency in recent years has been due to inadequate residential construction.

Basic Data: Dept. of Commerce, Office of Business Economics

Chart 6

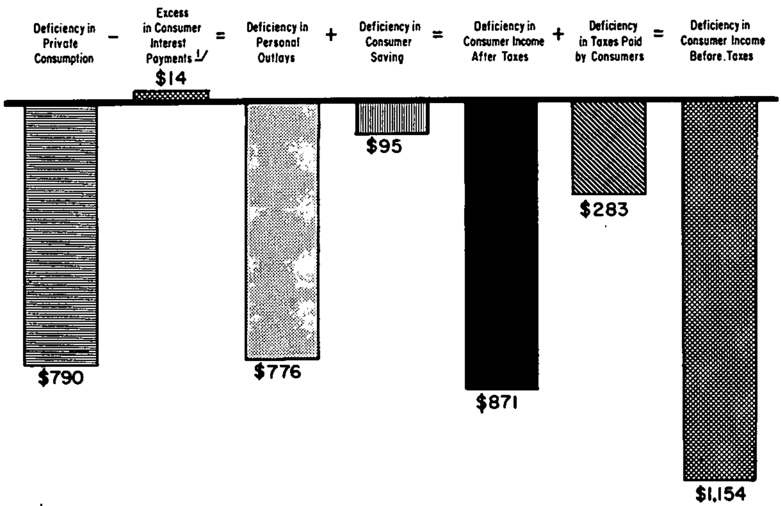
INADEQUATE CONSUMPTION GROWTH STEMS FROM INADEQUATE INCOME GROWTH

Average Annual Rates of Change in Constant Dollars



THE PRIVATE CONSUMPTION DEFICIENCY OF $790 BILLION, 1960-1973, REFLECTED A $1,154 BILLION INCOME DEFICIENCY

Billions of 1970 Dollars

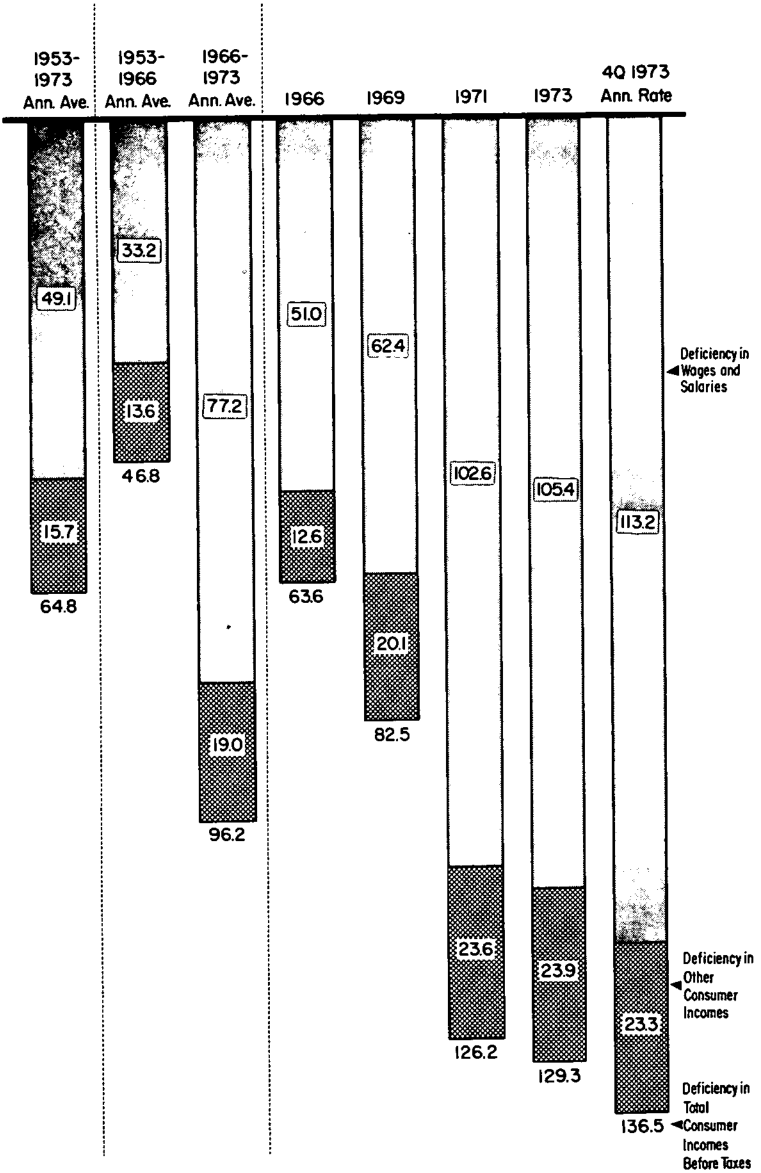


1/ Also includes personal transfer payments to foreigners, which is a minimal amount.

Chart 7

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

Billions of 1970 Dollars



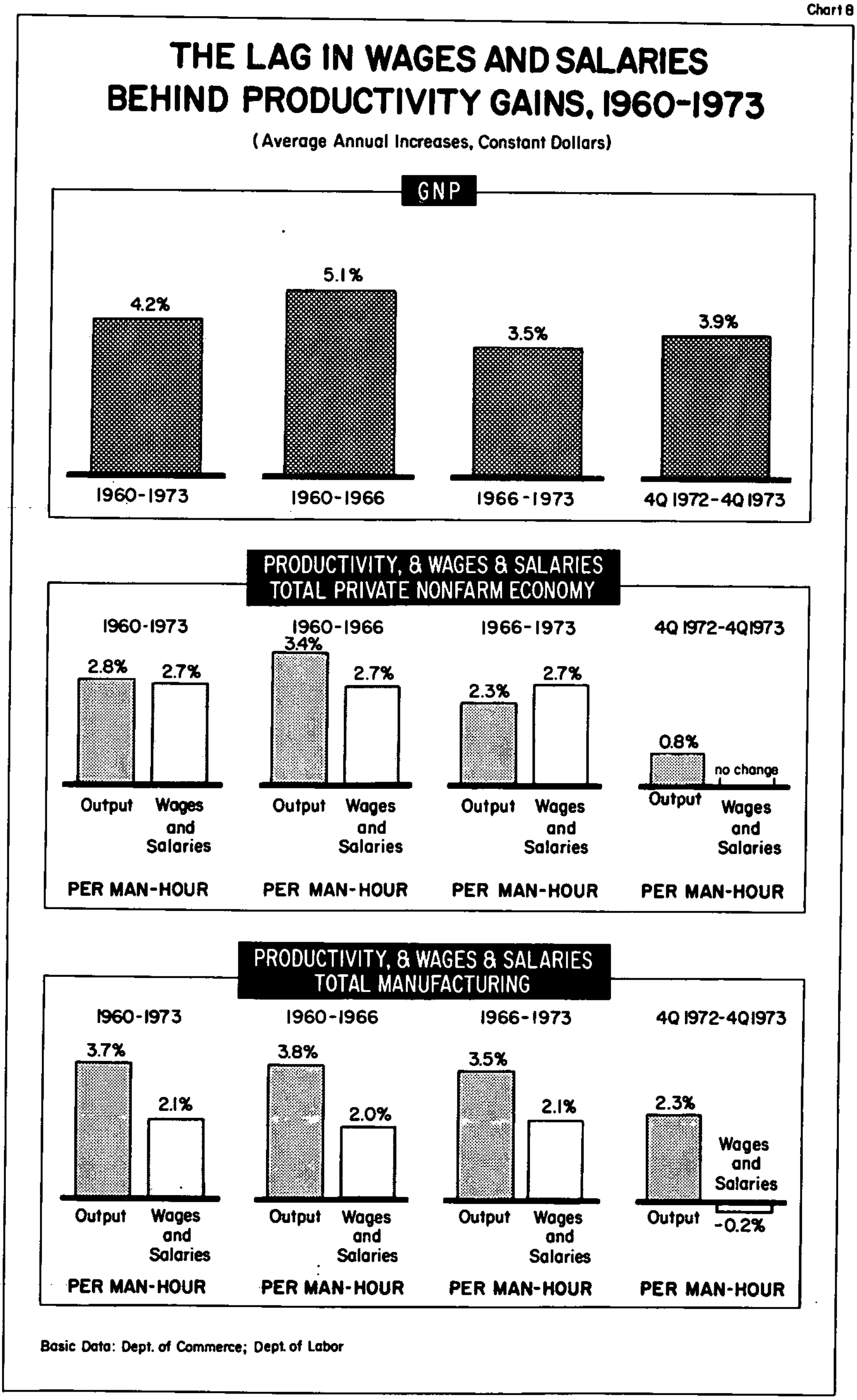
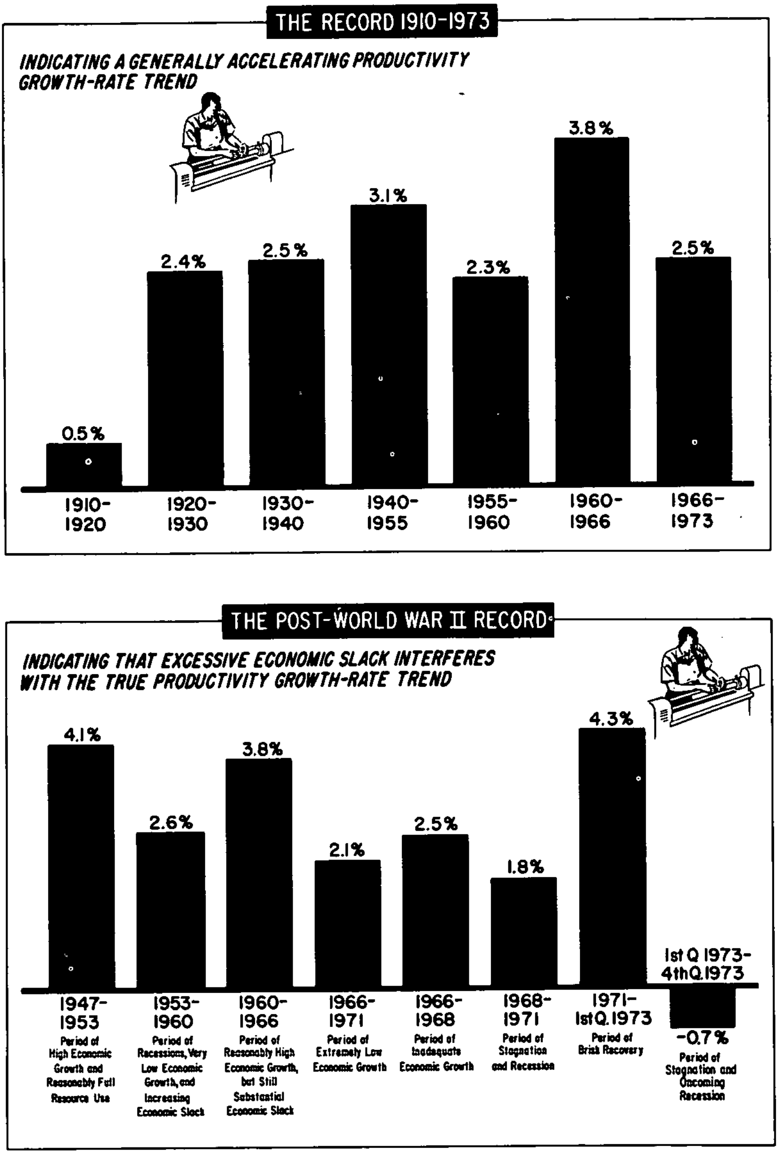


Chart 8
THE LAG IN WAGES AND SALARIES BEHIND PRODUCTIVITY GAINS, 1960-1973
(Average Annual Increases, Constant Dollars)
GNP
4.2%
5.1%
3.5%
3.9%
1960-1973
1960-1966
1966-1973
4Q 1972-4Q 1973
PRODUCTIVITY, & WAGES & SALARIES TOTAL PRIVATE NONFARM ECONOMY
1960-1973
1960-1966
1966-1973
4Q 1972-4Q 1973
2.8%
2.7%
3.4%
2.7%
2.3%
2.7%
0.8%
no change
Output
Wages and Salaries
PER MAN-HOUR
PRODUCTIVITY, & WAGES & SALARIES TOTAL MANUFACTURING
1960-1973
1960-1966
1966-1973
4Q 1972-4Q 1973
3.7%
2.1%
3.8%
2.0%
3.5%
2.1%
2.3%
-0.2%
Output
Wages and Salaries
PER MAN-HOUR
Basic Data: Dept. of Commerce; Dept. of Labor

Chart 9

LONG-TERM TRENDS IN PRODUCTIVITY U.S. PRIVATE ECONOMY, 1910-1973

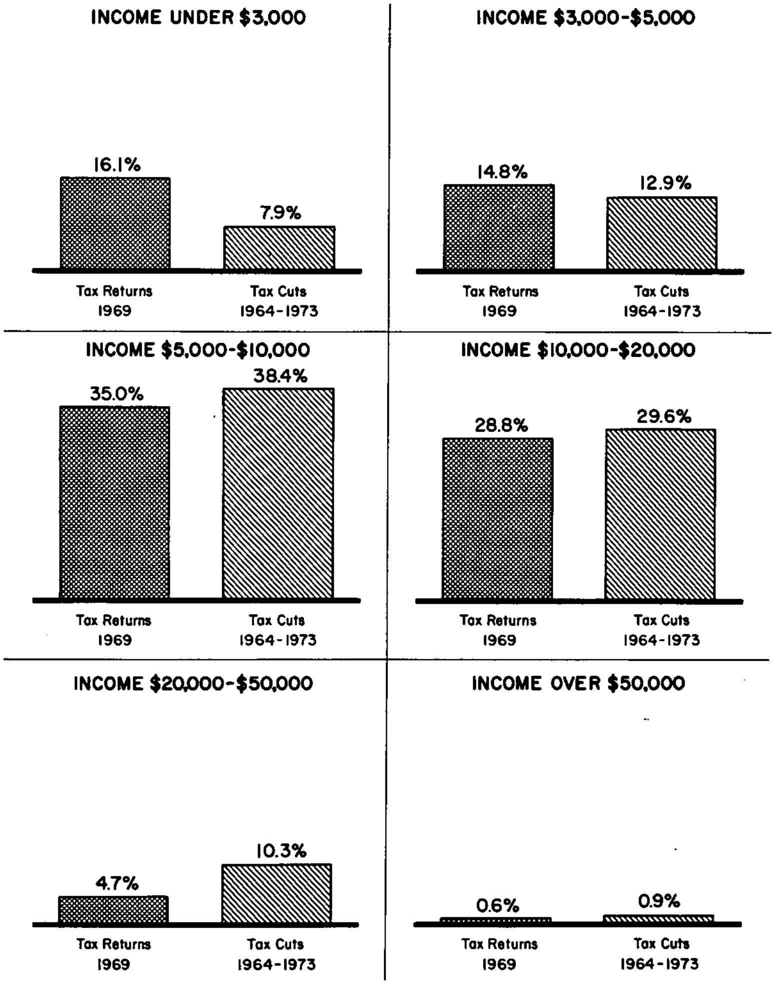
Average Annual Rate of Growth in Output per Man-hour for the Entire Private Economy



Source: Dept. of Labor estimates relating to man-hours worked (Establishment basis)

Chart 10

PERCENTAGE DISTRIBUTION OF TAX RETURNS, 1969 AND OF TAX CUTS, 1964-1973[1] AMONG VARIOUS INCOME GROUPS[2]



1/ Weighted average of percentage distributions of tax cuts in Revenue Act of 1964, Tax Reform Act of 1969, and Revenue Act of 1971 (H.R. 10947, as reported by the House-Senate Conference Committee). Weights are relative size of three tax cuts, each expressed as a percentage of total personal income: 1.92 percent for 1964, 0.99 percent for 1969, and 0.21 percent estimated for 1973.

Tax cuts in each bill are net permanent effect, ignoring any phase-ins and (in the 1971 Act) accelerations of previously scheduled tax reductions.

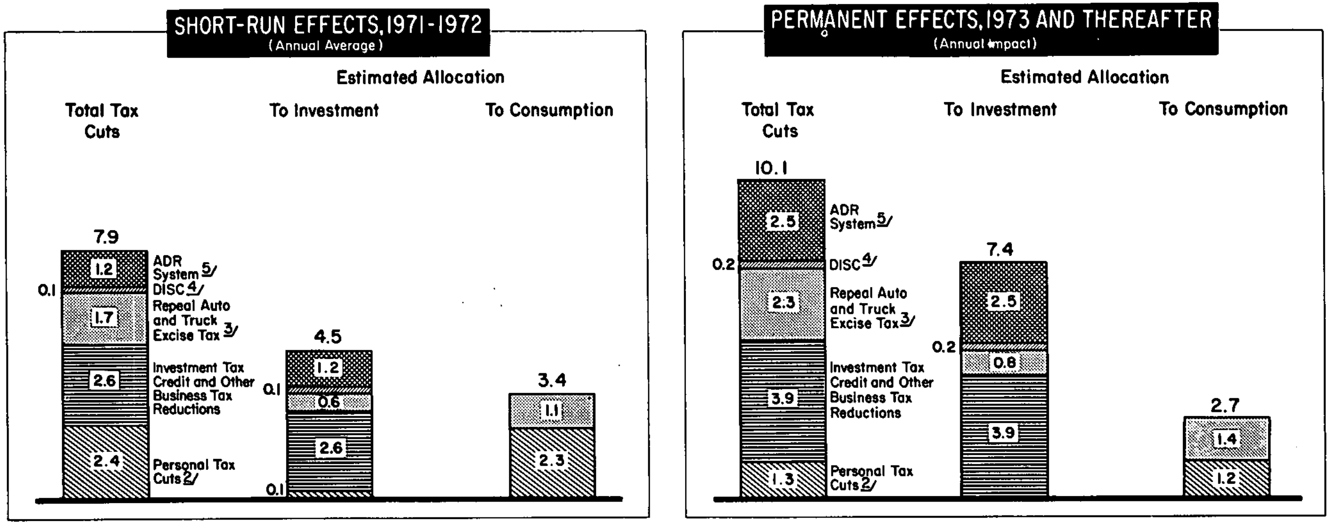
2/ Adjusted gross income classes.

Basic Data: House Ways and Means Committee and Senate Finance Committee Reports, and Congressional Record

Chart II

ALLOCATION OF 1971 TAX CUTS[1]: BETWEEN INVESTMENT AND CONSUMPTION

(Billions of Dollars)



1/ H.R. 10947, as reported by the House-Senate Conference Committee, and Asset Depreciation Range (ADR) System promulgated by the Treasury Department.

2/ Allocation to investment based on portion of cuts for those with income over $15,000, which they would save; remainder allocated to consumption.

3/ Allocation between investment and consumption based on business or nonbusiness use of vehicles.

4/ Tax deferral by Domestic International Sales Corporations (DISCs).

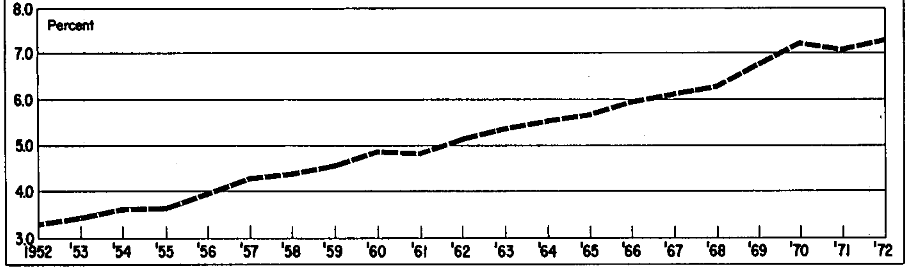
5/ Treasury regulations as modified by H.R. 10947 as reported by the conference committee.

Note: Components may not add exactly to totals, owing to rounding.

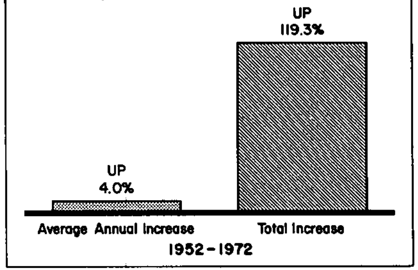
AVERAGE INTEREST RATES ON TOTAL PUBLIC AND PRIVATE DEBT, 1952-1972

Calendar Years

COMPUTED AVERAGE INTEREST RATE



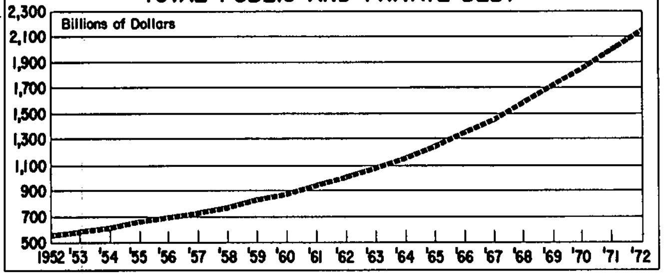
PERCENTAGE INCREASE



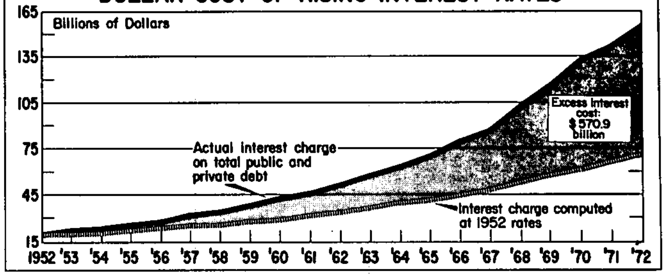
TOTAL PUBLIC AND PRIVATE COST OF RISING INTEREST RATES, 1953-1972

Calendar Years

TOTAL PUBLIC AND PRIVATE DEBT



DOLLAR COST OF RISING INTEREST RATES



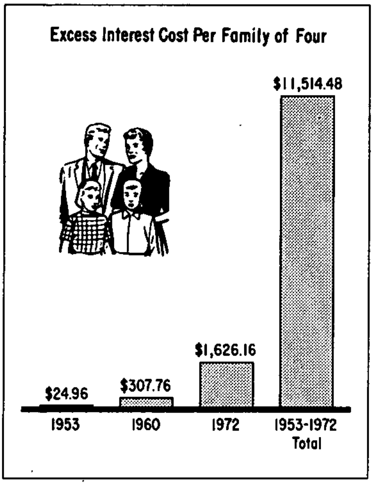
Source: Economic Report of the President, Dept. of Commerce

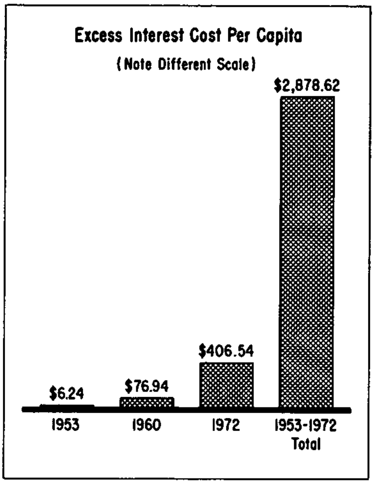
Chart 12

Chart 13

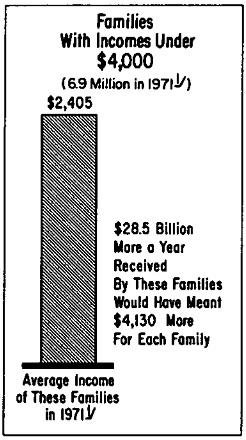
THE BURDEN OF $570.9 BILLION IN EXCESS INTEREST COSTS, 1953-1972 UPON THE AMERICAN PEOPLE

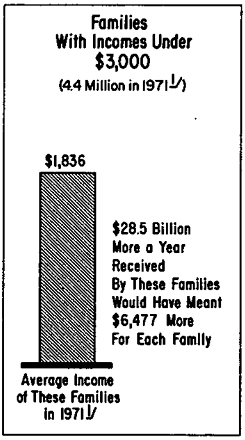
Calendar Years

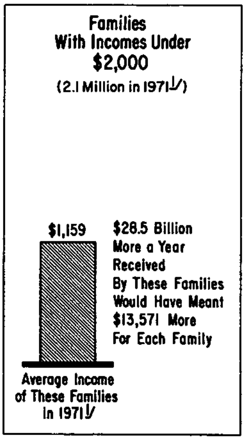




HOW $28.5 BILLION A YEAR, 1953 - 1972 - EQUAL TO ANNUAL EXCESS INTEREST - MIGHT HAVE RELIEVED POVERTY







1/ 1971 Latest Available

Source: Economic Report of the President, Dept. of Commerce, Bureau of the Census.

Chart 14

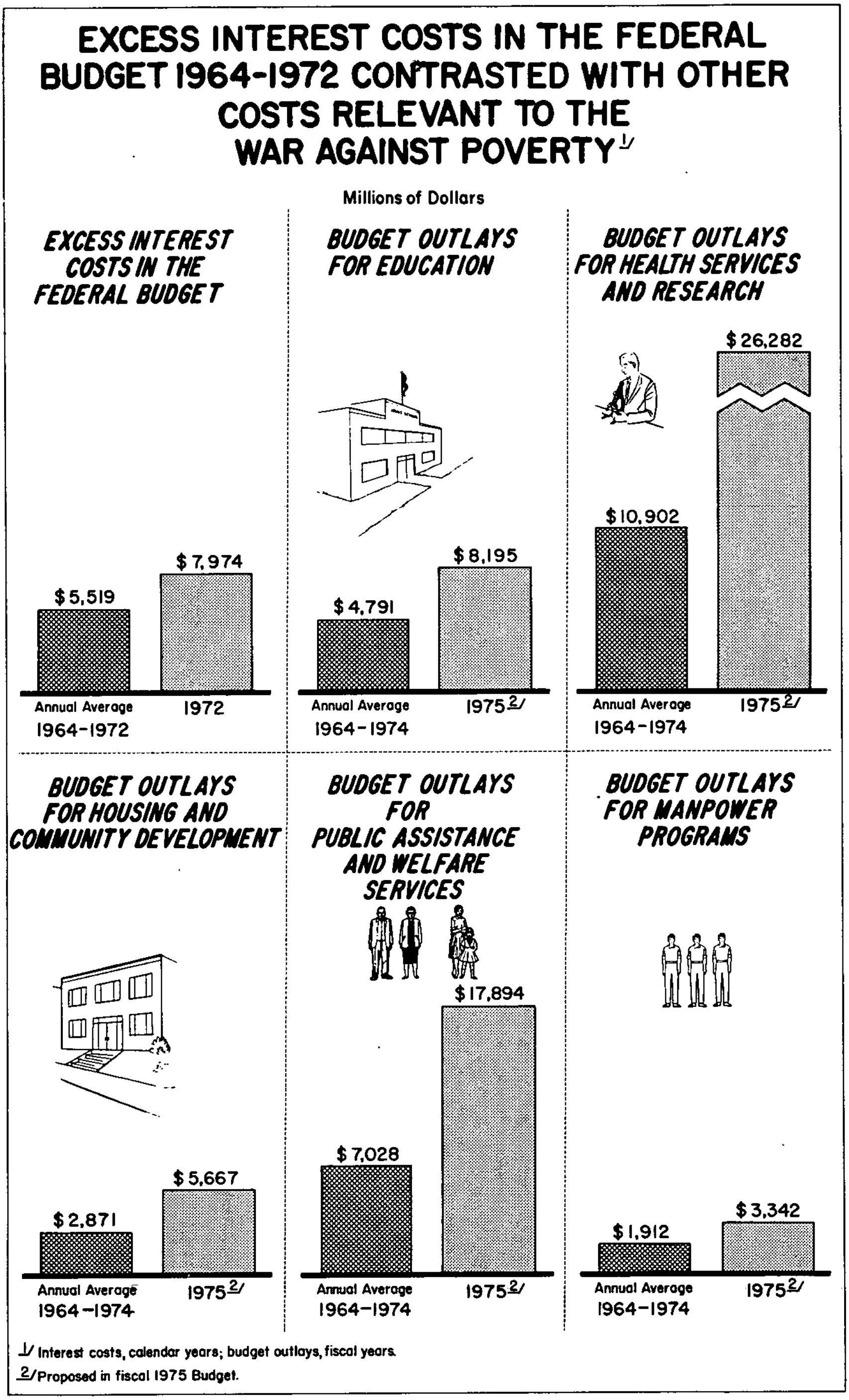
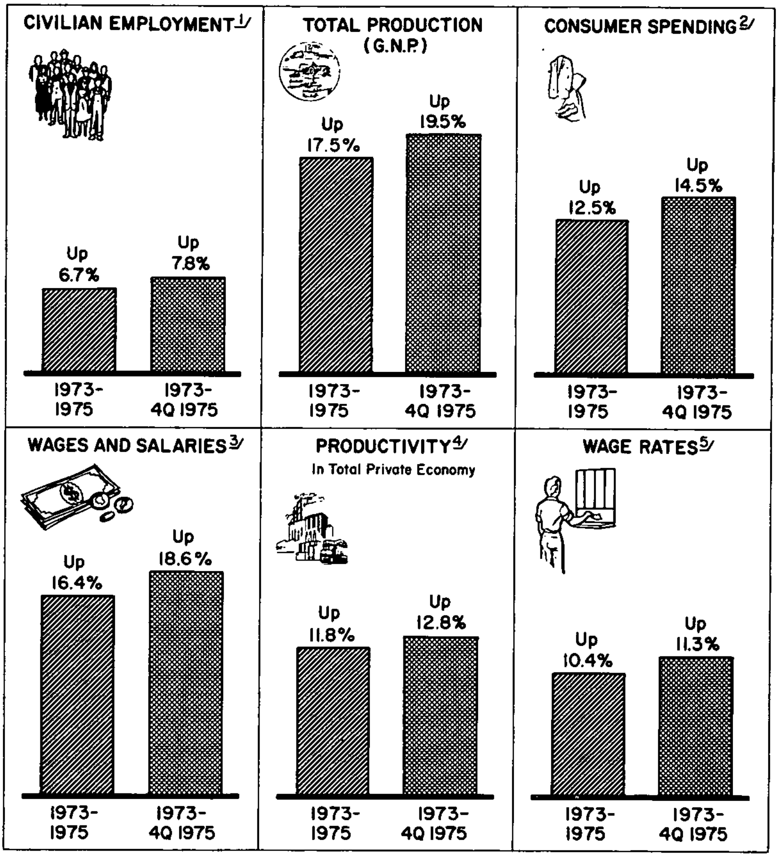

EXCESS INTEREST COSTS IN THE FEDERAL BUDGET 1964-1972 CONTRASTED WITH OTHER COSTS RELEVANT TO THE WAR AGAINST POVERTY 1/
Millions of Dollars
EXCESS INTEREST COSTS IN THE FEDERAL BUDGET
$5,519
$7,974
Annual Average 1964-1972
1972
BUDGET OUTLAYS FOR EDUCATION
$4,791
$8,195
Annual Average 1964-1974
1975 2/
BUDGET OUTLAYS FOR HEALTH SERVICES AND RESEARCH
$10,902
$26,282
Annual Average 1964-1974
1975 2/
BUDGET OUTLAYS FOR HOUSING AND COMMUNITY DEVELOPMENT
$2,871
$5,667
Annual Average 1964-1974
1975 2/
BUDGET OUTLAYS FOR PUBLIC ASSISTANCE AND WELFARE SERVICES
$7,028
$17,894
Annual Average 1964-1974
1975 2/
BUDGET OUTLAYS FOR MANPOWER PROGRAMS
$1,912
$3,342
Annual Average 1964-1974
1975 2/
1/ Interest costs, calendar years; budget outlays, fiscal years.
2/ Proposed in fiscal 1975 Budget.

Chart 15

GOALS FOR THE U.S. ECONOMY, 1975 & 4th Q 1975 PROJECTED FROM 1973 BASE TO ACHIEVE FULL RESOURCE USE BY 4th Q 1975

Total Percentage Changes

(Dollar Items in Uniform Dollars)



1/ Unemployment down 28.6% and 34.6%, respectively.

2/ Growth is less than growth of G.N.P., primarily because of needed growth in public outlays to meet domestic priorities, projected at 33.4% and 35.6% respectively.

3/ Total labor income, 16.2% and 18.4%, respectively.

4/ Much higher than long-term productivity growth, which must be the case in vigorous recovery movement. Less than G.N.P. growth, part of which would result from expansion of employment. Growth in employment plus growth in productivity exceeds growth in G.N.P., due to changes in working hours and other factors in composition of labor force.

5/ Projected at slightly slower than growth in productivity, so as not to move wage rate growth too far out of line with longer-term sustainable trends, in view of extremely high and nonsustainable growth in productivity during vigorous recovery movement.

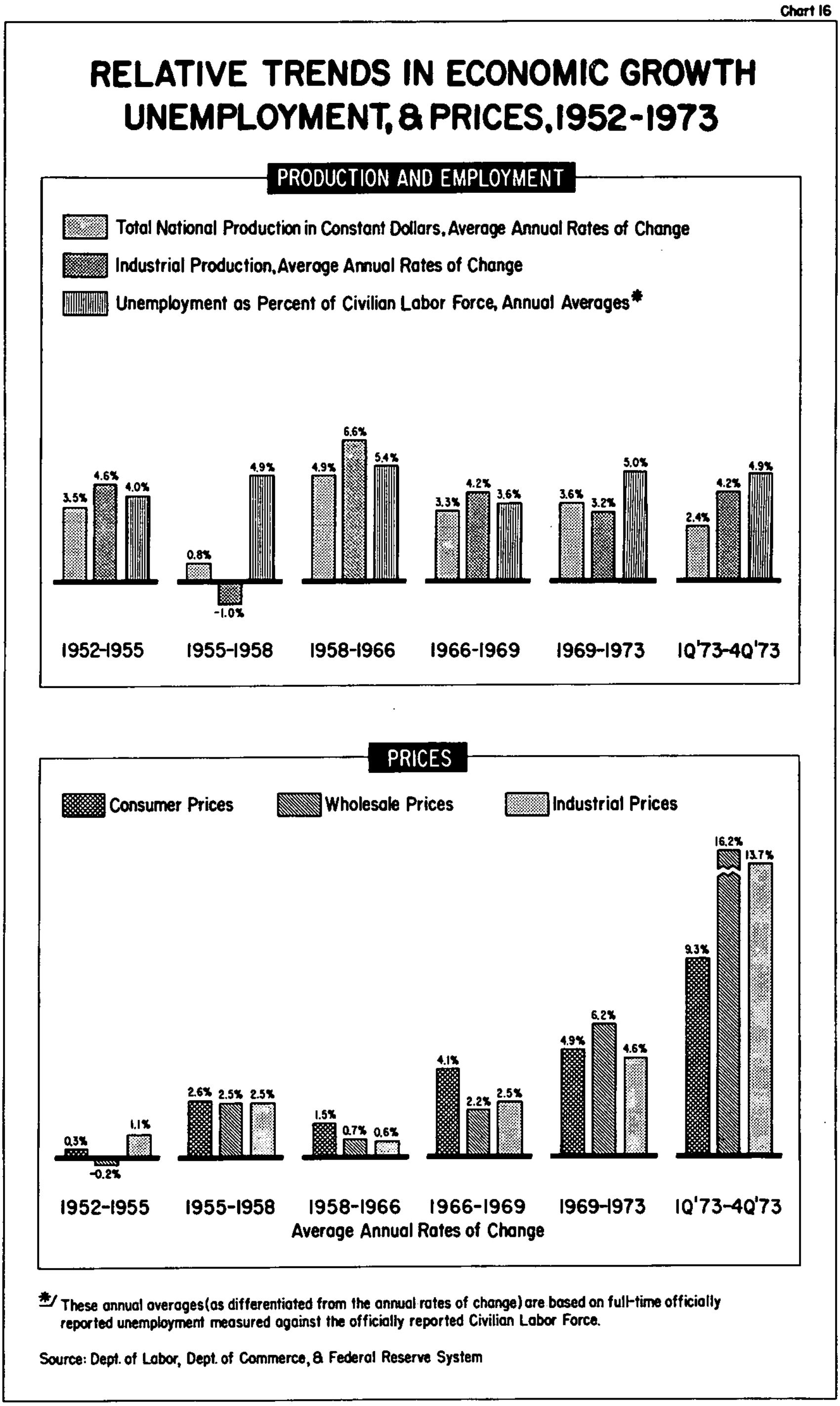


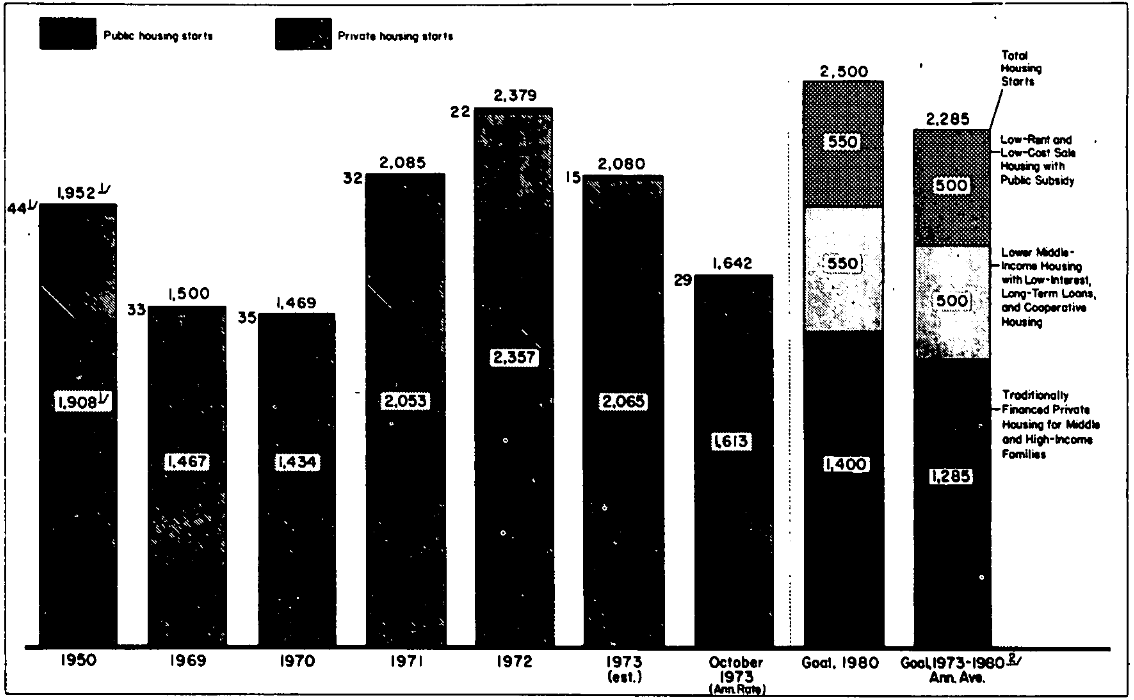
Chart 16
RELATIVE TRENDS IN ECONOMIC GROWTH UNEMPLOYMENT, & PRICES, 1952-1973
PRODUCTION AND EMPLOYMENT
Total National Production in Constant Dollars, Average Annual Rates of Change
Industrial Production, Average Annual Rates of Change
Unemployment as Percent of Civilian Labor Force, Annual Averages*
3.5%
4.6%
4.0%
0.8%
-1.0%
4.9%
4.9%
6.6%
5.4%
3.3%
4.2%
3.6%
3.6%
3.2%
5.0%
2.4%
4.2%
4.9%
1952-1955
1955-1958
1958-1966
1966-1969
1969-1973
1Q'73-4Q'73
PRICES
Consumer Prices
Wholesale Prices
Industrial Prices
0.3%
-0.2%
1.1%
2.6%
2.5%
2.5%
1.5%
0.7%
0.6%
4.1%
2.2%
2.5%
4.9%
6.2%
4.6%
9.3%
16.2%
13.7%
1952-1955
1955-1958
1958-1966
1966-1969
1969-1973
1Q'73-4Q'73
Average Annual Rates of Change
*/ These annual averages (as differentiated from the annual rates of change) are based on full-time officially reported unemployment measured against the officially reported Civilian Labor Force.
Source: Dept. of Labor, Dept. of Commerce, & Federal Reserve System

Chart 17

1127

HOUSING STARTS, 1950-1973, AND GOALS FOR 1973-1980

(Thousands of Units)

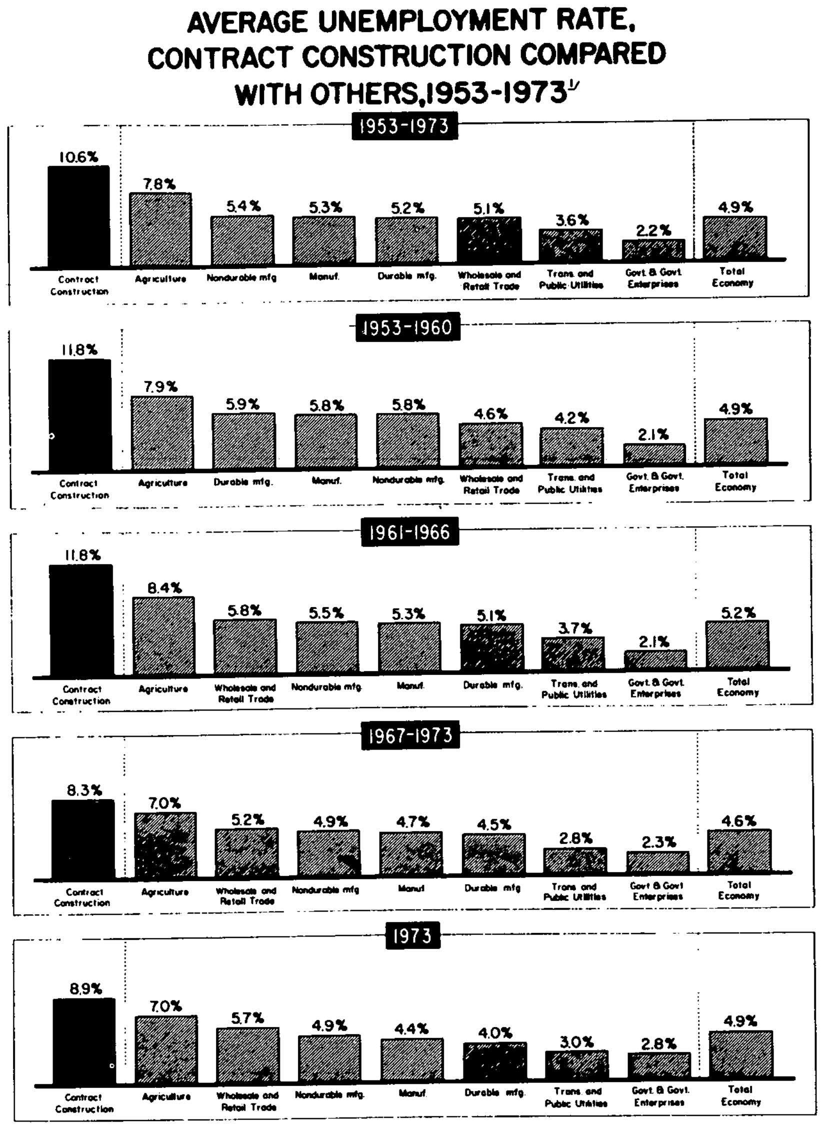


1/ Non-farm only; farm not available

2/ Inclusive. Based on needed annual average of 2.2 million during 1970-1980 inclusive.

