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CONGRESS OF THE UNITED STATES

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THE 1977 ECONOMIC REPORT OF THE PRESIDENT

THURSDAY, FEBRUARY 10, 1977

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

The committee met, pursuant to recess, at 10 a.m., in room 1202, Dirksen Senate Office Building, Hon. Richard Bolling (chairman of the committee) presiding.

Present: Representatives Bolling, Moorhead, and Long; and Senators Proxmire, Javits, and Percy.

Also present: John R. Stark, executive director; Louis C. Krauthoff II and Courtenay M. Slater, assistant directors; William R. Buechner, William A. Cox, Kent H. Hughes, Sarah Jackson, John R. Karlik, and L. Douglas Lee, professional staff members; and Charles H. Bradford, George D. Krumbhaar, Jr., M. Catherine Miller, and Mark R. Policinski, minority professional staff members.

OPENING STATEMENT OF REPRESENTATIVE BOLLING, CHAIRMAN

Representative BOLLING. The committee will be in order.

I just learned that the Democrats in the Senate are having a caucus to decide on committee assignments. I think I will go ahead while Senator Proxmire is here. He will have to leave but will be back. Normally on this committee people wander in after we get started.

We are very pleased to have as our witnesses this morning Mrs. Juanita Kreps, Secretary of Commerce, and Mr. Ray Marshall, Secretary of Labor.

I want to welcome both of you on your first visit to this committee in your new official capacities. I want to thank you for coming here to testify on the state of the economy and on the President's economic program.

Our witnesses up until now have been able to provide us with some general ideas about the impact of the President's economic proposals. Our two witnesses today are in the unique position of being able to testify not only on the overall impact but also on the structure and effectiveness of some of the proposed job creation efforts. This administration has done a remarkable job in presenting major economic programs within a week of taking office. Our questions and criticisms today should not be allowed to detract from the basic fact that we welcome the prompt and intensive way in which the new administration is approaching the urgent challenge of bringing down unemployment.

We think the administration has a good program. We want to see if we can make it even better.

First we will, hear from Secretary Kreps. You may proceed precisely as you wish. You may summarize or read it all.

STATEMENT OF HON. JUANITA M. KREPS, SECRETARY OF COMMERCE, ACCOMPANIED BY LUCY A. FALCONE, STAFF ASSISTANT

Secretary KREPS. Thank you. Mr. Chairman and members of the committee, I appreciate the opportunity you have afforded me to testify on the President's economic recovery package. I trust that this meeting today will continue a long and fruitful relationship between the Department and the Joint Economic Committee.

Thank you, too, for your remarks regarding the administration's economic package which we will discuss in some detail; Ray Marshall and I are here, as you indicated, primarily to talk about those jobs programs within our Department.

First, I have some preliminary remarks on the state of the economy. The recovery as you know from the 1973–75 recession has now passed through three different stages: The very brisk, if somewhat irregular, growth from the first quarter of 1975 through the first quarter of 1976; a somewhat slower growth after the first quarter of 1976; and finally, a very modest pickup at the end of 1976.

To avoid a prolonged period of unsatisfactory growth, the President has recommended a package with which you are so familiar now, $31.2 billion, spread over 2 years.

We feel that the costs of failing to achieve the full potential of our economy in the last several years have been enormous.

In 1976, the U.S. economy operated $132 billion below its high employment potential, based on estimates of the outgoing Council of Economic Advisers. The $1,800 lost by the average household as a result of his economic waste dwarfs even the most pessimistic estimates of the impact from the extreme cold temperatures of the past 6 weeks. Unlike the added expenses associated with this cold weather, however, the economic costs of underutilized resources are a continuous drain on our economy.

Even the stimulus package recommended by the administration will not result in the economy operating near its potential until the end of the decade. We must try now to create an economic climate that will maintain output equal to the economy's potential in the decade of the 1980's and beyond.

You have already received testimony on the overall impact and timing of this stimulus package. This morning, I want to focus on two aspects of the recovery which are of concern to the Department of Commerce: The outlook for business investment and the implementation of an expanded local public works program.

First consider business investment.

Early last year, business fixed investment expenditures had been widely expected to provide a major stimulus to continued economic growth in the second half of 1976 and in 1977. However, due in part to the more moderate rates of economic growth experienced after the first quarter in 1976 and only moderate improvement in the rate of capacity utilization, the acceleration in investment expenditures has, as you know, failed to materialize.

For 1976, business fixed investment increased in real terms by slightly less than 4 percent, a remarkably low rate of growth for the second year of an economic recovery. Both major components, that is, nonresidential structures and producers durable equipment, grew at low rates. In the final quarter of 1976, expeditures in real terms remained about 12 percent below the peak rates reached in early 1974. This is in sharp contrast to overall economic activity, which regained its previous peak in the first quarter of 1976 and by the fourth quarter had increased by another 3 percent.

One of the major contributing factors to the disappointing recovery in business investment has been lagging consumer demand. Consumers are spending a high proportion of their income, but the recovery in consumer income in 1975–76 has been only a little more than half as large as the average for previous postwar recoveries.

Significant portions of this country's physical capacity remain idle. The Bureau of Economic Analysis estimates that in September of last year, the capacity utilization rate in manufacturing averaged only about 80 percent. The low rate of growth in the fourth quarter of last year suggests that December's estimate, when it is released, will show little change. Let me emphasize that during the period from early 1973 to early 1975, the utilization rate declined by 11 percentage points, from 86 to 75 percent. In the economic recovery to date, only 5 of these 11 percentage points have been regained. It should come as no surprise, therefore, that investment expenditures are growing only modestly.

Another factor which may have contributed to the sluggish recovery of investment last year is the continuing concern of business about long-term inflationary impact.

These factors dictated the major thrust of the President's economic program. To create jobs and a demand for products that will provide the stimulus for continued growth and capital expansion. At the same time, to avoid the possibility of future capacity bottlenecks as the economy expands, the President also has proposed an optional increase in the investment tax credit to 12 percent.

The size of the recovery package reflects dual priorities—one, to provide enough stimulus to put the economy on a solid recovery path: the other to avoid excess stimulation that would trigger higher rates of inflation.

A question before us is this: How rapidly will real investment expenditures grow in 1977? The Bureau of Economic Analysis conducts two surveys of capital spending plans at the end of each calendar year to assess likely trends.

According to these surveys conducted in late 1976, in 1977 business expects to spend about $135 billion for plant and equipment, an increase of 11.3 percent over 1976. If prices should increase at the same rate as in 1976, this would imply a 6.5-percent increase in real expenditures.

This real growth is, however, distributed unevenly through 1977. In the first half of 1977, real investment expenditures are expected to increase very little, but they are expected to accelerate sharply in the second half.

Spending plans may be revised upward this year, because the surveys were conducted in November and December—before the administration's tax incentives to business were announced and before it was generally realized that the slowdown in economic growth was ending. Recent energy problems may stimulate additional capital spending for alternate fuel capability.

The economic stimulus package coming on top of a moderate economic recovery, will soon boost the level of output and increase capital utilization. This, combined with the added incentive of a larger investment tax credit, should accelerate the recovery.

The President's economic program will take an important step in the direction of stimulating investment expenditures, not only to insure a more rapid rate of economic growth in the immediate future, but also to provide a foundation for addressing the long-term needs of our country. Further actions to strengthen business confidence in the outlook, including regulatory reform, and increased emphasis on research and development will reinforce the expected acceleration.

I turn now to the area of local public works. That component of the stimulus program for which the Department of Commerce is responsible is, of course, the expansion of local public works (LPW). As part of the administration's economic recovery package, the President has recommended a $4 billion increase in authorization for local public works projects.

This program offers the President and the Congress an ideal vehicle for alleviating the extremely high levels of unemployment in many communities and in the construction industry by creating jobs in the private sector. At the same time, it provides an opportunity for constructing vitally needed public facilities which will result in meaningful benefits to many of our Nation's communities. I know of no stronger testimony to the need for this program than the overwhelming response received by the Economic Development Administration to the first round of appropriations for LPW—where, as you know, we received $24 billion in applications for the $2 billion we had available.

The evidence of need for additional stimulus to local public works is corroborated by the decline in construction by State and local governments in the last 2 years, as falling tax revenues reduced local capital budgets. As shown in attached table 1, expenditures for State and local construction in real terms declined 6.5 percent in 1975 and 9 percent in 1976.

The projects approved during the first round of LPW, authorized and funded by Congress late last year, reflect a wide range of local priorities. Almost 2,000 projects were approved throughout the country, the largest percentage being in public buildings and water, sewer, and drainage projects as shown in attached table 2.

As many members of this committee are aware, the allocation of assistance for local public works projects resulted in some inequities. A few local governments with significant needs were bypassed, while projects of some local governments with lesser needs came to be funded.

The Economic Development Administration, at my direction, has just completed a thorough review of the legislation, regulations, and the implementation of the existing LPW program. We have completed our specific recommendations for change in the program and have made these available to the public works committees.

We look forward to working with Members of Congress in improving the legislation, formulas, and the regulations for allocating the second phase of the program.

In the past, the use of public works as a countercyclical tool has sometimes been criticized because of the long leadtimes involved in construction. I do not believe that this criticism is valid with respect to the current program for these reasons:

1. The legislation requires that onsite construction begin within 90 days of grant approval.

2. The 20,000 projects in EDA's inventory are, so to speak, on the shelf. Local governments in most cases have already completed architectural plans for these projects and therefore, the leadtimes should be minimal.

3. A 2- to 3-year construction period is not disadvantageous at the present time since unemployment is expected to be at higher than acceptable levels for several years. Thus, we need long-term stimulus.

I will direct the Economic Development Administration to proceed with any expansion of this program as quickly and efficiently as possible. Furthermore, I can assure you that EDA will make every effort to maximize the countercyclical impact of LPW by close monitoring of the construction process.

Mr. Chairman, that concludes my prepared remarks. I would be pleased to answer any questions you may have.

[The tables attached to Secretary Kreps' statement follow:]

TABLE 1.—STATE AND LOCAL GOVERNMENT PURCHASES OF GOODS AND SERVICES

[In billions of 1972 dollars]

	Total		Structures	
	Dollar amount	Percentage change from previous year	Dollar amount	Percentage change from previous year
1972	$151.0	3.9	$26.4	−4.7
1973	155.9	3.2	26.2	−.8
1974	161.1	3.3	26.1	−.4
1975	165.2	2.5	24.4	−6.5
1976	167.5	1.4	22.2	−9.0
1975:				
I	162.2	1.3	23.5	−12.0
II	163.8	1.5	23.6	−12.6
III	166.9	3.5	25.7	−.4
IV	168.0	4.0	25.0	.4
1976:				
I	166.6	4.4	22.7	−3.4
II	167.7	2.4	22.6	−4.2
III	168.2	.8	22.4	−12.8
IV	167.7	−.2	20.9	−16.4

Note.—1976 4th quarter and annual figures preliminary. Quarterly data at seasonally adjusted annual rates.

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

TABLE 2.—EDA SCORED, SELECTED LPW PROJECT TYPES FINANCED UNDER TITLE I OF THE PUBLIC WORKS EMPLOYMENT ACT OF 1976

Category and description of projects	Amount	Percent
1—Public buildings (e.g., town halls, court houses, minicipal offices, libraries	$481,112,645	24.6
2—Water, sewer, and drainage	405,664,549	20.7
3—Schools	372,846,575	19.1
4—Streets, roads and/or bridges	179,228,619	9.2
5—Public safety detention facilities	97,681,176	5.0
6—Recreation buildings and parks	78,771,824	4.0
7—Hospitals	62,365,658	3.2
8—Industrial development	50,225,560	2.6
9—Miscellaneous or multiple civil works	119,354,303	6.1
10—Miscellaneous or multiple building	91,378,624	4.7
11—Miscellaneous or multiple not classified elsewhere	16,767,109	.8
Total	1,955,406,642	100.0

Note.—$2,000,000,000 already funded in 1977.

Representative BOLLING. Thank you very much.
Secretary Marshall.

STATEMENT OF HON. F. RAY MARSHALL, SECRETARY OF LABOR, ACCOMPANIED BY WILLIAM B. HEWITT, ACTING ASSISTANT SECRETARY, EMPLOYMENT AND TRAINING ADMINISTRATION

Secretary MARSHALL. Thank you, Mr. Chairman and members of the committee. I welcome this opportunity to participate in your annual hearings on the state of the economy. The influential role played by this committee in providing leadership and perspective on the Nation's economic outlook is well-known. While this is my first appearance as Secretary of Labor before the committee, I look forward to a long and continuing relationship with you.

Accompanying me today is Mr. William B. Hewitt, Acting Assistant Secretary of Labor for Employment and Training. I would like to concentrate my attention primarily on the part of the economic recovery package that is the responsibility of the Department of Labor; namely, the employment and training component of that package. Other members of the administration have testified on other parts. Secretary Kreps has just concluded her discussion of the Public Works component. Other members have talked about the tax and other parts of that package.

The perspective to be taken by the Department of Labor is that unemployment is a serious problem and that we ought to do everything that we can to effectively diminish it. We are not persuaded by arguments that because the composition of unemployment might be new, that there is therefore any less of a problem. We are well aware of the significant material and human impacts of unemployment.

We also know that the impact of unemployment on people varies a good bit according to place and according to particular groups within the population. We believe that the best way to bring unemployment down is to concentrate and to target our activities in those areas with the highest unemployment and among those people with the highest level of unemployment. Our programs are, for the most part, based on that assumption, that we need to establish priorities and to concentrate on those groups with the highest levels of unemployment.

To be more specific, we need to concentrate on minorities, young people, veterans, and especially Vietnam era veterans, and on rural and urban areas with inordinately high levels of unemployment.

I might say just a bit about the economic outlook. Others have discussed that with some precision, and I have some comments on that in my paper. I think it is sufficient to make the point that while there might be some doubt about the precision of the estimates on the economic outlook, there is no doubt about the need for stimulus; and that economic growth will not be fast enough to reduce unemployment by very much without this stimulus.

Let me turn to the employment and training part of this package. The first part of this particular component is public service employment. We base our public service employment program on a number of assumptions. One is that the most important way to reduce unemployment in quantitative terms, is in the private sector; and that public service employment for the most part is seen as a temporary approach to the problem of unemployment. However, we also recognize that because there will always be some structural unemployment, that is that there will be cases where people have trouble finding work, even when unemployment is very low; there will be the need for some continuing, relatively small level of public service employment. We hope that it will be a relatively small component.

We also recognize that in all of our employment and training efforts in the Department of Labor, it is very important for us to involve the private sector as much as we can and to attempt to establish linkages between public service employment and public training programs and the private sector, because clearly, since five-sixths of all jobs are in the private sector, if we are going to make a lasting impact on unemployment, we must concentrate on measures to get more jobs and get more people employed in the private sector.

Another consideration that we have in our public service employment program is that we are trying to do everything that we can to see that the public service jobs provide meaningful employment and that useful things are done.

It is our view that it is unnecessary to have make-work when so many things need to be done in our society. We are endeavoring to see to it to the extent that we can that we accomplish this objective and that the work done is meaningful and that the programs are administered as efficiently as we can cause them to be administered.

We think that if we do that, the public service employment component of the package provides rich dividends for society. As I mentioned, one dividend is that we target on the high levels of unemployment and among people with high unemployment rates. Another dividend that the society gets from public service employment is that we reduce other public expenditures. We believe that it is much better where possible and practical to have people involved in public service employment than to have them on extended unemployment insurance or on the income maintenance program. It is better for them and better for society if we can provide meaningful jobs and meaningful output.

We also recognize that these programs cannot be expanded overnight. This is one of the most important concerns that we have. It is because we are frequently asked if public service employment has all the advantages that we say, then why don't we expand the program much faster than we have?

Well, the answer to that is that we wanted the work to be meaningful, and we wanted the programs to be well administered so that we did not want to expand faster than we thought our delivery capability could carry us.

We are proposing to expand the program very rapidly. We are proposing to virtually double the public service employment program in about 6 months, which means that we are increasing at the annual rate of quadrupling the program. It will have gone from 310,000 jobs currently authorized to 600,000 by the end of this fiscal year; and then in fiscal 1978, to 725,000, which is a fairly rapid increase in the public service employment program. We think that with the best estimates that we can make, that this was about as fast as we could prudently go with that program.

Another component of our package is training; and here again we are trying to target our training programs on people with special needs. We are proposing some special initiatives. One is a new youth initiative which we think we can do initially within the CETA Act as it currently exists. What we hope to do is to collect a number of youth programs to provide kind of an umbrella for—in order to give greater visibility and greater coordination of youth programs while we are preparing a long-range youth initiative.

As part of that process, we propose a doubling of the Job Corps, going from 22,000 slot now to double that number. This will mean, of course, many more individual participants in the Job Corps program, because each of these slots is used for about two participants, since the average duration is about 6 months.

Another new initiative in this area is to expand apprenticeship training. Our evidence shows very strongly that apprenticeship training is good training, that people who complete apprenticeship programs have higher earnings, less unemployment, and are upgraded much faster than people who do not finish apprenticeship programs.

The basic rationale behind apprenticeship is that people learn the theory of their trades as well as practical-on-the-job training, and that this makes them more flexible and produces well-rounded craftsmen.

We think it unfortunate that the on-the-job training component of the Labor Department's effort declined under CETA. Therefore, we want to try to do some things to increase on-the-job training. We think one of the most important things we can do is to get the private sector involved. The reason that we are concerned about on-the-job training is that it is a more effective training procedure for many kinds of training than institutional training. In addition, it is relatively inexpensive training. It is good from both of those perspectives. But in order to have an adequate on-the-job training program, we must have the involvement of the private sector. The President has proposed to do that, to meet with leading business and union people in order to get their involvement in our employment and training efforts.

We also have launched a new veterans' initiative. As you know, unemployment rates among veterans, particularly Vietnam-era veterans, all much higher than among nonveterans in the same age group. We don't know all the reasons for this, but we know it is a serious problem and that the country has an obligation to do something to help veterans catch up to their age groups who did not serve in the Vietnam War or who were not in the armed services during that period.

Our veterans' program has three major initiatives to it. One is what we call a "HIRE" program, to try to involve the private sector in hiring and training Vietnam-era veterans.

A second component is to try to establish public service employment hiring goals under CETA for the Vietnam-era veterans. We also proposed a special program for disabled veterans, who suffer much more than other veterans, to establish a veterans' outreach program in employment service offices in major cities. We propose putting about 2,000 disabled veterans to reach out to other disabled veterans to make employment and training services available to them.

What we found from our experience is that you cannot simply make services available and assume that people who need them will get them. What you frequently have to do is to take the message to the people who are supposed to benefit from the program and be sure that they know about them and that they are able to participate in the program.

In addition, we have some other considerations which are mentioned in my prepared statement. One is that we propose a 1-year extension of the CETA program rather than making any major changes in it. Our basic reason for that is to give us time to think through more thoroughly than we have been able to do by this time the kinds of changes that ought to be made in the act. We think that we can do most of what we propose within the framework of the present law.

Second, we are proposing an extension of the Federal supplemental benefits program. We are thinking about a 9-month extension with a 3-month phaseout, at a maximum not to exceed 52 weeks of benefits. The reason for our request for the extension is not because we believe that unemployment insurance is the best way to deal with the problem of long-term unemployment. We do not believe that it is. We believe that it would be much better to have the long-term unemployed in jobs and training programs than on unemployment insurance programs; better for them and better for the country.

But we also recognize that since we are not likely to be able to bring unemployment down to where we would like to see it, that we need to have some safety net under unemployed workers to be sure that they have some income when they exhaust their regular unemployment insurance eligibility.

The supplemental benefits program did provide that for them, and we think it ought to be extended while we try to bring the unemployment down.

Thank you, Mr. Chairman.

[The prepared statement of Secretary Marshall follows:]

PREPARED STATEMENT OF HON. F. RAY MARSHALL

Mr. Chairman and members of the committee; I welcome this opportunity to participate in your annual hearings on the state of the economy. The influential role played by this committee in providing leadership and perspective on the Nation's economic outlook is well-known. While this is only my first appearance as Secretary of Labor before the committee, I regard it as the beginning of a continuing and important dialog.

Before discussing the economic outlook and the administration's proposals, I would like to make a few, very brief, observations.

First, a major source of this Nation's strength is its labor force. During periods of high unemployment, substantial portions of this vital human resource are wasted. Unemployment means lost time, and we are never going to be able to put unemployed workers back to work yesterday.

Moreover, during periods of high unemployment, the disproportionate representation of certain segments of our population among the unemployed continues, and in some respects worsens. Any progress which may have been made among such groups as minorities, youth, and Vietnam-era veterans, is jeopardized if the economy falters. The longer that high levels of unemployment persist, the more acute becomes the loss in human terms and in terms of economic impact.

Second, to utilize our human resources, there must be jobs—productive employment harnessed to a healthy economy.

Third, and finally, I must emphasize that the economic and employment outlook, together with any assessment of the administration's proposals, involve only our best judgment in the light of available evidence. This assessment is complicated by the unseasonably cold winter and the shortage of natural gas in some regions which have led to widespread business curtailments and layoffs. In the face of this uncertainty the strength of the administration's economic package is that it provides a stable framework, offering the continuity of a 2-year program of tax and spending measures. At the same time, it is flexible enough to adapt to changed circumstances. Moreover, the proposals, particplarly in the employment area, enable us to target many of our activities to those groups within the labor force in greatest need.

Economic outlook

In discussing the economic outlook. I will focus on the employment situation.

Generally, there is a consensus that, without fiscal stimulus, employment will continue at unacceptably high levels. Last year, the total labor force grew by approximately 2.6 million; the total number of employed workers grew by slightly more than 2.8 million. Thus, the total growth in employment little more than offsets the labor force expansion. Available indications point to the possible addition of more than 2 million workers to the labor force during 1977. This means that over 2 million jobs must be added to the ecoonmy in 1977 just to keep up with labor force growth during the year.

The latest figures published by the Bureau of Labor Statistics offer a mixed economic picture. Moreover, they were based on data compiled during mid-January, prior to the intensification of problems created by our sustained harsh winter, the lack of natural gas, and the rise in layoffs generated by business curtailments.

Therefore, any assessment of the employment outlook must be guarded, at best. Much depends on the impact of the future winter weather, the supply of natural gas, and the resumption of businesses presently disrupted by those factors. In addition, we must be wary of problems that may be created by such other factors as the lack of precipitation in the west this winter, with the potential for adverse impact on irrigation and hydroelectric power later this year.

One thing remains clear, however, the labor force will continue to grow, and economic growth must be stimulated if we are to make inroads on overall unemployment.

In addition particular segments of our working population continue to bear disproportionate burdens of unemployment. The trends there are not very encouraging. Unemployment decreased only slightly among such groups as teenagers, blacks and other minorities, and veterans, during 1976. The unemployment rate for teenagers is presently 18.7 percent (compared to 19.4 percent a year ago). The unemployment rate for black and other minorities is 12.5 percent (compared to 13.2 percent a year ago); for minority youth, however, the rate of unemployment is presently 36.1 percent (compared with 35.0 percent a year ago). For veterans aged 20–24, the unemployment rate is presently 16.8 percent (compared with 18.3 percent a year ago). The situation for women improved during the year, but their unemployment rates are still significantly higher than for men.

The continuing waste of human and economic resources represented by these figures requires immediate attention.

The administration package

1. *General*

It appears that attaining a real growth rate of 6.0 percent and the achieving of substantial reductions in unemployment will be difficult. Strengthening the present recovery will require a careful mix of stimulation measures. Accordingly, the administration's proposals include tax measures designed to stimulate the economy in general, and in revenue sharing designed to make this program more sensitive to the unemployment rate and its fluctuations. The spending programs are geared to the capabilities of Government to realistically absorb new or expanded responsibilities.

The economic impetus provided by the proposed $11.4 billion tax rebate may create indirectly several hundred thousand jobs by the end of calendar 1977. Business tax reductions may have little effect on employment in 1977, but in the longer run, will encourage increased hiring in labor-intensive industries and more investment in capital-intensive industries, meaning more jobs and increased productivity. Emergency public works programs, appropriations of $2 billion for each of fiscal years 1977 and 1978, will be targeted towards areas of high unemployment. This will especially help the severely depressed construction industry.

2. *Department of Labor Components*

Many of the administration's proposals deal with overall stimulation of the economy, with resulting expansion of employment to be created in the private sector. Other components of the administration's recovery package, such as those administered by the Department of Labor, are designed to supplement the overall effort and to focus selectively on particular problem areas. In this regard, Department of Labor activities involve new and expanded efforts in the areas of public service employment and employment training.

a. Public Service Employment

The primary source of new jobs must remain the private sector of our economy; this is where five-sixths of the jobs are located. However, a general economic upturn cannot by itself solve structural unemployment. We cannot ignore those whom the private sector is not ready or able to absorb. Therefore, programs of meaningful public service employment are a vital supplement.

We want public service employment to be useful and meaningful. There is no need for make-work when so much needs to be done in so many areas, such as energy conservation and weatherization, local emergencies such as those created by the harsh winter, repair and renovation programs, rehabilitation of blighted urban and rural areas, and many other activities.

Moreover, meaningful public service employment opportunities provide abundant dividends. They can be targeted to areas of greatest need. They can move people from welfare and unemployment rolls. This can result in a lowered net cost to government, and provide meaningful services from which we can all benefit.

At the same time, large scale expansion of public service employment programs, as well as new initiatives in training programs, cannot be accomplished overnight. We will move at an accelerated pace, but at one which is within our capacity to administer efficiently.

The number of federally funded public service jobs, under the administration's proposals, will be raised from the level of 310,000 to 600,000 during fiscal year 1977 and to 725,000 during fiscal year 1978. For Fiscal Year 1977, this represents almost a doubling of such jobs in the next 8 months.

b. Employment Training

The training aspects of the stimulus package provide both new and expanded efforts to combat structural unemployment through developing job skills. These efforts will both supplement general economic recovery by providing more trained workers to meet expanded employer needs, and concentrate many programs on the needs of those with problems in obtaining the skills required to obtain jobs. At the heart of these programs will be increased efforts to establish better linkages between job training and private employers, with increased employer participation a key goal.

Our proposals include special measures targeted to special groups such as youth, veterans, migrants and Indians. Within and for these groups, there must be carefully tailored programs to develop marketable skills and to encourage private industry to hire them.

With regard to youth training and employment, we must recognize that unemployment among the Nation's young people is particularly severe.

The Nation's young workers represent our future. Their attitudes and workforce attachment are given shape and direction early in their working lives. Yet a substantial proportion of the young population continues to be plagued by persistent unemployment which may have long-term adverse consequences.

Latest available figures indicate that there were more than 3.2 million unemployed jobseekers among those aged 16-24. In percentage terms, we have an 18.7 percent unemployment rate among youth aged 16-19, and an 11.4 percent rate among those aged 20-24. Even more significant, these figures are little different from corresponding figures for the same age groups a year ago. We have a problem which is not only severe in magnitude, but chronic in duration.

To date, progress in meeting the employment problems of young people has been negligible. Overall high unemployment still places the young in competition with more experienced workers for those jobs which are available. In many cases, young workers still lack marketable job skills; in too many cases, their training and education have not fitted them for jobs which are available.

For these reasons, I believe the administration's proposals for dealing with youth are among the most important aspects of the entire recovery package. The administration's proposals represent a first step along the road of what we can do to improve the situation of our younger workers. We propose expansion of youth-oriented programs using the authority in titles III and IV of the Comprehensive Employment and Training Act (CETA). Youth training program under CETA would increase by 72,000 slots by the end of fiscal year 1977, with a further increase of 82,000 slots by the end of the fiscal year 1978, for a total increase of 154,000. For Job Corps activities, we propose a doubling of the present 22,000 capacity by the end of fiscal year 1978.

Within these overall expansions, we intend to concentrate on developing marketable job skills, where none presently exist. We will make every effort to improve linkages with private industry, seeking a more active role for the private sector in developing training programs which are tailored to jobs which need to be filled. There will be increased emphasis on a broad range of job training efforts—apprenticeship, on-the-job training, and institutional education. All of this will enhance the ability of many young people to operate more effectively in the labor market. We also seek to implement innovative measures to expand the horizons of our young unemployed workers through their participation in innovative programs related to conservation and service activities.

Our proposals represent measures which can be implemented promptly, within existing program frameworks. It is our intention to move toward a comprehensive attack on the chronic problems of unemployment among our young workers. We intend to give prompt and active consideration to the development of a comprehensive legislative framework within which the employment problems of youth can be addressed. In this effort we will work closely with those members of Congress who have a special interest in this important area.

With regard to veterans, the proposals involve both the private sector and public employment and training measures. Under a new "HIRE" program, which could eventually be expanded to include nonveterans, we will enlist the aid of the private sector in putting unemployed Vietnam-era veterans to work. As incentive, we propose to pay a variable amount per veteran hired—depending on occupational level and job—to cover the extra costs of training and other services needed to make the veteran more employable. To assure the creation of new jobs, Federal assistance will be available only if employment of targeted groups does not result in displacement of presently employed workers, workers laid off, or workers on strike. We will be undertaking other veteran-related initiatives to increase the enrollment of veterans in expanding public service employment programs, with a national enrollment goal of 35 percent of all new public service jobs to be filled by veterans. We are also proposing an amendment to present law to establish a preference for younger Vietnam-era veterans for employment in all federally-assisted public service employment. For disabled veterans, we propose the establishment of outreach units in the 100 largest cities, staffed by disabled Vietnam-era veterans who will concentrate on bringing these veterans back into the mainstream of the labor market.

In addition to the measures I have discussed, the unique problems of migrant workers and Indians will be addressed with expanded training opportunities geared to the special needs of these groups.

The measures I have reviewed will be the vanguard of a continuing effort to deal with the special problems of the structurally unemployed.

3. *Other Initiatives*

The administration's proposals are measures to counter the most urgent and immediate problems as we view them. There are, of course, other near-term actions which will be needed.

For example, the appropriations authorization for the federally-assisted public service employment and training programs in CETA expires September 30, 1977. Time constraints will limit the development of administration proposals for amendments to that act.

As an interim measure, we would propose a 1-year extension to appropriations authorization for all titles of CETA. Any substantive amendments which we would propose at this time would be limited in nature.

We also have under consideration proposals regarding extension of the current Federal Supplemental Benefits program (FSB). Under this program, duration of unemployment compensation paid to individuals may go to a maximum of 65 weeks when triggered in States where unemployment is especially severe. The FSB program will terminate on March 31, 1977. In view of persisting high levels of unemployment in many States, we must extend the program. Our present thinking involves an extension for another 9 months, with three months for a phaseout, and a duration of benefits at a maximum of 52 weeks.

In concluding my remarks, I would like to emphasize that assessment of the economic outlook is a continuing activity. We will devote our best efforts to tracking and interpreting events as they occur over the coming year in order to take or propose appropriate action in a timely fashion.

I appreciate the opportunity to appear today, and I am looking forward to working with this committee and the Congress in responding to the challenges which confront us.

This concludes my prepared statement. I would be pleased to respond to any questions you may have.

Representative BOLLING. Thank you, Mr. Secretary.

Congressman Moorhead.

Representative MOORHEAD. Thank you, Mr. Chairman.

Mr. Chairman, I would comment that it's a great pleasure to see both Labor and Commerce representatives here. Maybe this is symbolic of the new relationship between labor and industry throughout the country. I enjoyed the statments that both of you made. I want to first discuss with you, Madam Secretary, the local public works program.

Are you familiar in general with the bill as reported by the Public Workers Committee of the House yesterday?

Secretary KREPS. In general terms, yes.

I, of course, have not seen it. Perhaps you would like to walk me through the details?

Representative MOORHEAD. Well, I have only the press release issued by the committee. It is a $4 billion authorization. It does make certain changes. It eliminates the 30-percent formula which was used, in my judgment, as an excuse rather than as a real thing for some of the inequities.

For example, from very personal experience in my own city of Pittsburgh which has a high rate of unemployment, received zero out of the Public Works—first Public Works Act. One of the problems was that some of the neighboring, more affluent suburban communities were allowed to include in their unemployment rates the unemployment of adjacent communties; and the bill as reported eliminates that provision. Of the changes the requirement of just looking at the previous quarter, the previous 12 months. It requires the States and localities applying for more than one project to list them in order of priority and prohibits the States and localities from using their own employees, requires letting of jobs—projects on a competitive bidding project.

There's a percentage for Indian tribes, and there are other provisions that I don't think are as important. Based on your general knowledge of the legislation and your intentions, do you believe that you can administer the legislation so as not to have the inequities which existed, unfortunately, under the previous administration?

Secretary KREPS. Yes, I think we can; may I just say parenthetically, sir, that I am acutely aware of the failure to send any funds on the first phase of the program to Pittsburgh. I am sure you know that EDA people have met with your staff and with the mayor of Pittsburgh to explain the problem and also to assure him that we will try to target the second round of LPW moneys for the high unemployment areas, provided we have the legislation which you just indicated is in the bill.

With respect to the legislative changes you have just discussed, they were all our recommendations as well. EDA's staff has been working with the committee on that legislation.

The elimination of the 30–70 split, the elimination of the ability to gerrymander the area, the substitution of unemployment rates for the last 12 months, and the provision for Indianas were all in our initial recommendations. We felt that those were albsolutely essential to allow us to operate in a reasonable fashion on the next $4 billion or whatever amount is finally approved.

We would hope, therefore, that given the changes in the legislation we could avoid the inequities we felt were inherent in the first set of projects we approved. Moreover, we are hopeful that we can move rather quickly on this since we would expect to draw from the remaining applications that we already have on file.

Representative MOORHEAD. That should enable me to move more quickly than did the previous administration when they were starting without a backlog of applications; is that not so?

Secretary KREPS. Well, we must have them do some updating. That will take a little time. Certainly it would minimize the time constraint.

So, to answer your question, I am very optimistic that given these changes, we can move ahead and avoid some of the pitfalls we fell into before.

Representative MOORHEAD. Thank you, Madam Secretary.

It occurs to me that a large part of the economic stimulus package is across-the-board. The tax rebate, the permanent tax cuts are not targeted toward either areas or groups of individuals or particularly disadvantaged. The one exception I think would be the countercyclical revenue sharing which does focus on areas that have higher than normal unemployment, but that the program part of the package that both Commerce and Labor are focusing on can be targeted. The labor program is targeted particuarly toward groups; but I think also that there should be some concern about what I call geographical differences.

I think, Secretary Marshall, you mentioned the drought in the West in addition to the cold of the winter. I might also add that the potential of flooding where there has been more than normal snowfall and less than normal runoff of snowfall and frozen rivers; there may be some areas that you should be focusing on. I am thinking about the difference between how you handle a drought area and a flood area; and then those areas where there is nothing particularly unusual happening to their economy.

I would think, Madama Secretary, you would have in your local public works program—you should be thinking about the problems of the prosperous areas of the country and those where the economy is faltering worse in another area. Would both of you agree with me on that point?

Secretary MARSHALL. Yes.

In our programs, we have been trying to pay particular attention to that problem. For example, in the present emergency related to the natural gas shortage and the weather, we have made funds available to public service employees to do necessary work.

I think we need to anticipate allowing the same kinds of things for future emergencies; that is, to allow particular things you can do within the guidelines, to deal with emergencies.

One thing we tried to do is to be sure that we had a rapid response capability in emergencies. We tested it this time. I think we did respond relatively rapidly and there are things we can do to improve it.

We want to study our capability after we get through the emergency to be sure that we do improve it and learn from that lesson, because it is clearly very important to be able to respond in a hurry if you have an emergency situation.

We also are trying to see where our public service employment program particularly can be used to help meet other objectives, like flood control or winterization of homes so that we help particularly low income people meet these emergencies as they come along.

I agree that it is extremely important for us to think about those kinds of things, and we are trying to do that.

Secretary KREPS. May I respond also to this?

Representative MOORHEAD. Yes.

Secretary KREPS. As you know, I am sure, the EDA has some permanent programs which may be used to provide assistance for communities that are threatened by drought or floods. We have been studying this problem in the last few days with particular concern for prompt response should those programs prove necessary; but the more substantial long-run point should be made that it was a function of the Economic Development Administration from the beginning to attend to precisely the kind of regional imbalances which you suggest.

The function of regional development was embedded in the initial legislation. We would look, therefore, to it as a long-run matter to the EDA to be concerned about parts of the country that are less developed than others, and that would be an ongoing part of our responsibility.

Representative MOORHEAD. Thank you, Madam Secretary.

In your statement, you refer to regulatory reform. What would your reaction be to a legislation which would require any department, agency, or commission to include an economic impact statement?

I am concerned that sometimes regulations are issued without consideration of the cost-benefit ratio or the possibility of less cumbersome, less expensive forms of regulation.

Would that be included in your suggestion of regulatory reform?

Secretary KREPS. Yes.

We really have not thought this through with sufficient detail to lay out the program yet, but there is included in our thinking a need for costing out some of the regulations that we have been imposing to see whether on the merits—the merits including the costs—those regulations are cost-efficient.

Representative MOORHEAD. Thank you both for excellent statements.

Thank you, Mr. Chairman.

Representative BOLLING. Congressman Long.

Representative LONG. Thank you, Mr. Chairman.

Mrs. Kreps, Mr. Marshall, I would like to add my welcome to you to Washington. Most of the people I have known that went into the Government service at the level you have, have been looking for a challenge, and I think you are going to find one here.

I did it a little over 4 years ago, and I found it most challenging.

Last Friday we had Secretary Marshall and Mr. Shiskin from the Bureau of Labor Statistics here. He testified about the decline of unemployment in the United States in January to a 7.3-percent level.

Do you have any views as to whether or not this decline resulted from a real improvement in our economy, or did it result from workers dropping out of the labor force because of the bitter cold weather that we had in January?

Secretary MARSHALL. Well, it seems to me that in the first place this 7.3 percent does not, of course, represent the full impact of the cold weather, because the sample was taken too early to reflect that.

Beyond that, I think one of the real problems that we have with the unemployment statistics is, as you know, that it does not measure very precisely people who are not working.

One of our long-range objectives is to get more precise measurements so we can answer questions like that. We have an Employment and Unemployment Statistics Commission that is supposed to look into this. We are at work on putting that commission together.

In other words, things could really be worse, even though the unemployment statistics indicate that they are better.

I think there is no question that at the time the statistics were put together that there had been some improvement in the categories that they measured; but there had also been some other areas where you had not had much improvement. This is particularly true of young people. Their employment situation is sticky and, therefore, is not declining with the overall unemployment rate. Veterans and minorities have similar problems.

The answer to your question is that it could very well be that the overall unemployment statistics do not reflect—I am sure they do not reflect the entire situation with respect to people who are not working. We need to improve that.

Representative LONG. Mr. Shiskin also testified that the Bureau of Labor Statistics had prepared a special survey. To gather information on the unemployment impact of the extreme cold that we had, and the natural gas shortage, but that they hadn't received as of the time he was here the authorization from the Department of Commerce to proceed with that survey.

Have you since that time given him the authority to proceed, or is it within your discretion to give him such authority? Has it started; and if not, do you have any intentions to proceed?

Ms. FALCONE. I believe it is the Statistical Policy Office of the Office of Management and Budget which has to give the approval for that survey to proceed, not the Department of Commerce.

Representative LONG. Do you know whether they have given that authorization?

Ms. FALCONE. No, I don't.

Representative LONG. It seems to me what the Secretary was saying is that because of the effect it might have on our economic stimulus package, this information should be available as soon as possible.

Secretary MARSHALL. Mr. Long, we have been trying to do some things to get daily information on that. Mr. Hewitt informs me that the BLS has not formally asked for any authorization to conduct a special survey.

Mr. HEWITT. This is not really my general area of expertise, but I have been talking with the BLS people about it rather considerably. This week is the survey week in the regular current population survey, so this week the look at unemployment, employment, and so forth, is being taken. Those data will be reported the end of the first week in

March. A special survey would take at least 3 weeks to mount and get anything back. There is no point in doing any special work this week. It would have to be done next week.

We wouldn't have data back from any special survey until about the week when we would have a report based on the regular monthly survey, that is early March, anyway.

Representative LONG. But if we had it for that period, at least it would give us some broad, general guidelines. Even though they might not be pertinent to the particular time, if we saw an impact of the weather on a comparable date then we could draw some general conclusions, if it continues.

Mr. HEWITT. We will have data from the regular survey available shortly after the first of March for this week, which is the regular survey week.

Representative BOLLING. If the gentleman will yield, I think what it amounts to is that the regular survey, by coincidence, is going to get it to us faster than a special survey could at this moment in time; if we had been able to have the special survey last week, that would have been something else.

Representative LONG. My question, Mr. Chairman, is whether or not the general survey that comes with the month-to-month variance that we have seen recently is going to be able to adequately distinguish how much of the variance was caused by extreme weather conditions. That seems to me to be important information that we really need.

Secretary MARSHALL. Mr. Long, we tried to estimate this in, as you say, a rough and ready way, in a general way, with daily telephone surveys of unemployment due to adverse weather conditions and energy shortages. We asked the specific question. We did it by region and State, utilizing primarily the State employment security network to find out the impact of both weather and energy shortages. We have that by States. We have been doing it daily in order to give us the kind of estimate that we needed to know when we might have to respond with our disaster unemployment assistance program.

There are a lot of problems with that kind of survey, but it does give us in a rough way the kind of information that you mentioned here.

Representative LONG. Do you have any general conclusions drawn or surveys from that that you would like to make available to us, Mr. Marshall?

Secretary MARSHALL. Yes, sir.

One conclusion is that it is very volatile. As the weather and energy factors change markedly from day to day, the unemployment situation changes. Our last estimate was, I believe, about 1.8 million unemployed people. Do we have a later one?

Mr. HEWITT. Yes, two later ones. It dropped from 1.8 million people the next day to 1.2 million people. The last one as of the close of business February 7, 1977, was about 933,000.

Secretary KREPS. February 7——

Secretary MARSHALL. If you look at the figures from State to State they would change markedly because of large layoffs in particular places like Ohio.

Representative LONG. Mrs. Kreps——

Secretary MARSHALL. We can make that available to you, if you would like.

Representative LONG. Would you please, for the record? I think it would be important.

[The surveys referred to follow:]

FEBRUARY 7, 1977.

EXECUTIVE SUMMARY, EMPLOYMENT AND TRAINING ADMINISTRATION, SPECIAL ENERGY REPORT NO. 4

DAILY REPORT TO THE WHITE HOUSE

Based on regional reports received February 4 (covering activities as of COB February 3), an estimated 1,816,806 individuals were unemployed due to abnormal weather conditions and fuel shortages. The sharp increase from the previous national estimate of 1,149,063 (Report No. 3) is due primarily to the 900,000 estimate provided by the State of Ohio. Previous estimates from this State only covered individuals filing claims due to weather/energy factors. The 900,000 figure purports to be the best estimate of the State employment security agency and the Governor's office. Based on other data sources, we surmise that the estimate is somewhat inflated and may be adjusted downward as more comprehensive information is received. In the initial returns from the special ES-210/Energy Report (summarized below), Ohio reported 8,200 "initial claims" and 3,900 "continuing weeks" for the week ending January 29. Statistics for the week ending February 5 will be available later this week.

Two other States (Illinois and Michigan) continue to report estimates based only on the number of unemployed filing claims due to the weather/energy factors. These States seem to be in a somewhat better position in terms of plant closings and layoffs but we presently lack sufficient hard data on which to develop our own estimates.

Region II reports that CETA prime sponsors in New York fear that competition with UI will impede enrollment into the CETA emergency jobs programs. Chautauqua is experiencing difficulty in recruiting people for emergency PSE jobs, due to eligible applicants preferring to collect UI benefits. Several sponsors in the region have also raised the issue of enrollment policy in the emergency PCS program, i.e., can they concentrate their enrollment efforts on those laid off due to weather/energy factors and who are ineligible for UI? Sponsors are pointing out that many of those laid off who are eligible for UI have no interest in these emergency jobs, because they expect to return to work within the month.

Sponsors also are beginning to raise questions about the possible extension of the emergency jobs program beyond February 28 since the weather/energy problems are expected to continue beyond that date.

Pennsylvania reports increasing concern for flooding when the weather turns warmer and both sponsors and the regional office are recommending that the national office begin planning for increased funding needs for emergencies expected in the spring. Some preliminary work has already commenced regarding such additional emergencies.

North Carolina reports a significant number of firms experiencing partial layoffs and total closings for 1 to 2 weeks duration or have instituted on-a-week/off-a-week work schedules. No indefinite closings have been reported. Similar sporadic work schedules are being reported elsewhere. This makes daily estimating and intermediate range forecasting more difficult.

The rippling effects of plant shutdowns in the heavily impacted States are beginning to show up as far away as California. Plants in the less impacted States are closing down for lack of parts because they have been told to curtail further shipments until current inventories decrease and for other related reasons, including depletion of their own alternative energy sources such as propane gas. We can expect an acceleration of such disruptions nationally until weather and energy conditions improve.

On February 4, the Washington Post reported that the three largest glass fiber insulation manufacturers—accounting for 80 to 90 percent of the home insulation market—cannot meet the demands of their customers because of a lack of gas needed for the manufacturing process. Two major manufacturers are operating far under capacity and one is operating slightly less than capacity but is taking no new customers because it already rationing supplies among its established accounts. This situation has a direct impact on plans for winterization projects in which our CETA prime sponsors and PSE hires are expected to be heavily involved.

ES-210/ENERGY REPORT

The first returns from this special weekly report, reinstituted late last month, have been received and processed. Only 18 States were able to report for the week ending January 29. All States should be reporting for the week ending February 5.

The 18 States reported 29,625 "initial claims" (energy-related), 39,921 "continuing weeks" and 35,203 "recalls." These States also estimated that as of the time of the report's submission, 387,975 individuals were unemployed because of energy shortages. A variety of industries are being impacted including auto, steel, textiles, apparel, glass, water transport, metal fabrication, furniture, fishing, and food processing.

UNEMPLOYMENT ESTIMATES DUE TO ADVERSE WEATHER/ENERGY CONDITIONS, AS OF FEBRUARY 3, 1977 [1]

Regional Summary

Region I	3, 695
Region II	458, 637
Region III	230, 988
Region IV	158, 000
Region V	950, 020
Region VI	---------
Region VII	[2] 8, 666
Region VIII	5, 700
Region IX	1, 100
Region X	---------
Total	1, 816, 806

Total Unemployed Workers Due to Adverse Weather/Energy Conditions, As of February 3, 1977

Region 1:	
Connecticut	408
Maine	0
Massachusetts	3, 213
New Hampshire	14
Rhode Island	0
Vermont	60
Total	3, 695
Region 2:	
New Jersey	38, 637
New York	420, 000
Puerto Rico	---------
Virgin Islands	---------
Total	458, 637
Region 3:	
Delaware	2, 781
District of Columbia	7
Maryland	15, 000
Pennsylvania	164, 000
Virginia	14, 600
West Virginia	34, 600
Total	230, 988
Region 4:	
Alabama	15, 000
Florida	25, 000
Georgia	26, 000
Kentucky	60, 000
Mississippi	1, 400
North Carolina	4, 400

See footnotes at end of table.

UNEMPLOYMENT ESTIMATES DUE TO ADVERSE WEATHER/ENERGY CONDITIONS, AS OF FEBRUARY 3, 1977[1]—Continued

Total Unemployed Workers Due to Adverse Weather/Energy Conditions, As of February 3, 1977—Contined

Region 4—Continued.	
South Carolina	15,000
Tennessee	11,200
Total	158,000
Region 5:	
Illinois	[3] 3,500
Indiana	44,500
Michigan	[3] 2,020
Minnesota	0
Ohio	900,000
Wisconsin	0
Total	950,020
Region 6:	
Arkansas	0
Louisiana	0
New Mexico	0
Oklahoma	0
Texas	0
Total	0
Region 7:	
Iowa	0
Kansas	80
Missouri	8,586
Nebraska	0
Total	8,666
Region 8:	
Colorado	[3] 3,000
Montana	[4] 500
North Dakota	[4] 200
South Dakota	[4] 500
Utah	[4] 1,000
Wyoming	[4] 500
Total	5,700
Region 9:	
Arizona	0
California	1,100
Hawaii	0
Nevada	0
Total	1,100
Region 10:	
Alaska	0
Idaho	0
Oregon	0
Washington	0
Total	0
Grand total	1,816,806

[1] Estimates cover both insured and uninsured workers, except those for Illinois and Michigan which cover only unemployed workers who have filed claims due to weather/energy factors.
[2] Unemployed due to drought conditions and lack of snow.
[3] Unemployed workers who have filed claims due to weather/energy crisis.
[4] Unemployed due to drought and lack of snow.

DAILY ENERGY REPORT—PART A

[Data as of COB, Feb. 3, 1977]

United States	Estimate of total weather/energy related unemployment	Special problems and/or actions identified (see pt. B for details)
Alabama	15,000	
Alaska	0	
Arizona	0	
Arkansas	0	
California	1,100	
Colorado	[1] 3,000	
Connecticut	408	
Delaware	2,781	
District of Columbia	7	
Florida	25,000	
Georgia	26,000	
Guam		
Hawaii	0	
Idaho	0	
Illinois	[2] 3,500	
Indiana	44,500	
Iowa	0	
Kansas	80	
Kentucky	60,000	
Louisiana	0	
Maine	0	
Maryland	15,000	X
Massachusetts	3,213	
Michigan	[2] 2,020	
Minnesota	0	
Mississippi	1,400	
Missouri	8,586	
Montana	[1] 500	
Nebraska	0	
Nevada	0	
New Hampshire	14	
New Jersey	38,637	X
New Mexico	0	
New York	420,000	X
North Carolina	4,400	
North Dakota	[1] 200	
Ohio	900,000	X
Oklahoma	0	
Oregon	0	
Pennsylvania	164,000	X
Puerto Rico		
Rhode Island	0	
South Carolina	15,000	
South Dakota	[1] 500	
Tennessee	11,200	
Texas	0	
Utah	[1] 1,000	
Vermont	60	
Virginia	14,600	X
Virgin Islands		
Washington	0	X
West Virginia	34,600	X
Wisconsin	0	
Wyoming	[1] 500	
Total	1,816,806	

[1] Unemployed due to drought and lack of snow.
[2] Unemployed workers who have filed claims due to weather/energy crisis.

DAILY ENERGY REPORT (PART B)

STATE OF MARYLAND

1. Current estimate of weather/energy related unemployment (insured and uninsured). 15,000.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: High incidence of unemployment in the fishing industry and severe curtailment of construction projects along with factory shutdowns.

Mail delivery problems because of snow and ice cropping up in western Maryland and the Chesapeake Bay area. Garrett County and Smith Island are isolated. Major ice and snow problems and water main damages.

3. Summary of State and local agency actions in response to the identified problems: The Baltimore CETA program sponsor is developing 680 jobs to handle the damage to city facilities. The Chesapeake Bay area was declared a disaster area and special arrangements have been made to take claims by phone and other emergency means. Couriers and National Guard helicopters have been used to obtain claims and deliver checks to claimants in isolated areas. Additional staff have been hired to expedite the claims loads.

4. Requests by State for Federal assistance to resolve or minimize the problem(s):

5. Departmental actions contemplated or taken:

STATE OF NEW JERSEY

1. Current estimate of weather/energy related unemployment (insured and uninsured). 38,637.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: The increasing Unemployment Insurance claims load and the

resultant space and staff problems remain the State employment security agency's principal concern.

3. Summary of State and local agency actions in response to the identified problems: The State agency has extended weekday and Saturday hours; waived the maximum limit of working hours per quarter for intermittant claims takers; and investigated the need for and availability of additional space. The Governor has waived the "waiting week" requirement to expedite payment of benefits. Three hotlines have been established for direct response to inquiries to keep the public as informed as possible.

4. Requests by State for Federal assistance to resolve or minimize the problem(s): The Commissioner of Labor has requested the Governor (and requests Federal assistance in this regard) to seek emergency legislation which would provide disaster unemployment assistance for the fuel crisis claims and for the provision of Federal general funds to cover benefit costs being borne by the States.

5. Departmental actions contemplated or taken: New Jersey's needs for additional unemployment insurance funds are being carefully considered.

STATE OF NEW YORK

1. Current estimate of weather/energy related unemployment (insured and uninsured). 420,000.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Cessation and delay of mail is a new problem faced by the State employment security agency. Space and staff shortages continue to be a problem.

3. Summary of State and local agency actions in response to the identified problems: The State agency is using employment service staff and space where necessary to cope with increased claims load and have set up their own courier service between central and local offices by special trucks. The Governor also has waived the waiting week statewide for fuel shortage claims and in nine counties for weather-related claims.

Approximately $1.8 million in emergency CETA funds has been allocated to prime sponsors in New York. Employment Service and CETA sponsors participating in joint recruitment efforts. In Buffalo, those determined eligible will be referred immediately to work areas. Other areas are following similar procedures. Emergency programs consist primarily of snow removal from roads, airport runways, and fire hydrants, delivery of food, fuel and medical supplies, and winterization of homes.

4. Requests by State for Federal assistance to resolve or minimize problem(s):

5. Departmental actions contemplated or taken:

STATE OF OHIO

1. Current estimate of weather/energy related unemployment (insured and uninsured). 900,000.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Heavy accumulation of snow in some areas is creating hardships and disrupting community services.

3. Summary of State and local agency actions in response to the identified problems: Approximately 100 CETA program enrollees are assisting communities in emergency snow removal operations; other enrollees are expected to join in the same activity within a few days.

The State employment security agency is extending its hours of operation and will be open on February 21 which is normally a State holiday.

4. Requests by State for Federal assistance to resolve or minimize problem(s):

5. Departmental actions contemplated or taken:

STATE OF PENNSYLVANIA

1. Current estimate of weather/energy related unemployment (insured and uninsured). 164,000.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Substantial problems reported with snow and ice removal, breakdown of water and gas mains, and poor conditions of many dwellings. Some families isolated in outlying areas. The State employment security agency reports space problems as well as growing claims loads.

Parts of the State are deeply concerned about flooding when the weather turns warmer.

3. Summary of State and local agency actions in response to the identified problems: The State employment security agency has extended local office hours during evenings and weekends. Temporary offices have been established in four localities. Seventy-five additional staff have been hired for claimstaking activities, some of whom were claimants themselves. The agency is considering a courier service to expedite claims handling. The State Civil Defense unit is planning for possible floods and the State employment security agency is keeping abreast of the plans.

4. Requests by State for Federal assistance to resolve or minimize problem(s): The regional office is processing 18 requests for CETA Title I supplemental funds to handle the emergencies. Thus far $1.4 million has been allocated to prime sponsors in Pennsylvania.

5. Departmental actions contemplated or taken:

STATE OF VIRGINIA

1. Current estimate of weather/energy related unemployment (insured and uninsured). 14,600.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Tangier and Chincoteaque Islands are isolated by the harsh weather.

The Flatwoods Job Corps Civilian Conservation Center may have to be evacuated because of a lack of water due to ruptured and frozen water pipes.

Increasing claims loads in several areas of the State are creating space and staffing problems.

3. Summary of State and local agency actions in response to the identified problems: Local employment security agency staff were airlifted to both islands to take claims on site. An armory and a community college are being used as temporary claims offices and 25 additional claims takers were hired and overtime is being utilized. Work Incentive (WIN) program staff are assisting with UI claims loads in Newport News.

4. Requests by State for Federal assistance to resolve or minimize problem(s):

5. Departmental actions contemplated or taken:

STATE OF WEST VIRGINIA

1. Current estimate of weather/energy related unemployment (insured and uninsured), 34,600.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Heavy increase in claims loads and ice and snow removal are reported as major problems.

3. Summary of State and local agency actions in response to the identified problems: Temporary employees are being hired and an armory in Charleston is being used as a claims office site.

CETA PSE program participants have been directed to assist in snow and ice removal and emergency reports.

4. Requests by State for Federal assistance to resolve or minimize the problem(s).

5. Departmental actions contemplated or taken.

FEBRUARY 8, 1977.

EXECUTIVE SUMMARY, EMPLOYMENT AND TRAINING ADMINISTRATION, SPECIAL ENERGY REPORT NO. 5

DAILY REPORT TO THE WHITE HOUSE

Reports received on February 7, reflecting information as of COB February 4 (and, in some cases, through the weekend) added up to an estimated weather/energy unemployment figure of 1,224,961. The primary factor accounting for the drop from the previous estimate (1,816,806) was a substantial reduction and Ohio's estimate (from 900,000 to 464,000). Many of the 900,000 unemployed apparently were idled by weather factors rather then energy shortages and are now back at work. Also, a number of workers had been temporarily laid off while firms converted to other fuel, e.g. oil and coal. With the completion of the conversion, the workers returned to work. Region IV reported that some South Georgia plants are successfully burning peanut hulls for fuel instead of gas.