Source: Dept. of Commerce, Bureau of the Census

Chart 18



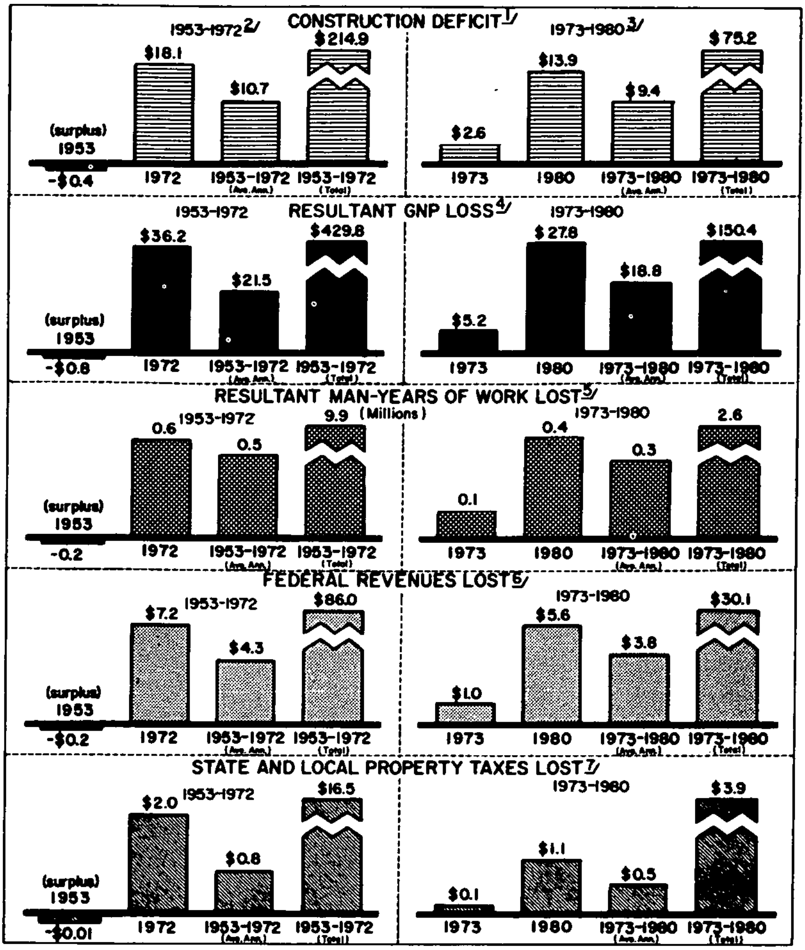
[1] 1973 estimated
Source: Dept of Labor, Bureau of Labor Statistics

Chart 19

IMPACTS OF DEFICITS IN RESIDENTIAL & COMMERCIAL CONST. 1953-1972, AND PROJECTED 1973-1980

(All Dollar Figures in Billions of 1970 Dollars)

(Note Different Scale in Each Box)



1/ Deficits measure actual (estimated for 1972-1980) performance against estimated needed performance in terms of model for total economy.

2/ Actual average annual growth 3.5%; needed, 4.9%, or higher than needed growth rate of 4.3% for total economy.

3/ Projected performance, 3.0%; needed, 5.3%, or lower than needed growth rate of 5.8% for total economy.

4/ Based on multiplier of 2.0.

5/ Based on G.N.P. loss, after allowing for that part of the G.N.P. loss due to repressed productivity growth among those employed even in slowly growing economy.

6/ Equals 20% of GNP loss.

7/ Assumes property tax loss is 2% of private construction deficit, cumulated.

Chart 20

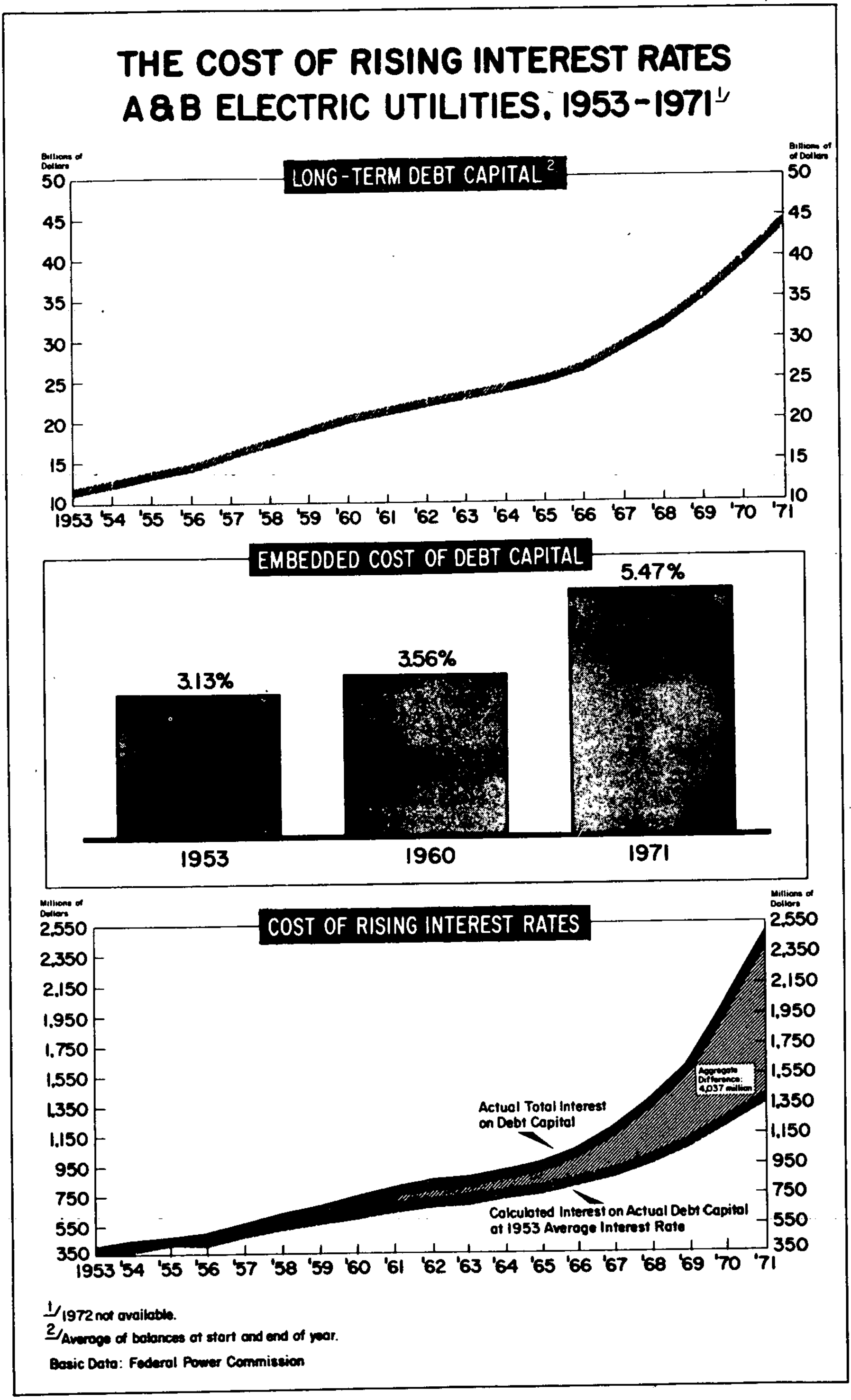

THE COST OF RISING INTEREST RATES
A&B ELECTRIC UTILITIES, 1953-1971 1/
LONG-TERM DEBT CAPITAL 2
Billions of Dollars
50
45
40
35
30
25
20
15
10
1953 '54 '55 '56 '57 '58 '59 '60 '61 '62 '63 '64 '65 '66 '67 '68 '69 '70 '71
EMBEDDED COST OF DEBT CAPITAL
3.13%
3.56%
5.47%
1953
1960
1971
COST OF RISING INTEREST RATES
Millions of Dollars
2,550
2,350
2,150
1,950
1,750
1,550
1,350
1,150
950
750
550
350
Aggregate Difference: 4,037 million
Actual Total Interest on Debt Capital
Calculated Interest on Actual Debt Capital at 1953 Average Interest Rate
1953 '54 '55 '56 '57 '58 '59 '60 '61 '62 '63 '64 '65 '66 '67 '68 '69 '70 '71
1/ 1972 not available.
2/ Average of balances at start and end of year.
Basic Data: Federal Power Commission

Chart 21

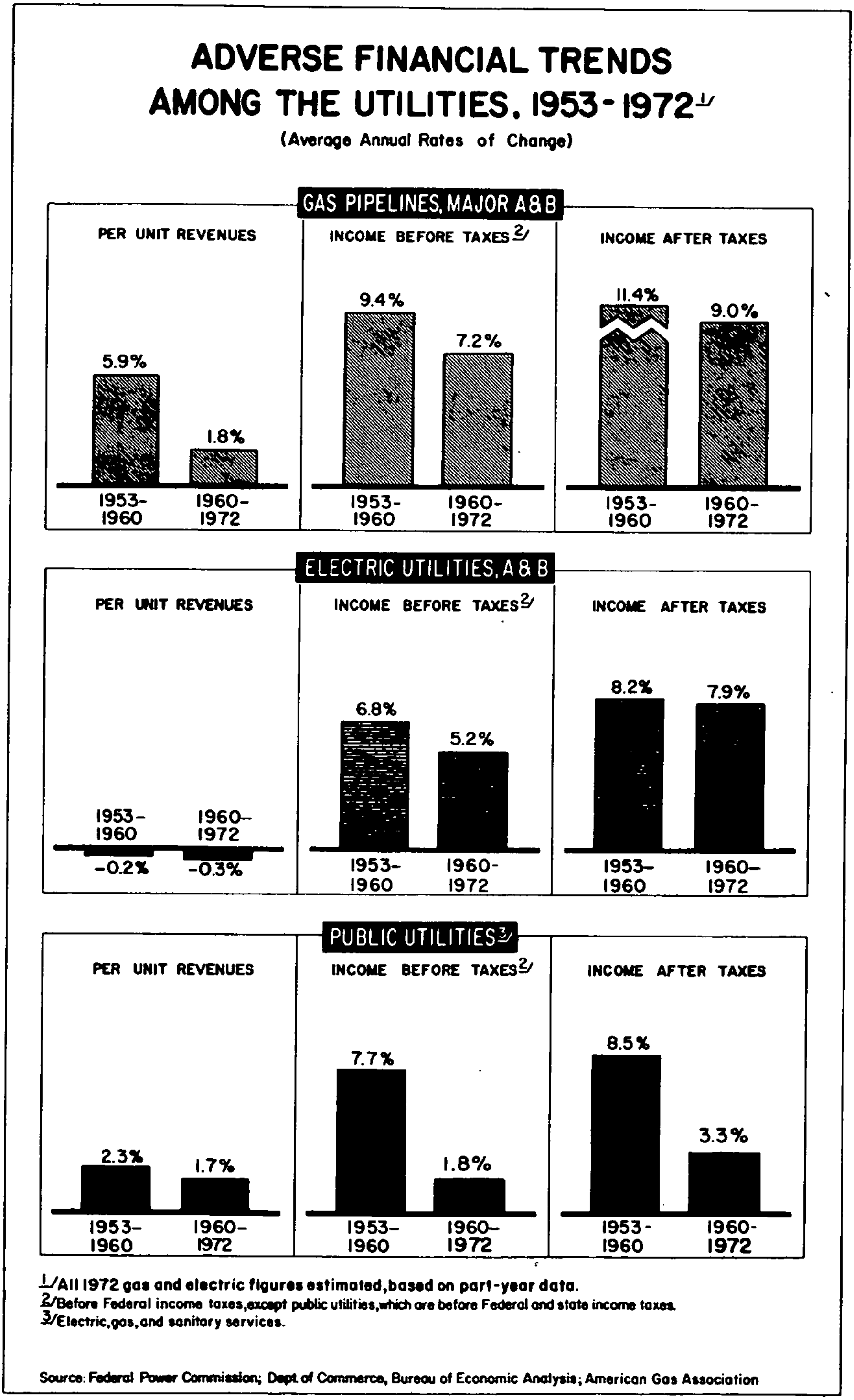
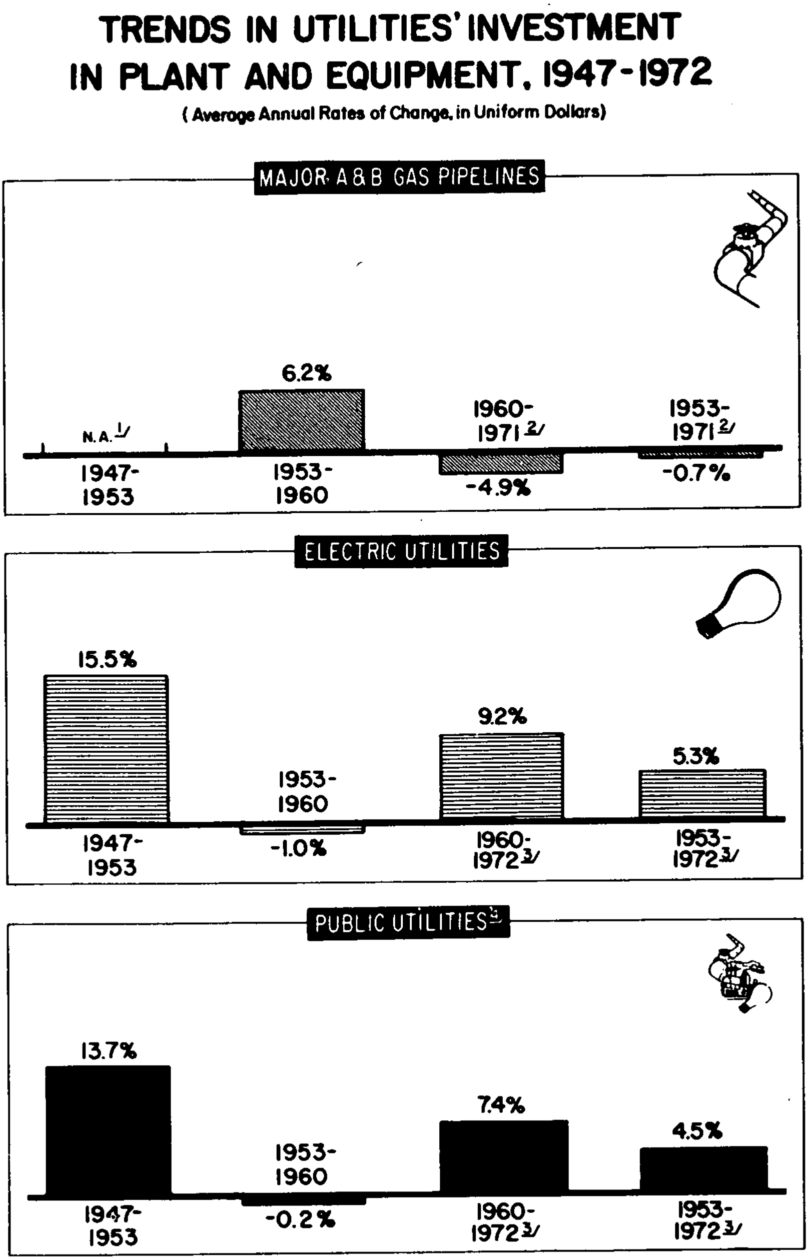

ADVERSE FINANCIAL TRENDS
AMONG THE UTILITIES, 1953-1972 1/
(Average Annual Rates of Change)
GAS PIPELINES, MAJOR A&B
PER UNIT REVENUES
5.9%
1.8%
1953-1960
1960-1972
INCOME BEFORE TAXES 2/
9.4%
7.2%
1953-1960
1960-1972
INCOME AFTER TAXES
11.4%
9.0%
1953-1960
1960-1972
ELECTRIC UTILITIES, A & B
PER UNIT REVENUES
1953-1960
1960-1972
-0.2%
-0.3%
INCOME BEFORE TAXES 2/
6.8%
5.2%
1953-1960
1960-1972
INCOME AFTER TAXES
8.2%
7.9%
1953-1960
1960-1972
PUBLIC UTILITIES 3/
PER UNIT REVENUES
2.3%
1.7%
1953-1960
1960-1972
INCOME BEFORE TAXES 2/
7.7%
1.8%
1953-1960
1960-1972
INCOME AFTER TAXES
8.5%
3.3%
1953-1960
1960-1972
1/All 1972 gas and electric figures estimated, based on part-year data.
2/Before Federal income taxes, except public utilities, which are before Federal and state income taxes.
3/Electric, gas, and sanitary services.
Source: Federal Power Commission; Dept. of Commerce, Bureau of Economic Analysis; American Gas Association

Chart 22



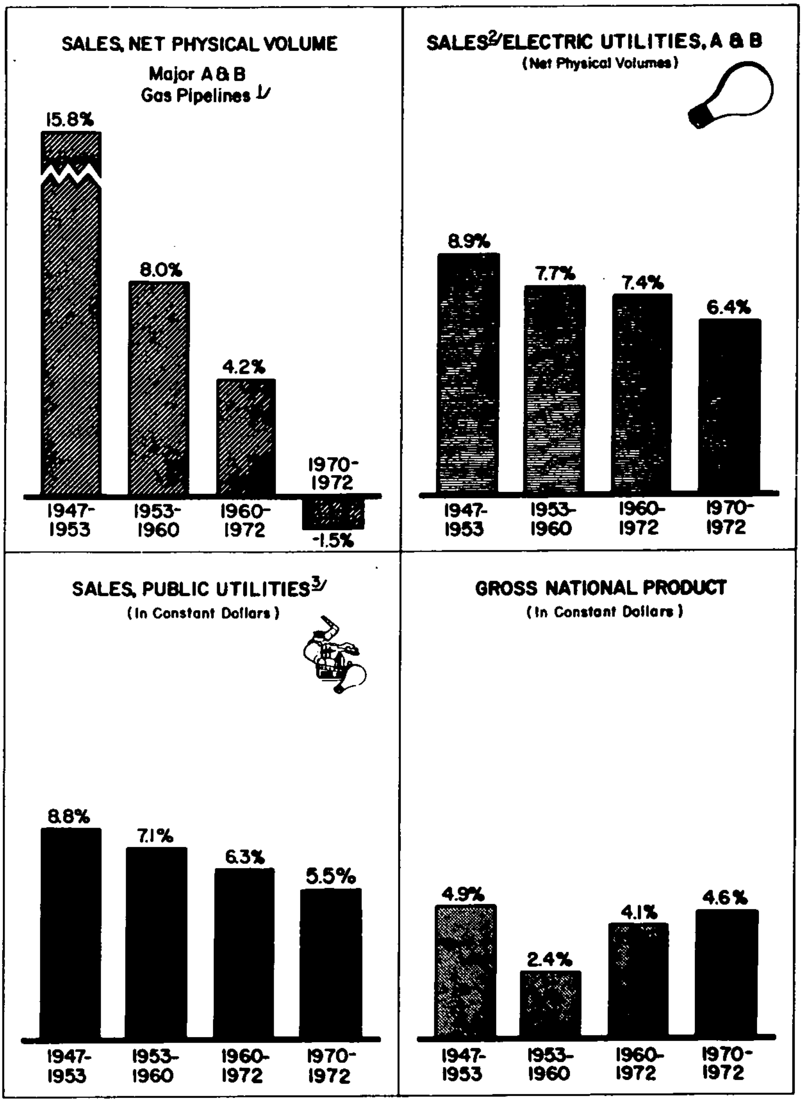
1/ 1947-1953 data not available.
2/ No 1972 data available.
3/ 1972 preliminary.
4/ Electric, gas, and sanitary services.

Basic Data: Federal Power Commission; Dept. of Commerce, Bureau of Economic Analysis

Chart 23

GROWTH IN UTILITY SALES, 1947-1972 COMPARED WITH U.S. ECONOMIC GROWTH

(Average Annual Rates of Change)



1/ 1972 estimated.
2/ To ultimate consumers. 1972 is estimate based on growth of total industry.
3/ Electric, gas, and sanitary services.

Basic Data: Federal Power Commission; Dept. of Commerce, Bureau of Economic Analysis; American Gas Association

CONSUMERS UNION

By PETER H. SCHUCK, *Director, Washington Office*

The fourth consumer right has been described as "the right to participate in the decision-making process." In the following article the director of the Washington office of Consumers Union outlines the concentration of power in the Federal Capital of the USA, where "the 'administrative state' has become the central ingredient in the process of consumer choice." The article then traces the development of the process of public regulation in the public interest, and describes the role within that process of the law office established in Washington by CU just over a year ago.

Can a small band of young brash consumer lawyers find happiness and professional fulfillment in a product-testing and publishing organization? Can legal activism and journalistic integrity coexist in one integrated enterprise? Is the packaging of information for courts and Government agencies inevitably inconsistent with the packaging of information for consumers? Is Washington, D.C. a million miles from Mount Vernon, N.Y.?

Consumers Union, the father of the American consumer movement, set out to answer these questions in November 1972, when it launched a new venture—its own Washington law office. When Consumers Union was founded in 1936, the idea of a consumer law firm in Washington, had anyone been so bold as to consider it, would have seemed outlandish. Americans had developed little consumer consciousness; that phenomenon would have to await the proseprity of the postwar era. As often as not, young lawyers in the depression years were working as department store clerks; the legal profession, caught up in the general economic cataclysm, did not yet recognize consumer representation as a worthy calling. Consumer abuses abounded, to be sure, but the Federal Government in Washington had little to say about them; massive Government bureaucracies manipulating the rules of the marketplace were spectres for a dimly perceived future.

TRANSFORMATION

Thirty-six years later, the nature of consumerism in America had been radically transformed. Ralph Nader had challenged General Motors and many others, and had achieved astonishing legislative victories which electrified the American people. The awesome spectacle of one man standing alone against the world's largest corporation had nourished the growth of a modern consumer movement. Riding the crest of this wave, Consumers Union had enrolled 350,000 members and Consumers Reports enjoyed a paid membership of 2.2 million. Consumer law was taught at virtually every American law school, and if young lawyers could not yet "do well by doing good," one could at least earn a living representing consumers. The American economy now produced one trillion dollars of goods and services annually, and many of those goods and services were demonstrably hazardous, shoddily made, deceptively marketed, monopolistically priced, and protected from competition. Perhaps most striking, the Federal Government had become the single most important influence on this market system. The steady accretion of corporate, economic, and political power had been accompanied by the flourishing of regulatory bureaucracies which, while intended to control that power, succeeded only in nourishing it.

Federal administrative agencies now decided what consumer products were safe enough to market (the Consumer Product Safety Commission), what foods and drugs could be sold and with what labeling (the Food and Drug Administration), what the price of widgets would be (the Cost of Living Council), what type of advertising was permissible (the Federal Trade Commission), what kinds of television programing might be aired (the Federal Communications Commission), what chemical additives might be added to meat and poultry (the Department of Agriculture), what interest rates could be paid by banks (the Federal Reserve Board), and an infinite variety of other decisions formerly made in a relatively autonomous marketplace.

Administrative Process

In short, the "administrative state" had become the central ingredient in the process of consumer choice, fundamentally shaping the nature and rewards of the economic system for producer and consumer alike. To tame this Leviathan, the American system turned not to countervailing power or decentralized power through income redistribution, but to public regulation in the public interest. If consumers could not work their will in the marketplace because the critical decisions affecting them were made instead in Washington, then consumers would be given a full panopoly of procedural rights of access to the administrative process of the Federal bureaucracies. Once inside the process, consumers could impress their interests and preferences on the body of the law of each agency, thus insuring that the regulated marketplace functioned to protect them from exploitation. Or so the argument ran.

There were—and are—several difficulties with this theory. By itself, the administrative-regulatory process is simply an instrument, and like all intruments, needs skillful players to make it function properly. The process depends almost entirely upon organized expertise and professional advocacy, and consumers have little of either. There are some 10,000 lawyers representing organized economic interests in Washington, D.C., alone, and they often have access to battalions of economists, statisticians, researchers, public relations personnel, lobbyists, academic consultants, and technical experts. This powerful cohort pours a steady stream of data, research, arguments, information, petitions, political pressure points of view, personnel, and "trade secrets" into the great open maw of the administrative agencies. Favors and future job opportunities for agency officials—what Ralph Nader has dubbed "deferred bribes"—make the agencies particularly receptive to the importunings of the organized economic interests. When a commissioner or high official of the Civil Aeronautics Board leaves office, he will almost certainly exploit the special access, influence, and expertise which he has gained while in office, by joining or representing the airline industry. The subtle effects which such a career prospect may have upon the official's decisions while in office can only be imagined.

Arrayed against this well-equipped army are a handful of consumer groups active in national consumer policy affairs. Poorly organized, staffed largely by volunteers, represented by a total of perhaps 75 lawyers in Washington, and hampered in fund-raising by Internal Revenue Service restrictions, they must confine their efforts to only the most visible, least technically complex consumer issues. Perforce, most of the consumer groups concentrate on a single agency or cluster of regulatory issues. They have little or no legislative lobbying resources to lend "clout" to their advocacy. The national press, with ample political corruption and intrigue to fill their pages and broadcasts, no longer courts consumer activists, making access to public opinion more difficult and attenuated. The administrative agencies continue to be led by officials enjoying a brief, mid-career sabbatical from their corporate positions. And mountains of valuable information, the staff of administrative life, lie in agency files, unused by consumer groups for lack of anyone who can process, organize, and disseminate it.

In an effort to begin to redress this massive imbalance in the advocacy resources molding the administrative process, Consumers Union established a Washington law office a little over 1 year ago. Now five lawyers strong (one is an engineer as well), the Washington office perceives its role as a new application of an old Consumers Union principle—that the carefully accumulation of facts, forcefully presented, can significantly affect the consumer's strength in the marketplace. The audience, however, is different. For while Consumer Reports and CU's other publications disseminate information directly to the consumer, the Washington Office presents facts—often the same facts—to the three branches of the Federal Government. Through litigation in the Federal courts, testimony before legislative committees of the Congress, petitions and policy analysis to the regulatory agencies, the Washington office seeks to develop the legal implications of those facts.

Restrictions

There are many instances, for example, in which the law inhibits competition, thereby preventing consumers—even those armed with perfect information—from indulging their preferences in the marketplace. Some of these restrictions are susceptible to legal challenge. For example, New York savings banks sell life insurance which, because it is sold over-the-counter rather than through agents, is significantly less expensive than virtually all competing policies. (This is demonstrated by a comparative cost study of life insurance policies appearing in the January, February, and March 1974 issues of Consumer Reports.) A New York statute, however, prevents any consumer who does not live or work in New York State from purchasing savings bank life insurance, and severely limits the amount of such insurance which may be purchased even by New Yorkers, while no such restrictions are placed on other insurance companies selling essentially identical policies. The Washington office is suing to invalidate these anticompetitive restrictions, thereby enabling consumers to purchase insurance at greatly reduced cost.

Product safety, an issue of long-standing concern to Consumers Union, has received much attention. The Washington office, working closely with Consumers Union technical staff, has sued the new Consumer Product Safety Commission over the commission's regulations on electrically-operated toys, the first consumer suit ever filed against toy safety regulations. Additional legal challenges were made to the commission's regulation to permit the sale of flammable mattresses with negative labeling. The Washington office has petitioned the commission to prohibit or restrict the sale of pet turtles due to the uncontrollable Salmonella hazards which they create, and of certain types of acetone-based bubble balloon toys, a demonstrated cause of illness in small children. And the office followed up the Consumer Reports study on the potential hazards of microwave radiation from home ovens with a successful petition for strengthening the testing standards and labeling.

In the administrative-regulatory universe, information is power, and the Washington office has filed a series of lawsuits directed at disclosure of corporate and governmental information. A suit against the Cost of Living Council contends that the Council has illegally restricted the types of price, cost, and profit information which may be made publicly available. And three suits under the Freedom of Information Act against the Interstate Commerce Commission (on freight rate bureaus), the Federal Reserve Board (on interest rates for consumer loans), and the Justice Department (on premerger negotiations between the Government and private industry), seek to arm consumers with the information which they need to participate in the administrative process in a meaningful fashion.

Petition

In the tradition of Consumer Reports, the Washington office has also stressed product information. A petition to the Food and Drug Administration urges that drained weight labeling be required for packaged fruit and vegetable products. And a petition to the Federal Trade Commission argues that all advertising for over-the-counter drugs disclose medical conditions of symptoms requiring adjustment of dosage, discontinuance of use or consultation with a physician after onset of use. A petition to the Cost of Living Council to require posting of octane ratings on gasoline pumps has been adopted and is now in effect.

A recent victory which may have great potential impact occurred when the District of Columbia Public Service Commission accepted the argument of the Washington office that a one-time, flat-rate 5 percent late payment charge imposed by the local electric utility—and also imposed in most other jurisdictions—was unjust and discriminatory, and must be replaced by a monthly credit charge. Consumers Union is now seeking to establish the right of consumer groups to recover from the utility the costs of successful participation in utility rate cases, a principle which could encourage such participation by impecunious groups in the future. And the Washington office has now challenged the right of a regulated public utility to use its customers' money to propagandize them on controversial issues—in this case, the safety of nuclear generating plants—and to do so in a deceptive and one-sided fashion.

The Washington office does not confine its role in the administrative process to formal agency proceedings and court litigation. Monitoring of ongoing agency activities, while less visible and dramatic, is perhaps more important, if only because industrial and bureaucratic interests operate with greater freedom from outside scrutiny at the informal level. Accordingly, the Washington office submits analytical comments on proposed agency actions on a wide variety of consumer issues, from price controls to priorities in fuel allocations to nutritional labeling of foods. And in the product safety area, we are actually helping to shape the priorities and policymaking procedures of a new regulatory commission.

Congressional committees need information and viewpoints from consumers, and the Washington office frequently presents testimony on pending legislation. Thus, Consumers Union attorneys have testified on such subjects as life insurance, meat inspection, consumer credit, price controls, and the proposed Consumer Protection Agency. The Washington office does not lobby, but frequently analyzes legislation upon request and works closely with lobbying groups on significant legislative issues.

If Consumers Union's new law firm has demonstrated one truth after 1 year of life, it is that Washington, D.C. and Mount Vernon, N.Y. are not very distant after all. The engineers, technicians, and editors at Consumers Union headquarters seem far more sensitized to the legal implications of their research and the potential leverage effects of their work on national policies affecting consumers. The pages of Consumer Reports increasingly reflect this awareness. The lawyers in Washington, for their part, have come to recognize the extraordinary value of technical expertise and information in persuading courts, agencies and Congress to recognize and advance consumer interests. Consumers Union is an organization in great and often painful flux, echoing the changes in the larger society of which it is a part. The Washington office is a symptom and perhaps, in small measure, a catalyst in that process of change.

COOPERATIVE LEAGUE OF THE USA

By Stanley Dreyer, *President*

This statement from the Cooperative League of the USA is submitted in response to the invitation of the Joint Economic Committee to give our reactions to the budget for the coming fiscal year sent to the Congress last month by the President.

The Cooperative League is a federation of organizations representing every major type of customer-owned business in our country. The League is the United States member of the International Cooperative Alliance. With a membership drawn from the fields of farm marketing and supply, housing, health, credit unions, rural electric, consumer and many other segments of our broad-based and diverse economy—a total of some 23 million families in every State, and Puerto Rico—ours is no narrow concern for particular limited aspects of national public expenditure but rather what we hope is a balanced, comprehensive look at this proposed deployment of resources as contemplated by the Executive and spelled out in detail by the Office of Management and Budget.

It was only a short 12 months ago that the Cooperative League of the USA found itself responding to a similar request from your committee to react to the national budget for the year in which we now find ourselves. That budget aggregating a staggering $269 billion came just when the last of over half a million soldiers were extricating themselves from a profligate military adventure in Indo-China stretching back over a decade. We dared then to hope—and had reason to expect—that with this return to peace the substance being extracted from our people by the Federal Government in support of the war would be redirected toward human needs so long neglected while the war ground on.

In the cities where by a great and growing majority people choose to live, and in rural areas where this tilt toward urban America leaves serious economic imbalance, the need for decent housing, better health care, and all the basic services that support an orderly society has been accentuated. The justification of our criticism and concern expressed a year ago in reference to the $269 billion budget submitted in 1973 has been emphasized by further deterioration in respect to these all too obvious requirements if the quality of life for ordinary Americans is to be sustained at an acceptable level. Instead in another year of relative inaction and drift we have seen the housing program frozen in its tracks, a health care situation teetering on the brink of chaos with daily hospital costs climbing toward an utterly unacceptable $200 level, and similar inadequacy reflected in the all but nonexistent mass transportation system.

Much of the criticism of the budget heard by your committee centers on its sheer size which has grown 100-fold in the lifetime of millions of Americans—from $3 billion in 1925 to $300 billion in 1975—and this criticism, which we share, is pertinent. But the thrust of our concern is directed more toward how this money is being spent than for its size. To maintain perspective and get a handle on what is happening we need only point out that the major element of expenditure, military hardware, reaches toward an astronomical $100 billion which is more than the entire budget 12 years ago.

This voracious appetite for more and more defense spending has made a captive of a distorted civilian economy. The economy has come to depend more and more for its momentum and employment level on the sums we spend in this way. To mortgage our economy to such sterile purposes has the immediate effect of denying sustenance required to meet elementary demands in the areas of health, housing, education, transportation, and support of the growing segment of elderly citizens whose plight is a stark accusation directed at our ability to make the obvious choice of priorities characteristic of any civilized society.

In surprisng testimony before the House Appropriations Committee, the Secretary of Defense gave sharp point to our objection when he said $1½ billion was in his budget to stimulate local economy in certain places. The chairman of the committee, in agreeing, said the sum was nearer $5 billion. If local economies require the stimulus of Federal spending, we submit that it should be done for useful public works. The prospect of turning the Pentagon toward WPA-like activity, as its Secretary proposes, is both a frightening and depressing misconception of how a free people should set about defending themselves.

It is our conviction that nothing so mirrors the sort of people we are, the quality of our judgment, the direction in which we want our society to move, than does the budget we adopt. Heavy outlay in preparation for future conflict bespeaks a concern for building strength on the periphery, but this will be self-defeating if done at the expense of intrinsic values that make the effort worthwhile in the first place. Those inner strengths of a people at peace with themselves are more durable than the brittle Maginot Lines our dollars prop up when those dollars were better spent building a social order so acceptable that it will call forth from its people a will to defend what in their eyes is worth saving because it serves them well. A generation ago when a beleagured Britain was confronted by Hitler we had hard evidence of how much this strength matters in a crunch.

A rightful ordering of priorities not only results in a happier people but assures the base for a prosperity that will generate out of that prosperity the means to provide solid balanced defense against all the threats to it from within and without. The will of a united, contented, and prosperous people provides more security than the most sophisticated technology set up to defend a society lacking those attributes.

To avoid repetition we invite a rereading of comments made to the Joint Economic Committee a year ago by the Cooperative League regarding that budget because what was said then with great conviction is reaffirmed now in the light of another year's experience with the fruits of misplaced emphases on what we spend our money for.

As your committee has wisely noted, there is nothing more suitably finite than a budget to provide a point of departure for this national seminar on our purposes and aspirations, one that forces upon us hard thinking about our role in a world afflicted by great inequalities at home and abroad. We are grateful for the chance you give us to participate in your seminar.

CREDIT UNION NATIONAL ASSOCIATION, INC.

Credit Union National Association, representing over 90 percent of the Nation's 23,000 Federal and State credit unions, welcomes the opportunity to comment on the important issues contained in the 1974 economic report of the President.

In general, 1973 was a difficult year for credit unions and their members. The continuing problems of inflation, record high interest rates, and eroding consumer confidence extracted their toll on all segments of the economy including credit unions. While there are many steps proposed in the economic report that should help alleviate some of the problems of 1974, the prospect of still more inflation, rising unemployment, and a dramatic slowdown in consumer spending for durables present particular problems for credit unions. In addition, the broader issues of proposed changes in the structure of financial institutions in the United States, and the evolving changes in the payments system which may threaten the privacy of financial transactions are ones that concern credit unions and deserve continued attention by the Congress.