New York, Pennsylvania, Kentucky, and West Virginia also reported substantial recalls as utilities companies were able to supply additional gas and State-imposed restrictions were relaxed somewhat. Additional recalls are expected in the next few days in Indiana, New York, New Jersey, Maryland, Missouri, and elsewhere. A number of plants in Kentucky, Tennessee, and other States have reopened but are keeping thermostats in the work areas low to conserve energy.

Regions II, III, IV and V continue to bear the heaviest brunt of the layoffs, with Ohio, New York, Pennsylvania, Indiana, Kentucky and New Jersey reporting the highest estimates. A comparison of the current estimates with those immediately preceding show 13 States and D.C. lower, 9 higher, and 29 reporting the same figures.

State agencies receiving approval for supplemental CETA funds have moved expeditiously to recruit and place new hires in critically needed jobs necessitated by the emergency, such as freeing the ConRail system in the Buffalo area so that food and other supplies can be transported. The Pittsburgh Job Corps Center is providing auto maintenance for police vehicles to relieve the city's regular maintenance staff tied up with snow removal and other road-clearing equipment.

Florida, recently approved for disaster relief, expects a substantial increase in applications for DUA and other unemployment benefits within the next two weeks. Temporary offices have been opened in Central and South Florida and staff trained to handle the projected needs.

ES–210/ENERGY REPORT

Revised figures were received for the week ending January 29. The revised figures (22 States) show:

Initial claims	46,336
Continued weeks	37,128
Recalls	35,203
Estimated Total energy/related unemployment	387,975

ADDITIONAL STATES DESIGNATED FOR AID

Several more States have been approved by the President for Federal assistance under "disaster" and "emergency status" designations. Portions of the following States have recently received such designations:

DISASTER	EMERGENCY STATUS
Florida	Indiana
Maryland	Michigan
New York	New York
Virginia	Ohio
	Pennsylvania
	Virginia

Disaster Unemployment Assistance (DUA) is available for eligible workers in counties designated as "disaster" areas but not for those localities in the "emergency-status" designation. Current estimated cost for DUA for the four designated States is approximately $40 million.

STATE LEGISLATIVE ACTIVITIES

The N.Y. Times reports that State legislatures in New York, New Jersey, and Connecticut have begun to consider various proposals to cope with the increasing energy shortages. One of the more widely discussed proposals is the revamping of building codes to encourage efforts to winterproof dwellings. Other State legislatures are becoming increasingly interested in the general area of energy conservation, a priority goal of the current Administration. The various activities relating to home improvements to conserve energy have implications for future training and job placement services provided by CETA sponsors and State employment security agencies.

UNEMPLOYMENT ESTIMATES DUE TO ADVERSE WEATHER/ENERGY CONDITIONS, AS OF FEBRUARY 4, 1977

Regional summary

Region I	3,650
Region II	338,543
Region III	204,920
Region IV	134,200
Region V	514,491
Region VI	12,000
Region VII	8,666
Region VIII	[1] 5,700
Region IX	2,791
Region X	0
Total	1,224,961

Total unemployed workers due to adverse weather/energy conditions, as of February 4, 1977

Region 1:	
Connecticut	3
Maine	0
Massachusetts	3,485
New Hampshire	101
Rhode Island	4
Vermont	57
Total	3,650
Region 2:	
New Jersey	38,543
New York	300,000
Puerto Rico	0
Virgin Islands	0
Total	338,543
Region 3:	
Delaware	2,781
District of Columbia	11
Maryland	10,000
Pennsylvania	147,000
Virginia	15,128
West Virginia	30,000
Total	204,920
Region 4:	
Alabama	12,100
Florida	25,000
Georgia	24,500
Kentucky	45,000
Mississippi	1,400
North Carolina	4,400
South Carolina	15,000
Tennessee	6,800
Total	134,200

See footnote at end of table.

UNEMPLOYMENT ESTIMATES DUE TO ADVERSE WEATHER/ENERGY CONDITIONS, AS OF FEBRUARY 4, 1977—Continued

Total unemployed workers due to adverse weather/energy conditions, as of February 4, 1977—Continued

Region 5:	
Illinois	3, 500
Indiana	45, 400
Michigan	591
Minnesota	0
Ohio	464, 000
Wisconsin	1, 000
Total	514, 491
Region 6:	
Arkansas	12, 000
Louisiana	0
New Mexico	0
Oklahoma	0
Texas	0
Total	12, 000
Region 7:	
Iowa	0
Kansas	80
Missouri	8, 586
Nebraska	0
Total	8, 666
Region 8:	
Colorado	[1] 3, 000
Montana	[1] 500
North Dakota	[1] 200
South Dakota	[1] 500
Utah	[1] 1, 000
Wyoming	[1] 500
Total	5, 700
Region 9:	
Arizona	0
California	2, 791
Hawaii	0
Nevada	0
Total	2, 791
Region 10:	
Alaska	0
Idaho	0
Oregon	0
Washington	0
Total	0
Grant Total	1, 224, 961

[1] Unemployed due to drought and lack of snow.

DAILY ENERGY REPORT—PART A

[Data as of COB, Feb. 4, 1977]

United States	Estimate of total weather/energy related unemployment	Special problems and/or actions identified (see pt. B for details)
Alabama	12,100	
Alaska	0	
Arizona	0	
Arkansas	12,000	
California	2,791	
Colorado	[1] 3,000	
Connecticut	3	
Delaware	2,781	
District of Columbia	11	
Florida	25,000	X
Georgia	24,500	
Guam		
Hawaii	0	
Idaho	0	
Illinois	3,500	
Indiana	45,400	
Iowa	0	
Kansas	80	
Kentucky	45,000	
Louisiana	0	
Maine	0	
Maryland	10,000	
Massachusetts	3,485	
Michigan	591	
Minnesota	0	
Mississippi	1,400	
Missouri	8,586	
Montana	[1] 500	
Nebraska	0	
Nevada	0	
New Hampshire	101	
New Jersey	38,543	X
New Mexico	0	
New York	300,000	X
North Carolina	4,400	
North Dakota	[1] 200	
Ohio	464,000	
Oklahoma	0	
Oregon	0	
Pennsylvania	147,000	X
Puerto Rico		
Rhode Island	4	
South Carolina	15,000	
South Dakota	[1] 500	
Tennessee	6,800	
Texas	0	
Utah	[1] 1,000	
Vermont	57	
Virginia	15,128	X
Virgin Islands		
Washington	0	
West Virginia	30,000	
Wisconsin	1,000	
Wyoming	[1] 500	
Total	1,224,961	

[1] Unemployed due to drought and lack of snow.

STATE OF FLORIDA

1. Current estimate of weather/energy related unemployment (insured and uninsured). 25,000.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: The State employment security agency is anticipating a significant increase in layoffs related to the citrus industry in the next 2 weeks. The agency also is expecting substantial workloads as a consequence of the recent approval by the President of Florida's request for disaster designation.

3. Summary of State and local agency actions in response to the identified problems: The State agency is gearing up those local offices expected to be impacted by the projected layoffs and DUA claimants. A separate processing office has been opened in Tallahassee to expedite the handling of DUA claims. In addition, seven temporary offices have been opened in South Florida and they started taking claims on February 3. Adequate staff was trained on February 1 and initial checks (for 2 weeks) will be delivered on February 14. Both Employment Service and Unemployment Compensation staff are operating from an FDAA command post at Riviera Beach, Florida coordinating employment security activities. Selected Employment Service offices are remaining open until 7:00 p.m. each day to provide needed employability services.

4. Requests by State for Federal assistance to resolve or minimize the problem(s):

5. Departmental actions contemplated or taken:

STATE OF NEW JERSEY

1. Current estimate of weather/energy related unemployment (insured and uninsured). 38,543.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Need for emergency assistance relating to the weather/energy crisis.

3. Summary of State and local agency actions in response to the identified problems: Sixteen CETA sponsors have received approval of their plans for utilization of the special allocations to hire public service employees. An additional five approvals are expected shortly. So far, the allotments authorized total $923,077. Those sponsors who had been approved hoped to have persons working under PSE on or before February 9.

4. Requests by State for Federal assistance to resolve or minimize the problem(s):

5. Departmental actions contemplated or taken:

STATE OF NEW YORK

1. Current estimate of weather/energy related unemployment (insured and uninsured). 300,000.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Mass lay-offs in several upstate counties continue to plague the agency with a constantly changing claims load.

3. Summary of State and local agency actions in response to the identified problems: In three upstate districts—Buffalo, Rochester and Syracuse—the local office workday Monday to Friday is 8:30 am to 9:00 pm and on Saturday from 8:30 to 5:00 pm. Mass lay-offs are being handled at industry plants and union halls. Emergency staff have shifted from Utica to Lowville in Essex County because Watertown staff who normally service Lowville are still isolated. Buffalo recruited workers for snow removal and repairs over the weekend, and reports that approximately 1,000 people will be working as of today. Two hundred of these participants will be working to free the Conrail system to facilitate four transportation Erie County plans to use approximately $200,000 of its Title I (CETA funds to fill about 100 slots which remain unfilled after its weekend recruitment.

4. Requests by State for Federal assistance to resolve or minimize the problem(s):

5. Departmental actions contemplated or taken:

STATE OF PENNSYLVANIA

1. Current estimate of weather/energy related unemployment (insured and uninsured). 147,000.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Pittsburgh police car maintenance is backlogged because city services are being concentrated on servicing of snow removal trucks and equipment.

3. Summary of State and local agency actions in response to the identified problems: Pittsburgh Job Corps Center is providing routine maintenance for police vehicles during the current emergency.

4. Requests by State for Federal assistance to resolve or minimize the problem(s):

5. Departmental actions contemplated or taken: To date, $1,458,479 Title I supplemental funds have been allocated to CETA prime sponsors in the State for emergency activities.

STATE OF VIRGINIA

1. Current estimate of weather/energy related unemployment (insured and uninsured). 15,128.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Severe water main damage in Wise County Virginia has led to a decision to evacuate all but a small number of Job Corps members at the Flatwoods Job Corps Center. The town of Coeburn has been experiencing shortages which have resulted in a lack of water for municipal buildings and many residences.

3. Summary of State and local agency actions in response to the identified problems: Corps members are being placed on administrative leave with pay and

allowances. Charter buses will take a majority of Corps members to central points near their homes from which they will travel with government paid transportation to their homes.

The State employment security agency is proposing legislation to waive the waiting period for unemployment insurance benefits for energy/weather-related claims.

4. Requests by State for Federal assistance to resolve or minimize the problem(s):

5. Departmental actions contemplated or taken:

FEBRUARY 14, 1977.

EXECUTIVE SUMMARY, EMPLOYMENT AND TRAINING ADMINISTRATION, SPECIAL ENERGY REPORT NO. 9

DAILY REPORT TO THE WHITE HOUSE

Unemployment due to weather and energy factors continued its downward trend, with the latest estimates totaling 604,678—a decrease of about 78,000 from the previous report. The decrease may be somewhat larger since several States, including Pennsylvania, did not report new figures because offices were closed due to State holidays. Pennsylvania had been reporting a steady decrease in unemployment for the past week.

Ohio (with a reported estimate of 300,000), Pennsylvania, Indiana, Florida and Georgia continue to rank among the hardest-hit States, with about 75 percent of the national estimate coming from these five States. Kentucky, New Jersey, and West Virginia, three other States with substantial unemployment, all reported lower estimates as thousands returned to work.

Overall, Region IV (Atlanta) declined by almost 17,000 but only because of major decreases in Kentucky and Tennessee. Four of the eight States in this Southeast region reported net increases as fresh layoffs outstripped recalls. The gas situation is becoming critical in several of the Southern States. For example, in Scottsboro, Ala. a rolling mill producing aluminum closed down as fuel ran out. Textile plants and other industries in Georgia were forced to lay off additional workers as they did not receive the amount of fuel they had expected.

DISASTER UNEMPLOYMENT ASSISTANCE

Thus far, portions of five States (Maryland, Virginia, Florida, New York and New Jersey) have been declared major disaster areas, with other impacted States seeking Presidential approval for such designations. The affected State employment security agencies are taking emergency measures to expedite the paymenit of DUA benefits to the thousands of claimants who have applied. The latest reports provided FDAA show that approximately 37,500 DUA claims have been filed in four States (no report for New Jersey). FDAA currently estimates that approximately $55 million—$58 million may be paid out in DUA benefits for the current crisis. If these expectations are realized, this will be the most expensive period for DUA since the inception of the program in December 1969. Up through this year approximately $57.5 million had been paid out to 236,000 claimants involved in a variety of natural disasters.

ES-210/ENERGY REPORT UPDATE

The week ending February 5 reflected a sharp jump in energy-related initial claims. With only a few significant States (i.e., Michigan and Illinois) not reporting before the weekly deadline, 195,641 initial claims (excluding DUA) were filed by workers impacted by energy stortages. These claims represented about 27 percent of all initial claims filed at local unemployment insurance offices during the reporting week (exclusive of DUA).

In addition to the 195,641 energy-related initial claims, State agencies recorded 122,702 continuing claims and 87,812 recalls. At the same time, the agencies estimated total energy-related unemployment of 352,000 at the time of their report.

UNEMPLOYMENT ESTIMATES DUE TO ADVERSE WEATHER/ENERGY CONDITIONS, AS OF FEBRUARY 10, 1977

Regional summary

Region I	1,419
Region II	30,900
Region III	104,864
Region IV	107,800
Region V	345,892
Region VI	4,623
Region VII	1,770
Region VIII	[1] 600
Region IX	6,810
Region X	0
Total	604,678

[1] Unemployment due to drought conditions and lack of snow.

Total unemployed workers due to adverse weather/energy conditions, as of February 10, 1977

Region 1:	
Connecticut	442
Maine	92
Massachusetts	547
New Hampshire	236
Rhode Island	0
Vermont	102
Total	1,419
Region 2:	
New Jersey	20,900
New York	10,000
Puerto Rico	0
Virgin Islands	0
Total	30,900
Region 3:	
Delaware	5,385
District of Columbia	12
Maryland	[1] 5,567
Pennsylvania	[1] 63,000
Virginia	13,000
West Virginia	17,900
Total	104,864
Region 4:	
Alabama	14,100
Florida	31,000
Georgia	23,000
Kentucky	20,000
Mississippi	500
North Carolina	8,500
South Carolina	8,700
Tennessee	2,000
Total	107,800

See footnote at end of table.

UNEMPLOYMENT ESTIMATES DUE TO ADVERSE WEATHER/ENERGY CONDITIONS, AS OF FEBRUARY 10, 1977—Continued

Total unemployed workers due to adverse weather/energy conditions, as of February 10, 1977—Continued

Region 5:	
Illinois	[1] 10,685
Indiana	34,800
Michigan	249
Minnesota	[1] 62
Ohio	300,000
Wisconsin	96
Total	345,892
Region 6:	
Arkansas	4,113
Louisiana	96
New Mexico	0
Oklahoma	122
Texas	292
Total	4,623
Region 7:	
Iowa	0
Kansas	0
Missouri	1,770
Nebraska	0
Total	1,770
Region 8:	
Colorado	[2] 500
Montana	0
North Dakota	0
South Dakota	0
Utah	[2] 100
Wyoming	[2] 100
Total	[2] 600
Region 9:	
Arizona	0
California	6,810
Hawaii	0
Nevada	0
Total	6,810
Region 10:	
Alaska	0
Idaho	0
Oregon	0
Washington	0
Total	0
Grand total	604,678

[1] State holiday. Figures are those of the preecding day (Feb. 9, 1977).
[2] Unemployed due to drought and lack of snow.

DAILY ENERGY REPORT—PART A

[Data as of COB, Feb. 10, 1977]

United States	Estimate of total weather/energy related unemployment	Special problems and/or actions identified (see pt. B for details)
Alabama	14,100	×
Alaska	0	
Arizona	0	
Arkansas	4,113	
California	6,810	
Colorado	[1] 500	
Connecticut	442	
Delaware	5,385	
District of Columbia	12	
Florida	31,000	
Georgia	23,000	×
Guam	----	
Hawaii	0	
Idaho	0	
Illinois	[2] 10,685	
Indiana	34,800	
Iowa	0	
Kansas	0	
Kentucky	20,000	
Louisiana	96	
Maine	92	
Maryland	[2] 5,567	
Massachusetts	547	
Michigan	249	
Minnesota	[2] 62	
Mississippi	500	
Missouri	1,770	
Montana	0	
Nebraska	0	
Nevada	0	
New Hampshire	236	
New Jersey	20,900	
New Mexico	0	
New York	10,000	×
North Carolina	8,500	
North Dakota	0	
Ohio	300,000	
Oklahoma	122	
Oregon	0	
Pennsylvania	[2] 63,000	×
Puerto Rico	0	
Rhode Island	0	
South Carolina	8,700	
South Dakota	0	
Tennessee	2,000	
Texas	292	
Utah	[1] 100	
Vermont	102	
Virginia	13,000	
Virgin Islands	0	
Washington	0	
West Virginia	17,900	
Wisconsin	96	
Wyoming	[1] 100	
Grand total	604,678	

[1] Unemployed due to drought and lack of snow.
[2] State holiday. Figures are those of the preceding day (Feb. 19, 1977).

DAILY ENERGY REPORT (PART B)

STATE OF ALABAMA

1. Current estimate of weather/energy related unemployment (insured and uninsured). 14,100.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: New layoffs reported in Scottsboro. A rolling mill plant that produces aluminum is completely out of gas and has closed down.

3. Summary of State and local agency actions in response to the identified problems: The State employment security agency is processing new claims for unemployment insurance benefits as expeditiously as possible. The agency will keep tabs on developments in this important plant.

4. Requests by State for Federal assistance to resolve or minimize the problem(s):

5. Departmental actions contemplated or taken:

STATE OF GEORGIA

1. Current estimate of weather/energy related unemployment (insured and uninsured). 23,000.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: New layoffs reported as textile mills in some parts of the State have not received the amount of fuel they expected.

3. Summary of State and local agency actions in response to the identified problems: The State employment security agency is taking necessary steps to expedite claimstaking relative to the new layoffs.

4. Requests by State for Federal assistance to resolve or minimize the problem(s).

5. Departmental actions contemplated or taken:

STATE OF NEW YORK

1. Current estimate of weather/energy related unemployment (insured and uninsured). 10,000.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Some problems are being encountered by some CETA sponsors in implementing the emergency jobs program. In other areas, the program seems to be operating smoothly.

3. Summary of State and local agency actions in response to the identified problems: Schenectady is reporting recruitment problems and is planning to advertise extensively in the media over the weekend. Orange County has 90 participants enrolled and on winterization jobs. Chautauqua has enrolled 339 and Niagara 300.

Syracuse city offices plan to operate on a 4-day (10 hours per day) work week beginning Monday to conserve energy.

4. Requests by State for Federal assistance to resolve or minimize the problem(s):

5. Departmental actions contemplated or taken: As of February 10, $3,339,126 of emergency funds had been allocated to 16 CETA prime sponsors.

STATE OF PENNSYLVANIA

1. Current estimate of weather/energy related unemployment (insured and uninsured). 63,000.

2. Description of urgent problem(s) identified by State agencies and/or regional offices: Need for emergency manpower to assist with cleanup, repair, and other emergency activities.

3. Summary of State and local agency actions in response to the identified problems: To date, 1,014 individuals have been hired under the emergency allocation of CETA funds. The new hires are working on a variety of jobs, some of which have been previously reported.

4. Requests by State for Federal assistance to resolve or minimize the problem(s):

5. Departmental actions contemplated or taken:

Representative LONG. Mrs. Kreps, since the weather has played such an important part in the performance of our economy for the past year, I would like to pursue it with you for just a moment and I recognize you have not been in the position for very long, and may not know the answers to these general questions. If you don't, could you have somebody get it for the record?

Is the weather service able to give us any predictions about the rest of the winter? How far in advance can they predict? What can they tell us?

Secretary KREPS. They have made some estimates, and those have been published which run along the general line that the cold weather would continue for another month. Now, that is an oversimplification and the Weather Bureau would not like me to play weatherman—weatherperson. [Laughter.]

So I would have to make available to you their specific reports.

I suppose that no prediction is more subject to debate than that one, but yes, we do publish those projections for short and somewhat longer range periods. We would be glad to send those to you daily.

Representative LONG. Could I ask you to get some related information while you are asking them to provide that?

Secretary KREPS. Yes.

Representative LONG. One, it seems to me we might be a little penny wise and pound foolish. Would an increased budget for the Weather

Bureau improve—and if so to what degree—their ability to make long range weather predictions? Would you ask them that? The state of this art is something that I know very little about.

Second, relating to the cold weather in the Eastern part of the United States, a week and half ago I had an opportunity to be on the west coast. Particularly in the rural areas, in the California and San Joaquin and some of those other valleys, and the Sierra Nevadas. It appears to me the drought problem in that part of the country has really not come anywhere near reaching what it is going to be when those reservoirs start going dry. I understand in the past, they depended upon the snowfall in order to replenish the reservoirs.

That is going to present us with a very, very difficult problem 6 or 8 months from now, just as we are in a very difficult situation because of the weather in this part of the country now.

Secretary Kreps. Yes.

The Weather Bureau is acutely conscious of these threats and has made some statements on this which I will send up to you immediately. The threat of a drought is very much in their minds. There is also some concern on their part with respect, as you know, to spring flooding in other parts of the country.

All of these statements should be perhaps more widely disbursed than they are. Going back to your question of budget, I really don't know that it is a budget constraint here. I would be glad to look into that, but it may be simply that we are not doing a good enough job of disseminating the weather reports.

[The following information was subsequently supplied for the record:]

Twice each month, the National Oceanic and Atmospheric Administration's National Weather Service (formerly Weather Bureau) publishes 30-day outlooks of departures from normal of average temperature and total precipitation for the Northern Hemisphere. During the winter, the temperature outlooks also are translated into expected ranges of heating degree days for major cities. In addition, 3-month outlooks of departures from normal of average temperature over the United States are published at the beginning of March, June, September, and December. The accuracy of the monthly and seasonal temperature outlooks presently is about 60 percent with the accuracy of monthly precipitation outlooks less.

Several recent reports, e.g., A United States Climate Program by Domestic Council Subcommittee on Climate Change, December 1974, and Understanding Climatic Change, by the National Academy of Sciences, 1975, addresses the complex problems of climate research, impact assessment, and prediction. These reports point out that the science and technology have advanced to a level such that tests should be made of the capability to develop improved predictions. It is widely believed that some improvement is possible although the amount of improvement is uncertain.

As a modest initiative, the fiscal year 1978 budget now before the 95th Congress includes a request for five people and $300,000 to begin a climate diagnostics activity that would focus expertise from several NOAA components to improve awareness and prediction of seasonal weather anomalies. Essential first steps required for improvement in climate forecasts include exploration of new applications of statistical analysis techniques, diagnostic case studies of selected recent short-term climatic fluctuations, new studies of physical and statistical relationships between atmospheric and oceanic anomalies, and increased use of satellite observational techniques. However, it is too soon in a research enterprise of this nature to estimate the impact these activities will have on forecast capabilities.

Representative Long. It is one of those things nobody gets very interested in until it gets to be an extreme type of situation. I well recognize your problems.

Thank you very much.

Representative BOLLING. Senator Javits.

Senator JAVITS. Thank you.

Mr. Chairman, I am sorry that I am late. We had a Republican conference this morning. I was trying to get an idea as to what has been said.

I would like to turn to the Secretary of Labor first and ask him about this hire program, which relates essentially to Vietnam veterans.

I notice you emphasize throughout your statement—I just had a brief opportunity to run through it—the two points: One, the very heavy impact of unemployment on the young; and, two, the need for fitting the job situation to the private enterprise system.

For example, in your prepared statement, you say:

> There would be increased emphasis on a broad range of job training efforts, apprenticeship, on-the-job training, and institutional education.

Then you go into this hire program which ultimately you hope to include nonveterans.

Now, the fact is that while I agree with you about our obligations to the Vietnam veterans, I also feel that targeting respecting youth is critically important because of the tremendous social impact of their unemployment. We had a witness yesterday who was a vice president of J. C. Penney Co. who told us that his company is kind of a typical operation. He said he could use young people even if they were new to the job market, provided that they could work out some contractual arrangement by which the Government would pay the cost of their training; but he did not want to break the minimum wage, which is a big thing with me and with labor generally, as the Secretary knows.

Now, without challenging you, Mr. Secretary, because I think you want exactly what I want, I would like you to give us some kind of a perspective upon what could be relatively conflicting entities.

After all, the youth is included in the veterans aspect; but then there is a tremendous youth problem in the urban areas, as you know.

It is belaboring the obvious. The 40- to 50-percent unemployment in very depressed areas of cities is an enormous problem of social waste, of criminal activity. It is just ghastly.

Senator Humphrey's youth bill and mine, and the youth bill put in by Senators Domenici and Bellmon, which is more or less in the Republican pattern, all seek to tie together education, training allowances, and employment in the private sector.

You have come forward with a very big block of public service employment for the Vietnam veterans. The question I would like to put to you is to try to put those things for us into perspective.

How should we legislate, bearing in mind that your objectives are exactly the same as my objectives are?

Secretary MARSHALL. First, I think that there is no conflict here. Our initial approach was to target our programs on groups with special needs. We see no conflict between having a veterans program separate from a youth program, to give it more identity and to have people who have common problems, common perceptions, and common experiences try to deal with others with similar backgrounds and experiences. Even though the Vietnam era veterans are mostly young, we have found that they are young people with special problems. If you control for everything else other than age, the Vietnam era veteran has a problem, and that causes unemployment to be much greater among that group.

This is true for the younger veterans. So we thought it important to try to focus special attention to make it possible for Vietnam era veterans to, in some sense, catch up with what they have lost.

I think one of the major differences between veterans of the Vietnam war and nonveterans of that period is that a relatively small number of people lost a sizable chunk of their lives and therefore came back from the war behind large numbers of other people in similar circumstances. In World War II, that was not the case. A whole generation tended to lose for the most part that time. We did not come back out of that war very much behind most other people, because most of us were in similar circumstances; but these veterans came back not only with that problem, but with other problems associated with the nature of that war and the attitudes of people about it and about them.

We think that all of this warrants special treatment, special efforts to try to examine that problem in some depth, to find out more than we know about the problems involved. We need to have the outreach component made up of veterans who understand that problem and understand the difficulties that other veterans have faced in reentering the labor market.

Now that doesn't mean that because we have the veterans program, that there is necessarily any conflict with the youth program. There will be some overlap, to be sure, in all of these things. We also think it is important to get the private sector involved in both of these programs. If we are to make long run improvements in the conditions of youths and veterans, we must do some things to provide linkages with the private sector and get people into good training programs and good jobs, which provide for upward mobility.

I think this is particularly critical for the youth program because their working lives are mainly in front of them. Therefore, what kinds of training, what kinds of work experiences they get early in their working lives will determine how well they do for the rest of their working careers.

Senator JAVITS. Well, Mr. Marshall, I put this up to you as against the Vietnam life dislocation. I understand it very well. I have served here all through the Vietnam war and was in Vietnam myself many times, at least four that I can remember.

You have a dislocation to millions of other Americans attributable to the idleness of youth who are nonveterans. I would strongly comment to you, sir, a balance between those programs. We owe it to the Vietnam veteran as an individual; but with the idle youth in the urban ghettos, you are affecting the whole community multiplied almost geometrically in terms of impact.

I would hope, sir, that you would work with us in a balance between the two. I have no objection to the Vietnam situation. I shall work with you all the way. I think equally, in equal numbers. That is the thing that worries me. In equal numbers we have to target our situation to youth employment which is a dreadful social problem as well as an economic problem and more than the personal problem which is the case of the Vietnam veteran.

Secretary MARSHALL. I agree that dislocation and the needs of special groups need to receive special treatment. There is a difference, of course, between the young people who are still in school and the young people who dropped out. I think that the approach that you take with those youngsters should be different. Each program needs a different approach. Similarly, we have a rural youth problem that we frequently tend to ignore because the rural poor are not as visible as the urban poor. We think that the kinds of things that you should do for young people in urban areas are not necessarily the same kinds of things that you need to do for people in rural areas. We agree with the need to target; and the veterans' program is a part of that targeting effort.

Actually, in our proposal, the youth program is a much larger program than the veterans' program.

Senator JAVITS. May I make a suggestion, Mr. Marshall, while you are before us, and not necessarily in the labor context?

That you should now coordinate both with Secretary Kreps on the EDA and with Secretary Califano on HEW, so that we may have your expertise as to a program which will have in it the components of education, training support, and a job.

I think that is where we have missed. There is no reason why with a new administration we can't get on the ball, even if it straddles three departments, instead of waiting, you know, until the horse trading starts. I really strongly urge you to do that. Try to bring to us the benefit of your expertise for a program which ties in with all three.

I think you will find that to be the way we would like to go and certainly the way our country ought to go.

Secretary MARSHALL. I agree with that. We think it is possible also to tie into other departments like Agriculture, Interior, Transportation, and HUD, where they have important things that need to be done that could be done by the people who are unemployed. We have been undertaking just such a coordination.

Senator JAVITS. Mr. Chairman, my time is up but may I ask Secretary Kreps one question?

Representative BOLLING. Go right ahead.

Senator JAVITS. I am troubled a little bit, Secretary Kreps, and forgive me, I have not analyzed your statement. I know that your prediction as to growth says, "In the first half of 1977, real investment expenditures are expected to increase very little but are expected to accelerate sharply in the second half."

Now, feeling as we do that there is tremendous underutilization of our industrial plant, only about 80 percent, and feeling as we do that we are falling alarmingly behind in the productivity field, would we have a right to turn to you and say as we consider this economic stimulus package, that we ought to consider whatever live option to the rebate you suggest, perhaps even cutting rates, because I think this is another one of the things that could help us enormously if we took a specialized look at what will materially accelerate progress in those areas?

Could you just answer that question, please?

Secretary KREPS. I am not quite sure I understand the question. If it goes to the heart of what we might do to stimulate business investment in particular——

Senator JAVITS. Right. And with a special crash effect for investment, just as we are spending according to President Carter $11 billion for what I think is a very transient shot in the arm, really.

Secretary KREPS. Yes. Well, of course, it is our hope really that the $11 billion tax rebate will stimulate consumer spending which is, in our view, the quickest way to stimulate business spending in turn. We have built the package around the proposition that business would respond quickly to an increase in consumer spending.

Now, the relatively small part of the package directed precisely at business investment was not larger because we thought in terms of the total package. Obviously, there are alternatives. If the package is not sufficiently stimulative, one could go, as you indicate, to tax cuts. One could go to larger tax rebates. One could go to a larger percentage for business investment rebates. One could increase the amount available for payroll tax offsets and so on.

It is very difficult to tell how soon and how much the stimulation will in turn stimulate business spending; but it was our reasoned judgment that in trying to go down the path between stimulation and overstimulation, which might encourage inflation, that this was about the right sized package.

Now, different things happen in very short periods of time. It looked for a while as though the business upturn was better than we expected it to be, and that was a plus. Then there is the offsetting question of what the weather will do to that, and that is an offset in the other direction.

I would think it unwise, however, on balance to fluctuate on a day-to-day basis with an economic stimulus package, particularly with reference to the weather, for example. I would much prefer to wait a bit on that until we have some firmer data to decide whether in fact we guessed too low. I am sure that I do not have to say among this group that projections of the economic response to the stimulation are best estimates, and they are not to be counted on down to the last penny. One simply has to give the stimulants enough time to have their impact and then change them if we guessed wrong.

Senator JAVITS. Thank you very much.

Representative BOLLING. I have a number of questions that I don't want you to answer today, but I would like to have you answer in writing, if possible, before the fifth of March. The reason for that date is that we start putting our response to the President's annual Economic Report in print on the 10th of March.

I can give you the long form or the short form. What I would really like is for each of you to comment on the point of the Lester Thurow article that appeared in Newsweek the other day in which he indicates that we have excused our slow rate of growth relative to the Western European economies by saying that our competitors have benefited by borrowing from our more advanced technology.

The implication is that their growth rates slowed to ours as their economies caught up with ours, but this hasn't happened. Most of the Western European countries have or will soon catch up with us in per capita GNP, yet their growth rates have not slowed.

He goes on to in effect say that while many in this country say that the interference of Government with the economic process had impaired the ability of the economy to function, that at least from his point of view, a study of the European economies would indicate that the contrary was the case, that they had done better on growth and better on a variety of other indicators, although there is a great deal more Government intervention there than there appears to be here. I don't want an answer now. I merely want to pose the question so if you have any time in the next 25 days, you could give me some kind of an answer as to your view of the arguments.

I have another one or two I consider long range. I don't want answers now. That is to raise specifically the question that Chairman Greenspan did in his last appearance before the committee on the 19th of January in connection with the President's and the Council of Economic Advisers' report which for all practical purposes proposes the notion that a 4-percent unemployment rate during the early 1960's is the equivalent of a 4.9-percent unemployment rate today.

Now even 25 days may be too short a time to try to answer that one, but I would like to have an indication of your views on that; and I don't mean by that a scholarly study. I just mean sort of a reaction that is a little bit more than off of the top of your head.

Then another one. Mr. Kendrick, the Commerce Department's chief economist, has estimated that the weather will cut the growth in GNP during the first quarter by about $2.5 billion which will cut the growth rate by 2 percentage joints from an estimated 6-percent growth at an annual rate to about 4 percent. In addition, he estimated there was about 1.25 million in additional employment at the peak which will fall off to about 100,000 by March. I am not going to ask if you agree with that. What I am going to ask is that we be informed how these estimates were made in some detail.

I think you perhaps touched on another aspect of an attempt to find out that kind of thing in a different context.

I have a couple that are long range on the foreign economic aspects. Direct investment in new plant and equipment in the United States by foreign-owned businesses could help spur the new investment needed to help strengthen the recovery. Is there room for a significant increase in foreign investment in this country; and if there is, what is the Commerce Department proposing to do to attract it?

I am not even sure that that question is fair in 25 days, but I will ask it anyway.

Then, I would like to have a report, of what Congress is doing to stimulate the export of American goods; and finally, on that subject, in the past the Commerce attachés in many of our foreign embassies have had very little business experience. This is something I have run into personally in a variety of contexts. Our businessmen abroad have had very little help compared to the services that I understand are provided to their European and Japanese competitors. I would wonder if you were giving consideration to perhaps working with the State Department to improve that.

Again, I don't want an answer to that on the record. I am going to have some short-range questions that will be very specific that I want answers for. Before I go to them, I will have another round from other Members.

Senator Proxmire.

Senator PROXMIRE. I apologize for having to absent myself after I arrived at the beginning of the hearing. We are having a caucus. I want to thank both of you for excellent statements. I did have a chance to read them during the caucus. [Laughter.]

I would like to ask both of you to comment on what appears to me to be a very serious omission in the administration's proposed or so-called stimulus program. I have asked other witnesses about this and I am kind of a Johnny-one-note on it. That is the area of housing. As you know, we have gone through a period of 3 years in which we have fallen far below any kind of estimate of the housing we need. We had 1.3 million housing starts in 1974; 1.1 in 1975; 1976, better, 1.6 or so.

In the last 3 months, 4 months of 1976 were somewhat more encouraging. This seems to me to be an area where we can have work in the private sector, employ people who are unemployed in the construction trades; minimum cost to the Federal Government, because much of the cost is borne by the homeowner who would be buying the home to provide a modest subsidy; yet there is no housing component at all.

The President did say in his economic statement on January 31 that he thought that housing should be done on a long-term basis without a—not using it for countercyclical purposes; something to that effect. I think he is overlooking an awfully good thing, a good opportunity, and a tremendous backlog of need for housing.

Mrs. Kreps, would you like to start off?

Secretary KREPS. I think the major reason we didn't have a housing component in this package was that we felt we needed a bit more time to work with the new Secretary in developing a reasonable program in this area. I would not like to foreclose the possibility of coming back to Congress with a housing proposal. I think the only additional fact one should cite here—and it certainly does not obviate the problem you suggest—is that there has been, as you know, an upturn in housing starts, up to 1.94 million in December.

I think that one swallow doesn't make a spring, however, and we can't——

Senator PROXMIRE. May I interrupt you on that point? Not only does it not make a spring, but those housing starts were of a particular kind. One thing, the cost of the houses were averaging around $50,-000. For another thing, it was erratic geographically. It wasn't throughout the country, and not particularly in areas where either vacancy rates were lower or where unemployment was high. It would seem to me that by using the tandem plan and other programs that are available, $1.8 billion is right there waiting to be used, if the administration simply says "Use it or lose it." We did that in the past and the money ran out within a week.

This is something that could get houses started in areas where there is a need for housing, where there certainly is a need for jobs.

Secretary KREPS. As I say, Senator, I would not like to foreclose the possibility of moving in that direction, and I think that the administration will be back to you on that issue.

Perhaps Mr. Marshall has something more.

Secretary MARSHALL. Well, I have very little to add to that except to say that I agree. We can use housing to provide jobs in the industry with heavy unemployment. You can also use housing to promote economic development in rural places where the need for rural housing exists; and you could coordinate that development with the employment program. That, of course, is and will be done.

My undertsanding is that because of the thing that Secretary Kreps has mentioned and because of the need to work out a longer-range housing program, Secretary Harris didn't want to make that a part of the stimulus package.

Of course, as we get a housing program underway it will in fact stimulate the economy.

Senator PROXMIRE. Well, I hope we can have something forthcoming just as soon as possible. There just is no question that it is something for people who work in the private sector.

In your prepared statement, Secretary Marshall, you say "Generally, there is a consensus that without fiscal stimulus, unemployment will continue at unacceptably high levels."

I agree with that personally but I wonder about that consensus. We see people who disagree with that: Mr. Burns, a very wise and able man; the Wall Street Journal, which has indicated in their editorials they think no stimulus is needed now. When you say there is a consensus, what do you mean? Can you give us a clearer picture of how broad and deep that consensus is?

Secretary MARSHALL. I think it is fairly broad and deep. I don't know of any people who argue that unemployment is at an acceptable level.

Senator PROXMIRE. They don't argue that. But they argue its is recovering. That 1976 was at the best since 1955 and if we leave the economy alone, it will do better. I disagree with that as I say, but I wonder how deep the consensus is.

Secretary MARSHALL. I think the consensus is fairly deep. If you look at the statements by economists from a wide range of political spectrums, there seems to be general agreement among most of them that some level of stimulus is necessary and that the present rate of growth will not be expected to reduce unemployment within an acceptable period of time.

By consensus, I would say the overwhelming economic evidence supports the view that we ought to move faster to get unemployment down. I noticed, for example, that members of the Council of Economic Advisers under several previous administrations came to that same conclusion as our own analysis of the problem.

Senator PROXMIRE. Well, as I say, I agree with that, except I go a little further by feeling that the package probably is too small, too weak. When you consider the argument made yesterday by the Committee on Economic Development, the business organization, they say that we ought to have a 6-percent growth in each of the next 2 years in real terms. As I said last year, we had a 6.1-percent growth. It was the biggest since 1955. There have been no 3 years, since the end of World War II, when we had a 3-year growth that is as big as the CED said we ought to have now where the President and everybody would like to see us, except during the Korean war years, 1950, 1951, and 1952. To argue that we can take this—what seems to be a rather weak and small package in relationship to the 1.8 trillion economy we have—gross national product we have, and do it with a—just a small impetus doesn't seem to me to be very logical.

You, I think, said something about that.

Secretary MARSHALL. Yes. There is less consensus on the second point.

Senator PROXMIRE. You said you left the consensus?

Secretary MARSHALL. There is less consensus on the stimulus that you need, than on the fact that you need stimulus.

My own view was that, in the jobs and training programs, I would like to have been able to have done much more. I think that is an area where we could have brought unemployment down much faster; but once we went through the planning process and tried to figure out what we could do prudently and effectively, we came up with what we thought we could do.

Senator PROXMIRE. I noticed that in your prepared statement, you seem to feel the limits on what we can do, and the limits on what we can do prudently in the spending program. I agree with that wholeheartedly. However, it seems to me we could substantiate a larger—a tax reduction, tax rebate, whatever, where you don't have to worry in the same way about doing it in a way that is orderly and in a way that permits the program to proceed without wasting money you spend.

Secretary MARSHALL. You can't be sure the tax reduction won't be wasted. One problem I have with the tax cut is that that is a very expensive way to bring unemployment down.

Senator PROXMIRE. It seems to me we should have the wisdom to devise—with the tax revenues we have—to devise a tax system that would stimulate the economy without wasting money, if we could get another $10 billion or more perhaps in this package. You don't think we could?

Secretary MARSHALL. Well, no; I don't really know what we can do with the tax component of it. I paid much less attention to that. My objective was to try to reduce the part of the package that went to taxes as much as possible and make the public-service and jobs component as large as possible. I felt, and had the evidence to indicate, that, relatively, public service employment would reduce unemployment at lower cost and more efficiency than the tax cut. Now, what the overall level of stimulus ought to be—we figured once we got it together, this was about right.

Senator PROXMIRE. What kind of growth do you expect in each of the next 2 years, in 1977 and in 1978?

Secretary MARSHALL. What we are hoping for is about—what? Six percent? But it may be somewhat less.

Senator PROXMIRE. In each of the next 2 years?

What do you project that would do to unemployment?

Secretary MARSHALL. Well, we would like to get it down to 6.5 percent; but it would be between 6.5 and 7 percent.

Senator PROXMIRE. 6.5 percent by the end of——

Secretary MARSHALL. Of 1977.

Senator PROXMIRE. What by the end of 1978?

Secretary MARSHALL. Well, we want to get it down, of course, as far as we can. I don't know what it would be then. I am really leery of the projections that we make. Our objective is to try to use the resources we have to get it down as far as possible.

Senator PROXMIRE. To what?

Secretary MARSHALL. As far as we can. We can do that by taking certain measures to make the programs more labor-intensive and less capital-intensive. We hope to be able to move it as low as possible.

We have some specific projections on how far down we expect it to go.

Secretary KREPS. Everyone is in the projection business. I think it is unwise—or not very useful—to speculate beyond two or three quarters.

Senator PROXMIRE. To what?

Secretary KREPS. I don't think it is very useful to speculate on what the gross national product will be beyond a very short period of time.

Senator PROXMIRE. Well, it is hard to do it. I think it is extremely useful to us. It suggests what kind of policies we should follow. If we do not know or have some notion of what 6-percent growth is likely to do to unemployment, what it is likely to do for inflation, it seems to me we are unlikely to adopt the right kind of policies. It may be that 6-percent growth is too much; maybe it is too little. You see, this should be, it seems to me, to be spelled out the best that you can. I know you have to guess. But nobody is going to hold you to it.

Secretary KREPS. The difficulty, sir, is not translating a 6-percent growth rate into a percentage rate reduction in unemployment. We can do that. What I find difficult is to project the 6 percent growth rate in the first place and, in effect, promise that any particular package will produce that. If I could just back up for a minute on your earlier questions to Mr. Marshall, actually Ray and I have some small differences of view here, which is not unusual among economists, as you know.

I think that I would lean rather more heavily on tax stimulus than he would. I agree completely that there is a limit to how fast we could create jobs either in the public service area or through public works; but my own preference would be that if we want to go to a larger stimulus package, we should do it via taxes.

Secretary MARSHALL. Let me say I don't agree with that. That is what we did. The main rationale, it seems to me, for the tax package is that once we concluded we could not get as much stimulus as we needed through the direct job programs, then we needed to have more stimulus. It seems to me on that basis the tax component is justified.

Senator PROXMIRE. My time is up, but I would like to see us move along on a reasonable kind of a goal. You say 6.5, 7 percent by the end of 1977.

Secretary MARSHALL. Maybe 6.

Senator PROXMIRE. I would like to have that down to 6.5 by the end of 1978. You haven't said that. That is my figure. If we should have a figure like that, then if we don't move that way, then it seems to me it would be a signal to the Congress and the President that we ought to consider at least additional stimulus.

Secretary MARSHALL. We had in mind all along that we would monitor the process. If we didn't seem to be on track, that then we would do additional things.

Representative BOLLING. At that point, we will pause.

I am going to recognize Senator Javits.

Senator JAVITS. Mr. Chairman, I will take exactly 5 minutes.

Mrs. Kreps, if I may have your attention, we are interested in the figures on capacity utilization in American business. You are very new at the job. I am not expecting miracles, but if you are prepared to answer, please do. We are very concerned about the accuracy of those figures. They are very important. I have used them. Lots of other people have used them.

Let me give you what is troublesome. Apparently there is a considerable difference between the Department of Commerce's index from your Bureau of Economic Analysis and the Federal Reserve index. Your Bureau of Economic Analysis says that the ratio of the utilization fell by 11 percentage points from the first quarter of 1973 to the first quarter of 1975; and that it has risen only 5 percentage points since; less than half.

On the other hand, the Federal Reserve index of capacity utilization which fell by 16 points from 1973 to 1975 has already risen by 10 points since the first quarter of 1975; to wit, by two-thirds.

That is a quantum difference and could very materially affect many of our considerations. So as I say, I am not trying to press you for an answer now, but could you look into that for us in order to see two things: One, what is the situation on the seeming difference in rate of recovery; and second, what is an optimum utilization of our capacity?

For example, we had a rate—a peacetime rate of 88 percent in 1973. On the other hand we had a wartime rate of 92 percent in 1966. So the question: give us an optimum and also account, if you can, for apparent disparity in the rate of recovery.

Secretary KREPS. Yes. Thank you, Senator, I would like to respond for the record later when I have had a chance to check these for definitional differences. I will be glad to provide that for the record.

Senator JAVITS. I ask unanimous consent that that be included in the record.

Representative BOLLING. Without objection, so ordered.

[The information referred to follows:]

I. DIFFERENCES BETWEEN BEA AND FRB MEASURES OF MANUFACTURING CAPACITY UTILIZATION

Both the Bureau of Economic Analysis and the Federal Reserve Board develop and publish estimates of capacity utilization in manufacturing. Despite important differences in the methods used to develop these statistics, they are remarkably similar in the story they tell. Both series indicate that in September 1976 (the latest date for which comparable statistics are available), capacity utilization in manufacturing averaged about 80 percent. Moreover, during the entire period 1968–1975[1] the average for both series was identical—82.4 percent. Despite these similarities, however, as Senator Javits has pointed out, the two series peaked at 86 percent in June 1973 and reached a cyclical low of 75 percent the recent contraction in economic activity, the FRB series on manufacturing capacity utilization dropped 18 points, from a cyclical peak of 88 percent in June and July 1973 to a cyclical trough of 70 percent in March 1975. The BEA series peaked at 86 percent in June 1973 and reached a cyclical low of 75 percent in March 1975—a drop of only 11 points.[2]

[1] Although the BEA series on the utilization of manufacturing capacity, introduced in the July 1974 issue of the *Survey of Current Business*, presented estimates starting with December 1965, estimates for 1966 and 1967 are available only for June and December. Starting in 1968, estimates are available covering four months of each year, March, June, September, and December. For this reason, the comparison of the two sets of statistics is confined to the period starting in 1968.

[2] In the questioning of Secretary Kreps, Senator Javits referred to a 16 point drop in the FRB series as compared to an 11 point drop of the BEA series. These comparisons are not strictly valid, however, because they relate to somewhat different time periods. The FRB data on manufacturing capacity utilization represent quarterly averages of monthly data, while the BEA series relates to a single month in each quarter; i.e., March, June, September, and December. The comparisons shown here, utilize FRB monthly data rather than the quarterly averages utilized by Senator Javits.

Although some of this difference may be related to statistical error, it is believed that the major causes of the discrepancy relate to basic differences in methods of data collection and computation and to the concepts of capacity implicit in the estimates. The FRB derives manufacturing capacity utilization rates by dividing estimates of production by estimates of capacity. The BEA bases its measures on a survey of 3,000 manufacturing companies that are asked to report "at what percentage of manufacturing capacity did your company operate in______" (month and year specified). Each method of collection, and hence each statistical series, has its own weaknesses and strengths; however, our knowledge of what is going on in the economy is strengthened, rather than weakened, by having both sets of data available.

While the analysis which follows below highlights possible reasons for differences between the FRB and BEA measures of manufacturing capacity utilization, more definitive answers require an extensive research effort. BEA and FRB are embarking on an informal, cooperative effort to do this. Based on a preliminary review, however, the following observations seem appropriate.

Recent revisions in the FRB series have greatly improved the reliability of this measure of manufacturing capacity utilization; however, as we see it a continuing problem with the FRB series relates to the weaknesses of the data base available for constructing time series on capacity by industry. Moreover, additional difficulties may derive from the fact that the capacity measures and the production measures (which are divided so as to obtain utilization rates) do not come from the same sources and may thus present problems of consistency of coverage and classification.

The Federal Reserve Board utilizes three basic data sources to develop indexes of capacity for individual groups of manufacturing industries:[3] (1) periodic measures of the book value of gross capital stock by industry available from the Bureau of the Census; (2) information on the current dollar value of business fixed investment by industry available from the Bureau of the Census and the Bureau of Economic Analysis' survey of plant and equipment expenditures; and (3) indexes of capacity and capacity utilization rates available from McGraw-Hill. Much of this information is available only annually; moreover, difficulties arise because the basic reporting units for the various sets of data are not always comparable. Thus the production, investment, and gross capital stock data from the Bureau of the Census relate to manufacturing establishments, while the information on investment, capacity, and capacity utilization from BEA and McGraw-Hill, relate to manufacturing companies. This can be a serious problem in some industries as, for example, petroleum refining, where companies engage in substantial mining, transportation, and distribution activities in addition to their major activity of manufacturing refined petroleum products.[4]

Difficulties noted above may lead to estimation errors in the FRB measures of capacity utilization. This would be particularly true at the detailed level of industry estimates but would, however, tend to cancel out at the overall level of total manufacturing.

Although the BEA series is not subject to the same data problems as the FRB series, it may nevertheless be subject to measurement error. The BEA series is not derived from any precise measures of output and capacity, but rather depends on utilization rates reported directly by companies. These company reports in themselves may not derive from actual numbers on manufacturing capacity and output, but rather may represent the corporate respondent's "best judgement." Moreover, the BEA survey may be subject to unknown sampling error.[5] It was estimated that the respondents in the reporting panel accounted for about 75 percent of gross depreciable assets held by manufacturers in 1969. (A more recent estimate of this coverage ratio is not available.) However, this coverage ratio varies by industry and by company size class with better coverage in industries characterized by primarily large companies.

The problems and differences in procedures described above undoubtedly are responsible for quarter-to-quarter difference in the two governmental measures

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[3] The procedures used by the FRB are quite technical and complex and of necessity the description presented here is quite brief. For a more complete description of the FRB procedures, see the *Federal Reserve Bulletin*, November 1976, pp. 892–905.

[4] The BEA information used for its estimates of manufacturing capacity utilization relates only to the manufacturing activities of manufacturing companies, its information on investment, however, relates to all activities of these companies.

[5] The procedures used by BEA to combine company reports into universe estimates are designed to minimize sampling errors and bias, but the actual size of these errors is not known. See technical notes to the article, "The Utilization of Manufacturing Capacity, 1965–1973" in the July 1974 *Survey of Current Business*.

of manufacturing capacity utilization. However, as already noted, over a long period of time, and particularly at the aggregate manufacturing level, these differences should tend to cancel out. A special set of factors, however, may help to explain the systematic differences between the two series in the degree of cyclical sensitivity of manufacturing capacity utilization rates.

The FRB procedures for estimating capacity imply continually growing capacity and do not allow for the possibility of cyclical declines in capacity as a result of bankruptcies or closings of costly, obsolete or environmentally damaging facilities. Moreover, they also do not provide for cyclical variations in the relationship between the growth of investment and the growth of capacity. It is quite likely that businessmen alter the mix of investment as between replacement and expansion according to the phase of the business cycle. Thus, in periods of economic expansion and strong demand a larger share of new investment may go for expanding facilities than for replacing outmoded facilities, while in periods of contraction of demand the reverse would be true. Thus, the FRB measures may tend to underestimate capacity somewhat at peaks and may considerably overestimate capacity at troughs. This possible bias in estimating capacity levels would result in an overestimate of utilization rates at peaks and an underestimate at troughs, thus exaggerating the sensitivity of capacity utilization rates to cyclical fluctations in demand.

The BEA estimates, on the other hand, may understate cyclical fluctuations because manufacturers' definitions of "existing" capacity may vary with the business cycle. In periods of peak demand, high cost facilities that are infrequently used may be considered as part of capacity, while in periods of slack demand they may be excluded. Moreover, facilities which are temporarily shut down during recessions beacuse of inadequate demand may not be considered as part of capacity. Any such tendencies to vary the definition of capacity with the business cycle would tend to reduce the cyclical amplitudes of the utilization rates. A comparison of BEA and unpublished FRB data on manufacturing capacity utilization rates by industry indicates that the tendency for the FRB data to show greater cyclical fluctuations than the BEA data is prevalent for most industries.

II. Optimal Utilization Rates

The question of what is an optimal capacity utilization rate is a difficult one to answer, particularly if one attempts to specify a single overall rate for manufacturing which would apply to all time periods. Some guidance as to the optimal level of capacity utilization can be obtained by looking at the rates actually achieved in the past at various cyclical or wartime peak periods. However, such comparisons are of limited value since these overall manufacturing rates disguise a wide dispersion in the operating rates for individual industries and companies. For example, while the overall manufacturing utilization rate peaked at 86 in June 1973, according to the BEA statistics, the rate for individual industry subgroups ranged from levels of 107 percent in the motor vehicle industry [6] and 97 percent in the petroleum indusrty to 70 percent in the aircraft industry.

Perhaps a better indication of optimal utilization rates can be obtained by reference to the preferred operating rates reported by companies in the BEA survey. As part of the BEA capacity utilization survey, respondents are asked to report "at what percentage of manufacturing capacity would your company have preferred to operate in order to achieve maximum profits or other objectives?" Although the rate varies somewhat by industry (ranging from a high of over 100 percent in the motor vehicle industry to a low of about 90 percent in the food and beverage industry) and by company-size class, the overall rate for manufacturing has been remarkably stable over time—never varying from the 94 to 95 percent range. This fact, however, should not be interpreted as indicating that a 95 percent rate can or will be achieved in all periods of peak demand. For if all companies and industries simultaneously attempted to increase their capacity utilization rates to the preferred levels, raw material, labor or other shortages could present obstacles to the achievement of this goal.

[6] This operating rate in excess of 100 percent may at first seem surprising. However, because capacity output in the BEA survey is defined as the volume of output that could be produced given existing plant and equipment and given the company's standard number of shifts and use of overtime, it is quite possible for companies to exceed "normal" capacity during peak periods of demand by using overtime and extra shifts in excess of usual practice.

Senator JAVITS. Just one other point. Again, because you are new, no pressing for an answer. I do hope you give us the philosophy of this administration on the subject.

General Motors reported the other day a $2.9 billion profit for 1976. That immediately is a scare word for the American people. My God, $2.9 billion in profits, notwithstanding that we owe $700 billion and our national product is $1,750 billion—what do you do with such profits is the question. It immediately becomes the subject of demagoguery.

Yet, business complains—and this is almost universal in business, that the disappointing performance in keying up the productivity of American business, and in modernizing the American industrial plant, which gravely threatens to become obsolete is a result of inadequate cash flow, and that means inadequate profits. Even this great industrial power is in many areas behind the Germans, the French, the Japanese, even the British and many other countries in the modernizing and productivity of various branches of industry. Could we have some questions or philosophy on that. Is it the Government's duty to announce a policy which makes clear to the people what such a large profit means to the economy and what it means to our economic future?

I ask unanimous consent that the article on GM's profits from the New York Times of February 8 be included in the record.

Representative BOLLING. Without objection, so ordered.

[The article referred to follows:]

[From the New York Times, Feb. 8, 1977]

$2.9 BILLION PROFIT AT GENERAL MOTORS IN 1976 SET RECORD

Earnings of $797 Million in Fourth Quarter a New High—Sales for Year Climbed 32%

By Reginald Stuart

Special to The New York Times

DETROIT, Feb. 7—The General Motors Corporation, the nation's leading domestic automobile manufacturer, reported today fourth-quarter and full-year sales and profits that were the highest in the company's history.

Profits for the fourth quarter were $797 million or $2.77 a share, on sales revenues of $13 billion, 29 percent higher than 1975 fourth-quarter profits of $618 million, or $2.14 a share, on sales of $10.5 billion.

For the year, one in which the corporation introduced a new line of scaled down big cars designed to deliver better mileage, G. M. reported profits of $2.9 billion, or $10.08 a share, a 132 percent increase. Sales of $47.2 billion were up 32 percent from the previous year. Earnings in 1975 were $1.2 billion, or $4.32 a share, on sales of $35.7 billion.

G.M. PROFITS SURPASS EXXON'S

Compared with other major United States corporations, General Motors' earnings for the year surpassed those of the Exxon Corporation, the nation's largest corporation based on sales. And while G.M.'s sales were higher than those of the American Telephone and Telegraph Company, the principal telephone utility in the nation, its earnings were lower than A.T.&T.'s.

For the year 1976 Exxon, a leader in the petrochemicals industry, reported profits of $2.6 billion on sales of $52.7 billion. A.T.&T. reported profits of $3.8 billion on sales of $32.5 billion. Both companies are based in New York City.

General Motors is the first of the big three automakers to report its results for the year 1976.

Net income as a percent of sales in 1976 increased to 6.2 percent last year, compared with 3.5 percent in 1975, but was below the 6.7 percent the company reported in 1973.

"OPERATING EFFICIENCIES" CITED

According to the company's earnings statement, much of the past year's increase in profits compared with the record 1973 resulted from "improved operating efficiencies" through continuing cost reduction programs. "These measures," the statement said, "more than offset increased economic costs not recovered in price and the effect of slightly lower unit volume."

In 1976, General Motors sold 8.57 million cars and trucks worldwide. But in 1973, the company sold 8.68 million.

Company employment, still reflecting some signs of the deep slump it experienced in the months immediately following the 1973 Arab oil embargo, was 748,000 last year compared to 811,000 in 1973.

At their regular meeting today, G.M. directors declared a quarterly dividend of 85 cents a share.

Meanwhile, the company reported that under its incentive program for salaried employees of the giant automobile company, some 139.7 million will be divided among approximately 6,500 employees of the company, reflecting the improved financial condition of the company and their role in making it so. This compares with $112.8 million in incentive pay in 1973, the best year prior to this one.

General Motors makes the Chevrolet, Pontiac, Buick, Oldsmobile and GMC line of cars and trucks as well as automobile parts under the Delco and AC name and appliances.

Also, at today's meeting of the G.M.C. board of directors, two vice presidents were elected.

Robert D. Burger, general sales manager of the Buick Motor Division, was elected vice president of General Motors in charge of the marketing staff, effective March 1. He will succeed Mack W. Worden, who is retiring April 1.

James G. Vorhes, general sales manager of the Pontiac Motor Division, was elected vice president of the newly created Consumer Relations and Service staff, effective March 1.

The new section is being established to improve manufacturer-customer relations, according to Thomas A. Murphy, General Motors chairman, at a time of "heightened expectations" on the part of the consumer.

Secretary KREPS. Senator Javits, I recognize that you are asking for a response for the record, but let me say quickly that I really don't know how to evaluate that $2 billion profit figure. I don't know, first of all, whether it is before or after taxes; I don't know secondly what it is—when you relate it to sales or equity, I don't know what percentage it comes out to be. I don't know what it has been in the past. I think the question that you raise as to how those profits are related to the corporation's capacity to retool itself, to modernize, to increase its productivity is the key question.

I would be glad to supply something for the record on that subject.

[The information referred to follows:]

Profits are the underlying motive force of the private sector of the economy. It is the anticipation of a profit that induces a business firm to purchase the plant and equipment and to hire the labor to offer a product to the marketplace. It is the realization of a profit that induces the firm to expand its offers of employment and to replace and augment the plant and equipment that wear out.

Substantial increases in private investment are necessary if the unemployment rate is to be reduced to a tolerable level. At the same time the increases in output that this new plant and equipment will produce is necessary to achieve reasonable price stability. Our short-run stratetgy is to increase consumer incomes so that consumer spending will increase. With current levels of excess capacity the increase in business sales resulting from higher consumer spending will be readily translated into higher business profits. This combined with the incentive of our proposed increase in the investment tax credit will lead to increases in investment. Our longer run strategy will be articulated in part by our plan for permanent reform of the tax system. This will insure that businesses have the incentives to undertake the investment that will bring the economy back toward full employment.

Senator JAVITS. Thank you very much. It's not that I am trying to draw a brief for anybody. My own feelings and views on that are too well known. I really think it is time to put it in focus for the benefit of our people. After all, we all seem to agree that if there is going to be major reemployment, if there is going to be a major increase in the productivity, if there is going to be greater economic activity, it all hinges on the private sector. The private sector comes around to us and says you politicians, demagog every time you see a big figure, and hence you destroy in the public mind a perspective on what business means, how it operates, and how it can perform.

I think it is our duty, and I welcome it, in your job and Ray Marshall's job and the other jobs in the Cabinet. Again, I said this before. It's like Eisenhower settling the Korean war. Nobody could accuse him of being pro-Communist, not even Joe McCarthy. I think it's a great opportunity for a liberal administration to put in focus this whole question. I hope very much to pursue it with all of you so that we may have—give the American people the benefit of our best judgment. What are profits? What do they mean? Does an absolute figure mean anything.?

Mrs. Kreps quite intelligently has spoken to that. How do we regard it in the future? For example, is this a pretty important and large part of any economic stimulus package?

Thank you.

Representative BOLLINGS. Congressman Moorhead.

Representative MOORHEAD. Thank you, Mr. Chairman.

In the first round of questioning I expressed some concern that maybe the economic stimulus package wasn't big enough in the beginning, particularly in fiscal 1977. Now I would like to turn to the other side of the coin, and that is will it be in the future inflationary; and both of you have testified that it would not. I would presume that part of it is, one, the rebate is a one-shot thing, will not recur; two, that the public works program will phase out, the one we were discussing, the local public works; and three, that the counter-cyclical has an automatic reduction; as unemployment goes down, there is an automatic termination date; and that, Mr. Secretary, to the extent that your programs of CETA and the like are considered permanent, they would be designed to increase productivity of workers and hence would not be inflationary; and finally, however, there is the $6 billion of permanent tax cuts which have the potential of inflationary impact.

Do you have any other reason that I can tell my people that this is not going to rekindle the flames of inflation?

Secretary KREPS. Let me respond very quickly. I would think that the best evidence would turn on the very small amount that $6 billion is when related to the GNP or to the total budget or whatever. It is comparable to the question of profits. In comparison with the base with which you work, it is simply too small to have an inflationary impact of any significant magnitude.

Secretary MARSHALL. Well, I think an added factor is that there is considerable slack in the economy, and therefore, as we expand, we ought to be able to expand without putting upward pressure on prices because we are increasing productivity, taking up that slack. I think there is also slack in the sense that there are many ways that the economy could operate more efficiently. In many ways, parts of this package are very cost-effective to the Government, because the return to the Government is greater than the expenditure. In that sense, you tend to increase output more than you increase the money supply. The consequence of that is to be deflationary.

Representative MOORHEAD. I would like to say that I join with Senator Javits in hoping there will be cooperation between your two departments and others. One example of this, Madam Secretary, there is a provision in the basic law governing public works, the Public Works and Economic Development Act, known as title 10. As I understand it, this authorized small-scale public works in areas of high unemployment; and these funds can be combined with funds from title 6 of the CETA program or other title programs to develop temporary work projects for the unemployed.

This is a separate program from the larger emergency public works program which is being discussed as part of the stimulative program and fills a somewhat different need. The only problem is that title 9 has never received an appropriation—$300 million has been authorized but not appropriated; and the Ford budget doesn't recommend any funding.

Two questions. Do you think this program should be funded? And will the President's budget amendments include funding for this program?

Secretary KREPS. Well, the local public works program, which, as you say, has not been funded, would enable us to do certain thing of a different kind from what the local public works program would do. We would look upon that with favor. In terms of your initial point of cooperation between departments, it would enable us further to do some work with the Labor Department that we cannot now do.

I would like to bolster your points that we should combine efforts on these things by noting that I have argued against having written into this local public works bill a provision for a youth program, not because I didn't believe that it was very important to have one, but rather because I thought that it should be put in the Labor Department rather than in the Commerce Department. I don't know how that will come out, but I am hopeful that it will be in Ray's bailiwick and not in mine.

Representative MOORHEAD. We are getting copies made of that press release from the Public Works Committee I referred to. I wanted to give a copy to you, Madam Secretary. I think they have followed your suggestion and do not have a special youth program.

Madam Secretary, I am coming back to the distribution end of the public works program. I am not trying to be parochial because there actually were 10 or 12 cities that had high unemployment rates that received no benefits. The previous administration said this was a computer error.

You have the same machines down there. I hope that what I said was that computers don't make errors, people who feed information into computers make errors; and I hope that you agree with my analysis of how computers behave.

Secretary KREPS. Yes. Yes. [Laughter.]

Representative MOORHEAD. I would now like to close, Mr. Chairman, quoting a letter to the Secretary of Commerce, a copy of which was sent to me. It was from a very ardent Republican, a high officer of one of the big national corporations, headquartered in Pittsburgh. Just a portion of one paragraph which says—this is a man who seldom has a kind word to say for Democrats—"Ever since I got word of the possibility that President Carter would appoint you the Secretary of Commerce, I couldn't have been more pleased. I am so happy for the country and for the new administration that you have seen fit to accept the responsibility. You add real stature to what I believe is a fine Cabinet."

Thank you, Mr. Chairman.

Representative BOLLING. Congressman Long.

Representative LONG. Thank you, Mr. Chairman.

A question and perhaps a request of both of our outstanding witnesses. Both of you know the recession of these last 2 years has hit the northeastern part of the United States and also the north central part substantially harder than it has the rest of the Nation.

One result of this, of course, was the growth in a very unusual way, particularly for those of us from the South, of old northern tier States and the sunbelt States' argument relative to the distribution of Federal spending.

The northern tier States argue that their higher unemployment was due in a substantial degree to the proportion of Federal spending in the sunbelt States. As you perhaps know, Madam Secretary, last November the Department of Commerce issued a report on that issue called "A Myth in the Making: The Southern Economic Challenge and Northern Economic Decline."

This report evidently shows—without going into it in too much detail—that the North has been losing industry to the South but that the South's growth is not at the expense of the northern tier of States. In addition, it shows that both the North and the South receive a lower share of Federal spending in most programs on a per capita basis than other areas of the country do. This leaves the whole thing really as the title of the paper your department issued—a little bit of a myth, in my opinion.

Certainly it, as a minimum, did not establish a case. I wondered if either of you had an idea about this. I was going to request that if you didn't, that perhaps this matter should be explored a little further and that perhaps a more detailed analysis of the problem was justified.

Secretary KREPS. We are beginning to work toward a White House Conference on balanced growth, and in the course of preparations for that Conference we will be examining a great many of the questions which you have pinpointed here.

We are particularly concerned with the long-run economic movements of peoples and industries, the extent to which this is a myth; and we will be documenting, I think, the case that you put forward: That the growth in the South is not necessarily or always at the expense of industries elsewhere. It may be part of the overall economic growth, but in any case, I would be glad to respond to your question in some depth since we will be working in precisely that area in the coming months.

Secretary MARSHALL. I have given some thought to that question, Mr. Long.

Representative LONG. I would suspect you have, Secretary Marshall.

Secretary MARSHALL. I think you have to separate out several parts. A lot of people pay particular attention to is the Federal expenditures part of the problem. I think once you do that it is very difficult to make the case that Federal expenditures have been very significant in causing industry to locate in the South relative to the rest of the country.

Representative LONG. Would you say that again?

Secretary MARSHALL. I think it is difficult to demonstrate that Federal expenditures alone have had much to do with the growth of industry in the South. What you will find if you break it down by categories is that the funds have been expended pretty much for what they were intended to be expended. Even though incomes have been rising faster in the South than in the rest of the country, they are still below the national average. We still have an inordinate proportion of the Nation's poor. Any poverty program you could think of would allocate more resources to the South relatively than other areas.

I think it would be extremely unfortunate for us to get divisions based upon this particular problem. It seems to me the reality is that all sections of the country have problems, and serious problems. We ought to try to get a better measurement of those problems. Many of our problems in the South don't get measured adequately. The unemployment rate tends to understate our unemployment and overstate the unemployment in an urbanized industrialized area. If you are a rural area, much of the unemployment does not get counted.

The problem in rural areas often is not that you are not working. It's that you don't get paid very much for what you do; and secondly, that you are not working full-time. It would be very difficult to find many people in rural areas who aren't doing any work, who are able to work.

So it seems to me that we ought to have programs that are evenhanded whether they are designed to deal with poverty, or are designed to deal with the problem of unemployment. There are heavy pockets of unemployment in places with low overall unemployment rates and we need, therefore, to have programs to get at that.

It seems to me that we really do need to do careful analysis and head off the divisiveness that you are likely to get by concentrating on what proportion of Federal expenditures goes into what regions.

The trouble with that, of course, is that you need to look at the reasons they went there; and if it is because you have a higher proportion of that target population, then it makes sense that that would be the outcome that you get.

Representative LONG. Well, you can well understand that we in the South have long known the advantages of living there and have seen the rest of the country getting exposed to it through national media and television. They are starting to move there and now the rest of the country is saying the South has to be penalized because of that. I hope this is not allowed to go unchallenged. There is no question that you can get to work substantially more days in the South than in the rest of the country. Therefore, your production rates go up. There are also a number of other factors involved, not counting the very personal factors.

One other thing I am particularly pleased with is your statement relating to the problems in rural areas. The fact is that special recognition has to be given to those. You stated earlier that just because a program works in a city with a high density of population is absolutely no assurance that it is going to work in a sparsely populated rural area. What appears to be developing—people beginning to move to rural areas, and a slowdown of the people moving to the inner cities—requires understanding to enable the rural areas to do perhaps better planning for it. Your recognition of that problem ought to help substantially in improving it.

I compliment you on it.

Secretary MARSHALL. Thank you.

Representative BOLLING. Senator Percy.

Senator PERCY. Thank you very much indeed, Mr. Chairman.

This is the first opportunity I have had to meet with the new Secretary of Commerce. I have met privately with the Secretary of Labor. We have not had a chance to reason together in this forum. I certainly welcome the opening statements that you made about your hopes for a long and fruitful relationship with this committee.

This is an exciting committee because it does call for a lot of ideas, the chance to think aloud. I can assure you that we welcome you now. We will welcome you in the future. We will lean heavily on you for counsel and advice. We have a joint responsibility with respect to the economy; and a tremendous responsibility to industry and labor and to the Federal Government. We share, after all, 50–50 with most corporations in their success or failures. We all want to see success. We have different approaches, obviously, in this economic stimulus package.

I don't suppose there is unanimity totally and completely within the executive branch. There won't be in Congress. There are 535 individualists down here. There is no chief executive officer. The leadership has no control over any one member. You can imagine the struggle we are going to have. I think we must struggle earnestly toward an objective and a goal.

How do we really get this economic income going in this country and hopefully in Japan and Western Germany? We are all interlinked and prove out the free enterprise system, so that it can respond.

The major part of the many parts of the package I am for—the major problem I have is the rebate part of the program; whether or not it is going to make sense. Under a Republican President, I really questioned whether it was cost effective, whether people aren't going to say, "I paid those taxes. I am getting a check back, an average $50 per individual." They had to go out and borrow the money. They had to pay 7.5 compound percent with no foreseeable chance of paying it back within 50 years.

How can they afford it? What am I supposed to do? Go buy a house, a car with this $50? It costs them $11 billion.

That is what I really worry about. I am not at all concerned about an across-the-board permanent cut. People don't just buy with what they have in their hand. They buy based upon their confidence in future income. We all do that. Business invests on that basis, and so forth.

With a permanent cut, they have income coming in they will spend with confidence. With just this check in hand, it didn't have that effect last time.

I went back over it just to check wih a good economist, a fine man, Arthur Burns, who agonized in coming out on his first appearance on an economic package and coming out against the administration on that one phase. I said the economic stimulus would be 4 to 5 weeks at the most and then it would pass right off. There you have $11 billion gone.

What arguments can you really give to do that as against investing in a longer term permanent tax cut? Is that $11 billion part of it really crucial to the total overall economic package? The package we ought to have is about the same cost overall for the 2-year period as this one, but I don't like that $11 billion. I don't think it is really cost effective. I think it is going to make people really worry about their government, that we were going to give them back out of what we don't have, money they have already paid in for taxes and should be paid.

Everyone ought to fairly share the tax load. I talked with hundreds of people on this. I haven't found one that thinks it makes any sense.

Secretary MARSHALL. Senator Percy, I will respond to that.

I agree with much of what you say about taxes. I think the impact of rebates in the past has been exaggerated and that it has not had as much effect as other things that you could do. I think there are several considerations that made it necessary in this case to use the rebate. One was that we contemplated a reform of the tax system and that a permanent tax cut now would make it difficult to do that later on.

The other main concern was that we felt that we could not do other things fast enough, because of the time constraints that we were operating under, to be able to stimulate the economy as much as we thought was necessary simply through spending programs alone.

So, when we got through putting all of that together, it was clear that we needed a mix, and the judgment was made that the fastest way that you could do it would be to rebate and that just because it was not permanent, it commended itself; that is to say, you wouldn't interfere with your ability in the long run to reform the tax system. Second, if you had done too much, the fact that it is temporary and, therefore, phases out means that you wouldn't be exerting undue inflationary influence on the system in the long run before you had a chance to really think it out.

I think the thing that is very important to keep in mind is that we had to do all of this in a hurry. We didn't have time to think through as much as we will in the long run all aspects of the tax reform part of the administration's objectives. We felt the need, because of the performance of the economy, to get a reasonable amount of stimulus into the system.

Now people disagree. Some say we stimulate too much; some not enough. I think that the judgment that was made is that we needed the rebate for those reasons. Those were the main considerations, I think involved in the rebate.

Do you want to add to that?

Senator PERCY. Secretary Kreps.

Secretary KREPS. I think Secretary Marshall has added up most of the arguments on this side. I would emphasize the long-run question of tax reform as needing to accompany substantial tax cuts; and certainly there is no disagreement with your proposal that a permanent tax cut is more stimulative than a tax rebate. There is no question about that.

Senator PERCY. Let me disagree on some subjects. Let me raise a subject on which I think we agree wholeheartedly. The reason I couldn't be here at the outset is that I was at the White House with the President and Jim Schlesinger talking about launching a new organization entitled the "Alliance To Save Energy" of which both of you are honorary chairman, you, Secretary Kreps, for commerce and industry, and you, Secretary Marshall, for labor.

It was 65 degrees in the office that I met the President in. It is 77 degrees in this room. The Senate of the United States ought to be admonished and someone condemned for being 12 degrees over the temperature that we ought to maintain. We are wasting and squandering here and making it uncomfortable for many of us in this room. I don't know what is wrong. I have tried to get the temperature in this room down before without success. We ordered the Sergeant at Arms to order the building superintendent to control and get it down to what the President has asked us to do.

We are announcing this Alliance To Save Energy at 1:30 today. We are grateful for the participation of both of you. The President is issuing a strong statement on it. Vice President Mondale and former President Ford will be honorary chairmen on it. We have the A. C. Nielsen Co.; Mobil Oil; Arthur Wood last night at 11 o'clock accepted to be on the advisory board; the head of Sears, Roebuck, Rob Ingersoll; the Deputy Secretary of State, George Meany; Leonard Woodcock and Glenn Watts from the labor movement are on our board of directors of the organization.

Do you think that saving energy is one of the highest priorities this country now has to bring down inflation, bring down the cost of production, to make us less dependent upon outside sources and to start to show the intestinal fortitude this country ought to have to work together to make this a better and stronger America and that the biggest single source of energy available is not North Slope oil, not offshore, not shale, not coal gasification. The cheapest, most efficient, lowest cost is saving energy that we are wasting and squandering.

Would any of you care to make a comment as to how you feel about that and what the effect would be on the economy when you see schools closed, factories closed, and a million and a half people out of work because of wasted energy and not fairly sharing among ourselves?

Secretary Kreps. Senator Percy, this is an eloquent statement to which we all subscribe heartily. The figures clearly indicate that saving energy is much more effective and much less expensive than trying to produce more.

I might, in addition to agreeing with you, heartily say that from where I sit this morning, the temperatures seems higher than 77 degrees. [Laughter.]

Secretary Marshall. I was relieved to learn that it was the temperature causing it to be so hot here. I agree, also. I think it is one of the most important problems the country faces. I think we need to take advantage of this concern that people have now because of the emergency that we have been in to build a longer range energy policy, and not let that opportunity go by.

People can get a little insight from this particular problem that we are having now into what might be a much more massive long-range problem if we don't address ourselves to the energy problem and develop better sources of energy, but at the same time conserve what we have got. I thoroughly agree with that.

Senator PERCY. Thank you very much indeed.

My time is up, Mr. Chairman. I have a few more questions that I would like to come back to.

Representative BOLLING. I suspect that what is wrong in this room and in this building has to do with design and engineering more than the lack of will on the part of the building superintendent.

Mrs. Kreps, I have a question which is in effect in writing that Senator Humphrey was anxious to have you respond to. It includes a letter that he sent to Elmer Staats with regard to the whole question of the availability of statistics and information, the lack of coordination, and so on.

He has asked for a study and I understand Mr. Staats indicated that the GAO would pusue it. We would like a comment on a couple of specific questions. It will be given to your assistant.

Now I have one subject that has been driving me nearly mad in the latst 3 weeks. In another capacity, I have been working with a number of committees, individuals, and groups on the outside on the stimulus package. The one thing that really bothers me, and I find it incredible, is that it is almost impossible to get really good information as to what a program of job stimulation will do in the short run and when.

I will give you an example. A very knowledgeable member of the staff was talking to me and indicated that a public works program would put people to work only after *x*—I am not even going to identify *x*. Then I talked to a very knowledgeable member of the leadership of the labor movement. I didn't quote the figure because I didn't believe that one; and he came back with a response that said, "Oh, that is completely untrue. All you have to do is pass an authorization bill on public works, I can issue a letter of intent, and the people go to work at once."

Well, I think part of the problem we have been having on the Hill in this particular case is that nobody really knows what they are talking about. They set up their own particular prejudices as to what the fact is, as to how quickly people go to work under this program, that program, the other program. It was suggested to me that I ask a question to you as to whether the 90-day requirement that something begin to happen wasn't too fast in terms of planning and management, and so on.

Well, the question is, Have we ever monitored any of these programs well enough, any of the programs that have passed, so that we really know how quickly this program, that program, the other program will put people to work? And if the answer to that is generally yes or generally no, I am not going to ask for specifics. I am going to ask that we be very, very sure so that this time we do monitor those programs so that this time we can come up not with some kind of a theory, or a correct answer, but with figures that say this is what happened.

I am aware that the agglomeration of each case is going to end up with a mean figure that is going to be very buried in reality. One of the things that has disturbed me over the years is our inability to learn from our own programs.

I remember that in another context, Secretary Marshall. You stated that in some jobs programs, we learned quite a lot. I don't know whether you would disagree with what I have said as inaccurate or pessimistic, but I am sure we have learned quite a lot. I hope we can learn a lot more in the next year or so.

Am I wrong or right?

Secretary MARSHALL. I share in your frustration, I might add.

When I first got responsibility for putting our part of the package together, the assumption I made—in fact, I am on record, before I got to be Secretary of Labor. I was a part of a group saying we could get a million public service jobs by—I don't know if we put a time on it. It is a lot different giving general advice from the outside and having to sit down and figure out how to do it.

Once I got in and tried to figure out how to do it, it was different. I will tell you what kind of elements we put together. We have monitored some of these programs. I know we had the Emergeny Employment Act where there was a deliberate effort made on the part of the Department of Labor to move as fast as you could; and to put that into operation as fast as you could.

It was monitored relatively carefully. You never get precision with those kinds of evaluations, but that program was monitored both inside the Labor Department and outside the Labor Department to see what the consequences of rapid movement really were.

We did learn some things about how you can move faster and what kinds of techniques you can use. We have been very alert to them. We built those in and made our estimates on those basis. We said that we believe that given the constraints we have, given the information we have, our judgment is that going to 725,000 public service jobs by the end of fiscal 1978 is just about all that we can do.

In fact, a lot of my people are nervous and many don't believe we can do it and that we are really going too far based on our past experience.

Now there are several things that complicate that problem. One is that if you make an effort to target on a particular group, you slow down the process, because you have to be sure about the eligibility requirements. A second complicating factor that we had to deal with was the flexibility of the delivery mechanism and the linkages built into that delivery mechanism—the leakages I should say. Because if we give public service emploment to local units of government, for example, there is a problem of estimating how much of that would be general revenue sharing in a sense. That is, they use that money like they use all the rest of the money they get, which I think is the natural inclination of any organization.

You estimate the leakages you get through that process. There are ways to avoid the leakages. One way to do it is to try to tighten up the regulations, to make it short term and to specify the way you do it. Once you start doing it, it slows up the process. You have to be sure you meet those kinds of deadlines. There are other ways you can move relatively rapidly to get people to work faster. One is to contract with nonprofit corporations to do a lot of these things, and title VI of SETA now permits that.

I think interagency agreements within the Federal Government, using the local private sponsor mechanism to actually carry it out, is another way to speed up the process.

In other words, make an agreement such as we are in the process of doing between the Department of Labor and the Department of Agriculture, to use public service employment as a way to do forest work and reclamation work, and make an agreement with the Department of the Interior to use public service employment as a way to get work done in the national parks.

Now, the thing that makes it slow is how do we know that we didn't just give somebody some money to do what they would have done anyway? How do we know we didn't do too much for those who didn't need it and not enough for those who did? If we just wanted to throw money out, we could get it out fast and get people to take it. We feel responsibility for accountability. We know something about what is required because people have been at this a long time and know what our experience has been and know what kind of problems we have encountered. We finally just have to make the judgment.

What I hope is the next time I get asked that question, though, I can answer it with much greater precision because we are studying that very question: How do we find out more about the flexibility of the system and how do we find out more about the impact that we have and how do we monitor and measure these processes?

Representative BOLLING. That is a very encouraging answer. I will tell you why I am so frustrated. I can't remember how long it was but Paul Douglas and I sponsored a piece of legislation, early, I think, in the Eisenhower administration to set up a shell for public works. I would hesitate to say how long it took to get that done.

Secretary MARSHALL. I remember that.

Representative BOLLING. There is some kind of insanity in it taking 20-odd years to get to the point where I am encouraged by what you replied to my question. I am not obviously criticizing you or anybody else. It just is a good example of how difficult it is to relate a legislative process to an executive enterprise; and there's been a terrible inability to put the two together in a rational way in this particular field in my judgment.

Secretary KREPS. I am sorry to say, Mr. Chairman, that we have no experience in monitoring local public works. These are new programs, as you know.

Representative BOLLING. Right.

Secretary KREPS. The work should be getting underway now. It is impeded somewhat by the weather and therefore we have no information of the sort that Mr. Hewitt has been accumulating for years in the Labor Department. We will, of course, monitor these programs very carefully.

Representative BOLLING. Thank you.

I understand that you have another engagement. I would like to yield to Senator Percy if he has a question for you. I know he doesn't want to impose on your time.

Senator PERCY. I don't, but I have one burning question that I want to ask.

Senator Humphrey is the cochairman of the Alliance To Save Energy with me and we will be launching it this afternoon at 1:30. We also introduced—I introduced with him, as the principal sponsor, I cosponsored it, a resolution last year or a bill entitled "The Investment Policy Act of 1976." We will reintroduce it with modifications this year. The reference is S. 3693. It is like the unemployment bill of 1946. It doesn't have any money in it. It is just declared a national policy. Here is the declaration: The Congress hereby declares it is the policy and responsibility of the Federal Government to use all practical means to assist with other essential considerations of national policy to provide sufficient incentives to assure maximum investment in private enterprise in order to increase the production of goods, the providing of services, the employment of workers, the opportunity for profit, and the payment of taxes.

Is that a declaration of policy just offhand that you think you could support? Do you think it would be a good thing for us to move that forward now as a matter of national policy so that we do recognize in the private enterprise system, so we can create public service jobs and public works and so forth?

Do you think that a huge bulk of our future employment for youth, women, minorities, everyone will come from the private sector?

Do you think they must have sufficient investment and capital in order to provide for the efficient hiring and the adequate hiring of our future potential labor force?

Secretary KREPS. In principle I would support such a policy statement, Senator Percy. It does seem to me that we have often erred in the direction of looking to the Federal Government for programs that create jobs directly as opposed to looking for ways in which we can induce business to create a much larger number of jobs and permanent jobs at that. So the Department would be very enthusiastic about such a statement.

Thank you.

Senator PERCY. Secretary Marshall.

Secretary MARSHALL. Yes. Let me say that I think it is clear that we must do everything we can to stimulate the private sector. I think it would be unfortunate for us to take an antipublic attitude, just as I think it would be unfortunate for us to take a position against the private sector. What we are in is a partnership.

I think there are some things that a "Department Secretary" cannot do. There are many things he or she can do very well. We ought to let them do those things they can do very well. We will need the kind of partnership and cooperation between the private and public sectors in order to resolve any of the problems facing the country. As I understand it, for example, we have a serious investment problem in the energy field. The amount of investment that would be required to resolve that question is not likely, I am told, to be put out by the private sector alone. Some mechanism might have to be worked out.

There has to be a partnership to solve our health problems, our employment problems, or any other problems the country faces. We need to examine carefully what the private sector can and will do and what the public sector ought to be doing. I think one of the unfortunate things is that too often people are antibusiness or antiprofits or antiprivate sector or antipublic sector without recognizing the need for the joint undertaking.

Representative BOLLING. Madam Secretary, I understand that you have to leave. We thank you, very much.

Senator PERCY. Thank you very much, Madam Secretary.

Mr. Chairman, I would ask unanimous consent that several questions I have be included in the record and be forwarded to the Secretary of Commerce and the Secretary of Labor. I am particularly interested in Secretary Marshall's reaction to a "workfare" provision in welfare reform which I happen to support strongly.

Secretary Kreps and Secretary Marshall, I would like your comments on simplifying Government regulations and what your approach is to that and what you think the cost of various Government regulations are now to industry and the American consumer.

Finally, your reaction to a package of economic stimulus that would put highest priority on people insulating their homes, buying weather-stripping, storm windows, insulation, factories, school buildings, everyone else doing it, providing a tax credit for a certain portion of it so as to stimulate and then to demonstrate and prove to them they can get a 40- to 50-percent return on their investment. They can go out and borrow this money. I talked to the American Bankers yesterday, borrow it at 7, 8, 9 percent and get it back in 2 or 3 years, and save, and do something in the national interests.

I would appreciate your comments on that.

Representative BOLLING. Without objection, the appropriate action will be taken.

If there are no further questions, we will recess. Secretary Marshall, we are very grateful to you. It has been a most interesting morning and part of the afternoon. We thank you very much.

Secretary MARSHALL. Thank you, sir.

[Whereupon, at 12:30 p.m., the committee recessed, to reconvene at 10 a.m., Wednesday, February 23, 1977.]

[The following questions and answers were subsequently supplied for the record:]

RESPONSE OF HON. JUANITA M. KREPS TO ADDITIONAL WRITTEN QUESTIONS POSED BY REPRESENTATIVE BOLLING

FULL EMPLOYMENT-UNEMPLOYMENT RATE

Question 1. At our first hearing in this series, on January 19, former CEA Chairman Alan Greenspan argued that changes in the demographic nature of the labor force—more women and teenagers—have made a 4 percent unemployment rate during the early 1960's the equivalent of a 4.9 percent unemployment rate today. His argument is that instead of using 4 percent as our definition of full employment, we should use 4.9 percent or 5 percent. May we have your ideas on this?

Answer. Chairman Greenspan's estimate of a 4.9 percent full employment-unemployment rate is derived by developing relationships between the unemployment rates of various age-sex groups and then attributing these rates to the labor force as it is currently composed. The results one obtains by doing this will of course vary depending on the initial division of the labor force into groups. Each different grouping is likely to be associated with a different full employment-unemployment rate.

The methodology of Chairman Greenspan's computation assumes relatively stable conditions of demand and supply (excluding age-sex composition changes) in both labor and capital markets. Changes in technology lead businessmen to change the characteristics they seek in their employees. Changes in educational levels, in the average age at marriage, in average family size and in other population characteristics all combine to change the types of jobs sought by members of the labor force. Given the profound changes that have occurred over the last generation in both technology and in the characteristics of the labor force one should question the usefulness of assuming that past conditions of supply and demand in labor markets exist unchanged in the present. Many characteristics other than the age and sex composition of the labor force must be taken into account in attempting to define a full employment-unemployment rate. This Administration will carefully review the estimates made by the outgoing Council on Economic Advisers.

EFFECT OF THE WEATHER ON THE ECONOMIC OUTLOOK

Question 2. Dr. John Kendrick, the Commerce Department's Chief Economist, has estimated that the weather will cut the growth in GNP during the first quarter by about $2.5 billion which will cut the growth rate by two percentage points—from an estimated 6 percent growth at an annual rate to about 4 percent. In addition, he estimated that there was about 1.25 million in additional unemployment at the peak, which will fall off to about 100,000 by March.

Do you feel that these are accurate estimates?

If you think they are accurate, what implications do they have for economic policy?

Would you supply for the hearing record an explanation of how these estimates were made?

Answer. Dr. Kendrick was quoted in the news media to the effect that the severe weather would cut growth in GNP during the first quarter by $2.5 billion, or $10 billion at an annual rate. In terms of 1972 dollars, the reduction would be at an annual rate of $7 billion, which would cut about 2 percentage points from the overall real growth rate in the first quarter.

The estimates cited by Dr. Kendrick are based on data that were available early in February 1977. Although the estimates are highly judgmental, they seem reasonable. As new information appears, the estimates will be reviewed.

Most of the output lost in the first quarter is expected to be recouped by the end of the year. To the extent that the weather impact on the economy in the first quarter has its origin in supply shortages rather than in a basic weakness of demand, there is a question whether it would be appropriate to try to mitigate these developments by macroeconomic stimulative measures. Specific policies tailored to meet industrial requirements for natural gas and other fuels are, of course, needed.

The methodology underlying the estimates of the cold weather impact on the first quarter 1977 change in GNP is as follows: the impact on total GNP in 1972 dollars was estimated by multiplying the estimated number of persons that were not at work because of the cold weather in the first quarter of 1977 (about 450,000) by an estimate of the constant-dollar GNP per employee for the nonfarm business sector ($15,600). The figure for those not at work was based on an assumption that it would peak at 1.2 million in the first half of February and decline to about 100,000 in the second half of March. Translation of the loss in real GNP into current dollars was made by reflating the constant-dollar figure.

Various expenditure categories of real GNP in the first quarter, in terms of 1972 dollars at annual rates, were estimated as follows: personal consumption expenditures for natural gas, electricity, fuel oil, and coal were estimated to be nearly $4 billion higher than they otherwise would have been, based on utility firms' estimates of increased sales to residential customers. Constant dollar expenditures on other consumer goods and services were estimated to be about $5 billion less than they would have been because of income losses due to layoffs and shortened hours, economizing by consumers on nonfuel goods and services, and because consumers probably would do less shopping due to the cold weather.

A 6 percent decline in real outlays for private constructions was estimated; this amounts to about $2.5 billion for residential construction and somewhat more than $1 billion for nonresidential construction.

Business inventories of natural gas and fuel oil were estimated to be drawn down by about $1.5 billion more than otherwise would have occurred in the absence of the cold weather.

Net exports were estimated to decline by $0.5 billion, primarily because some commodities were not expected to be exported in the first quarter due to transportation delays caused by the cold weather.

State and local government purchases were estimated to decline about $0.5 billion, primarily in outlays for construction.

All other GNP components were estimated to decline by less than $1 billion.

BUSINESS INVESTMENT

Question 3. Direct investment in new plant and equipment in the U.S. by foreign-owned business could help spur the new investment needed to strengthen the recovery. Is there room for a significant increase in foreign investment in this country, and if there is, what is the Commerce Department proposing to do to attract it?

Answer. Possibilities exist for increased investment in the U.S. economy—from foreign as well as domestic sources. Foreign-controlled direct investment in the United States still accounts for a quite small share of our Nation's overall business activity. According to the Department of Commerce's recently completed comprehensive study of foreign direct investment in the United States, in 1974 foreign-controlled affiliates employed only about 1.6 percent of all workers in private nonfarm jobs. Furthermore, the sales of the foreign-controlled manufacturing affiliates accounted for no more than about 6 percent of the total output of any major manufacturing sector. Outside of manufacturing, the stake of foreign investors in American industry is not much higher.

There are a number of significant factors that act to attract new foreign direct investments. Perhaps the most significant of these are: (1) the extremely large size of the U.S. market; (2) the democratic institutions and political stability of this country; (3) a greater freedom from economic controls and government intervention than in most other countries; (4) the traditional U.S. "open door" policy in regard to investments from abroad; (5) U.S. leadership in managerial and marketing know-how and innovations; (6) the efficient and highly skilled U.S. labor force; (7) well-developed capital markets; (8) technological leadership in many fields, along with extensive research and development capabilities; (9) the traditional receptivity of the United States to new products, methods, and ideas; and (10) relatively large supplies of some important natural resources. Another very important factor in attracting foreign direct investments to this country has been past depreciation of the dollar relative to the currencies of many major investing nations. This has resulted in lowering the costs of making investments in the United States while making exporting to the United States more costly.

In short, the continued attractiveness of the United States as a site for new investments will result from our efforts to stimulate the U.S. economy and provide a healthy environment for business activity.

Many of the individual states have very active programs to encourage foreign direct investments. The Department of Commerce assists states by providing information and analyses regarding foreign direct investment. We also transmit to the states specific investment opportunities that are identified by the Foreign Service. Such opportunities are also published in the Department's magazine, *Commerce America.*

The Federal policy, with respect to foreign investment, is one of general neutrality, that is one of avoiding artificial encouragement or discouragement of investment.

The neutrality stance is still consistent with some restrictions on sizable foreign ownership of sensitive industrial sectors such as energy and defense-related industries.

Question 4. Will you also tell us what the Commerce Department is doing to stimulate the export of American goods?

Answer. The Domestic and International Business Administration of the Department of Commerce possesses the capability to assist U.S. manufacturers. Through the Department's 43 District Offices located in major U.S. commercial centers and through professional counseling events in Washington, U.S. manufacturers are advised as to how best to modify their products and sales programs to successfully compete in foreign markets. Further, professional economists and marketing specialists are available to provide in-depth counseling and information on the business climate, market potential, promotion and distribution techniques, competition, end-users, et cetera, for all commercially significant foreign countries.

To inform U.S. firms about significant profits that are available to them through exporting, the Department operates a Trade Opportnities Program (TOP) which provides timely notification to appropriate U.S. suppliers of specific export opportunities abroad and maintains computerized data banks which serve the needs of American exporters in identifying, selecting and establishing mutually satisfactory and continuing relationships with specific foreign sales representatives, distributors, licensees and direct-purchase customers.

To provide U.S. exporters with the marketing data they need to make hard marketing decisions, DOC analyzes marketing information and market research. This information is disseminated to U.S. industry in more than 300 individual publications annually.

To help U.S. business to take advantage of the marketing opportunities, the Department offers a variety of trade promotion services including trade centers, trade fairs, trade missions, catalog exhibitions and in-store promotions geared to best exploit each marketing opportunity. The Department is currently reviewing these programs to ensure that they continue to assist American business in export promotion.

Question 5. "In the past, the commercial attaches in many of our foreign embassies have had very little business experience, and our businessmen abroad have had very little help compared to the services provided their European and Japanese competitors. Have you had any communication with the State Department concerning an improvement in the quality of our commercial attaches?"

Answer. Yes, the Commerce Department is in continuous communication with the State Department in efforts to improve the commercial skills of our commercial attaches abroad.

This basic issue was examined in depth in 1973 by the Office of Management and Budget Study on Commercial and Economic Representation Abroad, which made numerous recommendations for improvement. This same issue was examined again recently by a joint State/Commerce Evaluation Team, which also has made a number of recommendations as to how State and Commerce can work closely and effectively to provide support which is more responsible to the needs of American business. The numerous recommendations contained in this Evaluation Team's report are now being reviewed by both Departments.

GROWTH PROSPECTS FOR THE ECONOMY

Question 6. Industrial productivity gains in Western European countries continue to outpace productivity gains in the United States. What are your explanations for this and your ideas for reversing the trend?

Answer. It is true that during the last decade or so industrial productivity has been growing more rapidly in Western Europe than in the United States.

How can our Nation's lagging performance be explained? What we know about productivity suggests that increases in this important measure can be attributed to several factors. First, gains in output per labor hour, the most common measure of productivity, tend to be determined by the amount of real capital invested by business. In recent years, however, the United States has not been devoting as high a proportion of total output toward investment in real capital as have the countries of Western Europe.

Next, changes in the industrial composition of the work force influence the rate of productivity gain. For example, there is good reason to believe that in any economy the shift of the labor force out of manufacturing industries into service industries tends to depress productivity increases. Relative to the countries of Western Europe, the United States has a higher proportion of its work force employed in service industries. Given that the shift of workers toward service-type jobs has proceeded further in the United States than in the countries of Western Europe, it is to be expected that our productivity trend would be most affected.

Apart from the industrial composition of employment, the quality of the work force—the training, experience, and age of workers—bears directly upon achievable productivity gains. During the last decade we have seen the children of the post World War II baby boom enter into the American labor force. In relative terms, Europe experienced a smaller baby boom. As a general rule, young new entrants into the work force tend to have somewhat less training and experience than older workers. The upshot is that since the mid-1960's our economy has experienced an almost unprecedented influx of workers who, temporarily, lack the skills to make a full contribution to productivity gains.

Finally, one should not overlook the fact that research and development determine in some definite, though hard to measure, way the pace of any nation's productivity increase. On this score it must be admitted that the recent record of the United States has not been encouraging. In real terms, national R&D expenditures have fallen since 1970. By contrast, the record for member countries of the EEC does not reveal a comparable rundown in their national commitments to R.&D. activities.

We must explore means by which we can encourage business to increase its rate of investment and its research and development activities. Better management, better working conditions, better use of the full potential of workers add their full fair share to productivity gains. The Department of Commerce, so long as I am head of it, will do whatever it can to try to foster human effectiveness within industry.

Finally, it is imperative we develop new methods of measuring many different features of industrial activity. In my view, our conventional and longstanding measures of economic activity, including those purporting to indicate growth and productivity, often overlook outputs which make as much a contribution to our national wellbeing as those customarily regarded as beneficial. We must shift our attention from a fascination with conventional statistics, including those bearing upon productivity, to concern over how we can better judge what is happening to the life of the American people.

Question 7. There is an argument that our productivity and growth can be accelerated if only the government would reduce its presence in the economy and cut back on special programs. But Thurow argues (see "The Myth of the American Economy," *Newsweek*, February 14, 1977) that the fastest growth is occurring in Sweden, West Germany, and Japan, where government presence is much greater than it is here, and that the fastest growth in this economy occurred during the decades of greatest growth in social programs. What is your position on the conflict between social spending and growth?

Answer. As anybody acquainted with the economics profession knows, provocative ideas and Lester Thurow seem to go hand in hand. His recent *Newsweek* article is another example of his ability to challenge conventional notions of what makes our economic system tick. While I sometimes agree and sometimes disagree with what Professor Thurow has to say, I never, if I can help it, disregard what he has to say.

As for the substance of Professor Thurow's *Newsweek* article, I wish I could be convinced that matters were as simple as he implies. But I cannot. In Sweden, West Germany, and Japan the extent of government involvement and the extent of government expenditures on social programs has certainly played an important role in their economic progress. But other considerations—social homogeneity export orientation, work ethics, savings ratios, and social goals—have played equally important roles.

Economies grow more or less vigorously because of a combination of a great many policies, circumstances, and even degrees of good or bad fortune. By no means do I reject the possibility that greater social spending or government intervention in economic affairs may accelerate the growth of our economy, but I do reject the notion that we should push for more of both, without attention to what we hope to accomplish in specific terms, under what I regard as the unfounded belief that higher economic growth will automatically follow.

MORE EFFECTIVE INFORMATION

Question 8. In our hearings and in the daily press, we hear a lot about the specific policy measures which may be followed. What goes largely unnoticed is that the information and statistics used for our policy analysis in the Congress and in executive agencies are deficient. When the foundation is weak, it is hard to build a strong "policy house."

To begin remedying this, Senator Humphrey recently requested the Comptroller General, Mr. Staats, to have GAO carry out a comprehensive study of statistical collection and analysis activities in the Federal Government. Since the quality of national policy depends on accurate and adequate information, this study will be a most important one. To be successful, the GAO will need full cooperation from the primary agencies involved with economic and social data. Would you be willing to pledge your Department's support in this effort?

I'd like to ask you a few specific questions concerning what the Commerce Department can do in this area.

Do you plan to have the Commerce Department play a leadership role for improving statistical and analysis systems in the Government?

Will the Department begin development of a *national* model of the American economy which will be both regionalized and sectoralized? This, I feel, would be most valuable, since it would mean that we could determine the impact of any major policy proposal on the national economy, on regions in our country and on specific industrial sectors. Many European nations have such a capability. Do you agree with me that we should develop such a system as soon as possible?

One final specific question. Does your Department have plans for updating the input-output tables for the American economy? What are the plans in this area?

Answer. The Department of Commerce pledges full cooperation with the General Accounting Office in its comprehensive study of statistical collection and analysis activities of the Federal Government.

The Bureau of the Census and the Bureau of Economic Analysis (BEA), which are responsible for collecting and analyzing many of the statistics on which policy decisions are based, continuously strive to improve our Nation's data base.

BEA's current program includes the preparation of benchmark input-output tables for each of the years covered by the quinquennial economic censuses. These tables are highly detailed with respect to sectors but provide no regional detail. In addition, BEA updates these national tables annually by use of summary procedures. The updated tables contain less sector detail than the benchmark tables.

The latest benchmark input-output table for the Nation is based on the 1967 census. Currently, BEA is working toward completion of the 1972 benchmark input-output table, which is expected to be available early in 1978. Annual input-output tables for the Nation have been published for the years through 1970, and the update for 1971 is nearing completion. BEA is accelerating the preparation of the updated tables, so that they will be available 3 years after the year of reference.

BEA plans to construct an input-output model of the U.S. economy, which will be both regionalized and sectoralized—one that will provide industry detail by State. Budgetary conditions permitting, funds for constructing this model could be in the Department's budget request for fiscal year 1979. That is the earliest feasible date for beginning the project because the regional-sectoral model will be developed from the 1977 benchmark input-output table, based on the 1977 economic census which will not be available until fiscal year 1979.

Question 9. The Commerce Department could be of great help in the coming years in helping to fashion a balanced national growth policy for the U.S. One immediate possibility is to help set up the White House Conference on Balanced National Growth and Economic Development authorized in title II of Public Law 94–487. The conference is to be held within one year following the law's enactment, which was last October. I have a number of questions concerning it:

(*a*) Are there plans to move forward with such a conference?

(*b*) Will it receive broad Administration support?

(*c*) Could it be tied in with the President's 1978 National Growth and Development Report?

(*d*) What, in general, do you feel can come from such a conference?

Answer. (*a*) President Carter has designated the Department of Commerce, working with the Departments of Housing and Urban Development, Agriculture, and other domestic agencies, to organize the statutory White House Conference on Balanced National Growth and Economic Development. I have assigned staff to develop the organizational structure of the conference and give consideration to the focus of the conference. We are moving forward to initiate the conference in as expeditious a manner as is possible.

(*b*) The conference will receive broad Administration support. The Administration's concern about resolving the issues which will be discussed, and the potential for our gaining new insights into the regional and national problems needed for the consideration of a balanced national growth policy guarantees our support.

(*c*) The National Conference, including the preconference work, will be carried out in a fashion so as to support, and receive support from, the Biennial Growth Report for which HUD has the lead responsibility. We believe that the two activities are complementary, and we will coordinate them to the greatest extent feasible.

(*d*) It is my expectation that the conference will permit the development of a consensus on such important economic issues as how to balance economic growth with environmental concerns, how to achieve balanced economic growth among regions, and how to ahieve a balance between urban and rural growth. The involvement of State and local governments, Title V Interstate Commissions, and the public in the preconference and National Conference activity, hopefully will ensure that the unique problems of each State and region will be discussed openly. By identifying the problems, present policies, and priorities of the subnational entities, the President will have the necessary information to submit recommended legislation to the Congress.

RESPONSE OF HON. F. RAY MARSHALL TO ADDITIONAL WRITTEN QUESTIONS POSED BY REPRESENTATIVE BOLLING

FULL EMPLOYMENT-UNEMPLOYMENT RATE

Question 1. At our first hearing in this series, on January 19, former CEA Chairman Alan Greenspan argued that changes in the demographic nature of the labor force—more women and teenagers—has made a 4 percent unemployment rate during the early 1960's the equivalent of a 4.9 percent unemployment rate today. His argument is that instead of using 4 percent as our definition of full employment, we should use 4.9 percent or 5 percent. May we have your ideas on this?

Answer. I appreciate the opportunity to comment on former CEA Chairman Greenspan's assertion that the full employment rate of unemployment has increased over the past twenty years from about 4 percent to around 5 percent.

Considerable work has been and is being done on this subject. A recent report of the National Commission on Manpower contained a study by Michael Wachter of the University of Pennsylvania addressing the problem, and Paul Flaim of the Bureau of Labor Statistics is continuing to conduct research in the area.

The point that Dr. Greenspan and other researchers make has some validity; however, any conclusions that may or may not be drawn are open to serious question.

The point that Dr. Greenspan and others have made is that changing demographics and life styles can change the meaning and interpretation of unemployment statistics. Historically, we have thought of the American worker as a male household head. This is no longer the case. Women and young people have become increasingly important members of the labor force. Teenagers and women enter and leave the labor force more frequently than adult men and historically have had higher rates of unemployment. Thus, as the share of the labor force made up of women and young people has increased, any given set of disaggregate rates of unemployment has translated into a higher overall rate.

I would hesitate to comment at this time on the magnitude of the change in the overall rate of unemployment which is caused by changing demographics. BLS is currently doing some work in this area, and I would be glad to provide you with the results obtained when the study is complete.

However, I would like to comment on the implications of Dr. Greenspan's assertion. Here, the differences between Dr. Greenspan and myself, are more fundamental than any debate over numbers. I think Dr. Greenspan was attempting to imply that because more of the unemployed are today women and young people rather than adult men, unemployment is somehow less of a problem. I am unconvinced by these arguments. The promise of a job and a decent life in our great nation is not extended only to adult men, or to whites, or to any other special group. Unemployment is an evil no matter who is unemployed.

I think we have a commitment to find jobs for all of our people who want them. During the next four years I look forward to working with your committee and with the whole Congress in searching for new and better solutions to our Nation's unemployment problem.

THE GROWTH PROSPECTS FOR THE ECONOMY

Question 2. I would like to ask you some questions about an article by MIT Professor Lester Thurow which appeared in February 14th's *Newsweek.*

According to Thurow, we have excused our slow rate of growth relative to the western European economies by saying that our competitors have benefitted from borrowing our more advanced technology. The implication is that their growth rates would slow to ours as their economies caught up with ours. But that hasn't happened—most of the western European countries have or will soon catch up with us in per capita GNP and yet their growth rates have not slowed. Industrial productivity in western Europe countries continues to outpace productivity gains here. I would like to have some explanation for this, and your ideas on reversing the trend.

There is an argument that our productivity and growth can be reaccelerated if only the government would reduce its present in the economy and cut back on social programs. But Thurow argues that the fastest growth is occurring in Sweden, West Germany and Japan, where government presence is much greater than it is here, and that the fastest growth in their country occurred during the decades of greatest growth in social programs. What is your position on the conflict between social spending and growth?

Answer. I appreciate the opportunity to comment on the Les Thurow article which appeared in *Newsweek.* Dr. Thurow is a gifted economist. However, there are passages in the article concerning the prospects of the American economy which might mislead a reader who was not well versed in economics.

It is true that some nations in Europe have achieved larger rates of real growth and larger rates of productivity increase than we have. On the other hand, the United States has had larger rates of growth in real GNP and productivity than some other nations in Europe and still has the highest level of productivity as measured by GNP per hour of all employees.

The possible causes of these intercountry differences are numerous and complex. They are probably too complex and too numerous to be dealt with constructively in a one page article. Several years ago an interagency task force on economic growth was established under the auspices of the Council of Economic Advisers. The Labor Department has been, and continues to be vitally inteersted in the issue of productivity growth as productivity is the key factor affecting the real wages of American workers. The level of education, training, and experience of the labor force; the size, age and quality of the capital stock; the level of investment; the rate of technological innovation; the mix of final products produced; the amount and type of government intervention into the market place; all these factors can affect the rate of growth and of productivity.

Comparisons between the United States, which has a diverse labor force of almost 100 million persons and a highly differentiated and highly integrated economy, and Kuwait with a total population of less than 1 million persons and an economy which is totally dependent on one resource—oil, are not valid. Comparisons between the United States and nations such as Sweden, Switzerland, Japan or West Germany are perhaps more valid but are made difficult because of differences in size, population, resources, et cetera.

The borrowed technology argument addressed by Dr. Thurow has been often voiced. Empirical work done for the Department of Labor by Dale Jorgenson of Harvard University and Laurits Christensen and Dianne Cummings of the University of Wisconsin have indeed suggested that rates of technological change have been smaller on the United States than in Japan and some European nations since the early 1950's. Whether differential growth is accounted for by borrowing, and whether the U.S. now has the "easy task of adopting existing technologies" developed elsewhere remains an open question. Productivity growth is associated with the adoption of new technologies rather than their development, and the rate of adoption depends upon the size, and age of the capital stock, and the rate of investment since new technologies are adopted "at the margin." Differing rates of productivity growth need not imply that the United States has lost its position as a seedbed of innovation.

With regard to poverty and social programs I believe that Dr. Thurow is on the mark. Poverty does not increase productivity. Social programs which enable economically disadvantaged Americans to find good, productive jobs in the mainstream of the American economy, likewise, will not inhibit productivity or growth. On the contrary, enabling a man or a women to leave the welfare roles and produce needed goods and services in the public or private sector can only increase productivity and real output. I have stated repeatedly in public forums that I support more and better programs to put our people back to work. The Administration's fiscal stimulus package contained sizable increases for jobs programs.

In my view, we must deal in an imaginative and innovative way with the hardships suffered by economically disadvantaged members of our society. We must put our people, who are able and willing to work, in productive, non-dead end jobs. At the same time, we must create a climate conducive to growth and gains in productivity within both the private and public sectors.

Response of Hon. F. Ray Marshall to Additional Written Questions Posed by Senator Percy

Question 1. I am particularly interested in your reaction to a "workfare" provision in welfare reform which I happen to support strongly.

Answer. If by "workfare" you are referring to mandatory public service employment for employable welfare recipients, this is a concept I consider worth exploring. The Employment and Training Administration is currently developing a "work equity" project to be operated by the State of Minnesota that will feature a guaranteed public service job as the ultimate test of a welfare recipient's willingness to work as a condition of benefit continuation.

Question 2. I would like your comments on simplifying government regulations and the cost of various government regulations to industry and the American consumer.

Answer. The Department of Labor strongly supports President Carter's goal of simplifying government regulation as much as possible. The people of the United States should be able to understand the regulations and know what regulations they are being subjected to. We are attempting already to eliminate any overlap between regulations developed by the Department of Labor. At the same time, however, the diverse and complex nature of the subjects covered by some regulations impose some limitations on the extent to which regulations may be simplified. We will continue to review our regulations and will simplify them where possible.

In regard to the cost of government regulations, it is extremely difficult to assess these costs since both direct and indirect effects are involved. Each regulation must be examined separately since the nature of these effects may differ with the type of regulation. Some regulations may impact directly on a firm and the costs of production while others may affect the composition of the work force or output. Regardless of the nature of the direct effects, indirect effects on prices, employment, and output will result. In some cases these effects may be negligible and in others they may be quite large. It is necessary, therefore, to examine regulations on an individual basis.

The Department of Labor is attempting to assess the costs of some of the regulatory programs we administer. For example, studies of the costs of ERISA on small firms are underway. It is, however, extremely difficult to reach definitive conclusions, even through indepth studies.

It should be pointed out that to consider the costs of government regulations not only the costs of imposing the regulation should be considered, but also the costs of not implementing the regulation should be evaluated. For example, in the safety and health area, the cost of not imposing safety regulations must be evaluated—such as payments of workers' compensation and other benefits, lost income, disrupted production, and the unquantifiable value of the affected human lives. In some cases the costs of a proposed standard are very small while in others capital costs of compliance are estimated to be several billion dollars.

Generally in calculating these costs, it should be remembered that significant social benefits accrue from most government regulations, and such evaluations should in some manner take cognizance of those benefits.

Question 3. Finally, I am interested in your views regarding the development of economic stimulus measures related to energy conservation.

Answer. In regard to developing economic stimulus measures that would put a high priority on efforts designed not only to attack the problem of recession but the energy problem as well, the Department of Labor is working closely with the Federal Energy Administration in providing the services needed to implement the weatherization provisions of Title IV of the Energy Conservation and Production Act of 1976.