Inflation

The problem of inflation is one of particular concern to credit unions and their members. Approximately 80 percent of all credit unions have a common bond of employment. These credit union members of industrial firms, educational institutions and governmental units face rising prices, particularly food and fuel prices, that are in excess of their wage increases. At the same time, credit unions face rising costs of operation on all fronts, since all federally chartered and most State-chartered credit unions are limited to a 12 percent consumer loan rate. Credit unions have never had an increase in this 12 percent maximum since the Federal Credit Union Act was passed in 1934, but a continuation of escalating costs driven by high rates of inflation in the general economy ultimately is certain to jeopardize this record. In short, we share the great concern of all Americans in the 8.8 percent rise in the Consumer Price Index during 1973 and the prospect for a similar rise in 1974.

We applaud the administration's efforts to capitalize on our great agricultural productivity for increased food production in the hope of stemming rising food prices and alleviating balance of payment concerns. We recognize the need to expand production in certain food and raw material areas in order to have sufficient quantities available at competitive prices. The administration's efforts along this line deserve support. Monopolistic industries, however, should not be allowed to use current shortages as a justification for unconscionable price increases that generate monopoly profits and promote more inflation.

High Interest Rates

Inflation breeds high interest rates since suppliers of funds demand higher rates to protect their purchasing power while borrowers are willing to pay higher rates since they will repay cheaper dollars. This is, however, a very dangerous treadmill. It is particularly troublesome for credit unions and other thrift institutions. In periods of high interest rates like 1973, the flow of savings into credit unions slows at the time that consumer credit demands increase. Unlike large commercial banks which can aggressively bid for funds and pass the costs on to the borrower through progressive prime rate hikes, credit unions face a fixed 12 percent interest ceiling on the consumer loans they make. Although credit unions have traditionally paid their savers equal or greater returns than other financial institutions, they do not have the flexibility of banks to charge progressively higher rates to borrowers. The solution should not have to be higher rates to borrowers but rather a more orderly economy in which both inflation rates and interest rates are more moderate.

Consumer Confidence

The experience of early 1974 and the prospect for the remainder of the year are not encouraging in terms of instilling confidence in the American consumer. The 28 million credit union members are buying fewer cars and other durables and are traveling less as they are confused and uncertain as to the prospects for energy sources and the economy.

The effect of this lack of consumer confidence has been and will continue to be one of a drastic slowdown in the amount of new loans made by credit unions to their members for cars, boats, mobile homes and other consumer purchases. This further exacerbates the revenue/cost problem faced by many credit unions.

Over time credit union members' financing needs change both in terms of items financed and the way they are financed. Since credit unions exist to serve their members' thrift and credit needs, they have the power to serve their members in terms of their consumer financing requirements. As auto and motor home loans decline in importance, it is important that credit unions have the ability to make all types of point of purchase loans in a manner convenient to the credit union member.

Financial Institutions Act of 1973

In the 1974 economic report of the President, the administration called for enactment of the Financial Institutions Act of 1973. Credit Union National Association, after extensive information gathering seminars in major sections of the country, has adopted a policy statement on the proposed legislation. We do not believe that this proposed legislation as drafted, as in the interest of the American public. Credit unions support the concept of efficient financial markets with many alternative sources of supply for those needing capital. We do urge, however, that Congress give thoughtful consideration to the implications of the proposal as presented.

As discussed earlier, the financing needs of credit union members are changing as their buying habits change. While credit unions have no desire to change their cooperative nature, they do desire to have the ability to provide their members services to meet their financial needs. We consequently have asked that we be granted powers to offer a variety of saving instruments, to have checking and NOW account powers, and to have loan power to make all types of point of purchase loans. Having this type of service available from credit unions as well as other institutions appears to us to be in the interest of the consumer public.

Credit unions are not convinced that the proposals in the Financial Institutions Act of 1973 are all in the interest of the American consumer, however. Removal of regulation Q is one example. It is our opinion based on the "wild card" experience of 1973, that totally unrestricted competition for savings deposits would mean that in periods of restrictive monetary policy, funds would flow to large commercial banks serving business needs, and away from the savings and loan associations, mutual savings banks and credit unions which service the consumers' mortgage and other financial needs. All of these thrift institutions lack the ability to change their earning rates in the short term, thereby being unable to generate the revenues needed to pay higher rates on savings. Credit unions have a 12-percent interest ceiling, while savings and loan associations are locked into fixed return mortgages and bonds. Only large commercial banks have large amounts out in loans where they can change their earnings rate by raising their prime. Consequently, in periods of restrictive monetary policy they will progressively raise savings rates until they have priced other financial institutions, without that flexibility, out of the market. The flow of funds figures on page 312 of the economic report show that in 1969, both bank and thrift felt the impact of tight money. Time deposits at commercial banks fell $10 billion while at savings institutions they grew only $8 billion. In 1973, with extensive use of "wild card" promotion, banks had a $54 billion seasonally adjusted inflow during the third quarter while savings institutions had nearly $8 billion inflow. We do not believe that all of the impact of tight money should fall on savings institutions and therefore their customers while the large commercial banks buy funds at high rates to pass on to accommodate their large commercial accounts. Consequently, we do not see how removal of regulation Q is in the consumers' interest.

There are many other issues raised in the proposed Financial Institution Act of 1973. Any legislation of this magnitude should be given thorough consideration before enactment, to assure that its impact will be to maintain and enhance the diversity and availability of financial services to the American public rather than destroy it. We have serious reservations as to whether the FIA proposals do this.

Changes in the Payment System

In addition to those issues raised in the report, we believe that the entire issue of the evolving payment system deserves the immediate attention of Congress. Decisions are being made by private, semipublic, and public bodies that could lock all people and institutions into a payment system that is not responsive to the public and which may be an invasion of privacy. Recently the Federal Reserve has asked for comments on changes in regulations regarding the transfer of funds. While the technical nature of the release obscures the nature of the policy issues involved, these issues are massive indeed since they may well determine the control and participation in the evolving system. We believe these issues are of such magnitude that they should be debated by and decided by Congress and not one agency established to serve one type of financial institution.

Conclusion

Credit Union National Association believes that (*a*) the Federal Reserve should not spend what are in effect public dollars to build a system for exclusive use by banks, (*b*) that all financial institutions should have access to any electronic payment system, (*c*) that Congress should insure that consumers retain as much control over and privacy in their financial transactions as they presently have, and (*d*) that the Financial Institutions Act of 1973, as written, fails to serve the best interest of the American consumer.

MACHINERY AND ALLIED PRODUCTS INSTITUTE

By GEORGE TERBORGH, *Economic Consultant*

INFLATION AND PROFITS

The effect of rising price levels on the accounting of profits is not a new subject. During the sharp postwar inflation of 1946–48 it generated a lively discussion in accounting and management circles. This was revived, on a lesser scale, by the price run-ups of 1950–51 and 1956–57. But under the relatively stable price level of 1958–64 interest waned. It was widely believed that inflation was a thing of the past, that the aftereffects of earlier inflation would gradually wear off, and that no corrective action was needed. This proved to be an illusion. By 1965 inflation was under way once more, and it has continued at a distressing pace ever since. It is now high time to take another look at the problem.

The Principle

The overstatement of profits during and after a period of inflation arises from the practice of charging only the historical cost of physical asset consumption (fixed assets and inventory). When the purchasing power of the dollar is shrinking, the charging of historical costs—reflecting earlier, and hence lower, price levels—is insufficient for the restoration of the real assets used up in production. A proper reckoning requires the restatement of previously incurred costs in the dollars of realization, that is to say, in the revenue dollars against which they are charged. Only when costs and revenue are measured in the same dollars can the difference between them (profit) be correctly determined.

It follows that when the real cost of physical asset consumption is undercharged the shortfall is accounted as profit. It follows also that this much of the reported profit is fictitious, representing simply the understatement of costs.

The Project

What we intend to do is to translate into current-dollar equivalents (equivalents in the dollars of revenue) the costs of physical asset consumption now accounted on an historical basis. We can then see what difference the conversion makes in the profit figures. The study is limited to the corporate system because profit as such is not available for the unincorporated sector, and more specifically to nonfinancial corporation, the category principally concerned with physical asset consumption. It is limited alo to the inflation of 1965–73.

In doing this we rely for both fixed assets and inventory on data compiled by the Department of Commerce—in the case of fixed assets, on its computations of current-cost depreciation; in the case of inventory, on its "Inventory Valuation Adjustment." [1]

[1] In both its depreciation and its inventory adjustments the Department uses specific price indexes to compute the current-dollar equivalents of historical costs. While we prefer a general index of the purchasing power of the dollar for this conversion, its use would not alter the results fundamentally. For a discussion of this issue see "Realistic Depreciation Policy," MAPI 1954, chapter 12.

I. Fixed Assets

The Department computes annually current-cost depreciation on the fixed assets of nonfinancial corporations, using two writeoff methods (straight-line and double-declining-balance) and a variety of service-life assumptions.[2] It is noncommittal on the choice of depreciation methods, but does have a preference on service-life assumptions (85 percent of bulletin F lives). We shall use that assumption in conjunction with the double-declining-balance writeoff.

A word on the choice of writeoff. Notwithstanding the Department's neutrality on the issue, we entertain no doubt that the straight-line writeoff is in most applications a grievously retarded measure of capital consumption, and that the double-declining-balance method is in general more realistic. This is not the place to argue the issue, which we have done at length elsewhere.[3] Suffice it to say that this writeoff conforms quite well to both theoretical and empirical evidence on the typical course of capital consumption, especially for capital equipment (as distinguished from structures), which accounts for around five-sixths of corporate depreciation.

The following table compares the Department's computation of current-cost double-declining-balance depreciation with its estimate of the depreciation allowed for income tax purposes.

TABLE 1.—COMPARISON OF THE CURRENT-COST DOUBLE-DECLINING-BALANCE DEPRECIATION OF NONFINANCIAL CORPORATIONS WITH THE DEPRECIATION ALLOWED THEM FOR INCOME TAX PURPOSES

[Billions of dollars]

Year	Current cost DDB[1] (1)	Income tax depreciation (2)	Excess of (1) over (2) (3)
1965	35.8	35.4	0.4
1966	39.7	38.4	1.4
1967	44.4	41.7	2.7
1968	49.0	45.4	3.6
1969	54.7	50.1	4.6
1970	60.6	54.0	6.6
1971	65.7	58.1	7.6
1972	70.6	63.2	7.4
1973	[3] 75.8	[4] 68.1	7.5

[1] The Department's "Current-Cost 2." This employs a more conservative index of construction costs than "Current-Cost 1."
[2] Differences may not check exactly because of rounding.
[3] Our estimate.
[4] Average of second and third quarters at annual rate.

Note that the excess of current-cost DDB over tax depreciation has grown from a negligible amount in 1965 to $7.5 billion in 1973.[4]

II. Inventory

As indicated earlier, the conversion of inventory consumption charges from historical cost to their current-cost equivalent is computed by the Department of Commerce as the "Inventory Valuation Adjustment" (IVA). The calculation allows for inventory consumption

[2] Both writeoffs are extended over estimated full service lives. The double-declining-balance method is applied with a straight-line switch.
[3] "Realistic Depreciation Policy," MAPI 1954, chaps. 3, 4, and 5.
[4] The stability of this margin over the last 3 years reflects the introduction in 1971 of the asset depreciation range system for tax depreciation.

presently charged for income tax purposes by LIFO and similar current-costing procedures, and converts only the balance under historical-costing systems. The results follow.

TABLE 2.—*Inventory Valuation Adjustment for Nonfinancial Corporations*

	Billions of Dollars)
1965	1.7
1966	1.8
1967	1.1
1968	3.3
1969	5.1
1970	4.8
1971	4.9
1972	6.9
1973	[1] 19.0

[1] Average of 2d and 3d quarters at annual rate.

Here again we have a gradual rise in the excess of current-cost over historical-cost charges, culminating in this case in a sudden surge to $19 billion in 1973.

III. Adjustment of Profits

We are now ready to put the pieces together and adjust profits as reported for income tax purposes.

TABLE 3.—ADJUSTMENT OF REPORTED PROFITS OF NONFINANCIAL CORPORATIONS [1]

[Billions of dollars]

Year	Profits before tax as reported (1)	Income tax liability (2)	Profits after tax as reported (1)-(2) (3)	Under-statement of costs [2] (4)	Profits before tax as adjusted (1)-(4) (5)	Profits after tax as adjusted [3] (3)-(4) (6)
1965	65.8	27.6	38.2	2.1	63.7	36.1
1966	71.2	30.1	41.2	3.2	68.0	38.0
1967	66.2	28.4	37.8	3.8	62.4	34.0
1968	72.4	34.0	38.3	6.9	65.5	31.4
1969	68.0	33.7	34.3	9.7	58.3	24.6
1970	55.7	27.6	28.2	11.4	44.3	16.8
1971	64.1	29.7	34.4	12.5	51.6	21.9
1972	74.3	35.0	39.2	14.3	60.0	24.9
1973	[4] 99.8	[4] 48.2	[4] 51.6	26.5	73.3	25.1

[1] Figures may not check exactly because of rounding.
[2] The sum of the excesses of current costs over historical costs shown in tabl es 1 and 2.
[3] Since this is a retrospective recomputation of profits, it takes as given the corporate income taxes actually paid. If tax liabilities had been figured on the adjusted pretax profits, the after-tax effect of the adjustment would, of course, have been reduced by the tax saving resulting therefrom. But since they were actually figured on the reported profits throughout, there were no such tax savings. Adjusted after-tax profits are simply adjusted pretax profits minus actual taxes on reported profits.
[4] Averages of 2d and 3d quarters at annual rate.

Here is a startling picture. Adjusted after-tax profits started out in 1965 not far below the reported figure. They wound up in 1973 less than half as large as reported. They were, moreover, only 70 percent of the 1965 figure in absolute amount.

Restatement of Retained Earnings

An even more startling picture emerges when we subtract dividend payments from adjusted after-tax profits to derive adjusted retained earnings.

TABLE 4.—ADJUSTED RETAINED EARNINGS OF NONFINANCIAL CORPORATIONS

[Billions of dollars]

Year	Adjusted after-tax profits (1)	Dividend payments (2)	Adjusted retained earnings (3)
1965	36.1	16.9	19.2
1966	38.0	8.2	19.8
1967	34.0	18.9	15.1
1968	31.4	20.9	10.5
1969	24.6	20.7	3.9
1970	16.8	20.0	−3.2
1971	21.9	20.3	1.6
1972	24.9	21.2	3.7
1973	25.1	[1] 22.3	2.8

[1] Average of second and third quarters at annual rate.

Over the past 5 years adjusted retained earnings have been negligible—in one case negative. Nonfinancial corporations have been distributing practically all of their adjusted earnings, their reported savings representing little more than the amount required to cover the understatement of costs.

Adjusted Profits and Retained Earnings in Constant Dollars

To make the horror story even worse, the dollar has been shrinking over the interval and it is necessary to adjust for this by stating the results in constant dollars. We use for this purpose the private GNP deflator (1965=100).

TABLE 5.—ADJUSTED PROFITS AND RETAINED EARNINGS OF NONFINANCIAL CORPORATIONS IN 1965 DOLLARS

[Billions of dollars]

Year	Adjusted after-tax profits (1)	Adjusted retained earnings (2)
1965	36.1	19.2
1966	37.3	19.4
1967	32.1	14.2
1968	28.8	9.6
1969	21.6	3.4
1970	14.0	−2.7
1971	17.5	1.3
1972	19.5	2.9
1973	18.6	2.1

In constant dollars the adjusted earnings of 1973 were slightly over half of 1965. As for retained earnings, the 1973 figure was down by nearly 90 percent.

IV. Effective Income Tax Rates on Adjusted Profits

Since the income tax liability—Federal and State—is computed on overstated historical-cost profits it is obvious that the effective rate on profits adjusted for the overstatement is higher than the rate reported. The following table shows the difference.

TABLE 6.—EFFECTIVE TAX RATES ON THE PRETAX PROFITS OF NONFINANCIAL CORPORATIONS AS REPORTED AND AS ADJUSTED[1]

Year	On profits as reported (percent) (1)	On profits as adjusted (percent) (2)
1965	41.9	43.3
1966	42.3	44.3
1967	42.9	45.5
1968	47.1	55.3
1969	49.4	57.7
1970	49.6	62.3
1971	46.3	57.6
1972	47.1	58.3
1973	48.3	65.8

[1] Column (2) of table 3 as percentage of columns (1) and (5), respectively.

It is obvious at a glance that effective tax rates on real profits have moved away from those n reported profits. Over the past 5 years they have averaged 60 percent against 48 percent. In 1973 the rate reached 66 percent.

V. What Does it Mean?

It is clear that American business has not yet learned how to protect itself against inflation. Overall, it has been unable to maintain normal margins even in the overstated profits of conventional accounting. In terms of real profits, the shrinkage has been drastic.

It is extremely difficult to protect even nominal profit margins in the face of inflation, owing to the tendency of unit costs to move up faster than realized prices. Under prevailing practice, prices are often fixed for substantial periods ahead. Catalogs may be issued only annually or semiannually; seasonal merchandise may be priced months in advance of delivery; long-cycle production may be quoted before work is started, et cetera. But even where prices are more quickly adjustable there is a general tendency to lag behind the march of costs.

If it is difficult to protect nominal profit margins it is still more so protect real margins. Since the latter are more adversely affected by inflation their maintenance requires even bolder and more aggressive action, not to mention their restoration after they have been allowed to decline.

The core of this action is of course pricing policy. Management must learn how to price its products in an inflationary economy. This means first of all anticipatory pricing—pricing in anticipation of cost increases prior to sale. It means, second, a proper accounting of costs themselves, especially the cost of physical asset consumption.

It must be acknowledged, of course, that such a pricing policy may be impracticable for an individual company in a market where the competition is pricing on understated costs. The real remedy lies in the reform of policy across the board. If all competitors are targeting their prices on fully stated costs, there is a better chance that they can make them stick.

Obviously these exhortations assume the absence of price controls. Given such controls, the efforts of management to maintain real profit margins are likely to be frustrated by bureaucratic action. Since the authorities deal with nominal margins only, and conceive it their mission to squeeze even these, real margins suffer an amplified crunch. There can be no doubt that the controls prevailing since August 1971 have contributed to the subsequent erosion of these margins, but it is easy to exaggerate their impact. It is clear that the erosion was going on before controls entered the picture, and that the basic problem is much deeper. It will be with us after they are gone.

Let us add in closing that the present situation is bad not only for business, but for the Nation as a whole. Despite the suspicion and disfavor that attach to profits in the eyes of many politicians and of a considerable part of the public, it is vital that they be large enough not only to motivate the expansion of productive investment, but to finance a substantial part of it. It is frightening from the public-policy standpoint that the reinvestment of corporate earnings, realistically measured, has almost ceased. If this continued it will cost the country dearly.

Let us add further that the Alice-in-Wonderland accounting of costs and profits that now passes for orthodoxy is a problem not only for business management, but for the accounting profession, the regulatory agencies of the Government, and, not least, for the tax authorities. It is high time for concerted action by all concerned.

It is gratifying in this connection that the accounting profession appears at last to be grappling with the problem. In Britain, the Institute of Chartered Accountants is studying a full-scale restructuring of accounts to reflect inflation. In this country, the Financial Accounting Standards Board may soon consider the subject (its advisory council has recommended that it be placed on the agenda). Another straw in the wind is a recent statement of the Securities and Exchange Commission urging its reporting companies to disclose to stockholders the amount of their earnings representing "inventory profits" (but not, unfortunately, the amount reflecting underdepreciation).

These are hesitant first steps, to be sure, but we may hope that others will follow. We may hope also, and even more fervently, that the tax authorities will not be far behind. For the evils of undercosting are compounded by the present practice of taxing capital consumption as income. No reform of costing procedures can be more than partially successful so long as this practice continues.

[From the Capitol Goods Review, December 1973]

BUSINESS CAPITAL FORMATION—PUTTING IT IN PERSPECTIVE, 1925–70

INTRODUCTION

It has been a decade since the Institute last reviewed in detail the record of business capital formation.[1] The sixties was a decade characterized by real economic expansion, save for the mini-recession of 1960–61 and the significant increase in the rate of inflation after the mid-point of the decade. In a climate of real economic expansion it is not surprising that the capital goods industries turned in an excellent performance.

[1] "Sixty Years of Business Capital Formation," George Terborgh, MAPI, 1960.

The Measurements Employed

To gain perspective, we intend to review the record from 1925 to 1970, employing the same measurements used in the earlier Institute study. These are as follows:

1. The record of business capital expenditures by years.
2. Business capital expenditures as a percentage of the privately produced gross national product.
3. Gross investment in the stock of business capital goods.
4. National output per dollar of gross investment.
5. Gross investment per worker in the private labor force.
6. The ratio of the net to the gross investment in the capital stock.

Coverage

The study is confined to business capital goods, defined as plant and equipment privately held, and is based on U.S. Department of Commerce estimates. Capital goods held by governments and consumers are excluded.

A caveat is in order. Because of the highly aggregative nature of the data and the great diversity of situation among the wide range of product lines subsumed under the heading of capital goods, a good deal of care should be used in applying the findings of the study to individual sectors of the economy.

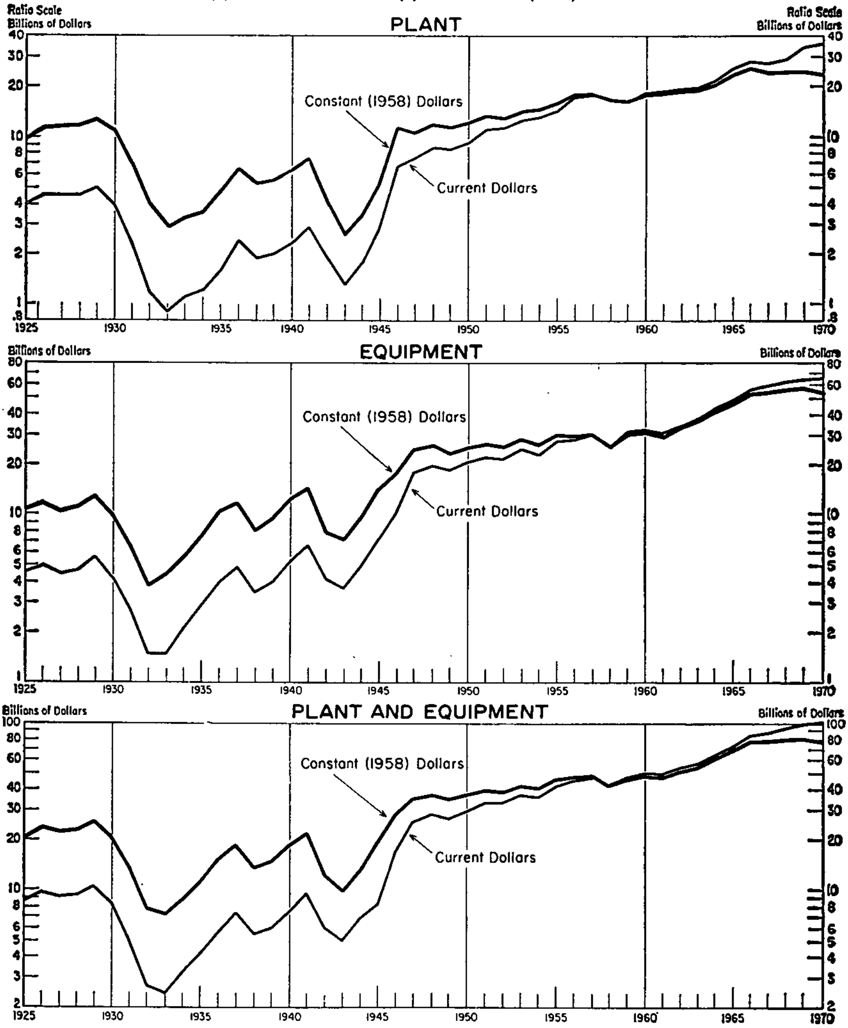
I. Record of Capital Expenditures

The basic data from which all subsequent calculations are derived are the estimates of domestic business capital expenditures by years. These are shown in chart 1 for plant, equipment, and the combination of the two, both in the actual dollars of investment (current dollars) and at their equivalent in the dollars of 1958 (constant dollars).

CHART 1

Expenditures for Business Plant and Equipment:

(1) in Current Dollars; (2) in Constant (1958) Dollars



Source: U.S. Department of Commerce

It is obvious that both plant and equipment expenditures experienced a broad upsweep over the period covered, interrupted only by the downturns reflecting the effect of the great depression and World War II. The slower rise of the constant-dollar line in the years prior to 1960 and the leveling off since 1966 reflect, of course, the persistent and, recently, more rapid rise in capital goods prices due to inflationary forces. While at an alltime high, capital expenditures leveled off in real terms from 1965–70.

As to the components, a new relationship has been established. Equipment expenditures have risen more rapidly than those for plant since World War II. When combined with the overall higher levels of expenditures for plant and equipment, this obviously bodes well for equipment producers should these trends continue.

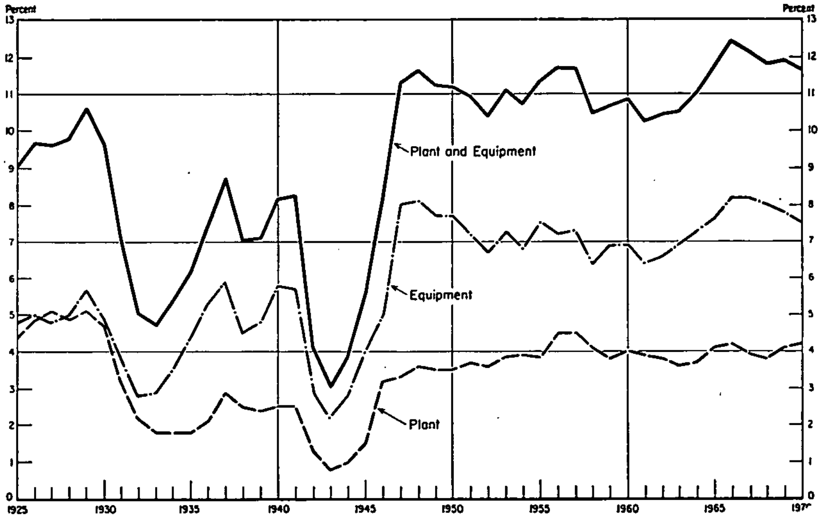
II. Share of Business Plant and Equipment Expenditures in the Privately Produced Gross National Product

As we have seen, plant and equipment expenditures in current dollars are at all-time-high levels. But how high is high? For this we turn to a relative, as contrasted with absolute, measure; namely, business capital expenditures as a share of the privately produced gross national product. This is shown in chart 2, the comparison being in current (actual) dollars.

CHART 2

Expenditures for Business Plant and Equipment as a Percentage of the Privately Produced Gross National Product

(Current Dollars)



Source: U.S. Department of Commerce

While the percentages fluctuate widely from year to year, in large part reflecting changes in general business conditions, several points stand out:

1. The plant ratio, while below the 1925–29 levels [2] of 4.4 to 5.1 percent, rose above its depression and wartime lows and since 1960 has remained relatively stable, ranging between 3.6 and 4.2 percent of the gross private product.
2. The equipment ratio, by way of contrast, rose sharply to 8 percent in 1948 and since then has fluctuated between 6.4 and 8.2 percent. It is significantly above the 1925–29 levels of 4.8 to 5.7 percent.
3. There has been a notable change in the relationship between the plant and equipment ratios. The gap between them has become substantially wider as compared with the predepression period. It narrowed somewhat during the 1950's but has widened again since 1961.
4. For plant and equipment expenditures combined, postwar ratios have run significantly higher than those in the 1925–29 period. In only 1 year (1929) prior to the war did the ratio reach 10 percent; since 1947 every year has been above 10 percent.
5. Since the early part of the postwar era the combined ratio has remained on a new high plateau. The figure for 1970 of 11.7 percent is only slightly below the peak of 12.4 in 1966 and is higher than any year in the predepression period.

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[2] The figures for the period 1925–28 underlying charts 2, 4, and 5 are extrapolative, based on data underlying the charts in "Sixty Years of Business Capital Formation."

Further Comment

The relatively long period of higher ratios during the postwar period for plant, equipment, and the combination of the two no doubt is in some part an offset to the deficiency accumulated during the period of low installations (1930–45). This higher level of demand was made effective through a combination of improved financial availability, due in large part to more realistic depreciation allowances and since 1962 the investment tax credit.

III. Gross Investment in the Stock of Business Capital Goods

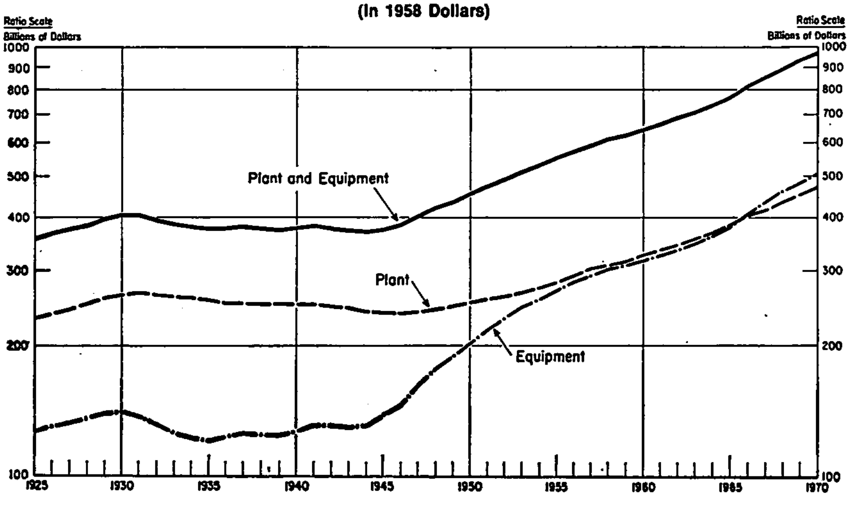
Still another measure of business capital expenditures is the investment in the existing stock of capital goods in place. Here we are concerned with the gross investment before allowance for the accrued depreciation of the stock.

The Commerce Department's capital goods stock estimates assume a consistent application of double-declining-balance depreciation—with straight-line switch—to the historical-cost installations of prior years at service lives equal to 85 percent of Bulletin F lives. In order to state the capital goods estimates in constant (1958) dollars, it was necessary to value identical assets at the same (1958) price regardless of their actual price in the year of acquisition. This measure is shown in chart 3.

CHART 3

Gross Investment in the Stocks of Business Plant and Equipment

(In 1958 Dollars)



Source: U.S. Department of Commerce

A number of conclusions seem obvious:

1. From 1925 to 1945, the stock of plant, equipment, and the combination of the two was generally stable.
2. Since 1945 both plant and equipment have grown. However, investment in the stock of equipment has risen far faster than plant investment, 265 percent against 100 percent.
3. Because of this differential growth rate, the investment in equipment has exceeded that in plant in recent years. Both are in the general vicinity of $500 billion.
4. Investment in the combined stocks is more than 2½ times its 1945 level.

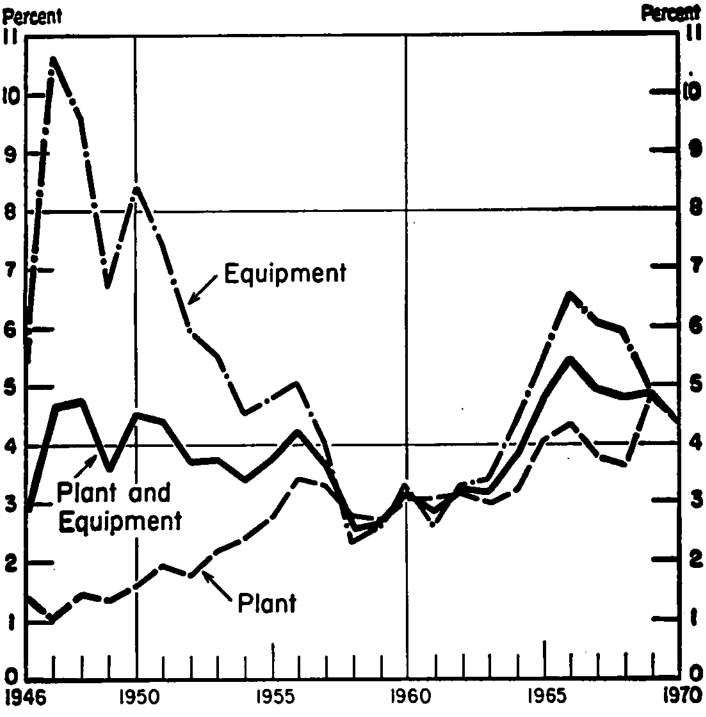
Annual Growth Rates

While the equipment series has grown more rapidly in the post-war era than the plant series, its growth has been significantly slower than its peak years of 1947–48. In fact, the two growth rates in the 2 most recent years covered are about the same. As can be seen from a glance at chart 3A, however, this has happened in the past only to have the two rates diverge. Perhaps the most pertinent observation that can be made is that the two rates once again seem to be approaching rates more in line with the long-run growth rate of the economy; that is, roughly 4 percent.

CHART 3A

Annual Percentage Increases in Gross Investment in the Stocks of Business Plant and Equipment

(In 1958 Dollars)



Source: U.S. Department of Commerce

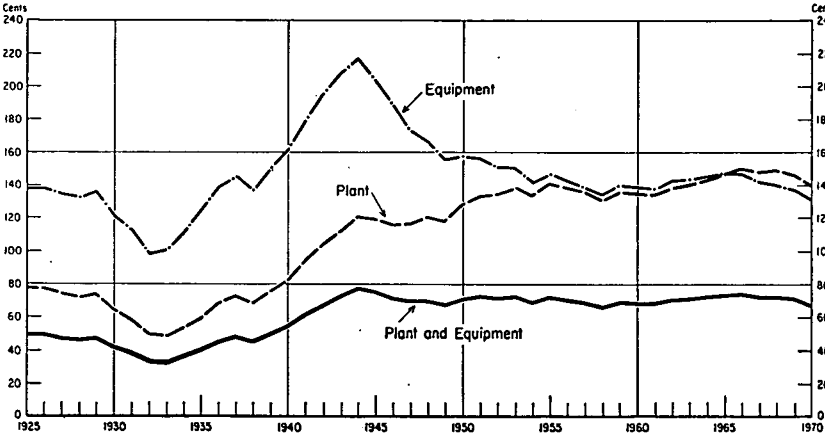
IV. Output Per Dollar of Gross Investment

In section II we related business capital expenditures to the privately produced gross national product of the same year. Now that we have computed the investment in the stocks of capital goods, it is possible to relate the product to this investment. This is shown in chart 4.

CHART 4

Privately Produced Gross National Product Per Dollar of Gross Investment in the Stocks of Business Plant and Equipment

(In 1958 Dollars)



Source: U.S. Department of Commerce

Here, too, a few points are worthy of comment:

1. Over the postwar period, annual output per dollar of investment in plant has moved more or less sideways in the $1.20 to the $1.50 range.
2. Interestingly, after following a significantly different pattern from that for plant from 1925 to the mid-1950's, equipment has followed a similar pattern. In fact, there is now little difference between the two.
3. The result for the combination of plant and equipment is that the two combined have been on a plateau since 1945, ranging between 66.4 and 75.6 cents. This is significantly higher than the predepression period average of 48.2 cents.

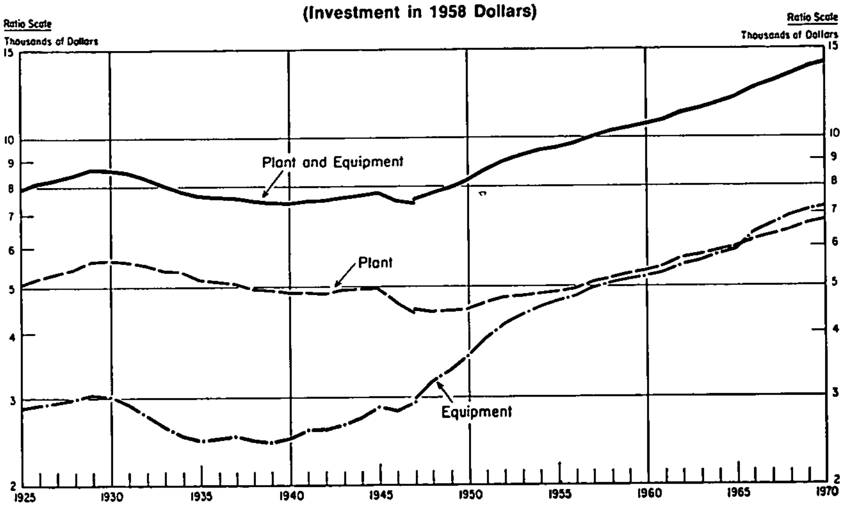
V. Gross Investment Per Worker

Still another measure of interest is the amount of investment per worker. To arrive at this estimate we will use the number of workers in the private labor force. This is shown in chart 5.

CHART 5

Gross Investment in the Stock of Business Plant and Equipment Per Worker in the Private Labor Force

(Investment in 1958 Dollars)



a/Labor Force includes persons over 14 years of age prior to 1947 and persons over 16 thereafter. The 1947 figures are shown on both bases.

Source: U.S. Department of Commerce

Here too, the picture is rather clear. Investment per worker rose in the period 1925 to 1930; it then declined until 1940, when it leveled off during the war. It has climbed since then to new highs. However, as to the components, equipment per worker has grown much faster to the point where the investment per worker in 1970 was slightly greater for equipment, $7,191 against $6,741 for plant. The combined investment is $13,932, in 1958 dollars, and $18,698 in current dollars.

A Look Forward

The amount of capital thst is required to maintain the same rate of increase in investment per worker is of course dependent on the size of the labor force. Since the projected growth rate is now around 1.8 percent as compared with an earlier figure of 11 percent, if expenditures are not increased, the tempo of progress will be slowed up. The moral is that public policies should encourage the higher volume of saving and capital formation required to equip the added workers without detriment to the rate of economic improvement.

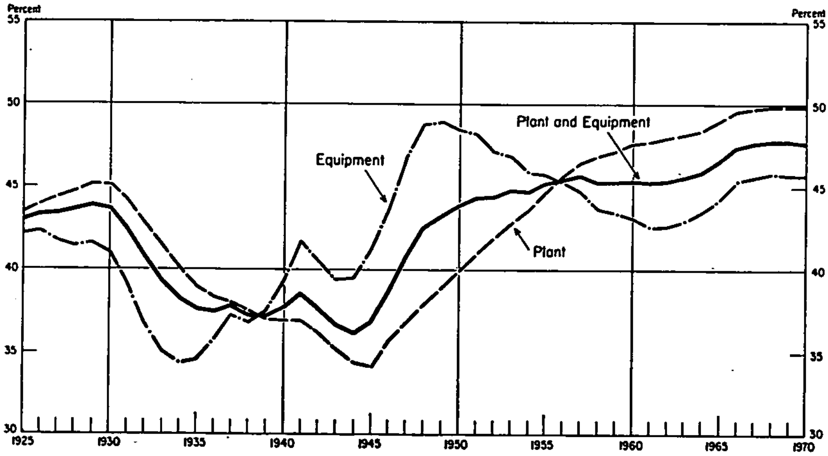
VI. Ratio of Net to Gross Investment

As a final measure of capital expenditures we turn to the ratio of net to gross investment, the net being, of course, the gross minus accrued depreciation. This is shown in chart 6.

CHART 6

Net Investment in Stocks of Business Plant and Equipment as a Percentage of Gross Investment

(In 1958 Dollars)



Source: U.S. Department of Commerce

In the case of plant investment, the net-to-gross ratio declined continuously from 1929 to 1945. Since then it has risen to a present level well above that prevailing before the depression. The equipment ratio has had a more irregular history, declining during the depression, rising a little in the late thirties, and declining again during the war. Thereafter it rose to a very high level during the late 1940's, and has since receded to a point still notably above its predepression position. The combined ratio has risen slightly since the early 1950's to a level well above 1925–29. This is a result of a more rapid growth of installations.