The Department also has a weatherization program in place which is coordinated by the Community Services Administration in cooperation with various prime sponsors under Title II and VI of the Comprehensive Employment and Training Act. The program is directed at the poor and the elderly and involves insulating attics and basements, caulking and weatherstripping windows and entrances, and similar activities. In addition we are carefully exploring ways that a weatherization type program might be extended to a larger segment of our society.

I see no inconsistency between attaining the goals of full employment and energy self-sufficiency. To the extent practicable, policies should be designed to address each of these issues simultaneously.

THE 1977 ECONOMIC REPORT OF THE PRESIDENT

WEDNESDAY, FEBRUARY 23, 1977

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

The committee met, pursuant to recess, at 10:04 a.m., in room 1202, Dirksen Senate Office Building, Hon. Hubert H. Humphrey (vice chairman of the committee) presiding.

Present: Senators Humphrey, Proxmire, and Javits; and Representative Long.

Also present: John R. Stark, executive director; Louis C. Krauthoff II and Courtenay M. Slater, assistant directors; G. Thomas Cator, William A. Cox, Kent H. Hughes, and L. Douglas Lee, professional staff members; Michael J. Runde, administrative assistant; and Charles H. Bradford, George D. Krumbhaar, Jr., M. Catherine Miller, and Mark R. Policinski, minority professional staff members.

OPENING STATEMENT OF SENATOR HUMPHREY, VICE CHAIRMAN

Senator HUMPHREY. We will convene the meeting of the Joint Economic Committee.

Mr. Burns, I am filling in for Congressman Bolling, our chairman. I guess that is what a vice chairman is for.

I might say we surely, as you are so well aware, welcome you to this committee. We know that this will be an interesting and most enlightening and exciting bit of testimony and cross-examination.

I believe that this is the first time since the new administration came in that we have had the chance to visit with you and we look forward to your observations.

I have a statement here. I don't think it is quite as long as your testimony, but I shall try to get on with it and give you the chance, the opportunity to tell us what you have on your mind. So we welcome you back, and it is good to have seen you last evening at the Canadian Embassy. I say very happily that my visit with Mrs. Burns was even more enjoyable than my visit with you, sir. [Laughter.]

We welcome you back, because monetary policy, as everyone knows, is important to the proper functioning of the American economy and I always enjoy talking with the man who keeps his hand on the bank vault door. I feel if you are going to talk to a banker it ought to be the best one you can find and that is who we have here this morning.

Mr. Burns, we have invited you today as part of the Joint Economic Committee's annual hearings on the state of the U.S. economy. We, as you know, have already heard from the Cabinet members, leading academicians, and representatives of both labor and business. In having you before us today, we have saved one of the very best until almost last.

As far as I am concerned, the best, for almost last.

Our annual hearings will conclude tomorrow at 9:30 a.m. in 345 Cannon House Office Building with testimony from former Chairman of the Council of Economic Advisers, Leon Keyserling and 11 o'clock with Bert Lance, the present Director of the Office of Management and Budget.

Monetary policy affects so many aspects of economic life that I am afraid that you are likely to be subjected, as you would expect, to a very wide variety and wide range of questions. I know my own concerns range from the success of the administration's proposed fiscal stimulus to the health of the housing industry.

I was just speaking to Senator Proxmire here about the housing industry and regrettably about the lack of emphasis that is being given in this administration, as well as in the previous administration, on housing construction and the ways and means of being able to absorb unemployment through much expanded housing programs.

Looking back over the past year, I certainly can say that monetary policy has accommodated a relatively modest economic recovery. It is my understanding and my hope that the Federal Reserve Board will continue that policy. I was particularly pleased to note that at the January meeting of the Federal Open Market Committee, the committee voted to keep the Federal funds rate between $4\frac{1}{4}$ and 5 percent. But it is not all good news.

The unemployment situation continues to be totally unacceptable. This is the most serious problem in our economy. Every day I read in the press about inflation and there isn't any doubt that inflation itself can contribute to unemployment. But unemployment is the stickiest problem that we have had in our so-called economic recovery and in economic developments.

Millions of Americans want to work, but simply can't find jobs. Most of last month's improvement in rate of unemployment appears to have been caused by people who have become discouraged and they have given up as we say, looking for work.

A lukewarm economic recovery has run into the shock of very cold weather. The rising food and fuel bills for the American consumer may call for more fiscal stimulus than the administration originally felt was necessary. This whole subject will be reviewed very carefully by the Congress. That is why we have hearings such as this and, of course, hearings in the Budget Committee, the Committee on Ways and Means, Finance, and other committees.

Mr. Burns, as my comments suggested, the Joint Economic Committee is concerned with the immediate problems facing the U.S. economy. And we also are interested in the long-run prospects for economic growth, for the achievement of full employment, and price stability. We would welcome any thoughts you may have along these lines.

In your oral statement you may wish to summarize some of the points contained in your prepared text. I always enjoy whatever insight you give us into your observations on the economy. Or if you wish to read the whole statement that will be fine, whatever you have in mind will be welcome.

Now, I yield to the Senator from New York.

OPENING STATEMENT OF SENATOR JAVITS

Senator JAVITS. Mr. Vice Chairman, I came very specially this morning for the markup on ethics for the Senate, but I think Arthur Burns is getting to the stage in his life when we ought to be here on time for his appearance. He has been an extremely valuable asset to our country for many years and we have never more than now needed him to exercise his judicious influence over the economic policies of our country.

I made a quick note, when the Chair spoke about money supply, that Mr. Burns' goals are very, very much broader than that and, of course, with his usual sensitivity, the Senator realized that himself and expressed to you what we hope to hear from you.

Now, I have here the subjects I will get down to in the questioning, but I wanted to leave these thoughts in your minds as you testify.

One, is unemployment a symptom or a cause?

I think it is a symptom. And I think that we are applying the remedies which are justified, but without, in my judgment, the main thrust. Can those remedies—because the cause is very much deeper—the cause is that the American industrial machine is getting obsolescent and our people are not as keen, as they once used to be, for the struggle. Now that doesn't mean they won't be again, but they are not right now.

Second, that the word is still "hungry, poor and deprived," and that that criterion more and more becomes the criterion of our own ability to set a moral tone in our country that justifies our existence and even sustain our economy.

Last, that somehow or other, we have to give the people of the United States a cause, that cause should be the sharing of domestic justice and domestic improvement; with the number in poverty very, very much reduced, revolutionarily reduced over the previous decades or whether it should be as said in an evangelism to raise the condition of the world, which is in complete misery in its main parts, and is very gravely threatened economically; or whether it is, as I say, to do this domestic job or whether we are well able to do both?

These seem to be the main questions of our day. As you are a very old friend, Mr. Burns, I really look to you and indeed I look to myself and to Senator Humphrey and my other colleagues, to lift the discussion above the mundane because that is what this committee is all about. We are the think committee of the Congress, we have no legislative authority, but I do believe that with Dick Bolling, Hubert Humphrey, and the other members we have a real opportunity to present a doctrine and we have a good chance to have other committees follow by way of implementation. It is for those rather profound reasons that I look forward to your annual appearance before us on this subject.

Thank you, Mr. Chairman.

Senator HUMPHREY. Congressman Long.

Representative LONG. No statement, Mr. Vice Chairman.

Senator HUMPHREY. Senator Proxmire.
Senator PROXMIRE. No statement, Mr. Vice Chairman.
Senator HUMPHREY. Mr. Burns, you may proceed as you wish.

STATEMENT OF HON. ARTHUR F. BURNS, CHAIRMAN, BOARD OF GOVERNORS, THE FEDERAL RESERVE SYSTEM

Mr. BURNS. I am most grateful to you, Mr. Vice Chairman, and to my dear friend, Senator Javits, for welcoming me here this morning. I have had the privilege of appearing before this committee over the period of a quarter of a century or longer. I am especially glad to be here this morning, Senator Humphrey, and to find you as joyful, vigorous, and as youthful as ever.

In fact, if my memory serves me correctly—and I think it does on this occasion—your love of life and your youthfulness and vigor are as prominent, and possibly more prominent, today than they were some 20 years ago when we first met.

Senator HUMPHREY. Mr. Burns, you can just stop your testimony right there. [Laughter.]

I don't see that we ought to go any further.

Thank you very much.

Mr. BURNS. I need hardly say that I welcome the opportunity to meet with this distinguished committee to present the views of the Federal Reserve Board.

Your deliberations this year take place at a time when the interpretation of statistical information has been made especially difficult by the vagaries of the weather.

Senator HUMPHREY. Could you just speak up a little louder, please.

Mr. BURNS. While that is troublesome, there is good reason, I believe, to feel a sense of encouragement about underlying trends in our Nation's economy. We at the Board are especially pleased that the financial stituation stands out as a significant positive factor in the economic outlook for the year ahead.

The task for monetary policy in the recent past has been clear—to facilitate a substantial expansion in economic activity, while guarding against the release of new inflationary forces. In its pursuit of that basic objective the Federal Reserve has fostered moderate rates of monetary growth.

During the period extending from the cyclical trough of March 1975 to January of this year, M–1, the narrowly defined money stock—grew at an annual rate of 5.7 percent. A broader monetary aggregate, M–2—which also includes savings and consumer-type time deposits at commercial banks—increased at a 10.7 percent rate. Contrary to the predictions of many economists who urged a more expansionist monetary policy, these increases in the stock of money have proved sufficient to finance a large gain in the physical volume of output and employment. Indeed, the evolving stock of money could readily have accommodated larger growth in economic activity than actually occurred.

The Federal Reserve's moderate policy, by damping inflationary expectations, has helped to restore public confidence—both here and abroad—in the value of our currency and in the future of our economy.

The dollar is once again a respected currency in international markets. The demand for U.S. securities and other dollar-denominated assets is again strong. And the substantial increase in the exchange value of the dollar since the recovery began has relieved some of the upward pressures on the general price level in this country.

Moreover, and mainly as a result of the lessening of inflationary expectations, interest rates have not increased as they usually do in a period of cyclical expansion. On occasion during the past 2 years, yields in securities markets have registered noticeable upward movements—sometimes, as last month, because of shifting market expectations or the pressures of heavy Treasury borrowing, at other times as a result of Federal Reserve actions intended to hold monetary growth within desirable bounds. But the general trend has been downward, and the level of market interest rates on both short-term and long-term securities is appreciably lower now than it was at the beginning of the economic recovery.

Declines in interest rates have not been confined to public markets for securities; they have extended also to loans by financial institutions. Interest rates have come down on residential mortgage loans. The rate of interest on bank loans to borrowers of the highest credit rating has declined sharply. Rates paid by other bank customers are also down; in fact, at the end of last year, interest rates on loans to small businesses and farmers were at, or very near, their lowest levels since 1973.

Meanwhile, the stock market has shown a good recovery. Despite some decline since the beginning of this year, the average price of a share on the New York Stock Exchange at present is more than 65 percent above its 1974 trough. A large measure of financial wealth has thus been restored to the millions of individuals across our land who own common stocks.

Our Nation's business enterprises have taken advantage of the prevailing financial climate to improve their liquidity, corporations have issued a huge volume of long-term bonds, and they have used the proceeds largely to repay short-term debt and to acquire liquid assets.

For a time, access to public markets for long-term funds was confined primarily to firms with the highest credit ratings. During 1976, however, lower-rated firms began to find a more receptive market for their debt issues; the yield spread between Aaa- and A-rated bonds, which was 1½ percentage points when the recovery began, has averaged only about one-half percentage point since last summer.

In addition, many medium-sized firms, as well as firms with lower credit ratings, have met their needs for long-term funds in the private placement market where life insurance companies and other institutional lenders have extended a record volume of credit.

Besides this, the improved stock market has made it much easier for corporations to raise equity funds for financing new investment projects or for rebuilding capital cushions. The dollar volume of corporate stock flotations in 1976 was far above the depressed level during the recession. By following conservative dividend policies, business enterprises also have been able to add substantially to their retained profits, and debt-to-equity ratios of corporations have generally declined.

The market for State and local government securities was troubled in late 1975 and early 1976, when the New York City financial crisis made investors very cautious and drove up borrowing costs to many States and their political subdivisions.

Since then, interest rates on municipal securities have declined sharply—more sharply, in fact, then interest rates on other fixed-income obligations. In addition, the spread between yields on higher- and lower-quality issues of municipal securities has narrowed. Record volumes of new tax-exempt bonds were sold in 1975 and 1976, in part to pay off short-term debt. These repayments, as well as the progress made in strengthening budgetary positions, have improved the standing of State and local governments with the investment community. In addition, the recent court decision setting aside the moratorium on certain of New York City's debt repayments has added materially to the confidence of investors in the safety of State and local obligation.

The condition of financial institutions has also improved over the past 2 years. Commercial banks, for example, have greatly increased their liquidity by doubling their holding of Treasury securities and reducing their reliance on volatile source of funds. With greater attention to canons of prudent management, banks have achieved moderate increases in profits—even in the fact of substantial loan losses and larger allocations to reserves for possible future losses. A large share of bank profits has been used to enhance capital positions, so that the ratio of capital to risk assets, which had declined steadily during the early 1970's, has risen appreciably. These changes have done much to enhance public confidence in the soundness of the Nation's banking system.

Other depository institutions have made similar progress in strengthening their financial condition. Savings and loan associations, in particular, have repaid large amounts of debt besides adding heavily to their holding of liquid assets. Furthermore, with savings inflows continuing very amply, the thrift institutions have stepped up their mortgage lending to a record level.

Outstanding loan commitments are at an alltime high, and mortgage rates have continued to edge downward despite the huge volume of mortgage borrowing and the recent upward movement in sensitive market rates of interest.

In sum, it is clear that the financial base for economic activity has greatly improved. That, of course, is a highly important positive factor in the general economic outlook.

Other factors also suggest the likelihood of gathering economic strength as 1977 unfolds. During the closing months of last year, the demand for goods and services—except for inventory additions—picked up, reflecting primarily a resurgence in consumer buying and a further strong advance in homebuilding.

The higher level of sales enabled business firms across the Nation to work off a good part of the excess inventories that had accumulated over the preceding months. With sales and stocks coming into better balance, the pace of orders and production began to quicken and the demand for labor strengthened. We thus began this year with employment and incomes increasing briskly.

During the past month or so, jobs, output, and sales have been adversely affected by cold weather and interruptions of fuel supplies.

In some parts of the country, drought conditions have led to the rationing of water and may later affect some branches of agriculture as well as the cost and availability of hydroelectric power.

Although the weather is leaving a mark on household budgets through its impact on incomes, fuel bills, and food prices, the overall economic effect seems to be considerably less than has been suggested by many news headlines.

In fact, production and employment have already snapped back smartly in most places. The hardships imposed on many American families by this inclement weather will be long remembered and, I hope, will stimulate long-needed action on a national energy policy. The recent difficulties, however, are not likely to have large or lasting effects on the performance of the economy during 1977.

Most major sectors of demand can be expected to contribute to the expansion of economic activity over the remainder of the year. Consumers have been showing an inclination to spend more freely; during the fourth quarter the percentage of disposable personal income devoted to consumer spending was the highest in several years.

Except in areas where the weather has been especially unfavorable, retail sales since the beginning of the year have continued at a satisfactory pace. Moreover, consumers have built up their stocks of liquid assets substantially during the past 2 years. With their financial condition thus improved, they are now displaying an increased willingness to incur added indebtedness in order to finance the purchase of automobiles and other big-ticket items.

The strong pace of consumer buying during the Christmas season resulted in a sharp decline in the ratio of inventories to sales in many lines of activity. Stocks of some goods probably have been further depleted in recent weeks because of production curtailment caused by weather and fuel problems. Businessmen may be reluctant to reorder in volume until they are more confident that the economy has regained its upward momentum. But as sales rise, they will soon have to add substantialy to their inventories in order to meet customer demands.

Prospects for residential construction are also bright. Construction of single-family homes has already rebounded sharply, and production of multifamily homes is now gradually recovering from the overbuilding and other problems that have been troubling this sector. Mortgage credit is readily available in practically all parts of the country, and residential building activity should therefore continue to move upward.

The outlook is less clear for the demand for U.S. exports. Our merchandise trade balance fell sharply last year—in large part because of our increasing dependence on foreign sources of oil and the weak revival of economic activity in many other countries. During 1977 imports will increase as the domestic economy continues to expand, but the rise is not likely to be as rapid as last year. Our export trade can be expected to improve, with the extent of the gain depending on the pace of worldwide economic expansion.

At present economic recovery is underway abroad, but the recovery in many countries is less decisive than in the United States. In a number of instances, less vigorous economic growth reflects action taken to cope with inflation and severe imbalances in international payments.

Among other difficulties, the process of adapting to the harsh reality of much higher oil prices is by no means complete. Thus, our export trade may be adversely affected for some time, particularly since credits to many foreign countries cannot very well continue rising as rapidly as they have been, or as they have in reecnt years.

There is much less uncertainty about the outlook for investment in business fixed capital in our country. Indeed the near-term prospect is clearly favorable. It is our judgment at the Board—based on the continuing improvement of product markets, the intentions of business firms disclosed by survey data, the upward trend of capital goods ordering, the increasing number of new firms, and the improved state of financial conditions—it is our judgment that business capital investment will grow significantly over the remainder of this year and into 1978. There is some question, nevertheless, as to just how vigorous or how durable the rise may be.

Historically, investment in plant and equipment has often increased rapidly even in the early stage of cyclical expansions. In the current recovery, however, business capital outlays have been sluggish; measured in constant dollars, they rose only 3 percent through the final quarter of 1976. This contrasts with an average increase of 15 percent during corresponding periods of the earlier business cycle expansions since World War II.

Of late, businessmen have been especially hesitant to commit themselves to major investment undertakings. The capital spending that has occurred so far in this expansion has been heavily concentrated in relatively small-scale items—for instance, office equipment, light machinery, and trucks. Relatively few large sized industrial or commercial construction projects have been recently started.

I believe that a major reason for the inadequate expansion of plant and equipment spending is the impact of the recession of 1974–75 on the psychology of the business community.

Not many of the current generation of business managers had ever experienced an economic decline of comparable severity. In recent times, the view spread in business circles, as it already had in the academic community, that the business cycle was dead—that any recession that might occur would prove brief and mild, because governmental policies could be relied upon to keep the economy moving forward at a rather steady pace.

Businessmen certainly were unprepared for the slump in sales and production in late 1974 or early 1975 that resulted from an inflationary process that had gotten out of control. In the aftermath of this hard experience, it is not surprising that corporate managers became more cautious in their planning and that rebuilding of the confidence needed for a new surge of investment activity is taking time.

The pattern of events has been worldwide in scope. Industrial nations generally have suffered a cycle of inflation and recession similar to that in the U.S., and businessmen everywhere have since then tended to be unusually cautious in making major long-term investment commitments. During the past year, economic expansion in most countries has been held back by weakness in business capital outlays.

Contributing to this lack of confidence is the fact that, despite heartening progress over the past 2 years inflation is still proceeding at a troublesome rate almost everywhere. In 1976, consumer prices in this country rose about 5 percent. This was down from 7 percent in 1975 and 12 percent in 1974. But our businessmen as well as other citizens fear that the continuation of even a 5 percent rate of inflation may be incompatible with the attainment of a durable prosperity.

In an inflationary environment such as we have had in recent years, many business managers are apt to feel that they cannot reliably assess costs and profits over the long-time horizons frequently involved in new investment projects. This inevitably affects their investment planning.

In addition, businessmen have been concerned for some time about the possibility of an early reintroduction—in one form or another—of price and wage controls. I sense, however, that this particular apprehension has diminished, thanks in large measure to President Carters' perception that concern about controls was complicating the process of business decisionmaking.

I must note also that governmental regulation has become an important deterrent to capital spending. Businessmen tend to shy away from costly investments whose useful economic lives may be cut short by the introduction of more stringent safety, health, or environmental standards. Rigid price regulation—as in the natural gas and transport industries—has served to reduce the incentives for investment. And the failure of the Federal Government to formulate a coherent, long-range energy policy has left the business community troubled and uncertain about the future cost and availability of fuels and petroleum feedstocks.

Futhermore, compliance with existing environmental and safety regulations adds to the cost of building and operating productive facilities—without increasing their salable output. These costs involve not only expensive equipment—such as pollution control devices—but also the time lost in going through extensive governmental review procedures.

I understand that any given industrial construction project may be subject to as many as 10 different environmental regulations at the Federal level alone.

And overlapping regulations at the Federal, State, and local levels, besides causing confusion and delay, sometimes work at cross purposes. This tangled regulatory system has caused some extraordinary delays both in the launching and completion of major capital projects.

The consideration of remedies deserves high priority. We must find the political courage to consider objectively not only the very real benefits of environmental and safety regulations, but also their economic costs.

We should give serious consideration as well to reform of our system of Federal taxation in order to reduce the disincentives to business capital formation and to equity investment in American enterprises. The current congressional study of proposals for integrating the personal and corporate income taxes is a step in the right direction. I hope that the Congress will also examine the distorting effects of inflation on the corporate income tax, which have contributed to the weakness in after tax earnings of our businesses over the past decade.

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It may be well to emphasize that the Nation's stock of industrial capital has been growing too slowly not just during the current recovery but over a period stretching back at least to the beginning of this decade. The volume of business fixed investment per person added to the labor force was appreciably smaller between 1970 and 1975 than it had been between 1960 and 1970. This unquestionably has affected the trend of productivity, which has been decidedly disappointing in recent years.

What should concern us perhaps most of all is the distinct possibility that a continued lag in capital formation will make the attainment of full employment of our labor force extremely difficult further along in the current expansion—simply because we may have a defiicency of plant capacity relative to available labor. It is important therefore, to focus attention on the whole range of problems relating to capital formation.

Senator Humphrey and Senator Percy wisely called attention to this need last year by introducing S. 3693—the Investment Policy Act of 1976—a bill that stresses the importance of creating an environment that is more conducive to business capital formation.

The steps here suggested will not suffice, however, to bring about a lasting improvement in the level of investment activity if our Ntiaon fails to pursue fiscal and monetary policies that promise continuing progress in moderating inflation. Forward business planning, which is extremely challenging under the best of circumstances, becomes exceptionally hazardous in an inflationary environment of the kind that has existed in our country since the midsixties.

Nor for that matter can there be satisfactory planning in such an environment by households or governments. Many of the problems that our cities have been living with are traceable to the stresses of inflation in the early 1970's; specifically, to the ballooning of costs for municipalities whose tax revenues, unlike those of the Federal Government, respond sluggishly to inflation.

In conducting fiscal and monetary affairs, we in the Federal Government must not allow ourselves to be lulled into thinking that stimulative actions are riskless because there is now considerable slack in the economy. As we should know by now, pressures on resources and prices can arise even at a time of substantial unemployment.

For its part, therefore, the Federal Reserce System is committed to a course of monetary policy that will permit sufficient growth of money and credit to support good expansion in economic activity, but which will avoid the release of new inflationary pressures or expectations.

On the fiscal side, it is no less imperative that budgetary deficits be gradually reduced and before long eliminated. If they are not, anxieties about the future path of inflation may thr enten the hard-won progress that has been achieved in improving the condition of our financial markets and the overall economy. As our economy continues to expand, a significant and steady lessening of Federal Government demands on capital markets will be vital to release savings for use in the private sector of the economy.

The supportive role which government appropriately plays at a time of extensive unemployment, such as we have been experiencing, must be scaled down as the Nation moves toward fuller utilization of its resources.

No problem more urgently requires our attention that the unemployment of some 7 million Americans. But we must be skeptical of solutions that require ever-larger governmental deficits or ever-faster money creation.

Fortunately, understanding of the complexities of our Nation's economic problems has grown as a result of the hard lessons of recent years. If all of us in government work together and share ideas, I am optimistic that we can fashion policies that will go far toward strengthening the state of confidence on which the jobs and prosperity of our people ultimately rest.

Thank you, Mr. Vice Chairman.

Senator HUMPHREY. Mr. Burns, thank you. Thank you in behalf of the committee and my own behalf for a very far-reching and thoughtful and in-depth presentation of your observation of our economy. I think you have given us a great deal here this morning to think about; you have also given reason for hope and growing confidence. But what I appreciated most in your statement is your ability and your capacity to weave into one fabric the many factors that make up what we call the American economy, and its relationship to the international economy, the factors which show improvement in strength, and strengthening those which still leave us with concern.

I noticed that you have emphasized the lag in capital formation. Therefore, the importance of investment policy on the part of government.

What you have indicated as I understand it is that that policy is not merely one of tax policy but also one of our ability to curb inflation, curb the forces of inflation. And, also, of course, you have brought to our attention the impact of Federal regulations, all which is most helpful.

I truly feel this is one of the most significant statements that we have had before this committee. I thank you for it. I hope that it will be studied not only by those few of us that are here today but our colleagues in the Congress.

Now, just to be a little more specific—because we need your guidance and whatever you have to say has such a tremendous impact upon the public, on public confidence in our economy, and the public's attitude toward economic developments.

You have not given us any specific figures in terms of how you see the economy in the coming year, looking forward to calendar year 1977 and then into 1978. I realize it is hazardous to make predictions, even of short term. But, we need your guidance.

What would you think will be the rate of growth, true growth in the economy for the coming year? What would you project for 1977 and then going into 1978?

Mr. BURNS. My own judgment is that the projection that President Carter and his economic staff have made is entirely reasonable; we can look forward to an expansion of our production at a rate of some 6 percent this year, and I would expect unemployment to come down and to fall below 7 percent by the end of this year. But as I think you know, it has become especially difficult to forecast unemployment because of the changing environment in which we live. Additions to the labor force have proved to be very much larger than past experience would have suggested. This is due in part to changing customs in our society; women are now accepted in industry on a far larger scale than before, and they are taking advantage of their new opportunity.

Also, I believe that inflation has put a burden on many of our families. When we look at wage statistics and the like, we see the curve rising month by month. That may suggest to some of us that wage earners are becoming better off month by month but, of course, that isn't true. As far as the wages of any particular individual are concerned, there may not have been an increase for 6 months or a year or two. That, of course, is dramatically true of the incomes of our farmers and of many of our small businessmen.

Meanwhile, the cost of living is rising for every American family. For tens of millions of people, that means that real incomes are going down month by month. That, of course, put pressure on households. Many women are responding to this pressure; they seek work in order to maintain the living standard of the family or perhaps to improve it. Because additions to the labor force have recently proved to be much larger than in the past, it has become especially difficult to forecast unemployment trends with any degree of accuracy.

Senator HUMPHREY. I think that is a very fair statement. We have had difficulties as you know the past few years really understanding the labor force or getting a fix on it, so to speak. The figures as you have noted are very flexible and variable. There isn't any doubt in my mind that inflation has played a very distinct role in this as well as lifestyle, the change in lifestyle in the American community.

What do you believe, looking forward to what is not in the Congress in terms of the economic package; how do you see the inflation rate for the coming year, Mr. Burns? Is there a chance that we can bring it down? Will it stabilize? Will it go up? Do you have any forecasts that you would like to make?

Mr. BURNS. I wish I could say that I am optimistic that the inflation rate will come down this year. I am not.

There has been some quickening in the pace of inflation in the past 6 months or so. Also, I believe that the drought in the midwest and west, including California, and the freeze in Florida, will have some impact on food prices. The energy crisis will result in price rises. Finally, while I don't want to criticize anyone, in all honesty, I am bound to say that the increase in the Federal budget is stirring up new fears, new expectations of inflation—which to some degree may turn out to be a self-fulfilling prophesy.

Senator HUMPHREY. I think we have to face the facts of fuel prices and food prices and bottlenecks as well in production facilities which lend themselves to inflation.

What I think is very, very important is to get away if we can, from the fear of inflation—you said a self-fulfilling prophesy—but not to get away from it by pretending it doesn't exist. I don't mean that. I do think it is imperative that we come to understand that the inflation rate is a deterrent to our economic growth; that it is a stimulant to unemployment; and that it does cast a shadow of fear and doubt in the investment community. I don't think there is any doubt about these things. We have learned a great deal in these last few years. The old economics of looking at unemployment as inevitably bringing down prices, that is out the window, it simply hasn't happened. But if we somehow or another could get the business community to feel there was a true sincere desire on the part of government to combat inflation, then this self-fulfilling prophesy might not materialize.

I don't quite know how we do it except through men like yourself. I think men have great confidence in you, Mr. Burns, and that is why I noticed in your statement, I take note in your statement of certain signs of basic improvement in our economy.

Am I correct in assuming that you believe that the year 1977 will see a steady improvement in the economy?

Mr. BURNS. You are entirely right in concluding that I see a steady improvement in production and jobs.

I wish I could add that I see a steady improvement in the rate of inflation. I do not.

Senator HUMPHREY. You have, outside of what you call the budgetary deficit difficulty, do you have any practical sugegstions for us on how to combat this festering sore of inflation?

Mr. BURNS. Well, I have a negative comment. I hope there will be no pressure on the Federal Reserve Board to expand the money supply faster than it has been doing. I think that the money supply has been growing at a rate which, if anything, is a little too fast.

I think that this country needs, and needs badly an anti-inflation policy.

May I, as an old friend, give you a word of advice? Along with Mr. Hawkins, you are the author of the Humphrey-Hawkins bill, and your deep concern about unemployment—really, your deep concern about human beings and about life in our America—comes through in every portion of that bill. But that bill does not give sufficient attention to inflation. I hope that you will continue working on that bill as you have been doing and try to develop an anti-inflation policy.

Senator HUMPHREY. I might say that the most recent version as you know is the result of testimony such as yours, hearings before the Banking Committee, Senator Proxmire, and in the House. We have incorporated a section on anti-inflation policy but I would be less than honest with you if I didn't say it needs further clarification.

As I see the economy—and my time is up now—we have all of the essentials here now for a substantial economic recovery. If we can maintain a policy or if we can sustain a policy that does not permit greater inflation, inflation at about 5 percent is severe enough, that is very severe. But I seriously doubt that we will get much lower than 5 percent in this coming year. But if we could give the country the belief and confidence that it was not to go beyond that, despite the pressures of food and energy, I think it would do a great deal to trigger substantial growth in both production and in employment.

Mr. Burns, we have not been too critical of late of the Federal Reserve Board and its money policy. I want to come back to that as monetary policy. My time is up. I want to come back to you and talk to you about those magic symbols M_1 and M_2 but we will wait.

Senator Proxmire.

Senator PROXMIRE. Mr. Burns, we all know that you are a superb economist and analyst of the economic situation, but I want to take this occasion to differ with you right across the board. I think your analysis couldn't be more wrong on the present outlook. It's very rosy, very optimistic, but I just don't see that we have a basis for that.

You talk, for example, about the good performance of the stock market. What I have seen is that we have had a very bad January in the stock market with a significant drop. And while it is true that there was some recovery last year, the stock market has not been performing very well lately.

No. 2, you talked about the fact that there was an increase in the proportion of consumer income that was being spent. I point out that the drop in savings rate to 6 percent, which is the lowest in 4 years, might also suggest that that expenditure rate is unlikely to continue.

In other words, people are going to spend less.

Now, to put prospective lost income into figures. Higher social security taxes will decrease the average family's income by about $70 this year, that is a loss of about $3½ billion. An estimated extra fuel bill is about $150 a family, that's likely to be another very large loss.

I figure that at perhaps $7½ billion.

Federal Energy Administration officials are predicting that prices will rise about 3 cents a gallon, I understand that is about $1 billion for every cent rise, that would be another $3 billion; it is the same as a tax increase.

We also have, as you pointed out, a strong prospect, because of a drought in the West and cold weather in the East, of a rise in food prices and that could cost $5, $6, or $7 billion.

The difficulty is that all of these inflationary items I have talked about, the energy and the food developments, can't be reached by any kind of economic restraint. It is outside the reach of any kind of economic policy to dampen it down.

In other words, if we reduce aggregate demand, it is not going to do very much in reducing the price of food. It is not going to do very much in reducing the price of energy. That kind of inflation is independent of fiscal or monetary policy.

For that reason, it seems to me that the kind of inflation that we suffer from is likely to be the kind of inflation that will not be reached by restraining the economy.

Now, I agree with you that exports are likely to be weak. I agree with you that capital spending has been disappointing and is likely to continue to be disappointing. But I would argue there is not much substance to the notion that this is primarily because of inflation.

Every businessman I have talked to—I asked them why they don't expand in plant and equipment—says the market isn't there.

They can't sell what they produce. They are operating below capacity now; why build more capacity? We have a situation in Japan with far worse inflation that we have had and yet their capital investment rate has been higher. Inflation hasn't inhibited them.

So as I look at this whole picture, I just fail to see why this notion, that the economy is likely to grow as vigorously as you indicated it will and that we don't need more stimulation, can stand up.

What's your answer?

Mr. Burns. The only answer I can give you is that you and I see the world differently.

You have assembled, as comprehensively as any reasonable man could, all the negative factors. I don't think you have presented a balanced view of the economy. However, I must admist the possibility that I may turn out to be wrong and that you may turn out to be right.

Senator HUMPHREY. Don't give in too soon.

Mr. BURNS. I am giving up nothing. I am just being courteous.

Senator PROXMIRE. Well, I gave some specific figures. Would you quarrel with the notion that we lost because of the weather-related loss in income that people won't have, they won't be able to spend that, therefore demand will be less? We lost because of the higher social security taxes, because of the higher fuel bills—aside and apart from the weather-related loss of income.

Mr. BURNS. But you ignore the resilience of human beings. As I have observed life over more years than you have——

Senator PROXMIRE. Not much.

Mr. BURNS. You're still a very young man.

As I have observed life, people normally react to adversity with great energy. They start rebuilding. They will dip into savings and they will borrow, and they will work overtime, and they will moonlight, and——

Senator PROXMIRE. But all those things, working overtime, moonlighting, depend on an expanding economy. You can't moonlight if the job isn't there. You can't work overtime if the employer won't permit you to work overtime, and he won't do it unless there is demand for his product.

Mr. BURNS. I think Americans have made great opportunities for themselves, and they have done so over our entire history. Let's not underestimate the energy of our people.

We have gotten into the habit, no matter what happens in life, of turning to the Federal Government for assistance. We ignore the fact that we have a very vital private economy. We are weakening ourselves, I think, through constant fussing with very short-range problems.

Then there is the weather. What are we going to do about it?

"The Federal Government has to move in," or "We need more rebates," or "Just distribute checks to people, throw them out from airplanes across the land." [Laughter.]

I think we had better calm down. As far as the weather is concerned, what has happened has not been much more serious than the effects of serious strikes in the past. When you look back over the historical record of major strikes, you find that things looked gloomy for a few weeks, but later on you have trouble remembering when the strike occurred.

Senator PROXMIRE. Now, Mr. Burns, let's put this in perspective. I didn't claim a huge loss because of weather. I said about $2 billion which isn't very much loss in a $1 trillion or $1.5 trillion economy.

Mr. BURNS. It is such a trifle——

Senator PROXMIRE. But I say it is an important element. And when you consider the weather along with the additional fuel cost, along with the additional social security cost, along with the additional cost of gasoline and oil, along with the prospect of increased prices for food, when you put all that together, it adds up to, I think, a figure of $25 billion.

We have a stimulus package that would give us about $15 billion this year, and you seem to think that is premature. What do we have to do before we are in a position where you think the economy deserves or needs, requires additional stimulation? Would it ever require it under any circumstances? Should we have a tax reduction? I agree with you on the excessive spending. I think that is the wrong route.

Mr. BURNS. I have testified before this committee over a long period, and time and again, I have urged tax reduction. But when the economy is expanding and generating growth on its own, as it is now, I have doubts about the wisdom of so-called fiscal stimulation.

And I think all of us ought to keep in mind that so-called stimulative fiscal policies involve risks—involves costs. Consider what has happened in the past 2 or 3 months. During that period monetary policy has been unchanged; the one interest rate over which we have substantial control—the Federal funds rate, which in effect is the interbank lending rate—has been virtually constant. Yet, according to figures I happen to have before me now, between December 21 and February 22 the 1-year Treasury bill rate rose by 54 basis points. Rates on 3-year Treasury notes rose by 75 basis points and those on 7-year Treasury notes rose by 76 basis points. Yields rose on longer-term Treasury bonds and also on corporate bonds.

These interest rate increases in part were due to the discovery by the market that Treasury borrowing will be larger than before, to the discovery by the market that the budget is going up. Not only have interest rates risen; fears of inflation have been to some degree reignited.

So, let's not talk about fiscal stimulative packages as if they would bring blessings to the people without some costs and offsets elsewhere in the economy.

Senator PROXMIRE. Well, Doctor, elsewhere you described a situation where we have a rise in interest rates as you point out, with a very weak loan demand, with only a 2.4-percent growth on an annual rate in the 4th quarter of 1976; it seems to me that you have something to answer for as the monetary policy leader in this country, that we have not provided the funds necessary.

You have a 19-page statement here and there is one sentence in your statement that is devoted to monetary policy.

I have some questions and Senator Humphrey does, too. Unfortunately, my time is up. I will be back when Senator Humphrey is through.

Senator Humphrey. Mr. Burns, I must say that this is a very unusual meeting. I am a little more optimistic than my friend from Wisconsin, primarily, I think, because of your persuasive eloquence this morning, and also my own view of the economy.

You have presented in your paper to us, in your testimony, certain developments in the economy, in the liquidity position of industry, certain industries, the general trend of the interest rate picture both in terms of short term and long term; the better position of our financial institutions; in other words, the certain building blocks of the economy have given us a heartening picture.

I think that is a fair statement, is it not?

Mr. BURNS. I think so. Thank you, Mr. Vice Chairman.

Senator HUMPHREY. Now, I think the difference that some of us have with you is whether or not in light of what Senator Proxmire has indicated, as related to the restricting of certain building blocks in the economy, there is a need for additional stimulus and what kind of stimulus should it be.

The fact that there are some risks, I think they are inevitable. There is a risk that if you don't do anything things might not work out. In fact, there is a considerable risk that that could happen.

The risk of the stimulus package with whatever inadequacies it may have and some of us are not in full agreement with the stimulus package. Those risks are minimal as compared to not having such a package. For example, on the tax rebate, I was never really too excited about the tax rebate as a proposal except for one consideration, that it does offer some immediate relief to those that have suffered from increased fuel costs. For example, the increased impact of taxation rates upon what is considered to be improved or larger income. So that the rebate has the immediate effect of some stimulation as compared to long-term, or basic changes in the tax law.

I happen to believe that there is a certain body of unemployed in the country, particularly among unskilled and among the youth that will not be absorbed at least in the immediate future by even a substantial improvement in the economy, and therefore, the question is, Is it better to have them on work programs or is it better to have them on welfare programs? Recognizing that there are differences in cost in terms of money, but the costs in terms of dignity and work habits also have to be weighed.

We had a considerable argument here on inflation of late with our friends in the labor movement.

For example, I would be interested in what you have to say about the President's request for prior notification on price and wage increases. This seems to be a hot topic in light of the meeting of the AFL-CIO at Bal Harbor, Fla., and Mr. Meany's comment. Do you have any observations you would like to make on that matter as a means of dampening down inflationary fires or pressures?

Mr. Burns. I don't really understand what the fuss is all about as far as prior notification of wage increases is concerned. The Labor Department's mediation service is thoroughly informed about wage contracts—when they expire and which ones are coming along. Prenotification is not a problem at all in that area; we have the information now. I don't know what that debate is all about, really. I think it is an emotional debate rather than a debate of substance.

Prenotification of price increases is something else again. I think you have heard me talk about that approvingly in the past, Senator, and I have not changed my basic views. But I do believe there is a time for everything; and now, when businessmen across the country are deeply concerned about possible price controls down the road, it seems doubtful to me whether this is the right time to stir up that issue.

Senator Humphrey. Despite the President's repeated statements that he will not support wage and price controls nor will he ask the Congress for wage and price controls, which I think has been made not only by the President, but by his advisers. I heard Mr. Schultze this morning on TV, Mr. Blumenthal, et cetera.

Mr. Burns. There is not the slightest doubt in my mind about the complete sincerity on the President's part and on the part of his economic advisers. There is not the slightest doubt in my mind that they will keep their pledge to the American people and to the business community.

But this confidence of mine is not shared by a large section of the business community. Although I believe they are wrong in their judgments, that does not alter the fact that these are their judgments, these are their opinions, these are their doubts.

As an old educator, I have learned that the amount of educating that you can do in a short period is very, very limited. Being concerned about the economy and its prospects, I for one, have said nothing about incomes policy in recent months, although I do believe—and I will say so candidly once again to you and to your colleagues—that this country will need to develop an incomes policy even though we as yet do not know how to do it properly.

But I don't think this is a good time to talk about this subject since businessmen are so fearful.

Senator HUMPHREY. Well, there is a certain irony here and paradoxical situation. On the one hand, the business community talks to itself about the concerns over inflation, and I think really gets into an emotional lather over it, even though there is reason—obviously reason for concern.

But at the same time, they don't want to talk about an incomes policy which has some relationship to curbing inflation. It is very difficult to deal with this volatile complex subject that we call inflation in this type of an economy that we have that's affected by worldwide factors such as energy costs and fuel costs, food costs, commodity costs. But an incomes policy is an anathema to the American business community, and apparently to the labor community. And yet the same ones that have this concern over or antagonism toward an incomes policy are the very ones that go around and daily place in the press and in the public media their deep concern over the revages of inflation.

Well, how do you get them out of this syndrome?

What you have said to me this morning, Mr. Burns, is that there is money in the banks, that the banking and lending institutions, financial institutions are stronger today than they have been for a long time; that they have been able to liquidate a number of their losses, they have even cushioned for further losses; they have had some profits. You have indicated that corporations have been expanding their financial base by both short-term and long-term bonds; that mortgage money is there, that interest rates at least over the past 18 months have been declining somewhat while there are some variations and of recent date there is some increase in Federal paper rates or Treasury notes. That basically that they are building blocks of the economy and they are in better shape today than they were at any time in the past 3 years. I think that is really what you are saying to us.

Now, what do we need to do to convince these doubters that it is time to move? What Senator Proxmire says has great merit if for only one reason, that the traditional indicaters for investment, for expansion of plant or modernization of equipment and thereby improving productivity, that those traditional indicaters are on the plus side, they are good.

What's negative? The lack of market?

Now therefore, the stimulus package comes along for one reason, well, I would say two reasons. No. 1, to increase the spending capacity of the American consumer; and to put people to work on what would be at least more productive constructive jobs than sitting around on their posterior portions waiting for the unemployment compensation or the welfare.

Now, how do you get us out of this? Dr. Burns, you notice I didn't say Mr. Burns, I say Dr. Burns, what is your prescription other than just concern over the Federal budget? The Federal budget is here simply because of the needs. Very frankly, Mr. Carter has cut out programs that many Members of Congress are deeply concerned about not because they are Members of Congress, but because there are people right out here in this hallway waiting to talk to me about projects that have been cut out.

Business people that want to know why we are cutting out the water programs. Why are we doing this? Why are we doing that?

What do you offer? I realize that you don't have a magic formula for everything, but I have such faith in you I want you to give the country this morning the reassurance that it needs, Mr. Burns, and I will look at the market tomorrow.

Mr. BURNS. Let me start by indicating what I think large sections of the business community are concerned about at the present time.

There is a certain nervousness within the business community. What is it that businessmen fear? What is it that troubles them?

They are troubled, first of all, by the size and the growth of the Federal budget.

They are worried by the continuance of inflation and the possibility that inflation may intensify. They are worried about the possibility that wage and price controls may come along 3 months, 6 months, or a year from now.

As far as wage and price controls are concerned, what I would do is nothing; I would just stop talking about them.

As far as the budget is concerned, I would make every effort to cut back on Federal spending rather than augment it. Beyond that, as far as the fear of inflation is concerned, I believe that it is important that an anti-inflation policy be developed and presented to the Congress and the country. This is something that I know the administration is working on. But the sooner a plausible, persuasive anti-inflation program is put forward, the better.

There are still other concerns on the part of the business community. This country does not have an energy policy.

Senator HUMPHREY. A what, sir?

Mr. BURNS. An energy policy.

Senator HUMPHREY. Yes.

Mr. BURNS. Our economic future at the present time is at the mercy of a half dozen Arab sheiks who could impose another embargo on imported oil. Our national security is in danger. We spend over $100 billion on defense a year at the present time, and yet our Defense Establishment could be rendered powerless if oil is cut off. Once again, I know that the President is working on such a policy and will announce it. But until that happens, there will continue to be doubts within the business community.

These are the directions in which I would be inclined to move.

Senator HUMPHREY. May I say that I thoroughly agree on the energy policy matter. I have said in our seminar with the President and his Cabinet that until we get an energy policy we have neither an economic nor a security policy. I couldn't agree with you more. Until that energy policy is resolved, the billions and billions that we are putting into defense loses much of its meaning in terms of its effectiveness; and secondly, until it is resolved, there is no way that you could make any safe predictions on the performance of the economy because energy in America is so vital to our entire economic structure.

Senator Javits.

Senator JAVITS. Thank you.

Senator HUMPHRY. Thank you for returning.

Senator JAVITS. Mr. Burns, I have read your statement with great interest, and I take great satisfaction from the fact that a report of the minority of Joint Economic Committee on what is to be done about our existing situation, which I reviewed last night, almost tracks exactly your views and they said they didn't consult. That gives me great satisfaction to know that we have come to very much the same conclusions.

The thing that I would like to ask you is this: generally the ideas as they emerge from your paper tell us not to do certain things. There are relatively few things we are to do.

For example, you are not too excited about rebates as compared with the tax reductions.

You are not very anxious to have any implications of wage and price controls, feeling that that is unwise. You tell us that we should not be quite so gung ho on environmental outlays. Generally speaking, you seem favor—I don't want to put any words in your mouth—the deflation rather than inflation which has taken place in the last couple of years which has tended to—it claims to keep unemployment high at the price of keeping inflation low.

You have taken a few cracks out of development regulation of their excessive character.

Now, that kind of characterizes the situation as I read it.

The question I would like to ask you primarily is what can we do in your judgment which is confidence-building rather than just, you know, say we won't do this and we won't do that and we won't do the other, though that, itself, of course, has a tendency to bulid confidence. But I so thoroughly agree with you when you say, "I believe that a major reason for the inadequate expansion of plant and equipment spending is the impact of the recession of 1974–75 on the psychology of the business community."

So my question, what can we do in your judgment—because I believe you define the business community as I do to include the labor community, there is no seperation there—what can we do in an affirmative policy, for example. I would like to give you three illustrations so I make my question precise.

Project independence, $100 billion. The kind of expenditure we made in war. I mean that is a massive national dedication to a great objective.

Second, we do not contribute up to 1 percent of our gross national product to the acceleration of the development of the LDC's, a dedication of our country to contribute, say, even three-quarters of 1 percent would increase our whole position in order of magnitude so enormously that we would be able to play a very much stronger hand in what we ask of the LDC's in return, and the north-south dialog would be backed up by vast resources and that is a very, very meaningful operation.

Item 3, perhaps some massive effort to deal with the world's health which is miserable, again, outside the billion people who are in the industrialized countries, to deal with the world's food and to deal with technical assistance, to even agricultural development on a Peace Corps to out-Peace Corps Peace Corps would be an inspiring and monumental national adventure.

I only suggest that by way of implementing the question that I ask.

Mr. BURNS. Thank you very much for giving me the opportunity to address some of the major questions that you have raised. I think your comments on my statement were entirely fair; my statement does lack the major forward look to which you correctly aspire.

Let me try to fill this gap to some degree.

I did comment in my statement on the need for a constructive tax policy, a tax policy designed to stimulate business capital investment in areas in which our Nation has been lagging. I won't say any more about that.

You have commented on the need for a long-range energy policy that would reestablish this country's independence in the energy area, and I endorse that completely. Whether that calls for a $100 billion project such as Vice President Rockefeller put forward is perhaps debatable. But I do think that a massive approach to this matter is desirable, and that massive expenditures on the part of the Federal Government will probably be necessary—along with a conservation program, another area in which we have been lagging badly.

I would like to comment now on two subjects. One is the need for a comprehensive program for mobilizing the latent energies and enthusiasm of the American public.

I think there are millions of people in this country who would be only too glad to have a purpose in life—something that many of us haven't had in recent times—who would be very willing to devote their time and energy to help educate many of our youths who are wandering the cities and many of our unskilled people, to find jobs for them, to help them in their manner of living.

I think we badly need to revitalize our cities. But when we talk about that subject, what we commonly do is focus on Federal spending. Well, we have had massive Federal programs, and they haven't accomplished very much.

You have put forward some ideas in that area yourself, Senator, over the years.

We need to establish productivity councils within individual plants, in individual cities across the country. We need a national productivity center that would supply some seed money for projects of this kind, so that businessmen and trade union leaders and government officials could sit down and diagnose the problems of our cities.

So many of our cities are decaying. I think solutions will have to be found on the local level. The good will and energy of millions of Americans can be mobilized for that purpose. I think that would do a great deal more than the Federal programs manufactured in this city.

Also, we need a coherent anti-inflation program. It has to start with a policy of budgetary restraint and a moderate monetary policy, but it has to go further. I have talked over the years about the need to be fair to our young people. We have a Federal minimum wage which is pricing hundreds of thousands of our young people out of the labor market. I think we need to revise the Federal minimum wage law.

I think that the Davis-Bacon Act is restraining construction over the country. That act should be suspended or repealed.

I have already mentioned the need for a national productivity center. I have already mentioned the need for stimulating investment and thereby revitalizing productivity, which has been lagging in our country.

We need to reform our building codes and regulations across the country. We need to modify our environmental standards. We need to remove remaining restrictions on agricultural production. We need to liberalize tariffs. We need to relax and, to a degree, remove various regulations that impede progress in our transportation industries. We need to establish national bargaining committees in the construction trades.

These are some of the elements of an anti-inflation policy that ought to be articulated, developed, and put before the country. If that is done, I think a new spirit may arise in our America.

Senator JAVITS. Well, I think it is terribly inspiring to hear you say this and very, very important to our country.

Mr. Vice Chairman, my time is up.

Senator HUMPHREY. You were entitled to a little more time, if you wish.

Senator JAVITS. I just have one question that I would like to ask.

The $64 question, and you have certainly inventoried much better than I did the possibilities and the need for our country in terms of the spirit of its people, but the $64 question is: Where you gonna get the money?" as an old friend of mine used to say in the House of Representatives.

Now the question is, this is the big one, we budget so that if you tried to go into any one of these things you would increase the deficit.

Nonetheless, they represent capital improvement to the United States of enormous consequence. Any business concern will tell you not what it owes alone, but what it has and what it earns.

And yet under our budgeting, we have got a $70 billion deficit coming up this year, a good deal of which is this very kind of capital investment, albeit very inadequate, so my question is: Must we not couple with these ideas which may really free the American people and their energy, some other concept of how we are going to raise the money on the theory that we cannot expect to raise it out of current taxation, therefore, we cannot in justice signal the deficiency of current taxation which is all the deficit does; and shouldn't we, therefore, have to consider some kind of capital establishment?

Now I might point out, Mr. Burns, that we do exactly that in all kinds of Government guarantees of which we have tens of billions, and incidentally we have never really lost any money on them.

On the contrary, we have always made money. So we get around it by Government guarantee instead of by appropriation, and we feel that even for a capital expenditure for which we should be borrowing, we have an appropriation.

Now this is a riddle which in my judgment has tied the hands of Congress for decades in what it could or couldn't do respecting the country.

I would like to get your views on that.

Mr. BURNS. I think we have to watch our budgets. You understand that. You understand that fully. I think that regaining, rebuilding a state of confidence in our country is our most important need. I believe that we should not concentrate on the question, "Do we need a stimulative fiscal policy, and if so, what should its character be?"

If, instead, we ask the question "What do we need to do in order to rebuild, to strengthen the state of confidence in our country?" we will have a better starting point for constructive governmental action.

Spending money to assure our national security—spending money to regain independence in the energy area, I think would be well received by the American people. There is quite a contrast between that and spending money on public works.

I don't like to criticize the fiscal package that has been put together by the administration. I think the President went about that in a conscientious manner; he consulted many, he sought to achieve a moderate program, he sought to achieve balance. I think there is much to recommend the package. But as far as the so-called tax rebate, let's be sure it puts money into the pockets of the people immediately, as Senator Humphrey has pointed out. But I have not found one businessman who would be willing to spend an additional dollar on new plant or equipment just because retail trade will spurt for a period of 4 or 6 or possibly 8 weeks.

No, that doesn't build confidence, whatever its merits otherwise may be. The program that would appeal to me most, I think, is one of mobilizing the energies of our people on a volunteer basis which I think can be done. I think President Carter, because of his great sincerity and the love that he has generated across the country, could achieve success in this area. People are waiting to find a purpose, and revitalizing our cities, helping disadvantaged youths by educating and providing jobs for them, getting rid of our slums—these are things that people can do on their own in very large part.

As to your concept, Senator, of a national productivity center with local productivity councils seeking to improve productivity, seeking to create new jobs, seeking to remove the difficulties that are causing industry to move out of this city or that city—I think the President could initiate a program like that without great cost to the budget and possibly with substantial savings to the budget. Such a program would not only help to rebuild confidence across the country, but would also enable people to lead happier, more useful lives.

I think people in our country are starving for a purpose, they are so frustrated. I think the President could mobilize their latent energy. I very much hope he will do so, and I think you can help him, Senator.

Senator JAVITS. I am going to do my best, and I feel deeply gratified that you feel as you do.

Thank you.

Senator HUMPHREY. Senator Proxmire.

Senator PROXMIRE. To follow up on your response to Senator Javits. I was in Milwaukee last Friday. Milwaukee has had a system since the WPA days of requiring everybody on general relief to work or get off relief, general relief. They have ADC, of course, and others.

Now, I had an opportunity to meet with 20 people who were in this position, they were equally divided between blacks and whites, men and women.

They were told this is what they had to do:

They would work 32 hours a week at $2 an hour, they would provide their own transportation, they would provide their own clothes for work, they would get a little bit better break than they got on welfare, because they would be earning a little more, not much, a few dollars more per month.

Now, as I say, Milwaukee has done this for a long time. It is good. People were grumbling about the fact that they also had withheld from that $64 a week income tax and Social Security. Nevertheless, they wanted to work. They didn't want to lie around.

I was very impressed by this because it was the people who were in hard and difficult times.

I think what you propose is the kind of thing that Milwaukee is doing, and that we could perhaps provide throughout the country. But it doesn't solve the fundamental problem. It doesn't permit us to recover economically.

As I say, these people have a little more, they are going to contribute to a better Milwaukee, sweeping the streets and straightening up the parks and assisting in the hospitals and other public buildings.

But it is not the kind of economic stimulus that will really permit us to advance as we should. People will be happier, it is a better set-up, and I agree wholeheartedly, but I don't think it is a satisfactory economic answer. What is your response to that?

Mr. Burns. I think it is an important part of an economic answer. For people who are not working at the present time, finding some work—and not the jobs that they would prefer, to be sure, but some kind of employment—is a part of the answer.

As for the rest, I think that our private enterprise system is enormously capable of generating jobs——

Senator Proxmire. Hasn't done it, though. We have 7.3 percent unemployment, almost 2 full years into the recovery.

Mr. Burns. We had a substantial expansion of jobs last year. I think we could have a larger expansion in the future, once we have had a sufficient return of confidence.

Senator Proxmire. Now, let me follow up on an entirely different issue. I want to get back to monetary policy, which is your responsibility, and where you have the authority.

Can you provide a little more detail on how you would accommodate the tax rebate? To what extent? How much may the money supply, for instance, be increased at an annual rate in the second quarter?

Mr. Burns. Let me tell you how we went about this task in 1975 when we had a similar problem, and what our plans are at the present time.

Our staff made estimates of the increase in money supply that would occur as a result of the 1975 tax rebate. The estimates indicated a sharp increase in the money supply for a month or two, and then a progressive diminution. These estimates served as a basis for Federal Reserve monetary policy at that time.

We found in May and June of 1975 that the money supply was increasing a good deal more than our estimates had suggested. We inferred that something was happening in the economy—in the way of an increased demand for money—in addition to the flow of checks from the Treasury to people across the land. And, therefore, to indicate to our Nation that the Federal Reserve was alert and doing its job, and that we would not release a new wave of inflation through the monetary side, we pulled back just a little.

This time we have a better basis for making estimates than we had in 1975, because we have that experience to draw upon. Also, the estimates that we will make now will not be single point estimates. We will make a range of estimates, recognizing the error that may occur in the estimating procedure. After all, neither we nor anyone else knows precisely how much of the so-called rebate will be spent by the people, how much will be saved, or how fast spending will occur. We will go through exactly the same procedure that we did last time, but we expect to have better estimates and to govern our policy over this difficult period a little better than we did in 1975.

Senator PROXMIRE. Let me ask, the Carter forecast for the budget is for a 5.4 percent increase in real growth, and a 5.6 percent inflation.