CONCLUSION

No one with an appreciation of the fallibility of these measures will wish to any but the broadest and most general inferences from their use. A few such inferences are worth noting in conclusion.

Normalization

The period prior to the great depression saw a vigorous and persistent expansion of capital goods activity. The next 15 years was a period of contraction and stagnation in this area. The early part of the postwar era, now 25 years in length, was devoted in large part to normalizing the situation—to repairing the damage left by depression and war.

By normalizing we do not mean restoring the situation to what it would have been if the depression and the war had not occurred. These two calamities have doubtless left permanent scars on the economy, and on capital goods in consequence. We mean restoring a normal relation, both qualitative and quantitative, between capital goods and contemporary economic activity—actual activity, not what would have been without the misfortunes of 1930–45.

By this test, the normalization appears to be well along, if not virtually complete. Output per dollar of gross investment in capital goods has substantially exceeded the 1925–29 average. The ratio of net to gross investment has attained a new high. This means that the capital goods industries have been living recently, and will have to live hereafter, on currently accruing needs, without benefit of the restoration or normalization process. This should not be too disturbing a thought; apparently it is years since they have derived any major benefit from this process. The adjustment has already been made.

Beyond Normalization

Normalization of the quality and quantity of the capital goods stock does not imply that the present situation is satisfactory, or that current levels of capital expenditure are adequate. There are several important considerations that argue to the contrary: The increase in the growth rate of the labor force; the forced expenditures for antipollution equipment; the essential expenditures for energy; the present high percentage utilization of capacity; and the economic competition worldwide. All of these considerations argue for higher ratios of capital formation to national product than we have heretofore considered normal.

To assure adequate performance in the future, Government must maintain and even increase measures to augment the flow of funds as a means of stimulating business capital investment. This means, of course, that the present realistic depreciation allowance and the investment tax credit should remain a permanent part of our tax law. Beyond this, it is essential that we eliminate or reduce the present bias in our tax structure against private saving and capital formation. Finally, because of the recent rapid rate of inflation, it is more than ever necessary that the Government adopt an alternative to historical cost depreciation.

The moral is clear. If we are at all right in predicting higher levels of demand for plant and equipment, since the enlargement of business investment depends primarily on an increased flow of funds available for the purpose, there is a pressing need to assure that tax policy encourages private saving and capital formation. This is the surest way to achieve and maintain the higher rate of economic growth which is essential to our national well-being.

NATIONAL ASSOCIATION OF MUTUAL SAVINGS BANKS

By Grover W. Ensley, *Executive Vice President*

These comments on the 1974 Economic Report of the President and accompanying Annual Report of the Council of Economic Advisers focus on major issues of concern to the mutual savings bank industry. Few issues are of greater importance to savings banking and the Nation than controlling rampant inflation and implementing changes in the financial system to strengthen mortgage-oriented thrift institutions and the flow of housing credit.

The Council correctly notes that bringing 8 years of inflation to an end will be a difficult and lengthy task. The administration is to be commended for its expressed determination to "stay the long course" in fighting inflation, and for its continued recognition of the need to develop a more efficient financial system. Success in both areas, essential to assuring an increased and more stable flow of funds to meet the Nation's high-priority housing needs in the years ahead, will require:

(1) The early implementation of basic proposals to strengthen the long-run competitive position of mortgage-oriented thrift institutions through the provision of broadened powers and a Federal charter alternative for State-chartered mutual savings banks;

(2) The maintenance of Federal regulatory authority to establish deposit interest rate ceilings, with realistic differentials for mortgage-oriented thrift institutions; and

(3) The more flexible use of fiscal policy to bring persistent inflationary pressures under control, to reduce excessive reliance on monetary policy with accompanying destabilizing swings in interest rates, and to reduce the overall level of interest rates.

Achieving a better-balanced fiscal-monetary policy mix over the business cycle to control inflation will be the single most important requirement for reducing extreme shortrun swings in the flow of funds into thrift institutions and housing markets. Given the persistent nature of present inflationary problems, the possibility of Federal tax increases should be seriously considered once the economy emerges from its present slowdown, if a recurrence of soaring interest rates, widespread disintermediation and renewed cutbacks in homebuilding is to be avoided.

And the implementation of basic structural changes to strengthen thrift institutions, together with the maintenance of a realistic deposit interest rate ceiling structure, will be the essential requirements for savings banks and other thrift institutions to compete on more equal terms for household savings with full-service, "one-stop" commercial banks in the years ahead.

The intent and ability of commercial banks to compete for household savings is dramatically underscored by the progressive increase in their share of total household savings account growth at major depository institutions since the end of World War II: From 30 percent in the 1946–56 period; to 42 percent in the 1957–65 period; and to 51 percent in the 1966–73 period. The commercial bank share in the 1966–73 period would undoubtedly have been substantially greater in the absence of Federal deposit interest rate ceilings and differentials for thrift institutions. Since mutual savings banks and savings and loan associations hold the bulk of their resources in residential mortgage loans and commercial banks place only a small share of their resources in such loans, this fundamental shift in the pattern of household savings account flows has clearly represented a major, and continuing, longrun diversion of funds from housing.

The July 5, 1973, changes in the deposit rate ceiling structure—including the narrowing of rate ceiling differentials on basic passbook accounts from one-half to one-fourth percent, the authorization for commercial banks to pay a "full 5 percent" on such accounts, and the creation of a new class of small-denomination, ceiling-free "wild-card" certificates with maturities of 4 years and over—further tilted the longrun competitive balance against mortgage-oriented thrift institutions and contributed significantly to massive savings outflows from thrift institutions in the July–October period. The imposition of rate ceilings on "wild card" certificates last November reduced but did not eliminate the strengthened longrun competitive position of commercial banks in household savings account markets resulting from the July 5 changes.

These changes were unaccompanied by any broadening of thrift institutions' consumer-service powers and longrun ability to attract savings. They occurred, moreover, at a time when "tax equality" between thrift institutions and commercial banks had already been substantially achieved under legislation enacted by the Congress in 1969, reflecting substantial increases in thrift institution tax payments and effective tax rates and declines in commercial bank effective tax rates.

All of these considerations underscore the worsening longrun competitive position of mortgage-oriented thrift institutions in household savings account markets, and the urgent need for structural change to strengthen their longrun ability to generate funds for housing. The position of the savings bank industry on structural change is longstanding and unequivocal: mutual savings banks must continue their evolution into "full-service family banks." This will require:

(1) The ability to provide a complete range of financial services to consumers, including consumer loans, checking acounts, NOW accounts, other modern funds transfer services, and full partnership in the emerging electronic funds transfer system;

(2) The ability to invest in a wide range of Federal, State, and local government and corporate securities, as well as mortgages; and

(3) A Federal charter alternative, so that savings banks will have access to the benefits of dual chartering long available to all other types of depository institutions.

All of the consumer-service and investment powers required by modern family banking institutions are in fact already available to mutual savings banks in one or more of the 17 States where they presently operate, but no single State authorizes all of these powers.

Our industry has consistently sought a Federal charter alternative since the late 1950's to hasten the uniform availability of these powers to all savings banks, while simultaneously seeking broadened powers at the State level to serve housing and other consumer financial needs.

Fortunately, the momentum for structural change to strengthen savings banks and other thrift institutions has accelerated, even as the need for change has become increasingly apparent. Both the administration's program for change in the financial system—the Financial Institutions Act of 1973—and proposals advanced last summer by the staff of the House Banking and Currency Committee would provide a dual system for savings banking, and broadened powers in the crucial funds transfer and consumer lending areas.

Even with all of the powers proposed by the administration, however, savings banks and other mortgage-oriented thrift institutions would still have substantially less flexibility and a considerably narrower range of powers than commercial banks. They would, in particular, still be far less able than commercial banks to raise earnings and deposit rates in periods of rapidly rising interest rates because of their substantially longer-term asset structure. It is for these reasons that the savings bank industry strongly supports continued Federal authority to establish deposit interest rate ceilings, with realistic differentials for mortgage-oriented thrift institutions.

In sum, the savings bank industry urges vigorous and realistic steps to control inflation and early action by the Congress to enact legislation to strengthen and modernize the Nation's thrift and home financing system. We look forward to cooperating in every way with the Congress and the administration in these vital undertakings.

NATIONAL FEDERATION OF INDEPENDENT BUSINESS

Letter of Transmittal

Focus Into The Future

FACULTY
ASSOCIATES
INC

January 15, 1974

Joseph H. Fee
President

Mr. Wilson S. Johnson, President
National Federation of
Independent Business, Inc.
150 West Twentieth Avenue
San Mateo, Calif. 94403

Dear Mr. Johnson:

We are pleased to present you with the first National Federation of Independent Business Quarterly Economic Report. This report is based upon data gathered from a scientifically selected sample of the 350,000 - plus members of the National Federation of Independent Business. All facets of this study including the design of the survey questionnaire, choice of firms to be surveyed, analysis and interpretation of results, and reporting of findings and conclusions have been done solely under our direction. We assume full professional responsibility for the entire report.

We believe that this joint undertaking by the NFIB and Faculty Associates, Inc. represents the beginning of a noteworthy venture to gather, analyze, and disseminate, on a regular basis, factual knowledge about prevailing attitudes, current economic conditions, and future expectations of the small business community in this country. This information, in conjunction with other scientifically conducted surveys sponsored by the NFIB, will provide the nation with a wealth of valuable new insights on the functioning of this vital sector of our economy.

Respectfully,

FACULTY ASSOCIATES, INC.

Richard M. Bailey

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THE NFIB QUARTERLY ECONOMIC REPORT

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The first in a continuing series of quarterly economic reports based upon survey data obtained by questionnaire from members of the National Federation of Independent Business, San Mateo, California.

PREFACE

Reflections on economic events of 1973 seem to focus on a single theme – a year of recurrent surprises. One could hardly imagine a period in which more things could go wrong in the economy: record peacetime inflation, shortages of food, devaluation of the dollar, scarcities of many basic materials, lack of financing and historically-high interest rates, rapidly changing policies by government to control prices and wages, and as the year closed, the Arab oil embargo which contributed to a widespread energy crisis. The stock market started a period of decline near year-end which indicated serious concern by investors as to near-term profit prospects. Consumer confidence declined substantially. Many of the effects of politics, international rivalries, shortages and product changes are transmitted into reality for consumers through the small business sector. Somewhat amazingly, the small businessman did not seem overly-dismayed by many of the wildly-fluctuating occurrences in 1973 though he has been caught in their midst. Little despair is recognizable in this survey; in fact, more optimism is revealed than one might have reason to suspect. Perhaps this reflects the fact that for most small businessmen, business is more than business, it is a way of life. And, who wants to view life as dismal?

HIGHLIGHTS

1. Clearly, the most important problem facing small business today is felt to be inflation. The impact of inflation, moreover, is most adverse on those businesses with annual sales volumes under $150,000. The reasons for this particularly-uneven impact shows up in a number of ways in the survey results:

a. Nearly 40% of the firms in the survey reported a decline in earnings over the previous three months; another 40% reported no increase. (Nearly half of the firms in the study are very small, with annual sales under $150,000.)

b. 40% of the firms reported that their average selling prices were the same or lower than three months earlier. The proportion was even higher for firms with annual sales under $250,000.

These findings suggest that many small businesses have been squeezed by rising costs, reducing their profitability. Looking to the three months following the survey, one-third of the firms had no plans for price increases while a nearly-equal number expressed uncertainty about pricing decisions. By industry groups, about 40% of the firms in the construction, manufacturing, transportation, wholesale trade and agricultural industries planned to raise their prices. Only 8% of the firms in the financial services industry planned such increases.

2. Another major problem appears to be excess capacity. The resultant effects of this excess capacity are generally good for the economy as a whole at this time, but carry serious negative implications for the small businessman. Although the extent of excess capacity varies considerably among industry groupings, 49% of the firms reporting indicated they could increase output from 10-29%, and another 18% could expand output from 30-100% or more with no additions to their work force. Excess capacity also exists in terms of physical facilities and equipment, with 42% reporting they could increase production from 10-29%, and another 34% indicating they could increase production from 30-100% or more, with no additions to their plant and equipment. The presence of this excess capacity probably had a dampening effect on the pricing policies of small business. When demand is strong enough to keep an industry operating close to capacity, price increases in line with (or even greater than) cost increases are passed on to consumers more easily and quickly. This has been true in the agriculture sector in the past year, and currently is the case in many major industrial materials industries—basic metals, cement, paper, petroleum products, etc. The Federal Government estimated that at the time of this survey, these industries were operating at approximately 96% of capacity, and their price behavior reflected it. In its own opinion, small business having considerable excess capacity, appears to be holding the line on the prices of many goods and services. This should have provided a restraining influence on the rate of inflation in the economy, at the expense of profits in the small business sector.

3. The impact of tight monetary policy during 1973 reduced the availability of credit in the banking system, and a succession of rising interest rates broke post-Civil War historical highs. Most economists believe that such credit conditions wreak particular havoc on small businesses which are at a relative disadvantage when competing with large business borrowers for limited funds. This survey reveals that for the majority of established small businesses, external financing is of little concern since they do not turn regularly to the money markets for financing. Apparently, they rely largely on internal financing or friends and relatives. There may be a substantial impact on new small businesses unless they commence operations with adequate working capital. This survey did not address that issue.

4. The small business sector is a composite of many different firms. Certain issues and problems are of concern to all; some are unique to members of the same industry group; some are most common to firms of similar size and annual sales volume. In this survey, the major differences existing between firms and industries were:

a. Larger businesses (in terms of annual sales) are expecting considerable difficulty with the quality of labor. Firms in the construction, manufacturing, and transportation industries were particularly concerned about the availability of skilled labor.

b. Taxes are particularly distressing to the smaller firms, especially those in agriculture.

c. Agriculture is strongly concerned with minimum wage laws and the cost of labor.

d. Interest rate levels and the availability of financing is a problem of great concern to the financial services industry.

e. Government regulations and red tape are a problem of increasing significance to professional service firms and to those in the financial services industry.

f. The manufacturing, agriculture, and financial services industries are most optimistic about future business prospects, as reflected by expected sales, and expected additions to their labor force and inventories.

INTRODUCTION

The small business community is a large and vital part of the economy. Independent business employs a majority of the workers in the U.S. and accounts for a large share of the private Gross National Product (GNP exclusive of government expenditures). The small business community is the primary interface between the industrial sector and the consumer, and it functions primarily as the distributors of goods and services produced for the consumer.

In spite of its importance, little is known about this community of competitors. Big business effectively advances its interest to the government and influences business policy in numerous ways, while small business tends to be under-represented. Small businesses must function in the legal and regulatory environment dictated to them, but little is known about how they are affected.

In order to strengthen its position as a representative of small business, the National Federation of Independent Business (NFIB) has initiated a program of inquiry and analysis designed to collect information scientifically about the small business community. Each quarter a representative sample of NFIB members will be surveyed in order to assess their general attitudes, expectations, and opinions, and to gather factual data concerning the effects of government policy and economic fluctuations.

This is the first NFIB Quarterly Economic Report based on data drawn from a major survey of a random sample of member firms conducted in October, 1973. This survey will be repeated each quarter and is expected to yield new information about economic conditions in the small business community -heretofore unavailable from any source, public or private. Some changes are to be anticipated in its format as time passes, although its general structure is expected to remain relatively stable to permit meaningful comparisons over an extended period of time. From these data, several new time series will be developed which should be useful for discerning important changes in the economic situation of small business, and for making comparisons and contrasts with other nationally-reported economic data which customarily focus more heavily on big business. Each report will emphasize certain aspects of the current economic environment vital to the small business sector, and will present trends on basic data contained in each survey.

The twenty questions posed in this survey were divided as evenly as possible between those with a past/present and those with a future perspective. It is important to report what happened to small business in the recent past, and also to analyze what the current attitudes and policies of small businessmen are with respect to the major decisions they are facing. The sharing of such information with other small businessmen should be of value to individual firms, as well as to national economic. policymakers who are concerned with the impact of their actions on small businesses.

Most Important Problem

QUESTION: ***What is the single most important problem facing your business today?***

TABLE[1] 1

PROBLEM	SALES OF FIRM (3rd Quarter Sales Annually Prorated, Less Sales & Excise Taxes) Under $50,000	$50,000-99,999	$100,000-149,999	$150,000-199,999	$200,000-249,999	$250,000-349,999	$350,000-499,999	$500,000-999,999	$1,000,000 and Over	Not Ascertained	ALL FIRMS—Oct., 1973
Labor Unions	*	1	1	1	4	5	3	7	4	4	2
Inflation	29	27	25	21	23	21	22	23	22	19	24
Interest Rates, Financing	12	7	6	9	10	9	11	11	14	13	10
Taxes	15	18	14	11	11	12	12	10	9	6	13
Minimum Wage Laws, Cost of Labor	7	5	6	11	6	9	12	5	6	10	7
Other Government Regulations; Red Tape	10	13	12	11	8	9	9	13	13	12	11
Competition from Large Business	12	11	13	12	11	6	9	9	4	6	10
Quality of Labor	7	9	11	14	17	18	12	17	17	12	13
Other	6	6	8	7	8	7	7	4	9	4	7
No Answer	2	3	4	3	4	4	3	1	2	12	3
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Actual Number Of Firms Polled	319	279	192	113	104	107	135	178	244	48	1719

[1]All figures in table are rounded-off percentages
*Less than .5%

TABLE[1] 2

PROBLEM	INDUSTRY[2] Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
Labor Unions	11	2	7	4	1	2	2	1	1	2
Inflation	16	23	33	20	26	24	16	32	31	24
Interest Rates, Financing	20	7	7	12	6	10	31	6	9	10
Taxes	9	11	12	16	12	24	8	17	14	13
Minimum Wage Laws, Cost of Labor	2	6	7	8	10	7	1	6	4	7
Other Government Regulations, Red Tape	11	13	7	5	12	5	15	9	18	11
Competition from Large Business	3	6	5	12	15	7	12	5	2	10
Quality of Labor	20	21	19	10	10	14	4	12	13	13
Other	7	8	5	10	5	7	6	9	5	7
No Answer	1	3	*	3	3	*	5	3	3	3
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Actual Number Of Firms Polled	167	176	43	133	696	42	131	208	122	1719[3]

[1]All figures in table are rounded-off percentages
[2]See Table 2A for detailed description
[3]Includes one firm for which industry was not ascertained or which fell into the S.I.C. "other" category
*Less than .5%

FINDINGS

The survey deals with a broad range of problems and issues. The findings have been organized into a set of topic areas (listed below) for presentation. The major results are reported and the inter-relations among the issues are presented as seems appropriate. The major topic groupings are:

Most important problem facing business today
Earning trends
Price trends and expectations
Wage expectations
Job openings and labor force changes
Sales expectations
Inventory levels and expected changes
Productive capacity
Credit conditions
Expected general business conditions
Expectations regarding expansion

MOST IMPORTANT PROBLEM FACING BUSINESS TODAY

Tables 1 and 2 indicate clearly that independent businessmen are most concerned about **inflation**, with nearly 25% of all firms selecting this problem from the possible choices. Table 1 indicates that firms with annual sales under $200,000 mention Inflation more frequently as their major problem than those whose annual sales are larger. Other less pronounced differences that appear are: (1) the smallest firms view Taxes as the second most important problem, while, (2) Quality of Labor receives second ranking by the larger companies. (3) Competition from Large Business is the third most important problem for the smallest firms while, (4) problems associated with Interest Rates and Financing rank comparably for the larger firms.

Categorizing major problems by industry classification (Table 2) provides a different perspective on the responses. For expositional convenience, one-word descriptions of S.I.C. industry classification are used in the text. A more-detailed description of the business activities included in each classification can be found in Table 2-A.

- The construction industry reported two difficult problems—the Quality of Labor, and Interest Rates and Financing.
- The manufacturing industry views Inflation and Quality of Labor as its greatest problems. This response pattern is found also for firms in the transportation industry.
- Wholesale and retail firms report that Inflation is their greatest problem. Other major concerns included Taxes and Competition from Large Business.
- Agriculture clearly shows Inflation and Taxes to be major problems.
- Firms in financial services indicated concern most frequently about Interest Rates and Financing. Inflation and Other Government Regulations and Red Tape also were cited frequently as problems.
- Non-professional service firms view Inflation and Taxes as their number 1 and 2 problems, respectively; whereas professional service firms rank Inflation, and Other Government Regulations and Red Tape in first and second place.

The findings indicate that problems faced by firms in different industries are quite diverse, but some concerns appear common to all. Inflation is a concern of all industries, and Government Regulations, Taxes and Quality of Labor appear to be common problems.

TABLE 2A

INDUSTRY CLASSIFICATION	DESCRIPTION
Construction	Construction (building contractors—general, painting, carpentry, plumbing, heating, electrical, etc.; highway & bridge contractors; swimming pool construction; etc.)
Manufacturing	Manufacturing and mining (including dairy processor, printer, publisher)
Transportation	Transportation, communication, public utilities (truckers, movers, broadcasters, etc.)
Wholesale	Wholesale (including grain elevator, livestock dealer, distributor of construction equipment, etc.)
Retail	Retail sales (including food store, service station, restaurant, bar, radio and TV store, drug store, furniture and appliances, auto dealer, etc.)
Agriculture	Agriculture, forestry, logging, fisheries
Financial Services	Finance companies, insurance, real estate, banks, savings & loans, etc.
Non-Professional Services	Beauty salon, barber shop, garage, motel, hotel, repair service, travel agency, bookkeeping service, photographer, funeral director, rental agency, credit bureau, laundry, etc.
Professional Services	Doctor, dentist, attorney, optometrist, engineer, architect, veterinarian, CPA, etc.

Earning Trends

QUESTION: ***Were your net earnings or "income" (after taxes) from your business during the last calendar quarter higher, lower, or about the same as they were for the quarter before?***

TABLE[1] 3

RELATIVE EARNINGS	Oct. 1973
Much Higher	2
Higher	20
About the Same	39
Lower	32
Much Lower	6
No Answer	1
Total	100%

[1]All figures in table are rounded-off percentages

TABLE[1] 4

RELATIVE EARNINGS	INDUSTRY									
	Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
Much Higher	1	2	*	1	2	7	1	2	1	2
Higher	26	24	19	23	16	36	26	19	17	20
About the Same	36	38	32	38	37	26	47	42	45	39
Lower	29	27	33	33	36	26	21	31	35	32
Much Lower	7	6	14	4	8	5	5	3	2	6
No Answer	1	3	2	1	1	*	*	3	*	1
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Actual Number Of Firms Polled	167	176	43	133	696	42	131	208	122	1719

[1]All figures in table are rounded-off percentages
*Less than .5%

Price Trends

QUESTION: ***In percentage terms, how much higher (or lower) are your average selling prices now compared to 3 months ago?***

TABLE[1] 5

RELATIVE PRICES		Oct. 1973
Lower		4
No Difference		36
Higher:		57
Less than 1%	4	
1-1.9%	6	
2-2.9%	10	
3-3.9%	7	
4-4.9%	7	
5-9.9%	14	
10% or More	9	
No Answer		3
Total		100%

[1]All figures in table are rounded-off percentages

TABLE[1] 6

RELATIVE PRICES	SALES OF FIRM (3rd Quarter Sales Annually Prorated, Less Sales & Excise Taxes)										
	Under $50,000	$50,000-99,999	$100,000-149,999	$150,000-199,999	$200,000-249,999	$250,000-349,999	$350,000-499,999	$500,000-999,999	$1,000,000 and Over	Not Ascertained	ALL FIRMS—Oct., 1973
Lower	5	2	4	*	1	6	5	4	4	*	4
Same	48	40	38	40	40	27	35	30	25	25	36
Higher Than:											
Under 2%	10	15	9	9	6	9	10	6	13	10	10
2-2.9%	9	12	10	7	5	10	13	9	8	15	10
3-3.9%	4	6	9	6	5	12	7	10	7	8	7
4-4.9%	3	7	5	8	17	9	7	10	9	*	7
5-9.9%	9	9	14	18	11	18	14	23	20	17	14
10% +	7	6	9	9	9	8	9	8	13	6	9
No Answer	5	3	2	3	6	1	*	*	1	19	3
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

[1]All figures in table are rounded-off percentages
*Less than .5%

TABLE[1] 7

RELATIVE PRICES	INDUSTRY									
	Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
Lower	1	5	*	5	3	12	11	1	2	4
No Difference	36	44	56	23	24	26	53	50	67	36
Higher:	62	50	38	71	70	57	28	45	30	57
Less than 1%	2	3	5	4	5	2	1	5	3	4
1-1.9%	8	8	*	7	7	2	7	5	2	6
2-2.9%	10	6	7	10	13	7	4	7	6	10
3-3.9%	10	5	*	7	9	2	3	7	1	7
4-4.9%	7	5	5	13	9	10	3	5	2	7
5-9.9%	17	15	14	22	17	12	5	9	10	14
10% or More	8	8	7	8	10	22	5	7	6	9
No Answer	1	1	6	1	3	5	8	4	1	3
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

[1]All figures in table are rounded-off percentages
*Less than .5%

EARNING TRENDS

Nearly 40% of reporting firms indicated no substantial change in three-month earnings in October 1973 (Table 3), when compared to the prior three-month period (April, May, June). Almost as many firms (38%), reported a decrease in earnings for the July-to-September period, and only 22% reported an increase. When these trends are examined by industry grouping in Table 4, most notable are the very frequent reports of declines in the transportation and retail trade industries, with 47% and 44% of the firms, respectively, reporting declines. The noticeable exception was agriculture with 43% of the firms reporting increased earnings, a finding consistent with Department of Commerce reports of record earnings for farmers in 1973 after a succession of not-so-profitable years.

PRICE TRENDS AND EXPECTATIONS

Tables 5 through 9 examine the pattern of reported price changes during the three months prior to October 1973, and indicate expected changes in the aggregate, and by industry, for the last three months of the year.

Price Expectations

QUESTION: ***In the next 3 months, do you plan to raise the average selling prices of your goods and/or services, and, if "Yes," by what percent on average?***

TABLE[1] 8

EXPECTED PRICE INCREASE		Oct. 1973
No		34
Don't Know		28
Yes, By:		
Less than 1%	1	
1-1.9%	2	
2-2.9%	5	
3-3.9%	3	
4-4.9%	4	
5-9.9%	8	
10% or more	4	
Don't Know	5	
		32
No Answer		6
Total		100%

[1]All figures in table are rounded-off percentages

TABLE[1] 9

EXPECTED PRICE INCREASE	INDUSTRY: Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
Yes	39	43	37	41	33	41	8	26	25	32
No	26	29	44	26	28	26	58	43	52	34
Don't Know	29	26	14	26	34	26	22	24	20	28
No Answer	6	2	5	7	5	7	12	7	3	6
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Actual Number Firms Polled	167	176	43	133	696	42	131	208	122	1719

[1]All figures in table are rounded-off percentages

Price increases were posted by the majority of firms (57%) during the July-September 1973 period, whereas only 4% reported price decreases, and 36% had stable prices (Table 5). Among those firms reporting higher prices, about 40% (23% of all firms in the survey) raised their prices by 5% or more.

Table 6 reveals a number of interesting differences in pricing behavior among firms with different sales volumes. In general, the smaller firms showed more of a tendency to hold their prices constant, whereas the larger firms reported price increases more frequently (often in the range of 5-9%) during the three-month period under discussion. These data provide few insights into why this is the case. Part of the answer may lie in the industry composition of each sales group. A higher proportion of the smaller firms are suppliers of professional and non-professional services. These smaller firms may have been affected differently by shortages and materials cost increases than the larger construction and manufacturing firms in the survey. Decision makers in smaller firms are more likely to have direct contact with their customers than is the case for the larger firms. This may contribute to a reluctance to increase prices.

Table 7 indicates that firms in the professional and non-professional services, transportation and financial services industries reported price increases less frequently than almost any other industry group. Agri-

Wage Expectations

QUESTION: ***Do you plan to increase the average wages paid per employee during the next 3 months?***

TABLE[1] 10	
EXPECTED WAGE INCREASE	Oct. 1973
Yes	35
No	58
No Answer	7
Total	100%

[1]All figures in table are rounded-off percentages

QUESTION: ***If your answer to above question was "Yes," by what percentage on average?***

TABLE[1] 10A	
PERCENT OF WAGE INCREASE	Oct. 1973
1-2	12
3-4	11
5	46
6-7	14
8+	16
No Answer	1
Total	100%
Actual Number Of Firms Polled	605[2]

[1]All figures in table are rounded-off percentages
[2]35% of all respondents

cultural firms have increased prices most dramatically, with 44% of the firms reporting increases of 4% or more—a reflection of the strong demand and agricultural shortages that occurred in 1973. The highest proportion of firms reporting price increases occurred in the wholesale and retail groups (over 7 out of 10 firms). Of the wholesale firms reporting, 43% raised their selling prices by 4% or more during the preceding three months, reflecting many across-the-board cost increases instituted earlier by manufacturers, energy suppliers, and raw material producers. Nearly as high a proportion (36%) of the retailers raised prices in excess of 4%, suggesting that many wholesale price increases were passed on by retailers to their customers. Construction industry price behavior showed 32% of the firms increasing prices more than 4%, consistent with substantial increases in both labor and material costs pervasive in this industry for the past few years.

In agriculture, 12% reported lower prices, but this is probably due to the marketing of seasonal fruits and vegetables where it is customary for prices to decline as the height of the harvest season is reached. Lower prices reported by 11% of the firms in the financial services industry may reflect lagging demand brought about by tight money conditions and high interest rates—policies instituted by the government to restrain general inflation in the economy. Stable prices were reported by over half of the firms in the professional and non-professional services, transportation and financial services industries. A combination of demand, competitive and regulatory circumstances explains the price stability of these sectors.

Looking ahead three months, Table 8 indicates that there is approximately an even split between firms planning no increase in prices, those planning some increases, and those uncertain of what their probable action may be. By industry, (Table 9) the results are more striking. Approximately 40% of the firms in the construction, manufacturing, wholesale and agricultural industries planned to increase their selling prices in the three months following the survey.

WAGE EXPECTATIONS

Table 10 indicates that about 35% of all firms expected to raise wages during the three-month period from October-to-December, while 58% say that no wage increases are expected. Of those firms anticipating wage increases (Table 10-A), 76% planned to increase wages by 5% or more. About 50% of the firms in the manufacturing and the transportation industries expected to increase wages, while 30% or less of the firms in the non-professional services and retailing industries expected to make such increases (Table 11).

QUESTION: ***Do you expect to increase the average wages paid per employee during the next 3 months?***

TABLE[1] 11

EXPECTED WAGE INCREASE	INDUSTRY									
	Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
Yes	37	52	49	36	29	36	40	30	42	35
No	59	43	49	60	64	48	50	61	57	58
No Answer	4	5	2	4	7	16	10	9	1	7
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

[1]All figures in table are rounded-off percentages

Current Job Openings

QUESTION: ***Do you have any job openings that you are not able to fill right now?***

TABLE[1] 12

AVAILABLE JOB OPENINGS	Oct. 1973
Yes	
Skilled	21
Unskilled	4
Both	5
No	68
No Answer	2
Total	100%

[1]All figures in table are rounded-off percentages

TABLE[1] 13

AVAILABLE JOB OPENINGS	INDUSTRY									
	Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
Yes: Skilled	31	33	30	16	18	24	12	20	18	21
Yes: Unskilled	3	6	2	3	4	5	1	3	3	4
Yes: Both	9	14	10	4	4	2	1	3	2	5
None	56	46	58	77	71	64	84	70	73	68
No Answer	1	1	*	*	3	5	2	4	4	2
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Actual Number Of Firms Polled	167	176	43	133	696	42	131	208	122	1719

[1]All figures in table are rounded-off percentages
*Less than .5%

JOB OPENINGS AND LABOR FORCE CHANGES

Nearly 7 out of 10 reporting firms indicated that they had no job openings that could not be filled (Table 12). Of those with hard-to-fill job openings, 21% reported the jobs were for skilled labor. Only 4% had openings for unskilled workers. Looking ahead to employment prospects in the next three months (Table 14), 74% of the firms expected no change in their work force. Almost equal proportions (13% and 12%) were expecting either increases or decreases.

Table 13 shows that the existing job openings were concentrated primarily in the manufacturing, transportation, and construction industries, where approximately 30% reported they had needs for skilled labor.

Expected Changes In Labor Force

QUESTION: ***In the next 3 months, do you expect to increase or decrease the total number of people working for you?***

TABLE[1] 14

EXPECTED CHANGE IN EMPLOYEES	Oct. 1973
Increase	13
Keep the Same	74
Decrease	12
No Answer	1
Total	100%

[1]All figures in table are rounded-off percentages

TABLE[1] 15

EXPECTED CHANGE IN EMPLOYEES	INDUSTRY: Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
Increase	17	31	7	11	10	14	10	10	16	13
Keep the Same	56	57	67	82	78	67	83	76	76	74
Decrease	26	11	21	6	11	14	6	13	4	12
No Answer	1	1	5	1	1	5	1	1	4	1
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

[1]All figures in table are rounded-off percentages

TABLE[1] 16

EXPECTED CHANGE IN EMPLOYEES	SALES OF FIRM (3rd Quarter Sales Annually Prorated, Less Sales & Excise Taxes): Under $50,000	$50,000-99,999	$100,000-149,999	$150,000-199,999	$200,000-249,999	$250,000-349,999	$350,000-499,999	$500,000-999,999	$1,000,000 and Over	Not Ascertained	ALL FIRMS—Oct., 1973
Increase	7	10	11	15	11	11	17	15	24	17	13
Keep the Same	82	82	78	72	74	75	67	69	57	69	74
Decrease	8	7	11	11	15	13	13	16	18	8	12
No Answer	3	1	*	2	*	1	3	*	1	6	2
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

[1]All figures in table are rounded-off percentages
*Less than .5%

These responses are consistent with the results reported in Table 2 where these industries indicated that Quality of Labor was a significant business problem.

Manufacturers were by far the most positive about expanding their employment, with 31% expecting to increase the number of their employees in the next three months (Table 15). Conversely, the construction industry showed that 26% expected to decrease the number of their workers. Part of the expected decline may be related to seasonal factors, but housing starts also have declined.

In Table 16, expected labor force changes related to firm sales show that the largest firms are the ones anticipating both the greatest increase and the greatest decrease in number of employees. At this time it is impossible to state whether these responses are due to the different mix of industries that comprise similar dollar-sales groupings of firms in the survey, or are a reflection of greater overall uncertainty for the larger companies.

Real Sales Expectations

QUESTION: ***Overall, what do you expect to happen to the real volume (number of units) of goods and/or services that you will sell during the next 3 months?***

TABLE[1] 17

EXPECTED REAL SALES VOLUME	Oct. 1973
Up a Lot	8
Up a Little	34
Stay the Same	21
Down a Little	20
Down a Lot	8
Don't Know	7
No Answer	2
Total	100%

[1]All figures in table are rounded-off percentages

TABLE[1] 18

EXPECTED REAL SALES VOLUME	INDUSTRY: Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
Up a Lot	6	7	7	6	13	7	5	4	3	8
Up a Little	19	39	30	32	37	38	40	31	32	34
Stay the Same	18	26	28	21	17	19	19	23	34	21
Down a Little	35	19	14	29	17	26	18	18	19	20
Down a Lot	13	5	14	7	8	5	9	9	2	8
Don't Know	8	4	2	4	7	2	5	13	8	7
No Answer	1	*	5	1	1	3	4	2	2	2
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Actual Number Of Firms Polled	167	176	43	133	696	42	131	208	122	1719

[1]All figures in table are rounded-off percentages

SALES EXPECTATIONS

Expectations of increases in real sales volume (in contrast to the dollar value of sales which might rise even if real sales decline when inflation is substantial) are foreseen by 42% of all firms reporting. Table 17 also shows that 21% expected sales to remain the same, 28% expected real decreases, and 7% expressed uncertainty about the direction of sales. Among the various industry groups (Table 18), the most bullish expectations for real increases in sales were in retailing, manufacturing, agriculture and financial services with nearly 50% reporting optimism. The industries expecting the greatest declines in real sales were construction and wholesaling. In the cases of retailing, agriculture, construction, and possibly wholesaling, the importance of seasonal factors such as Christmas, fall harvests, and the adversity of winter weather, cannot be overlooked as important determinants of the responses.

INVENTORY LEVELS AND EXPECTED CHANGES

Changes in inventory levels often are viewed as significant components of business spending in the short-run, both because of their impact on overall economic activity and their reflection of businessmen's sentiment regarding sales prospects. However, analysis of inventory change is fraught with many problems. From Table 19, it appears that 57% of all firms were satisfied with their inventory levels in October, 1973, with about equal percentages (11% and 14%) reporting inventories were too large or too small; 16% of the firms were engaged in activities requiring no inventories and 3% did not answer the question. From Table 19-A, expectations for inventory accumulation in the next 3-6 months showed that 48% expected to maintain their current levels, 16% expected to increase their stocks and 18% expected decreases. The implied changes stem

Inventory Levels And Expected Changes

QUESTION: ***At the present time, do you feel your inventories are too large, about right, or inadequate?***

TABLE[1] 19	
CURRENT INVENTORY LEVEL	**Oct. 1973**
Too Large	11
About Right	57
Too Low	14
Not Applicable	16
No Answer	2
Total	100%

[1]All figures in table are rounded-off percentages

QUESTION: ***Looking ahead to the next 3-to-6 months, do you expect, on balance, to add to your inventories, keep them about the same or decrease them?***

TABLE[1] 19A	
EXPECTED INVENTORY CHANGES	**Oct. 1973**
Add	16
Keep the Same	48
Decrease	18
Not Applicable	14
No Answer	4
Total	100%

[1]All figures in table are rounded-off percentages

QUESTION: ***At the present time, do you feel your inventories are too large, about right, or inadequate?***

TABLE[1] 20

	SALES OF FIRM (3rd Quarter Sales Annually Prorated, Less Sales & Excise Taxes)										
CURRENT INVENTORY LEVEL	Under \$50,000	\$50,000-99,999	\$100,000-149,999	\$150,000-199,999	\$200,000-249,999	\$250,000-349,999	\$350,000-499,999	\$500,000-999,999	\$1,000,000 and Over	Not Ascertained	ALL FIRMS—Oct., 1973
Too Large	6	9	7	10	9	16	16	15	18	6	11
About Right	55	60	65	55	62	59	54	58	50	40	57
Too Low	17	13	10	19	8	6	17	12	16	17	14
Not Applicable[2]	20	17	17	14	19	15	12	13	13	15	16
No Answer	2	1	1	3	2	4	1	2	3	22	2
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

[1]All figures in table are rounded-off percentages
[2]Firm had no inventory

from different business evaluations of the future, and necessarily involve a mix of attitudes about total sales and the desired level of inventories to support the sales expectations.

By sales (Table 20), again the findings seem quite inconclusive. The larger firms appear to be more dissatisfied than the smaller ones with current inventory levels and, in about twice as many instances, feel that these levels are excessive.