That would mean about 11 percent in terms of dollar growth.

The M–2 target is 7 to 10 percent. Would that accommodate that 11-percent demand for additional money? That is the M–2 target.

The M–1, of course, is substantially less, about 5 percent.

Mr. BURNS. Our judgment is that it will fully accommodate an increase in the dollar value of our gross national product such as you have suggested.

Senator PROXMIRE. Then you make an assumption, of course, as far as velocity is concerned, to the extreme based on the experience being this far into the recovery?

Mr. BURNS. No; I don't think we are making an extreme assumption. Our financial system has been undergoing very rapid changes which have served to augment the turnover of money in the narrowly defined sense. If you take account of those changes in financial technology, I don't think our assumptions are at all extreme.

I think that the Nation is awash with liquidity at the present time. Our monetary policy as we have projected it will allow for substantial increase in the money supply. It does assume a moderately high turnover of money, but I think experience justifies that assumption. If we should find that we made a mistake—well, I assure you we don't live very long with our mistakes.

Senator PROXMIRE. Let me ask, how does the Federal Reserve coordinate its monetary policy with the administration? You have several proteges now in the administration—Mr. Gramley and Mr. Brill.

Is the Quadriad an active group in policy formulation now? Do you meet regularly?

Mr. BURNS. As you know, the new administration is getting its bearings. I have met with the Secretary of the Treasury on a regular basis once a week, and I have seen him at other times during the week. He and I have met with the members of the new Council of Economic Advisers. I have had one or two meetings with the Director of the Budget.

The new economic policy group is still getting its bearings. The chances are that I will be meeting with them with some frequency, but as yet I have not done so.

Senator PROXMIRE. Now, I am very concerned, as you know, about housing and I am extremely disappointed in the fact that the administration doesn't include—not only doesn't include it in their economic stimulus package, but doesn't include it in a significant housing program in my view in their 1978 budget.

Mr. Burns, housing, as you know, is particularly sensitive to monetary policy. Every credit crunch, housing is the number one victim. We have had a very poor performance over the past 3 years. The last 4 months of 1976, the housing starts were somewhat better, but they dropped again in January. And those housing starts in 1976, as you know, were confined to expensive houses primarily in scattered areas of the country.

You talked about favorable mortgage rates in your presentation. I don't see that. The last figure I have for January is 9.05 percent for mortgages, and that is about as high as it's been in history except for 3 or 4 months in 1976.

It is a very, very high rate and it is a discouraging rate and it makes it extremely hard for the average family to buy a home when they have to pay 9-percent interest on it.

It makes monthly payments so high that they priced 70 to 75 percent of the American families out of the market.

And housing is just a marvelous way to stimulate the economy, as you know. Very high unemployment in construction trades, we need the houses very badly. The industries that feed housing are operating far below capacity.

Why wouldn't it be desirable—I realize it would have great impact on you and maybe cause some difficulty for your operation—but why wouldn't it be desirable to have a vigorous program in the Federal Government of providing money at 7 or 7½ percent, if it would be permitted, if it were implemented as the administration would like, which I think it should, instead of 9 percent? That would provide for hundreds of thousands of housing starts and provide for millions of jobs.

What would be wrong with that approach?

Mr. BURNS. First, a very minor technical point: I think that the typical mortgage interest rate is more nearly 8¾ percent. The most representative figure is 8.7 percent. I think that is a better estimate of the average interest rate on mortgages than the figure that you cited.

Senator PROXMIRE. Well, mine are from the economic indicators, new mortgage yields, Federal Home Loan Bank Board. That is the latest figure.

Mr. BURNS. The series on mortgage interest rates that I find most dependable is the weekly series that covers about 120 savings and loan associations.

Senator PROXMIRE. At any rate, the interest rate is extremely high. You would agree with me on that?

Mr. BURNS. Yes, the interest rate is extremely high, if you consider interest rates without recognizing the inflation premium that is built into them. With a 5- to 6-percent rate of inflation, a mortgage interest rate of 8¾ percent is really not high, but it is still uncomfortable for millions of our families. You are quite right in your basic point—namely, that millions of our people are being priced out of the housing market.

A permanent solution to that problem, I think, is to be found not by adopting this or that governmental program, but by getting the rate of inflation down and eventually eliminating it.

But now let me turn to your question, why not embark on a large new housing program?

I think we have to watch our step. Homebuilding has revived very significantly. As far as single-family housing starts are concerned, at the present time we are approaching the peak level of 1972. We certainly want to avoid overbuilding in that industry. We may get another major boom in homebuilding and then have a depression in that industry a year or two or three down the road. You don't want that any more than the rest of us do.

At the same time, I have a great deal of sympathy with a housing program such as the GNMA tandem plan. Some expansion of that program would enable low- and moderate-income families to acquire a new home. I think I could readily support some modest expansion in that.

Senator PROXMIRE. My time is up, but let me say that we very carefully calculated what our housing goals should be for the 10-year period beginning in 1968. We calculated for 26 million housing starts, 2.6 million a year. The last 3 years have been disastrous. We are far below what we should be. We have a tremendous backlog to catch up with.

As I pointed out, our annual housing starts in January are only 1.3, half of the housing goal.

In our view, will interest rates in 1977 be conducive to recovery in the housing industry?

Mr. BURNS. I don't think I ought to be forecasting interest rates, Senator.

Senator PROXMIRE. Well, my time is up, but I think that the fact——

Senator HUMPHREY. I yield some more time to you, if you can get an answer out of him. [Laughter.]

Senator PROXMIRE. You pointed out how interest rates have been low, although they have been increasing somewhat for Treasury bills and for other Government obligations and indeed for most business loans.

They have fallen in 1975, 1976, and by and large they have been modest compared to what they were, but not the mortgage interest rate. The interest rates that apply to housing did not respond.

If your contention about the inflation premium is right, why it is that business loans have fallen, and long-term rates for Government bonds have gone down and for municipals, but not housing?

Housing interest rates have stayed up.

Mr. BURNS. First, a fact: mortgage interest rates have come down. The weekly series I referred to earlier—which I think is the most dependable one—showed an average interest rate on mortgages of a little over 10 percent in October of 1974, and it shows a rate of 8.7 percent presently.

So mortgage interest rates have come down. They have not come down nearly as much as market interest rates. The question is, why not?

I think one major reason is that the demand for mortgages has been enormous, not only because home building has been rising, but also because many people have refinanced their mortgages. Mortgage lending has been at a record rate.

Senator PROXMIRE. Well, you can't see that in the figure on starts, but you may be correct on refinancing used homes, sales, turnover, but that just indicates there is not enough money around, there are just not funds available. Money supply isn't available, and that's your shop.

Mr. BURNS. I don't think you can justify that statement. The mortgage commitments made by savings and loan associations are now at a record level. The inflow of funds to our savings and loan associations has been enormous. All you have to do is talk to any savings and loan association.

Senator PROXMIRE. But we are not getting the results. My time is up.

Senator HUMPHREY. Mr. Burns, we have discussed today the impact of the weather on the overall economic picture, and in January in testimony before the House Banking Committee you expressed reservations about the need for the administration's fiscal stimulus package which you have expressed again today.

But as has been noted, since that time the Nation has been through a time of extremely severe weather. I asked the Library of Congress to prepare through its Congressional Research Service an estimate of how much consumer demand would be channeled into higher heating bills. Assuming the severity of the cold weather continued throughout the winter.

Again there is always some problem about that. We are having some changes right now. But assuming that the severity would continue, the Congressional Research calculated that consumers would spend $8 billion more this winter than they did last winter to heat their homes.

I thought that was a rather high figure myself, but that was the top figure that they gave. I believe they gave us a range between $5 and $8 billion.

At the same time I asked Mr. Schultze, Chairman of the Council of Economic Advisers, to provide this committee with his best judgment or the CEA's best judgment of the impact of the weather on the American economy.

Chairman Schultze responded to my request yesterday, and according to the CEA estimates, the cold weather will cost consumer expenditures to rise between $2 and $5 billion, as Senator Proxmire alluded to earlier.

It is my understanding from your comment today, Mr. Burns, that the severity of the weather and the impact on the economy, whatever that figure might turn out to be, is not sufficient to change your views on the economic stimulus package; is that correct?

Mr. BURNS. That's correct, yes.

Senator HUMPHREY. Well, I will place in the record then, if someone will handle this, the report of the CEA.

[The report referred to follows:]

ASSESSMENT OF THE PROBABLE EFFECTS OF THE COLD WEATHER ON THE PERFORMANCE OF THE ECONOMY IN 1977

SUMMARY

Assessment of the economic effects of the cold winter weather and of natural gas shortages is fraught with hazard. Weather prospects for the remainder of the winter are uncertain; data on plant shutdowns and curtailments of construction and other forms of economic activity during the first quarter are fragmentary; and the effects of the cold weather on business and consumer confidence remain problematical.

Based on such information as we have been able to glean, our tentative conclusions are these:

1. Production curtailments because of natural gas shortages and cold weather will have a significant, but largely temporary, depressing effect on total real output of goods and services in the first quarter of this year. Real output will still rise appreciably, but the level for the quarter may be from ½ percent to 1 percent below earlier expectations. These production losses will be largely made up by the fourth quarter of 1977.

2. Because of additional consumer expenditures for fuels, and to a lesser extent because of higher food prices, consumer expenditures for other goods and services will rise slightly less during 1977 than had been anticipated. The magnitude will be quite small if normal weather prevails for the rest of the heating season and somewhat larger if abnormally cold weather returns.

3. Prices will increase somewhat faster in 1977 because of the cold weather. Increases in demands for fuels will lead to an increase in oil imports and hence to a rise in the average price of a barrel of oil, and to some increase in prices of gasoline and heating fuels. Emergency sales of natural gas may lead to a small rise in natural gas prices. Because of crop damage in Florida, fresh fruit and vegetable prices will be sharply higher through the remainder of the winter and early spring months. As a rough estimate, the annual rate of increase in consumer prices during the first half of this year may be about ¾ of one percent higher because of the cold weather than had been anticipated. The underlying rate of inflation, however, is unlikely to be affected by these developments, and remains in the range of 5 to 6 percent.

4. The dampening effect on the overall rate of economic expansion from these developments will be mild. If temperatures stay close to normal for the rest of the heating season, the real GNP by the fourth quarter of this year is not likely to be affected significantly. If abnormal cold returns for a lengthy period, the fourth quarter effect could be observable, but still modest—perhaps reducing real GNP in that quarter by about 0.2 percent below earlier projections.

This assessment makes no allowance for possible ice jams and floods related to the cold weather that may develop this spring, or for continuing shutdowns of industrial plants—to restore inventories of natural gas—on a significant scale after April. Also, the estimated effect on consumer prices makes no allowance for developments unrelated to the cold weather. There are substantial uncertainties at the present time with regard to the effects on agricultural production and food prices of water shortage in the West and the potential for drought in the grain belt.

WEATHER ASSUMPTIONS

Estimates of the effects of cold weather on usage of fuels depend on the extent of subnormal temperatures, the time period over which subnormal temperatures persist, and the size of the population. Weather severity for this purpose is conventionally measured as the number of degree days (weighted by population) relative to earlier periods. As of the end of January 1977, the population-weighted number of degree days was 38 percent above the winter of 1975–1976 and 22 percent above the average of the last 30 years.

For purposes of this assessment, two assumptions have been made about the weather for the remainder of the heating season:

(1) A return of temperature and fuel consumption to normal about mid-February. Under this optimistic assumption, degree days for the entire winter would be about 14 percent above normal and 28 percent above last year.

(2) A continuation over the remainder of the heating season of cold weather as severe, relative to normal, as the period through the end of January. Under this *pessimistic assumption*, degree days for the entire winter would be 23 percent above normal and 38 percent above last year.

PRODUCTION ADJUSTMENTS IN THE FIRST QUARTER

As yet, there are relatively few hard facts about the effects of the cold weather on production and employment in the first quarter. Residential construction is being curtailed, as is industrial production. In January, new housing starts fell sharply—particularly in the North Central and North Eastern States—and industrial output declined an estimated one percent. However, a large number of the industrial plants that were shut down in the latter half of January and early February by shortages of natural gas, cold weather, or heavy snow have already reopened, and activity on many construction sites has probably resumed also.

Since the middle of January, the U.S. Departments of Labor and Commerce have made efforts to develop as much information as possible on the extent to which fuel shortages or cold weather have curtailed employment. These estimates are subject to an extremely high degree of uncertainty, but they are the best available. It appears that workers off the job for reasons related to weather rose to a peak level in the neighborhood of 1¼ to 1¾ million during the first week of February. Since then, the number has declined steadily to around ½ million by the middle of February.

Based on our optimistic weather assumptions and these estimates of employment losses to date, we believe that manhours lost due to plant shutdowns and curtailment of construction activity during the first quarter might total about 0.3 to 0.4 percent of total manhours worked. If the pessimistic weather assumption proves correct, the proportion of aggregate manhours lost due to the weather might run as high as 0.6 to 0.8 percent.

In translating these figures into estimates of lost production, we have made allowance for the possibility that widespread plant shutdowns may affect productivity adversely. Accordingly, our estimates of weather-related output losses during the first quarter range from ½ percent to 1 percent.

Offsetting these losses of output in manufacturing and construction in weather-affected areas will be increases in consumer expenditures for fuels that will probably not be offset fully by reduced consumer expenditures for other goods and services or by reductions in fuel inventories. As a rough estimate, the addition to measured real GNP from this source during the first quarter will range from 0.1 to 0.2 percent.

The net reduction in real GNP during the first quarter due to weather-related phenomena would thus be in the range of 0.4 to 0.8 percent.

CONSUMER EXPENDITURES ON FUEL

Consumer expenditures on fuel will be substantially larger this winter than last. Prices of energy items in the consumer price index have been rising rapidly since May 1976; the quantity of fuel purchased will be much higher this winter because of the cold weather, and this larger quantity purchased will itself tend to exert some upward pressure on fuel prices.

To obtain estimates of the effects of cold weather on the consumer fuel bill, it is important not to include the increase in expenditures over last year that is attributable to the general rise of energy prices since last year. That had already been allowed for in our earlier projections of economic activity during 1977. What is needed is an estimate of the additional expenditures for fuel associated entirely with the cold weather.

Based on statistical studies of past relationships between temperature and fuel usage, the cold weather is expected to lead to residential fuel bills that are $2 to $5 billion higher for the entire winter of 1976–77 than had been anticipated—toward the lower end of the range if our optimistic weather assumption obtains; toward the upper end of the range if the pessimistic assumption proves to be correct.

AGRICULTURAL PRODUCTION

The Florida freeze destroyed a large portion of Florida tomatoes and other cold-sensitive vegetables, and damaged a substantial part of the Florida citrus fruits. It is estimated that the loss of vegetables will be approximately $100 million, and of citrus fruits between $50 mililon and $100 million, at last year's prices.

The impact of these losses will show up in higher consumer prices for fresh fruits and vegetables for the remaining winter and early spring months. The particular vegetables lost in the Florida freeze have a relatively high weight in the consumer price index, and that weight will rise as a consequence of higher prices. We estimate that the annual rate of increase of the total CPI may be boosted by ½ of one percent during the first half of 1977 due to price increases for fresh fruits and vegetables,

EFFECTS ON ECONOMIC PERFORMANCE OVER THE REMAINDER OF 1977

To assess the significance of the cold weather on longer-run economic performance, it seems desirable from a conceptual standpoint to distinguish carefully between the effects of plant shutdowns and work stoppages in the first quarter, and the effects of additional consumer expenditures for fuel because of the cold weather.

Additional purchases by consumers of fuels will tend to reduce consumer spending on other goods and services. To be sure, the funds going into additional fuel expenditures will not be entirely lost to the spending stream. Part of these added outlays will result in additional oil imports in 1977—and to higher receipts by oil-exporting nations. Eventually, some of the dollars going abroad will work their way back into the spending stream through larger demands for our exports. Another part of the added outlays for fuel will accrue to domestic producers and distributors of fuel, or to electric utilities, mainly in the form of higher profits, and this will eventually result in higher dividend payments or larger investments. But the return of these funds to the spending stream may occur mainly in 1978 or later years, rather than in 1977. As a result, the drain of consumer purchasing power stemming from higher fuel bills will tend to exert a dampening influence on the rate of economic expansion during the course of this year.[1]

This drain of purchasing power due to higher fuel bills is a once-for-all loss rather than a continuing drag on consumer real incomes. The adverse effect on economic growth is therefore unlikely to be either large or long lasting. The results of stimulations on an econometric model suggest that if additional consumer fuel expenditures for the heating season were to equal or somewhat exceed the upper limit of our estimate—$5 billion—real GNP by the fourth quarter of 1977 would be only about 0.1 to 0.2 percent below our earlier expectations.

Turning to the potential longer-run effects of the production loss in the first quarter, note first that the estimated magnitude of this loss is no larger than has sometimes occurred during a strike in a major industry. For example, a strike at a major auto manufacturing company in the fourth quarter of 1970 reduced auto output by more than one percent of real GNP—an amount greater than our estimate of the output loss in the first quarter of 1977.

Apart from responses of the economy to major strikes, there is little or no empirical evidence available to judge how the economy's longer-run performance might be affected by a development of this kind. It seems reasonable to expect, however, that both producers and consumers will recognize the transitory character of the work stoppages and will hold to their longer-range spending plans. Plants shut down in the first quarter will tend to work overtime later in the year, and the loss of wage and salaries during the first quarter will thereby be made up. Workers off the job in late January or early February will tend to maintain their consumption expenditures by digging into savings, and later build up their savings funds again.

A good part of the production loss—though probably not all of it—may be made up in the second quarter. We believe that virtually all of this loss will have been made up by the fourth quarter.

CONCLUDING REMARKS

Our overall judgment is that total real output of goods and services in the last quarter of 1977 will only be slightly affected by the cold weather. This effect could range from near zero to about an 0.2 percent reduction, depending on whether not severe cold returns over the remainder of the winter. Even the maximum loss would be well within the range of normal forecast error.

It must be emphasized, however, that the economic outlook for 1977 has become considerably more uncertain because of adverse weather. As noted earlier, we have made no allowance in our assessment for several possibilities that may eventuate—such as floods this spring, continuing work stoppages to restore inventories of natural gas, or draught in the Mid-West and the West. Nor can we take into account such imponderables as the effect of the weather on consumer and business confidence. Thus, while our point estimates of output and employment in the fourth quarter of 1977 remain essentially unchanged, there is now a larger band of uncertainty surrounding them.

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[1] A similar argument could be made about additional consumer expenditures for food because of rising food prices. The resulting enlargement of farm income—at the expense of real incomes of wage and salary workers—might result in some reduction in aggregate demand because farmers may spend less of their additional income on goods and services this year than wage and salary workers would have. The return of funds to the spending stream in this case, however, is likely to be much larger and more prompt than is the case with additional consumer fuel expenditures, and the magnitudes, in any event, are much smaller.

Senator HUMPHREY. Now, I want to get to a matter of the money supply, because we had testimony here by Mr. Modigliani of MIT, Massachusetts Institute of Technology, he found projected rates of monetary growth too low to accommodate any expected real growth, and probable increases in the level of prices. He went into this at some length.

In the past you have been willing to lower the limits of monetary growth or M–1 in part to reflect the technical innovations of regulatory changes that allow corporations to hold more of their funds in savings rather than checking accounts.

Now the question is, Mr. Burns, Is the current target range for M–1 growth adequate to meet the economy, the needs of the economy? And can you assure us that the Federal Reserve Board will be as flexible in increasing its target ranges in the light of changed circumstances?

Mr. BURNS. I can assure you that the Federal Reserve will continue to monitor economic and financial developments with the greatest of care and that our thinking about monetary targets is by no means frozen. But I must add the comment that we will proceed very prudently.

Senator HUMPHREY. Very what?

Mr. BURNS. Very prudently.

Senator HUMPHREY. Yes.

Mr. BURNS. We have lowered our targets for M–1; you are quite right about that. But we have been doing it, I must add, at a snail's pace. If we continued on that course, it would take us perhaps 10 years to arrive at monetary targets which would be consistent with general price stability; and that's too slow a pace.

In my judgment, if the Federal Reserve has erred at all in the past 2 years, it's been on the side of excessive liberality.

Senator HUMPHREY. Let me continue with another question in this area, just to expand it in our record as to your views.

I think it is well recognized that limiting the growth in the money supply can be relatively effective in situations where domestic demand is simply too high. This is rather standard observation. But it is apt to cause economic harm if it is used to deal with rising prices caused by foreign cartels or natural disasters. The unusual weather in early 1977 threatens to seriously reduce harvests, as you have indicated today, in the South, Midwest, and Far West. This will have an impact on food prices; also, the serious weather problem in the citrus areas and vegetable areas is going to have an impact on food prices.

Now, if the Federal Reserve reacts to higher wholesale prices by slowing the rate of growth of the money supply, isn't it fair to say that the entire economy could suffer?

Therefore, my questions are:

Has the Federal Reserve Board predicted the magnitude of the future increases in food and fuel prices? And how will the Federal Reserve Board react to those higher prices?

Mr. BURNS. Our staff has made projections of those prices. My general answer to your second question is that the question implies an ability on the part of the Federal Reserve to engage in a degree of fine tuning that we simply are incapable of carrying out.

Senator HUMPHREY. But in this instance, Mr. Burns, at this stage in this latter part of the month of February, it is pretty well understood that there will be increased costs because of fuel and because of projected harvests. I think almost everyone recognizes that. I mean the future market, the raw materials, grains, soybeans, wheat, pork products, beef, et cetera.

It all indicates price rices in the food area. There is nothing to indicate that fuel prices are going to come down. You yourself have indicated that they will most likely go up. I think Senator Proxmire has given us some statistical evidence here today that that increase will be rather sharp.

So my point is the Federal Reserve must undoubtedly take these factors into consideration as you look at monetary policy. I just wondered whether the Federal Reserve Board will react, how it will react, and will it react to these higher prices?

Mr. BURNS. Let me tell you what I know, or what I think I know.

As far as the freeze in Florida is concerned, the judgment of our experts is that the prices of some vegetables—green beans and tomatoes—will go up for 1 month or 6 weeks. The effect will be no more lasting than that.

As far as the drought in the West is concerned, the effects could be much more serious, but we will not have any firm knowledge about them until early May. If and when and as the effects occur, I assure you that we will examine the facts as we then know them.

We don't respond to every little wiggle in prices or in our exepectations of prices, if only because our control over the money supply over a very short period is so imperfect.

Let me remind you of this, Senator; it is a thought worth contemplating. We had a mild winter last year and 2 years ago. I don't recall anyone at that time suggesting that Federal Reserve policy should be tightened just because we had a mild winter or that taxes should be raised just because fuel bills were a little lower and people therefore had more money at their disposal.

Now we have become much more sensitive to evey item of adversity and are in danger of overdoing things.

Let me say this to you: Whatever benefits may result from the new fiscal package, there is at least the possibility—the very distinct possibility—that, together with the weather, that package may induce an inventory cycle in our economy; later in the year we may be talking about a pause or a lull in the economy that might have been induced in part by governmental policy itself.

When we consider manipulating the economy over the short run let's not be too sure that we know precisely what we are doing.

What is important is stable policy, and that is what we at the Federal Reserve try to achieve. I hope you will not ask us to try to respond to every little wiggle—first, because we don't know how to do it; and second, even if we had the knowledge, I doubt that that would be wise or sound policy.

Senator HUMPHREY. I think what we are really asking for is what you have indicated; namely, prudent flexibility. We have never really tried to bring pressure to bear on the Board, at least I haven't during the times when——

Mr. BURNS. You certainly——

Senator HUMPHREY. When prices were down and fuel costs and the weather was moderate because the Board by its nature is somewhat conservative in terms of money supply. There wasn't any need of any coaching on my part. But——

Mr. BURNS. I think you have been wonderful over the years, Senator. I think that the Board is simply carrying out the policy that the Congress laid down. Congress gave the Federal Reserve a measure of independence because it wanted to remove us as far as seemed reasonable from day-to-day political pressures. And you have respected that throughout your career, to the best of my knowledge.

Senator HUMPHREY. To a reasonable degree, I have, yes.

I wouldn't want the record to indicate that I am beyond trying to bring sufficient pressure to bear on what I think needs to be done.

Senator PROXMIRE. If the Senator would yield, that is our function, is it not?

Senator HUMPHREY. That is our function.

Senator PROXMIRE. You are a creature of the Congress, Mr. Burns, and you are supposed to do what the Congress decides you are to do. isn't that right? Isn't that your understanding of it?

Mr. BURNS. When Congress passes legislation, you can be quite sure we will live by the laws enacted by the Congress.

Senator PROXMIRE. That is right.

Senator HUMPHREY. But up to now you have been extraordinarily competent with the Congress to see that it didn't get out hand as you would say.

Now, I have this question, and I think this will complete my questioning.

In recent years we have seen a disturbing pattern of the behavior where banks have made risky loans and wound up in trouble because of it. You have testified here on this, how the Federal Reserve Board has as one of its first responsibilities, to move in and try to stabilize the banking structure.

Recent experience with the real estate investment trust REIT's is the classic example. Now, it appears that a similar situation may be developing with loans that commercial banks have made to less developed countries. I have been concerned about this for some time.

A recent article in the Morgan Guaranty Trust Co.'s world financial markets, outlines the huge buildup in external debt experienced by oil-poor LDC's as a result of rapid oil price increases to the less developed countries. According to this report, U.S. commercial banks hold approximately $50 billion of that debt and I might add that most of these countries to which this indebtedness applies are on the verge of insolvency. I don't know how in the world they make these loans, but they make them. I mean we have people out in my State that are much better credit risks, the city of Minneapolis is a much better credit risk for what it needs than some of these less developed countries, but the banks have been loaning money like it is going out of style.

$50 billion worth of loans are sitting out there and we get worried about a stimulus package here of about $13 to $15 billion this year or $30 over 2 years in the American economy where you have got a highly integrated economic establishment.

We have got $50 billion out there on loans to the less developed countries.

At a recent meeting attended by one of our staff members, a former employee of the Ford administration, in the financial circles, noted that two of the New York big five banks were currently on the Fed's watch list because of this situation.

What can you tell us about this situation? We don't read much about this in the press. I keep reading about inflation, inflation, inflation, and here are two of the big banks in which the American people have put their money that are off here playing games with these loans to pay for high fuel costs to countries that have a lousy credit rating.

Mr. BURNS. All I can say to you, Senator, is that I share your concern, and that I have communicated my concern to the leading bankers of the country.

Senator HUMPHREY. Have you communicated it in the kind of persuasive language that you use with this committee?

Mr. BURNS. I have even communicated it in strident tones, Senator.

Senator HUMPHREY. Well, thank you, that is very reassuring. I know that I was a bit facetious in some of my comments here, possibly a little overdramatic, but I want to be very sincere with you about this. I do think there is only so much credit, it is like a well out of which you draw water and if you are going to take $50 billion out to pay for loans for high fuel costs in the less developed countries which they need, there isn't any doubt about it, they need it, but the farmers in western Minnesota need it a whole lot more. They have had 3 years of no crops, absolutely been down the tube. And my local bankers out there tell me that they are in dire straits, they have loaned their money, they are demanding young farmers pay up and there is going to be mass liquidation of real estate and of farm animals because we cannot pay.

The drought is not new in our State. Three years of severe drought we have had. Now here are the two big banks loaning $50 billion to people we have never met, never will see, and my folks out home that I get to see at least once a month and most of them, a lot of them, are out in the hallway waiting to meet me today, they can't get a dime. They are told there are limits on how much money is available, and the Government has a budget problem, and the banks have got to be careful about loans and so on, and so on.

Gobbledy, gobbledy, gobbledy, and he doesn't get a loan. That is off somewhere I haven't been and possibly you have been there. I don't know. But I just hope you will be there to tell them, I hope you crack down on them and tell those banks you are not going to bail them out.

We had the Franklin National situation, and we had these boys playing with REIT's and they are playing with other people's money. The banker never plays with his money. He plays around with other people's money. He has a fiduciary responsibility and I just think it is time for the Government of the United States through its central bank to blow the whistle and say, "Look, Buddy, why don't you borrow that money from the Arabs? They got the price up."

Mr. BURNS. The shortest answer I can give you is, "Amen."

Senator HUMPHREY. Thank you.

And that's a good way to end this service.

Do you have any questions?

Senator PROXMIRE. I would just like——

Senator HUMPHREY. Would you like a hallelujah chorus? [Laughter.]

Senator PROXMIRE. I want to follow up on Senator Humphrey's questions, but I want to say, Mr. Burns, the reason that Congress has become so sensitive to adverse developments is that we are not recovering satisfactorily from the recession.

Up to now, the problem has been complacency, not overreaction. I don't think anybody can say that we have recovered too rapidly so far, that we have gotten unemployment down too fast.

In fact, it has been the reverse.

That is, I think, why Senator Humphrey and I are so concerned that we don't seem to be moving with enough vigor, enough force.

Let me follow up on Senator Humphrey's questions.

This is a little different, because I am talking about all foreign lending by U.S. banks not simply lending to LDC's. Last week the Commerce Department released a figure showing a record increase of $20.6 billion in foreign lending by U.S. banks. That report comes on top of estimates that about one-fifth of all claims of U.S. banks and their branches are to oversea borrowers.

I understand that is about $250 billion.

Now I wonder what are the implications, of lending abroad, for the domestic recovery? Do you feel that this kind of lending abroad could result in perhaps a more rapid rise in interest rates than if we recover as vigorously as we all hope we will?

Mr. BURNS. I don't think that lending abroad by our banks will continue at any thing like the extremely rapid rate of the past 2 years. I do think certain facts ought to be recognized in this connection. One is that loss experience on foreign loans thus far has been extraordinarily good. In fact, loss experience has been better on foreign loans than on domestic loans. However, this is an unfinished story and that, I think, was the burden of Senator Humphrey's remarks.

The second point I would make is that it is to our own interest to have an international economy that functions reasonably well, and that this lending, whatever dangers may be connected with it, has helped to maintain activity in foreign economies and therefore has played a certain supportive role not only for our economy but for the international economy.

Senator PROXMIRE. I wouldn't argue with that.

Senator HUMPHREY. Yes, I want to join you in that. I think that is great.

Senator PROXMIRE. Morgan Guaranty, Bankers Trust, and Chemical Bank had all subscribed to a loan to Sweden and a loan to Britain aggregating about $2½ billion and the argument is that this was because it was their notion that loan demand was going to remain weak in this country and they, therefore, felt that they might as well make these loans abroad, they are fairly long-term commitments.

Mr. BURNS. I think that with domestic loan demand relatively weak—as it has been up until recently—our banks have gone abroad on a far larger scale than they otherwise would have. Loan demand has been increasing recently; it has taken quite a jump since last October.

Senator PROXMIRE. Let me ask you, in the longer term how does this internationalization of the U.S. banking system—and I think one-fifth of our loans abroad now suggest there has been a great internationalization—how does that affect the Fed's ability to manage the domestic monetary policy?

Mr. Burns. It is a complicating factor because there are no controls whatever on the enormous Eurocurrency markets that have developed across the world. These are entirely uncontrolled markets. Our ability to control the domestic money supply has not been diminished, but the international money supply that is being created has an impact here over which we have no control—neither we nor anyone else.

Senator Proxmire. There has been some talk about linking future lending to programs acceptable to the IMF. What do you think is the appropriate relationship between the International Monetary Fund and our commercial banks? What role should the U.S. Government play in these transactions including the Federal Reserve Board?

Mr. Burns. I have given a great deal of thought and attention to that problem. I believe that in the kind of world that has emerged—with floating currencies everywhere—we need to develop a rule of law in the international monetary area, and that the only instrumentality through which we can achieve that is the International Monetary Fund.

I believe that lending by governments—by ours or by other governments—to other countries around the world should be viewed very carefully in the light of what the International Monetary Fund is doing.

Let me indicate the problem that now exists.

A given country comes to the IMF for a loan. The IMF imposes conditions, as it should, to help that country reestablish its national finances. Now, conditions imposed by the IMF are often uncomfortable for a given country; its prestige, its pride, its domestic policy, will be injured, at least in the eyes of the government in power. Therefore, the country that is negotiating with the IMF may come to the United States or to Germany or to Japan and seek to circumvent IMF controls. Moreover the country may go to private bankers in an attempt to obtain loans from them and in that way circumvent the rule of law that only the IMF can impose.

Therefore, I lean strongly to the view that the IMF will have to play a much larger role in the conduct of international finances than it has been doing. First, individual governments should completely avoid circumventing the IMF by making loans. Second, I believe that the time may come and probably should come when at least some informal surveillance of private lending by the IMF will be the proper course. This is a subject that I will develop in the near future at some length, because I don't know of any more important subject in the international area.

Unless we have a rule of law in the realm of international monetary affairs, we will have chaos.

Senator Proxmire. Meanwhile, would it be wise to consider the possibility of legislation or some kind of action by the Government to provide the discipline for private banks? There is nothing to prevent them in a competitive world, with the bank, or course, seeking the best opportunity, of private bankers going out and ignoring any recommendation the IMF can make and they are free to do so under the circumstances. There is no discipline from your agency or from any other regulatory agency; isn't that correct?

Mr. BURNS. I think that is substantially correct, but I would proceed very cautiously. I believe that effective informal procedures can probably be worked out. If we fail in that, as we may, then I think we may have to turn to the subject of legislation. But it is not easy to see how legislation can cure the difficulties from which we seem to be suffering—and, to a degree, actually are suffering—without impeding international trade and international relationships. I would proceed cautiously in that area—for a time, anyhow.

Senator PROXMIRE. I assume you are going to address this subject when you appear before the Senate Banking Committee in a few weeks to tell us about the state of our banking system?

Mr. BURNS. I will have something to say on that subject on that occasion and on a somewhat later occasion as well, perhaps at greater length. When I appear before your committee, I will have to cover a very large number of subjects; I intend to devote a full-length talk to this international subject alone.

Senator HUMPHREY. Mr. Burns, I say that this recent testimony, or your comment on the international financial world, is very heartening. First of all, of course, you have recognized the complexity of it, and we all understand the interdependent world in which we live. We understand the competitive structures of financial institutions.

The Congress is organizing itself and has been arguing considerably over a considerable period of time as to how we should structure ourself to study foreign economic policy. There has been this argument in the Senate between the Banking Committee and the Foreign Relations Committee and I think it is fair to say that it somewhat resolved that both committees are giving a good deal of attention to the whole matter of foreign economic policy.

Foreign economic policy must, of course, include loans and credits both by governments and private institutions.

Mr. BURNS. You know, it is not part of my business to interfere with the organization of the Senate—that is the business of the Senate—but I must say I regret that as of today the Senate Banking Committee does not have authority to explore questions relating to the International Monetary Fund and other international financial institutions.

As far as I can judge, that committee, which is constantly working on banking and financial problems, is perhaps best qualified to deal with that subject. But Members of the Senate have considered the matter and in their wisdom have decided otherwise.

Senator HUMPHREY. The Foreign Relations Committee has a special subcommittee now on foreign economic policy.

It was a battle royal in the Rules Committee, there is no doubt about that. But I don't believe that the jurisdiction is that exclusive, Mr. Burns, and we have a way around here of doing what you mentioned a moment ago, being able to accommodate ourselves to the realities.

Senator PROXMIRE. We could have been accommodated a lot better by allowing us to win the fight though.

Senator HUMPHREY. I understand that, but we outpunched you.
Senator PROXMIRE. Yes.
Senator HUMPHREY. There are times when political cannons are as important as political wisdom and in this instance, Senator, I am sorry, old buddy.
Senator PROXMIRE. So am I.
Senator HUMPHREY. Do you have any more questions?
Senator PROXMIRE. No.
Senator HUMPHREY. Mr. Burns, we thank you very much. As usual you have been most helpful in this area.
Mr. BURNS. Thank you, Mr. Vice Chairman.
[Whereupon, at 12:27 p.m., the committee recessed, to reconvene at 9:30 a.m., Thursday, February 24, 1977.]

THE 1977 ECONOMIC REPORT OF THE PRESIDENT

THURSDAY, FEBRUARY 24, 1977

Congress of the United States,
Joint Economic Committee,
Washington, D.C.

The committee met, pursuant to recess, at 9:37 a.m., in room 345, Cannon House Office Building, Hon. Richard Bolling (chairman of the committee) presiding.

Present: Representatives Bolling, Hamilton, Pike, Brown of Ohio, and Rousselot; and Senators Humphrey and Bentsen.

Also present: John R. Stark, executive director; Louis C. Krauthoff II and Courtenay M. Slater, assistant directors; Richard F. Kaufman, general counsel; William R. Buechner, G. Thomas Cator, Kent H. Hughes, Sarah Jackson, John R. Karlik, L. Douglas Lee, and Katie MacArthur, professional staff members; Michael J. Runde, administrative assistant; and Stephen J. Entin, M. Catherine Miller, and Mark R. Policinski, minority professional staff members.

Opening Statement of Representative Bolling, Chairman

Representative Bolling. The committee will be in order.

As we continue the hearings on our annual report this morning, the Joint Economic Committee is especially pleased to have as its first witness Mr. Leon Keyserling. He has been for many years a good friend of this committee and a personal friend of mine.

Many of you here this morning will remember him as the Chairman of the Council of Economic Advisers under President Truman. Since then he has continued his keen interest in good government and good economics. Today he serves as President of the Conference on Economic Progress. Throughout his career, he has been a fighter for full employment. In the last few years, he has been in the front ranks of those staunch advocates of the Humphrey-Hawkins bill as a way out of our present unacceptable level of unemployment.

It is a great pleasure to have you here, and you may proceed as you wish.

STATEMENT OF LEON H. KEYSERLING, PRESIDENT, CONFERENCE ON ECONOMIC PROGRESS, AND FORMER CHAIRMAN, COUNCIL OF ECONOMIC ADVISERS

Mr. Keyserling. Mr. Chairman and members of the committee, I appreciate the kind remarks.

Mr. Chairman, I ask that my full statement be put into the record.

Representative Bolling. It will be done.

92-625—77——8

Mr. KEYSERLING. I have a short summary and would prefer to read it.

I submit that the President's first-year package and budget proposals consistent with it are seriously deficient in size and misdirected in detail.

Assuming adoption, I estimate that real GNP in calendar 1977 as a whole would be only 4 to 5 percent higher than in 1976 as a whole, or very far short of the about 6 percent needed for adequate inroads upon idle resources.

This puts unemployment at end of 1977 unacceptably above the 6 to 6.5 percent we should achieve—I think it should be 6; I think we won't do better than 7—toward the minimal acceptable goal of about 4 percent within 4 years, and lower later on.

I do not believe that the package would hold inflation for 1977 as a whole below 5.5 to 6 percent, which is not good enough, nor is the package the right start toward a balanced budget at full resource use. I hardly discuss the second-year package nor the parts of the 1978 budget consistent with it, as I believe that drastic reconsideration will result from conditions at the end of the first year.

Before discussing the President's proposals in more detail and offering alternatives, I shall deal with other matters far more fundamental.

The unfavorable current economic situation and unpromising outlook are essentially in a pattern of economic developments during 1953–76 which I first predicted in 1954; a roller-coaster performance of stagnations, recessions, and inadequate upturns, with more unemployment and other unused resources at the bottom of most recessions than at the bottom of the previous one, and more idle resources at the peak of most recoveries than at the peak of the previous one.

The five business cycles since 1953, really similar in causes and consequences, have borne this out. The most poignant examples are the most recent recession, the extremely deficient and deteriorating recovery for three quarters even before the weather freeze, and where we stand now, with responsible forecasts of another large recession in due course.

The roller-coaster performance during 1953–76 caused us to forfeit 4.4 trillion 1976 dollars worth of GNP, forego about 67 million man- and woman-years of useful employment, do without so much Federal deficits at existing tax rates as to run horrendous federal deficits even while starving some of our most vital domestic priority needs, and suffer chronically rising inflation.

This long and bitter experience should warn us that we cannot straighten ourselves out with disjointed and fragmentary short-range measures, which have officially been called a "shot" or quick-fix in the first year, and another in the second.

We have tried this several times before, along practically the same lines as proposed now, and it has not worked. We need now a drastically altered national economic policy and program, both comprehensive and coherent, and developed in a long-term perspective. I can best suggest how we should change our course by discussing the long-enduring errors which are still manifest in the President's program. Here they are:

First, due to assuming the trouble to be with excesses or shortfalls in total purchasing power, we have injected stimuli or restraint in the form of general fiscal and/or monetary policies. This is like somebody driving up to a filling station, and when the attendant asks whether the gas should be poured into the radiator, the oil into the tires, or the water into the gas tank, the driver replies, "What difference does it make; have you never heard of Lord Keynes?"

But the basic trouble has always been maladjustments in the structure, which is fundamental to economic analysis, regarding both income flows and resource allocation, which make high or even growing prosperity nonsustainable. Yet even today ignoring the precise nature of these maladjustments, the stimuli are not appropriately directed. There is no meaningful analysis underlying the direction of the stimuli.

Second, national policies have not paid sufficient attention to national values and priorities. Quite apart from the relative inefficiency and higher costs of tax reduction in stimulating jobs and production, the widely disbursed spending of tax concessions by most of our consumers will not buy the goods and services which they and the economy need nearly as much as those which would derive from well concentrated additions to public investment. These additional public outlays should not be mainly in the public sector, as I shall discuss further.

Third, technological trends have never been factored in property. Consumer spending of tax concessions will largely by goods produced in industries where productivity will advance so much in consequence of higher plant utilization that there will be only disappointingly small increases in employment. Far more can be added to employment, national wealth, and well-being by Federal outlays in the public sector and to help stimulate the private sectors, that is, housing, to enlarge production of some other types of more needed goods and human services, where in addition productivity growth is lower but real needs more urgent.

In other words, we are taking potshots, but we are not analyzing the real basic cause of what has been troubling us all along, or directing ourselves to a long-range program to correct it, and preventing the roller coaster from getting worse and worse.

Fourth, we have continuously placed excessive reliance upon a narrow range of conventional or stereotyped fiscal and monetary policies of a general nature, instead of using them in proper combination with other national economic policies, and supplementing them with microeconomic measures.

This reminds me of a violinist who holds a Stradivarius in one hand, which is no more marvelous in its capabilities than the American economy, but applies the bow which calls forth the performance on only one string, and the G string at that. This restricted approach calls for three illustrations. Now I am going to summarize further.

Three of our most difficult problems are the farm shortage problem, the energy shortage problem and the transportation problem.

Going back 15 or 20 years in each of these three areas, I warned we were running into long-range shortages in these areas, that they would become more acute, and in the case of the farm situation, they would drive millions of farmers and their families into the cities where they would go on relief rolls and cost the Government more in addition to being wasted human beings.

We otherwise wouldn't have the farm shortages that have not been caused primarily by crop failures, just as the energy shortage has not been caused primarily by what the Arabs did.

When I drew the farm, energy, and mass transportation problems to the Council of Economic Adviser's attention, they told me this was none of their business with respect to the Economic Report of the President, but rather the exclusive responsibilities of the Department of Agriculture, the utility commissions, and the ICC, but how could such vital matters as food, energy, and mass transport remain outside the ambit of overall national policies?

Then, the use of the Federal budget for many years and even today involves strange misconceptions. The central purpose of the Federal budget is neither to be balanced nor to stimulate the economy, although a well balanced budget could and should have desirable results.

The central purpose of the Federal budget as a national priority instrument is to allocate to the public sector those goods and services which the economy and the people need and which cannot be provided or provided so well in some other way. Thus, I hold that the spending side of the budget at almost all times should we set at that percentage of our total GNP capabilities at estimated full resource use which would represent the needed allocations to the national priorities which the budget should serve.

When we are far below full resource use, this policy would yield the additional benefit of helping to expand the economy; and whether we can afford this use of the budget depends upon the amount of our idle resources and not upon the condition of the budget itself at such time.

Moreover, that is the only policy which can balance the Federal budget in due course. On the other hand, if the pressures on the economy are so large that inflation results from strains in excess of our capabilities at full resouce use—which has never been the case in recent years—then restraining Federal outlays in a manner adverse to these great priority needs which the budget should serve sacrifices them first instead of imposing restraints upon activities of lesser or no lesser or no real utility, through appropriate tax policies. So, cutting out first what we need most and not touching what we need least has been and still is the case.

Tax policy should be used to impose stimulus or restraint, as the need may be at the time, by running a surplus or a deficit when a balanced budget is not appropriate. But for many years in the past, and the President's proposal is another good example, we appear first to decide how much we want to accomplish through tax reduction—toward objectives not even clearly stated in terms of specific goals or timetables—and then to decide what Federal spending policy will fit conveniently into the predetermined tax policy.

To repeat, this is entirely erroneous. This is completely upside down with respect to proper use of the Federal budget.

For a long time past and again under the President's proposals and the explanations related to them, we recognize the need for public investment in the great national priorities such as energy, resource development, mass transportation, urban relief and renewal, environmental improvement, housing, health and education, welfare reform, et cetera.

But it is then claimed that the package will stimulate the economy enough to provide a large enough fiscal dividend around 1980 to enable us to take care of now underserved priority purposes adequately through increased public outlays.

This puts the cart before the horse. The fiscal dividend cannot be achieved without balanced economic growth at an optimum rate for several years. And for reasons already stated, such growth is veritably impossible, unless we start now to blend into the structure those very priority programs which we now tend to postpone until the growth is first attained.

In other words, if you don't have the policies that will put together the kind of bricks that will build a house, and you won't be able to get the house, and you won't be able to put somebody in it.

Through belief in the trade off, we have for a very long time and still are bungling unspeakably the treatment of inflation. I cannot review here all of the empirical refutation of the tradeoff.

In brief, as I have noted repeatedly since 1954, there has emerged an unmistakable inverse correlation between the rate of real economic growth and levels of unemployment on the one hand, and the rate of inflation on the other.

The periods 1947–53, 1955–58, 1958–66, and 1966–69 are excellent examples. But the best examples came thereafter. Even though the combination of the highest inflation since the Civil War with the highest unemployment since the Great Depression was due in part to special factors such as Arab actions and crop failures, the underlying rate of inflation under conditions of low growth and high unemployment was unusually high, about 6 percent.

In other words, even if you x-out the effect of those special developments we had inflation 2½ times as high under conditions of high unemployment and low plant use as we had had under better conditions.

The very rapid recovery movement from fourth quarter 1975 to first quarter 1976 was marked by sharp reduction of inflation, and since then augmenting inflationary trends have marked the serious economic slowdown.

Some strange ratiocinations have been attempted to support the tradeoff theory. One is the time lag argument that wage and other costs built into the economy during high prosperity result in inflation when stagnation and recession come.

But costs which are desirable and supportable when the economy is growing will become hard to bear when growth wanes and productivity gains decline or vanish. The real inflation cause is therefore the economic slowdown, and the consequent productive slowdown.

My good friend, the current Chairman of CEA, has occasionally told us that the inflation would rise dangerously if unemployment were reduced to 5 or even 5.5 percent, unless we adopted price and wage controls, and that the earlier evidence was based upon a different kind of economy. But there is now little or no empirical evidence that acceleration of inflation starts when unemployment is reduced to 5–5.5 percent. And if that were the case, what are we ever going to do about intolerable levels of unemployment, since President Carter, and Mr. Schultze presumably, are now adamantly against the direct controls except in a great national emergency?

The tradeoff proponents then tell us that rampant inflation precedes and causes recessions; but empirically, this was not true before the Great Depression, or before most of the recessions since early 1953. Avoidance or modulation of the business cycle depends upon corrections in income flows and resource allocations, which require far more than willy-nilly attempts to restrain inflation per se.

In any event, the economic, social, and civil costs of the roller-coaster economic performances have been infinitely greater than any marginal differences in price behavior which might have resulted if there had been no such performance. And it is morally indefensible to impose the cruel burdens of unemployment upon millions of families on the alleged ground that this protects the employed and the affluent against inflation. The tradeoff theorists have not even analyzed whom unemployment hurts and whom it helps; it does not affect all equally.

Yet, Mr. Chairman, and members of the committee, the tradeoff theory remains the undisclosed premise for the inadequate stimulation program offered by the President.

My entire record demonstrates that I am not soft on inflation. At the end of the Truman administration, in which I served as Chairman of CEA, there was 2.9-percent unemployment and 0.8-percent inflation, and during 1947–53 the average was better on all scores including economic growth and the condition of the Federal budget, than at any subsequent time.

Whether I am right or not, I think I am, in the empirical observation that the first and foremost way to restrain inflation is to move toward reasonably full resource use as quickly as practical and then maintain it, by now it must be absolutely clear that damaging inflation occurs at times at all stages of the business cycle.

We should therefore make restraint of inflation through a range of nondirect control measures which we do not now have and restoration of a fully healthy economy, simultaneous goals with each reenforcing the other, instead of continuing the farrago of the tradeoff. The inadequate stimulus in the President's package is due largely to adherence to the tradeoff theory; no independent measures to restrain inflation are proposed.

Among measures to restrain inflation, I have long favored a voluntary national incomes policy. But guidelines or analogous measures designed only to restrain inflationary price and wage increases are shallow and ineffectual, and in the past have been excessively repressive on the wage front without doing much about prices. And the larger but neglected chronic problem, existing now, is to use voluntary price and wage criteria to bring about a sufficient expansion of consumer purchasing power to promote restoration of full resource use. Besides, all major income flows and resource allocations are basic determinants of the entire economic performance.

Thus, a mature national incomes policy must extend to national fiscal and monetary and other policies importantly affecting income flows and resource allocations, all developed in the perspective of an economic model and goals which I shall further describe. Without such a model and goals, all national policies are disjointed and flying blind.

Most of what I shall now state in detail about the President's proposals is implicit, or even explicit, in what I have already said. The "package" for the first year comes to less than 1 percent of the size of the economy, or a much smaller percentage than proved adequate when similar "shot" or "quick fix" approaches were tried.

As earlier stated, I am not discussing the second year package, or its implications for the Federal budget, except to say that economic conditions at the end of the first year "quick fix" would require drastic revision of the second.

Far more important, I do not subscribe to first or second year "shots" or "quick fixes."

We are not on the *Lusitania*, which sank in 5 minutes, or on the *Titanic*, which sank in 5 hours, because it was a British ship. [Laughter.]

The benefits claimed for the "quick-fixes" are excessive or illusionary, and we can do much better in every year by a longer-range and more systematic approach. The six-parts tax reduction and one-part direct job creation in the first year package is, in my judgment, a gross distortion.

The widely heralded tax reductions in 1964 gave the economy a shot in the arm for a short while. But for reasons which I then predicted, the real growth rate slowed down greatly by 1966, and the general view was that another recession was just around the corner; it was postponed but not avoided by the vast acceleration of Vietnam war outlays, which were not accompanied by prompt and adequate tax reductions as we had done in the Korean war.

The large tax reductions in 1975, as we all know, went only in disappointingly small proportion to stimulation of employment and production. The proposed tax reductions in the current "package" have inherently the same defects.

I have noticed the recent arrival of a gifted and pulchritudinous member of the staff of the Joint Economic Committee. The Joint Economic Committee in recent years has put out study after study reflecting what I have said, but due to the horrible lag in American economics, this has not been translated into action, and the older theories are applied after the empirical studies discredit them entirely.

The President's proposals are also hopeful but short of specifics on the anti-inflation front, and they ignore the imperative need for large changes in current and prospective monetary policies.

The Federal Reserve can again cancel out a large part of the benefits of any given fiscal stimulus.

Based upon a continuous model of goals related to the U.S. economy in action, which I have developed and corrected from year to year, I submit that the first year package should be \$25 to \$30 billion, instead of about \$16 billion. I submit that at least two-thirds and perhaps more of the first year stimulus should be Federal outlays for direct job creation, but I am concerned about excessive reliance upon conventional public works and public service jobs of a nonsustainable nature.

Therefore, while I agree with the size of the proposal recommended by the AFL-CIO, I think it is too much committed to traditional shots in the arm, unrelated to our long-range needs in these areas, I think that the Secretary of Labor's concern with job training is excellent, but most job training is really on the job, as we learned again and again, and job training without a long-range program of what we should train people for and to create the jobs for them and make shifts in the job patterns in accord with technological changes and real needs, is the essence of an effective job training program and much neglected now.

Moreover, we should distribute additions to Federal outlays across the entirety of our great priority needs, geared to optimum and balanced economic growth on a long-range basis.

The preponderance of these additional outlays should be marginal assistance to job expansion in the private sector, housing and energy being good examples.

The argument that tax reduction will create jobs faster is simply not true on empirical grounds and it would be wrong even if it did, for reasons already stated. It would be far wiser to start now what offers enduring and highly needed gains in worth of product terms, rather than to make effective, even if a few months earlier, a stimulus which will be of much inferior value in worth-of-product terms, wash out in short order, and leave us with the same old difficulties we had before and with another shot in the arm next year, and the year after that, and the year after that.

I submit that tax reduction, at not more than one-third of the first year package, and perhaps less, should be entirely in the form of personal tax reduction in the lower half of the income structure. This is greatly needed on a long-range basis, on both reasons of economic equilibrium and social grounds.

I see need for more effective measures to restrain inflation. And I submit that legislative means should be found to enable the President and the Congress to assert more influence upon the Federal Reserve System, in order to help make its policies consonant with the declared objectives of the elective representatives of the people and the Nation's economic and social needs.

I recognize that all of what I have recommended cannot be put into motion at once. But we can and should put into motion at once the basic requirements for measuring correctly the size and composition of the national economic policies we need, and making them consistent with one another. This does not call for planning the whole economy nor the private sector. But it does call for long-range planning of what the Federal Government itself does. It does call for recognition that economic maginot lines are not enough; that it is not enough to throw up short-range breastworks against recession or economic stagnation.

We should abandon an anti-this-or-that defensive posture, and take the offensive on a long-range and purposeful prosperity policy and program, toward full employment, balanced growth, and serving priority needs.

Finally, I recognize also that this committee does not make legislative recommendations. But as a prime congressional custodian of the purposes of the Employment Act of 1946, this committee can lead the way toward the new accents which are needed, not only in what it says to the Chief Executive, the Congress at large, and the American public, but also through some reconsideration of some of the content of its own studies and hearings.

And not as a committee, but as influential Members of the Congress, I hope that members of this committee will contribute to the enactment in this session of the Humphrey-Hawkins bill, which I regard as indispensable to substituting a comprehensive, integrated, and successful national economic policy and program for the hit and miss, fragmented, and limited approaches which unfortunately still prevail.

Again, I thank the committee for the opportunity to be heard.

[The prepared statement of Mr. Keyserling follows:]

PREPARED STATEMENT OF LEON H. KEYSERLING [1]

Mr. Chairman and members of the committee, I appreciate this opportunity to appear before you again, and to summarize the current significance of studies and observations which I have made since this Committee commenced its operations in 1947 under the Employment Act of 1946. I say this advisedly, because I have become increasingly convinced that appraisals of current national economic conditions and development of current national economic policies have been seriously handicapped for more than two decades, and still are, by excessive concentration upon short-range matters. My reasons for this conclusion will become obvious as I proceed.

IMMEDIATE NEED FOR A LONG-RANGE AND COMPREHENSIVE ECONOMIC POLICY AND PROGRAM

The Chairman's letter inviting me to testify requested that I discuss the economic outlook, the President's economic "package," and his fiscal 1978 budget. I shall discuss these matters today, although it may be rather repetitious and not very helpful to the Committee for me to confine myself to what most others at these hearings are covering. Briefly, my views shared by many are that the short-range outlook is not good. Without changes in national economic policies far more extensive than and considerably different from those proposed by the President, we are most likely to find ourselves a year from now far shorter of full use of our labor force and of other productive resources than we ought to be, and certainly have the capabilities and know-how to be. I believe that the President's economic "package" and related Budget proposals are far smaller than they should be, and poorly composed in various respects.

I anticipate, even with the President's "package" and new Budget, a real GNP in 1977 only 4–5 percent above 1976 as a whole, far below the 6 percent needed to make desirable inroads upon idle resources. This imports unemployment at the end of 1977 far above the 6–6.5 percent we should and can achieve by that time. I anticipate during 1977 as a whole a rate of consumer price inflation of 5.5–6 percent, or far higher than what is achievable with appropriate measures. And I anticipate that these trends will militate severely against balancing the Federal Budget in the longer run. I shall not discuss the President's second year "package" and Budget proposals consistent with it, for I feel that the first year proposals if unmodified will lead to economic conditions at the end of the first year requiring drastic revisions of the second year proposals.

But before elaborating upon these conclusions, I shall now turn to other considerations of an even more fundamental nature. For without prompt and adequate attention to these fundamentals, I am deeply concerned that our short-range efforts will again turn out to be as disappointing as quite similar efforts made repeatedly during the course of the five business cycles we have experienced since 1953, and doomed to lead us into another recession in due course. Instead of forecasting just when that may occur, I submit that we should start now to change the course.