PRODUCTIVE CAPACITY

Economists frequently seek data on one or more measures of the use of a firm or industry's current work force or its physical facilities and equipment to serve as a proxy for determining the present use of total productive capacity. Firms operating at a level far short of their potential capacity incur higher costs of production, earn lower returns on investments, and in the longterm, may find it difficult to remain economically viable. In

Efficient Use Of Work Force

QUESTION: ***Approximately what percent increase in business volume could you handle without changing the size of your work force?***

TABLE[1] 21

% VOLUME INCREASABLE WITHOUT INCREASING WORK FORCE	Oct. 1973
None	17
1-9	15
10-19	27
20-29	22
30-49	11
50-99	4
100 or More	3
No Answer	1
Total	100%

[1]All figures in table are rounded-off percentages

TABLE[1] 22

% VOLUME INCREASABLE WITHOUT INCREASING WORK FORCE	INDUSTRY									
	Construction	Manufacturing	Transportation	Wholesale	Retail	Agricultural	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
None	31	30	19	8	12	43	2	17	21	17
1- 9	23	19	30	12	13	16	11	15	13	15
10-19	24	27	23	30	28	19	24	27	29	27
20-29	13	14	14	35	26	12	28	21	18	22
30-49	4	4	7	9	13	5	19	11	11	11
50-99	1	3	5	4	5	5	5	4	6	4
100 or More	4	1	*	2	2	*	10	3	1	3
No Answer	*	2	2	*	1	*	1	2	1	1
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

[1]All figures in table are rounded-off percentages
*Less than .5%

Table 21, only 32% of the firms reported operating at or near their capacity, using work force data as the criteria. Nearly half said they could expand output by 10-to-29% without adding to their labor force. In Table 23, similar patterns appear with reference to physical facilities and equipment: only 23% felt they were operating within the range of 0-to-9% of potential capacity; 42% reported their current equipment would support a sales increase of from 10-to-29%, and almost 35% said volume could be increased by over 30% with current capacity. Not surprisingly, the utilization problem for plant and equipment appears more severe since the size of the labor force probably is adjusted more easily to meet the needs of the firm. The results seem to indicate a fair amount of excess capacity. But capacity utilization is difficult to measure, and considerable caution should be exercised in interpreting the results. Results from the same questions over a longer period of time will make this interpretation easier, particularly if these data can be related to other measures of capacity.

In Table 22 when employing the labor force measure of capacity, it appears that the agricultural industry ranks first as the industry operating closest to its potential – 59% of the firms reporting they could expand output only from 0-9% without increasing their work force. Other industries ranking high in this regard are construction, manufacturing, and transportation. Industries with considerable amounts of unused labor force capacity (20% or more) are: financial services (62%); wholesaling (50%); and retailing (46%). The explanation for the unusually-large amount of excess labor force capacity in financial services may be related to the generally-depressed activity in this sector occasioned by the tight money policies of the last year or so. Being a highly labor-intensive form of business employing a skilled and experienced work force, this industry may be reluctant to reduce the number of its employees when troubled by cyclical declines in sales

Efficient Use Of Facilities/Equipment

QUESTION: ***Approximately what percent increase in business volume could you handle without changing the size of your physical facilities or the amount of equipment you use?***

TABLE[1] 23

% VOLUME INCREASABLE WITHOUT INCREASING FACILITIES/EQUIPMENT	Oct. 1973
None	11
1-9	12
10-19	21
20-29	21
30-49	16
50-99	8
100 or More	9
No Answer	1
Total	100%

[1]All figures in table are rounded-off percentages

TABLE[1] 24

% VOLUME INCREASABLE WITHOUT INCREASING FACILITIES/EQUIPMENT	INDUSTRY									
	Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
None	14	13	5	7	8	31	6	14	15	11
1- 9	16	13	23	12	10	14	5	13	15	12
10-19	25	23	26	16	21	24	14	20	20	21
20-29	18	21	16	31	24	12	19	18	17	22
30-49	13	·11	19	20	18	7	16	15	15	16
50-99	5	10	9	6	9	7	15	8	8	8
100 or More	9	8	*	7	8	2	24	10	10	9
No Answer	*	1	2	1	2	3	1	2	*	1
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

[1]All figures in table are rounded-off percentages
*Less than .5%

volume. Moreover, part of the costs of underemployment are customarily borne by the employee himself, since sales commissions are the customary basis for determining part of one's income in this field. Thus, it may be that this industry functions regularly with above-average levels of excess labor capacity. Subsequent surveys will be needed to verify if this pattern holds, or to highlight just how depressed business conditions are in this industry.

Employing the measure of underutilized physical facilities and equipment to indicate excess capacity, Table 24 shows that the agricultural sector is most tightly employed, with 45% of the firms falling within the range where output could be increased by less than 9% with existing plant and equipment. In many of the other industries, about 30% of the firms reported operations close to capacity. Again, the financial services industry led the field of excess capacity: only 11% of the firms indicating they were near their production potential, and nearly 75% indicating they could expand output from 20-100% without additional facilities. Wholesaling and retailing followed in second and third place (as with the work force measure) with respective percentages of 64% and 59%, indicating they were operating at less than 80% of capacity.

CREDIT CONDITIONS

One of the most interesting findings in this survey came from several questions related to the cost and availability of credit. Consistently, more than 50% of the respondents indicated little concern with or knowledge about interest rates or possible difficulties in obtaining financing because they borrowed so infrequently as to make this issue insignificant! Conventional economic wisdom lays heavy emphasis on the uneven impact of tight money conditions. This line of reasoning generally incorporates the proposition that the small businessman is disproportionately affected because he deals with only one or possibly two banks (irregularly) and cannot present his banker with substantial guarantees of solvency. Thus, when credit con-

Credit Conditions

QUESTION: ***If you borrow money regularly (at least once every 3 months) as part of your business activity, how does the rate of interest payable on your most recent loan compare with that paid 3 months ago?***

TABLE[1] 25A

RELATIVE INTEREST RATES	Oct. 1973
Much Higher	11
Higher	22
Same	6
Lower	*
Much Lower	*
Don't Know	1
Not Applicable (Borrow Infrequently)	52
No Answer	8
Total	100%

[1]All figures in table are rounded-off percentages
*Less than .5%

QUESTION: ***Are these loans easier or harder to get than they were 3 months ago?***

TABLE[1] 25B

RELATIVE AVAILABILITY	Oct. 1973
Easier	1
Same	26
Harder	13
Don't Know	5
Not Applicable (Don't Borrow; No Answer)	55
Total	100%

[1]All figures in table are rounded-off percentages

ditions are tight, the small businessman is turned away in favor of larger firms. For half of the reporting firms, this is not an issue.

Four questions were asked about current and expected credit conditions with the results shown in Tables 25A, B, C and D. Among those who responded that they do borrow, the answers regarding trends in interest rate costs and credit availability were generally consistent with reports in the business press about the relative degree of tightness in money markets and short-term expectations for continuation of the same. Almost no firms reported easier terms and no firms reported lower rates. Almost all borrowers felt rates were higher, and many reported tougher terms.

Table 26 provides additional insight into the issue of the effects of recent tight money polcies. First, it is clear that the smaller businesses are the less-frequent users of external financing, with 65% of the smallest firms indicating they borrow infrequently, in contrast to 32% of the largest of the small businesses reporting this way.

The small businessman is more likely to operate using his own, or possibly, family funds. The larger the business becomes, the more it needs access to credit markets. Table 26 also indicates that awareness of higher interest rate levels differs among firms by sales levels. Larger firms, with easy access to credit markets, seem more aware of the higher rates observed in 1973.

Table 27 presents industry group expectations about future credit availability indicating that the agriculture and wholesaling industries seem most assured that credit conditions will not change in the short-run. Aside from these differences, expectations are quite uniform across industry groups.

QUESTION: ***Are the other terms of the loan, such as maturity, compensating balance, etc., easier or tighter now?***

TABLE[1] 25C

RELATIVE OTHER TERMS	Oct. 1973
Easier	1
Same	24
Harder	12
Don't Know	8
Not Applicable (Don't Borrow; No Answer)	55
Total	100%

[1]All figures in table are rounded-off percentages

QUESTION: ***Do you expect to find it easier or harder to obtain your required financing during the next 3 months?***

TABLE[1] 25D

CREDIT EXPECTATIONS	Oct. 1973
Easier	2
Same	23
Harder	15
Don't Know	8
Not Applicable (Don't Borrow; No Answer)	52
Total	100%

[1]All figures in table are rounded-off percentages

QUESTION: ***If you borrow money regularly (at least once every 3 months) as part of your business activity, how does the rate of interest payable on your most recent loan compare with that paid 3 months ago?***

TABLE[1] 26

RELATIVE INTEREST RATES	SALES OF FIRM (3rd Quarter Sales Annually Prorated, Less Sales & Excise Taxes)										
	Under $50,000	$50,000-99,999	$100,000-149,999	$150,000-199,999	$200,000-249,999	$250,000-349,999	$350,000-499,999	$500,000-999,999	$1,000,000 and Over	Not Ascertained	ALL FIRMS—Oct., 1973
Much Higher	5	7	9	9	11	9	13	17	23	12	11
Higher	18	20	17	22	19	25	30	26	31	6	22
Same	4	6	6	7	9	5	5	5	9	8	6
Lower; Much Lower	1	*	*	*	*	*	*	*	1	*	*
Don't Know	1	1	2	*	*	*	1	*	*	2	1
Not Applicable (Borrow Infrequently)	65	57	60	54	50	57	44	47	32	48	52
No Answer	8	8	7	9	12	4	7	5	5	23	8
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

[1]All figures in table are rounded-off percentages
*Less than .5%

QUESTION: ***Do you expect to find it easier or harder to obtain your required financing during the next 3 months?***

TABLE[1] 27

CREDIT EXPECTATIONS	Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
	INDUSTRY									
Easier	3	5	5	2	2	*	2	*	*	2
Same	26	22	21	38	21	41	22	21	18	23
Harder	21	14	9	15	14	12	12	11	19	15
Don't Know	4	5	14	8	9	2	7	7	8	8
Not Applicable (Don't Borrow; No Answer)	46	54	51	37	54	45	57	61	55	52
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

[1]All figures in table are rounded-off percentages
*Less than .5%

Expected General Business Conditions

QUESTION: ***About the economy in general, do you think that 6 months from now general business conditions will be better than they are now, about the same, or worse?***

TABLE[1] 28

EXPECTED CONDITIONS	Oct. 1973
Much Better	1
Somewhat Better	20
About the Same	38
Somewhat Worse	21
Much Worse	5
Don't Know	14
No Answer	1
Total	100%

[1]All figures in table are rounded-off percentages

TABLE[1] 29

EXPECTED CONDITIONS	Construction	Manufacturing	Transportation	Wholesale	Retail	Agriculture	Financial Services	Non-Professional Services	Professional Services	ALL FIRMS—Oct., 1973
	INDUSTRY									
Better[2]	19	17	14	20	19	10	43	21	29	21
About the Same	37	37	49	44	36	50	33	40	35	38
Worse[3]	26	28	28	26	28	19	14	26	25	26
Don't Know	16	15	9	9	15	21	10	13	10	14
No Answer	2	3	*	1	2	*	*	*	1	1
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Actual Number Of Firms Polled	167	176	43	133	696	42	131	208	122	1719[4]

[1]All figures in table are rounded-off percentages
[2]Includes responses ranging from Much Better to Somewhat Better
[3]Includes responses ranging from Somewhat Worse to Much Worse
[4]Includes 1 firm classified as "Other" industry.
*Less than .5%

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Expectations Regarding Expansion

QUESTION: ***Do you think that the next 3 months will be a good time for small business to expand substantially, and why?***

TABLE[1] 30

Reasons	Time to Expand: Yes	No	Uncertain
Economic Conditions	29	36	39
Sales Prospects	59	6	4
Financing, Interest Rates	1	33	22
Cost of Expansion	2	17	21
Other	7	7	5
No Answer	2	1	9
Total	100%	100%	100%
Actual Number Of Firms[2] Polled	176	1050	484
% of All Firms	10%	61%	29%

[1]All figures in table are rounded-off percentages
[2]Nine firms not answering the question were omitted.

EXPECTED GENERAL BUSINESS CONDITIONS

Businessmen's expectations regarding general business conditions in the next six months reveal (Table 28) a rather balanced assessment, with 38% reporting essentially no change from the present, 21% expecting improvement, and 26% foreseeing a worsening in conditions. These expectations are detailed in Table 29, where the most bullish industry group is financial services, with 43% expecting better business conditions within six months.

Given the various comments made by economic observers about an easing in money markets, this group may have good cause to feel optimistic. Other industry groups do not share this optimism. Surprisingly, agriculture seems pessimistic. Perhaps this reflects a combination of feelings: that circumstances improved so much during 1973 that they only could turn worse in 1974; and that certain favorable events in 1973 (The Russian Wheat Deal, for example) will not be repeated in 1974. Agriculture, interestingly, also reports the greatest percent (21%) expressing uncertainty about future business conditions. With the exception of the agriculture and financial services industries, about 25% of all other industries report they expect worsening of conditions in the next six months.

EXPECTATIONS REGARDING EXPANSION

The prevailing attitude in the small business community regarding whether or not this is a good time to expand substantially is: NO! This negative response (Table 30) was provided by 61% of those surveyed; another 29% expressed uncertainty; and only 10% felt that expansion was justified.

In addition to asking for a specific answer, the survey asked for selection from one of several reasons why the respondent felt as he did. Of those who believed that this was not a good time to expand, about equal weight was assigned to current economic conditions and problems with financing (36% and 33%, respectively). Those who were uncertain regarding expansion cited the same two reasons but with different frequencies (39% and 22%). Those believing that the next three months were good for expansion cited sales prospects (59%) and general economic conditions (29%) as their reasons. Responses to this question over a period of time may provide a useful indicator of small business investment activity. The data suggest that few firms will undertake expansionary activity in the near future.

NATIONAL LEAGUE OF CITIES AND THE UNITED STATES CONFERENCE OF MAYORS

The Energy Crisis and Its Current and Projected Effect on City Unemployment

It is extremely difficult to obtain a specific picture of energy-related unemployment or employment changes in many areas. Direct effects of the "crisis" started to be felt in December 1973. Secondary or "ripple" effects in sectors of the economy related to energy supply (the results of various interindustry relationships) are having impact during the months of January and February, and will continue through the spring and summer of 1974.

This paper is a brief discussion of some general areas of impact with respect to the energy crisis. It summarizes both selected city problems of energy-related layoffs and reasons for lack of adverse energy effects in some cities, and finally, discusses some possible ways to deal with the situation.

Response to a NLC and USCM manpower project questionnaire/memo sent out in late January to both mayors and city manpower planners (cities of 100,000 population and over) has been good (list of responding cities attached). Over 50 cities have sent or telephoned information regarding their particular situation with respect to employment and unemployment shifts due to direct or indirect energy crisis effects. Precise figures are not always available, but consultation with knowledgeable persons and in cooperation with local employment security labor market analysts, the judgments or special surveys conducted provide reasonable approximation of the direct impact and the secondary effects on unemployment for those areas. However, no presentation of a "total" impact for the 54 city respondents can be made because of the varying range of information. Some cities have already experienced severe direct and secondary effects, some anticipate future effects but have not experienced significant impact at this time, while still others indicate little direct or indirect effects are, or will be, experienced in their area.

It is obvious that labor market areas having industries using a high proportion of petroleum or petroleum-based products, relative to national totals, or areas with high proportions of their industrial base in industries expected to be hardest hit by energy supply or energy consumption cutbacks, will be the first affected, have the highest direct impact, and, consequently, the higher secondary or indirect effects.

In addition to unemployment increases in industries having high energy requirements, negative impacts may be expected from the following secondary effects: (1) decreases in output stemming from increases in the cost of energy, or local legislation/ordinances calling for mandatory percentage reduction in energy use; (2) decreases in the demand for products or services where demand is a function of high energy requirements (e.g. tourism depends in large part on cars which use gasoline); (3) decreases in the sale of products using significant amounts of energy (many electrical home appliances); (4) general or regional recession; (5) multiplier effects of an unknown magnitude will cause employment decreases as a result of lower consumption and, perhaps, investment; and (6) structural changes in industries shifting from high energy-using products to low energy-using products (e.g. automobile manufacturers closing plants currently producing large cars and expanding plants producing small cars in other areas). In addition, automobile industry layoffs (estimated to be about 80,000 nationwide) as well as recreational vehicle and mobile home assembly industries layoffs may, in large part, be quite long term and some sizable portion may be permanently displaced. Retooling may take place in some plants but this takes time.

These effects, coupled with rising inflation may change the industrial mix on a nationwide basis. Obviously, lower demand caused by changes in consumer buying patterns will reduce production requirements in many instances, and may force closures of straight luxury or higher energy-consumption items. Thus, cutbacks in hours worked, layoffs of part-time employees, followed by full-time employees, or cutbacks in capital equipment in order to avoid these situations will result. The current economic slowdown in the nation coupled with rising prices of raw material inputs will affect industrial production lines. Normally, when the price of one input in the production equation increases, the proportion of inputs used is shifted; where little or no substitution of input mix is possible, serious dislocations may take place.

In addition to industrial effects, dilatory effects on State and city budgets (particularly with respect to gasoline taxes and sales taxes) may be experienced. Maryland, for example, has estimated a drop of $9 million from anticipated 1974 revenue due to decreased gasoline, sales and income taxes. One estimate by the Municipal Finance Officers Association predicts that there will be $3 to $6 billion less than anticipated in State and local revenues for 1974. At the Federal level it is estimated that about $10 billion is lost in the Federal Treasury for every 1 percent rise in unemployment.

The impact of the crisis, reported in the survey conducted by the Manpower project varied from "quite significant" to "expected to be wide sweeping" to "no effect at all." Most cities, of course, experienced at least some layoffs in directly related services (gasoline service stations, hotels/motels on interstate highways, restaurants, some retail stores). Other industries affected quite severly in some areas (dependent upon that area's economic dominance of those industries) are those using large inputs of petrochemicals (e.g. plastics, electric wiring, synthetic textiles, carpets, toy manufacturers, fiberglass boats and the like). Shortages of petrochemical supplies and their rapid increase in price are currently being examined at the national level in hope that the problem can be reduced (see city summaries—city of Bridgeport).

If the energy crisis worsens, or continues at the present level for several more months, the secondary effects, and therefore, the consequences for employment could be quite severe in many areas. As shown by the city summaries, several cities have organized specific energy task forces which use a wide range of methods to obtain a reasonable "grasp" of the situation. Finally, the effect of the energy crisis on many manpower plans or operating programs could be serious.

Cities responding to our survey are listed below:

Akron, Ohio
Allentown, Pa.
Amarillo, Tex.
Baltimore, Md.
Baton Rouge, La.
Bridgeport, Conn.
Cedar Rapids, Iowa
Charleston, W. Va.
Chattanooga, Tenn.
Columbia, S.C.
Columbus, Ohio
Duluth, Minn.
Elizabeth, N.J.
Erie, Pa.
Flint, Mich.
Fort Wayne, Ind.
Fresno, Calif.
Greensboro, N.C.
Hartford, Conn.
Huntsville, Ala.
Jackson, Miss.
Jacksonville, Fla.
Lincoln, Nebr.
Los Angeles, Calif.
Macon, Ga.
Madison, Wis.
Memphis, Tenn.
Milwaukee, Wis.
Montgomery, Ala.
Nashville, Tenn.
New York, N.Y.
Norfolk, Va.
Oakland, Calif.
Philadelphia, Pa.
Pittsburgh, Pa.
Providence, R.I.
Raleigh, N.C.
Richmond, Va.
Roanoke, Va.
Rockford, Ill.
St. Louis, Mo.
St. Petersburg, Fla.
San Bernardino, Calif.
San Francisco, Calif.
San Jose, Calif.
Savannah, Ga.
Scranton, Pa.
Shreveport, La.
South Bend, Ind.
Spokane, Wash.
Stockton, Calif.
Tennessee—State perspective
Toledo, Ohio
Tulsa, Okla.
Washington, D.C.
Wichita Falls, Tex.

City Summaries

A total of 54 cities responded to the survey and summaries of their responses follow. A total of 11 cities reported no energy-related effects on unemployment, predominantly in the South and Southwest regions and isolated areas of high growth or absence of energy-related industries in the area; the majority, 29 cities, had some minor effects and analyzed expected short-term effects for the remainder of 1974 (at least four cities are expecting some significant impact) and 14 cities had quite significant increases in unemployment.

An appendix is attached, with tables showing data,[1] gleaned from several cities to further illustrate specific problems and outline specific industries where unemployment has been experienced in both minor and major ways.

Akron, Ohio

As of late December 1973, about 2,200 persons in the three county labor market area were laid off due to the energy shortage and still remained close to that level at the end of January. These layoffs represented both direct and indirect effects, the indirect effects being

[1] Where data are available from employment security special reports on new "fuel related" unemployment insurance claims, it should be understood that additional unemployment has occurred as a result of long-distance commuters unable to obtain gas to reach work and no alternative mode of transportation is currently available, and this reason for unemployment is unacceptable for unemployment insurance claims. This problem is currently being examined by the Department of Labor Energy Task Force, but no quantitative measure of the extent of this problem is yet available. This task force will file an official report on manpower aspects of the energy crisis to Congress by Mar. 31, 1974.

the more serious. Direct effects have resulted in layoffs of truckers, service stations closing, elimination of service station night shifts, and reduction in air passenger travel. Indirect effects appeared as decline in large car sales, and shortages of essential production materials derived from petrochemicals, leading to layoffs of 1,400 to 1,500 production workers from a car stamping plant, as well as car salemen, repair personnel, et cetera.

Petrochemical shortages have resulted in layoffs in small manufacturers of plastics, rubber products, soap, adhesive, steel fabricators, et cetera. The rubber tire industry, although declining, still represents a sizable portion (41 percent) of the area employment, and if miles driven continually declines, because of acute fuel shortages of possible rationing, further reduction in rubber demand will ensue. Other layoffs from plants just outside the labor market area affect the area itself, because those unemployed reside within the labor market area and will be collecting unemployment compensation there.

If the energy situation reaches a more critical point where most manufacturers cut capital investment in new machinery, further employment reductions would result, bringing the area unemployment rate to over 6 percent—the current estimated rate is 4.4 percent. If the layoffs are only temporary, most semiskilled and skilled unemployed will be reabsorbed into the economy, but if consumer buying habits permanently shift from large cars—for example—experienced semiskilled and skilled operatives will have difficulty being reabsorbed into the local labor market.

Allentown, Pa.

Energy crisis impact on area appears minimal. Steel and electronics industries are not visably affected. However, the knitting industry has experienced a reduction, resulting in approximately 20 to 25 unemployment claims per week.

Amarillo, Tex.

A check with local resources and the Texas Employment Commission revealed no energy-induced employment lay-offs at the present time in the Texas Panhandle.

Baltimore, Md.

At this time, the Baltimore area has not experienced significant increases in unemployment directly related to the energy crisis, according to employment security sources. Only 1,800 unemployment insurance claims in the State of Maryland are directly attributable to the energy crisis, representing less than 4 percent of the total unemployment insurance claims. No major layoffs have been reported, and unemployment is scattered among occupations such as service station attendants, car dealers, construction workers, and airline attendants.

However, a prolonged energy crisis may in fact cause significant problems; and an input-output model of the Baltimore area economy developed by the regional planning council is currently being used to estimate the potential effects of the energy crisis. The results of the study show that a significant impact could occur.

The input-output model is being used to examine the implications for local industry and employment of general economic trends and of different assumptions about energy availability. An input-output model is designed to reveal the interdependencies of the economy of an industrialized area such as the Baltimore SMSA. Although the data base of the model is for 1968, the relative magnitudes and directions of the impacts of various energy shortfalls can be indicated; both the primary and secondary effects of energy scarcity in terms of dollars, total job losses in various occupations, and job losses in specific occupations have been examined.

Although no short-run shortfall of electric power is expected because of voluntary conservation and although the natural gas supply should be adequate to serve the needs of existing industrial and commercial users, the limited petroleum supply will affect users to various extents. For example, output in steel and chemicals could be reduced by 5 percent, air transportation by 15 percent, and retail gasoline sales by 25 percent. Other assumptions, such as changes in consumer preference, can be introduced into the model as needed.

The overall impact of the energy crisis may reach $500 million with a 2.5 multiplier causing 9,500 direct lob losses and a total loss of 19,800 jobs—20 percent in the service sector. This distribution is similar to the overall occupational structure. The gasoline shortage alone could cost 1,000 jobs directly and 2,500 to 3,000 with the multiplier in effect. Thus, the energy crisis may have definite adverse effects on the Baltimore regional economy.

Baton Rouge, La.

The Baton Rouge labor market area has experienced only a small increase in unemployment insurance claims, directly and indirectly resulting from the energy crisis. Since a large portion of the labor force in the area is involved in the production and refining of fuel resources, this industrial sector is "enjoying" an increase in activity because of current pressure to increase fuel production. In addition, the Baton Rouge area is "enloying" a significant construction boom and is one of the fastest growing cities in the South.

Most layoffs which did occur in the area were concentrated in the transportation and service stations areas (drivers, salesmen, mechanics and general laborers), while some layoffs in the chemical and allied industries occurred, as did drops in average weekly hours worked, which reduced the average weekly earnings in some petrochemical industries.

Bridgeport, Conn.

The effect of the energy crisis on the Bridgeport employment situation cannot be measured in terms of what has happened, but by what almost happened and still could happen. The Bridgeport labor market area is currently experiencing one of the highest unemployment rates in the Nation, and is an economic development area. In early January, a firm employing 1,000 persons was in danger of immediate closure because of lack of supply of a relevant petrochemical product. Only due to the mayor's, the Governor's, and two Senators' efforts was the problem at least temporarily alleviated.

Not only Bridgeport, but thousands of jobs within the State of Connecticut whose employment rests on a steady supply of petrochemicals could have been severely affected. It is, of course, difficult to determine whether the problem of petrochemicals affecting so many industries throughout the United States is a result of the energy crisis, oil company manipulations, overexportation of those products, or black marketeering on the part of suppliers.

As a result of pressure by Connecticut elected officials, and others, Cost of Living Council and the Federal Energy Office attempted to lift controls and alleviate a potentially serious situation, although it is expected that planned full production will still not be possible. Production of petrochemicals is now expected to increase, monitoring of supplies to firms and reduced exports will take place, and the anticipated 15-percent shortfall in basic petrochemical materials will be reduced, but by how much is not yet determined.

Cedar Rapids, Iowa

The manpower staff performed an analysis and survey of their labor market area, but no significant or measurable changes in the unemployment rate directly attributable to the energy crisis are foreseen. However, the situation is being continually monitored and any future changes will be transmitted.

Charleston, W. Va.

The Charleston area has not experienced any energy-related unemployment as a real factor in the labor market area, nor has there been real noticeable trends toward the future impact of the energy crisis on unemployment.

This situation could be attributable to the fact that in the midst of an energy crisis, coal is plentiful in West Virginia. The area anticipates that despite all the conjecture and speculation the coal industry will "boom" as a result of the energy crisis.

An example, of how the energy crisis unemployment claims have not been a factor in the unemployment of the area, can be witnessed by the latest weekly report of selected unemployment activities regarding the energy crisis. According to this report for the week ending January 18, 1974, there have been only 16 unemployment claims made as a result of the "energy crisis" since December 1973 in the Charleston SMSA area (Kanawha County). Only 5 of the 16 claims were made during the week ending January 18, 1974. There are currently 11 continuing claims in the Charleston area at present as a result of the energy shortage.

Chattanooga, Tenn.

The Chattanooga area has experienced new unemployment insurance claimants of about 250 persons, directly attributable to the energy crisis, and concentrated primarily in fiberglass boat building industries, with smaller numbers from gasoline service stations and trucking industries. These layoffs are expected to be offset by increases in energy production and equipment and manufacturing industries (i.e. Tennessee Valley Authority construction program).

However, it is anticipated that the Chattanooga area will continue to feel the effect of the energy crisis more and more because of the inability to receive raw materials for construction and manufacturing. Some of the industries are already feeling the pinch of delayed shipments of parts and equipment needed to continue production or construction. The continued shortage of petroleum based products critical to the manufacturing process and energy producing companies is expected to worsen in this area in the future. (For a further elaboration of expectations in the State of Tennessee, see the summary of an academic analysis of energy effects in Tennessee in the near future.)

Columbia, S.C.

Some unemployment can be expected in the manufacturing sector This unemployment should be minor (e.g. 200 to 300 persons), but i fuel shortages become severe, then the textile industry using oil derived polyesters would be affected and severe shortages could cause as many as 1,000 persons to lose jobs.

Energy-related Government spending could absorb many of those unemployed. Two factors prevent the Columbia SMSA from being too severely affected by the crisis: (1) the primary employer is Government; and (2) industries in the area are traditionally labor—rather than energy-intensive.

Only in the case of severe shortages would the weekly payroll loss be greater than $100,000.

Columbus, Ohio

The Columbus manpower staff analyzed the Columbus labor market situation with respect to the effects of the energy crisis on employment and unemployment. Excerpts from their summary report to the Department of Labor are shown below:

> Central Ohio plastics industry anticipate 20 percent cutback for 40,000 workers in 1974 (8,000 full-time equivalent employees) due to shortage of plastics and increased costs of materials.
>
> A division of General Motors laid off 130 workers out of 4,000 because of cutbacks in other GM plants because of the energy crisis.
>
> A glass firm with 1,800 workers may have to reduce its workforce, if natural gas allocations are cut and production goes down.
>
> The statewide unemployment level is less than half the level 2 years ago, but 10 percent fuel oil reduction could cost the State 15,000 to 30,000 jobs.
>
> Ohio auto plants have been producing compact, rather than standard sized cars, so that fewer jobs will be lost in this industry compared to the significant impact in Michigan.
>
> Building industry jobs will be cut, if fuel for space heaters at construction sites is unavailable.
>
> Over 500 local drivers of bulldozers, cranes and other heavy equipment are idle due to the shortage of fuel.
>
> Bricklayers and iron workers unions have reported layoffs because of fuel shortages.

The impact on existing manpower programs has also been investigated. Training programs independent of business and industry are proceeding as planned, but the fuel shortage may adversely affect placement once training is completed. Programs dependent on private business and industry show no clear pattern—one on-the-job training program is having difficulty in placing clients in the private sector for the first time, while another program developed new marketing techniques and is having the best placement record ever.

Duluth, Minn.

Analysts from the area do not expect much of an immediate energy crisis impact since the area is not highly industrialized, but certain potentially susceptible areas have been identified for the secondary effects of a prolonged energy shortage, effects expected to appear after January. They are:

Cement plant—layoffs of 150 to 200 persons, owing to lack of further funds for highway construction.

Coke plant—150 to 200 persons. Coke is a steel plant input; if steel demand falls, the coke oven will no longer be needed.

The developing tourist industry is not insignificant in size, dependent upon the season (hotels/motels employ from 750 to 900 workers and eating/drinking establishments have 1,900 to 2,250 employees). If gas rationing is imposed, employment could be kept to low levels in the industry, resulting in layoffs of 500 in seasonal heights.

Retail trade employment is currently 8,540, and 24 percent reduction (1,708 jobs) could result if Saturday and Sunday closings for energy conservation became a reality.

Shipping industry important to Duluth, and if steel tonnage shipping drops, layoffs would occur.

Two colleges and one private high school enrollments could drop affecting a further 100 jobs.

If the energy crisis reaches the level of severity where the above industries are affected, layoffs of 2,700 persons would raise the unemployment rate for the city of Duluth to about 10 percent.

Elizabeth, N.J.

Based on several news articles sent by the mayor's staff, the Elizabeth, N.J. area has experienced a sizable unemployment rise because of the energy crisis.

The total jobs lost in the State of New Jersey by the second week of February was 10,285 and the manufacturing sector and automobile-related industries were hardest hit. Immediate effects of the energy crisis on the job market were worst in Union County where employers have reported laying off 4,500 workers because of gasoline or raw material shortages (Star-Ledger February 10, 1974).

A survey of employers in Union County was taken by the Eastern Union County Chamber of Commerce which showed varying responses. Over 100 firms responded (including the Linden, N.J., GM assembly plant laying off 2,200 on a temporary basis). Fuel shortages caused layoffs of nearly 1 month in 14 firms, for 548 persons; 19 firms would soon close because of petrochemical shortages, while many said their operations would be curtailing from 10 to 25 percent. Thirty-five firms were experiencing shortages of other raw materials perhaps not directly attributable to energy but symptomatic of the economy today (i.e. strikes, transport difficulties, exports, environmental laws, lack of imports, price controls, market conditions). If the winter becomes more severe a follow up survey will be made.

Erie, Pa.

A survey of Erie's unemployment picture indicated as of January 26 only 26 energy induced layoffs for all of Erie County. There have been no reductions in the work week and the following figures bear out an interesting fact in overall Erie industry. The month of December 1972 showed an average of 42 hours per week per employee while the same month in 1973 showed an average of 42.6 hours worked; an increase of 0.6 hours. The only industry operating under 40 hours was the food service production at 38.1. There have been no payroll losses. At this time it is not feasible to project the future unemployment picture regarding layoffs, pay loss, and so forth related to the energy crisis; but as of now there is little significant change in regards to Erie unemployment and the energy crisis.

Flint, Mich.

Flint, as might be expected is going to have a serious problem in the coming months. The employment service labor analyst for the Flint Labor Market Area reports a 10,000 energy-related unemployment level for the month of January 1974 and payroll losses per week total over $2 million (see appendix). Transport and motor vehicle equipment, fabricated metals, trucking and services are the industrial areas affected.

In addition to the average weekly unemployment rolls, there has been a significant reduction in the workweek from 42.8 weekly hours in October 1973 to about 37 hours in January 1974; the normal sesasonal week hours are between 40 and 41 per week.

In addition, General Motors has reported that in February one of their plants will close entirely, representing an additional 11,700 unemployed workers and if these persons are recalled in March, it will be for half days only.

It has been estimated that the unemployment rate for the Flint Labor Market Area for January 1974 is in the order of 12 percent and the estimated rate for February is 15.

On the basis of past severe strike experience in the Flint area, it is determined that the ripple effect on the rest of the economy will be considerable.

When General Motors is off, nobody in the area spends money and retail sales will go down badly, and no new construction will be in evidence. Throughout the spring months, the unemployment rate will remain as high as in January and February, because of the ripple effect, and this forecast is based on the 1970 General Motors strike experience.

Fort Wayne, Ind.

Following an extensive survey of the energy-related unemployment problems, it was determined that no energy-related unemployment claims have occurred. The present unemployment rate is 2.1 percent for the labor market area, with a slight seasonal increase expected for February. Early in February 1,000 employees were laid off at International Harvester due to slow arrival efforts because of independent truckers slowdowns, but this has passed and hiring is again taking place.

Fresno, Calif.

Only a small impact on unemployment has occurred to date in the Fresno area with spotty layoffs from service stations and truckstops: Only 6 percent of the total unemployed in Fresno County can be attributed to energy shortages, and only 1 percent of total unemployment insurance benefits have been paid to sufferers from the energy crisis.

However, should the shortage carry on into late spring, the local economy would begin suffering from ripple effects but to what degree is difficult and too premature to determine.

Greensboro, N.C.

The proportion of persons in the Greensboro area who are out of work due to the energy crisis is small. At end December 1973 an estimated 1,970 persons were unemployed, out of a civilian work force of 134,850, or a 1.5 percent unemployment rate. At that date, only 10 persons had filed unemployment insurance claims because of energy crisis job loss, and since the Greensboro labor market remained tight, additional persons may have been laid off but were able to find another job and were not included in the unemployment security tally.

Lack of available data precludes the feasibility of estimating energy-related unemployment likely to occur in 1974. If the crisis and its subsequent shortages of fuels and related products becomes no more serious than now, the effect on employment will be minor. In the Greensboro area there have been no planned expansions which had to be curtailed because of the energy crisis. And, since the area enjoys a broadly diversified economy, cutbacks in one sector, unless substantial, could be absorbed without major effect.

Future developments could change the employment picture. Several industries in the area are dependent upon natural gas for their energy source, and if curtailed could have a significant impact on employment. In addition labor market analysts expect some economic slowdown in 1974 after strong growth in 1972 and 1973, and materials shortages and inflation are the most pressing concerns of the area.

Hartford, Conn.

There is no specific information from a city like Hartford, since there are no large manufacturing concerns that would be directly related to the energy crisis with the exception of areas such as Bradley Field (an international airport), and United Aircraft Corp. that may have difficulty in obtaining certain materials that would result in certain layoffs. The material chain or interindustry dependency is difficult at best to determine, and is always based on certain assumptions in input-output analysis.

Subjective analysts indicate there is probably some energy crisis related unemployment, but no way to specifically quantify the amount, although a marked increase in unemployment claims was experienced within the last few months, definitely more than normal seasonal fluctuations—based on the month of December, since January figures are as yet unavailable from the State office.

There are a substantial number of long distance commuters in the Hartford labor market area and certain numbers of persons may be leaving their places of "employment and becoming unemployed" simply because of unavailability of gasoline, but this is not a legitimate reason for obtaining unemployment insurance—it is assumed that if a job is offered the person will be able to get there—and total unemployment claims may be an understatement of the problem.

Huntsville, Ala.

No direct layoffs attributed to the energy crisis have taken place. Two area industries (gasoline engines and automobile production) at the beginning of the crisis were hesitant to pursue planned expansions, but have now done so, and another auto plant scheduled to open in the spring of 1975 will now open 1 year earlier.

A minimal number of service station attendants are currently unemployed but this is not attributed to the energy crisis but part of the current local trend of self-service operation stations.

Jackson, Miss.

The number of persons laid off by the end of January in the Jackson labor market area totaled 438, and involved auto-related and plastics or chemical-related industries. The total payroll loss per week is in excess of $56,000. (See appendix for specific data.) Some of these companies have indicated that full responsibility for the layoffs may not be totally due to the energy crisis, since the general economic condition and other factors could be considered partially responsible. For example, the inability to obtain materials such as steel and raw materials has been cited.

A number of larger employers have adopted a day-to-day wait-and-see attitude with some alternative plans that can be put into effect rather quickly if the energy crisis affects them adversely. Some employers report that instead of layoffs, they are not filling the positions that become vacant at this time. It is felt that only one (auto wiring) large company will be drastically affected by the energy crisis.

Jacksonville, Fla.

The mayor of Jacksonville has set up a Manpower Energy Crisis Task Force to apprise him of energy crisis related unemployment. A survey of Jacksonville area businesses and industry was taken in December on the grounds that Federal guidelines on consumption would be announced then.

Slightly less than half the respondents felt the crisis would cause work schedule readjustments (except finance, real estate, and insurance with no adjustments, and agriculture with significant adjustments). If adjustments were necessary one-third predicted a reduction in volume and type of services; nearly one-third would reduce employees and about one-fifth predicted a reduced workweek; of course varying by the major industry sector. Many expected businesses declined because consumer budget reallocation and decreased product demand, and about 40 percent expect material shortages (primarily in construction, services, and wholesale-retail.

In those firms planning to reduce employees, the range of reduction was 5 to 25 percent, with areas of highest reduction in construction and manufacturing. (Most firms indicated that part-time employees would be cut first.) In terms of reducing services, firms using outside firms for auxiliary services would drop this aspect prior to releasing employees.

The industry and business survey ranked the seven energy reducing measures in order of priority. They are:

1. Conservation measure.
2. Reduce frequency of delivery.
3. Eliminate part-time help.
4. Curtail hours.
5. Reduce/eliminate reliance on outside services.
6. Eliminate delivery of service/goods.
7. Reduce full-time employees.

Industry has begun conservation measures, which at this time cause them to believe that they will not have to reduce many employee positions. But if they are forced to reduce employees, part-time employees would be terminated, resulting in an increase in underemployment, as many low income workers subsidize their incomes with part-time jobs. Full-time employees would not be significantly affected at first, but if the economy is cut back by loss of part-time job earnings the "ripple effect" will undoubtedly cause full-time employment to be reduced as the year progresses. Because Jacksonville is a more industrial than tourist economy, the impact of the energy crisis is not yet fully specified and more precise guidelines are issued, industry will have a better picture of what it will be required to do.

Lincoln, Nebr.

No reported layoffs or unemployment due to energy crisis as of February 1974.

Los Angeles, Calif.

Figures released by the employment service indicated that the largest number of claims for unemployment benefits were persons working in the mobile homes industry. A major automobile manufacturer has reverted to a one-shift operation and in so doing indefinitely laid off 1,970 employees. Due to large car sales lag an additional major manufacturer laid off it's entire 2,350 employees.

Preliminary statistics indicated a loss of 4,000 jobs in Los Angeles County. That figure is expected to reach as high as 25,000 by the summer. No specific figures but heavy layoffs were reported in the recreational vehicle industry. A predicted 15-percent increase in unemployment insurance claims was caused in part by an order that commercial plants cut back on power expenditures by 20 percent.

Macon, Ga.

The city of Macon, Ga., and the counties constituting the labor market area are fortunate in experiencing no energy related unemployment. This is an area with an adequate supply of electric energy, natural gas, and coal. All industries are working to normal capacity, less than 1 percent of homes heated by oil, and no shortages have to date been experienced. In addition, no shortages of gasoline in major or smaller independent dealerships have been evidenced and price increases have been averaging only 9 percent for a gallon of gas. No future layoffs are predicted and a Japanese-based plastic zipper manufacturing firm is currently opening in the area, so no shortage in the petroleum based products for plastic production has occurred in this local area.

Madison, Wis.

After consultation with various knowledgeable groups and organizations concerning the energy crisis impact, the concensus was that unemployment will increase in the Madison area. Most persons, however, were hesitant to make definite predictions on the effect for the following reasons: (1) Government is the largest employer in Madison and most effects will thus be indirect and slow to occur; (2) if the Arab countries turn the oil back on, most shortage effects will disappear; (3) predictions are hazardous because of the uncertainties of both policies and extent of effects; and (4) Wisconsin will not be as affected as severely as other regions of the country because oil comes primarily from domestic sources.

Since layoffs in the area due to the energy shortage have already taken place, it is almost certain that unemployment will increase. Construction company layoffs occurred during Christmas because of the energy shortage, an aviation school will layoff because of aviation fuel shortages, and a plastic pipe manufacturer is unable to obtain adequate supplies of plastic.

The area is presently using available moneys to counter the effects of the energy crisis, but if the situation worsens, it will be necessary for the Federal Government to make more moneys available for public employment. Plans are being developed to make use of the money, but a complete strategy cannot be devised because the situation for the near future is still unclear. The situation in the area continues to be carefully monitored.

Memphis, Tenn.

Survey on energy related unemployment indicated that a major producer of light bulbs experienced the most severe impact. Total employees affected reached 129 while the transportation industry (primarily service stations) suffered as a result of fuel shortage.

Milwaukee, Wis.

Unemployment data, as reported to the local employment service, are recorded for the four county SMSA area. However, to date all affected manufacturers are located within the metropolitan boundaries of the city. Thus, the employment service has assumed that all individuals affected have been residents of the city of Milwaukee. Furthermore, the employment service has not correlated layoffs due to material shortages as being energy-related layoffs. It is therefore impossible to determine an accurate compilation of energy-related layoffs experienced to date by Milwaukee.

No projections have been established relative to the impact of the energy crisis on the unemployment situation for calendar year 1974.

All sources contacted indicated an inability to produce such projections at this point in time. It was thought that the impact may not be as severe on the city as in the remainder of the State. Several sources indicated that if major suppliers in other States become severely affected by the crisis, the city of Milwaukee would suffer residual effects.

The energy crisis has necessitated the layoff of about 7,000 workers statewide since November 1973. As the following indicates, 2,100 of those workers are residents of Milwaukee: in the automotive industry there are 1,730 crane helpers, press operators and production welders; 200 auto assemblers; 95 seatbelt assemblers; and 81 air-conditioner assemblers.

Montgomery, Ala.

No real impact has been evidenced in the Montgomery, Ala. labor market area because of the energy crisis. A report, dated February 1 from the Alabama Employment Service stated that no signficant layoffs have been reported or identified with the exceptions of about 15 persons (a few each in the railroad supply company, furniture manufacturing, lumber company and hotels).

Nashville, Tenn.

There is no energy-related problem at present and analysts do not anticipate any significant unemployment problems in the near future owing to the energy crisis. Ford Motor Co. has laid off 175 persons on a temporary basis—out of a total company work force of 2,400, but this represents the only energy-related layoffs. The Nashville area industrial base has no plastics, fabricated metals, mobile homes, recreational vehicles, or textiles—synthetics—which are being hit by material shortages in other areas of the country.

New York, N.Y.

Precise data were not available to show the current impact of the energy crisis in the New York area, but directly attributable joblessness is expected to remain a small percentage of total unemployment, currently at 180,000. However, two reports on the expected outlook for 1974 prepared by New York economists are summarized below.

The lackluster performance of the New York region economy during 1973 does not provide a very optimistic base from which to view the prospects for 1974.

The full extent of energy-related shortages on the regional economy is still difficult to assess. The reaction of many business and government officials contacted by the regional studies section appears to be that "no one knows." Several firms in the plastics and pharmaceutical industries, where intermediate oil products are critical, have moved to a 4-day week. Other firms are, or will shortly be reducing overtime situations. Auto makers have announced "furlough" periods, and the airlines industry has cut back on personnel. Area unemployment could well approximate the national rise to 6 percent.

Rapidly rising prices for oil and other energy sources, as well as indications of further increases in the price of food, could well push the Consumer Price Iudex up by 8 percent in 1974 in both the New

York region and in the United States. Recent increases in the wholesale price index have yet to be felt at the consumer level. The prospect of this serious rate of inflation, together with further increases in social security taxes makes the outlook for real earnings growth increasingly unlikely for both the Nation and the region.

Over the long run, the prospect of higher-priced energy favors denser patterns of development for both corporations and for housing. Out-migration from New York City of middle-income families and business firms will slow. Clustered housing and planned unit developments in the suburbs will benefit. Still, energy considerations, in and of themselves, will not cause drastic changes in land use from trends already in motion.

In the short term, New York's performance will be shaped by spillover effects from energy shortages combined with a national economic slowdown. On the plus side, New York City entered 1974 from a more solid base than in recent years. The city's 4-year decline in employment bottomed out in Spring, and employment moved sideways from then on. Total economic activity rose in spite of the minor year-to-year loss in jobs, and personal income increased nearly 7 percent to reach an estimated $47 billion.

New York City is in a good position to withstand certain facets of a national economic slowdown. Neither the auto industry nor its major suppliers is located in the city. Further, the lack of local buildup during the 1971–73 national expansion suggests that the city has no fat to be cut from operations as was the case in 1969–70.

The New York area is at a relative disadvantage in terms of energy supplies and prices. New York imports virtually all of its supplies from elsewhere in the United States or abroad, with petroleum products comprising 75 percent of its fuel requirements compared to only 42 percent for the Nation. Energy costs are already high in the region. Preembargo electricity prices are highest among 23 metropolitan areas, and further increases are in store.

New York City is in a relatively favorable position in terms of its industrial structure. None of the highly energy-intensive industries is located in the city. However, particular specialties—such as apparel, textiles and plastics—which rely on high-energy synthetics are vulnerable to bottlenecks in materials supply and higher prices. Cutbacks in the airline industry will affect New York which employs 14 percent of the Nation's total. The suburban counties enter 1974 with greater economic momentum, but with a higher concentration of energy-intensive manufacturing than New York City proper.

The region is in an advantageous situation with its mass transit system, helping to keep per capita energy usage roughly two-thirds that of the Nation. To the extent that fares are held down, commuters and city residents can counter higher gasoline prices by shifting from autos to railroads and subways.

Norfolk, Va.

Unemployment in the Southeastern Tidewater Area does not appear to have been significantly affected by the energy crisis. Some layoffs of automobile sales and service stations have occurred, but numbers involved are small and the majority of them quickly obtained other employment. The unemployment rate is currently very low for this area (3.1 percent in September 1973).

An auto assembly plant cut back about 4 percent of their work force, but was thought to be seasonal; plastic extrusion industries in the area are carrying out precrisis expansion plans; the Federal work force continues at normal levels and no unanticipated layoffs in tourist-related industries have occurred.

By July 1974 however, unemployment applicable to the energy crisis could occur in the hotel/motels, plastics (boat building), and recreation equipment industries, if petroelum products continue to remain in short supply. For the present, the overall impact has been minimal, and the area continued to experience the nominal growth as projected for the current year. A Volvo assembly plant is being opened in the area and will involve a growth in jobs in an industry where cutbacks normally take place as a direct result of the energy crisis.

Oakland, Calif.

A full assessment of the impact of the energy crisis is unavailable at this report time, but the manpower staff is continually monitoring and assessing the situation.

Philadelphia, Pa.

The employment service has been sending weekly reports to the manpower planner in Philadelphia which give specific numbers of unemployment claimants directly related to the energy crisis (initial claims, continued claims, and persons recalled) by specific industry two-digit code. The table in the appendix is a summary of the weekly reports since December 14.

As can be seen, the volume of direct energy impact on unemployment is not significant, in terms of the total Philadelphia work force, or even level of unemployed. The initial claims though small follow much the same pattern as is expected from reading news reports and special studies of the energy crisis—primarily in retail trade, some chemicals and plastics, and primarily in service stations and related auto sales and repairs. However, as can be noticed toward mid-January, even though still small, several firms had to lay off a small number of workers because of shortages of supplies from suppliers in other parts of the country. Thus, the direct impact of the crisis may be small, but the buildup and repercussions of a lengthy series of shortages will be more far reaching, and more long term.

Because of a personnel crunch, the ES office is unable to determine occupations of the energy-related unemployed claimants in tabular form not to estimate the direct payrollers.

Pittsburgh, Pa.

The energy crisis has begun to make significant inroads into the Pittsburgh area labor scene as of the end of January. Increased claims activity, stepped-up layoffs and more widespread infiltration of industry groups have occurred.

During the December 31, 1973, through January 25, 1974 report period, a total 1,541 initial U.C. claims filed in local offices of the Bureau of Employment Security in the Pittsburgh labor market area were caused by the energy crisis. This number was a marked increase of 978 over the 563 claims filed during the December report period. An analysis of the claims showed a distribution among 16 major industry groups. The industries hardest hit with initial claims were: fabricated metal products (281), stone, clay and glass (187), car dealers and gas stations (167), airlines transportation (147), and transportation equipment (140). Of the 1,541 total, 435 claims could not be identified by a specific industry group code, but were scattered among industries including construction, stone, clay, and glass and transportation.

Lack of materials, fewer sales, and fuel shortages continue to be the principal reasons given for energy crisis related layoffs. The material shortage is the result of either cutbacks in transportation services or the use of petroleum as a base in the production of the material. Reductions in sales have been felt primarily by big car dealers.

Providence, R.I.

The total number unemployed in the city of Providence caused by the energy crisis is 687 persons, which represents 0.8 percent of the work force and nearly 12 percent of the 5,773 unemployed population. In addition naval civilian personnel cutbacks (426 Providence residents), while not directly related to the energy crisis, will further exascerbate the problem. (See appendix for specific data.) It is expected that as the duration of the crisis lengthens, data should become more specific and informative.

Raleigh, N.C.

The energy crisis has not yet directly caused a change in the unemployment rate for the area, but in the past few weeks the area has been significantly affected by gas shortages. Part of the reason was the closure of many independent gas companies and two major oil companies moving out of the State just prior to the start of the energy crisis. No other industries in the area have closed because of the crisis.

The largest number of people affected by the energy crisis relative to employment are those in jobs considered secondary jobs. Persons employed by gas stations have had a reduction in the hours worked per week, since stations are generally open only 3 hours per day. In addition, many clerks in department stores have had a reduction in their workweek because night shifts have been eliminated. Although the crisis will not impact directly on the unemployment rate, a significant amount of underemployment is expected to result.

Richmond, Va.

Overall effect of energy crisis in area is minimal. Only substantial workweek reduction occurred in the box manufacturing industry primarily due to elimination of overtime. A noticeable reduction in the wholesale/retail automotive sales and hotel/motel trade appeared due primarily to a reduction in moonlighting.

Roanoke, Va.

Actual layoffs to date in this labor market area owing to the energy crisis have not been as intense as predicted at an earlier date by area manpower staff. However, layoffs by mid-February had reached about 700, partial layoffs over 200 and planned expansions in firms which were either canceled or postponed total over 1,000 jobs (see appendix). The employment service reports that this increase in unemployment insurance claims can, for the most part, be explained by seasonal movements, but a drop in "permanent" job orders at employment service offices appears heavier than usual.

Shortages of supplies of petrochemicals (about 30 percent of the total demand is being received) has been evidenced, and it is assumed that current efforts to rectify the petrochemical situation at the national level will alleviate the situation but not for several months, by which time industries may have to shift their factor mix because of permanently increased costs of supplies.

The general atmosphere of firms in the area is an extreme concern if not fear, that shortages of construction materials and expected cost increases in both materials and transport will cause a reduction in construction activity through the summer months.

Although no hard data are available, the following points, based on many sources, were made by the manpower planning staff in the area and could serve as guidelines for pinpointing possible critical areas in time to make plan or program changes within the area:

> The extent of severity is a function of available raw materials; the duration is clouded by lack of data. Focus of attention has been on gasoline, fuel oil, and other middle distillates with the exception of the propane debate. The latter question mav have been resolved by making everyone a priority user.
>
> The importance of construction is vital. The amazingly low reported unemployment rate for this area can be largely attributed to this industry. Availability of materials again will influence the position within the ranges the number of unemployed will reach.
>
> Effects of transportation difficulties and rising costs in the face of economic upheaval and supply shortages may become a factor. These problems are unpredicatable, and trends will be followed with the help of local economists.

Expected effects on the Roanoke area labor force by the end of 1974 have been estimated by the manpower staff for the two State planning districts in the labor market area. In one district, an overall reduction of workers will increase from 3,000 to 6,000 bringing the unemployed total to 5,000 to 8,000 with a corresponding unemployment rate of 5 to 8 percent. Disadvantaged persons will be over represented in the layoffs, reflective of the increasing effectiveness of manpower programs. The effect on clerical personnel has not yet been determined, but will probably maintain the current pattern—demand for steno skills, but sharply slackened demand for general clerks, file clerks and nonstenographic secretaries.

In the other district, an increase of 1,000 or more unemployed persons is anticipated and the corresponding rate of unemployment would be 4.4 percent or higher. Construction in this planning district is vital to the economy, and there is less opportunity to absorb new employees.

Rockford, Ill.

The most telling effect of the energy crisis has been a temporary layoff at local auto assembly plants of 5,200 persons, which was the major factor in the rise of the unemployment rate from 3.1 percent in December 1973 to 6.7 percent in January 1974.

The outlook for 1974 is clouded at present due to the energy crisis. The local office anticipates an overall reduction in employment with a corresponding rise in unemployment for 1974. The degree of the fuel shortage will have a correlating effect upon economic conditions in the Nation as well as the local area. Unemployment dropped sharply during February following resumption in production of the automobile assembly plant. Despite this, joblessness is expected to remain above 4 percent during the spring. Overall, employers are rather optomistic despite impending fuel shortages.

The following effects in the Rockford area due to the energy crisis are expected to take place:

Shortage of fuel supply for heating and processing.

Reduced demand for products manufactured in the area because of operational reliance on energy.

Suppliers of subassemblies used in manufacture of finished product which rely on energy for operation will experience reduced demand.

Area manufacturers whose raw material usage is based on petroleum derivatives may be affected adversely.

Area manufacturers whose raw material requires a great amount of energy to produce may cut back.

The transportation industry which moves raw materials into the area and delivers the finished product to buyers is being affected by energy supply and fuel costs.

Area dealers of recreational vehicles are pessimistic about sales.

St. Louis, Mo.

Energy-related unemployment in the St. Louis labor market area has, by the end of February, reached nearly 7,000 persons. Of this number 4,600 were in durable goods manufacturing, over 500 in nondurable goods manufacturing, and 1,700 in nonmanufacturing (primarily service stations). See appendix for details.

As St. Louis is continually confronted with increased layoffs in area auto assembly plants, a further impact is anticipated for related industries.

St. Petersburg-Pinellas County, Fla.

The entire economic base of the county is composed of the tourist industry and the housing industry. There has been only a slight reduction in tourism due to the energy crisis—not exceeding 10 percent. Most people seem to be substituting the airplane for the car. The county has filed suit against the Federal Energy Office, disputing its current gasoline allocations, based as it is on the 1972 base year. The county argues to base year should be more recent to account for growth in the county in the last 2 years.

The unemployment rate for the county is very low; it has been 1.2 percent for the past 2½ years. At the most the rate has risen to

1.8 percent in the past 3 years. If fuel continues to be short, however this figure is expected to go up.

Unemployment claims have gone up slightly; generally the unemployed have been finding jobs within 2 weeks, however.

County government currently has a 10 percent vacancy rate (normal usually around 5 percent). These openings are gradually being filled by more qualified applicants because of some shifting in the labor market.

Pinellas County's economic stability is unusual in part because of the large percentage of its population that is retired, and living on a fixed income.

San Bernardino, Calif.

In early November the San Bernardino Manpower Area Planning Council formed a task force to assess the impact of energy shortages upon employment and manpower training programs, involving a cross section of qualified representatives, and the group was to actively explore all employment related aspects of the energy shortage, and reports were to be issued biweekly.

The impact of shortages on certain industries within the planning area was immediate and quite severe in some cases. In certain other industries, the impact was minor, and in still others the impact will be delayed and as yet undiscernable.

The speed limit of 55 mi/h., travel curtailment and voluntary rationing accounted for 500 to 1,000 layoffs of service station operators and attendants; more computerized carpooling systems may result in further cutbacks.

Severe effects have been felt in mobile homes, recreational vehicles, and plastics manufacturing, and retail gasoline marketing. About one-third mobile and recreational vehicle manufacturers have suspended operations, the layoffs over 500 employees.

It is anticipated that all existing manpower programs will be affected to some extent as job openings and particularly entry-level jobs will be restricted owing to tightening of labor market.

It was assumed that the seasonal upswing of Christmas spending postponed the impact on motel/hotels, recreational centers, and other related areas. Petrochemicals were expected to have delayed but noticeable impact on secondary or dependent industries.

Task force methods included daily survey of local newspapers, employer surveys, questionnaire completed by all recent unemployment insurance claimants, with parallel private sector assessment, and special survey of mobile home industry. The biweekly reports will be valuable in changing manpower training programs, in terms of available placements or job possibilities.

In a second report the task force reported that new industrial areas not previously identified are now showing evidence of unemployment. Some indications point to a small, but perhaps emerging, new impact upon the local construction industry, down 25 percent (seasonal) from the previous quarter and 2 percent from this time last year. This drop is considered low by local building trade unions who predict that updated data will reflect an over 5 percent drop with roadwork/freeway construction severely hit. All building trade craftsmen will be somewhat affected.

San Francisco, Calif.

The city is primarily experiencing a reduction in employment in service stations and garages. It is projected that there will be considerable impact on the trucking business, significantly affecting small trucking contractors. While manufacturing, trade, transportation and tourist-related occupations were most visibly affected, some 400 bay area airline employees have been laid off. However, on the whole, substantiating statistics are not available at this time.

San Jose, Calif.

Although the impact of the energy crisis on unemployment is relatively minor, the initial unemployment claims because of the crisis are fairly steady each week, and are concentrated in automobile industries, services (i.e. gas stations), transportation equipment, wholesale and retail trade and public utilities (see appendix).

Local analysts anticipate that a continuation of the energy crisis at current levels will significantly increase employment in the labor market area (Santa Clara County). Area economists predict a 1 or 2 percent rise above the present unemployment rate of 4.8 percent. If the unemployment rate should reach 7 percent during 1974, nearly 35,000 persons in the county work force would be unemployed.

In the near future several thousand workers will suffer cutbacks in the workweek, primarily in automobile assembly plants. In addition normal expected growth in such areas as transportation equipment will probably not occur.

Savannah, Ga.

Although no data are currently available on unemployment levels as a direct or indirect result of the energy crisis in this labor market area, the results of an employer survey in late November 1973 indicates expected effects of the gasoline shortage.

The total respondents to the survey represented 40 percent of the area employers and 26 percent of the area employment. Of this total number of respondents, one-fourth had plans to counteract expected shortages, the remainder had no plans at all. Again, about one-fourth anticipated shorter workweeks, layoffs and reduced production ranging from 10 percent reduction to total closure. In terms of commuting distance a total of 1,300 employees in the responding firms commute 20 miles or more one way to their job sites (a potentially significant problem); and while definite answers could not be given on reduced gasoline consumption on business activities, most employers felt that some difficulties would arise and would take a wait and see position.

Scranton, Pa.

Statistics indicate that while some workers are being adversely affected by the energy crisis, others are being called back to their jobs. Unemployment insurance claims at mid-February climbed to 4,473—an increase of 169 over previous weeks. New claims, identified as "fuel claims" for most layoffs, and increased fuel claims to a total of 800. While numerous firms have been affected to some degree, a review of claims on the whole indicates that 26 percent were in the construction industry; 51 percent in manufacturing; 9 percent in wholesale and retail trade; 6 percent in utilities; and about 8 percent in services. Fuel claims show a distribution of 11 percent in construction, 60 percent in manufacturing, 16 percent in trade, 10 percent in utilities, and 2 percent in services. The job sector, depressed by the economic uncertainties of the energy crisis witnessed reaction rather than action as new job openings, job vacancies, and job placements decreased although job opportunities remain abundant in many diverse occupations.

Shreveport, La.

The industrial layoffs occurring because of the energy crisis in the Shreveport area, while small relative to the total level of unemployment (50 layoffs in car battery production and gasoline service stations plus 25 partial layoffs in service stations) may be symptomatic of both area and national uncertainties.

For example, the mayor of Shreveport wirtes that "* * * during the week of 4–8 February, 25 of the 388 unemployment claims made were energy related. This is a documented 6.5 percent energy related unemployment figure but with the uncertainty that seems to pervade the Nation, I fear that actual energy related unemployment is much higher than our figures indicate and if the reduction in activity of Western Electric becomes more severe, this area will be in critical need of Federal assistance. We are optimistic of the long-range employment picture of the Shreveport area but concerned over the near future."

Western Electric Telephone Co. furloughed 3,000 employees (at half pay) for one week owing to poor telephone sales, and a steel works was forced to delay expansion due to steel shortages.

South Bend, Ind.

During series of discussions with the local employment service, it was determined that definitive information was unavailable and employment security personnel were hesitant to forecast the probable energy crisis impact. As a result, local manpower analysts made some assumptions, and are indicated in the appendix. The impact appears to be minimal in that most production slowdowns are attributed to parts and supplies shortages, while hiring has not suffered significantly.

Spokane, Wash.

The December 1973 energy-related layoffs were 320, and by mid-January reached 450. In addition, expected growth of 400–500 jobs in the 1974 period will not take place. Affected industries include highway construction, tile, plastic containers and tubing manufacturers, trucking, wholesale grocers and petroleum wholesalers, motor vehicle dealers, tire-battery-accessory dealers, service stations and household trailer dealers, as well as auto rental outlets.

The three occupations most affected have been truck drivers, sales personnel and assemblers. Consumer spending patterns have had an impact on full-size cars, and recreational vehicles, not only relative to sales staff, but repair staff, and clerical staff in those business operations. Reduced working hours and days in service stations have resulted in layoffs of attendants and auto mechanics.

Petrochemical shortages have resulted in temporary layoffs of goods production, while diesel fuel shortages have laid off many truckers. (December layoffs were 318, of which only 20 percent filed unemployment compensation claims.) Most layoffs are indefinite, although some auto and trailer dealerships may recall personnel in spring. Spokane County total employment for December was 113,200 with 9,300 unemployed representing 7.6 percent of the labor force. Special layoffs represent only a small proportion of total SMSA employment, but the prospects of recall or finding alternative employment are slim.

Stockton, Calif.

It is currently impossible to identify any unemployment as being directly attributable to the energy crisis in this area. San Joaquin County is characterized by seasonal employment (dominated by agriculture) which accounts for a high percentage of unemployment during winter months. However, there may be a potentially severe problem, if the energy crisis and consequent severe shortages persist through the spring and into the summer. Without fuel to run agricultural machinery, such as harvesting equipment, and to keep sludge pots burning during cool nights in the spring months, employment in the agricultural industry could be seriously affected.

Tennessee—State Perspective

Under a Department of Labor grant, a study was done on the expected effects of the energy crisis and the general economic situation upon the extent of unemployment in the State of Tennessee. Because there is a difference of opinion on a national basis as to how severe the extent of unemployment will be during 1974, the group found it difficult to predict and therefore fed several assumptions into their model.

Because Tennessee enjoys a large number of persons employed in primary and tertiary industries, which act as dampers to general effects of recessions on the secondary sector of the economy, in general Tennessee's unemployment rate usually lies slightly below the national average. The following table illustrates the range of possibilities, and allows some estimate for planning for crisis should any of the three models of the national economy take place:

TABLE 1.—FORECASTED TENNESSEE UNEMPLOYMENT, 1974

Consensus forecast	Tennessee unemployment rate percent	Absolute number	Unemployment attributable to energy crisis
Preenergy shortfall	4.0	777,000 to 79,000	
Model I:			
Mini recession	4.4 to 4.6	85,000 to 89,000	8,000 to 10,000.
Model II:			
Recession	4.9 to 5.1	94,600 to 98,500	10,000 to 18,000.
Model III:			
Maximum recession	5.2 to 5.5	100,500 to 106,200	23,000 to 27,000.

Insufficient information precludes a detailed estimate of the energy crisis impact, but it is estimated that the liklihood of the minirecession model will take place, while chances of a recession are 25 percent and of a major recession model about 12½ percent.

The authors think it hazardous to forecast unemployment for the State of Tennessee, much less a breakdown among urban and non-urban areas, but with the likelihood of significant error at the sub-State level, the following table illustrates the expected impact on unemployment using the three recession models.

FORECASTED URBAN UNEMPLOYMENT, 1974

	Consensus forecast	Mini recession	Maximum recession
Memphis	12,000 to 13,000	14,000 to 15,800	17,000 to 18,900.
Nashville	8,800 to 9,500	9,900 to 10,500	11,900 to 12,500.
Knoxville	5,600 to 6,000	6,600 to 7,000	7,800 to 8,300.
Chattanooga	5,400 to 6,000	6,200 to 6,800	7,200 to 7,700

Although current data are not available, a frame of reference for levels of unemployment can be observed from the latest published issue of Area Trends (November 1973).

Labor market area	Work force		Unemployed		Unemployment rate	
Chattanooga	159.8	159.1	4.7	4.9	2.9	3.1
Knoxville	186.0	184.6	4.0	5.1	2.2	2.8
Memphis	379.5	370.7	10.9	11.8	2.9	3.2
Nashville	282.1	275.5	7.7	8.9	2.7	3.2

The authors of this study for the State of Tennessee think the reality of a national average unemployment rate, while a definite possibility given past patterns, not a certainty, to be in the range of 8 percent because of three reasons; anticipated energy shortfall may not be as severe as first thought; rising energy prices will reduce energy demands, and greater efficiency in energy use is quite likely. In the short run, rising energy prices will curb production, and studies indicate a 2 percent rise in price reduces consumption by one-half of 1 percent, but even in the short run energy supplies can be used more effectively. Energy consultants, already increasing in number should, in the long run, through their advice prove the feasibility of increasing output per unit of energy input—rising energy productivity. This has been demonstrated according to the Council of Economic Advisors.

However, even in the short run and with a minirecession the additional 1,000 or 2,000 workers unemployed in a particular labor market area would have severe implications. Manpower funds through CETA are, at best, limited, and based on a slight reduction of existing possible services. An increase of 1,000 persons, even if only temporary for say 6 months, would be a considerable problem to the area, and a supplementary fund attached to CETA could alleviate a temporary problem, for without it, manpower services would be severely curtailed.

Toledo, Ohio

Overall economic forecasts for the Toledo metropolitan area are guarded because of the energy crisis, material shortages, transportation and inflation, yet the year ahead promises to see unprecedented building activity and job creation; 1973 was a good year and most business leaders believe they are prepared to withstand assaults on energy and some expect to turn these challenges into opportunities.

No foreseeable large scale layoffs exist and some area employers expect to hire. Major industries in Toledo area plan to invest $226 million in 1974 for capital improvements, centered around expansion, office space, and new industrial parks, which should create job opportunities.

Utility companies in the Toledo area think the area is better off than most in the country in the energy scramble. Toledo Edison has long-term coal contracts, and a nuclear power station is expected to be in service by 1976, and a new synthetic gas facility is expected to be in operation later in 1974.

Layoffs due to energy shortages in the area have been minor, with the exception of a brief few thousand layoff during the independent truckers' strike. Some employers may not fill openings as they occur but no large scale layoffs are expected. The largest cutback for area workers will come in reduced overtime hours worked.

Tulsa, Okla.

In relation to area's total labor force, the impact on Tulsa appears to be minimal. The biggest factor in layoffs to the automotive and transportation industries is attributed to fuel shortages in the area. Production workers in the plastics manufacturing were hardest hit, while retail/wholesale sales showed no visible decline.

Washington, D.C.

The basis of estimates of unemployment in Washington, D.C. as a result of the energy crisis are unemployment insurance benefit applications in which the claimant specifically indicated that his employment was terminated because of a shortage of energy. A total of 220 individuals, for a total 840 man-weeks, were directly affected by the energy crisis in the District of Columbia. The level was estimated from established relationships between total unemployment and unemployment insurance claimants in a continuing benefit status. Industrial estimates are based on the proportion of initial "energy" claimants by two-digit Standard Industrial Classification code.

The claimants in the special "energy" file are not regularly classified by occupation. This accounts for the unavailability of estimates by occupation. The records do indicate applicant-affiliated industry groups. Specifically, construction 29; transportation 24; retail and wholesale trade 113, service 12; Government 6, and not available 36. In the order most frequently mentioned, the groups of workers include gas station and car sales, construction, oil company, airline, car rental and food service. Some specific occupations mentioned were truck drivers, teachers, and chauffers. The assumption drawn from these facts is that the occupations affected greatest are salesmen, service station attendants, clerks, and bus and truck drivers within the industry groups mentioned.

Estimates of payroll losses are based on the average weekly earnings of persons covered under the unemployment insurance laws.

The special energy reports were initiated in early December 1973. The estimates in this report are based on the 9-week period December 15, 1973, through February 9, 1974. It is felt that this is a sufficient base for making projections for any extended period of time.

It is anticipated that a reporting system which will provide a more detailed and reliable data base for making estimates of this type will be instituted in the near future.

Wichita Falls, Tex.

Information provided indicated no considerable unemployment directly related to the energy crisis. The city has not experienced any energy-related industrial work reductions nor energy-induced layoffs.

Appendix

Supplementary Data Supplied by Cities to Support the Narrative Summary

AKRON, OHIO

[Unemployed related to energy crisis as of Jan. 31, 1974]

	Number	Weekly payroll
1. Auto sales agencies	30–40	$6,000
2. Fabricated metals (operatives, laborers)	1,400–1,500	[1] 300,000
3. Plastic manufacturer—operatives	150	20,000
4. Recreational vehicle manufacturer-assemblers	100	20,000
5. Gas stations, rest/motels serving interstates	200	18,000
6. Trucking industry (drivers, mechanics)	50	12,500
Total	1,930–2,040	370,000

[1] This is not necessarily all income loss, because some have supplemental employment.

The majority of those unemployed above are males, age 25–45 years.

No workweek reductions were evidenced in manufacturing, but hours have been reduced in many services—that is, gas stations and restaurants.

The local rubber industry, which accounts for over 41 percent of the area employment, anticipates a recordbreaking production year. However, this could change for the worse if fuel shortages become more acute and rationing is instituted.

COLUMBIA, S.C.

[Unemployment in SMSA due to energy crisis]

	Number	Payroll loss/week
1. Recreational trailer manufacturing	130	$15,600
2. New car transporter (truckdrivers)	30	3,720
3. Service stations	30	2,250
4. Construction (carpenters, laborers, welders, plumbers)	20	2,400
Expected growth which will not occur:		
1. Electronic calculators (electronic assemblers-15 training slots)	15	1,500
	225	25,470
Growth because of energy crisis:		
1. Stone crushing machinery (coal mining, mechanics/machine operators)	30	4,900
2. Railway machinery products (tool/due; assembly mechanics)	40	5,000
	70	10,400
Net effect	155	15,070

FLINT, MICH.

[Energy crisis unemployment]

Industry/product	Total persons/ work week/jobs	Estimated payroll loss per week
SIC 34, fab metal products	[1] 2,350	($517,000)
Transportation SIC 371, equip motor vehicles	7,051	1,505,000
Trucking SIC 42	400	80,000
Sales and miscellaneous, SIC 41-49, 70-89	500	60 000
Total	10,301	
Work week reductions:[2]		
October	42.8	
November	41.1	
December	39.9	
January	[3] 37	

[1] Average per week.
[2] These figures represent January 1974.
[3] Approximately.

Job Growth Not to Occur

The area of growth most significantly affected will be construction. Jobs in the construction field will be down approximately 1,000 from last spring. No new contracts will be started or bid on except for governmental projects.

Near Future Outlook

General Motors has already announced a temporary plant closing for February which will idle 11,700 workers. If some of these people are recalled in March, it is rumored that the plant will be on half days and/or a shift will be eliminated. This means that in February there will be some 22,000 additional unemployed due to the energy crunch over and above "normal" unemployment (8 to 10,000). The unemployment rate for February is expected to be 15 percent or some 30,000 individuals.

Longer Outlook

The huge layoffs this winter and spring will have a ripple effect on the local economy. As we experienced in 1970 after the GM-UAW strike, retail sales and service employment will be cut by several thousand workers. Construction, as already noted, will be down. It is expected that no relief from GM layoffs will come until the 1975 model year begins in August. Even then, GM will significantly decrease its total employment by some 4 to 5,000 workers. The layoffs in other industries hit by the ripple effect may continue for several years, as did the effects of the 1970 strike.

JACKSON, MISS.

[Unemployment caused by the energy crisis]

	Total persons	Payroll loss/ week
Electric company (auto wiring harness-assemblers and machine operators)	350	$45,500
Butane tank manufacture (welders)	14	1,400
Lamp production (operators)	56	6,720+
Telephone plastic conduits (machine operators)	18	2,100+
Total	438	55,720+

MILWAUKEE, WIS.

[Energy impact on unemployment—to date]

Industry/product	Total persons/work week/jobs	General occupational classifications	Sex: Male	Sex: Female	Age: −25	Age: 25–45	Age: 45+	Estimate payroll loss per week
1. Unemployment:								
Automotive frame manufacturing.	1,730	Crane helpers, press operators, production welders.	1,730		(1)	(1)	(1)	(1)
Automobile Manufacturer	200	Auto assemblers.	200		(1)	(1)	(1)	(1)
Automotive Supportive Manufacturer.	95	Seat belt assemblers.	95		(1)	(1)	(1)	(1)
Automotive Supportive Manufacturer.	81	Auto air-conditioner assemblers.	81		(1)	(1)	(1)	(1)
2. Work Week Reductions [1]								
3. Jobs expected/not created [1]								

[1] Data not available.

NEW YORK, N.Y.

[Energy indicators]

Industry	Employment 1972 (thousands)	Concentration index [1]	Energy requirements per dollar of sales
Apparel	186.5	295	$0.05
Banking and insurance	350.8	233	.05
Printing and publishing	108.1	204	.05
Business services	182.8	223	.06
High-energy industries do not locate in the city:			
Chemicals	32.6	70	.22
Primary iron and steel	11.4	19	.12
Stone, clay and glass	6.8	22	.12
Some New York specialties are vulnerable to energy shortages:			
Air transportation	53.5	302	.09
Drugs and cosmetics	18.4	150	.07
Plastic products	8.5	150	.09

[1] Concentration index is a measure of a region's industrial specialization.

Source: Chase Manhattan Bank.

PHILADELPHIA, PA.

[Energy crisis claims]

Industry/code	Initial and continued claims for week ended											
	Initial continued		Initial continued		Initial continued		Initial continued		Initial continued		Initial continued	
	Dec. 14		Dec. 21		Dec. 28		Jan. 4		Jan. 11		Jan. 18	
10–14 Mining				2		1		2		1		2
15–17 Contract construction	14	5	9	17	6	17	10	27	10	25	9	21
19 Ordnance	4	5		5		8		3		3		2
20 Food			4	1	9	2		10	4	3	4	3
21 Tobacco	6	1		1								
22 Textile	4		3	1	1	18		7	2	6	1	2
23 Apparel			1			1	1	2	4	8	6	10
24 Lumber and wood	2			1	5	2		5	3	2		8
25 Furniture and fixtures					1			3	2	2	2	1
26 Paper	1						1	3		1	1	3
27 Printing/publishing	1		1	1	1	1		2		2	1	6
28 Chemicals		1		1				2		4	33	62
29 Oil	2	3		6	2	4	4	2	1	7	2	12
30 Rubber/plastics	4	1	4	2	24	5	6	9	6	1	7	4
31 Leather							1	2		2		
32 Stone/clay/glass	3			4			1	4	2	3		3
33 Primary metal	3							1		1	1	1
34 Fabricated metal	5	5	2	4	2	3	3	9	5	5	1	5
35 Machinery (exec. elec.)					11		1	8		5		5
36 Electrical machinery	4	3		3	14	2	9	9	11	15	1	7
37 Transportation equip	4	10	6	8	8	16	7	24	26	24	19	25
38 Instruments	4	2	2	2	81	3	11	12	4	3		6
39 Miscellaneous mfg		2	3	1	10	2	5	3	9	7	6	5
41–49 Transport/pub. util	28	4	3	15	5	15	5	16	16	23	45	46
50–59 Wholesale/retail trade	96	62	68	112	28	116	29	144	64	146	22	215
60–67 Finance/ins./real est	2	1		2		2	1	6		8		2
70–89 Service	5		4	3	2	18	8	10	8	28	20	10
	192	105	110	192	210	236	103	324	177	335	181	467

Source: Employed Security District I Pennsylvania.

PROVIDENCE, R.I.

[Energy impact on unemployment—Future (1974)]

Industry/product	Total persons/ work week/jobs	General occupational classifications	Estimated payroll loss per week
1. Unemployment:			
Petroleum related industries, plastics, auto dealerships, petro-chemicals, trucking, service stations.	687	(1)	$75,570.00
Naval civilian personnel cutbacks [2]	426	Mechanics, clerical, construction, and other professional.	66,030.00
2. Work week reductions [1]			
3. Job growth not to occur [1]			

[1] Data not available.
[2] The Naval civilian personnel cutbacks although not directly related to the energy crisis will seriously exacerbate the unemployment situation created by the energy crisis.

ROANOKE, VA.

Official tally of energy crisis effects on unemployment to February:

Layoffs:	
Garment and textiles	115–240
Carpeting	400
Furniture	50
Lighting manufacturing	50
Service stations	20
Hotel and motel	25
Automotive	10
	670–795
Partial Layoffs:	
Garment and textiles	75
Service stations	60
Hotel and motel	50
Automotive	15
	200
Expansion canceled or postponed:	
Rubber	(50)
Metal fabrication	(80)
Furniture	(100)
Truck assembly	[1] (1, 100)
Planned expansion continuing:	
Glass	[2] 100

[1] This plant in Dublin, Va., has not been completed. Originally estimated at 1,500 to 2,100 employees; revised estimate at 400 to 500 as a "starter" plant. Energy considerations may have had some impact, but generally considered to be result of community resistance among business paying a lower average wage.
[2] This plant has laid off 60 to 65 persons who will be hired back. Reason for layoff was given as necessary to complete expansion.

ST. LOUIS, MO.