It has become rather habitual for us to regard every current economic situation as critical and immediate, and to attempt to deal with it accordingly on an emergency, fragmentary, and short-range basis. We are again tending to do that now. But most of our large problems today are neither new nor unique, and those which are new or unique are really of secondary import. For example, the weather freeze has introduced a special and transient factor, and some actions are required to relieve the distress caused by it. But we now know that each of the last three quarters of 1976 registered a declining rate of real economic growth, moving into a period of economic stagnation even before the freeze. Thus, it is clear that the economy was in deep trouble before the freeze occurred, and that the freeze has not altered fundamentally nor in the longer-run the big problems

[1] Former Chairman, Council of Economic Advisers; president, Conference on Economic Progress.

to be dealt with. The problems requiring vigorous and extensive treatment would have been about the same if there had been no freeze, and they will remain about the same when the freeze is over. Unacceptably high rates of inflation, and the inflationary shortages of today in energy, food, housing, and elsewhere are not of recent inception. They were initiated through errors of omission and commission many years ago, and these in turn were in large part offshoots of derelictions in general economic policies.

Circa 1954, I predicted before this Committee and elsewhere that, without changes in national economic policies more drastic than any which have since then been undertaken, the American economic performance would follow a roller-coaster course of stagnations, recessions, and inadequate upturns, with each recession at its trough tending to produce more idleness of human and other resources than the trough of the previous recession, and with each recovery tending to leave us at its peak with more unused resources than the peak of the previous recovery. I predicted that the rate of inflation, and the Federal Budget deficits, would augment in consequence of failure to maintain stable prosperity at reasonably full resource use. All of this has come to pass with a vengeance, and the most recent recession and highly inadequate recovery to date are the most poignant examples. The current economic slowdown, which commenced before the freeze, may well be followed by some quickening. But the hope of full or sustained recovery is now unrealistic, without much larger and different changes in national economic policies than those in the President's "package" and his new Budget; and my allusion to another and deeper recession in due course is not so unlikely that we should view it with equanimity, or fail to avert it.

THE COSTS OF THE ROLLER-COASTER ECONOMIC PERFORMANCE

The long-term costs of this roller-coaster economic performance, in which we are still enmeshed, have been staggering. According to my conservative estimates, which are not far different from those of other competent analysts, we have from the beginning of 1953 through the end of 1976 forfeited about 4.4 *trillion* 1976 dollars worth of total national production, and lost about 67 million man-and woman-years of employment opportunity.[2] Vulnerable groups have been hurt immensely more than others. The inflationary trends have at times become intolerable. Government revenues, at existing levels of tax rates, have fallen so far short of what they would have been at sustained reasonably full resource use that horrendous Budget deficits have been accompanied by financial inability to avoid starvation of some of our most pressing domestic priority needs.[3] And all of these difficulties have interacted and continue to interact upon one another. This dismal performance has not ended. It is operative even now.

THE REAL CAUSES OF ROLLER-COASTER PERFORMANCE

Manifestly, under circumstances set forth above, no adequate nor lasting remedial measures can be derived and applied without general appraisal of the central reasons for the roller-coaster performance. There has been no time, during the five cycles since 1953, when this genuine and full appraisal has entered adequately into the formulation and application of national economic policies. Instead, the uniform practice has been to begin with a finding that the volume of total economic activity has been either too slow or too fast, too high or too low, and then to attempt to apply stimuli or restraints without careful regard as just at what points in the economy they are applied. I have often stated that this is like somebody driving up to a filling station, and when the attendant asks whether the gas should be poured into the radiator, or the oil into the tires, or the water into the gas tank, the driver replies: "What difference does it make. Have you never heard of Lord Keynes?"

It should be much clearer than it has been to economic advisers to the President and others that the roller-coaster performance of the economy has not been due primarily to excesses or deficiencies in total purchasing power. For if that were the case, since any level of GNP generates an equivalent amount of purchasing power, one cannot explain how reasonably full resource use converts into stagnation and then recession. The basic explanation of the roller-coaster performance is to be found in maladjustments in the structure, with respect to both income distribution and resource allocation, which make high or even growing

[2] See charts 1, 2, 3, and also chart 4 as to the future.
[3] See chart 5.

prosperity nonsustainable. But neither during previous times nor today have we examined the precise nature of these maladjustments, and applied the stimuli at the right points accordingly.[4]

WHAT TYPES OF EMPLOYMENT AND PRODUCTION DO WE MOST NEED TO INCREASE?

A second and perhaps equal defect, in what has now become the chronic approach, is to apply stimuli on the alleged ground that they will speed things up, without regard for national vaules or priority needs. I am not arguing that the Government should interfere with the free choices of consumers in the spending of the money in their hands. But I am insisting that the role of the Federal Government, in its own policies, should be concerned with these values and these priorities. To take but one example which I will deal with further as I proceed, the question is not solely nor even mainly whether a given number of dollars of tax reductions will stimulate jobs and production as much as the same number of dollars of increased public outlays. Even if it would do that—and I share the views of many others that it certainly would not—there is the crucial question of whether the widely disbursed spending of tax concessions by most of our consumers will buy the goods and services which they and the economy need nearly as much as those to be derived from well-concentrated public investment, either in the short-run or the long-run. Such questions have not been dealt with satisfactorily in the current economic "package" and the new Budget.

IMPORTANCE OF TECHNOLOGICAL FACTORS

Technological considerations are equally important. In general, the spending of tax concessions by consumers will be directed largely toward acquisition of the types of goods produced in industries where technological advance is so rapid that the additional spending would add very little, if at all, to employment in these industries. By promoting fuller capacity use, such spending will mainly increase productivity in these industries. For example, in a recent year when the automobile industry was producing several million more cars than in an earlier year, there were more than 300 thousand fewer automobile workers than in a given earlier year, and the increased numerical size of the auto union was due to taking an aerospace worker and others. My studies over many years, and those of others, have demonstrated that the same situation is true of many of our basic industries. Actually, total unemployment in these basic industries has declined on a secular basis. In contrast, and in accord with national needs, there is room for greater increases in the production of some other types of goods and in the supply of human services. Also, the rate of productivity increase is usually lower in these fields. Thus, increased spending in such fields will add far more to the enduring strength and growth of the economy, and add far more to the human well-being which is the ultimate purpose of all we do on the domestic front. Yet everyone on this informed Committee must know that very little attention has been directed in past years to this problem, and the same is true today.

THE EXCESSIVELY NARROW RANGE OF APPLIED NATIONAL ECONOMIC POLICIES

Another defect in all that we have done in recent years, and still tending to do, is to place excessive reliance upon a narrow range of conventional or stereotype fiscal and monetary policies of a general nature, while neglecting to bring these into combination with other equally important national economic policies. I would like to give three very important illustrations of this from my own experience.

THE FARM-PRODUCT SHORTAGES

First, around 1954 we embarked upon a policy of driving millions of farm families off the land and into the urban centers, on the assumption that we had too much food and fiber production, that restraints upon production would improve farm prices and farm incomes, and that the Government would be relieved of the costs or of a large part of the costs of supporting farm prices and carrying so-called farm surpluses. I pointed out in 1954, and continued to do so repeatedly in later years, that we did not have farm surpluses related to the real food and fiber needs of the United States at full resource use plus a better

[4] See chart 6.

planned and more thoughtout export of our farm products. Most important of all, I pointed out that these farm policies would lead to chronic and inflationary food shortages, and this has been and still is more important than recent crop failures. And I pointed out that the millions of farm families driven into the cities would land largely on the relief and welfare rolls, be wasted instead of productive, and contribute infinitely more to public costs than if they had remained on the land. But when I took this matter up informally with members of the Council of Economic Advisers, I was told that farm policy was for the Department of Agriculture and not for them. To be sure, the details of farm policy are for the Department of Agriculture. But how can we have a mature and comprehensive employment policy under the Employment Act of 1946, if the Council of Economic Advisers and the Economic Reports of the President largely take the position that the agricultural problem is not for them?

THE FUEL AND ENERGY SHORTAGES

Second, fifteen or so years ago as a consulting economist, I commenced to appear in cases involving many very large utilities, both gas and electric, before Federal and also before State regulatory bodies. I found that these regulatory bodies were concerning themselves with a rate of return adequate to service capital requirements as set forth by the utilities, but were not even raising the question of what capital would be required to support the utility plant and services consistent with the demands of a fully healthy economy. I pointed out that real utility plant growth in many instances was moving negatively, and that we confronted the clear prospect of serious shortages in due course. A large contributory factor was the tight money and high interest rate policies of the Federal Reserve, especially in that the utilities finance a higher proportion of capital investment with borrowed funds than any other basic industry except housing. But when I took this matter up informally with members of the Council of Economic Advisers, I was told this was not their business nor the business of the Economic Reports of the President, but rather was the business of the regulatory commissions. How can something as important as utility plant and services not be the concern of those entrusted with a full and comprehensive national economic policy? If this crucial priority had been attended to rather than neglected, neither the Arab actions or anything else would have gotten us into nearly as much trouble as we have experienced and are experiencing now on the fuel and energy front.

THE MASS TRANSPORTATION SHORTAGES

A third example is the railroads. For six years before the Interstate Commerce Commission as an economist, and then before the Supreme Court of the United States as a lawyer, I opposed the Penn-Central merger. I did not object to big business as such, nor to mergers as such, and never have. I objected to the merger on the ground that it was based upon the deliberate policy of trying to save money for the two roads, and to save them from bankruptcy, by deliberate denial of necessary rail services to many communities, and by widening neglect of passenger traffic. I further pointed out that approval of the merger on such grounds would certainly result in the bankruptcy of Penn-Central. President Kennedy at one time set up an interdepartmental committee, including representation of the Council of Economic Advisers, to examine the rail-merger situation. But this effort came to naught, and the Justice Department supported the Penn-Central merger before the Supreme Sourt, after opposing it vigorously before the ICC. When I took this matter up informally with members of the Council of Economic Advisers, they informed me that it was not their business nor the business of the Economic Reports of the President, but rather the business of the ICC. How could the adequacy of our rail services not be of concern to those entrusted with levels of employment and the general health of the economy?

A reading today of the Economic Reports of the President, year by year, will abundantly illustrate the preoccupation with one or two lines of national policy, especially fiscal policy, and the oversight of others of equal importance. The performance of the Economic Advisers and many other economicts has reminded me of a competent violinist holding in his left hand a Stradivarius violin, which is no more wonderful in its innate capabilities than the U.S. economy, and then placing the bow which brings forth the performance on only one string, and the G string at that!

INADEQUATE TREATMENT OF STRUCTUAL PROBLEMS

Another difficulty is that economists and others have talked continuously about structural problems in the economy, but mainly as an excuse for magnifying the difficulties confronting them and explaining whey they have not been more successful. Structural difficulties there are, but they are not really new, and the urgent requirement is for a more thorough meshing in due proportions of micro-economic and macro-economic policies. That we certainly do not now have, as illustrated by the three examples of food, fuel, and mass transportation.

IMPROPER USE OF THE FEDERAL BUDGET: THE TRUE FUNCTION OF FEDERAL OUTLAYS

Still another difficulty, and a towering one at that, is the erroneous manner in which the Federal Budget as the most important single instrument in national economic policy is being developed and applied. In studying the Federal Budget from year to year, and also the impressive reports and commentaries emanating from the Executive Branch and from the Congressional Budget Office, it often seems to me that the dominant thinking is to the effect that the Federal Budget exists primarily for the purpose of being balanced, and second for the purpose of stimulating or restraining the economy as the need may be. But that position is obviously incorrect. The Federal Budget could be balanced with zero outlays and zero taxes. The economy could be stimulated with 20 or 30 billion dollars of total Federal outlays and zero tax collections, and restrained with 20 or 30 billion dollars of tax collections and no outlays.

Although a balanced Budget and stimulation or restraint through the Budget are highly desirable under given circumstances, the core purpose of the Federal Budget is entirely different. It is to use fiscal policy to allocate to the public sectors those goods and services which the economy and the people need and which, to repeat what Lincoln said, cannot be provided, or cannot be provided so well, in some other way. The expenditure side of the Federal Budget, at almost all times, should be fixed at approximately that percentage of our total GNP capabilities at estimated full resource use (whether we are currently at full resource use or not) which would represent that amount of allocation to the needed public priorities which the Federal Budget should serve.

When we are actually below full resource use at any given time, the application of such a Budget-outlays policy serves the additional useful purpose of helping to stimulate the economy toward full resource use. To claim that we "cannot afford" such a Federal Budget policy because it would lead to a Federal deficit or increase its size, at times when we are far below full resource use, confuses the condition of the Federal Budget with the real wealth potentials embodied in the condition of the national economy and the priority need to activate these fully. When real productive resources are idle in huge amounts, the enlarged use of these resources by serving those unmet economic and social priorities which the Federal Budget alone can serve, or can serve better than they would otherwise be served, is almost always desirable.

On the other hand, if the pressures on the economy are so large that inflation results from strains in excess of our capabilities at full resource use, then to cut back on the above suggested use of Federal outlays, in a manner adverse to meeting these priority needs, results in cutting back first on the things for which we have a very high need, and which should not be in the Federal Budget in any event if that high need does not exist. Instead, less useful or even expendable activities should be restrained by proper use of tax policy.

THE TRUE FUNCTION OF FEDERAL TAXATION

Contrary to what seems to be a misdirection in thought and action during many years in the past and today, Federal outlays and Federal taxation are not for the same purposes, and they should not be used interchangeable. Tax policy exists for the purpose of covering in appropriate degree the expenditures undertaken by the Government, and it is tax policy rather than spending policy which should be varied from time to time to impose stimulus or restraint upon the economy—but only after Federal spending policy is determined as I suggest above. I shall discuss further the appropriate Federal tax policy at this time, far different from the President's "package" and new Budget.

I do not understand how any economists can seriously challenge these propositions as I have stated them. They are simple common sense. But for many years in the past, and even today, we have used spending policy and tax policy more or less interchangeably. On many occasions, and even today, with the President's "package" a good example of this, we appear first to be deciding how much we want to accomplish through tax reduction, toward objectives not even clearly stated in terms of specific goals or timetables, and then we appear to decide what kind of Federal spending policy will fit conveniently into the prescribed tax policy. This is entirely upside down. It is also most unfortunate, in terms of the highly desirable objective of using the Federal Budget in a manner which will help to bring about full resource use and to balance the Budget or run a surplus at that time. For the huge deficits in the Federal Budget which we have been running have been almost entirely the consequency of all of the deficiencies in national economic policies which I am attempting to detail.[5] There is not comforting evidence that the President's "package" and Budget are adhearing to these sound principles, regarding the utilization of Federal spending and tax policies, respectively.

THE PROPER TIMING OF PRIORITY FEDERAL OUTLAYS

Still another deficiency in the President's economic proposals, and the explanations related to them, is that they appear to recognize the necessity for direct investment in the great national priorities, such as energy, resource development, mass transportation, urban relief and renewal, environmental improvement, housing, health and education, welfare reform, etc. But the official proposals then proceed upon the erroneous assumption that the "package" will stimulate the economy enough to provide us with a very large fiscal dividend several years from now, say around 1980, and that we will then be able to commence in sufficient measure to vindicate these priority purposes through increased public outlays.

But the error in this approach is quite clear. To move toward achievement of that fiscal dividend, we would need balanced economic growth at an optimum rate, and this cannot possibly result from erroneously designed policies and programs which do not build into the structure the requirements for optimum and balanced growth. Any serious study makes it abundantly clear that the achievement of sustained growth at these levels depends upon very substantial changes in income flows and resource allocations. And almost all of these needed changes are in the direction of devoting a larger portion of our total economic endeavors to these priority goods and services which the economy most needs. There is no other way to get back to full resource use, and incidentally to achieve the projected increase in Federal revenues.

This of course does not import that we can meet all of these priority needs fully nor at once. But it does mean that we should develop a long-range model of the whole economy in action, develop a balance sheet of our needs and capabilities, set a few meaningful long-range goals, and relate what the Federal Government does to its calculated share in the achievement of these goals. This means among other things that, once an appropriate total stimulus is decided upon, it should be supported in accord with proper beginnings, year by year, in the servicing of the priority programs I have mentioned. This calls for much more Federal outlays, and much less tax reduction. It calls for a careful examination of the needed changes in income flows and resource allocation, and of this there are slight signs of recognition in the current "package."[6]

TEMPORARY "SHOTS" ARE NOT ENOUGH, AND ARE MISDIRECTED

All of what I have said boils down to the observation that the current "package" does not represent that rationalized long-range approach which is absolutely essential to sound short-range measures. The current "package," as it appears to me, is merely another shot-in-the-arm, short-range in purposes and, in its deficient size and poor composition, hardly different from what has been tried several times before. And it is very likely to have the same results. I note that my good friend the new Chairman of the Council of Economic Advisers recently told the

[5] See again chart 5, and also chart 7.

[6] A "model" Federal Budget toward these ends is set forth on chart 8, and the costs and benefits of such a Budget are set forth on charts 9 and 7. However, the component and total quantifications in this model are lower than what I now recommend, due to the process of inflation, the inadequate recovery movement to date, and other factors. The model Budget when prepared did not contemplate further tax reductions, but my recommendations now include some along the lines I indicate.

House Budget Committee that the first year "package" was just a "shot"; that the second year "package" was a different kind of "shot"; and that after about two years the economy would be in such fine shape that, combined with renewed confidence, this would enable ebullient capital investment to take care of us from that point forward, with Government responsibilities greatly reduced. In other words, it is proposed to try once again a series of "shots" which have not worked well nor enduringly when tried before.

THE TRADEOFF, AND MISTREATMENT OF THE INFLATIONARY PROBLEM

Finally with respect to the deficiencies in our national economic thought and action during many years and even now, there is the serious problem of inflation. In 1953, the new Administration inherited from the Truman Administration an unemployment rate of 2.9 percent, and an inflation rate of 0.8 percent for consumer prices. But the new Administration, with Dr. Arthur Burns exerting a powerful influence as Chairman of the Council of Economic Advisers, concluded that *the* great danger was inflation. Both fiscal and monetary policies were tightened to the point where unemployment rose to 6.7 percent in the last year of that Administration, after three recessions, and with the inflation rate being 2.5 times as high in 1961 as 1953.

As early as 1954, I had commenced to state repeatedly that the so-called tradeoff between unemployment and inflation was a travesty on all grounds, and I cited many reasons why a sick economy would be prone to far more inflation than a healthy economy. Most economists did not pay much attention to this empirical observation at that time. Nor did they pay much attention to it when the years from 1958 to 1966 witnessed a high average annual rate of real economic growth and a tremendous reduction in the unemployment rate to 3.8 percent in 1966, accompanied by virtual price stability. Nor did they get straightened out about the tradeoff during later periods, including the time when the highest unemployment since the Great Depression was accompanied by the highest inflation rate since the Civil War. By then, they were attributing the double-digit inflation to the behavior of the Arabs and the farm failures, although even before these things happened the underlying inflation rate had mounted to unusually high rates under conditions of very high economic slack. Nor did these economists pay much attention to the empirical evidence that the inflation rate dropped very sharply when the current economic recovery was moving very fast in real terms, and commenced to increase seriously with the advent of a disappointly slow rate of economic growth thereafter, even before the weather freeze.[7]

SALIENT DEFECTS IN THE ANALYSIS OF THE CAUSES OF INFLATION

Some strange ratiocination has recently developed in the discussion of the relationship between unemployment and inflation. We are told that the rising inflation during recessions represented only a "time lag," in response to conditions when the economy was in much better shape. What really happened is that adjustments in the economy, including wage rate changes, which were proper and sustainable when the economy was in good shape, became hard to bear when the stagnation and recession came, and when productivity gains were consequently reduced from rewarding levels to very low or negative figures.[8] So in the main, it was really the stagnation and recession, and not high prosperity, which augmented the inflation.

More recently still, my good friend Dr. Schultze has come forward with some additional alarums. Last year, he alarmed some Congressional Committees, some members of the Congress, and the readers of The Washington Post with the proposition that inflation would become uncontrollable if unemployment were reduced to 5 percent or even 5.5 percent. He dismissed the much lower inflation in some earlier times when unemployment was 3 or 3.8 percent, by arguing that times had changed, and that we now live in a new kind of economy where the old rules no longer apply. What this amounts to is the insupportable implication we should move secularly toward acceptances of higher and higher unemployment rates as a cure for inflation. But as indicated above, there has been little or no empirical evidence that the acceleration of inflation starts when unemployment declines

[7] See charts 10, 11, and 12.
[8] See charts 12, 13, and 14.

to 5 or 5.5 percent. The forecast that this will happen in the future is arrived at by grinding materials through computers, but what comes out is all wrong because the assumptions fed into the computers are based upon preconceptions at sharp variance with the empirical evidence thus far

There is a very pertinent question to be posed to Dr. Schultze. He has stated correctly that full employment is the most vital of all of our domestic objectives. But last year, during his opposition to the Humphrey-Hawkins Bill in its form at that time, he stated that this meant that we would need price and wage controls when unemployment reached 5 percent or even 5.5 percent. But President Carter is now adamantly against the direct controls, and so presumably is Dr. Schultze. Does this mean that we should never try to get unemployment below 5 percent or even 5.5 percent, and if we accept that proposition, where do we go from here?

VIEWING THE INFLATION PROBLEM IN PROPER PERSPECTIVE

The official position on the tradeoff is confronted by even more serious defects in analysis. Dr. Schultze has told us, without qualification, that inflation is the basic cause of recessions, and that we must therefore succeed in restraining prices before we try to get the economy moving forward at the needed speed. But again, the empirical evidence is embarrassing to this thesis. The Great Crash was not preceded by inflation, but rather by a remarkably stable price level for seven years. Some of the recessions since early 1953 were not preceded by inflation; the inflation often grew as the recessions proceeded.

The crux of the matter is that the avoidance of the business cycle, or its modulations, depend upon attention to corrections in flows of income and allocation of resources, and this requires far more than willy-nilly attempts to restrain inflation per se. Most important of all, the tradeoff exponents have not brought to public attention the palpable fact that the economic and social and civil costs of the roller-coaster performance have been enormously greater than the costs of any marginal differences in price behavior which might have result if there had been no roller-coaster performance.

And all this is apart from the moral indefensibility of saddling upon many millions of families the cruel burdens of unemployment, on the ground that they should be the protectors of the employed and affluent against inflation. Actually, inflation hurts the unemployed and the poor most; and they are hurt more by unemployment than by inflation. Nor does it hurt everybody; it hurts some and benefits others; and we need much more examination, which has not been forthcoming, as to whom it hurts and whom it helps. This in itself would point the way to more correct national economic policies.

WHAT WE SHOULD DO ABOUT INFLATION

I am not soft on inflation. I insist that a stable price level is highly desirable. I believe in many types of weapons, apart from the direct controls, to restrain inflation. But I believe that the best way to restrain it is to restore and maintain reasonably full resource use as quickly as practicable. Whether I be right or wrong on this, it by now must be indisputably clear that damaging inflation occurs at every stage in the business cycle. We should therefore make the restrain of inflation and the restoration of a fully healthy economy simultaneous goal, with each reinforcing the other, instead of continuing the farrago of the tradeoff.[9] The President's current proposals do not tell us how to guard against inflation; they hope it will subside.

EVALUATION OF THE PRESIDENT'S "PACKAGE" AND NEW BUDGET

Having made these points, my evaluation of the President's first year "package," and of his budget proposals in accord with it, will not take much time, because it is implicit, or even explicit, in all that I have said above. On the basis of models which I have made yearly since 1953 of the American economy in action, and corrected in the light of evolving experience from year to year, I submit that the President's total "package" is much too small. The "package" for two years comes to less than one percent of the size of the economy, or a much smaller percentage than proved inadequate in earlier years when similar "shot" or "quick-fix" approaches were tried. The argument that a retarded recovery will be more likely to avoid recession than a more rapid recovery is not borne out by the empirical evidence; most of the recessions since 1953 were

[9] For discussion of a comprehensive anti-inflation program, see pp. 5–6 of the text of a printed pamphlet on the Humphrey-Hawkins bill, issued by the Senator and the Congressmen in January 1977, and obtainable from their offices or mine.

preceded by very inadequate recoveries. And, as earlier stated, the current recovery for more than three quarters has been in a stagnation stage. The argument that a retarded recovery is the best way to restrain inflation, or the best way to protect the Federal Budget, is invalid for manifold reasons which I have already discussed.

The first-year "package," coming to about six parts tax reduction and one part direct job creation, is entirely distorted for all of the reasons I have set forth above. Experience as well as reason supports this point of view. The widely heralded tax reductions in 1964 did give the economy a shot-in-the-arm for a short while. But for reasons which I then predicted, the real growth rate slowed down greatly by 1966, and the general view was that another recession was just around the corner; its advent was postponed but not avoided because of the vest acceleration of outlays for the Vietnam war. The large tax reductions in 1975, as we all know, went only in disappointingly small portion to the stimulation of employment and production. The proposed tax reductions in the current "package" which take the form of direct concessions to private investors are almost entirely wasteful. The basic barrier to plant expansion, at least in the mammoth corporations—small business is a special problem—are not in any current inadequacies in prices or in profits *per unit*, but rather in the inadequacy in demand for their products. The sure, sound, and economical way to enlarge these demands is through the expansion of consumer and public outlays.

The President's program ignores the need for drastic changes in monetary policy, a most serious omission, as the current policies of the Federal Reserve can again cancel out a large part of the benefits of any fiscal stimulus.[10]

As earlier indicated, I do not discuss the President's second year "package," nor any Budget proposals in accord with it, because my estimate of economic conditions at the end of the first year "package," if it be adopted as submitted, leads me to conclude that the second year "package" as submitted will need to be altered greatly. Far more important, first and second "shots" or "quick fixes" will, in my judgment, fall just as short as similar ones tried several times in the past. We urgently need a long-range restorative program, comprehensive and coherent, of which any short-range aspects will be found to be an inseparable part.

MY OWN PROPOSALS FOR FULL ECONOMIC RESTORATION

For reasons already made clear, I submit that the first year "package" should be 25–30 billion dollars, instead of about 16 billion. I derive this figure from my continuous model of the U.S. economy in action, which I have already described. I believe that at least two-thirds and perhaps more of the first year stimulus should be public outlays for direct job creation, with the preponderance of these public outlays in the form of marginal assistance to the creation of jobs in the private sector, housing and energy being good examples. I have developed a model Federal Budget which indicates a viable pattern for the composition of these outlays.[11] The President's new Budget should be modified along these lines.

I submit that the tax reduction, at not more than one-third and perhaps less of the first year stimulus, should be entirely in the form of personal tax reduction in the lower half of the income structure, this reform being greatly needed on both economic and social grounds, and long-range in nature.

My studies also indicate that the contribution of this fiscal approach to the achievement of balanced growth and reduction of overall unemployment to 4 percent within about four years would balance the Federal Budget at that time, and there is no other way to balance it.[12]

The prevalent monetary policy is in urgent need of drastic revision.[13]

THE PROPER NATURE OF A NATIONAL INCOMES POLICY

The stimulus program should be accompanied by a wide variety of measures to restrain inflation, pursued simultaneously, which the President's proposals do not include.[14] These in my personal view should include, inter alia, a vigorous

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[10] See again chart 12, and see chart 15.

[11] See again chart 8. However, the component and total quantifications in the model are lower than those I now propose, for a variety of reasons, including the process of inflation and the current slowness of the recovery movement. The model when prepared did not allow for further tax reduction, by my recommendations do allow for some along the lines I indicate.

[12] See again chart 7 as an illustration, although I now suggest higher outlays.

[13] For discussion of how to correct the current monetary policy, see pp. 45–46 of the Humphrey-Hawkins pamphlet.

[14] See again pp. 5–6 of the Humphrey-Hawkins pamphlet.

but voluntary national incomes policy. Such a policy, entirely unlike previous efforts in this direction through "guidelines" or direct controls, should be concerned not only with the restraint of inflation, but also with the chronic and even more serious problem of promoting adequate expansion of purchasing power, allocated in accord with the requirements for balanced growth, priorities, and restoration of full resource use. A national incomes policy really involves taking account of fiscal and monetary policies also, because the entirety of economic activity is determined primarily by income flows. The neglect of these broader aspects of a national incomes policy has thus far made the treatment of this problem shallow and superficial.

THE VITAL SIGNIFICANCE OF A FEW BASIC GOALS

I submit, above all, that the entirety of national economic policy formulation and application should be guided by a few basic quantitative goals, representing our full capabilities at full resource use, and paying due attention to economic balance and to the great priorities of our private and public needs. These goals should be embodied, first of all, in the Economic Reports of the President and/or in comparable submissions such as Full Employment and Balanced Growth Plans. There are no really firm and convincing goals or commitments in the current economic proposals of the President and the official discussion of them. Hesitant and qualified forecasts are no substitute for such goals.

It is the task of national policy, not to guess what is going to happen, but to commit ourselves to purposes, and to gear policies to their attainment. This was done during the Truman Administration, and for a number of years during the Kennedy-Johnson years, and that was when the economic performance record was best by all tests.

THE LESSONS TO BE DERIVED FROM THE TRUMAN ADMINISTRATION

I conclude with a reference to the Truman Administration, which I trust will not be regarded as prideful in view of my service on the Council of Economic Advisers from 1946 to 1953, and my Chairmanship from 1949 to 1953, but rather as an example which is very relevant today. Although there have been claims to the contrary, the Truman Administration confronted greater economic and financial difficulties and complexities than any since. There was the challenge of conversion from World War II to peace before the emergence of the cold war, and it was accomplished smoothly. There were vast inflationary problems arising primarily from the accumulation of wartime savings released very shortly after World War II. There were all kinds of shortages, especially during the early stages of the Korean war, which was larger relative to the size of the economy than the Vietnam war. But the subsequently unequaled economic performance during the Truman Administration was feasible because, in the main, we followed the principles which I have stated above. Above all, we recognized always that the greatest source of our wealth and well-being was recognition that the full marshaling of our human and other economic resources through optimum and balanced economic growth underpinned all else that we sought to do. Because of the very good economic performance, the Federal Budget averaged a surplus over the period for the last time to date. And the total performance was greatly aided by the willingness to increase taxes promptly and sufficiently in the face of a large war, a record not repeated during the Vietnam war.[15]

Substantiation of large parts of my analysis, and of events validating my declared views, are set forth very fully in the Invited Comments which I have submitted year by year to this Committee.

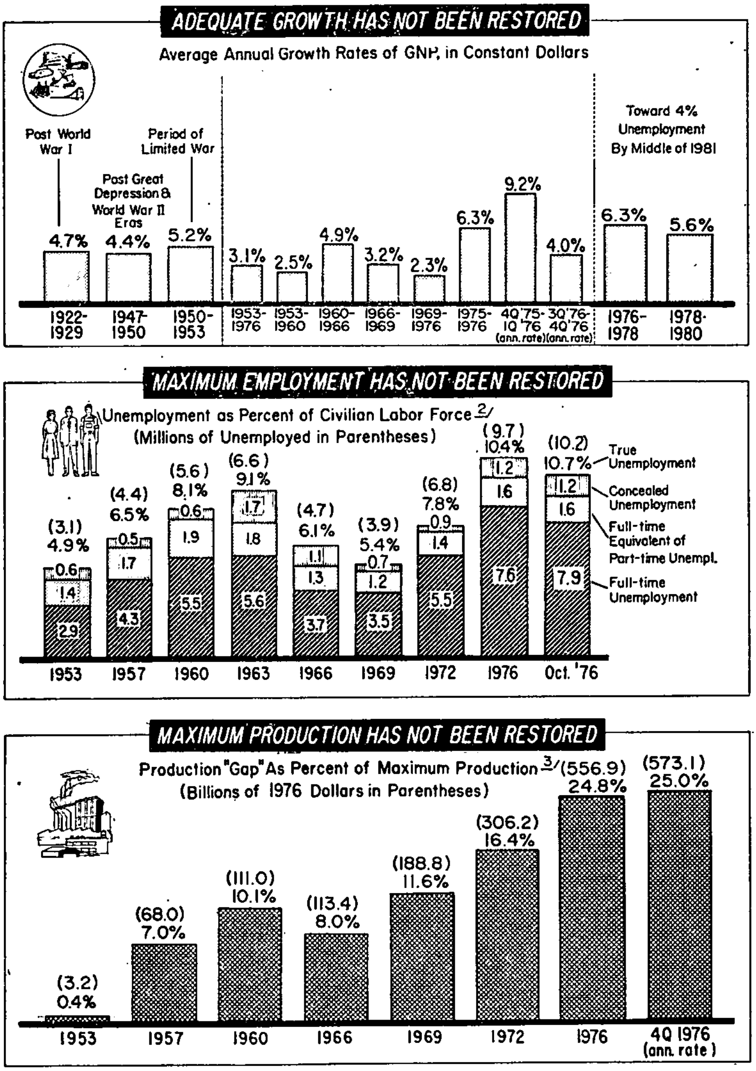
A complete coverage of the recent and current economic situation and of the current outlook, and of what I submit we should start to do now, are set forth in the new pamphlet on the Humphrey-Hawkins Bill, issued by Senator Humphrey and Congressman Hawkins in January 1977.[16] Instead of encumbering the record with the reprinting of this pamphlet, I am making a copy of it available to each member of this Committee. I regard enactment of the Humphrey-Hawkins Bill at this session of the Congress as indispensible to the substitution of a comprehensive and integrated national economic program and policy for the hit and miss, fragmented, and limited approaches which still prevail.

Again, I thank the Committee for this opportunity to make my views known.

[15] See again chart 11.

[16] Single copies of this pamphlet may be obtained from Congressman Hawkins' office, and in quantities from my office.

BASIC U.S. ECONOMIC TRENDS, 1953–1976[1]



1/ All 1976 figures estimated.

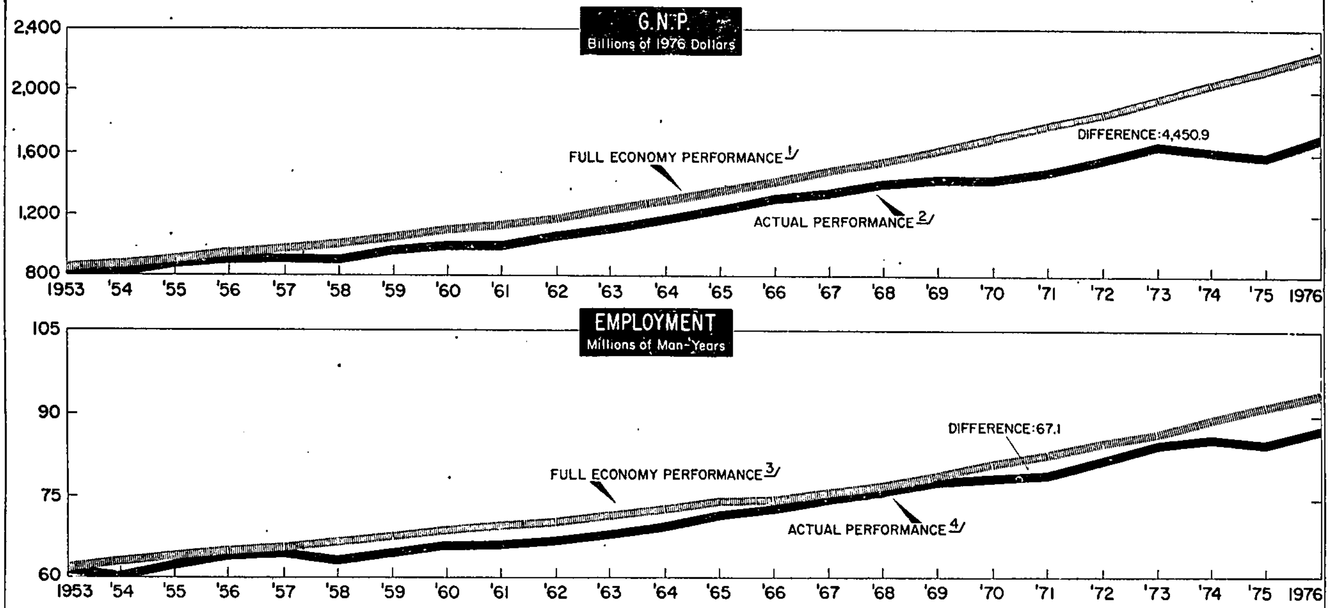
2/ In deriving these percentages, the Civilian Labor Force is estimated as the officially reported Civilian Labor Force augmented by concealed unemployment. Thus, some of the percentage figures on full-time unemployment vary very slightly from the official reports, which do not take account of the augmented 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.

3/ Maximum production equates with average annual growth rate of 4.4%, 1953-1976.

Basic Data: Dept. of Commerce; Dept. of Labor

CHART 1

COST OF DEPARTURES FROM FULL ECONOMY, 1953-1976



1/ Real average annual growth rate of 4.4 percent.
2/ Real average annual growth rate of 3.1 percent, the 1953-1976 average. 1976 estimated.
3/ Average true level of unemployment of 4.1 percent, or 2.9 percent full-time unemployment.
4/ Average true level of unemployment of 7.0 percent, or 5.2 percent full-time unemployment. 1976 estimated.
Basic Data: Dept. of Commerce; Dept. of Labor

CHART 2

COSTS OF DEFICIENT ECONOMIC GROWTH U.S. ECONOMY, 1953-1976 AND PROJECTED 1977-1980

(Dollar items in billions of 1976 dollars, except average family income)

1953-1976 [1]

Total National Production (GNP)	Man-years of Employment [2]	Personal Consumption Expenditures	Gov't Outlay for Goods and Services
1953-1976: $4,450.9 1969-1976: 1,423.2 1976: 337.8	1953-1976: 67.1 Million 1969-1976: 28.9 Million 1976: 6.1 Million	1953-1976: $1,967.0 1969-1976: 648.6 1976: 160.8	1953-1976: $1132.8 1969-1976: 379.4 1976: 88.3
Private Business Investment (Incl. Net Foreign)	**Average Family Income (1975 Dollars)**	**Wages and Salaries**	**Residential and Commercial Construction**
1953-1976: $1,351.1 1969-1976: 395.2 1976: 88.7	1953-1976: $35,891 1969-1976: 8,441 1976: 2,201	1953-1976: $2,232.7 1969-1976: 599.7 1976: 170.0	1953-1976: $551.3

1976-1980 [3]

Total National Production (GNP)	Man-years of Employment [2]	Personal Consumption Expenditures	Gov't Outlay for Goods and Services
1977-1980: $440.6 1980: 173.8	1977-1980: 8.1 Million 1980: 2.9 Million	1977-1980: $286.1 1980: 106.8	1977-1980: $65.6 1980: 30.0
Private Business Investment (Incl. Net Foreign)	**Average Family Income (1975 Dollars)**	**Wages and Salaries**	**Residential and Commercial Construction**
1977-1980: $88.9 1980: 37.0	1977-1980: $4,353 1980: 1,710	1977-1980: $188.0 1980: 71.0	1977-1980: $70.0 1980: 20.0

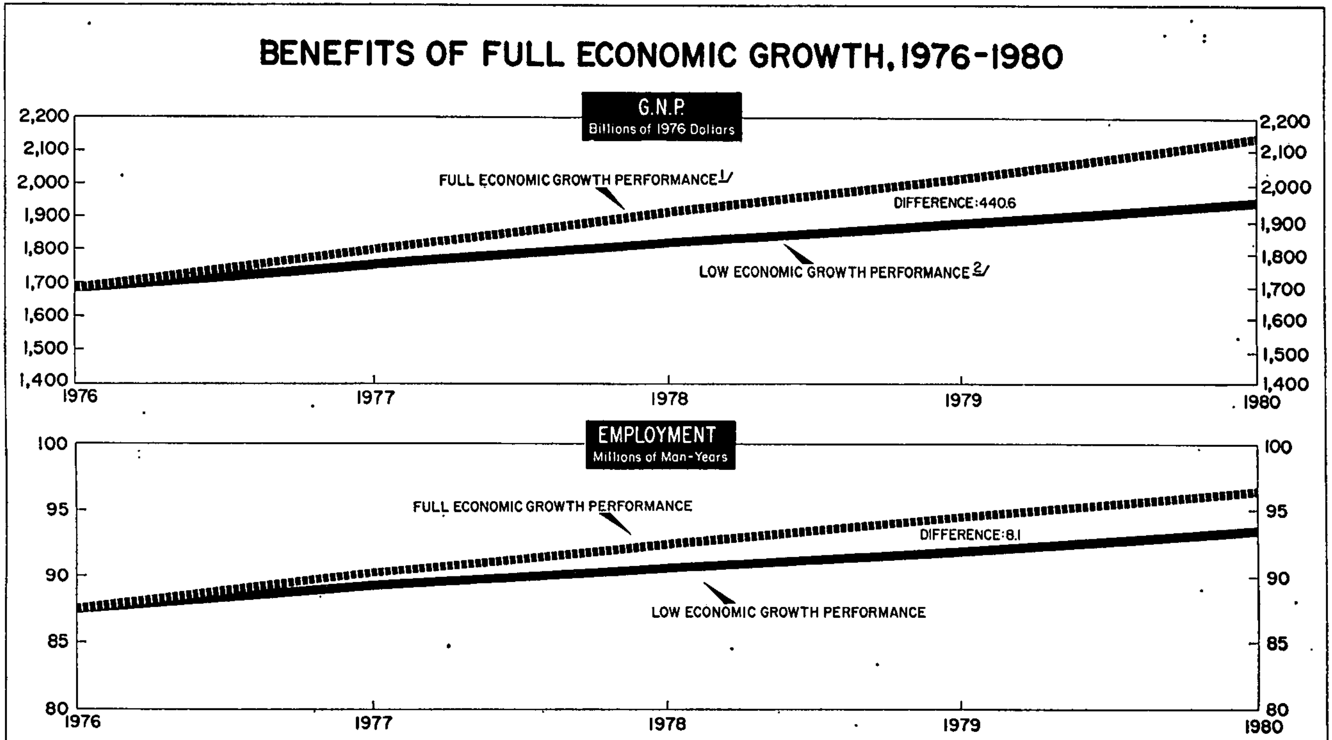
1/ Deficits 1953-1976 are calculated from a 1953 base, in that growth rates since then have averaged far too low. Deficits 1969-1976 and 1976 are projected from a 1968 base, writing off the cumulative deficits 1953-1968. 1976 figures are estimated. Residential and commercial construction deficits are calculated only from a 1953 base. In terms of what would have been needed, 4Q 1976, to restore full production as of then, the estimated deficit was 150-200 billion dollars, at an annual rate.

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 1976 base, writing off the cumulative deficits 1953-1976.

Basic Data: Dept. of Commerce; Dept. of Labor

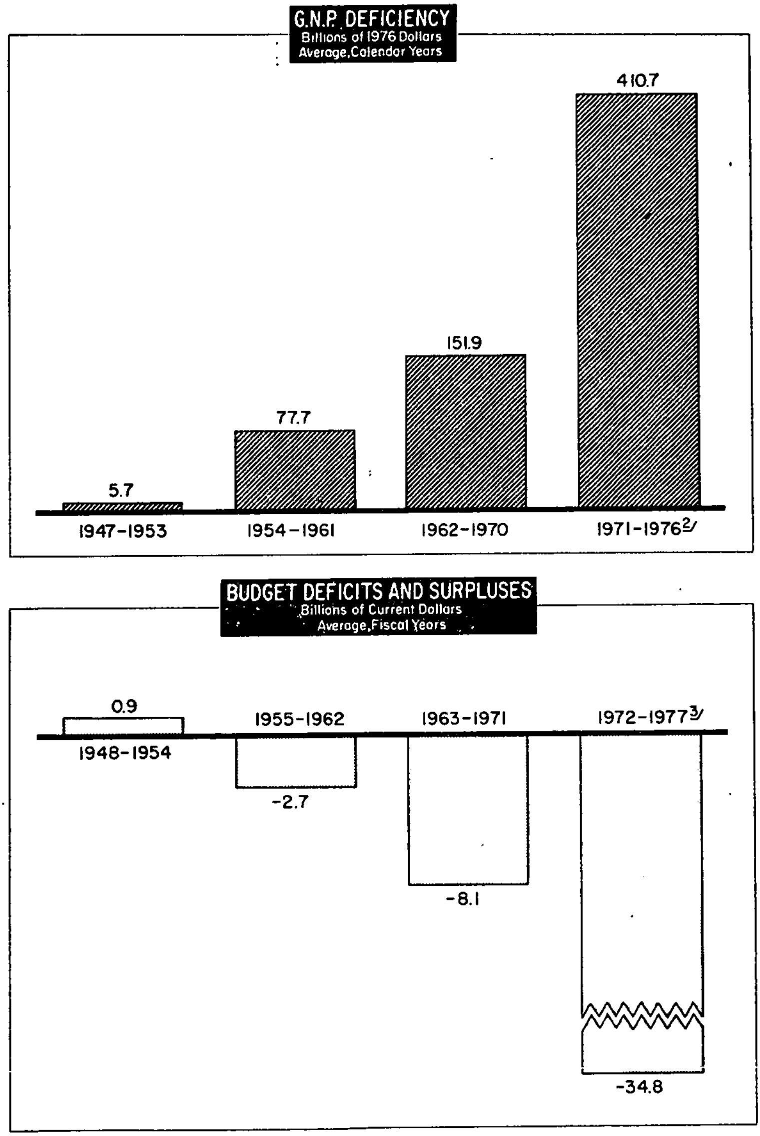
CHART 3



1/ Real average annual growth rate of 6.6%, 6.0%, 5.8%, and 5.3% in each of four years, respectively, and average of 5.9%, 1976-1980.
2/ Real average annual growth rate of 3.7 percent, compared with 2.3%, 1969-1976.

CHART 4

G.N.P. DEFICIENCIES[1] AND BUDGET DEFICITS



[1] Production deficiencies represent differences between actual production and production at full economy rate of growth. Projections from 1946.

[2] 1976 estimated.

[3] 1977 estimated.

Source: Dept. of Commerce; Office of Management and Budget, for actual figures

CHART 5.

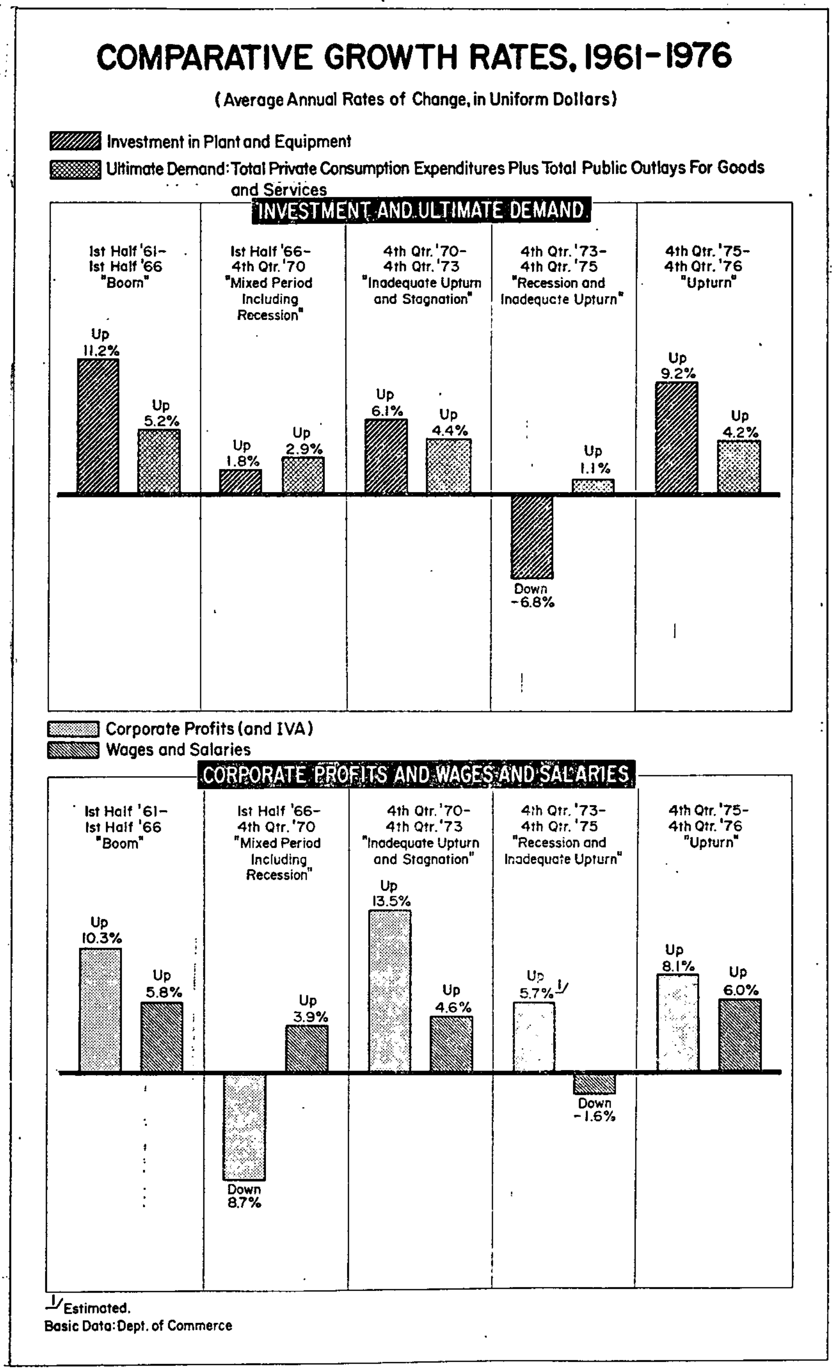
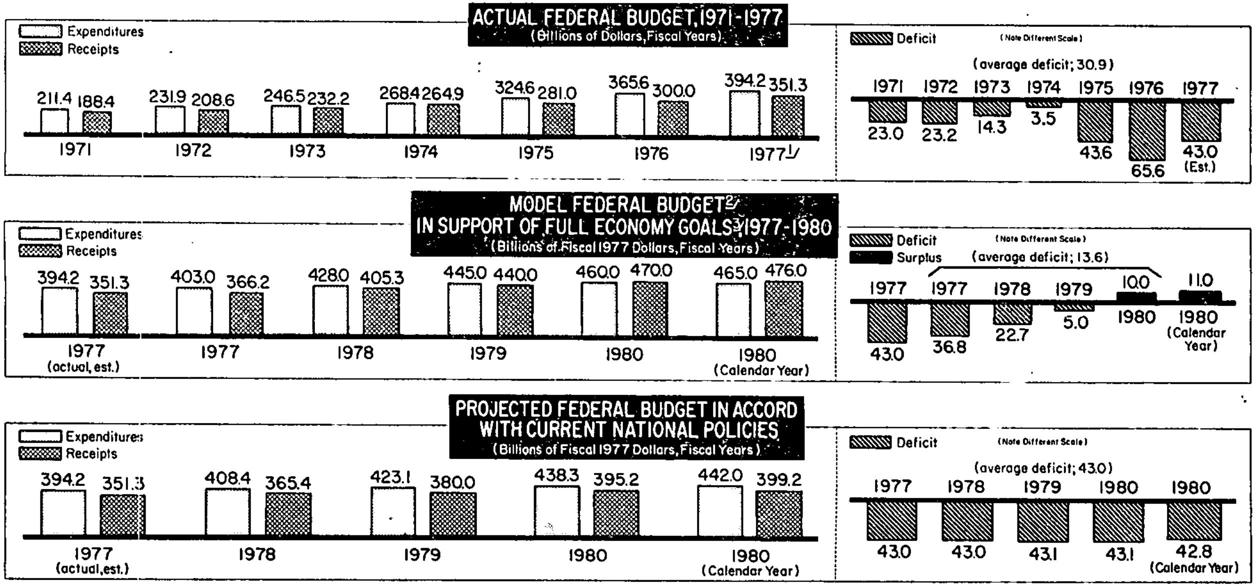

COMPARATIVE GROWTH RATES, 1961-1976
(Average Annual Rates of Change, in Uniform Dollars)
Investment in Plant and Equipment
Ultimate Demand: Total Private Consumption Expenditures Plus Total Public Outlays For Goods and Services
INVESTMENT AND ULTIMATE DEMAND
1st Half '61- 1st Half '66 "Boom"
1st Half '66- 4th Qtr. '70 "Mixed Period Including Recession"
4th Qtr. '70- 4th Qtr. '73 "Inadequate Upturn and Stagnation"
4th Qtr. '73- 4th Qtr. '75 "Recession and Inadequate Upturn"
4th Qtr. '75- 4th Qtr. '76 "Upturn"
Up 11.2%
Up 5.2%
Up 1.8%
Up 2.9%
Up 6.1%
Up 4.4%
Down -6.8%
Up 1.1%
Up 9.2%
Up 4.2%
Corporate Profits (and IVA)
Wages and Salaries
CORPORATE PROFITS AND WAGES AND SALARIES
1st Half '61- 1st Half '66 "Boom"
1st Half '66- 4th Qtr. '70 "Mixed Period Including Recession"
4th Qtr. '70- 4th Qtr. '73 "Inadequate Upturn and Stagnation"
4th Qtr. '73- 4th Qtr. '75 "Recession and Inadequate Upturn"
4th Qtr. '75- 4th Qtr. '76 "Upturn"
Up 10.3%
Up 5.8%
Down 8.7%
Up 3.9%
Up 13.5%
Up 4.6%
Up 5.7% 1/
Down -1.6%
Up 8.1%
Up 6.0%
1/ Estimated.
Basic Data: Dept. of Commerce

CHART 6

FROM FEDERAL DEFICITS IN AN UNHEALTHY ECONOMY TO A HEALTHY BUDGET IN A HEALTHY ECONOMY



1/ President's Budget, as sent to the Congress on January 21, 1976.
2/ Model Federal Budget depicted in detail on another chart. Goals would be higher in each year's dollars to extent prices rise above fiscal 1977 dollars.
3/ Full economy goals shown on another chart.

Basic Data: Office of Management and Budget for actual Federal Budget

CHART 7

GOALS FOR A MODEL FEDERAL BUDGET, FISCAL 1977 AND CALENDAR 1980 CONSISTENT WITH OTHER GOALS TO REACH MID-1981 UNEMPLOYMENT GOAL AND TO SERVE ADEQUATELY THE GREAT NATURAL PRIORITIES[1]

(In billions of fiscal 1977 dollars. All in fiscal years except calendar 1980)

	ALL FEDERAL OUTLAYS			NATIONAL DEFENSE, INTERNATIONAL AFFAIRS, AND SPACE			DOMESTIC PROGRAMS[2]			INCOME SECURITY, OTHER THAN VETERANS (Excluding Subsidized Housing)			MANPOWER PROGRAMS, INCLUDING PUBLIC AND PRIVATE SERVICE JOBS		
	Total Expenditures ($ Billions)	Per Capita ($)	% of GNP	Total Expenditures ($ Billions)	Per Capita ($)	% of GNP	Total Expenditures ($ Billions)	Per Capita ($)	% of GNP	Total Expenditures ($ Billions)	Per Capita ($)	% of GNP	Total Expenditures ($ Billions)	Per Capita ($)	% of GNP
President's Budget, 1977	394.2	1,820.78	21.37	112.5	519.63	6.10	281.7	1,301.15	15.27	137.1	633.26	7.43	5.7	26.33	0.31
Goals for 1977	403.0	1,861.43	21.21	112.8	521.02	5.94	290.2	1,340.41	15.27	138.5	639.72	7.29	6.0	27.71	0.32
Goals for Fiscal 1980	460.0	2,081.45	20.81	114.6	516.55	5.18	345.4	1,562.90	15.63	146.0	660.63	6.61	7.9	35.75	0.36
Goals for Calendar 1980	465.0	2,099.32	20.76	115.0	519.19	5.13	350.0	1,580.13	15.63	147.5	665.91	6.59	8.0	36.12	0.36

	HOUSING AND COMMUNITY DEVELOPMENT			AGRICULTURE, NATURAL RESOURCES, ENVIRONMENT AND ENERGY			EDUCATION			HEALTH			TRANSPORTATION		
	Total Expenditures ($ Billions)	Per Capita ($)	% of GNP	Total Expenditures ($ Billions)	Per Capita ($)	% of GNP	Total Expenditures ($ Billions)	Per Capita ($)	% of GNP	Total Expenditures ($ Billions)	Per Capita ($)	% of GNP	Total Expenditures ($ Billions)	Per Capita ($)	% of GNP
President's Budget, 1977	6.8[3]	31.41	0.37	15.5	71.59	0.84	7.5	34.64	0.41	34.4	158.89	1.86	14.9	68.82	0.81
Goals for 1977	7.5	34.64	0.39	16.0	73.90	0.84	8.0	36.95	0.42	36.5	168.59	1.92	15.5	71.59	0.82
Goals for Fiscal 1980	14.7	66.52	0.67	24.0	108.60	1.09	16.0	72.40	0.72	46.0	208.14	2.08	17.0	76.92	0.77
Goals for Calendar 1980	15.0	67.72	0.68	24.3	109.71	1.08	16.2	73.14	0.72	47.0	212.18	2.10	17.2	77.65	0.77

1/ Dollar goals would be higher to extent of further inflation.