Industry	SIC	Number
MANUFACTURING		
Durable goods:		
Lumber and furniture	24	180
Fabricated metal products	34	120
Electrical equipment and supplies	36	130
Transportation equipment/motor vehicles	371	4, 180
Nondurable goods:		
Bakery products	205	140
Textiles and apparel	22, 23	200
Rubber and plastics	30	80
Chemicals and allied products	28	120
NONMANUFACTURING		
Auto sales and service	551	210
Service stations	554	1, 100
Air transportation	45	190
Trucking and warehousing	42	210
Total		6, 860

SAN JOSE, CALIF.

[Weekly total of unemployment claims in Santa Carla Co.]

	Total counties	San Jose	Palo Alto	Campbell	Gilroy
Dec. 21 to 28	[1] 111	92	1	17	1
Dec. 28 to Jan. 4	44	18	10	14	2
Jan. 4 to Jan. 11	[2] 300	125	25	132	18
Jan. 11 to Jan. 18	105	40	24	33	8
Jan. 18 to Jan. 25	56	26	6	12	12

[1] Nearly all from General Motors.
[2] Two-thirds from Food Machinery Corp. (recreational vehicle division). The company is developing a new bus designed for the "Dial-A-Ride" feeder bus market. If the new product results in orders, these workers could be called back later this year.

Most of the initial claims shown above can be attributed to the energy crisis, and most claims have occurred in transportation equipment, airlines, and automobile manufacturing, public utilities, wholesale and retail trade and services, particularly service stations.

SOUTH BEND, IND.

In response to your memorandum on unemployment attributable to the energy crisis we held a series of discussions with the labor market analyst from the local employment service office.

The net results of these discussions constitutes a slim harvest of information. We found that local industry is both unwilling and unable to make any forecast of either decline or growth of employment for this fiscal year.

Secondly, the local employment service is unable at this time to provide us with the sex, race, age, and ethnic background of those who have filed unemployment claims as a result of the crisis. They inform us that such a comparison requires computer capabilities not available to the local office.

The occupations listed in the chart below are assumptions made by this office based on input from the labor market analyst.

[The energy impact to date: Jan. 19, 1974]

Industry	SIC code	Number	Occupations
Recreational vehicles	37	164	Assemblers, craftsmen.
Bendix	37	202	Assemblers, stampers.
Service stations	55	31	Attendants.
Ferrien Corp	37	5	Machine operators, stampers.
Diversified Plastics	30	18	Press molders, machine operators.
B & B Molders	30	10	Machine operator, press molders.
Pan Am	45	20	Stewardesses.
Total		450	

[As of Feb. 9, 1974]

Industry	SIC code	Number	Initial	Contin.
Airlines	45	3	1	2
Auto dealers [1]	55	9	3	6
Bendix	37	238	10	228
Ferrien	37	8	2	6
Service stations	55	32	5	27
Plastics firms	30	21	3	18
Recreational vehicles	37	468	12	456
Uniroyal [1]	30	51		51
		830	36	794

[1] Claims new since Jan. 19, 1974.

NATIONAL PLANNING ASSOCIATION

By WILFRED LEWIS, JR., *Chief Economist*

This year's Economic Report of the President is nothing if not frank. In discussing "Goals for 1974" (pps. 27 f.f.) tht report forecasts that "inflation will continue at a high rate through the early part of 1974" along with "a slow rate of economic expansion" during this period, "and possibly a decline, with rising unemployment." The report goes on to forecast "a moderate expansion" after the first half of the year as a result of "policies still to be adopted," which will be accompanied initially by a halt to the rise in unemployment and a slowdown in the rate of price increase for food and fuel, and, at a later unspecified time, a reduction in inflation generally and "a gradual decline in the unemployment rate."

Concerning this path, the report goes on to make two points: "First, it is at the same time our view of a feasible target and a prediction of what will be achieved if the planned policy is carried through. Second, that the path is feasible and that it will be achieved by the planned policy are both uncertain to a significant degree."

About this outlook, the following comments are in order:

First, the 1974 part of this forecast (that is, recession in the first half of the year and the start of a recovery in the second) conforms rather closely to the forcasts being put forth by most private forecasters and, given the policy assumptions being made, deserves a good grade as a forecast.

Second, I believe this is the first time since the Second World War that an incipient recession has been diagnosed so accurately and described so frankly by the administration in office at the time, so the report deserves a high grade for frankness also.

Third, the uncertainty quoted above about the forecast and the impact of planned policies is also refreshingly realistic and frank.

There are, however, some major problems with this scenario that I believe deserve the attention of the Joint Economic Committee.

First, the Economic Report of the President must be graded not merely as a forecast, but as a policy document, and I believe the policies it reflects and recommends are distinctly inferior to its forecasts. In fact, I do not believe the present and prospective economic stabilization policies of this administration comply with even the minimum requirements of the Employment Act, and indeed fly in the face of them.

Second, as the report itself points out, there is a band of uncertainty around any forecast, and the present policies contain a rather grave downside risk for which contingency plans so far in evidence are woefully inadequate.

Third, while the 1974 part of the forecast is achievable, the 1975 and later phases are not consistent with it. In my opinion, if 1974 is allowed to unfold according to the recommended path, there is next to zero probability that 1975 and subsequent years will feature the simultaneous gradual dimunition of inflation and unemployment that the administration is forecasting. If 1974 unfolds as forecast, and the administration maintains its present opposition to price controls, then we will be faced in 1975 not with the happy situation of watching inflation and unemployment both recede in the context of gradual expansion of the economy, but with an unpleasant choice between accepting a truly explosive rate of inflation or a further increase in unemployment or some of both.

All three of these comments require some explanation.

The Pursuit of Full Employment

It cannot have escaped the notice of this committee that the present administration has brought an extremely important innovation to the field of stabilization policy. This is the first administration since the enactment of the Employment Act in 1946 to accept, and indeed to recommend, recession as an anti-inflationary tool. The recession of 1970–71, unlike its four predecessors, was brought about by conscious and deliberate fiscal and monetary policy restraint, aimed at reducing inflationary pressures to be sure, but which persisted in the face of a recognized rise in unemployment. Higher unemployment was accepted in 1970 and 1971 as a necessary price for cooling off inflationary pressures.

I do not mean to imply that fiscal and monetary restraint played no role in earlier recessions. Indeed, fiscal and monetary policy bungling played an important causative role in all the first four recessions following the Employment Act. However, in each of these previous cases, the recession was unplanned and unwanted, and fought vigorously once recognized—albeit not always with the best tools or with immediate success.

We are now in the midst of a second "acceptable" recession in 4 years, and one that begins at a considerably higher rate of unemployment than prevailed at the start of the last one. I do not claim that the present recession was deliberately engineered by the administration. However, it certainly comes as no surprise to them; CEA members have been on public record for some months now as believing that some rise in unemployment in 1974 would be a necessary and acceptable concomitant of their anti-inflationary strategies; and even now we are being told that no expansionary actions are contemplated for the first half of the year. Rather, a shelf of contingency actions is being readied to be used if the decline threatens to get out of hand or if the economy doesn't turn up of its own accord in the second half.

I submit that the policy, new with this administration, of using recession as an anti-inflationary tool is illegal, inconsistent with the administration's own definition of "maximum employment," naive politically, and bad economics to boot.

The Employment Act, which is still the operative legislation in this area, directs the Government to pursue policies to promote maximum employment, production, and purchasing power. It nowhere says or implies that the "maximum employment" goal should be shelved during periods of inflation.

It is true, of course, that no precise statistic for "maximum employment" is defined in law, nor would it be wise to attempt to do so.

The two previous administrations pursued an "interim target" of 4-percent unemployment. The present economic report argues that in the contemporary economy, 4.9-percent unemployment is approximately consistent with "maximum unemployment," on grounds that a changed composition of the labor force, featuring more women and teenagers, makes 4.9 percent today roughly equivalent in labor force tightness to the 4.1 percent achieved in 1956.

Several observations must be made about this arithmetic. First, 4.1-percent unemployment in 1956 is equivalent to a rate as high as 4.9-percent currently only if given a string of rather stringent assumptions about inelasticities of substitution between different age/sex grades of labor, disproportionality between relative wages and relative marginal productivity for workers with varying skill backgrounds, and the like—assumptions which are nowhere discussed in the Economic Report, and unlikely to be more than partially valid. Second, the 4-percent target—or 4.1 percent in 1956—is itself a rather timid goal, given that we achieved a considerably lower rate of unemployment, less than 3 percent in fact, without inflation, for a period of several years during the Korean War. The plain simple facts, too little appreciated and ignored by this administration altogether, are that the rate of unemployment that can be attained without inflation depends on what anti-inflationary policies are being pursued simultaneously, and on whether the high employment "target" or "potential" is approached gradually or in a burst of demand expansion.

But the most important comment on the administration's new arithmetic of "maximum employment" is that it is blithely ignoring its own calculations for 1974 and, indeed, for the foreseeable future. Unemployment is already at 5.2 percent and rising, and instead of explaining how it plans to reduce it back to even the unsatisfactory level of 4.9 percent, we are being told in effect that contingency plans are being readied to keep it from going higher than 6 percent. As this committee is well aware, the differences between 4.9-percent and 6-percent unemployment are not trivial. That difference translates into about 2-percent difference in employment—or about 1½ million jobs—and 2½- to 3-percent difference in GNP—or over $30 billion in 1974 prices: more than $150 apiece for every man, woman, and child in the United States.

One reason for suspecting that if the first part of the forecast holds up the second part will not is that there is no way that those with political responsibility in the administration, once they realize what is happening, will accept the implied political costs. This is, after all, an election year. If unemployment rises steadily toward 6 percent over the first half of the year, you can be quite sure that the administration's economic and fiscal managers will be instructed by the administration's politicians, in no uncertain terms, to get things moving in the other direction in a big damn hurry. And if, in the meantime, the recession discourages some private investment, we will later encounter capacity bottlenecks and "excess demand inflation" at a still higher rate of unemployment than the newly defined "potential" of 4.9-percent unemployment. Such a "stop-go" approach to managing the economy can succeed only in reducing the average amount of private investment and productivity growth over time, and steadily notching up the rate of unemployment that can be achieved without intolerable inflation.

Recession as an Anti-Inflationary Policy

Aside from the legal and political aspects, recession is an inappropriate tool with which to try to counter inflation on purely economic grounds as well. To understand this point, it is important to recognize that there are different kinds of inflation, stemming from different sources, and differing quite a bit in their responsiveness to various remedial policies.

I think it is useful to distinguish at least crudely between three broad possible sources of inflationary pressure in an industrialized economy such as ours. First, it is possible to imagine—though rarely encountered in practice—a situation in which, while the capital stock and the supply of raw materials is adequate, the level of aggregate demand is such that there are widespread labor shortages; vigorous competition among employers for available labor; and a resulting inflation of wage rates that spreads to the general price level through the medium of escalating labor costs of production. If we ever encountered this situation, temporary demand restraint, kept on until labor force growth caught up with demand, would be an appropriate counter-measure. Aside from World War II, however, we have not encountered even superficial temporary symptoms of this variety of overall inflation in the last 45 years and probably longer—we don't really have meaningful statistics going back any further than that. There have been isolated industries and isolated labor markets, to be sure, where labor supply was tight enough to generate upward pressure on certain wage rates. But this phenomenon has simply never been general enough to play any significant role in overall national inflation.

A second distinct kind of overall inflation that we have occasionally encountered is where, for reasons of bad weather either in this country or abroad, there is a shortfall in one or more important basic agricultural commodity. The elasticity of demand for food and the elasticities of substitution between agricultural products are such, and the importance of food prices for real wages such, that a temporary shortage in even one major agricultural commodity can spread quickly to other food prices and generate upward pressures on wages and prices generally. When confronted with inflation coming from this source, the appropriate policies are to try to assure that next year's crops are better, and to try to damp down the tendency for this or any other kind of inflation to perpetuate itself through expectations and anticipatory price and wage increases. Aggregate demand restraint is an inappropriate remedy for this kind of inflation since it provides very little direct relief to price pressures in the relevant commodity markets, and therefore very little relief to pressures at the bargaining table to restore real wages, and introduces a new source of inflationary pressure to boot—namely, a reduction in productivity and rise in unit costs in manufacturing associated with restricting production to lower than optimal levels of output.

A third general type of inflation is a situation in which, while labor supply is adequate, the path of aggregate demand is such that there are widespread capacity bottlenecks in manufacturing and/or industrial raw materials. In this situation, demand management policies should be pursued to moderate the pace of expansion. But to halt or reverse the expansion would have perverse effects. First, unit costs would be increased as output declines. Second, breaking the capacity bottlenecks requires private investment in capacity expansion which will hardly be appealing during a period of stagnant or declining demand and declining profits.

It should be noted that industrial and raw material capacity bottlenecks can show up, as they did in 1973, while labor supply is still plentiful. It is hardly surprising that we encountered at 5-percent unemployment in 1973 the symptoms of "excess demand" inflation that we used to expect at 4-percent unemployment. That was the more or less inevitable consequence of keeping the economy deliberately depressed for 3 years, as was done from 1969 through most of 1971, and then allowing demand to shoot up much faster than "potential" in 1972.

Having encountered some capacity bottlenecks in 1973, it would have been one thing to say "we must now moderate the pace of further expansion to allow capacity to catch up with labor supply." It is something quite else, and counter productive in the extreme, to say "we must now accept a contraction in output because we experienced inflationary bottlenecks last year." This policy is disruptive to business planning, inflationary in its own right, and contains the distinct threat that the inflationary bottlenecks encountered at 5-percent unemployment in 1973 will be encountered at 6-percent unemployment in 1975. The very grave risk inherent in the Economic Report's recommended "game plan" for 1974 is that, if the recession drags on more than a very few months, business fixed investment plans—currently one of the few bright spots in the economy—will start to be trimmed back. This is undesirable not because of any danger that the recession will get "out of hand"—demand management can surely take care of that contingency. Rather it is undesirable because our capital stock is already too small for the available labor force, and any trimming back of business fixed investment plans will further retard productivity growth and postpone still further the day when we can hope to return the economy to even approximately full employment without inflation.

Energy Supply and Prices

A discussion of contemporary varieties of inflation must clearly take note of the oil crisis. Without attempting a detailed analysis of this fascinating and complex topic, certain observations are in order in the present context. First, oil has an economic importance in contemporary industrial societies that is quite unique—there is no other raw material a shortage of which would have a remotely comparable impact on the general level of prices. Therefore it is not a very useful model for drawing generalizations about appropriate policies for dealing with the inflationary consequences of raw material shortages. Second, there does not appear to be a whole lot that the U.S. Government, acting alone, can do in the short run about the price of oil, or about the induced increases in prices of other things that depend heavily on oil. What happens to oil prices depends on what happens to oil production. What oil producers will do is almost anybody's guess. On the one hand, prices are so far in excess of production costs that one might think that somebody someplace might be trying to expand production, and that enough such behavior would more than offset the apparently limited cutbacks that some Arab countries say they have made. On the other hand, the present prices are so profitable, and the present high prices so obviously dependent on the continuation of supply restraint, that perhaps no one on the production side will see much point to trying to expand output. International prices have been coming down recently. However, they are still above U.S. prices. Any significant discrepancy between the two can be maintained only through queuing or rationing, neither of which appear politically attractive, but just where or when the two will converge is not yet clear. Perhaps the best thing the U.S. Government could do would be to make sure that any tax incentives or subsidies to the oil companies are targeted more precisely to production expanding activities, and to have tough standards of evidence to support claims of such activities.

Expectational Inflation and the Need for Price Controls

With the announced end of price controls being cheered in almost all quarters, it may seem gauche to raise this unpleasant topic once again. The reason for doing so is that, the administration's wishes to the contrary notwithstanding, we have not seen the last of price controls. That is not because I, or anyone else I know, am enamored of controls or think they're a panacea. It is simply because the available alternatives are not, in the final analysis, acceptable.

I share the administration's expectation that food and fuel prices will be rising less rapidly, and perhaps even declining, in the second half of this year. As a consequence, the overall price indices should start behaving a little less badly than they have been recently. That should not be taken as a sign that demand management policies have succeeded in curbing inflation, or that the time has come when price controls can safely be discarded.

A moderation in fuel and food prices this year will signal nothing more than an easing of last year's shortages. The basic underlying inflationary pressures will be much worse in 1974 than they were in 1973. To start with, it is almost universally accepted that, as a lagged response to last year's increases in food and other consumer prices, wage settlements in many important industries will be pushing into two figures—10 percent and more. In addition, productivity, which has flagged badly since the current slowdown began in the second quarter of last year, and which became negative in the fourth quarter, will worsen still further during this year's recession, generating further cost pressures. On top of that, the recent announcement of an end to price controls has touched off a wave of price workups in steel, autos, paper, and many other industries. To make matters still worse, the planned contraction in demand is simultaneously restricting the markets for which business must plan their fixed investment and trimming their profits and cash flow with which to finance investment.

The sum total of all this is that, once the temporary effects of moderating food and fuel prices are past, we will be face-to-face with an even more virulent inflation than last year's. We can no doubt look forward, if not in next year's Economic Report, then shortly thereafter, to receiving an explanation of why 5½ percent, or maybe even 6-percent unemployment, rather than this year's 4.9 percent, is really the definition of "maximum employment."

Alternative Outlook

It is possible that the Economic Report is too pessimistic. While not the most likely course as of this moment, it cannot be ruled out that the recession now underway may bottom out in the next month or two, and the economy start rising in the second quarter rather than the second half.

That alternative would be distinctly preferable on several counts. It would mean less average unemployment for the year than the 5½-percent rate forecast in the Economic Report. It would mean higher productivity growth for the year. And it would leave us with a larger capital stock, and therefore more room to grow in 1975 before we began encountering capacity bottlenecks.

For all these reasons, the administration should be bending every effort to reverse the present decline and start the economy moving again as soon as possible—but not necessarily as rapidly as possible—rather than waiting for the recession to run its course in the mistaken belief that that will curb inflation.

NATIONAL SAVINGS AND LOAN LEAGUE

The National Savings and Loan League appreciates the invitation of the Joint Economic Committee to present the league's views on the economic issues facing the Nation and the thrift and home financing sector in the year 1974. The forum which the Joint Committee has afforded all facets of the American economic scene—congressional, executive, and affected labor, business, financial, and individuals—has been invaluable in eliciting the studied judgments of these participants in both critiques of past governmental policies and suggestions for new or varied approaches to current problems, domestic and international.

It has been the league's custom in past years in its statements to this committee on national economic issues to concentrate on national fiscal and monetary policies, proposed legislation, and other issues of special concern to the multitude of Americans who have invested over one-quarter of a trillion dollars in savings accounts in the Nation's savings and loan associations as well as the beneficiaries of those savings—the American homeowner and homeseeker.

This presentation will conform to our past practice of focusing our comments upon national monetary and fiscal policies and legislative proposals of particular concern to the Nation's savers and homeowners. We believe that the Congress and the administration desires to adopt and pursue policies advanced by the national league which assure the Nation's savers a strong, reliable institutional financial framework of savings institutions which reward their savers with safety, liquidity, and adequate return on their savings investments while providing desirous and needy homeowners an adequate source of credit to finance their needs.

The national league has been well aware of the fact, as noted in its presentations to this committee in prior years, that international developments were likely to have an increasing bearing upon the social and economic goals of American life and in consequence upon the formulation and execution of domestic monetary and fiscal policies. The deterioration of our balance of payments and the erosion of our trade balances, in particular, foreshadowed the official devaluations of the once almighty dollar in 1971 and again in 1972, and the unofficial market devaluation in early 1973.

However, no single event has brought to the average American the realization that the third quarter of the 20th century epitomizes the ever-growing interrelationship and interdependency of the world economies—as has the October 1973 oil embargo to the United State and accompanying highbinder escalation of oil prices to the rest of the world.

Regardless of whether the actions of the Arab oil exporting countries were activated solely by price objectives or motivated by politically hoped for realinement of Israel held Arab geography, the results of their actions will have a substantial impact upon world economies—industrialized, developing, and underdeveloped—for years to come. It

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is also obvious that the actions of the Mideast oil exporters heightens the necessity of the energy importing nations to coordinate policies relating to trade and currency relationships as well as the development of energy sources less exposed to disruptions such as those caused by the current oil crisis.

In short, the actions of the Mideast oil exporters has an immediate effect upon the programs, policies, and adjustments of oil user nations as well as long-term plans geared to reducing dependency via the development of acceptable energy substitutes.

The price of world oil, allowing for some reductions from current prices following the termination of the embargo to the United States, is likely to average around three times the prices prevailing before the October 1973 Arab actions. Translated into dollars Arab oil revenues which approximated $22 billion last year will increase in 1974 to an aggregate of from $75 billion to $90 billion. An appreciation of the magnitude of the 1974 oil revenues of the Mideast Arab exporting countries can be gleaned from the fact that the total oil revenues received by these countries will exceed the after tax income of all U.S. corporations for 1973.

The increased oil costs of importing nations will have to be paid for by either (1) increased trade with the Mideast or other countries, (2) the use of existing monetary reserves, (3) funds borrowed in international as well as domestic markets, (4) exchange of equity assets, or some combination of these four sources.

Since there is a physical limit upon the quantity of goods which the sparsely populated oil exporting countries can use and there will be a desire on the part of the oil importing countries to preserve existing monetary reserves, funds required to meet increased oil importation costs are likely to be channeled into the debt and equity markets. Nevertheless oil importing nations will be continuously aggressive in trying to improve their respective trade positions in both the Arab and the non-Arab world in order to minimize the use of nontrade funds for oil payments.

One of the disciplines expected to result from the higher level of world oil prices is the practical restraint importing energy countries will encounter if resort is made to currency devaluation. In this sophiscated world such attempts would only result in higher oil costs. As a consequence we can expect most countries to protect currency values in order to minimize the possibility of aggravating pressures upon balance of payments.

In view of existing world and domestic conditions it is imperative that national fiscal and monetary policies be pursued which are oriented neither toward deflation or overinflation. Policies designed to stagnate the money supply as well as those which would foster undesirable expansionary growth in the money supply would under the conditions that prevail today wreak the same havoc upon the economy.

Deflationary monetary and fiscal policies would produce intolerable rates of unemployment and interest rate levels which would lead to severe credit crises. Overinflationary policies would ultimately lead to the same results through different channels; that is, further currency deterioration, increased price pressures, skyrocketing interest rates, and exacerbation of the flight from nontangible exchange media.

The effects upon the domestic economy resulting from the oil embargo and energy shortages will continue for some years after the embargo is lifted. To date the greatest impacts have been felt by the automobile and its satellite industries and tourist accommodations dependent upon private transportation. Fuel and gasoline availability have also affected housing construction and sales as builders and home buyers, especially of suburban tracts, weigh the prospects of gas rationing and its impact upon the ability to commute. Lifting of the embargo and restoration of oil production levels to those prevailing prior to last October will have a decided effect upon the demand for new housing accommodations this year.

Increased energy costs have not yet been fully reflected in consumer prices although gasoline prices and oil heating fuel bills have been escalating rapidly. As the higher costs of oil and oil derivitives course through the veins of pricing mechanisms they will compound price pressures which already exist at both the wholesale and consumer levels. The wholesale and consumer price indices are already rapidly rising as more industries and businesses are released from price controls. Higher costs now in the pipeline plus those to be expected when most price and wage controls expire on April 30 will be subject to further upward pressures by the terms of postspring wage contract settlements.

These conditions require national monetary and fiscal policies which will not add to the pressures already existing. Extreme care must be taken to assure that we do not again encounter the "double figure" interest rates that prevailed for most of the last half of 1973. A new upward surge of interest rates to comparable levels would cause another immediate round of disintermediation from savings accounts and abort the hoped for recovery in housing construction later this year.

The hard realities of economic life constantly remind us that international factors now do have substantial effects upon domestic economic activities. The intensity of world trade competition, the successive dollar devaluations, and the oil crisis are constant reminders that our domestic economic policies and programs can not long run counter to world economic forces. Offshore influences must be taken into consideration in the adoption and implementation of our fiscal and monetary policies just as other industrialized nations also must recognize offshore factors which affect them.

In our rapidly changing world we must acknowledge that our energy and ecological problems, often conflicting and far from being resolved, will continue to affect our standard of living for some time to come. More rational husbanding of our national resources, the development of energy substitutes, together with basic environmental improvements in the quality of water and air will require time, money, labor, as well as sound and rational legislation and programs.

No one questions our ability to marshal the assets, technology, manpower, and capital to solve our economic problems. However, the solutions of these problems and others facing us today will require patience and moderation by all sectors of society—government, business, labor, and consumer.

On pages 38 and 39 of this year's economic report of the President, the Congress is urged to enact legislation which would radically change, if not eliminate, the institutional financial framework which has for so long successfully served the Nation's savers and homeowners. These proposals which emanated from the so-called Hunt Commission would seriously erode the ability of the Nation's savings and loan associations to continue their essential functions of channeling savings into the housing market.

The national league believes these radical proposals for financial institutions reform represent a grave threat to the future of housing finance in the United States. It is our studied judgment that the revolutionary suggestions contained in these proposals should be rejected in favor of an evolutionary approach to changes in the thrift industry.

Savings and loan associations over the years have been the mainstay of the housing finance industry—the only financial institution that can be counted on to invest the bulk of its funds into home mortgages. The reform proposals would subvert that institution.

The national league believes that important moderations to smooth out the flow of funds to the mortgage market should be accomplished within the structure of the savings and loan industry.

To achieve that end, the national league has urged the following positive actions be taken by the Congress and/or the Federal regulatory agencies:

(1) Provide a tax incentive for savings by individuals by exempting from taxation the first $750 in interest or dividends earned from savings accounts.

(2) Maintain dividend and interest rate controls over financial institutions, and provide a one-half of 1 percent differential for housing on all accounts under $100,000.

(3) Provide authority for savings and loan associations to issue checking accounts, with adequate reserves, to individuals.

(4) Provide authority for savings and loan associations to make up to a reasonable percentage of unsecured loans for any purpose up to $10,000 to existing savers and borrowers.

(5) Take appropriate action to insure that savings and loan associations can utilize electronic funds transfer systems for their customers as these systems are developed.

(6) Provide legislation to permit Federal chartering for stock savings and loan associations, and provide regulatory authority for the free and voluntary conversion of Federal associations to State stock form.

(7) Provide for regulatory amendments in the issuance of subordinated debentures by savings and loan associations, so that such debentures can be counted in part toward Federal Insurance Reserve requirements. Such counting would insure full use of the subordinated debentures—and in turn savings and loan associations would be able to better serve the housing needs of their communities.

(8) Provide legislation for 100-percent insurance of public unit accounts, so as to provide incentive for such accounts to be deposited with housing finance institutions, and increase substantially the FSLIC insurance limit from the present limit of $20,000.

(9) Increase the percentage of assets limitation that savings and loan associations can invest in affiliated service corporations from 1 percent of assets to 3 percent of assets.

(10) Provide legislation for a full range of trust powers for savings and loan associations.

(11) Provide the necessary tools via legislation and regulation for variable rate mortgage loans and flexible payment mortgages.

(12) Have Treasury deposits made in savings and loan associations as well as in commercial banks.

NATIONAL URBAN COALITION

By M. Carl Holman, *President*

The National Urban Coalition, since its founding in 1967 as an organization dedicated to improving the lives of the poor and dispossessed in our Nation's cities, has recognized the paramount role of jobs and income in achieving that goal.

Through our day-to-day work at the national level and in the 30-plus cities in which there are local coalitions, as well as through the findings of a recently conducted opinion poll (which can be made available to you), we know that people in the cities—labor, minorities, business and the poor—support our point of view on this matter.

We notice that unemployment also continues to be a dominant part of the discussion by the Council of Economic Advisers, as well it should; this measure of the economy's performance reflects important economic forces that affect almost every American family. Unfortunately, however, the Council's discussion lacks thorough analysis of the costs and benefits of various alternatives. Instead, the emphasis is put on statements that things are not so bad—the 4.9-percent unemployment rate, for example—or that things are not as bad as they look at first glance—such as the distribution of income—rather than on the fundamental question of whether things can be made better. Although there are a few statements which address this issue—such as the assertion on p. 61 that employment in 1973 was very close to its maximum, a presumption which we vigorously contest—large sections of the report imply that many of the unfortunate aspects of the Nation's economic performance are simply beyond our control.

The coalition contends that there are many policies available which can reduce the costs to the American people sustaining any given level of inflation or unemployment. We will then contend that starting from the levels of unemployment and inflation which prevailed last year, the country's overall welfare could be improved by moving to a lower level of unemployment, even at the cost of some additional inflation (although we argue that little additional inflation would result). In order to simplify the discussion, the complications of the energy crisis are ignored, since the fundamental causes of high unemployment will probably outlast the energy shortage.

We will discuss various ways in which the unemployment rate could be reduced without increasing inflationary pressure at all.

Unemployment

The Cost of Unemployment

Families and individuals in the lower half of the income distribution clearly bear a much larger share of the costs of an economic downturn than the remainder of the population. Conversely, the poorer half has much more to gain from more aggressive monetary and fiscal policies and a lower overall unemployment rate than the upper half. Some of these gains would be permanent and would thus be of lasting value in improving the economic position of the least advantaged groups in our society.

Statistics in the Economic Report clearly show that the unemployment rates of blacks, women, the young, and the unskilled go down much more than does the average rate when the economy experiences an upturn. These groups thus feel the monetary and psychological benefits of escaping unemployment—the wages from a new job and the end of the painful feelings of shame, defeat, and loss of self-respect and economic security which often accompany the search for employment.

The fact that women and young people are a larger proportion of the labor force than they were in 1956 is no reason for the Council to tolerate a higher unemployment rate, as the discussion on page 60 of the Economic Report suggests. White adult men usually have very low unemployment rates, almost always receive unemployment insurance when they are laid off, and are often rehired into their old jobs in a short time. The female and youth and racial minority components of the unemployed, however, are most likely to be reentrants or new entrants into the labor force; these groups do not receive unemployment insurance.

More importantly, the job search which accompanies labor force entry is likely to have a lasting effect on the individual's attitudes and expectations. Not only are these groups more likely to find a job when the economy is turning up, but they are more likely to find a good job, which will create a stronger attachment to the labor force and more motivation to acquire work-related skills.

The most important benefits of lower unemployment outlast the initial period of economic improvement. There is a great deal of evidence that many firms expand the higher occupation levels of their work forces largely by promotion from within. This benefits not only workers who are upgraded, but also those hired to fill their places. These new workers are thus able to accumulate valuable on-the-job experience and training—"human capital"—which is of lasting value. This experience generates new attitudes about work as well as useful productive knowledge. The most dramatic proof of the importance of these mechanisms for the lower half of the income distribution is the evidence that the 5 or 6 years of tight labor markets during World War II permanently narrowed wage differentials and made a step toward equalizing the distribution of income. The enormous mobility of workers into new jobs during that period brought many workers in contact with good jobs for the first time and had a lasting effect on their careers. The Nation must continue to seek peacetime ways of achieving such results. The permanent benefits of having tighter labor markets should be kept in mind.

Another source of permanent benefit of a period of low unemployment is the generation of information, information both about the characteristics of workers and the characteristics of jobs. Anyone who has ever been refused a job because an employer hires only experienced workers knows that employers desire evidence that potential worker is likely to be a good one. Similarly, workers, especially those who are unemployed, spend time gathering information about various job possibilities. Because of the greater number of job vacancies during a period of low unemployment, workers find it easier to acquire this information, which again may have a lasting effect on their careers. Thus, a period of low unemployment will greatly increase the amount of information available to both workers and employers about the characteristics of the other side of the labor market. This information will permanently increase the ease with which both firms and employees will satisfy their needs.

One important effort which is greatly hindered by high unemployment is the attempt by Government agencies to promote equal employment opportunity. The success of this effort during any given year depends on the number of available job vacancies into which women and minorities can be hired. Vacancies increase greatly as the economy expands, not only because of the desire of firms to expand their work forces, but also because a greater proportion of workers quit their current jobs in search of new and better ones. These conditions are essential for a successful program to break down traditional discriminatory behavior in the labor market.

One last permanent benefit of a period of low unemployment may be the greater success with which policies to redistribute income to the poor may be pursued. Most individuals are likely to feel more generous and more willing to improve various programs of transfer payments during a time when incomes are rising and jobs are plentiful than during a period of recession.

As we compare the costs of high unemployment with the costs of high inflation, it seems clear to us that high unemployment is a much more important problem than high inflation. The record of the past 10 years indicates that serious inflationary pressure does not develop until the unemployment rate approaches 3.5 percent. Thus, a move to a 4 percent unemployment rate, would be worthwhile, even at the cost of some increase in the inflation rate.

Policies To Reduce the Cost of Unemployment

Although the best cure for widespread unemployment is the creation of new jobs, income transfer programs should be redesigned. We see no reason for the pronounced difference in treatment of those who are laid off from their present jobs and thus are covered by an increasingly generous unemployment insurance program, and those who are just entering the labor force and who receive no public income support. This last group would greatly benefit from any policy which enabled a more thorough search of job possibilities.

One way of providing income support to all of the unemployed is to consolidate existing unemployment compensation and welfare programs into a uniform system of tax credits. Suppose that every person over 18 years of age were entitled to receive a tax credit of $100 per month, even if this was greater than the amount of income tax he owed. Such a program would also pay a lower amount for children under 18, say $80 per month, to their parents and guardians. Individual States could add to this amount if they so desired. This money could be received either as a credit against the income tax withheld by employers or in the form of a monthly check from the Internal Revenue Service. Thus, a man whose family included a nonworking wife and two children could receive his family's $360 per month tax credit from the Government if he were laid off. The amount of the payment would be independent of the division of the unemployed into new entrants and job losers. The tax credit would continue even if the wife decided to look for a job and found one, although she might decide to use her tax credit to reduce her tax withholding. Such a program could replace the unemployment insurance system, the aid to families with dependent children program (AFDC), food stamps, personal exemptions in the income tax, some programs for aid to college and graduate school students, and perhaps other current personal subsidy programs. Even if the income tax rate were made proportional, the uniform credit would insure that the overall system of income taxes and transfer payments was progressive. Such a system would also eliminate many of the adverse incentive effects of present income maintenance programs, which will be discussed in more detail below.

Policies To Enable an Increase of Employment Without Increasing Inflation

Any policies which make it easier for workers to find jobs and employers to fill their vacancies will probably reduce the average duration of spells of unemployment and thus the overall unemployment rate. In this section, we will suggest several measures which would increase employers' speed in filling vacancies and the incentives of workers to quickly take the best job they could find.

One important phenomenon which increases the overall unemployment rate is labor market segmentation. Basically, this is the tendency for employers to search more intensively among certain population groups than others while filling their vacancies. In general, employers favor adults over young people, men over women, whites over blacks, those with high education over those with low education. This tendency may result from several causes—employer or worker prejudice, organized racist and sexist rules of thumb, overreliance on largely irrelevant tests and certification, and lack of information about the potential performance of workers after they are hired. Because of this feature of the labor market, inflationary pressure begins to develop when the unemployment rate for white adult males is low, although the overall rate may still be rather high, since employers may make some effort to attract the preferred group through the use of higher wages before looking for other types of workers. Workers in the excluded groups may respond by not making much effort to acquire skills or not developing more commitment to the labor force, since such activity would not be worthwhile given the lower average probability of finding a good, steady job. Any initial belief on the part of employers that these workers were not as "good" as white adult males would thus turn out to be correct; a self-fulfilling prophecy would thus be confirmed. Therefore, policies which induce firms to consider a wider range of workers would even out the unemployment rates of these various groups and reduce the inflationary pressure associated with any average rate of unemployment.

Perhaps the most important tools to be used in achieving the breakdown of labor market segments are laws designed to promote equal employment opportunity. If aggressively enforced, these laws can prevent excessive competition for the favored groups and give the others incentives to become more desirable workers.

Public agencies can have an effective role in generating reliable information about the productivity of individual workers. The recent public service careers program, for example, showed great success in putting workers who lacked the usual educational credentials into regular civil service jobs. This was true despite the fact that in many instances funds for the program went to persons other than the poor and disadvantaged. Often the most effective of these public service employment efforts were combined with training programs which the worker had a large incentive to successfully complete because of the guarantee of a waiting lob. State and local government agencies should consciously engage in the very valuable activity of hiring and providing reliable information about workers who lack the usual credentials, which have recently shown to be far from perfectly reliable in sorting out different quality levels of workers. If private employers who ordinarily restrict their search to high school graduates could also have confidence in a dropout who received a good recommendation from a local government agency, segmentation based solely on education would begin to diminish.

Conclusion

The analysis presented in this statement clearly shows that employment in 1973 was far from its maximum. A wide variety of policies are available whose effect would be to reduce unemployment without increasing inflation. In addition, further reductions in unemployment would be warranted, even if they did result in some additional inflation. The Council's assertion that a 4.9-percent unemployment rate is anywhere near the minimum rate that can and should be achieved should be strongly rejected.

The coalition, its network of local affiliates and particularly the soon-to-be established panel on jobs and income would welcome the opportunity to work with the committee in developing strategies to provide all Americans with a decent job or income.

NEW YORK CHAMBER OF COMMERCE AND INDUSTRY, COMMITTEE ON FINANCE AND CURRENCY*

The New York Chamber of Commerce and Industry is honored and pleased to submit a statement for the record of the Joint Economic Committee's hearings. The New York Chamber of Commerce is the oldest organization of its type in the United States, having been founded in 1768, 8 years before our independence. The New York Chamber's membership of approximately 3,000 includes many of this Nation's major corporate enterprises. New York is the headquarters for many of our largest national and multinational companies, the center of our Nation's leading and financial and investment institutions and historically it has also been the focal point of our international trade and commerce. Accordingly, our membership is broadly representative of these vital areas of our Nation's business community.

The chamber submits this statement at a time of most serious concern over the inflation, and the energy and other supply shortages, which have gripped the U.S. economy. It is obvious that the Arab oil embargo has gravely aggravated the situation. Nevertheless, it should be noted that the price-wage controls had probably become counterproductive—even prior to the energy crisis—by distorting normal patterns of production and distribution. They cannot now be maintained and relied upon to help stem the inflationary tide. The burden is squarely back upon fiscal and monetary policy to deal with the general problems we face, while international diplomatic initiatives are pursued to deal with the specifics of the oil shortage.

Inflation has now become a clear and present danger to the effective functioning of the U.S. economy. This is particularly evident in the action of the financial markets. Because of our specialized knowledge of these markets and our considerable concern over their future, we shall return to this subject later to point out the imminent problems in these markets to the Joint Economic Committee.

Meanwhile, we wish to preface our comments on fiscal and monetary policy by recalling that we plainly warned 1 year ago in our statement to this Committee that "the American economy is once again threatened with overheating and a resurgence of inflation." At that time, administration economists forecase a 2.5 to 3 percent average rate of inflation for 1973 over 1972. The actual average rate has turned out to be 6.2 percent, with figures as high as 8.8 percent on a December 1973-December 1972 basis. Also, the administration foresaw Federal expenditures in fiscal 1974 at $269 billion with a $13 billion deficit (unified budget basis). Current estimates are for $275 billion in actual outlays, although the deficit will apparently be kept to a possible $5 billion through the effects of a corporate profit and personal income boom now clearly past its peak. Thus, our apprehensions have more than fully materialized, especially since the administration concedes a likely calendar year average price increase of 7 percent for 1974 and is planning on $304 billion in Federal outlays in fiscal 1975 with a likely deficit of over $9 billion.

*A list of the members of the Committee on Finance and Currency of the New York Chamber of Commerce and Industry appears at the end of this statement.