2/ Includes categories other than those listed in detail, i.e. veterans benefits, law enforcement, general government, interest, commerce, other community and area development, revenue sharing, and return allowances. The goals for domestic programs allow for savings of one billion in fiscal 1977, 19 billion in fiscal 1980, and 20 billion in calendar 1980, for lower interest, lower unemployment-related costs, government reorganization, zero budgeting, etc.

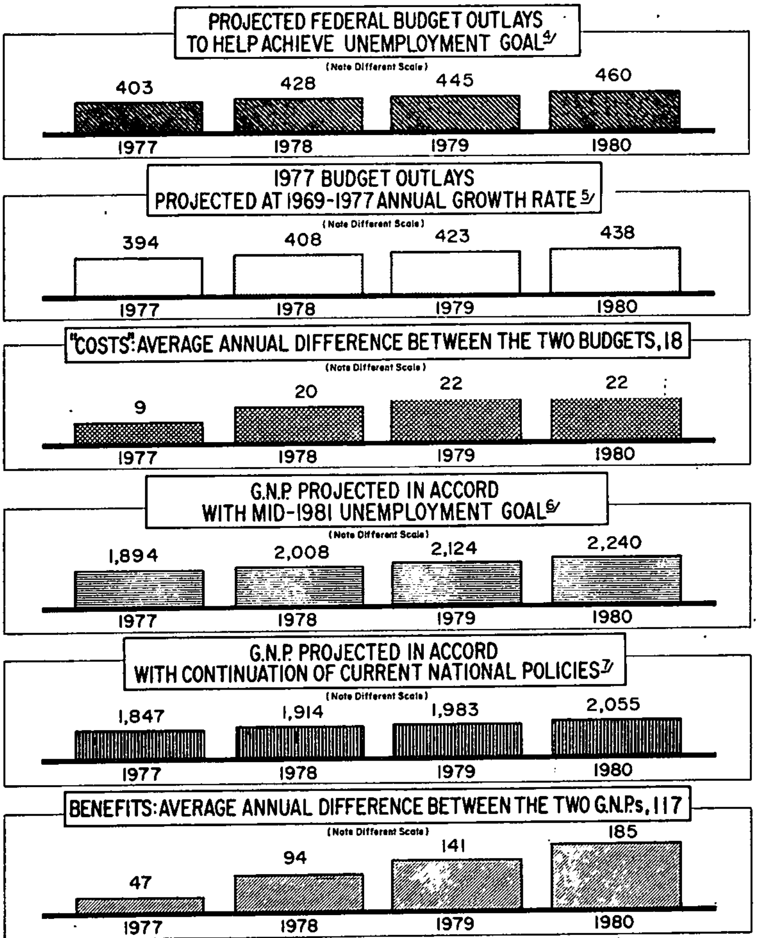
3/ The housing portion of this $6.8 billion in the President's Budget proposed for 1977, coming to $3.9 billion, appears in part in "income security" and in part in "commerce and transportation" in the President's Budget. The proposed goal increases for "housing and community development" includes $3.3 billion for housing for fiscal 1977 and $10.8 billion for calendar 1980.

Note: Population--216.5 million for April 1, 1977, 221.0 for April 1, 1980, and 221.5 for July 1, 1980. GNP (in fiscal 1977 dollars)--$1,845 billion for President's Budget; $1,990 billion for fiscal 1977 goal; $2,210 for fiscal 1980 goal, and $2,240 billion for calendar 1980 goal. Basic Data: Office of Management and Budget for President's Budget; Dept. of Commerce for population

CHART 8

"COSTS"[1] AND BENEFITS[2] THROUGH 1980, CONSISTENT WITH REACHING UNEMPLOYMENT GOAL[3] BY THE MIDDLE OF 1981

(Budget, fiscal years; G.N.P., calendar years; billions of fiscal 1977 dollars)



1/ "Costs" are difference between Federal Budget outlays needed to help achieve unemployment goal and 1977 Budget outlays projected with reasonably estimated adaptations of current policies and programs.

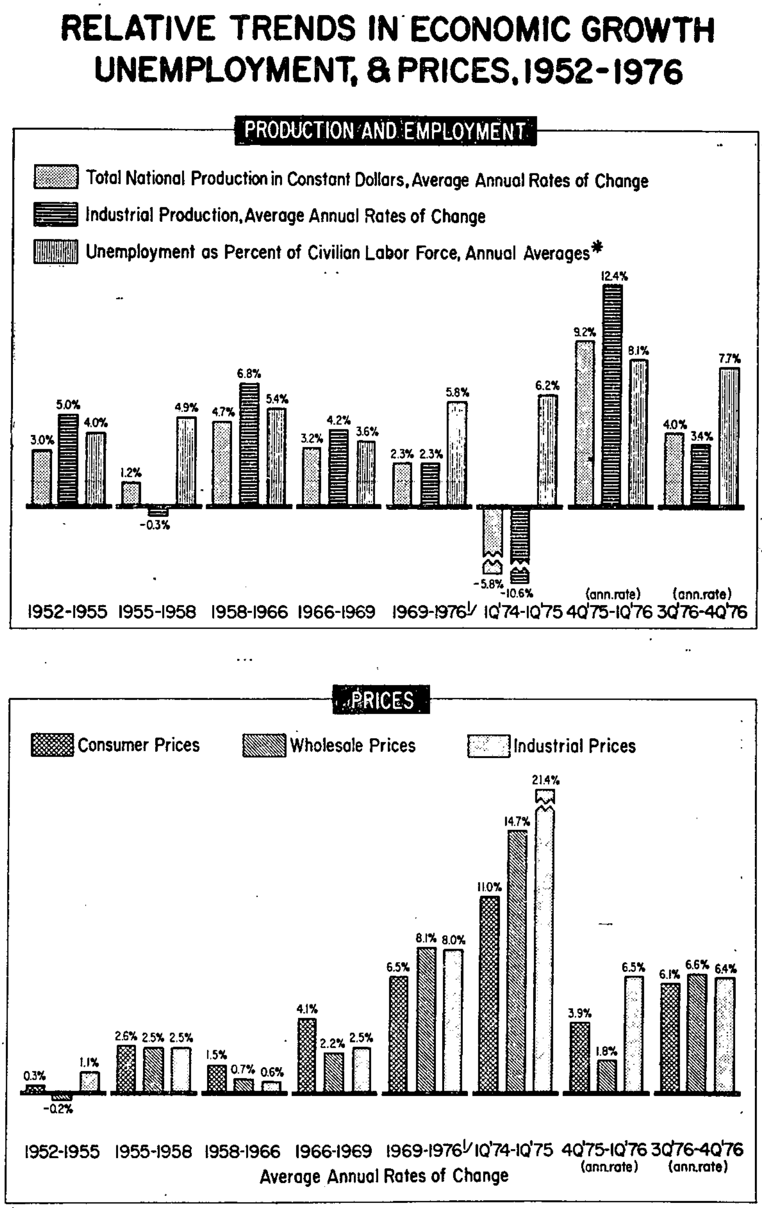
2/ Benefits are difference between G.N.P. in accord with unemployment goal and G.N.P. projected in accord with reasonably estimated adaptations of current national policies and programs. 3/ 4 percent unemployment (3.0% adult) by middle of 1981.

4/ The Full Employment & Balanced Growth Plan in H.R. 50 & S. 50 would use other policies besides those in the Federal Budget to help achieve the full employment goal. The average annual real growth rate in Budget outlays used for these projections is 5.1 percent, projected from fiscal 1976, with allowance for change in the fiscal year. 5/ The lower Budget projection is at the 3.7 percent real average annual growth rate, consistent with lower projections for G.N.P.

6/ The real average annual growth rate used for these projections is 5.9 percent, projected from calendar 1976 base.

7/ Based upon real average annual growth rate of 3.7 percent, projected from calendar 1976 base. The average was only 3.1 percent during 1953-1976, and only 2.3 percent during 1969-1976.

CHART 9



1/ All 1976 figures estimated.

*/ 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 10

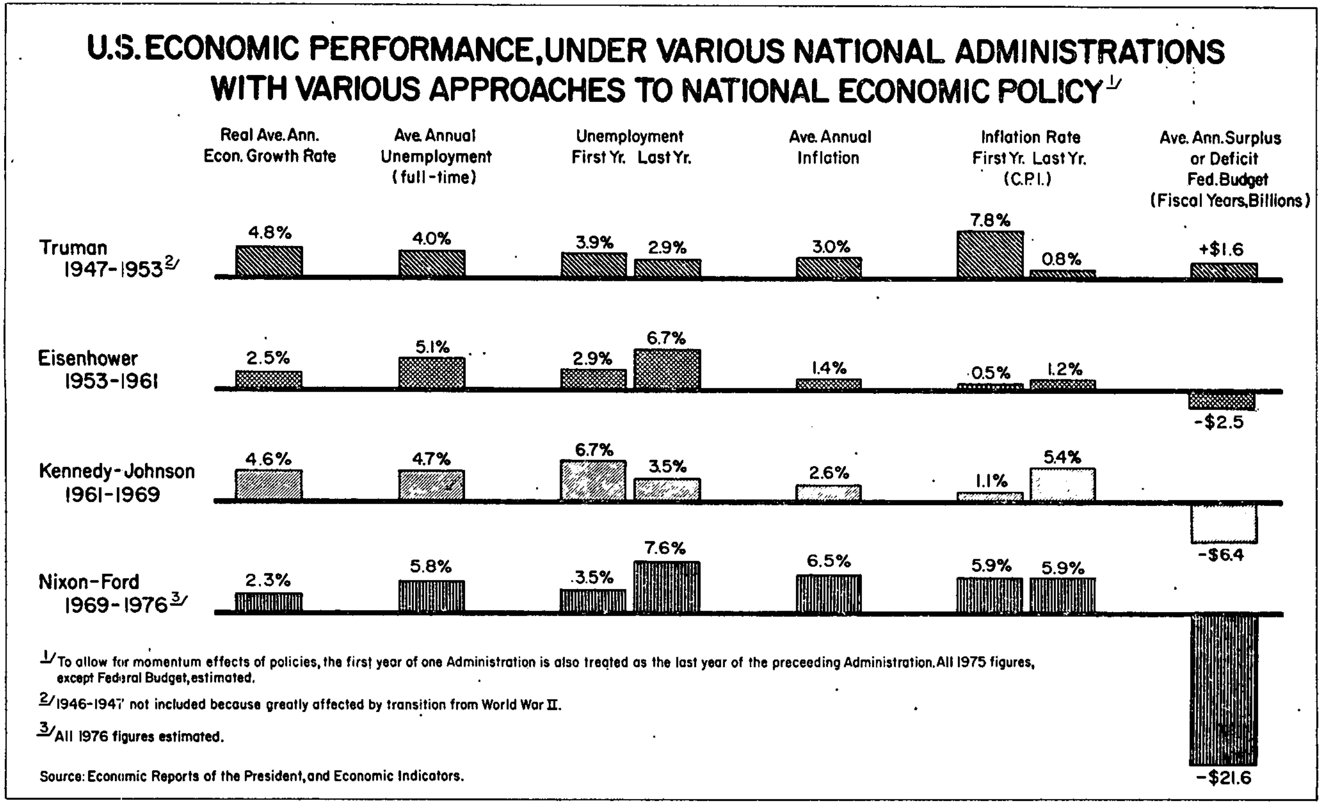
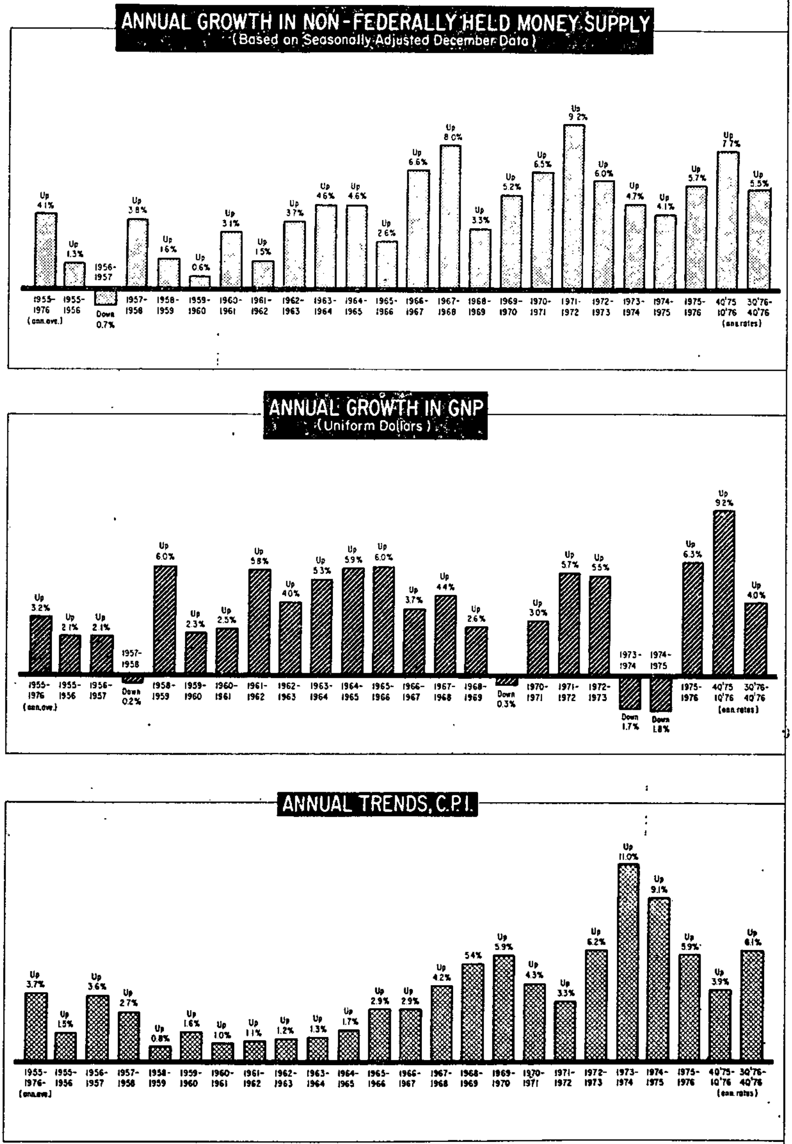

U.S. ECONOMIC PERFORMANCE, UNDER VARIOUS NATIONAL ADMINISTRATIONS WITH VARIOUS APPROACHES TO NATIONAL ECONOMIC POLICY 1/
Real Ave. Ann. Econ. Growth Rate
Ave. Annual Unemployment (full-time)
Unemployment First Yr. Last Yr.
Ave. Annual Inflation
Inflation Rate First Yr. Last Yr. (C.P.I.)
Ave. Ann. Surplus or Deficit Fed. Budget (Fiscal Years, Billions)
Truman 1947-1953 2/
4.8%
4.0%
3.9%
2.9%
3.0%
7.8%
0.8%
+$1.6
Eisenhower 1953-1961
2.5%
5.1%
2.9%
6.7%
1.4%
0.5%
1.2%
-$2.5
Kennedy-Johnson 1961-1969
4.6%
4.7%
6.7%
3.5%
2.6%
1.1%
5.4%
-$6.4
Nixon-Ford 1969-1976 3/
2.3%
5.8%
3.5%
7.6%
6.5%
5.9%
5.9%
-$21.6
1/ To allow for momentum effects of policies, the first year of one Administration is also treated as the last year of the preceeding Administration. All 1975 figures, except Federal Budget, estimated.
2/ 1946-1947 not included because greatly affected by transition from World War II.
3/ All 1976 figures estimated.
Source: Economic Reports of the President, and Economic Indicators.

CHART 11

COMPARATIVE TRENDS IN NON-FEDERALLY HELD MONEY SUPPLY, G.N.P., AND PRICES, 1955-1976 [1/]



1/ 1976 estimated.

Data: Dept. of Commerce; Dept. of Labor; Federal Reserve System

CHART 12

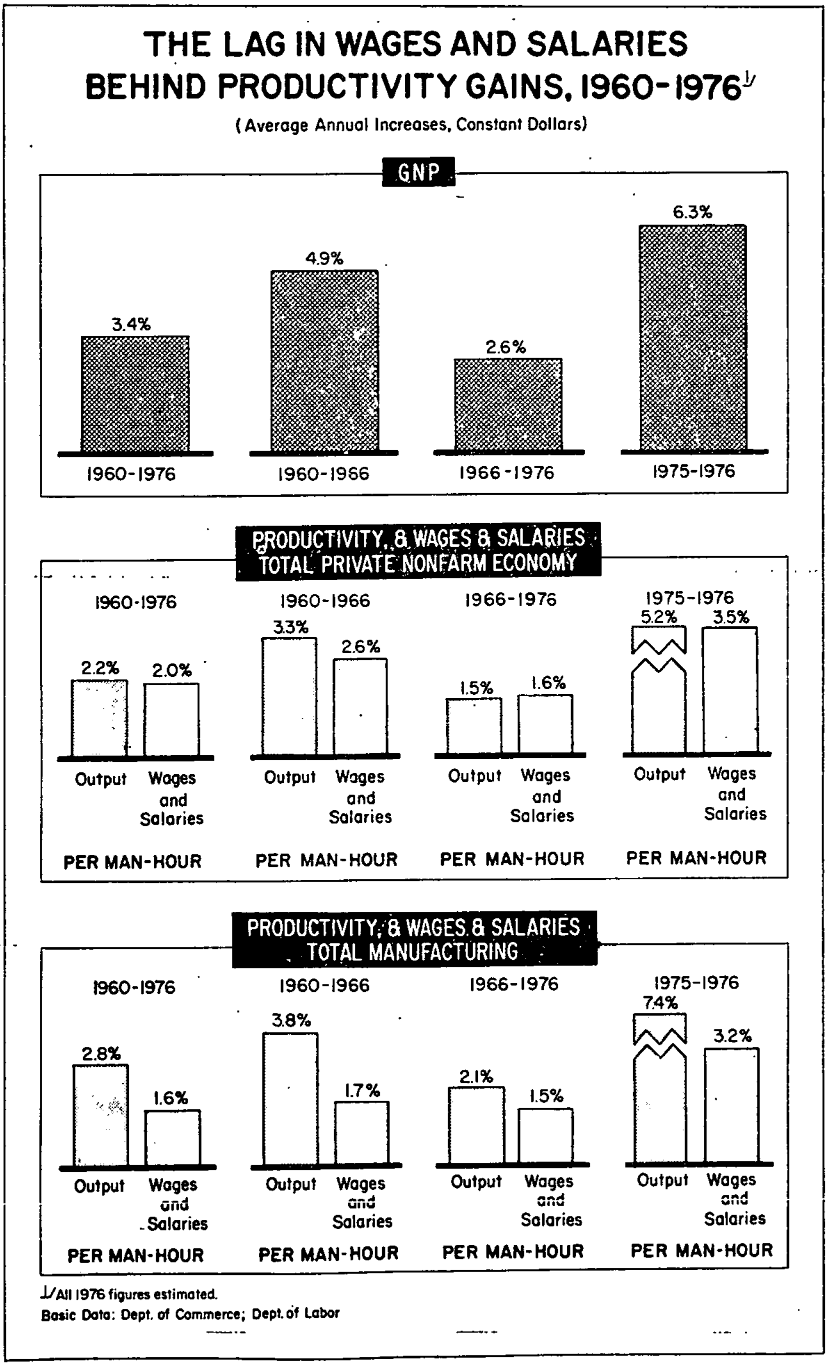
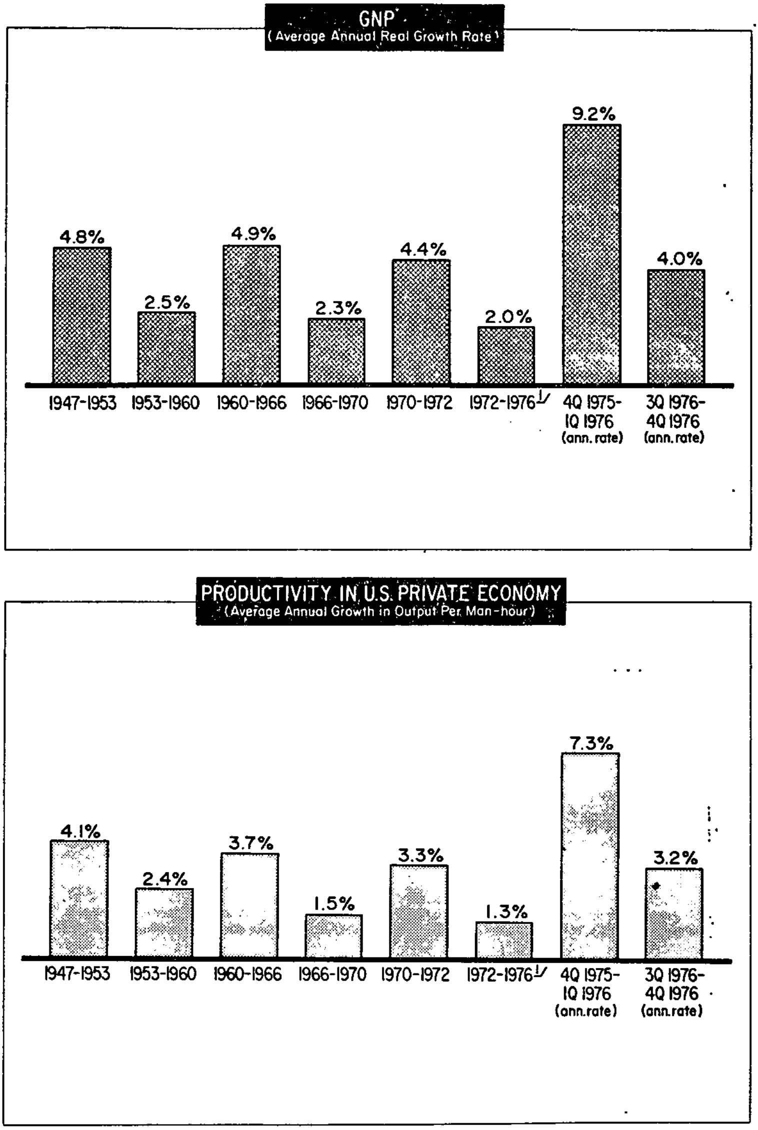

THE LAG IN WAGES AND SALARIES BEHIND PRODUCTIVITY GAINS, 1960-1976[1]
(Average Annual Increases, Constant Dollars)
GNP
3.4%
4.9%
2.6%
6.3%
1960-1976
1960-1966
1966-1976
1975-1976
PRODUCTIVITY, & WAGES & SALARIES
TOTAL PRIVATE NONFARM ECONOMY
1960-1976
2.2%
2.0%
1960-1966
3.3%
2.6%
1966-1976
1.5%
1.6%
1975-1976
5.2%
3.5%
Output
Wages and Salaries
PER MAN-HOUR
PRODUCTIVITY, & WAGES & SALARIES
TOTAL MANUFACTURING
1960-1976
2.8%
1.6%
1960-1966
3.8%
1.7%
1966-1976
2.1%
1.5%
1975-1976
7.4%
3.2%
Output
Wages and Salaries
PER MAN-HOUR
1/All 1976 figures estimated.
Basic Data: Dept. of Commerce; Dept. of Labor

CHART 13

IMPACT OF ECONOMIC GROWTH UPON PRODUCTIVITY GROWTH

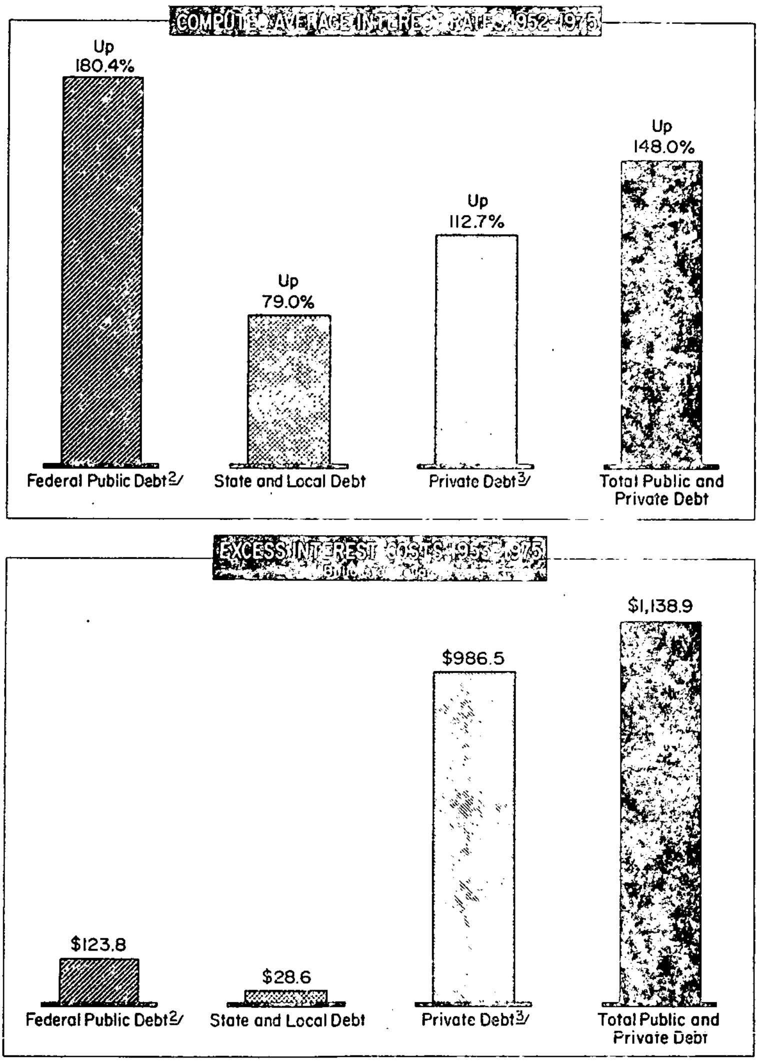


1/ All 1976 figures estimated.

Source: Dept. of Labor, Dept. of Commerce

CHART 14

INCREASES IN AVERAGE INTEREST RATES, AND EXCESS INTEREST COSTS DUE TO THESE INCREASES, 1952-1976[1]



1/ 1975-1976 estimated.
2/ Includes net foreign interest.
3/ Computed as a residual by subtracting Federal Public and state and local debt from total public and private debt.

Source: Dept. of Commerce; Economic Report of the President

CHART 15

92-625—77——10

Representative BOLLING. Thank you very much, Mr. Keyserling, for your statement.

Senator Javits.

Senator JAVITS. I wanted to say that I came especially this morning out of a respect for you and respect for my brother, Benjamin, who was an outstanding author, economist and lawyer, and literally revered you as a very wise mind, and as a unique analyzer of the American economic scene, years and years ahead of your time.

I have to go to the Senate to a number of very critical hearings, but I wish to just record that I will study everything you say in the greatest detail, and from a cursory examination, I believe the alternatives for development to the President's package are very strongly supported in many parts by your analysis of the situation.

Thank you.

Mr. KEYSERLING. Thank you very much, sir.

Representative BOLLING. Thank you, Senator Javits.

Congressman Pike.

Representative PIKE. Mr. Keyserling, I always enjoy your statements because you have the ability to inject a little humor in them, which we seem to find so absolutely lacking in our own debates all the time, and you also make pretty good points.

I don't understand, however, the scorn with which you apparently hold the G-string. Why is the G-string a lesser string than any of the other strings?

Mr. KEYSERLING. I would modify my statement by saying you need to play on all four.

The G-string is a little dull. I am a little more moved when I hear Jascha Heifetz on the E-string, but that is a personal preference.

My main point is that you need to play on all four strings.

REPRESENTATIVE PIKE. Fair enough.

I am very interested in your conclusion that the jobs part of the package should be directed to, in your words, "marginal assistance to job expansion in the private sector," and I feel very strongly that we have to go the route of jobs in the private sector, but I would like you to be more specific as to how you would structure the marginal assistance to job creation in the private sector.

Mr. KEYSERLING. Well, first of all, I take the heretical view, despite the importance of jobs, that we must also ask the question, "What do the jobs create in terms of what the economy and the people need?"

Taking an example, I fly the flag at the customary adherence to private enterprise very genuinely. My studies have shown that 80 to 90 percent of the new jobs which should be created between now and 1980 should be in the private sector, but we need another guideline.

I believe there is a derogation of the function of the Government, the function of our system, the function of the Congress itself, to say that the stimulation of the building of another cigarette plant is preferable on any ground to the building of another hospital with public gain. Until we have that economic analysis, we could have a country where wealth accumulates and people decay.

Next, I want to emphasize the technological factor. I am amazed that economists after 25 years have not asked, "Can we, even if we wanted to, get back to a healthy economy unless we change the patterns of production and employment."

We can't. The automobile industry employs 300,000 fewer people in auto production than it did a number of years ago when it was producing several million less cars.

Private industry as a whole, and I am not saying this critically, but because of the rate of technological change, has been in a chronic reduction of total employment.

We have more challenge in terms of needs still unmet adequately, to move more people into the service industries, into the health services, into education, into energy production, into environmental improvement and transportation, and this would have conservation as well as productive results, and it happens that the rate of productivity growth is relatively low in those areas, and therefore you get more jobs for each unit of increase in GNP.

We are in trouble now, but we will always be in trouble if we continue in the way we are going. We are not going to get out of this trouble just so. I think the package may stimulate things a little bit, and bring us down to 7 percent unemployment for a while.

That is not good enough. Then we will go up again and then down again. These are the fundamental problems with the economy, and they are not beyond the range of economists and not beyond the range of a great Congress and a great executive branch dealing with the problems of a great nation.

That is what we need to take into account with respect to the jobs problem. When we do that, we will find that four varieties of approaches are desirable. First, a major stimulus, which is foremost, stimulus of conventional private employment, across the board. This requires changes in monetary policies, changes in fiscal policies, and they should all be identified and pursued, but we have to have a set of goals as to what kind of distribution of employment you are shooting toward before you find the policies. That is category No. 1.

Category No. 2 is private jobs of a nonconventional nature that require some Federal aid. A good example of that is housing.

You can't get an ample housing program to meet the needs of all groups, to rebuild our cities, to keep up an adequate volume of home construction as it relates to the economy at large, without Federal assistance.

The other example is energy. Another is food supply.

Representative PIKE. Let's take energy. I think everybody in America is looking for some sort of breakthrough in the realm of solar energy, but how do you structure the aid, the marginal Federal aid that you are talking about, to put or to help the development, say, in the private sector, of solar energy or any energy?

Mr. KEYSERLING. I want to confess my noncompetence in some areas as well as my competence in others.

I don't come up here with the structure for a stimulus program for energy. I don't know.

Representative PIKE. That is the difficulty we are in. I don't have any trouble agreeing with anything you say, but we have the job of trying to decide how we do these things, but if we are going to take energy and we want to develop more, are we going to give additional benefits to the oil companies, for example, to develop solar energy?

Mr. KEYSERLING. Let me state it this way: My proposition is that a large part of the Federal assistance should be marginal Federal assistance, the expansion of private activity. If you ask me how we should structure it in housing, I could give you all the details you want, because I have studied that problem for many years.

I have recently put out publications on it. I put out a book in 1972 called "The Coming Crisis in Housing" and if the Government had listened to it, instead of not even including housing, while they played the Stradivarius violin on the G-string, we would be better off now. I could do it in mass transportation.

Representative PIKE. All right, do it in mass transportation.

How are we going to create jobs in mass transportation in the private sector?

Mr. KEYSERLING. Let me give the example I am most familiar with.

I spent 8 years opposing the Penn-Central merger. I opposed it, also, before the Supreme Court of the United States, as well as before the ICC.

What was my argument? Not that I am against big business—I said I don't care if there is only one railroad in the country if it will meet the transportation needs of the country consistent with a healthy and strong economy.

I opposed this merger because the philosophy of scarcity, which has entered into our economic thinking, was the merger proposal.

They were going to save $67 million and save themselves from bankruptcy by cutting out communities, by cutting out passenger traffic, by carrying only what they considered the most lucrative traffic.

I said, you put the imprimatur of the Federal Government on this, and it will be a farce.

There was a Government interagency committee set up to consider that merger and other rail mergers. It came to nothing. They were afraid to make a decision. They said, "That is the business of the ICC."

It can't be. It is perfectly feasible to compute, and I am not prepared today to give the statistical sides of every detailed program, but I am talking about a method. It is feasible to compute how much rail transportation we need in broad outlines, and it will require marginal Federal assistance, whether 5 percent or 10 percent is a relative detail, and it is not hard to structure.

Representative PIKE. Wait right there. It is not hard to structure, you say. There are railroads in the country making money and there are railroads in the country that don't make money.

Do you give the 5 percent to all of them?

Mr. KEYSERLING. There are farmers in the country who are making fortunes and farmers in the country going bankrupt and driven into the cities.

This is no reason we can't have rational farm support programs.

Representative PIKE. So, you give the money to all of them?

Mr. KEYSERLING. I didn't say that. You may apply criteria as to which ones you give it to, but that is not what I am testifying on now. I can give you a detailed breakdown of the farm area of how much farm production we need, of how much the Government should spend, and to which farmers it could go to. I can give you all the details.

The point I am making now is that the economic program by the economic staff of the President, and the President's message, which ignores all these things and does not begin planning on this basis is derelict. I have no appreciable staff. They have large staffs. They have recourse to every agency of Government which they could ask for continuous studies from.

I don't have to be able to detail. Frankly, I think that is a burlesque of my testimony, to say that I have to be able to detail a solar energy program in order to validate my theories.

Representative PIKE. It seems to me you are getting a little defensive here. I have tried to ask you to do that which you said you would do, which was to give us the structuring of a mass transportation program in the private sector.

Mr. KEYSERLING. All right.

I will not do it here today, but I will send you a massive, detailed study which I made at the time of the Penn-Central fiasco, which gives you everything you ask for, how much trackage we needed, where we needed it, how much Government assistance we needed to do it, and so forth and so on.

I have done it. I can give it to you. I will send it to you, and I have done the same thing in agriculture.

Representative PIKE. Fine. Thank you.

Representative BOLLING. The burden of what you are saying is that we need to plan our Government program policies and expenditures a little bit better?

Mr. KEYSERLING. Absolutely. Absolutely.

Representative BOLLING. In other words, if I understand you, what you are saying is that we need to have a specific set of plans dealing with the shortages that exist in terms of goods and services.

Mr. KEYSERLING. In terms of the shortages, in terms of national needs, in terms of a goal for the reduction of unemployment, which last, I think the Congress must set.

I don't understand how the Congress determines how many war planes we need, but says the fundamental economic and social and political question of whether we should have 3 or 5 or 7 percent employment should be left up to the executive branch economists.

Yes, I think we need those things.

Representative BOLLING. And what we need in energy is a plan that approaches the set of the problems and tradeoffs that exist, and if there is an area in which the Government needs to play a significant role in order to achieve or encourage the achievement of those goals, that it would then participate?

Mr. KEYSERLING. We certainly do, and we need to pay some modest attention to empirical evidence developed in the great laboratory of the $1.8 trillion American economy, instead of continuing to use shibboleths to bankrupt our policy.

Representative BOLLING. Let's take one example that deals with solar energy.

One expert, Barry Commoner, has said that if we committed $100 million investment in solar energy, we could break through the difficulty of achieving effective and useful results in a relatively shorter time than would otherwise be the case, and that since the technology is so complicated and difficult and relatively undeveloped, I suppose you would have to say that unles it were a public committment, solar energy would be knocked out in a competitive sense since other forms of energy increases can be developed in different ways, not necessarily more expensively or less expensively, but this requires a tremendous front-end investment.

Are you suggesting that there ought to be a deliberate, conscious attempt when we deal with energy policy to deal with anything as massive as that in terms of tradeoffs, or should we continue to do what I think is really the thing that you are complaining about, tinker with the bits and pieces in such a way that we end up with a policy that is not realy a long-range policy in any sense at all?

Mr. KEYSERLING. I think your question enables me to answer better the question asked by your colleague, and if anything I have said was inadvertententlly defensive, I offer my profound apologies.

Representative BOLLING. I don't think you were defensive. He may have felt you were not answering the questions.

Mr. KEYSERLING. Well, anyway, let me say again that in one sense I can't answer your question, and in one sense I can.

I am not technically equipped to evaluate the relative significance of a particular energy approach that you have outlined as against others. But I am prepared to say that, insofar as it is a serious, competently offered proposal of a broad and general nature, and I must assume that it is because of your interest in it, is should be given full attention, although I am not personally equipped to deal with it in detail.

Of course, it should be considered in the course of developing a comprehensive, long-range energy proposal instead of tidbits, and I think what is now talked about are excessively tidbits, and likewise what is done with the energy component should be done with the other major components.

This is not an undoable task. We have done this in the past.

During the Truman administration, we made fairly good models of requirements of needs in various sectors of the economy.

We used them as guides to national policies—the Government's policies. These have so profound an effect upon the overall economy, through tax policy and money policy and others, that I think you get a very good overall adjustment if you use those in the right way.

So, I would say to answer your question, yes, I believe that this approach should be considered and blended into the consideration of the energy problem.

Representative BOLLING. You mentioned more or less in the past that the United States had been able to accomplish national goals in a war which were really no more difficult goals than the kinds of goals we should be accomplishing, in effect, now.

Mr. Roosevelt said something about 50,000 planes a year, and everybody in the United States laughed at him. So, it might be that the point is valid.

Maybe we should really expect the Government to take a look at energy in much broader terms than it does, and deal with it.

I suspect that you are right, we must begin to look at these things in the large sense in terms of need, since we are now in a period of, if not acute shortage, some shortage, and acute misuse of energy resources.

It would seem to me that what you are suggesting, if I understand it correctly, maks a lot of sense.

I have a whole series of questions and most of them, don't really fit into the pattern that you have in mind.

You talked a little bit about your attitude toward inflation, and the points that were favorable during the years when you were Chairman of the Council.

You talked about a particular kind of approach. Could you give a little more detail in how you think the Government should be structured to deal with inflation?

I gather you mean largely by voluntary deed and perhaps structured kind of jawboning, and so forth.

Mr. KEYSERLING. I regard that as important in the last element I am talking about now.

Before we can deal effectively with inflation, you must determine its source. This is going to be subject to human fallibility, but we can do a lot better than we have done, because the prevalent analysis still is that inflation is caused primarily by a low level of unemployment, and a low level of idle plant use.

Now, so long as that theory prevails, we are going to continue to have policies, even as the President's new proposals—and many before—founded on that approach, and, therefore, deliberately costing us enormous losses in production and employment and Federal revenues as an alleged cure for inflation.

What I am saying, and I want to point out that I have brought this booklet in advocacy of the Humphrey-Hawkins bill; I brought it—not for the printed record—but as an economical way of introducing certain charts in it. These same charts appear in my prepared statement.

I have a large number of charts here that show not only during the Truman administration but during many other periods—there is really endless information.

I will first call attention to the chart on page 41, of the booklet. There is not time to read it fully here.

Representative BOLLING. Let's try this one.

I would like to be sure your view is in the record on this, your full view on how to deal with the problem of inflation, or at least a substantial outline.

Mr. KEYSERLING. I will do that.

I think first you have to discard the notion of a tradeoff, and it is interesting that there is not a single economist faced with the chart's analysis that I have shown on this subject since 1954 who has brought forth competing empirical evidence—not a single one.

The theory is accepted without empirical study.

Mr. Schultze is a competent economist, but the best thing he can say about the causes of inflation in his most recent testimony is that it was preceded by momentum.

I want to know what that is, and what do you do about it. The momentum of what, the worst recession since the Civil War, the momentum of three quarters in which we have stagflation?

Now, the first real cause of more inflation when you have a high amount of idle resources in that productivity growth goes down so far that wage trends exceed productivity trends.

That is shown on two of my charts here.

When the economy moved toward full resource use, wage trends lag behind productivity trends. Therefore, getting back to full resource use brings about a large acceleration in productivity, and this demolishes the problem of wage-push inflation, which has become not a legitimate concern so much as an overwhelming obsession with so many economists.

So, the first thing to do in fighting inflation is to get back to fuller resources.

We live in an administered price area, largely, and not a supply-demand area. We were taught in school that if you are selling 10 apples and there are 11 buyers the price goes up; if there are 9 buyers, the price goes down. Not if the seller controls the apples, and the buyer needs them. The seller raises the prices, because that is the way to try to meet costs and maintain profits despite inadequate volume.

There are published studies on all this over the years, much of them submitted to this committee, and I could support my many studies with some excellent ones by Gardner Means, one of the best economists in this field.

I am supported by a recent study made by the Joint Economic Committee itself. There is not a single competing study. Try and show me the opposite.

They raised their prices faster in steel recently, in automobiles recently, and recurrently through the last 25 years, when plant idleness is high and unemployment is high, first, because their costs are high due to low productivity growth, and second, they have a profit target, which they want to reach despite the inadequate demand in a seriously lagging economy.

They raised their prices less when the economy was in good shape.

Therefore, other volumes should be coupled with a more direct and meaningful antitrust and anti-monopoly program, which I think should take the form——

Representative BOLLING. We have been talking about that for I don't know how many decades. We never seem to get it.

How do you get more effective antitrust?

Mr. KEYSERLING. You get it by doing it.

You get it if the Department of Justice proceeds in that area. I think more important is the national incomes policy, which I am very much for, and which I think can be, on a voluntary basis——

Representative BOLLING. Did you you say "can be" or "can't be"?

Mr. KEYSERLING. Can be and should be, provided it is not what the President is talking about, and not what Kennedy and Johnson did, and not what Nixon did. It has been limited solely to trying to prevent price-wage increases which are inflationary, but giving no concern to the larger problem as to what kind of wage-price trend will meet the investment needs of business and the needs of the consumers.

We have let legitimate concern about inflation distract us from other things we need to do much better than we have been doing them. We could stop inflation by making a desert island of America.

So, I believe in a stronger antitrust policy, but far more important, I believe in vigorous voluntary use of genuine national income policy, which we have never had.

Representative BOLLING. Describe one in brief.

Mr. KEYSERLING. All right, I will describe it by starting with a model that I am talking about: What are the goals for the reduction of employment?

What are the goals for GNP?

What are the broad contours of Government outlays, private investment expenditures?

What are the income flows that are compatible with the support of these contours?

If you don't have that, you can't do anything. You are flying blind, because every national economic policy affects that, and you either affect it without knowing why and in what direction, or knowing why in what direction.

Once you have that, you can use your tax policy and the money policy and the national incomes policy toward the achievement of the related balanced growth.

We did it to a degree in the Truman administration, and we did it during World War II.

I must say that I find no merit in the arguments, "Oh, that was wartime." The American people think that, when I say we should do *some* things as in wartime, I mean *all* things, including all of the controls.

We didn't have unique controls and taxes in World War II because of planning, but because the planning revealed that only half of the produce was distributed to the people, and the other went into war materials. We have a defense program associating only 5 to 6 percent of the national product now.

But the idea that we should put programs together and make them mesh, and consider long-range factors, and draw a national incomes policy and tax policy and so forth in terms of these related goals, it is just as applicable now as in wartime.

Representative BOLLING. In very simple terms, tell me what a national incomes policy is.

I think I know.

Mr. KEYSERLING. It is applying to wage and price trends the analysis which will enable them, along with other policies, to contribute to full employment and full resource use, and not create excessive inflationary purchasing power.

Representative BOLLING. How do you then deal with the problem of investment?

Mr. KEYSERLING. The problem of investment?

Representative BOLLING. Obviously in some cases you deal with investment by enormous infusion of Government money, which, again, to use your wartime illustration, is perfectly valid.

We weren't going to get planes if it were based on profit, because the profit wasn't going to be there until the Government spent money.

Mr. KEYSERLING. How you deal with investment is in two parts. The first part I would say, the goals for capital formation, is one of the guides to national policies. There must be an overall target for investment.

Representative BOLLING. Overall and by sector?

Mr. KEYSERLING. I would not break it down into too many sectors, but that is a matter of degree. After all, one of the problems with the investment tax credits and the other concessions to investors is that they don't break it down by sectors.

That is another problem that I will be glad to discuss, but at least I would have the overall goal. With such goal or goals, we would be able to consider whether we need a tax concession to investors more or less than we need a tax concession to consumers, because we would have something to measure this against.

I have a chart here which shows analytically and quantitatively where the discrepancies have occurred, tracing all the way through the various business cycles, and it can be done.

If what I suggest had been followed, the national policies would have been based upon empirical analysis and more successful.

This really raises a problem of availability of capital. Let me state it as axiomatically as anything can be in economics that there is not really a problem of availability of capital for the large investors. The small business problem is a different problem. Sometimes the unavailability of capital is stated by saying that, if the Government undertakes a larger amount of borrowing, or of capital supply, and you can use different terms, through increasing the deficit in the budget, then there is not enough capital left over for private capital investment and that this cramps economic growth and also causes higher interest rates.

Suppose we said that in World War II?

We would have been in the German salt mines. Capital is not tangible or real wealth like oil and steel and human power. Capital is produced by the money system, and it is the function of the Federal Reserve Board, if and when the Congress and the President decide that more capital is needed through the public budget, to provide enough capital and a money policy which services both the policy of the Federal Government and private capital needs.

If the Fed acts counter to this, as it has done many times in the past, in the view of many economists, if it acts counter to this, then it can frustrate the Government's policy by not creating enough capital.

Even beyond that, as axiomatic as anything in the American economy, is the proposition that when the American economy is doing well, the operation of prices as they operate and the profits as they operate, produce a super abundance and not an inadequacy of private capital for investment.

Every boom has shown this over and over again. It is accompanied by several times as much real growth in capital investment as in the ultimate demand of consumer buying plus government outlays; the resultant imbalances are stagnation and recession.

So, the only inhibition on capital availability now, or investment now, if there is any, is not that prices are not high enough, not that her unit profits are not high enough. It is not even that aggregate prices are not high enough; they are breaking records. The inhibition on capital investment now is 80 percent plant use and 8 percent idle human resources and a $250 billion GNP gap.

When we start taking care of that promptly and adequately, the capital investment will be forthcoming. It always has been.

Representative BOLLING. Thank you.

Congressman Pike.

Representative PIKE. Mr. Keyserling, it is my understanding that Arthur Burns, in several appearances before this committee and other committees of the Congress, has expressed the view that at the moment the major danger, again, is not unemployment, but inflation.

Would you care to comment on that?

Mr. KEYSERLING. Yes, sir. I am going to be a little humorous at the end, because the Senator indicated that he appreciated that.

I say this in all sincerity. I was in Government for 20 years and I was Vice Chairman and then Chairman of the Council of Economic Advisers for more than 6 years.

During the Truman administration, our entire policy was founded on calling forth the great new secret weapon of the American economy, which is our unrivaled power to turn out goods and services at full employment and full production and optimum real economic growth. In fact, we built the whole concept of an expanding economy and adequate growth into the popular thinking. That is how we got 2.9 percent unemployment and 0.8 percent inflation by the last year.

That was our foremost and first approach. We didn't listen to those who said that inflation was a greater danger to us than the aggressors, and that we should accordingly smother or restrain real economic growth in accord with our full capabilities.

Now, I don't want to criticize any individual, but I think the Government needs a Department of Experience more than it needs any other kind of Government reorganization.

Arthur Burns has been here a long time. He came in as the Chairman of the CEA under Eisenhower. He had inherited an inflation rate of 0.8 percent, but he got so worried about inflation that he helped to tighten up the budget and the money supply, and he ended up moving toward 6.7 percent unemployment by 1961, and 2.5 times as much inflation as existed when he came in.

This is what the Department of Experience would reveal.

Arthur Burns came in again with President Nixon as his economic adviser in the White House. He pushed the same kind of policies. We then got the rare combination of unemployment and inflation that we have had with virulence.

Arthur Burns as Chairman of the Federal Reserve Board, has done nothing effectual to check the chronic rise of inflation. To the contrary, extraordinarily high interest rates, and the severe shortages caused by the Fed's policies are highly inflationary in themselves.

Arthur Burns has been subjected, not only by liberal economists like me, but by conservative economists, to the charge recurrently that he was acting contrary to the Government's stimulative policies, with very bad consequences.

I have a chart here that shows the trends in the consumer prices, the trend in monetary expansion and the trends in a real GNP. This chart demonstrates that every time Arthur Burns or his predecessor, Bill Martin, tightened up on the money supply to stop inflation, they usually got more inflation, they got lower economic growth, they got more unemployment.

It is all in here.

Now, I say that the time has come, after all these years, to judge people by the results of their policies, and not by their capacity to answer questions.

These are the results of the Burns policies.

Representative PIKE. Mr. Chairman, I think that the time might well have come to have both of these esteemed gentlemen here at the same time.

I think we could have a marvelous hearing.

Representative BOLLING. Let me ask you one thing that I should know the answer to.

Mr. KEYSERLING. Let me just say this: If my policies, when I was in the Government, had produced the results that Arthur Burns has produced, I would have been tarred and feathered and driven out of Washington on a rail, because I got enough brickbats despite the success of the policies.

Representative BOLLING. Since 1951, and having followed up on the Douglas subcommittee that in effect, I guess, had something to do with causing the accord between the Fed and the Treasury, I wonder, in looking back, if you approve the idea of that accord?

Mr. KEYSERLING. I am glad you asked that question.

I think in 1951 Mr. Mariner Eccles, who had started out as a progressive banker during the New Deal, and became a troglodyte, as was the case with some other people, he began agitating that the monetary policy of having the Federal Reserve support Treasury bonds, and the consequent moderate interest rates were an "engine of inflation"—that that monetary policy during World War II was an engine of inflation.

But the real engine of inflationary pressures was the war itself. Before we really had any Fed, and again in World War I, when we had it, war periods had been highly inflationary.

It is true that in the 1920's we had high interest rates, though not as high as recently. They were very damaging to the economy. They were a large factor in what happened. The policy of the Federal Reserve, when the "Great Crash" started, accentuated it a good deal.

During the early depression years, interest rates didn't go down very greatly, because interest rates are made in Washington. The Roosevelt administration came in, and interest rates came down drastically across the board—money generally. I regard that as one of the most important economic performances—and I include social performances—of the New Deal.

We went along that way until 1951. We financed the prosperity of the Truman years and the Korean war with low interest rates.

Then the agitation started. The bankers wanted higher interest rates. The insurance companies wanted higher interest rates. They had the phantasmagoria ideal of an "independent" Federal Reserve Board.

Why should a Board that regulates money, the use of the people's money, be more independent than the group that determines how much taxes we pay or what prices we pay and what wages we receive during wartime?

No other modern economy in the world has anything like that, and we never had before 1951. We never had it under Harding or Coolidge any more than we had it under Wilson or Roosevelt or Truman for most of the time—the concept of an entirely free-wheeling Federal Reserve Board.

Later on, in 1952, hearings were held before the Joint Economic Committee on the "accord." President Truman had earlier appointed a four-man committee. It was made up of mobilizer Wilson, Treasury Under Secretary Martin—Secretary Snyder was in the hospital—Federal Reserve Board Chairman McCabe, and myself. I was on that committee.

President Truman was very much against the change in the money policy. But this was one of the very few instances where he lost command. I was hardly kept informed as to what was going on. So, the accord went into effect.

Then I testified in 1952—and this is a question—I testified before the Joint Economic Committee and I got into a 2-day famous debate with Senator Paul H. Douglas, who was a great liberal on civil rights and a great man on various other matters, but in his basic economic thinking in many respect he was of the "Chicago school."

So, he took me to task on this great inflationary engine of moderate interest rates, and he favored the accord.

We disagreed. The debate got pretty rough. He said to me, "Mr. Keyserling, you haven't studied the most elementary economic textbooks," and I said to him, "Senator Douglas, you haven't looked at any of the more advanced economic textbooks."

It went on 2 days, and the Washington Post said that this was a battle between two giants and neither won nor lost.

Around 1962, my wife asked him to speak before the Women's National Democratic Club, of which she was president. He had the grace to say to the audience "Leon Keyserling and I had a big argument many years ago. I will now say that he was right and I was wrong."

Representative BOLLING. That is a good point to end it on.

Anything you wish to supply for the record, we will be happy to receive.

The committee stands adjourned for 10 minutes.

[A brief recess was taken.]

Representative BOLLING. The committee will come to order.

Our next witness this morning is Mr. Bert Lance, Director of the Office of Management and Budget.

Mr. Lance, we are pleased to have you with us this morning and we welcome you to the Joint Economic Committee.

As you know, this committee is charged with reporting to the Congress our evaluation of the economic outlook for the coming year. This year, the economic report of the outgoing administration together with the new administration's stimulus package, and just this week President Carter's proposed revisions of the 1978 budget are all central to our concerns here. We welcome you here this morning Mr. Lance, and we are looking forward to your statement.

STATEMENT OF HON. BERT LANCE, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET, ACCOMPANIED BY DALE R. McOMBER, ASSISTANT DIRECTOR FOR BUDGET REVIEW

Mr. LANCE. I am delighted to have this opportunity this morning. I have been looking forward to an appearance before this committee. I have not previously been privileged to appear before you.

I have a prepared statement which I would like to read. Let me quickly go through it. It is not very long.

The Congress, especially the Budget Committees and the Appropriations Committees, has a very tight schedule for acting on the budget and we have done everything we could to review the budget quickly. Because of the need for speed, we have not had time to review all tax and spending alternatives in depth. Moreover, many new proposals that the administration will want to place before the Congress will take more time to develop than we had for revising the 1978 budget.

While we have had to build on President Ford's budget, the changes we have made are significant. As you review our brief document on budget revisions, I think you will see how significant the changes are.

The revisions in the budget have added $6.2 billion to 1977 outlays and $19.4 billion to 1978 outlays. I would like, if I may Mr. Chairman, to place in the record at this point a table that shows the major categories of increases.

Chairman BOLLING. That will be done.

[The table referred to follows:]

BUDGET REVISIONS

[Fiscal years; outlays in billions of dollars]

	1977	1978
Fiscal stimulus	5.1	8.0
Restorations:		
For fiscal stimulus programs	.2	2.8
For other programs	1.4	5.0
Initiatives and program changes (net)	.2	2.6
Reestimates	−.7	1.0
Total revisions	6.2	19.4

Mr. LANCE. It is important to note that the unified budget deficit drops by over $10 billion between 1977 and 1978. We will need to speed up the rate of decrease in order to meet our goal of a balanced budget by 1981. At the same time, we need to get the economy moving. That is essential to achieving a balanced budget. Therefore, the President feels very strongly that his economic stimulus package—a large part of which affects only 1977 and 1978—should receive rapid action by the Congress.

The Chairman of the Council of Economic Advisers and the Secretary of the Treasury have appeared before this committee to discuss the stimulus package, so I will not go into its composition in detail. You will recall that the major items in the package are $50 per person in tax rebates and payments, business tax incentives, accelerated public works, expanded public service employment and job training programs, and expanded countercyclical revenue sharing.

A few refinements have been made in the stimulus package recommendations since they were originally presented. First, we would like to see the additional countercyclical revenue sharing begin in April, and this will require slightly higher funding than we had originally proposed.

Second, we want to change the standard deduction to a flat $2,200 for single persons and $3,000 for joint returns. Our initial proposal was for a $2,400 flat deduction for single people and $2,800 for married couples.

In addition to the economic stimulus package, we are proposing to extend the temporary tax reductions that would otherwise expire.

We believe that this stimulus package will give us a better rate of economic growth than would otherwise occur so that by the end of the year, real output of goods and services will be increasing at an annual rate of about 6 percent. This, of course, will help to bring down the unemployment rate. Both real economic growth and the decline in unemployment are somewhat greater than forecast in the January budget, while the inflation forecast is virtually identical.

The forecast does not reflect the effects of the severe cold weather recently experienced in part of our country or of continued drought in the West. When the effects of the weather can be more accurately estimated, the economic outlook will be reassessed. It now appears, however, that the overall adverse effects of the severe cold weather will be relatively moderate and temporary, and that real economic activity by the end of the fourth quarter of this calendar year will have recovered nearly all the ground lost due to the cold weather.

Moreover, generalized fiscal stimulus is likely to be of little help in reopening a plant that is shut down because supplies and raw materials are icebound hundreds of miles away, or needed natural gas supplies are not available, or irrigation water supplies or hydroelectric power are not available. To the extent something can be done about weather-created economic dislocations, we need specific targeted measures, not generalized stimulus, to deal with the problems.

President Carter will be working with the Congress on major tax reform. That is an important reason why most of the stimulus package is temporary. We need to work now on getting the economy moving, but we need time to work out the details of tax reform.

We have tried to take a similar approach in reviewing much of the budget. That is, in cases where we believe that serious problems would result from the recommendations of the previous administration, our recommendations remove those features. At the same time, we are trying to reserve the flexibility for the future when we will have more time to develop program alternatives.

In the defense area, for example, we are reducing the budget authority requested by nearly $3 billion. In most cases, we are slowing down the rate of planned activity or we are putting off the start of new activity, so that we can make sure that the defense programs we support are essential to national security. We have also recommended some initial efficiency moves that will save money but not impair the effectiveness of our national defense.

We are recommending some important changes in the natural resources and energy area. We want to accelerate the energy conservation and oil storage programs. We want to cut back somewhat the very high rate of growth proposed in the Ford budget for energy research and development, particularly in the nuclear area. We are also recommending more money for sewage plant construction for 1977—roughly $5 billion rather than the $1 billion in budget authority requested last January.

We are amending the budget to request no funding for 19 water resource projects that were included in the January budget. These projects appear to be environmentally damaging, economically unsound, or have potential safety problems. We are currently reviewing all water projects with potential adverse effects. At the conclusion of this project-by-project study, we will forward to the Congress any additional budgetary changes that may be required.

In the transportation area, our recommendations for highways are based on a $1 billion higher program level. We also are not recommending any ceiling on operating subsidy grants for mass transit.

Our budget would add $1.5 billion for education bringing the total request to $10.8 billion. The increase is particularly focused on the needs of disadvantaged students. The revised budget supports the reform of the impact aid program recommended in January.

In health care, we face a very serious problem of inflation. Therefore, the budget proposes a nationwide program to hold down the rate of inflation in hospital costs. We are also proposing a new comprehensive child health care program.

The previous administration recommended an increase in social security taxes. We do not agree with that proposal but we are beginning an intensive study of the social security system to see what steps need to be taken to maintain a sound system.

The previous administration also proposed cutting back the food stamp program and converting the child nutrition program into block grants for States, with sharply reduced funding. We will be looking into these areas with a view to finding improvements. However, we do not support the proposals advanced by the previous administration.

We believe there needs to be a much stronger effort to assure that Americans have proper housing. We plan to increase the number of subsidized housing units from 236,000 to 400,000. We are going to ask the Congress to increase the term of subsidiary contracts from 20 to 30 years. We are also proposing more funds for subsidized units developed by State housing authorities.

We are proposing permanent legislation to protect veteran's benefits against increases in the cost of living. We also do not support the proposal to limit the period of eligibility to the GI bill.

The document we sent to Congress Tuesday is intended to meet the needs of congressional committees as they prepare their recommendations to the Budget Committees in the House and in the Senate. Their recommendations are due on March 15, and we thought that they would like to have President Carter's views on the budget so that they could consider them as they develop their own ideas. The document is supported by a large amount of detail that we have not tried to print. Additional material has been sent to the Congress. We will be sending specific appropriation language within the next 10 days.

There is a great deal that we would like to do in the future that we have not been able to do in this budget revision. We are going to start zero-base budget reviews. We are going to reorganize the Government. We are going to reform the tax structure. Thus, our revisions represent only a beginning of our substantive efforts to improve the Federal Government. We think and we hope we have corrected the major shortcomings in the budget as proposed in January, and that we have set forth the appropriate fiscal policy.

Mr. Chairman, I would be pleased to answer your questions.

Representative BOLLING. Thank you very much, Mr. Lance, Senator Bentsen.

Senator BENTSEN. Thank you very much, Mr. Chairman.

Mr. Lance, on the reform of the tax structure, when do you expect that that will be before the Congress?

Mr. LANCE. Senator, Mr. Woodworth from the Treasury Department is in charge of that reform effort as it relates to the Treasury Department, and it is my understanding that by August 1, or mid-August, that proposal will be forthcoming. It is very complicated, and it is something that requires a great deal of study. I am sure that study will involve input of the people from the Congress as well as other people about what needs to be done in the area of tax reform. It will be very broad and all inclusive.

Senator BENTSEN. I am also interested in the tax reform bill, because last year was a reform of the 1969 reform which was a reform of the 1961 reform. I wish you well in that area.

Mr. LANCE. Thank you. We obviously need the well wishes.

Senator BENTSEN. I think we have to give serious consideration to capital formation in this country to keep us competitive in a world where we are trying to keep up our balance of trade, so that we don't get into the same situation that England is in, where they are not able to refurbish their manufacturing and get equipment that makes them competitive.

I think tax incentives built into the system need substantial review, because some of them don't fit the economic objectives of the country today.

Are you prepare to make any comments concerning the energy legislation at this time?

Mr. LANCE. No, sir, I am not. The legislation for the organization of a department of energy will be presented to Congress March 1. It is on the President's desk for review now. Then, by April 20, he will have a significant statement of policy on energy to be presented to the Congress at that time. So I would not be in a position to make any comments about that proposal now.

Senator BENTSEN. Are you prepared to comment on the action taken by the Ways and Means Committee concerning the tax proposals sent by the administration insofar as what was done on the tax credits, or the investment tax credit?

Mr. LANCE. Yes, sir, I think I am in a position to comment about the business tax area and the other areas.

I am not able to comment about the total number of jobs that may have been added, and what effect that might have with regard to the overall program. With regard to the increase in the jobs portion, that was a share of funds that were probably included in the administration's 1978 totals, and the funding was provided in the 1977 totals of the Congress. That would be an ongoing sort of authority that will be expended as those jobs come onstream.

With regard to the tax rebate, the lowering of the income levels, below $25,000, is certainly an appropriate action, one that we do not have any disagreement with. The reason we started out to include everybody was the fact that we were trying to be extremely fair in the whole stimulus package. We thought it important to go ahead and look at it from that viewpoint. The Ways and Means Committee decided otherwise, and we had no difficulty with that.

Senator BENTSEN. I think that cutoff is a good idea. A House Member asked the Secretary what he was going to do with his $50 when he got it.

Mr. LANCE. I thought his response that he would not significantly change his standard of living was very appropriate.

We, of course, in regard to the business incentives that are part of the stimulus, would like to see our proposals retained if at all possible, for the increase in the investment tax credit and the payroll taxes.

I think obviously as we go forward that if we are going to depend upon public jobs for a period of time as part of a stimulative package to deal with the problem of unemployment that we face, we have to have some mechanism in some way for those jobs ultimately to be transferred to the private sector.

If we lose sight of that fact, then we are not going to be successful in dealing with the economic problems we face. As a result, I would hope that we can certainly look at the kind of job incentive tax that Mr. Ullman is talking about in the future as it relates to jobs coming into the private sector. I think it has some real merit in that instance, and that it is something that ought to be looked at. I do not think on the face of it, from the understanding I have, that it totally solves what we are trying to do in the stimulus package per se.

Senator BENTSEN. I am sure it will not solve all of it, but I am a strong supporter of some sort of employment tax credit. I think small business and business ought to have the option of using the tax credits, and that you are putting people into jobs then will not be dead-end jobs. I think it is better for the taxpayer than creating a public service job, although I support that as a short-term measure.

Now, you make a recommendation about increasing the highways by approximately $1 billion. Can you tell me the justification for that?

Mr. LANCE. Yes, sir, I will attempt to tell you the justification for it. My experience with the Highway Trust Fund goes back firsthand to running the Highway Department of Georgia when those highway funds were impounded. The difficulties that we faced just from the administrative standpoint of trying to plan and complete the Interstate Highway System in our State were considerable. The impoundments created very real problems. That, of course is a thing of the past now, and the fact that they were not able to obligate the funds in times past I don't think is a sufficient justification for keeping the funding levels below what they really ought to be. We felt like, again, this was an area where jobs could be brought into the private sector through highway construction, that these funds could be obligated and put into the spending stream if we raised the funding level. Therefore, our recommendation was to go back to the $7 billion as opposed to the Ford budget proposal of $5 billion, I think.

Senator BENTSEN. Maintenance costs have gone up, and many States have difficulty keeping their highways in shape, not necessarily new construction. I agree with you.

Mr. LANCE. I think the subject of maintenance is a major concern for all of us, because we have a tremendous dollar investment in our highway system, and if we don't maintain it, we are not taking proper care of our investment.

Senator BENTSEN. Thank you, Mr. Chairman.

Representative BOLLING. Congressman Pike.

Representative PIKE. Thank you, Mr. Chairman. I apologize, Mr. Lance. We are at the mercy of the bells.

I am very interested in one of the changes that you refer to in your statement between the prior credits for married couples and single couples, and I would like to know the extent to which this was caused by the fact that the Carter tax package ran into the Carter moral package?

Mr. LANCE. Congressman, we went sort of through that process in the Ways and Means Committee, and the questions were being directed at Secretary Blumenthal. At that time I sure was glad, because I didn't think there was a good answer to that question, and I still don't think there is a good answer to that question.

Representative PIKE. What the revised proposals do, then, is to reduce the economic desirability of living in sin. Is that a fair statement?

Mr. LANCE. Congressman, again, I don't think I had better respond. [Laughter.]

I remember in my seventh grade civics book somewhere that the Ways and Means Committee originated tax measures, and I let that stand over there on that side rather than on our side as the reason for it.

Representative PIKE. Mr. Lance, in general I just would like to say that I think that we are beginning to see some directions of movement in terms of changing priorities which I find affordable. I wonder the extent to which you can make them stick. The increased deficit concerns people but the decreased spending influences people very, very directly and very, very painfully, and the extremes are already going up, and in my own area, they will have to do with impact aid, and not with the termination of water resource projects. But I can certainly understand the extremes coming from other areas on other issues.

To what extent do you think the projects are politically realistic?

Mr. LANCE. Mr. Pike, I would hope that what we have tried to do in our budget revisions—and as I stated earlier, they have been done in a relatively short period of time because of those restraints that I think are properly imposed upon the executive branch with regard to the budget process—is to be aware of the political realities. The water resource projects, the aid to education—those are sensitive political questions, I understand, and I understand that part of the process.

But I think it is obvious to me, and this stems from my business background, from which I can relate to it in that regard, is that we now have got to be aware of the fact that we are, in my opinion, at the point when we have to start making some hard choices, and we have to start making some tough decisions as they relate to the financial resources and the expenditure thereof in this country.

Now, the Carter administration is willing to make those hard choices. I am sure that the Congress has to deal with the question of hard choices, and that you are willing to face those hard choices.

I think you will see in the future that we will attempt to make some of those hard choices and take the political aspects of it that come as a result of those choices being made. Such was the case with regard to the aid to education, for example.

We increased some programs that we felt were appropriate; for example, that served a real need in the area of disadvantaged students. We said that we are not going to recommend any more money in the direct student loan program. You already have $3 billion in that program. We don't think until another look is given at it that it is something we ought to continue to put additional funds in. I know in Congress that presents a political problem. So, those realities are there.

But we have started in the process of having to make those hard choices that are part of the process, and we will continue that part of the process. I think it is important for the American people to realize that we are willing to begin in that area. There will be discussions, disagreement and debate. That is all part of the process, and that is the way it ought to be. We will be right in some instances, and wrong in others, but at least we will be in the process of making those hard decisions that I feel strongly, and I imagine a large number of people in the Congress feel strongly, have to be made in the future when we talk about the resources we have.

How many more do we have that we can really expend, and what should be our direction?

Representative PIKE. That is a whole answer as far as I am concerned.

Mr. Chairman, I have no further questions but I would like to put out a plea that I have put out before, and that is, when you get to the realm of tax reform, the key word be "simplification."

I started off on the Ways and Means Committee hoping to do great things through the tax code, and I have decided that I was wrong. The history—there is a story in today's Times which happens to come out of my home county, of an attempt made to see how good the tax preparers of the country are, and a sample tax situation was given to 10 different hired taxpreparers, and every one of them got it wrong.

Not only individuals can't do their own taxes, but the people we pay to do taxes can't do the taxes.

I just think that there is nothing better in the realm of tax reform than tax simplification.

Mr. LANCE. Of course, Congressman, as you know, that is part of the permanent tax relief that we have proposed in the stimulus package to begin with.

Representative PIKE. I am talking about more than just putting more people into the standard deduction, or into the—I can't think of the right word. I am talking about for the people who don't fit into the categories where Government does it all. It has got to be simplification.

That is all, Mr. Chairman.

Representative BOLLING. Senator Hmphrey.

Senator HUMPHREY. Please. I am just getting here. If you have somebody who hasn't had a chance to ask——

Representative BOLLING. Congressman Hamilton.

Representative HAMILTON. Mr. Lance, we are delighted to have you here. I think you probably know that the House and the Senate now have acted on the third budget resolution, and in both of these instances, they have increased the amount of spending over the figure that the President suggested—the increase in the House is $1.5 billion and I think the increase in the Senate is $1.2 billion.

I think these budget resolutions follow largely and are in agreement with the President's recommendations.

Can we assume that the President will accept these changes that the Congress has made in his budget if we go ahead and make the authorizations and appropriations pursuant to these resolutions?

Mr. LANCE. Yes, sir, I think that that is a safe assumption with regard to those totals. I am not sure, and I will have to get Dale to tell me what the numbers are, but whether the total increases meet what the budget resolutions call for.

Mr. MCCOMBER. There is a bit of confusion. It appears to us that the increase is about $1.1 billion rather than $1.5 or $1.6 billion. The reason for that is a different classification of what is fiscal stimulus. For example, both sides of that have money for highways. We also have added some money for highways, which was not counted in the stimulus. A reasonable figure seems to me 1.1.

Representative HAMILTON. When you use the $1.1 billion figure, are you going on the basis of the Senate or the House resolution?

Mr. MCCOMBER. It happens to be around $1.1 billion on both sides, if our arithmetic is correct.

Mr. LANCE. I wanted Dale to make that explanation, because I think that is of some importance. But we don't have any problem with the numbers. It may be when you get to the appropriations process there may have to be adjustments made in some aspects, but I am not in a position to comment specifically on that, because we again would like to see options preserved in that instance.

Representative HAMILTON. Mr. Lance, I would like to ask you a question about how you got these recommendations and under what kind of instructions from the President were you acting.

Now, in the changes that have been made. You have made a reduction in defense. You have made increases in environment, housing, and education. You have changed some of the emphases of the energy program away from nuclear to nonnuclear kinds of energy. Obviously, this is a stimulus package.

What kind of directions did the President give to you here? These were all, I presume, specific directions from the President with regard to these areas.

You mention in your statement how you couldn't possibly look at the whole budget, but you had to look at a few items in the short time you had.

The second part of the question is, can we expect these same trends to continue?

Mr. LANCE. Congressman, let me deal with the second part of the question first. When you talk about the same trends continuing, I would simply have to say that I would have to have a better understanding of what trend you have specific reference to.

Representative HAMILTON. Basically, the increases in health, or, rather, environment, housing, and education, and decreases in defense.

Mr. LANCE. I just wanted to make sure, because when we get asked questions about the budget, they say the trend definitely is up.

We think that is not an accurate statement. The trend in 1977 and 1978 is down. So, I wanted to be sure.

I would say to you that I think the changes that were made, speaking of trends, the second part of your question, relate to sense of direction of the Carter administration. The program of compassion and concern for the human factors that we face and the human problems that we have to try to solve in this country, I think, are reflected in the changes that were made, and I think you will see a continuation of that.

In the area of defense, we think we have made cuts without impairing the strength of our national security system. I would again think that that would be the sense of direction, that we want a strong defense, but we don't want one that is plagued with inefficiencies and expenditures of moneys that don't achieve the right kind of purpose.

So, I think those trends, I think as previously laid out, would connote a sense of direction.

Now, with regard to the specific instructions that I had, I had no specific instructions with regard to the budget from the President. We had, as I said, very little time to go through the process. I had in addition, and this is not an excuse, but simply a statement, in addition to the budgetary aspects of making revisions, I spent a great deal of my time on the Hill here testifying about the stimulus, so the time frame was shortened to less than 26 days which we thought we had, from January 20 to February 15.

I had an awareness of things that the President was concerned about. We tried to explore the major decisions in that regard. He also felt, and I knew that I felt, that the new cabinet officers ought to have a chance to not be faced with severe pressure on them without being able to get acquainted with their departments and agencies and have a lot of major changes coming forth early on in the budgetary process.

We tried to accommodate those cabinet officers who had a sense about the direction they wanted to go in, the programs they wanted to emphasize and the things they wanted to see their departments begin to make. So we tried to accommodate them.

It was that sort of process. We are proud of the results. We think we did a good job under the circumstances we were faced with. The President, as I said, did not give me specific instructions about what to do in the defense areas. He made those decisions after briefings and after consultation with the National Security Advisers and the Secretary of Defense and briefings from the Joint Chiefs of Staff.

Representative HAMILTON. What kind of growth rate do you feel you will need to have in the economy to balance the budget of 1981?

Mr. LANCE. Six percent.

Representative HAMILTON. Each year. Does that allow for any increased spending?

Mr. LANCE. Yes, that will allow us increased spending, if we have a 6-percent growth rate, and this is a matter on which Mr. Schultze testifies much more knowledgably on than I do in terms of the numbers, but we would have the fiscal ability to have additional money.

Representative HAMILTON. Thank you very much, Mr. Chairman.

Representative BOLLING. Senator Humphrey.

Senator HUMPHREY. Mr. Lance, my concern is not so much with the specific items in the budget and the activity of the departments of government. The Budget Office is called the Office of Management and Budget. I think it does much more budgeting than it does managing, and obviously I am not directing this to you, sir, because you are just new here and haven't had a chance to get your input into this system.

The Budget Office has been in the past a very good one at withholding funds that the Congress appropriated. It has been grossly negligent to seeing to it that funds we appropriated were properly and expeditiously used.

I think that the duty of the Office of Management and Budget is to remember that the title was changed, and that the title being changed to Management and Budget, that the management part is as important as the budgetary part.

The word "budget" to people means we are going to cut back. You can cut back at times and still do a good job of management. I know this is the policy President Carter has, and that you have.

Let me give you an example. There are funds in the Department of Housing and Urban Development that are not being used. We can't wait until fiscal 1978 to stimulate the housing program. I am sorry Senator Proxmire is not here, but we had quite a discussion with Mr. Burns yesterday.

The stimulus, the economic stimulus package which has been presented, which I support, and which I think is a reasonable package, does not include in the package as such, or even in its descriptive rhetoric, the possibilities that are found in housing construction. Housing has a ripple effect in the economy second to none. It is the bellweather of the economy. We used to think of the steel industry as the bellweather, but it is not.

There is what we call the tandem program over at the Department of Housing and Urban Development, which if properly used, has funds there really to stimulate housing construction. Quite honestly, I don't think we are going to come anywhere near balancing the budget or to reduce unemployment substantially unless we get construction underway in this country.

That is one of the reasons I support construction. There are some of our friends who speak of pork barrels.

There is no pork barrel out there to build water and sewage, or to improve bridges we need in our county roads, and it is no park barrel to put up a new firehall in a town that doesn't have one.

Pork barrel is putting people on relief. I had to get this out, and I hope the Office of Management and Budget will really get the whip out and demand that the departments they are to manage—not just here in Washington, and I want to put it in the record—Government is in the regional offices. They never get to see you. I had them lined up 50 feet deep in my hallway. People who want disaster relief, people who have had 3 years of drought. I have called up my friend, the Secretary of Agriculture, and said, "Get with it."

He has a big department. But we can't wait. All I am saying is that I hope you have someone in that department who is as big as you physically, that is as able as you are in terms of competence, that will just call up on the phone and say, "Look, the money is there, the program is there, let's get with it. If you have regulations that stand in the way, cut them out."

We are going to make some mistakes. The biggest mistake is overregulating.

I know this is what the administration says it wants to do, but I think I should forewarn you that I am a persistent cuss and I will be after this from here on out. We have money. It is incredible what you can do if you start to put the packages together. Billions of dollars are there unused.

Now, the Congress appropriated that money for a purpose, and I don't think the economic stimulus package is going to do its job as well as it could unless we use what is there that is not even called economic stimulus.

I think there are several billion dollars of funds lying around that are not in the package that could really give zest and thrust to the economy.

I understand the administration is looking at a whole new housing approach. God only knows it needs to be done. These programs under the previous administrations with Mr. Lynn, and even Carla Hills, whom I thought tried to do a good job, these programs have been relatively ineffective. We constantly hear that we are going to have more housing starts. We got starts and stops of housing. We are right now at one-half of the housing effort that we need.

So, I don't know who the gentleman is with you, but I believe he is from your office?

Mr. LANCE. Yes, sir.

Senator HUMPHREY. I hope you have listened to me.

Mr. LANCE. Dale is most responsive, Senator.

Senator HUMPHREY. May I have a response to that?

Mr. LANCE. Yes; I would like, if I can, to make a broad general response.

Senator HUMPHREY. Yes, please.

Mr. LANCE. With respect to the management function in the Office of Management and Budget, I agree with you wholeheartedly. One of the things we are interested in the reorganization process that has been presented to the Congress is to make sure that in OMB we have the ability to determine the management efficiencies that we see in the executive branch.

As I see it, again looking at it from the viewpoint of not having been in the process for a long period of time, there is no way to fix accountability in the Government, and that is one of the things I think you mean, very appropriately, when you talk about the regional office concept. Your constituents, when they get a social security check lost in the mail or they don't receive it in the mail on time, that is the single most important problem they are facing. If Government doesn't respond in that circumstance, they don't feel the Government is being of service to them.

If it gets bounced around between the regional office and the main office in Washington, if that is what we call the main office in Washington, then, you know, there is no way to fix responsibility. We have to be able to do that. We have to be able to point our finger and say, "You are responsible for dental care in children,"—if that is what the function is—"and if that function is being carried out properly, then you get credit for it, and if not, it is your responsibility.

"It is your failure, or your lack of concern, or lack of management."

We need to get to that point. We have got to do it. I share your concern about that.

The statement about moneys being available, I am sure that is the case. We have to look and see where the funds exist, where the programs have been authorized and appropriated for. I think we are going to change that sort of thinking in regard to the way that OMB does things.

The housing problem, you have made a very eloquent plea about the need for housing to be given its proper place in our overall policy and our overall setting of priorities, and I happen to agree with you totally and completely.

In working with Secretary Harris, we have made significant changes in the 1978 proposed budget. I think our budget authority increases in 1978 by about $24 billion—around $15 billion. The total amount is around 24. Fifteen of it is in the area of housing.

She will be having a policy statement in her testimony, I assume, about the tandem situation. I think this is awfully important, and we are going to be moving very aggressively in that area.

Senator HUMPHREY. This is a matter I know we have talked about, but I wanted to emphasize it, and I say it because of my long experience in Government. When I was on the other side, I found the Bureau of the Budget looking primarily to present the budget first and then to see we didn't spend too much.

I look upon the Bureau of the Budget now not only to see that we are frugal, but that we are efficient. That "efficient" is going to require a big stick.

You are at the President's right arm on this as the Director, and that means the regional offices have to get the message that when the mayor writes or calls them, they are supposed to get on the stick. They don't You know, I have had experience with them. I get my blood pressure up beyond the danger point, except that it subsides quickly.

I suppose you have had a lot of questions about these water projects.

Mr. LANCE. Yes, sir, and let me respond——

Senator HUMPHREY. Do we have western State members here? You are lucky?

Senator BENTSEN. All of ours were justified.

Representative BROWN of Ohio. As a water drinker, I sympathize with you.

Mr. LANCE. Let me respond to the statement you made about public works, because I think again in the budget process we have taken into consideration one of the things your colleague, Senator Anderson said, when we were before the Budget Committee in the Senate, the fact that when the fund runs out in certain States—I think Minnesota was one State where funds had run out—and we did bring into the 1978 budget some $400 million, or in that area—rather, $4.5 billion of budget authority—to deal with that specific problem. So I would hope that Minnesota and the other States which have run out of funds, and allocations, will see some of those projects move ahead and not be delayed.

With regard to the water projects specifically, this, again, was in my response to Congressman Pike, that it was one of the hard decisions that had to be made.

We felt that values have changed in this country over the last several years. In many instances, the question of water resource projects have a lot of people for theim and a lot of people against them, and a lot of them have been through the referendum process, actually having people vote as to whether they wanted them.

We needed to say where we are, and where we are going, and what criteria really needs to be developed. With regard to those 35 projects that were listed specifically, and the other 300-odd projects in various States, we felt that we ought to withdraw those 19 projects, because the corps or the Bureau of Reclamation thought that was an appropriate action.

Those projects will be studied under the new criteria, and if they appear to meet those criteria, then we will ask the Congress to reinstate those projects in the budget.

I am sure that if those projects don't meet the criteria and we don't ask for reinstatement, that there will be a great deal of interest in the Congress to put them back anyway. But that is something we have to wait and see about. But these projects have to be studied, criteria will be established by the Corps of Engineers, and so forth.

Senator HUMPHREY. My time is up. Thank you very much, Mr. Lance.

Representative BOLLING. Congressman Brown of Ohio.

Representative BROWN of Ohio. Thank you, Mr. Chairman.

Mr. Lance, let me say not for comment by you that I was in California when the announcement was made.

Mr. LANCE. I am glad I wasn't. [Laughter.]

Representative BROWN of Ohio. You should be very happy that you weren't.

Mr. Lance, Professor Modigliani of MIT told this committee when he testified here that rebates don't work. He said the last one in 1975 was saved, not spent, and that it really had no measurable impact on spending for at least a year after it was granted.

Rather, he said 1 year to 1½ years. Why doesn't this work any better?

Mr. LANCE. Let me respond to that question with a little detail.

Representative BROWN of Ohio. Not too much detail, because I have a whole list of questions.

Mr. LANCE. All right, but I think the question calls for a word on the practical as opposed to the world the professor may deal in. I have no reason to know whether that is an accurate statement of his views or not. I was in the real world during that time running a bank in Atlanta, where we had a terrible economic situation. The banks were loaned up to the extent of 90 or 95 percent. We had double-digit interest rates, unemployment, and inflation. I am convinced if we had not had the rebate at that time, that we would have had an ongoing economic circumstance greater than we had.

I think it did make a difference. I think it did work. I think it worked in the standpoint I saw it from, in the practical sense. It changed people's attitude that they were going to be able to exist, and prior to that time, I think there was real doubt in the minds of the Georgia people. I can't express what the rest of the people in the country felt. In Georgia, things were tough, and they weren't getting any better. I think it did work.

Now, it did not carry through with regard to capital investment and plant and equipment. I think that is where the problem is, and the only answer I can give to you in that regard is this: That the confidence factor was not present, in the decisionmakers who would have to expend the funds for investment in plant and equipment. They were not sure about what we were going to be doing into the future.

Representative BROWN of Ohio. Let me jump on that and suggest that we have had testimony before the committee that permanent tax reduction stimulates the economy in three ways. It stimulates consumer demand. The rebate is supposed to, but it lags 1½ years or so. But it does so more strongly and immediately.

Second, it increases aftertax takehome pay, encouraging laborers to work instead of being tempted to linger, because people keep more of what they earn, and at the same time, it increases aftertax return to investment, causing more investment projects to be profitable, and worth doing, and increasing the reward for people who make investments or savings.

It seems to me this has the impact, then, of increasing the country's growth rate.

A rebate may do the first thing, but it doesn't work in the second and third. Wouldn't it be better if we had a permanent tax rate reduction in order to have a more sure stimulating effect?

I understand your bank, and I run a business, and I have to, of necessity, maintain a friendship with a banker. I can tell you that that temporary rebate doesn't encourage me a great deal in my particular business. If that business, and if I personally had a tax reduction, then I could look at you and say, "Now, I have that much money coming in from now on, and I know what we can do with it in our company, and we can count on it."

But the rebate is a sort of a quick fix that doesn't get any place.

Mr. LANCE. I understand your comments, and I happen to agree with you on permanent tax reduction.

Representative BROWN of Ohio. Are you going to propose that?

Mr. LANCE. In the tax package——

Representative BROWN of Ohio. When, when, when? That is the big question.

Mr. LANCE. I responded that that would be about mid-August of this year. Permanent tax reduction has to be part of that process.

Now, in regard to rebates versus permanent tax reductions, it was the consensus that the only way that we had to get money into the spending stream of this country quickly was through the tax rebate.

Now, we have got $6.5 billion of permanent tax reduction in the stimulus package as it relates to the tax simplification process and the payroll credit to business.

Representative BROWN of Ohio. This is all borrowed money. I don't see in the total economy how it stimulates anyone. The Federal Government is borrowing it to give it to folks who are going to put it in the bank, and I think it is very likely to stimulate inflation.

Mr. LANCE. We don't think it is inflationary in its relationship to the total economy at this time, and I think there is broad and sufficient justification for that statement. The economy is operating at about 80 percent of capacity. We don't have the same sort of circumstances present with regard to high interest rates and high inflationary rates that we have had in times past.

I would say to you that, given the time to propose a stimulus package other than in the first 2 weeks of a new administration, that I think we could make a strong case for permanent tax reduction, but I think when you consider the timing problem and the circumstances that we faced, that we had to do two things. One, we had to try to get the funds into the economy as quickly as possible, and second, we needed to maintain the options that we would have going forward about how to structure tax reform and how to structure the other things that relate to the economic growth and development of this country.

So those were the reasons we opted for tax rebate instead of saying, "We have time to study this very carefully and make some proposals." We didn't have that time.

Representative BROWN of Ohio. I think you have gotten psychological emphasis on the permanent tax reduction. It seems to me the impact of that in the long run would have been better.

I want to make one reference to the tax reduction that we had in the President Kennedy area in the 1960's, and the results that that got in terms of increased Federal revenue, as well as the stabilizing impact on the economic activity of the country at that time, both with reference to inflation and the growth of the economy, because it literally enhanced investment and created job formation.

Now, we are going to need massive amounts of job formation in the future if we are going to keep up with the participation rates, if those stay up, and with the labor force, and if we are going to reduce unemployment at the same time. We would have had a much more successful reduction of unemployment if we had not had so many people entering the work force, and if we have those people entering the work force in the next few years and don't provide jobs for them, and jobs, I think, clearly come from the power to invest by people who want to start businesses or expand them, we are going to have real trouble.

A lot of the folks on your side of the aisle in Congress refer to a tax reduction as reducing the Federal income that the Government may seem to feel has not only a right to, but is in effect the Government's rather than the incomes of individual citizens. I am curious to know what your position is on that. Do you think we are going to be reducing or raising Federal revenues if we have a general tax reduction?

Mr. LANCE. My personal observation is that as you go through the process of permanent tax reduction, that there is an awfully good argument to be made for the fact that the revenues of the Government actually increase at a given time. I think that has been proven in previous circumstances. I have no problem in following that sort of thing.

Yet, as I said, I would personally come down on the side of permanent tax reduction as opposed to something less than permanent tax reduction. But under the circumstances that we were faced with, the problems that we had to solve, there was no way to put that sort of process together.

Representative BROWN of Ohio. When you say "personally", are you speaking as Bert Lance, banker, or Bert Lance, of the Office of Management and Budget?

Mr. LANCE. I am speaking as Bert Lance, and I don't think I could draw that delineation there. I think that is my personal view.

Representative BROWN of Ohio. That is not the Carter administration's approach yet?

Mr. LANCE. I make a distinction.

Representative BROWN of Ohio. Profits have been low—in spite of the fact that profits have been quite high, in spite of the fact that people say corporations are making big money, now, a capital spending boom isn't yet in sight. It seems to me one of the things about the recovery that never quite comes along, and perhaps when you adjust those corporate profits for inflation, that may be the explanation.

Doesn't that low rate of capital spending then reflect what is happening to corporate profits, and wouldn't the idea of a significant tax reduction, so that you could increase the after-tax return on investment somewhat be a good idea, and shouldn't we move on that more quickly than just sort of waiting until next August and then have it taken up in the second session of this Congress, and then it is an election year, and things get lost in election years.

Mr. LANCE. Again, to really be responsive to your question, I think that is the area of overall tax reform, and Senator Bentsen earlier related to the need for a capital formation process in this country. I am concerned about that. I think obviously we have to try to deal with that problem I don't think we can deal with it over the next 60 or 90 days. I think when we are talking about permanent tax reduction, then that becomes an overall part of tax reform, and you have to look at what you are doing now and what you want to be doing in the future, and what kind of goals you have toward being able to provide for the formation of capital, for investment in the plant and equipment for the private sector to do its thing, about the job creating process, and the job process in being able to deal with the problems of unemployment. I don't think you can do that over the next 60 days.

Representative BROWN of Ohio. My time is up, but I was surprised that the President came into office without programs in this. I am surprised they haven't been dealt with.

Mr. LANCE. I am surprised at that sort of comment, because these are not new problems. They have been here for a long time, and one month is a short period of time for us to try to deal with them. I didn't think anybody, the American people or the Congress or people in the Government or anybody else expects us to have all the answers to all of the problems that many of you have been wrestling with for a long, long period of time.

We have just begun the process. I would hope after we have been onboard a while that we will have some well defined, well laid out programs and plans for dealing with some of the problems that have been present, but I think again, talking about the time frame that we have been involved in the process, I think what we are doing is good. We proposed a stimulus package, introduced reorganization legislation, and you will have energy organization proposals by next week. I think we are moving along fairly well.

Representative BROWN of Ohio. Thank you.

Representative BOLLING. Before I yield to Mr. Rousselot, I would hope it wouldn't come up in too big a hurry. I have been here a long time, and I haven't ever seen an administration that came up in too big a hurry that didn't get into trouble. I would rather see solid recommendations somewhat delayed than superficial ones coming too quickly. The too quick ones haven't been exclusively the products of Republican administrations. I feel differently than Mr. Brown does. I hope it is well thought out before we get it. The worse thing the administration can do is to come up with half baked proposals.

Representative BROWN of Ohio. One came up with a lot of proposals, but it only lasted for 16 years.

Representative BOLLING. If you look back on the history of that, you find a great many of them were very good. There were a lot that were uneven.

Representative ROUSSELOT. Mr. Chairman, I appreciate your yielding to me, and I will try to be brief, Mr. Lance.

Let me comment as a followup to Congressman Brown and my chairman. I hope you certainly do give it careful, proper, adequate consideration, and I know the President started thinking about it long before he was elected. He said so during the election, and especially on the issue of economics, and since you were heavily involved in that in the private sector itself, I hope you will help us to get to it quicker than August as it relates to permanent tax cuts, because in the Budget Committee, we have to act in April, and heavily impacted on what we do in that budget will be targets for 1978 that we can't wait until then.

I really think that if we can encourage you to speak, and I know you will speak before the Budget Committee again, to the issues, since you do agree yourself personally that permanent tax cuts, both individual and corporate, are partial answers to proper stimulus. I hope that you will help us address that issue in the Budget Committee, because I think we need it, and we have to act on a law by April.

That doesn't mean that everything in the Budget Committee is perfect, but we have to address ourselves. We can't wait until August, because by August we are also discussing the second budget resolution, which then sets our permanent ceilings for the year.

I will be brief by saying this, that there is a tremendous ongoing debate in this Congress over the proper amount and type of economic stimulus, and that is very, very heavily influenced in the weight of our decisions by various econometric models that we use, that you use, and that the Federal Reserve Board uses to project into the future. We rely on that an awful lot.

Our chairman quoted on the floor, and various committees quoted them on the floor.

In the assumptions that go into econometric models, there is a heavy weight in the model on Federal spending and what that does to stimulate the economy, rather than on the supply side, and what happens in the private sector.

Mr. Blumenthal and you and Mr. Schultze have put heavy weight, and the Carter administration has, that 5 out of 6 jobs are provided by the private sector.

So I am going to write you a letter and ask for some long-term comments on use of econometric models, the ones you will be using in Treasury or in OMB and so forth, and the kind of assumptions that go into those econometric models as they relate to Federal spending, what that does in the general economy, et cetera.

I know in the banking business, I am sure you have many clients who utilized econometric models and long-term projections, and if you want to make any quick comment, all right, but I am more than willing to let you comment in writing.

Mr. LANCE. I will be glad to respond to your letter and to your questions.

One of the difficulties, I think, of econometric models, and I am not an expert in that area, and I always try to shy away from that sort of conversation in my own business, because I found out I——

Representative ROUSSELOT. You couldn't say?

Mr. LANCE. No, I say if I relied on them too much, I lost sight of what the real world was like out there.

In the models, it is very difficult for you to build in consumer confidence in those models.

Representative ROUSSELOT. You are absolutely correct.

Mr. LANCE. So you generally end up on the wrong side because of that. So I have to hear what people say, and what their thoughts and plans are as a part of the decisionmaking process in the private sector. I think we have to be aware of that, because I think that is one of the deficiencies in the model structure.

Having said that, I can't make much more response, because I understand you have to have them, that this is a proper statistical way of dealing with circumstances that you have to be able to deal with.

Representative ROUSSELOT. That is the best device we have at this time. I agree with you that I am glad all businesses in this country don't rely strictly on econometric models of the kind we see here, because, for instance, if they were existent today, Mr. Kennedy probably wouldn't have instituted the tax cut he did, and it turned out to be pretty good as a permanent tax cut.

I appreciate your comments, and I will give you my letter with a statement including some remarks from the floor on econometric models.

In the Budget Committee, we put a tremendous reliance on the econometric models.

Representative BROWN of Ohio. Would you yield to me for a question?

Representative ROUSSELOT. Yes.

Representative BROWN of Ohio. I would like to ask you what you expect the impact of the increased deficit to be, Mr. Lance? The President has increased it substantially over what President Ford recommended, and the Congress will, of course, if it follows its usual pattern, and if the Sun comes up tomorrow, increase it beyond that.

What do you think will be the result in terms of inflation? Could you predict for me the inflation rate about a year from now, or maybe 18 months from now?

I know one organization in the community here, an apparently sizable group which represents some private industry, people, that is predicting double digit inflation within 18 months.

Can you give me that picture?

Mr. LANCE. Let me try not to give you a figure, because I would have to give you the figure that Mr. Schultze has as his basis for dealing with the percentage increase in inflation, which is in the 5- to 6-percent range.

I think that a couple of things are present that we have to deal with here. There is no question about the problem of inflation in this country. It is one we have seen in the last four years. The real effects of double digit inflation and what happens when it becomes rampant—

Representative BROWN of Ohio. I might say that we have stimulated demand over the last 6 years by something like $236 billion of borrowed money, and I see no change in the pattern in the new administration in that thrust in the economic sense, and that is why I asked the question.

Mr. LANCE. And I am trying to respond to your question by saying that I think you will see a change in the thrust as we have a chance to implement zero-base budgeting in the fiscal year 1979 budget. We have a chance to really get into the budget process. The 1978 budget is really President Ford's budget with revisions by the Carter administration.

You know the time restraints there, and trying to make big decisions based on that sort of thing. Again, when you see the difference between the Ford budget and the Carter revisions to it, actually, you are not talking about that much of an increase in the deficit.

Actually, when you take the $57 billion deficit that we are talking about, and having started on a $47 billion base, we restored $8 billion of Ford cuts, and there were $4 billion that we did not restore. There are $8 billion in outlays for the stimulus package for 1978. So I don't think that should be considered by the Congress or by the American people as a move toward reinstitution of the inflationary syndrome in this country. I don't think that is a proper analysis. I have seen what Mr. Burns said yesterday, and I have seen what other people say about it. It is something to be concerned about, but in many instances, as you well know, if we talk about recession or depression long enough, we find ourselves faced with those circumstances.

My only comment is that I think we need to look at the realities of what we did with regard to the revision of the Ford budget.

Representative BROWN of Ohio. The reality that I see is that you increased the deficit and increased the spending. I guess what you are telling me is that doesn't indicate what you are going to do next year, and I want to push that inference one step further, and ask if you then anticipate next year being able to cut back spending increases that have been part of the Presidential budget, or that you are going to have some increase in income for the Federal Government that will cause the deficit to go down.

Mr. LANCE. Yes, I think the deficit will go down.

Representative BROWN of Ohio. By increased income, or by reduction in spending, or a lid on spending?

Mr. LANCE. Well, I really would rather not get involved in talking about a lid on spending, because, you know, that is an area that I don't think that we have given that sort of thought process to. We talked about the implementation of the zero-base budgeting concept in the 1979 budget, which gives to the Cabinet officer the hard setting of priorities on what they are doing from an extended viewpoint in their departments or agencies.

Representative BROWN of Ohio. If we could stop there, it seems zero-based budgeting is done for the purpose of the reevaluating of programs, and so the implication of zero-based budgeting, I think in the minds of a lot of my citizens back home, who think it is a pretty swift idea, is that you are going to terminate some bad programs at the Federal level, or at least put a lid on them or at least recognize that they are not working and say that somewhere we are going to make them more productive.

But what is the other choice that the man would have? If you say it is merely go set priorities as to which are good and which are bad, or which are good and which are better, it seems to me that that is the process that at some place along the line you draw a finish line and say, "Now, below here, we are not going to go into those programs yet," and that you are either then going to put a lid on the budget, or try to hold down the rate of increase or perhaps even try to reduce the budget.

Now, is that a proper inference from what you have said, or is it a wrong inference?

Mr. LANCE. No. I don't say it is a wrong inference. I would say it is an inference that you have drawn, but the zero-base budget process, where you deal with the problem of spending levels, is a part of the priorities choice process, the decision package that we will be talking about as we get into the process, where you say for the Cabinet officer in that case that here you have 85 percent of last year's budget, you have 100 percent of last year's budget, you have 105 percent of last year's budget. Now, how would you rank your programs, and functions of your department under that sort of circumstance, under that sort of discipline? Is that part of the process of zero-base budgeting?

There are people who think that represents a ceiling. Where you just put a ceiling on something, that generally implies you have across-the-board cuts or increase, in relationship to the ceiling that is imposed, whether it is an increase or a decrease. That is not what zero-base budgeting is all about.

In response to your question with respect to the 1979 budget as to whether we are looking on the expenditure side or on the revenue side, I come from the business sector, as you do, where you try to cut costs and increase income. You don't think there is anything wrong with looking at it as long as the increased income comes from increased productivity in the private sector, which is where it has to come from in my opinion.

That will be looked at in total, and there may be cuts made, and there may be increased revenue we have to deal with, and I think that is part of the process, but to say that we are talking about putting the lid on, I think that is a part of the process.

Representative BROWN of Ohio. I think my time, or Mr. Rousselot's time is probably up, and I am not sure whether I was too long, but I will have to say that I will pray that whatever the process you go through with zero-based budgeting that we get some reduction in the deficit process, because we have had it for 6 years now.

We cleared up, but things have not gotten any better in terms of employment and inflation.

Thank you, Mr. Chairman.

Representative BOLLING. Mr. Lance, pursuing this line a little bit, you, as I understand it, have stressed the administration's determination to balance the budget by 1981. Of course, this has attracted widespread popular support. The questions I raise are about other things.

Is a balanced budget by 1981 compatible with the objective of reaching full employment in that same year? Can you do both? You know perfectly well what is in the back of my mind.

There are other areas where people say there is a great incompatibility between the two unless we are very lucky in the way the private economy grows, and full employment is defined at a higher level than some of us wish to accept.

So, I am curious how you really feel about that, not having had a long time to look at it, and having had a great deal of your time taken up with questions like this.

Mr. LANCE. Mr. Chairman, I think the goals are compatible. Talking about full employment, depending on the definition of it, I understand that the Congressional Budget Office a couple of weeks ago said we would have to add substantial—or I forget the exact wording they used—growth in the economy in order to achieve that sort of a goal, but I don't think they are incompatible, and I don't think this is the time to be saying that we have to make a choice between those two sets of circumstances. I think that we can move forward in the direction of the balanced budget and the decrease in unemployment that we have certainly got to have in this country.

We can't continue at these high levels of unemployment. That means we have to have a viable economy, and the private sector has to be able to be viable and be vital, and be moving along, and that implies the 6-percent growth rate that we talked about earlier.

Representative BOLLING. I gather that in other places you have thought the growth rate for 1977, at least, was going to be lower than 6 percent.

Mr. LANCE. Yes; I think the rate in the last quarter, or the third quarter of 1976 was significantly lower than that. Again, this is something that Mr. Schultze has a better feel for than I have with regard to the numbers, but in order to get back on the track and have a 6-percent growth rate over the next 4 years, I would assume we would have to do better in 1977.

Representative BOLLING. In other words, we have to do more from a relatively low level, and that implies in some of those years we are going to be moving above six.

Mr. LANCE. Yes, sir, when you have to play catchup ball, that is the problem that you face.

Representative BOLLING. I have a problem in seeing how the thing is going to fit together. I think you are right that we shouldn't assume that it can't be done, because there are difficulties, and I think it is a fundamentally difficult problem to seek a balanced budget in 1981 and a set of economic circumstances that will get us to a relatively low rate of unemployment, a great deal lower than today, and at the same time not expect a growth rate in the economy which would be almost extraordinary, as I see it.

Mr. LANCE. Can I make a brief comment in that regard that I think is important, and I just throw this in for the sake of discussion more than anything else.

As you well know, in the past, what we have seen happen in the normal business cycle in this country is that we have seen consumer spending increase, and then toward the end of the cycle, investment and planned equipment come along, and that sometimes increases the problems we have instead of helping to solve some of the problems we have.

I think right now we face perhaps different sets of circumstances, and going on the assumption that we can be successful in dealing with them.

First of all, the business people I talk to—and I try to ask this question when I have the chance to do so—all of them respond that they have more plans on the shelves, fully engineered, ready to go, as relates to investment in plant and equipment than at probably any time in our history, and if we can bring the confidence back into being, where people feel good about the future of this country, and feel good about the course that we are taking and the fact that there is going to be predictability, and consistency in government, then we could see the economic growth change very quickly, again without the attendant pressures upon the inflationary side.

Because corporations are flush with liquidity, banks don't have any loans to make, and that sort of circumstance is really awaited out there, in my opinion, and it is awaiting the kind of confidence building that can be important.

I think this is the kind of process that would allow us to change those goals.

If we can do this, sir, if we can get the percentage of time that the people in the business area, and I am not talking about big business, but the drugstore and the barbershop, if we can get the percentage of time that they now have to spend filling out government forms and dealing with the problems of intervention and regulation on behalf of government, and let them begin to use that time in a productive manner, then I think we will see some significant progress made. We are going to do something about that with regard to the reports and that sort of thing, and hopefully with the cooperation of the Congress, and cut out some of these things that are totally nonproductive.

Representative BOLLING. I would like to comment on that. I happen to believe more that the psychological factor in the economy is a crucial factor. I came to Congress when we did the last major reorganization of the executive. It badly needed to be done, and it badly needs to be done now.

I also think that we have to go a step further in terms of our attempting to restore confidence, to restore the viability of government. Much government is nonviable today in my opinion, and not just the Federal Government, either.

We do have a very acute problem of perhaps doing a better job of leading our people more confidently in this economy. There is a set of choices that is difficult, energy and environment as one example. We have not done very well to date on these problems. Mr. Brown is on the Interstate and Foreign Commerce Committee, and I have had the luck to have to preside over the House on the bills that came out of his committee dealing with energy. They really haven't been very satisfactory results.

I believe that the posture that you outline is an essential part, but the problem we have in this committee is to recognize the psychological factor, to recognize, also, that there are real difficulties in numbers, and one of our problems is illustrated by Mr. Rousselot's comments on the speed with which we need to act on the tax program because of the Budget Act.

If I understand your tax program, it is not going to be enacted in this session of Congress. It will be proposed in this session, and hopefully enacted in the next session.

I know perfectly well that one of the things that we did not think very carefully about in considering the budget was the transition from an administration of one party to the administration of another party, and I don't think there will be any way, you know, to build in that kind of consideration.

There are a few things that I would like to get your longrange view in writing on, or otherwise. I am not pressing you for a quick answer on these.

There have been several innovations in the long-term budget-outlook process in the last administration. I am sure you didn't have time to deal with the longer term implications of your changes in the budget. It would be unreasonable to expect it. But I hope that you are going to give very careful consideration to the longer range projections that were included in the earlier budgets of the last administration. Because I think we are going to have to go to a longer range approach, a programatic approach, and so on. I am not going to ask you what you are going to do, but I hope you will give very careful consideration to the notion of considering longer range projections and perhaps even longer range than we have used so far.

We ought to grow up to the point in this country of knowing that when we make a projection, it isn't something we are going to be held to. It is something we are going to use as a goal, and I think the long-range budget objectives are extraordinarily helpful, and I think they fit in very nicely with zero-based budgeting.

There is one other factor—I don't know the answer to this, but a suggestion has been made—it is pretty well known that there was a very substantial shortfall in spending in the second or third quarter of the last calendar year.

Apparently that caught everybody by surprise. Obviously we weren't doing a very good monitoring job, or we don't have the tools for it. But I assume that you are going to be taking some steps to see to it that we are doing a better job on that. I am not going to suggest some of the suggestions that have been made, but I hope I would be correct in assuming that you are not going to allow in the managerial capacity that kind of thing to happen if you can avoid it.

Mr. LANCE. No, sir, and there are still some that we still have to contend with. We are trying to find the answer to that right now, because that shortfall is continuing. We know that is something we will have to deal with.

Representative BOLLING. Aren't there ways to deal with it? Aren't there actual things going on in the Treasury that can be counted and observed and reported?

Mr. LANCE. Yes, sir, it is difficult to get at. I found that. I share your thought that that ought not to be too difficult to see how the spending function is going along in this process, but it is a difficult situation to arrive at, and it is hard to tell, because of circumstances.

Secretary Blumenthal and Mr. Schultze and I have had meetings on how to deal with the problem, and Dale McOmber has been involved in it. It is something that is difficult. I don't minimize the difficulty of being able to find out, because I am not sure that the agencies or departments have kept that close to the expenditure process in their own operation. It is very difficult to tell whether they are spending along those levels or not.

Representative BOLLING. I find that—I am not doubting you—but I find that weird, or at least incredible.

Mr. LANCE. I think the other administration found it incredible last year.

Representative BOLLING. I know that. That is clear as a bell.

Mr. LANCE. That is why we have been concerned about aspects of it, but in our budget, if I might just refer to that, last year's spending estimates were too high, and economic policymaking was adversely affected because time did not permit detailed review of the estimates. I have instructed that this review be made in the President's message. The Congress was assured that it would be informed of the results. The apparent shortfall is something we are concerned about. I am not knowledgeable enough at this time to be able to respond to you all the reasons that are involved, but there are obviously some reasons out there.

It may be that the estimating process may be involved, and it may be systemic in nature. That is a new word I have learned in talking to the experts.

Representative BOLLING. I am not going to ask you the obvious question about the kind of effect this could have on the third congressional resolution and so on, but Mrs. Rivlin makes a suggestion about Federal agencies making available to Congress monthly spending plans and so forth, and the staffs could then check back and forth, and I hope that will be given some consideration.

Do you have some more questions, Congressman Brown?

Representative BROWN of Ohio. No. Mr. Chairman.

Representative BOLLING. I will go on for a little while, and we will let you get away and even get some lunch, maybe.

I am concerned about a very, very narrow subject. I was the first chairman of the Subcommittee on Economic Statistics of this committee before there was any general concern about economic statistics.

During the long process, we did everything, including appealing to an outside lobby to press the cause of statistics, because we found there wasn't anybody in Government or out who was concerned enough about having good statistical series for us to be able to get the money from the Appropriations Committee.

Somewhere along the line, and I forget the year, we managed to get something that provided in the OMB, then the Bureau of the Budget, a coordinated group. I have even forgotten the name. But my impression today is that one of the dilemmas that we have is lack of really good information on some very important areas—unemployment is one.

We have programs, and laws, and we have enacted them, which require that a trigger by local unemployment be used, but there is no good statistical series on local unemployment. I guess in some programs, they are triggered by regional unemployment, and there really isn't anything very good on that.

My question is, will you look yourself, or have somebody take a good look at the problem of coordinating statistical information, and a way of giving the OMB the power somehow to see to it that they aren't just negotiating among the agencies as to who is going to do what series, and at the same time, have that same group that has the coordinating responsibility, take a fresh look at what we need in the light of the programs that have been enacted, sort of hit or miss.

I don't see how any of us, either in the executive or here, or even in some segments of business, can do a very good job on dealing with economic policy unless we have a great deal better raw material than I think we have today.

Granted, raw material costs money, but certainly if it is better coordinated than it has been in my opinion in recent years, we could get more for whatever money we spent.

Mr. LANCE. I certainly agree with you, and I have had conversations with Joe Duncan in OMB who is responsible for that function, and we have talked about the very things you have talked about. I can assure you that we will give that every consideration. We are trying to resolve that problem, and this is off the top of my head, which I should not do, but I believe that there is some sort of congressional proposal now that relates to statistical information. I talked to Senator Cranston about it just briefly.

Representative BOLLING. We don't coordinate very well in Congress, and we can't demand that everybody coordinate perfectly in the executive, but I think a time when you are contemplating reorganization, and Congress is restless about their reorganization, I think it is a good time to improve the whole area. I think it is fundamentally important to deal with a more complicated economy than we have had in our history.

Mr. LANCE. I think that is true. When people talk about the computer programs, they talk about garbage in and garbage out. I think we need more information.

Representative BOLLING. The garbage in and garbage out is very true in some instances.

Do you have further questions?

Representative ROUSSELOT. One quick one. Relating to the balanced budget by 1981, following up on the chairman's questions, are there alternatives that you now consider for long-term economic stimulus, and since the President himself during this campaign emphasized that he would work for a balanced budget, and because any deficits that we have will be important. In the last 25 years, we have only had four surpluses, and these budget deficits are just getting out of sight, and since those deficits impact the private marketplace so heavily, because the Treasury is forced to go out and borrow money, is there consideration being given to speeding up the process of getting to a balanced budget? If you had all your "druthers," maybe before 1981—why should we wait that long? Maybe we could do it in 1980?

Mr. LANCE. There is no question about the validity of that comment. It would be good. I think I agree with you that the sooner the better.

Representative ROUSSELOT. And consider that as an alternative?

Mr. LANCE. I think when you consider the overall aspects of it, where we are now and where we want to get to, it was felt that 1981 represented a reasonable year. If we can get to it sooner, I would be very pleased.

Representative ROUSSELOT. And you would give that, then, serious consideration, that alternative?

Mr. LANCE. As it relates to being an alternative, we feel that we have got a long way to go in the process, and we are starting at a rather high level, so to say that, I have a difficult enough time to convince people that we are going to do it by 1981. I don't want to have to get into a position of convincing them we can do it in 1980.

Representative Brown of Ohio. Mr. Chairman, since I don't have the chance to get to the White House socially as much as I used to, and this may be the last chance I get to see you, I want to say something that I chose not to say a few months ago. Mr. Rousselot stimulated me. Perhaps I should not say it now.

But I have to suggest to you that the short time for the administration to come up with its positions on things like economic packages and the energy program, I really don't buy altogether, because I think the President has known since some time around the second of November that he was going to have that responsibility, and I understand the transition teams were already kind of at work before that, having read the polls earlier in the campaign.

A lot of these problems really are not all that new to either you or to me as businessmen—never mind our political positions—and I would hope that we can move somewhat quicker. An August proposal on taxes, as both Mr. Rousselot and Chairman Bolling pointed out, is really not a proposal for this year. It is a proposal for next year, maybe.

The energy program, which I was pleased to support the President on in order to get, was an emergency program to deal with the fact that we had people out of work in massive proportions.

Now, with all due respect, Mr. Bolling touched on that.

The Congress has been somewhat less than dramatically effective in getting results to deal with our energy problems, and I think we are going to have to have some strong, definitive and prompt leadership out of the White House if we are going to get things done.

I am like everybody else. I want to give the President a good, solid chance to develop his programs, and so I was happy to support this emergency proposal as an emergency proposal, but I pleaded with him before that to make long-range recommendations in the gas area. I pleaded with Mr. Schlesinger, not this year, but perhaps for next year, for breaking out the natural gas part of the program. I gather that is not going to be done.

I have to say to you in sort of a fair warning, that if it is a half-baked proposal on April 20, I have to call it as I see it at that time.

If it is one that the President does not get behind with his rather considerable political clout and connections, why, I don't see much prospect that we will do very much better in the Congress this year than we did last year with the energy problem, and I don't think our country can sustain too much more of that, because I think the February unemployment figures are going to jar us, just from the energy problem alone, and the capital formation problem, the whole economic problem, the inflation and the deficit. I recognize the need for you to develop methods and to find the right people to do the job; to get statistics and to make economic checks for your own benefit.

But these aren't new problems, and I would hope that we can act as I have learned to say, with all deliberate speed, but with the emphasis on the speed.

Thank you, Mr. Chairman.

Representative Bolling. Mr. Lance, we thank you very much.

Mr. Lance. Thank you, Mr. Chairman.

Representative Bolling. The committee stands adjourned.

[Whereupon, at 12:57 p.m., the committee adjourned, subject to the call of the Chair.]

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