The Need for Fiscal Restraint

Federal outlays, if they indeed are held to the planned $304 billion, will have risen at an annual rate of nearly 11 percent in the 2 fiscal years ending June 30, 1975 This the most rapid rate of increase in Federal outlays in the post-World War II period, except for the immediate post-Korea and Vietnam escalation periods. The proposed fiscal 1975 budget contains especially large increases for income security and for national defense purposes. Although the administration maintains that the budget is slightly more restrictive on a "full employment" basis than the 1974 budget when calculated at a 4 percent unemployment rate, it is conceded that this unemployment rate is unrealistic under circumstances of a supply-shortage-plagued economy. Besides, the Council of Economic Advisers has pointed to structural changes in the labor force that make it unlikely that 4 percent is a reasonable unemployment goal even apart from supply-caused disruptions.

It is therefore incumbent upon Congress to examine the administration budget closely with an eye toward possible savings. We would agree that considerations of equity may necessitate such measures as extension of unemployment benefits for workers especially affected by the energy crisis. We strongly urge, however, that the Congress not build into future budgets emergency appropriations that can become the basis for indefinite and increasing outlays even after the present difficult period has passed. A major resuscitation of housing programs, such as those under sections 235–36 of the National Housing Act, would fall into this category. The administration's modest 1 percent real growth projection for the year is in effect based upon supply constraints that cannot be readily solved by fiscal stimulus.

The Congress has an especially grave responsbility this year with respect to the budget. As a result of political events, fiscal initiative and responsibility will clearly have to be shared by the administration with Congress to a greater extent than in the recent past. It is no longer possible for Congress to pass excessive spending bills on the assumption that the Executive will act as a restraining factor through vetoes, impoundments, and so forth. Therefore, we judge the exercise of congressional responsibility to be vital; and we strongly reiterate our previous recommendation that, as an immediate demonstration of this point, the Congress enact the long-pending legislation establishing a congressional committee on the budget as a whole. Federal spending must be considered in conjunction with revenue. Congress must have a mechanism for curbing excessive deficits arising from appropriations however worthy on their merit, if they cannot withstand the test of an appropriate overall budgetary stance.

A Steadier Monetary Policy

The New York Chamber of Commerce and Industry has been concerned, and continues to be concerned, with the possibility that too large a burden of coping with inflationary stresses and unemployment will fall on the shoulders of monetary policy.

In the immediate future, it may be appropriate for the Federal Reserve to ease somewhat the fairly restrictive stance it took late last summer and into the fall. Nevertheless, we would like to support and reinforce Chairman Burns' observations that oil, not money, is in short supply, and that "an easier monetary policy can be only a marginally constructive influence in an energy-induced slowdown."

We might point out that there is no magic figure at which the money supply or some other monetary aggregate will contribute maximally to economic growth. It has to be strongly suspected, however, that the range of reasonable growth targets for M_1 (the narrowly defined money supply) should be conditioned by the real growth capability of the economy, judged at 1 percent by the administration and at perhaps 2 percent by optimistic private analysts. In this environment, it would appear that the M_1 target should be below the 5.7 percent average increase of 1973 over 1972, and certainly below the 6.3 percent and 8.7 percent figures for 1971 and 1972, respectively.

In this connection, it has been brought to public attention that the increase in the money supply in 1973 was seriously underestimated for some time because of the unusually rapid growth of demand deposits at nonmember banks. The problem of nonmember banks of course, extends beyond statistical information available to the Federal Reserve to the more basic question of the degree of effective monetary control at the disposal of the central bank. In principle, we support the Federal Reserve in its request for legislation that would subject all but the smallest nonmember banks to reserve requirements, in return for access to the discount window. The existence of the present reserve requirement distinction between member and nonmember banks unnecessarily complicates the already difficult task of the Federal Reserve.

At this point, we would reemphasize our previously stated conviction that excessive swings in monetary policy are undesirable, whether these swings are measured primarily in terms of money market rates or in terms of monetary aggregates. Such swings arise in good part from the potential overburdening of monetary policy, which in turn reflects unrealistic expectations held for monetary policy when confronted with destabilizing budgetary developments or international supply situations. In the context of 1974 prospects, it must be appreciated that monetary policy cannot overcome the unavoidable weakness in the real economy.

Inflation and the Financial Markets

The Joint Economic Committee should be clearly advised that in the opinion of a great many financial experts the proper functioning of the U.S. capital market is being seriously endangered by the persistence of large-scale inflation.

Under the impact of severe inflation, an element of distrust in financial instruments is beginning to develop among savers and investors. Whereas the traditional attitude of consumers toward a surge of inflation used to be to "retrench"—that is, save more and buy less—there are signs that this attitude is being replaced by "fear buying" in anticipation of still higher prices and shortages. This development, if it continues and spreads, has distinctly adverse implications for the private supply of capital, which in turn is vitally needed for investment in energy, housing, and other types of productive capital formation. The adverse implications extend beyond the boundaries of the New York financial markets to all thrift institutions across the country.

The more sophisticated investor has begun to question quite explicitly the value of any and all financial assets. A bond return of 8 percent, which was quite acceptable at a 3- to 4-percent inflation rate obviously does not provide anything in real terms at an inflation rate of 8 percent. Still higher bond and mortgage rates are not the answer, unless there is confidence in a stabilization, rather than further increases, of the inflation rate. What is needed here is concrete, positive reassurance through accomplishments rather than soothing words or paper controls.

The spending of inflation psychology is also continuing to express itself in increased use of escalator and reopening clauses in union contracts. The cost-push problem, and apprehensions over temporary palliatives such as price controls, has been a major factor in weakening the equities market—a vital source of risk capital. While a great deal of time and effort has been devoted to the structural problems of the stock exchanges and trading, all such efforts—and the possible improvements stemming therefrom—could be swamped by the erosive impact of inflation.

We therefore strongly urge the committee to pursue further the question of the impact of inflation on the financial markets, even if there is—perhaps especially if there is—disagreement with the point of view here expressed. The question is no longer a subject for academic debate but is coming close to a critical national concern.

MEMBERS OF THE COMMITTEE ON FINANCE AND CURRENCY

Francis H. Schott (chairman), vice president and economist, the Equitable Life Assurance Society of the United States.
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TAXATION WITH REPRESENTATION

By THOMAS F. FIELD, *Executive Director**

SUMMARY

Recent increases in the price of crude petroleum present two main problems: First, what should be done to lessen the impact of the large transfers of income from consumers to petroleum producers caused by these increases? Second, what is the appropriate future tax burden for the petroleum industry, in light of its changed circumstances?

The most satisfactory solution to these problems is repeal of the tax subsidies currently enjoyed by the petroleum industry, coupled with tax measures to shield those living in poverty from the effects of the recent price increases in petroleum and other products.

Specifically, the following tax subsidies and benefits should now be eliminated: the intangible drilling deduction, percentage depletion, and the overall foreign tax credit limitation. Furthermore, consideration should be given to establishing IRS authority to determine, on a facts and circumstances basis, whether foreign taxes on mineral production are actually disguised mineral royalties. These proposals, taken together, will raise $4 billion or more in new revenue.

Simultaneously, persons living in poverty should be relieved of the burden of social security taxes, through devices similar to the low-income allowance. Alternatively, the new revenues generated through reform of petroleum industry taxation could be used to make a modest start on a negative income tax program.

Price controls, and rollbacks are self-defeating, because they encourage consumption and discourage production. Special temporary taxes, such as the proposed windfall profits tax or an excess profits tax, are subject to a number of other serious objections.

I am grateful for this opportunity to offer testimony regarding the administration's December 19, 1973, proposal for an emergency windfall tax on receipts from the production of crude petroleum and other related proposals.

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Current Legislative Responses to Oil Problems

The recent sharp increases in petroleum prices, and the consequent increases in petroleum profits, pose two main problems:

Consumers are poorer, and petroleum firms much richer as a result of these price increases. This is the so-called income transfer problem.

The existence of very substantial oil company profits calls into question the need for continued tax subsidies for mineral producers. These profits also constitute a tempting target for additional taxation. The problem here is to determine the appropriate future tax burden for the petroleum industry, in light of its substantially increased revenues and earnings.

There have been three main responses, to date, to these problems:

First, there have been calls for price controls or price rollbacks. These proposals are aimed mainly at the income transfer problem.

Second, there have been proposals for the imposition of so-called windfall profits or excess profits taxes. These are aimed variously at the income transfer problem, the tax burden problem, or some combination of the two.

Third, there have been increasingly frequent calls for repeal of existing tax subsidies for petroleum producers. These proposals are aimed mainly at the tax burden problem.

Recommended Solutions

For reasons that I will outline in a moment, price controls and special temporary taxes are highly undesirable solutions to the problems that we now face. To me, by far the best alternatives available to this committee for coping with the problems resulting from the recent petroleum price increases are to repeal the existing tax subsidies for petroleum producers, and to provide relief to low-income consumers through the social security or income tax system.

The minimum steps needed to implement these recommendations are the following:

Repeal of section 263(c) of the Internal Revenue Code, relating to intangible drilling expenses. This step, taken alone,[1] would raise approximately $800 million in the coming fiscal year.

Repeal of section 613 of the Internal Revenue Code, relating to percentage depletion. This step, taken alone,[1] would raise approximately $2.6 billion in the coming fiscal year.

Repeal of section 904(a)(2), (b), and (e), relating to the overall foreign tax credit limitation. Revenue estimates are much more difficult here, but this step appears likely to raise at least $500 million in new revenue, and possibly much more.

In addition, I recommend that one or the other of the following proposals be adopted to relieve the poorest of our fellow citizens from the effects of the recent increases in the price of petroleum products—and, indeed, of prices generally:

First, the committee should lift the burden of social security taxation from the shoulders of those living in poverty, through use of a device similar to the low income allowance, or

[1] Because the percentage depletion and intangibles subsidies overlap to some degree, the revenue gain from repealing both subsidies simultaneously would be approximately $2.9 billion, not $3.4 billion.

Alternatively, the committee could use the revenues generated by increased tax payments by petroleum producers to begin a modest negative income tax program.

WHY PERCENTAGE DEPLETION AND THE INTANGIBLES DEDUCTION SHOULD NOW BE REPEALED

The traditional arguments for repealing percentage depletion and the intangibles deduction hardly need repeating. But they have lost none of their force in recent months. They include:

The lack of proof that either of these tax subsidies significantly increases our reserves of crude petroleum or otherwise contributes to national security.

The cost of these subsidies, currently about $3.4 billion annually,[2] and the tendency of these subsidies to grow as prices and profits increase.

The adverse effects of these subsidies on the fairness of the Federal tax system; indeed, percentage depletion has become a symbol of the tax favors that our revenue laws confer on special interests.

Added to these traditional arguments are new ones based on the petroleum industry's current profit picture. Today, oil industry claims that "incentives" are needed to attract capital for exploratory drilling and other related activities can be answered by pointing to:

The opportunity for self-financing inherent in the petroleum industry's financial situation, and

The attractiveness in the capital markets of securities issued by firms as profitable as the oil producers have now become.

Furthermore, the current price incentives enjoyed by the petroleum industry as a result of the increase in the price of crude oil dwarf any of the tax incentives provided by the Internal Revenue Code. For example, with crude oil selling at $6 per barrel, the tax saving attributable to percentage depletion is 66 cents.[3] Compared with the incentive provided by recent increases of $2.50 or more per barrel in the price of crude oil, the tax incentive is puny indeed. To argue for continued tax incentives for petroleum under these circumstances is to fall victim to cultural lag.

Moreover, our existing tax incentives for petroleum have failed to prevent the difficulties we are now experiencing; indeed, those tax incentives, by stimulating consumption, may actually have made our present situation worse. For that reason, "more of the same" is no answer to our present difficulties.

The price incentives and financial resources generated by the recent increase in the price of crude oil are so large, in fact, that we are likely to see vary sharp increases in petroleum production over the next few years. Indeed, if these prices hold at or near present levels, there is a distinct possibility of an oil glut by the middle of this decade. There is no need to further increase this coming glut by means of tax incentives that have outlived whatever usefulness they ever had.

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[2] This figure includes oil and gas subsidies of $2.9 billion—after taking into account the effects of the depletion-intangibles overlap—plus "hard mineral" subsidies of $500 million for coal, clamshells, sand and gravel, etc.

[3] The computation assumes a 50-percent tax rate and no restriction on depletion attributable to the 50 percent of net income limitation.

Underlying these arguments and recommendations is my conviction that the price system and the free market economy are the basic tools to be used to solve the petroleum supply problems now facing us. This means, among other things, that the petroleum industry can and should begin to make its way in the world without the crutch of Government tax subsidies.

Foreign Tax Credit Recommendations

As outlined earlier, I recommend repeal of the overall foreign tax credit limitation. This is a minimum step, which would be proper even if we were not experiencing petroleum supply problems. But it is also a way of coping to some degree with the problems caused by the conversion of deductible mineral royalty payments into creditable foreign "taxes."

There is nothing in the logic of the foreign tax credit mechanism—designed as it is to prevent double taxation of foreign earnings—which leads to the conclusion that excess foreign tax credits generated in one country should shelter earnings in other countries from U.S. tax. In fact, the per country tax credit limitation, which would remain in effect if the overall limitation is repealed, is the only tax credit limitation that is really consistent with the goal of eliminating double taxation of the overseas earnings of U.S. persons. To go further, by providing an overall tax credit limitation is, at best, an invitation to tax avoidance.

In the case of petroleum, a repeal of the overall foreign tax credit limitation would "bottle up" the excess credits generated in oil producing countries as a result of the creditability of royalty-type taxes, and would prevent those excess credits from being used to shelter shipping, refining and marketing income generated in non-oil-producing countries—income that would be fully or partially subject to U.S. tax in the absence of the overall foreign tax credit limitation. Thus, my proposal would put an end to the worst of the problems caused by the crediting of ersatz royalty type foreign mineral taxes against U.S. tax liabilities.

But simply repealing the overall limitation does not go to the heart of the problems created by royalty-type taxes on mineral production. There are strong grounds for believing that most or all of the "petroleum taxes" levied by oil producing countries are really disguised royalties; [4] if this is so, then all or most of these so-called taxes should be ineligible for the foreign tax credit. Accordingly, the committee may want to consider doing more than just repealing the overall foreign tax credit limitation as a means of dealing with the ersatz royalty tax problem.

If the committee decides that additional steps are appropriate in this area, I recommend that it consider enacting a mandate, similar to existing Code section 482, requiring the Internal Revenue Service to examine the taxes imposed by foreign countries on mineral production, and to determine on a facts and circumstances basis what portion of

[4] The small size of the Government expenditures in many oil producing countries for roads, education, and even defense, in comparison with the size of the "tax" payments they receive, casts doubt on the claim that those payments are in fact taxes to provide Government services, rather than disguised royalties. Furthermore, the Internal Revenue Service already treats "income taxes" on mineral production as noncreditable excises when computing transfer prices under section 482 of the Internal Revenue Code. Consistency requires that these taxes also be treated as excises for purposes of the foreign tax credit provided in section 901 of the Code.

those taxes are in fact creditable income taxes and what portion are deductible royalties. There are at least two ways in which the Service could do this:

The Service could examine and place a royalty value on foreign wells and mineral deposits, much as it now values closely held stock and other unique assets in decedents' estates. Only payments in excess of this royalty value would be treated as creditable taxes.

The Service could estimate what portion of these taxes are passed forward to the consumer in the form of higher prices, and could treat that portion as a noncreditable excise rather than as a creditable income tax. The Service already treats most of these taxes as excises for transfer pricing purposes under section 482 of the Internal Revenue Code.

It is undoubtedly true that these administrative determinations will be costly, since it will be necessary to hire experienced professional personnel to make them. But these administrative costs are trifling compared with the revenue losses now being experienced due to the perversion of the foreign tax credit mechanism by the crediting of royalty-type taxes on mineral production.

The Reasons for Rejecting Price Controls and Special Taxes

Price controls or attempted price rollbacks are the wrong way to deal with our present problems. Keeping a lid on prices will encourage consumption and discourage production. That is just the result that we don't want. The short term consumer benefits attributable to price rollbacks or controls will be obtained at the cost of longer term shortages—shortages that will generally affect those in poverty more severely than the affluent.

It follows that the attempt to control price increases through a windfall profits tax is equally objectionable. By interfering with the free market price mechanism, this tax will both choke off production that would otherwise have been forthcoming [5] and will stimulate consumption that would have been foregone by consumers due to cost.

The windfall profits tax proposal also suffers from a number of other serious defects:

It will discourage current petroleum production, because the tax on production in future years will be lower than the current tax. This gives oil producers a perverse incentive to leave their oil in the ground for the time being.

The windfall tax will add new complexities to the Internal Revenue Code, and the rates of tax ranging as high as 91 percent will encourage producers to litigate every aspect of their tax liabilities.

The windfall tax will do nothing to increase the fairness of the Internal Revenue Code, in contrast to repeal of percentage depletion and intangibles deduction.

The windfall tax is a temporary expedient, when what is needed is long term reform that will force the petroleum industry to forego continued dependence on tax subsidies.

[5] For example, if the market price of crude is say, $6, oil will be pumped from a stripper well even if the cost of production is $5.90. But the administration's windfall proposal would put a tax of 25 cents on this crude production, or 250 percent of the expected profit. Under these circumstances, the well, and all others like it, will be taken out of production.

Proposals for an excess profits tax are even less desirable than the proposed windfall tax. Those who wish to tax "excess" profits must first establish what profits are "normal," and this has proven to be an almost impossible task each time we have attempted to impose an excess profits tax.

I have had a good deal of experience with the Korean way excess profits tax, and I am also familiar with the working of the World War II statute. The most charitable thing I can say is that both statutes were administrative monstrosities. They were riddled with loopholes during the enactment process, the subsequent administrative regulations further weakened the already shaky statutory structure, and thousands of litigated cases established frequently inconsistent judicial rules which—due to the temporary nature of the tax—were never reconciled by Supreme Court review. The result was a tax that fell with undue harshness on some firms, and that others—generally the most profitable and intransigent—ended up paying less than their fair share. The rhetorical attractions of an "excess profits tax" are obvious. But a tax statute should be based on a firmer foundation than momentarily attractive political rhetoric.

Another proposal now frequently mentioned is the so-called plowback plan under which windfall or excess profits taxes would be forgiven, or tax credits or deductions granted, to the extent that petroleum firms plowed back their profits into exploratory drilling, the construction of new refineries, or the like. There are several serious problems with these proposals:

Current prices for petroleum products already give oil companies every incentive to drill wells or build refineries. Providing tax incentives to do the same thing is a costly waste of Government revenues.

Defining the activities that qualify for plowback treatment is an extremely difficult legal and engineering task, and the resulting definitions will have to be revised periodically as surplus capacity or new bottlenecks appear in the petroleum supply picture. Furthermore, administering a statute that is dependent on highly technical definitions will be an horrendous task.

Because petroleum industry investment in qualifying activities is already huge, the typical plowback proposal would actually impose few if any limitations on petroleum profits, credits, or deductions. If plowback proposals are more narrowly drawn to meet this objection, then the definitional and administrative problems become much more insoluble.

To draft any but the most slipshod statute, the Ways and Means Committee will have to make technical decisions about petroleum production and engineering matters. Decisions as to when and how to expand production are best left to a firm's managers.

Conclusion

The recent changes in the petroleum price and supply picture provide this committee with an opportunity to make a start on the job of genuine tax reform, while at the same time granting needed tax relief to those living in poverty. But this opportunity will be lost if the committee decides, instead, to concentrate on unsatisfactory temporary expedients such as the proposed windfall profits tax or an excess profits tax.

UNITED STATES SAVINGS AND LOAN LEAGUE

By Norman Strunk, *Executive Vice President*

We appreciate the opportunity to submit a statement for the record on current economic issues facing the Nation.

We recognize that there are many economic issues of importance which deserve attention, but believe that none is so important as that of inflation. When the economy approaches inflationary rates of the two-digit variety, many of the fundamental institutions of our society are threatened.

Slower rates of inflation have already eroded some of the fundamental supports of the economy, but higher rates seem likely to have extremely dangerous consequences. There is the danger that people will lose confidence in their savings, that there will be an effort to turn money and other liquid assets into goods, that there will be a psychology of spending now and worrying about the future later and that only a "boom and bust" scenario can be used to describe the probable future.

We need to recognize that we do not really understand the current wave of inflation which is not only affecting our economy, but that of many others throughout the world. We need to recognize, as Henry Wallich suggested recently, that traditional fiscal and monetary remedies for inflation have not worked in the present inflationary situation.

We recommend the declaration of a national policy against inflation. Such a declaration might take the form of a preamble to the extension of the Economic Stabilization Act and serve as a yardstick for measuring the various social, economic and financial policies adopted by Congress and the administration. It might serve as a policy guide in much the same way that the Employment Act of 1946 has served to set forth a full employment policy. Such a declaration of national policy against inflation was recommended by George Preston, the president of the U.S. League of Savings Associations in a speech to the California Savings and Loan League on February 27.[1]

We have applauded the efforts of the Federal Reserve to try to contain inflationary pressures although we have been disappointed in the results. We would recommend tax exemption allowances for personal savings to encourage higher savings levels and especially long-term savings at this time. If a corporate stockholder is entitled to a tax exclusion on the first $100 of dividends earned. then certainly the savings depositor in a financial institution is entitled to this kind of tax relief. Obviously, tax incentives for consumer savings would be an integral part of new strategies needed in the anti-inflation effort. Tax exemption may be tied into the Federal Reserve's "forced savings" concept.

[1] Excerpts from the speech appear at the end of this statement.

In recent years greater success in the fight on inflation has been impeded by a fear of increased unemployment. In order to break the political connection between inflation and unemployment, we urge that consideration be given to the abolition of unemployment by a law. This would require the Federal Government to provide either training or employment preferably through contracts with private organizations, but if necessary, with the Federal Government serving as the employer of last resort. This would require considerable modification of a number of present regulations including those related to minimum wages and various aspects of welfare programs. Machinery now used for the administration of unemployment insurance and compensation might be utilized to administer the kind of program suggested here.

It might be desirable for the Joint Economic Committee to sponsor extensive hearings on methods for containing inflation so as to make certain that the best ideas that may be prevalent can be collected together and perhaps joined in an all-out effort to attack inflation before it is too late.

EXCERPTS FROM AN ADDRESS OF GEORGE B. PRESTON, PRESIDENT, UNITED STATES LEAGUE OF SAVINGS ASSOCIATIONS, BEFORE THE CALIFORNIA SAVINGS AND LOAN LEAGUE, FEBRUARY 27, 1974

As some of you may have noticed in the last issue of "Washington Notes," the league officers and several senior staff members met with Chairman Burns of the Federal Reserve Board the day following our Legislative Conference in Washington. We had a leisurely visit of about an hour with Dr. Burns and I think we had ample opportunity to convey to him the feelings of the savings and loan business on many of the issues affecting our business.

Near the close of that conversation, Dr. Burns made a statement that ran generally along the lines that he knew of very few businesses that were as vulnerable to inflation as the savings and loan business. He thought the savings and loan business ought to be in the forefront of the fight against inflation.

Of course, he is completely correct. We have been through the tight money wringer three times in 8 years, and we know how vulnerable the business is to tight money conditions. This is why we—working along with the Federal Home Loan Bank Board—have made a very strong effort in recent years to strengthen the business and increase the flexibility of its operations. This is also why we have created a special Committee on Alternatives for Future Development, which will begin its work later this month and which I am very hopeful will develop a useful road map for the savings and loan business of the future.

We can work, and hopefully work successfully, to protect the business against inflation, but this does not protect the rest of the American people against inflation. If there is one thing that is certain about the period that we are in, it is that the current inflation is making it more and more difficult for the Government of the United States to function effectively and in an orderly manner. This is, of course, precisely what has happened in other countries where inflation has run out of control.

It is no coincidence that major opinion polls indicate that the primary concern of Americans is inflation and that the same polls indicate that the prestige of our major bodies of Government is at an all-time low. For inflation not only threatens pocketbooks, it also threatens the ability of Government officials to govern. More than most people realize, inflation invites disorder and strife.

Few subjects, of course, receive more discussion in Washington these days than inflation. Yet, I have yet to see a clear and precise declaration of national policy on inflation. We have the Housing Act of 1949 which promises a decent home for every American family, a declaration reaffirmed in the Housing Act of 1968. We have the Employment Act of 1946 which holds out the prospect of a job for every able American seeking work. These are landmark declarations of public policy and there are references to them, year-in and year-out, when matters of housing policy and economic policy are discussed in Congress.

It seems to me a clear public statement on inflation could also become a yardstick against which various social, economic and financial policies of the country may be measured.

It is argued by many economists that if we curb Federal spending, and if we employ a more restrictive monetary policy, this will solve the inflation problem. Perhaps the proponents of this view are right and perhaps they are wrong. We had a moderate monetary policy during 1973 and we will have—by far—the smallest budget deficit in 4 years for the period ending June 30. Yet the United States today is caught in the worst storm of inflation in its history. The problem of inflation may be so complex that it may not necessarily be solved to the satisfaction of this country through orthodox monetary and fiscal policies. This is why I would like to see a declaration of public policy on inflation that would be broad enough in its scope of purpose to hold out hope for those tens of millions of Americans whose real purchasing power has been eroded in recent years.

One senses a feeling of despair and hopelessness in the statements coming out of Washington. Let us remember one thing; this inflation was not created by the supernatural; it is manmade, the product of many mistakes and bad judgments. More than perhaps anything else, we need confidence that inflation can be checked and brought under control; for that confidence is essential to the development of a broad, comprehensive and persistent strategy to deal with inflation.

JERRY VOORHIS, FORMER MEMBER OF CONGRESS

For the second time during the Nixon regime the Nation faces what traditional economists have always said was impossible: A combination of galloping price inflation and economic recession with spreading unemployment.

How it has been possible in the short space of 5 years for misguided policies twice to perform this economic miracle must therefore be the opening subject for this statement.

First with respect to inflation.

The basic causes of the price inflation have not been attacked or even discussed by the administration but have been exacerbated by its policies. Policies, incidentally which the Congress has not been able to muster the necessary two-thirds majorities to reverse.

It is important to note that the strongest of these inflationary forces are immune to market conditions, that is, they tend to force prices up even when the economy is in recession.

Before we discuss these basic causes it is well to say what have not been the causes of the extraordinary price inflation. The price inflation has not been caused by excessive increases in salaries and wages. In fact, in 1973 the wage and salary workers of the Nation actually lost buying power, which is to say that such increases in wages as took place where not enough to keep up with price increases. Neither has an excessive supply of money been an important cause of the inflation. The money supply has not been increasing particularly rapidly.

What then have been, and are, the causes of the sharpest sustained inflation in our country's history culminating in an 8.8 percent inflation for the the year 1973?

First basic cause is clearly the unbroken succession of deficit budgets of the Nixon administration—the total of which has now added about $90 billion to the national debt of the American people, almost one-fifth of their total alltime debt. Had Congress not cut Mr. Nixon's budget requests by more than $20 billion the deficit and debt problem would have been even more severe. Governmental deficits are always an inflationary influence and no exposition of this fact is needed.

Second cause of price inflation is governmental expenditures which do not produce marketable commodities or add to the supply of useful goods or services. Mainly these are military expenditures and those devoted to space exploration. Military expenditures have been rising sharply, despite efforts by some Members of Congress to cut the fat out of them. They now approach $100 billion a year. Every dollar of such expenditures—as well as those for space exploration and some other economically wasteful and nonproductive purposes—is an inflationary dollar.

This is true because such expenditures pour vast sums of money into the purchasing power of the Nation—that is on the demand side—while they produce nothing on the supply side which can be bought with those billions. The result, therefore, must be an intense upward pressure on the prices of goods and services produced in the productive segment of the economy, even if there is widespread unemployment and recession.

The third major cause of price inflation has been, and is, the extortinate interest rates that have been in effect during the past 7 or 8 years and particularly in the past 2 years. Orthodox economists have for years claimed that high interest rates tended to curb inflation. The record proves them wrong. The only circumstance in which high interest rates curb inflation is if they actually bring on a depression. In that case not only will prices in competitive industries, if any come tubling down but so will the entire economy of the Nation. In the absence of such a complete disaster, however, high interest rates cause rather than retard price inflation. It requires no trained economist to see why. The cost of borrowing is an element in the cost of doing business. When interest costs are doubled, as roughly they have been in the past 6 or 7 years, then businesses must add twice as big a sum to their prices to cover the cost of borrowed money as before and if any proof is needed to demonstrate this it is readily available from the record of 1973. Interest rates were at an alltime high, with prime rates between 9 and 10 percent during practically the entire year. Not despite this but in large part because of it price inflation also reached a record level.

The higher the interest rate the greater the upward pressure on prices because of the increased cost of doing business.

Furthermore high interest shuts off much productive activity that would take place were lower rates in effect. The construction industry is an example. Lower cost houses simply cannot be built if contractors must pay 10 percent or even 6 or 7 percent, for money. Supply is therefore curtailed and this inevitably brings about upward pressure on the costs of the lesser numbers of houses available.

Fourth cause of price inflation is scarcity. The incredible sale of a quarter of the nations wheat to Russia at prices far below those charged anyone else brought almost an estimated $1 billion increase in the cost of bread to American families. Also by causing a critical shortage of feed grains it had the effect of so increasing farmers' costs in production of livestock that sharp rises took place in all animal products.

If the administration persists in its policy of sacrificing the American dairy farmer in order to bring about increased exports of other farm products, then it is already evident that thousands of dairymen will go out of business and we may be faced with a shortage of dairy products, including children's milk.

What the shortage—real or contrived—of energy, especially petroleum, has done to prices in that field is all too painfully evident to require comment.

Fifth and finally there is the major, continuing and, by the Nixon administration actually encouraged, cause of price inflation. That cause is monopolistic or "administered" pricing of commodities. If for example the so-called law of supply and demand were operating at all in the automobile industry we would at present be experiencing a sharp decline in automobile prices. Not so. Although dealers have unsalable cars running out of their ears, the big three manufacturers who completely dominate the industry ask for, and receive from the Cost of Living Council higher prices.

The simple fact is that there is now, and has been for years past, no price competition at all in the automobile industry. Or in meat packing, containers, steel, farm machinery, aluminum, oil, breakfast food, electric appliances, chemicals, detergents or a dozen other key industries.

Wherever two, three, or four huge corporations control an industry they are able to dictate prices, regardless of market conditions. And they always raise prices, never lower them. Their rule is to maintain their profit margins and to that end they welcome a scarcity of their commodity relative to effective demand. If the market is slack and fewer sales are being made then the prices are raised so as to realize a higher profit in each unit sold.

Hence to the extent that monopoly rules our economy—as it increasingly is doing—there is a built-in assurance of continuing price inflation.

There are remedies.

One is vigorous antitrust enforcement to restore competition and some resemblance to a free enterprise economy. But under the Nixon administration just the opposite has been done and all sorts of crass violations of the spirit and letter of the law have been permitted and sometimes encouraged. The Warner-Lambert and Parke-Davis drug merger, and the swallowing of Hartford Insurance by ITT are only two examples. Another is the resistance of the administration to the attempt of its own Federal Trade Commission to bring eight major oil companies to the bar of justice for price manipulation and other measures calculated to eliminate competition of the few remaining independents.

Another remedy is the remedy by yardstick. When the Tennessee Valley Authority began to distribute electric energy at something like its real cost, all utility rates in regions adjacent to the area of TVA operations came tumbling down. The same result took place when rural electric cooperatives began operations.

Either we need a massive encouragement to the growth of privately owned cooperative businesses—that is businesses belonging to and controlled by their patrons and customers—or else we need publicly owned corporations that can break the back of monopoly control of price and supply.

Inflation will plague this Nation until its basic causes are attacked—until we reduce military expenditures to what our real national defense needs are—without graft or waste or cost overruns, until we suspend trips to the Moon pending our conquest of inflation on the Earth, until we enforce the antitrust laws or create public corporations as yardsticks, and until interest rates are brought down to life size as Congress long ago empowered the President to do but which he has never lifted a finger to accomplish.

Meanwhile the only immediate answer appears to be imposition of controls on prices at least in industries affected by monopolistic controls.

As for unemployment the first requisite is to be concerned about it. The callous attitude of the administration has always been that "we can tolerate a 6-percent unemployment rate"—to quote an administration spokesman. The question is who can tolerate it. Certainly not the people who lose their jobs. To deny a man or woman the right to earn a living for self and family by honest labor is a social crime and sin.

Congress once enacted a piece of legislation that was squarely on target if we really want to do something about unemployment. That was the Nelson-O'Hara bill which would have created some 500,000 jobs in public-service employment. That bill was passed in 1971 by both Houses of Congress but vetoed by Mr. Nixon.

The highly technical economy of today has eliminated most of the kinds of jobs on which disadvantaged, semiskilled, or unskilled people once relied. And this process is continuing. To expect to reemploy any considerable number of the rising number of unemployed at the production of more physical commodities is to be naive. I realize that the administration is talking about following in Hitler's footsteps by expanding employment in the manufacture of weapons of war. But such employment requires more dollars, energy, and scarce materials per person employed than does any other field of employment.

Meanwhile a whole host of national needs are being sadly neglected. Among them are adequate police and fire protection, environmental cleanup, reforestation, mass transit, core city renovation, education, child care for children of working mothers, and health care. In all these fields there is work to be done at which the people presently unemployed can be put to work and, if necessary, trained on the job. Or trained beforehand. And most of such public service employment does not require consumption of much power. Which, today is certainly an important consideration.

The Supreme Court has recently ruled that it is unconstitutional to expect children to go to school in a foreign language. In other words, to take the big example, there must be billingual education for children whose families speak Spanish. There is, therefore, a need for thousands of teachers' aides to bring hundreds of schools into compliance with the decision of the court.

This is but one example.

The question is whether we really want to make critically needed work available to several million Americans or whether we want to force them to depend on what we euphemistically call "welfare."

Tempting as it is to write a small book on economics in response to the committee's invitation, this statement will be confined to just one more subject—the present "energy crisis."

To add to the Nation's woes an "energy crisis" which had been coming on for years and about which environmentalists and the National Rural Electric Cooperative Association have issued repeated warnings was suddenly announced by the Nixon administration and the oil companies late in 1973. That the crisis is real for the long run of American life there can be no possible doubt. How severe its immediate impact had to be is known only to the major oil companies and other suppliers of energy to the Nation. Certainly the people are, to say the least, skeptical.

As long ago as my own service (1937–47) in the House of Representatives, other Members and I were complaining on the floor of the House of the fact that the U.S. Government had then, as it has today, no information of its own about reserves or potential supplies of oil or or other sources of energy in the Nation.

In all the intervening years nothing has been done to correct this condition. The United States still depends for information about the petroleum industry upon what that industry decides to tell us. And it has resisted—and continues to resist—with all its very considerable political power every effort of the Congress to establish a means whereby the Nation might know what its available supplies of oil or its fossile fuel reserves actually are.

During my 10 years in Congress of some 30 years ago, we were regularly informed that oil reserves would probably last for 10 years. Year after year it was the same story. We had 10 years' reserves to look forward to. Essentially the same story is being told to us today. Maybe this time it is actually true. But no one knows except the oil companies.

And they, of course, won't tell.

The only clear statements that have come from the major oil companies have been to the effect that if Congress dares lay a hand on them, through rollback of prices or levying of an excess profits tax, then they simply won't even try to supply the Nation. The industry that has enjoyed the biggest profits and paid—by a country mile—the lowest taxes demands still more governmental subsidy or it just won't "play ball."

And yet as this is written it is administration policy to give this greedy industry as high prices as it wants and thus to ration the use of petroleum products to those wealthy enough to afford them.

Furthermore the major oil companies are well on their way again with ample assistance from the administration, to establishing for themselves an effective monopoly of energy sources. Already they own most of the national gas and practically all the pipelines, and many of the largest coal companies. And now the Interior Department is apparently about to lease to them the choicest sites for geothermal development, the mountain shale deposits and even the production of enriched uranium—a process for development of which the taxpayers of the Nation have paid an estimated $12 billion. The Justice Department ought to intervene in such leasing to prevent the leases contributing to monopoly. But it probably won't.

Whether or not the present "energy crisis" is real or contrived we cannot know. We do know that it is ridiculous to contend that it came upon us suddenly just at the time when Mr. Nixon most needed it to divert attention from Watergate and when the oil companies and other energy producing enterprises could use it to exact profiteering prices to eliminate competion, add to bring about suspension if not abolition of every measure to try to save the environment of the Earth.

Environmentalists have been warning of the coming of an energy shortage for a decade. Why was the voice not listened to until now?

It is noteworthy that almost every proposal advanced by the administration for increasing the supply of energy is one that threatens the environment. Use of high-sulfur coal, strip mining, relaxation of clean-air standards for automobiles and above all development of fast-breeder nuclear reactors for the lethal wastes from which no one has the slightest idea of a safe method of disposal, these are only examples.

Hydroelectric, an abundantly proven source of absolutely clean power, has been completely neglected by the present administration, probably at the behest of the so-called public utilities.

What Congress should do is to enact the legislation proposed by Senators Jackson, Mondale, and Muskie for a $20 billion crash program for the development of clean sources of energy in this country. If we spent half the effort on such a vitally necessary enterprise as this as we spend on weapon development or filling space with hardware there could be hope again. Senator Cranston's bill for solar energy development should also be quickly enacted.

But the job must not be entrusted to agencies which have, with all their power and resources, opposed through the years every kind of alternate sources of energy except the ones they themselves control. A number of major oil companies spent, secretly, large sums of money to prevent the people of California from voting for an initiative that would have allowed the State and cities to spend part of the gasoline tax money on development of mass transit instead of paving the best agricultural land of the State with more highways. And every effort to bring about development of pollution-free automobiles has met the bitter and determined opposition of both the oil and automobile companies.

We are just beginning to find out that it was covert action of General Motors and Standard Oil that destroyed the commuter rail services in many parts of the country so they could be replaced with GM manufactured buses burning Standard's gasoline.

These are again examples.

What they illustrate is a relatively simple fact. If we want to solve the energy problem of the country we had better entrust the job to agencies that want to do it, not to those with a vested interest in preventing its being done.

As was said before in discussing monopoly there are two kinds of agencies that have a motivation to provide the Nation with clean energy. One of them, and the most obvious one, is the Government itself. Its only interest is in the welfare of its people. At least we must believe that to be the case, despite contrary evidence in the past 5 years.

Therefore legislation to establish a publicly owned corporation with power and resources to develop every kind of energy is the rock-bottom requirement of the present hour. The bill introduced by Senator Stevenson of Illinois could be the answer. It should be enacted into law.

If it be desired to entrust part of the task to private enterprise then there is a way to do that. For, like the Government, cooperative business enterprises have a clear motivation to meet their members and patrons needs, as fully and in the best way they can. The coops lost a great deal of money recently. Deliberately. For they refused to export fertilizer when foreign prices were higher than domestic ones. They did this to supply their patrons. And they have taken losses on fuel in order to deliver it to their patrons at lowest possible cost. (Contrast oil companies' actions!) Those members and patrons are also the owners of cooperative businesses. Such businesses have no reason to profiteer at their owners' expenses, to fail to reveal all facets or to protect vested interests. Some of the cooperatives, especially those belonging to farmers, are big enough to undertake assignments for large-scale energy development. Certainly the rural electric cooperatives are capable of doing so. But the cooperatives lack the necessary capital. And either outright grants or long-term direct Government loans at low interest would be necessary to enable them to participate significantly in clean energy development.

But even if every possible measure shall have been taken to increase the supply of clean nonpolluting energy sources, there remains the stark fact that even under the best of circumstances the people of the United States cannot go on consuming energy even at the present rate without dooming the environment of the Earth.

And here let us commend the proposals of the administration as well as everyone else who has made proposals for the saving and conservation of energy. Lower speed limits, better insulated buildings, an end to glassy air-conditioned skyscrapers, mass transit as a substitute for the private automobile, sharp revival of railroads for both passenger and freight handling even if it takes Government ownership to bring it about, these and every other measure, including the rationing of the use of gasoline and other forms of energy are going to have to become part of a new and simpler American life style.

And we will learn to like it.

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